

SURVIVING THE CUTS and SECURING THE FUTURE

The funding and structure of the inland waterways in England and Wales

Inland Waterways Advisory Council

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What is the Inland Waterways Advisory Council (IWAC)?

IWAC is a statutory public body consisting of 14 Volunteer Members, a part-time Chair and two support staff. It provides independent advice to the UK Government, Scottish Government, navigation authorities and other interested parties on matters it considers appropriate and relevant to Britain's inland waterways.

IWAC was established in April 2007 by the Natural Environment and Rural Communities Act 2006. Its predecessor organisation was the Inland Waterways Amenity Advisory Council, formed in 1968. IWAC is funded by the Department for Environment, Food and Rural Affairs (Defra) and the Scottish Government.

In England and Wales, IWAC's remit covers all of the inland waterways such as:

- canals (including those managed by British Waterways, canal companies, local authorities and independent bodies);
- rivers (including those which are the responsibility of the Environment Agency, British Waterways and port authorities);
- the Norfolk & Suffolk Broads; and
- the navigable drains of the Fens.

In Scotland, IWAC's remit covers inland waterways that are owned or managed by, or which receive technical advice or assistance from, British Waterways.

In July 2010 it was announced by the present UK Government that IWAC will be one of the public bodies to be abolished during 2011.

What is IWAC's role?

IWAC's role is to ensure that the inland waterways are sustainably developed to meet the needs of all who use and enjoy them. Once used mainly for freight transport, inland waterways now have a strong recreational and amenity use. They are an effective catalyst for the regeneration of local economies, acting as a distinctive focus to bring economic, social and environmental benefits to cities, towns and rural communities.

IWAC has published reports which include: using inland waterways to tackle social exclusion, funding and income sources for a selection of overseas waterways, insights into the funding of inland waterways in Britain, balancing the needs of navigation and aquatic wildlife, awareness and appreciation of the canal network in Scotland and reducing carbon dioxide emissions by moving more freight onto inland waterways.

More about IWAC

Please visit the IWAC website at www.iwac.org.uk for further information about IWAC and to see copies of its reports, including this one.



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Section 1

Introduction and Objectives

1.1 Introduction

The inland waterways of England and Wales form a unique asset enjoyed by millions of people. The waterways help to define our landscape, provide habitat for wildlife and offer leisure opportunities to boaters, anglers, walkers and cyclists. Less obviously they contribute to flood prevention, aid the supply of water and provide route ways for the pipes and cables of our public utilities. In recent years they have been the focus for the social and economic regeneration of many of our great cities, converting derelict wastelands into vibrant communities. The waterways are very popular. According to recent surveys, well over 250 million visits are made to our rivers and canals each year, sometimes to view the exceptional range of heritage sites along the waterway corridor and often simply for the quiet enjoyment of walking along a waterway path.

1.2 Background

Recent decades have seen a renaissance of the waterways. However economic circumstances have changed and during the next five years the country faces cuts in public expenditure of a severity not experienced in recent history. As these cuts fall on the inland waterways there will be adverse consequences for the many dimensions of public benefit that the waterways provide and, in some of those respects, an irreversibility of decline. The big questions for the waterways sector in the short term are, "How much cutting is appropriate?" and, "What are the consequences in terms of benefits foregone, or put at risk, as a result of significant cuts?" In the background is an even grimmer consideration, "How far will it be possible to repair the resulting damage in the future and how much of that damage will be permanent?"

Throughout the last half century the government has been supporting the inland waterways with grants of about £90 million per annum (GB total), when expressed in present day prices. Yet there has never been a public discussion of the appropriate level of government support, at least not in the sense of linking expenditure incurred to the public benefits that are provided by the assets and services which are created.

Taking a longer time period than the one over which the current fiscal situation is likely to persist, one which goes beyond the next five years, there is still an information gap to be filled. The big questions for the long term are quite different, "What level of public sector funding is justified by the benefits provided?" and, "How can the sector be organised in a way that the call on public funds is minimised without putting these benefits at risk?"

This report provides an assessment of the funding options for the inland waterways. Of primary concern are the immediate policy issues associated with making cuts, but this report recognises that addressing the vital longer term policy issues is of fundamental importance to the future stability and viability of the sector.

Inevitably the discussion is dominated by the two large organisations, British Waterways (BW) and the Environment Agency (EA). IWAC's intention, however, is to arrive at conclusions for the sector as a whole, reflecting the importance of ensuring that the many smaller navigation organisations feel able to participate.

The report covers the Inland Waterways sector in England and Wales. The Scottish Government has asked that it be kept informed of the thinking as it developed.

1.3 Objective

IWAC's principal objective for this report is:

“To explore how best to maintain or to improve in real terms the current level of income and expenditure in order that the whole network can be maintained in the long term in a sustainable condition thereby ensuring that the full economic and social benefits can continue to be enjoyed for many generations to come.”

The report seeks to achieve this objective by:

- a) Summarising and presenting factual material on existing funding and organisational arrangements for all of the navigation and other waterways bodies in the sector, the understanding of which is essential to put into context proposals both for the current (2010) and for the longer term funding and institutional changes.
- b) Providing advice and guidance to government on the options for change and their implications for the funding of the sector as a whole in the context of the current discussions of the national fiscal concerns and the institutional changes in the sector presently being considered, including the possible mutualisation of BW and the navigation functions of the EA.
- c) Discussing what steps need to be taken to ensure that all parts of the inland waterways sector are organised in a manner which gives the sector the best opportunity to thrive in the longer term, using an appropriate level of public funding and providing the best mix of public benefits in relation to the expenditures incurred.

The report presents conclusions which IWAC has drawn from its research into the issues of waterways funding and organisation, offers advice and makes recommendations to the UK government and to navigation authorities.

Section 2

Summary and Conclusions

Principal Conclusions

The principal conclusions of the Report are that:

- the current structure of the inland waterways is cumbersome with significant weaknesses which result in an inefficient use of existing resources;
- the existing funding gap - which would be exacerbated by any further cuts in Government financial support to the sector - will result in sections of the current waterways infrastructure becoming unserviceable perhaps on a permanent basis;
- there are opportunities to increase non grant income within the present structures and to achieve efficiencies in the existing cost base;
- there is a strong case for public funding for the sector, and this support should be based on the key funding principles identified in this report;
- the move of BW into the third sector could have significant potential advantages but will not resolve many of the current funding problems of BW and will do little to address the inefficiencies and weaknesses in the structural arrangements of the inland waterways sector as a whole; and
- the best chance of achieving long term stability and financial security, not just for BW but for the inland waterways as a whole, is by the creation of a new structure and governance arrangements which embrace all parts of the sector.

2.1 Structural and financial weakness

The inland waterways of England and Wales form a unique national asset which has brought many important public benefits ranging from recreation to regeneration and has the potential to deliver many more. However the present financial and structural arrangements for the sector are seriously flawed.

For historical reasons the inland waterways are not managed as an integrated resource but in a diverse and highly fragmented manner by over twenty very different navigation authorities. The navigation authorities vary enormously in size with the biggest, British Waterways (BW), being responsible for 2,615kms of waterways and the smallest being responsible for only a few kms.

Ownership and management varies greatly. BW is a public corporation; the Environment Agency (EA) is a non-departmental public body; the Broads Authority (BA) has many features of a National Park; the Middle Level operates mainly as a drainage board; eight navigations are owned or managed by local authorities; two are operated by charities; two are private companies.

The sector as a whole is under-funded and the two largest navigation authorities have a funding gap of over £40 million a year.

There is great diversity in the way the sector is financed. BW and EA receive substantial funding from central government but many of the small navigations receive no public funding of any kind. BW earns substantial income from its property portfolio; EA earns little commercial income; BA funds its navigations almost entirely from tolls and charges on boaters; Middle Level has no powers to raise charges from recreational boaters; and, several other small navigations have other restrictions.

The current structure is cumbersome with significant inefficiencies and weaknesses:

- **the sector is fragmented and under-resourced;**
- **many small navigation authorities lack management capacity and relevant specialist advice;**
- **management of the two largest authorities is hampered by government financial constraints;**
- **there is limited engagement of many navigation authorities with local authorities or with the private sector; and**
- **the two largest navigation authorities are heavily dependent on public funds and the level of public funding is not secure.**

2.2 The cuts programme

With a very cumbersome structure and against a background of financial weakness, the inland waterways sector now faces very severe cuts in public funding as part of the deficit reduction programme.

Substantial reductions in funding will have a long term detrimental impact on the condition of the network, and will very likely lead to reduced standards of service provided to users, such as deterioration or loss of towpaths as footpaths, and over time to the loss of some existing waterways. This bleak outcome is particularly likely if serious breaches and collapses occur and, against the background of funding cuts, funds for repairs cannot be found.

Defra, as the government department responsible for sponsoring the waterways, expects cuts of about 25% in its departmental budget. If Defra makes cuts of a similar size in the grants paid to the two largest navigation authorities, BW and EA will have great difficulty in maintaining their waterways in good order. BW and EA have little room to manoeuvre. The conventional management option of cutting costs by replacing outdated equipment is not widely available to most navigation authorities because they manage heritage assets which must be conserved.

Cuts in overheads and client service provision will not be sufficient to achieve such large reductions in expenditure and the navigation authorities will have to make substantial cuts in maintenance, including most likely a significant cut-back in dredging. Waterways managers might try to make expenditure cuts where public benefits will be least badly hit. However the value of the benefits of the inland waterway network is not well understood. So targeting of cuts will, at best, be approximate and to some extent arbitrary. There is the added issue that where cuts are made, deterioration in the system at that point may become irreversible as waterways decline in status and usability.

2.3 Public funding: the need for greater transparency and security

The case for the public funding of some part of the cost of the waterways is strong. The inland waterways provide many services and benefits like flood defence, drainage, landscape enhancement and heritage conservation that are of value to the whole population and which it is appropriate to fund from the public purse. In other cases specific beneficiaries, like walkers on towpaths, can be identified but for practical reasons or for reasons of policy are not charged directly, so local or national government need to act as funding proxies for those beneficiaries if the benefits are to be retained.

Successive governments over more than forty years have not developed a framework of principles to determine the public contribution to the funding of the network. This aspect of the government process has meant that funding is never secure and forward planning in the largest navigation authorities is very difficult. Because little is known about the extent and value of the public benefits provided by the inland waterways, funding cannot easily be linked to the delivery of those benefits.

These two related issues - the absence of transparency in the process of reaching funding decisions and the dearth of detailed information the benefits of the inland waterways - have inhibited rational debate about the best means of achieving sustainable funding of the sector.

The Government should:

- **continue with its research into the value of public benefits that was started by Defra in 2008 which has yielded very positive results to date and which needs to be taken further; and**
- **develop a framework for funding the waterways based on the following seven principles:**
 1. Local, regional or national governments should fund public goods functions of the inland waterways where there is an inability to capture benefits through charging mechanisms, and research should continue to be undertaken to inform the level of these public benefits in monetary terms.
 2. Government should fund the provision of facilities and services for the benefit of the socially deprived or the excluded where inland waterways offer solutions on cost-effectiveness grounds either as good as or superior to other government programmes with similar objectives.
 3. Local or national government should fund inland waterways based regeneration where it can be demonstrated that individual projects are worthwhile in comparison with alternative schemes in economic, social and environmental terms.
 4. Government should fund inland waterways activities where they contribute significantly to the achievement of the government's political priorities even if they can not otherwise be wholly justified by the underlying principles of economic efficiency and/or redistribution.
 5. Government should fund inland waterway expenditure on environmental improvements, broadly defined, to secure net gains.
 6. Within the current level of operations of the inland waterway network the resources used should provide best value for money for the taxpayer.
 7. An allowance in the determination of funding levels should make provision for benefits for "non-users", which could in part be funded by private contributions to societies, charities etc, but which would also come from the public purse.

The intention to apply cuts in public expenditure in the immediate future does not relieve it of the responsibility to preserve the important national asset in the long term. To reconcile these two objectives the **Government should use the principles in Section 5 of this report to establish the basis and trajectory for long term public funding. Although immediate economic pressures might mean that Defra is unable to follow this trajectory for some years, Government will need to return public funding to this trajectory as rapidly as possible.** Any other policy would involve accepting that the inland waterways will sink into long term and probably irreversible decline. This approach should be the basis of the funding settlement made between Defra, BW and EA.

Paying grant-in-aid (GIA) from one sponsoring department should not prevent other departments from funding waterways projects relevant to their own policy targets.

2.4 Increasing income and reducing costs

Navigation authorities need as much freedom as possible to manage their affairs and to increase their income. Unfortunately, apart from the BW navigations, much of the legislation which governs the waterways is archaic and restrictive. In some cases the authorities cannot even levy licence fees. **Government should use secondary legislation to create a legal framework that permits all navigation authorities to manage their operations efficiently and to levy reasonable charges.**

Boaters should meet a reasonable proportion of the cost of navigation. **Increases in licence fees should reflect cost rises within the navigation authority.** However, on the basis of past practice and international experience, a policy of large and continuing increases in licence fees above the rate of inflation is neither an effective nor a reasonable way of closing the funding gap.

Each waterway should be regarded as a valuable local amenity and the success of the waterways in delivering public benefits requires very close cooperation between navigation authorities and local authorities. **Navigation authorities should give a much higher priority to effective engagement with local authorities.**

Navigation authorities badly need to raise the level of income that they generate. **Retail and franchise revenue earned by navigation authorities is too low. Many millions visit the waterways each year and the opportunity to sell services and products to these visitors needs to be taken much more seriously.**

BW wishes to raise revenue in the form of donations and legacies from individuals but building a sizable income from this source is likely to take many years. **A fruitful source of income in the medium term would be through sponsorship agreements with private companies and relevant organisations. Navigation authorities should actively consider developing such sponsorship agreements.**

Great attention needs to be given to reducing costs. IWAC has been surprised at the high level of head office costs in BW. Some of the smaller navigations provide instructive lessons in how waterways might be run at low cost and the larger navigations should be open to dialogue with the most cost effective smaller navigations to discover what lessons can be learned.

Volunteers have an important role to play in increasing the potential of the inland waterways to deliver valuable benefits and to improve the quality of life of local communities. Unfortunately the larger navigation authorities have sometimes taken an ambiguous attitude to volunteers. **Navigation authorities should re-examine their policies on volunteering and follow the examples of best practice that the recent IWAC report has identified in organisations outside the waterways sector.**

2.5 Moving BW into the third sector: potential benefits and many problems

BW's proposal that it should cease to be a public corporation and be transformed into a charitable trust in the third sector is a clear recognition that fundamental change is needed in the governance and management of the inland waterways.

The move of BW into the third sector could have significant potential advantages but will not resolve many of the current funding problems of BW and will do little to address the inefficiencies and weaknesses in the structural arrangements of the inland waterways sector as a whole.

Even if the new third sector body takes advantage of the suggestions for increased revenue in this Report, and even if it achieves the anticipated income from private donations, a decade at least will pass before significant income is built up to fill the funding gap. During this time the cumulative deficit could be so large as to have a damaging effect on the condition of the assets managed by the new body. **During the transitional period, there will be an overwhelming need for the new third sector body to be supported by a substantial level of public funding if it is required to maintain the current network in a sustainable condition.**

Who should own the assets following mutualisation? IWAC expects the ownership of BW's assets to remain in the public sector and can see little merit and many risks in a model which involves the transfer of assets to the third sector organisation.

The transformation in BW's status and culture will be very difficult and will require considerable and highly focused management skills. This raises doubts about the possibility of combining the move into the third sector with a merger between BW and EA's navigation interests.

A merger between BW and EA's navigation interests is desirable to bring greater coherence to the inland waterways sector, but a merger would be difficult to achieve concurrently with mutualisation and is likely to bring many problems and only modest benefits in the short term. To expect BW to manage a merger with EA navigations at the same time as a new third sector body is created will place great burdens on managers at all levels in the new organisation and could lead to a lengthy period of dislocation. The less risky approach would be to make the move to the third sector first and, providing the transformation is successful, plan the merger for some time later.

Any restructuring of BW should take account of the need to address the wider problems of the inland waterways sector and should be a step towards a more comprehensive solution. It would be a great disappointment and a significant missed opportunity if BW's proposed move into the third sector were to be regarded by Government as the last word on structural change in the sector.

2.6 A more comprehensive solution to structural and financial weakness

There is the opportunity to achieve long term stability and financial security, not just for BW but for the inland waterways as a whole, by the creation of a new structure and new governance arrangements which:

- have the potential to include all parts of the sector;
- address the inefficiencies and weaknesses in the current system;
- are highly decentralised;
- facilitate the involvement of stakeholders;
- actively engage with local authorities;
- create a single culture based on the principles of participation and stewardship; and
- preserve the identity of the smaller organisations.

The new structure would have as its key element the creation of **locally based business units** charged with maintaining and promoting the waterway in a particular area. Engineering, property, support services and museums would be established as non-core specialist businesses serving the locally based business units and selling services outside the sector as appropriate. A compact **Strategic Authority** would be formed to set objectives, give strategic direction and to receive and distribute public funding.

The principles of decentralisation, local engagement and stakeholder participation should be reinforced by suitable governance arrangements.

Implementation of the new structure could be by a stage by stage approach, involving amalgamations and by using the concept of affiliation to provide smaller navigation authorities with immediate benefits while paving the way for the longer term integration of the sector.

Section 3

The Existing Funding and Structure of the Sector

3.1 The inland waterways sector

There are approximately 5,090kms of fully navigable inland waterways in England and Wales, about 445kms of which are tidal. BW is responsible for about 2,615kms, of which about three quarters are canals. The EA manages almost 954kms, most of which are navigable rivers. The Broads Authority controls a 200km river-lake system. The Middle Level Commissioners manage 190kms, most of which have a dual function as drainage channels and navigations. Other waterways are managed by a wide range of other bodies, including local authorities, port authorities, private companies and charitable trusts. In addition there are about 890kms of managed un-navigable waterways, about half of which are the responsibility of BW (320km) and the EA (120km). There are a further 2,095kms of abandoned un-navigable waterways.

3.2 The existing funding of the sector

In 2009 IWAC commissioned consultants to conduct a survey to gain insights into and knowledge of the funding of navigation authorities in Great Britain. The members of the Association of Inland Navigation Authorities (AINA) were asked to provide details of their sources of funding in the two financial years ending in 2007 and 2008. 19 of the 21 AINA members provided information. The findings have been published on IWAC's website.¹ Much of this information was brought together for the first time.

Figure 1: Sources of Revenue of 19 Navigation Authorities (averages for 2007 and 2008)

	British Waterways		Environment Agency		Broads Authority		Others		TOTAL	
	£000's	%	£000's	%	£000's	%	£000's	%	£000's	%
Total Earned Income	120,800	63	9,287	39	2,098	89	3,468	59	135,653	60
Total Grants etc	72,100	37	14,506	61	250	11	2,385	41	89,241	40
Donations & Legacies	0	0	10	0	0	0	4	0	14	0
Total Revenue	192,900	100	23,803	100	2,348	100	5,857	100	224,908	100

Source: IWAC, *Insights into the Funding of the Inland Waterways of Great Britain* (November 2009). Data for GB

Note: All figures quoted are as reported to IWAC by the organisations responding to the survey

Figure 1 shows that total average annual revenue for these 19 navigation authorities for the 2007 and 2008 period covered by the review was about £225 million per annum. If the PLA and the Cardiff Harbour Authority (excluded from the table) had been included, the annual revenue is estimated at about £300 million. Of the 19 authorities, 86% of revenue is attributable to BW². Of the remainder, the EA accounts for about 11% and the balance is accounted for by the Broads (1%) and the smaller authorities (3% in total).

Earned income made up 60% of revenue. Public sector grants and funds of one kind or another contributed almost all of the remainder. Total public sector funding for all navigations is about £90

¹ Please refer to the References given at the end of this report for details of reports and studies mentioned in the text. The website address for the IWAC report of navigation authority finances is:

http://www.iwac.org.uk/downloads/reports/IWAC_GB_Waterways_Funding.pdf

² The aggregate figures should be interpreted with care. Not only is BW so large that its figures dominate the findings but the IWAC survey also found that the differences between the funding arrangements of individual navigation authorities were great and that as a consequence the averages can be a little misleading.

million pa. The third source of revenue, donations and legacies, made an average contribution of less than 0.01% of the total income of the whole sector.

The two largest navigation authorities have very different financial structures. BW derived 63% of its revenue from earned income but EA earned only 39% of its total revenue and depended for the majority of its navigation funding on grants from national government. The immediate past level of public funding is about £70 million pa for BW. The EA has received about £16 million in grant-in-aid each year from central government for its navigations.

Data for the categorisation of revenue rely to some extent on judgments made by the navigation authorities themselves. Investment property is a critical part of the present funding structures particularly, but not solely, for BW. The BW portfolio was recently valued at around £400 million. 18% of BW's revenue comes from income earned from its property portfolio. BW regards this as earned income but it derives from the development of publicly owned land, producing revenue which the Treasury regards as analogous to a grant from public funds. On the other hand the property income of the smaller authorities, which amounts to a substantial 21% of their total income, relates to property whose ownership is clearly in their own hands.

By contrast, the Broads, which is the third largest authority, earned almost all of its revenue from charges levied on users and received little public money for its navigation activities. The fourth largest authority, the Middle Level in the English Fens, has no legal right to raise money from recreational boaters and relies for its income on levies which are collected to pay for its drainage functions.

The smaller navigation authorities also vary widely. The Avon Navigation Trust received no public money during the two years of the survey; the Basingstoke Canal Authority received over two thirds of its income from the local authorities that own the canal. Overall the 15 smaller navigation authorities received 48% of their income from public funds of various kinds.

3.3 Institutional effects on the structure of funding

To a great extent the sources of public funding reflect the ownership of particular waterways. BW and EA are national publicly-owned organisations receiving grants from national government. Although BW recorded that it received no funding from local authorities during the two years of the survey there is evidence to suggest that some small payments have been received in other years. On the other hand EA recorded that it received significant local authority funding for work on the Fens Waterways Link. If these sums are aggregated with other payments from local authorities, the impression can be given that local authorities provided a major source of funding for the inland waterway network. In reality, the contributions made by local authorities tend to be narrow and specific.

Of the 15 smaller navigation authorities which were surveyed, seven are owned by local authorities and one is managed using local authority powers. These eight are supported with local authority funds.

The seven smaller navigation authorities which are not owned or managed by local authorities receive comparatively little funding from local authorities, although it was acknowledged in the study that there may be definitional issues concerning income coming from local authorities that have resulted in allocation to other income categories. According to data provided by the study, five receive no funding from this source and one (the Conservators of the River Cam) only received the small sum of £1,500 in 2006/7 from a local authority contract. A significant exception was Essex Waterways which is a private company owned by the Inland Waterways Association (IWA), the largest user organisation. It received £52,300 in the first year and £39,400 in the second year for delivering a number of contracts.

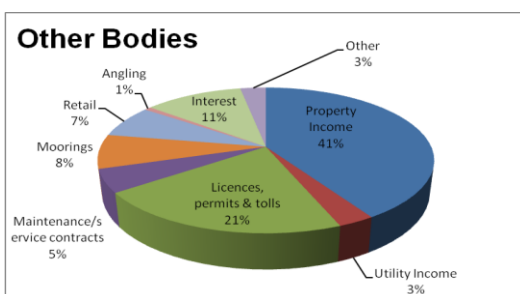
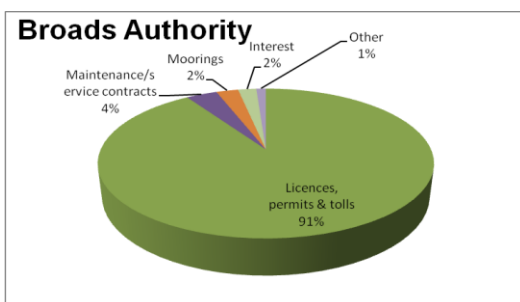
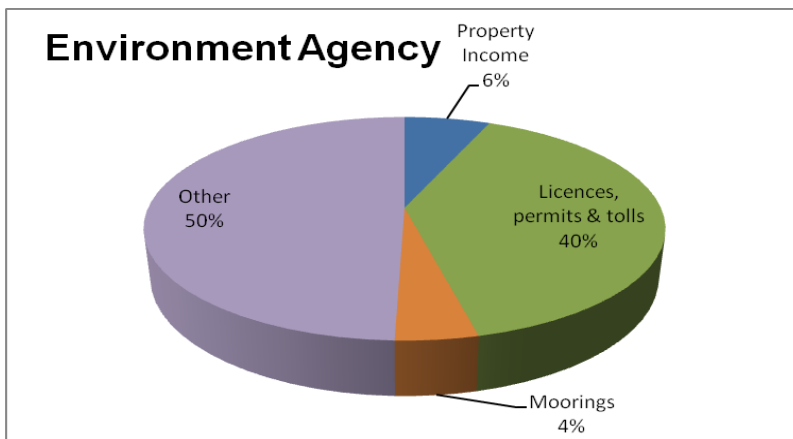
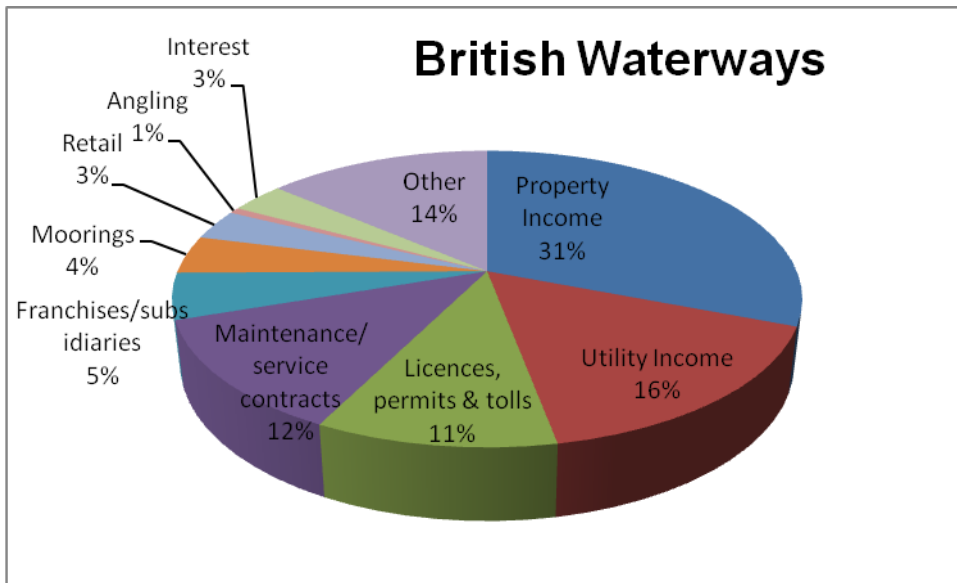
Information from the IWAC survey established that European funding is not a significant source of revenue for the waterways. The navigation authorities as a whole received an average of £450,000 in each of the two years, a sum that was only about 0.2% of total revenue.

Apart from the amounts of public funding, a second strategic issue for the funding of the waterways is the mix of the sources of funds; that is, the structure of funding. The structure is also heavily influenced by the nature of the institutions that own and manage the waterways.

Self-generated income for the management of the waterways comes from many sources and varies with the type of ownership. Commercial income comes typically from boat licences, tolls, mooring fees, drainage rates, angling activities, franchises, retail activities and water sales. Towpaths are used as wayleaves for telecoms and other utilities. Additionally, where authorities have land and property linked

in some way to the waterways, as is the case currently with BW and with a number of the smaller authorities, the profits can be fed back into waterways management.

Figure 2: Earned Income Sources of BW, EA, Broads and Others



Source: IWAC *Insights into the Funding of the Inland Waterways of Great Britain* (November 2009)

IWAC's survey examined these sources of earned income, excluding grants and donations/legacies (see Figure 2). This revealed significant differences in the main sources of income between the different types of body, including:

- Service contracts and franchises produced 12% of BW's earned income, and utility income for the running of cables and pipes, mostly along towpaths, contributed another 16%. The other navigation authorities derived very little income from these sources.
- The smaller navigation authorities overall derived 11% of their earned income from interest. Equivalent figures for the three largest navigation authorities were much lower.
- £19.9 million pa of income to the navigation authorities came from licences, registrations, permits and tolls, and together these sources represented about 13% of earned income. However the variation was again very considerable. 91% earned income of the Broads came from charges on users; the equivalent figures for the much larger EA and BW navigations were significantly lower at 40% and 11% of earned income respectively.
- Overall the earnings from moorings were small: about 4% of earned income on average and about 8% for the smaller authorities.
- Income from retail activities was very small. It represented 7% of earned income for the smaller authorities but only 3% to BW and was of negligible importance to EA and the Broads.

Income from donations and legacies was very small. EA received an average of £35,000 in donations each year. BW and the Broads recorded no donations in the two survey years. Smaller navigations might have been expected to have been more effective in securing donations but in fact the 15 smaller authorities recorded only an average of £6,000 in each of the two years of the survey.

For most public agencies borrowing against the commercial value of their assets is tightly controlled by government, so differing ownership arrangements also lead to different borrowing structures.

Overall the survey revealed a picture of great diversity in size, financial structure and governance. The importance of public funding to BW, EA and many of the navigation authorities owned or managed by local authorities was very evident. Commercial income was quite modest and donations were surprisingly small. Few navigation authorities generated sufficient income to be self-sustaining in the long term.

As discussed elsewhere in this report, currently there are many ideas and proposals for changes in these existing institutional arrangements and these have been subjected to scrutiny to test them for their likely funding implications and assessed against the current arrangements outlined above.

3.4 The existing governance and structure of the sector

Figure 3 shows governance structures of the bodies in IWAC's survey and they vary enormously. Of the largest, BW is a public corporation and the EA is a non-departmental public body. The Port of London Authority (PLA) is a public trust. The Lake District navigations are run by the National Park and while the Broads Authority (BA) has its own legislation it has many features of a National Park and describes itself as "part of the National Parks family". In addition there are eight navigations owned or managed by local authorities and two operated by charities. There are just two private companies, Neath Canal Navigation and Essex Waterways.

Figure 3: Governance and Size of 19 Navigation Authorities

Navigation Authority	Status	Length (kms)	Type
Avon Navigation Trust	Charitable Trust	73	River
Basingstoke Canal Authority	Via local authority powers	51	Canal
Bristol City Council	Statutory NA –local authority	13	Docks and River
British Waterways (GB total)	Statutory NA – Public Corporation	3,540	Canal and River
Broads Authority	Statutory NA	200	Lake and River,

			some canals
Cardiff Harbour Authority	Statutory NA –local authority	13	Lake and River
Cheshire West and Chester Councils	Statutory NA –local authority	19	River
Chesterfield Canal Partnership	Via local authority powers	8	Canal
City of York Council	Statutory NA –local authority	3	River
Conservators of the River Cam	Statutory NA	12	River
Devon County Council	Via local authority powers	18	Canal
Environment Agency	Statutory NA – non-dept. govt. body	1,368	River
Essex Waterways Limited	Private company	22	River
Exeter City Council	Statutory NA – local authority	8	Canal
Lake District National Park Authority	Statutory NA – National Park	41	Lake
Middle Level Commissioners	Statutory NA – Public Corporation	150	Part river, part canal
Neath Canal Navigation Limited	Private Company	21	Canal
Port of London Authority	Public Trust	125	River
The National Trust (Wey Navigations)	Charitable Trust	32	River

Source: IWAC *Insights into the Funding of the Inland Waterways of Great Britain* (November 2009)

The navigation authorities also vary considerably in size and many are small. Twelve of the navigation authorities each operate less than 50kms. The City of York navigation authority operates only 3kms and there is one navigation authority outside IWAC's survey that manages an even smaller waterway.

3.4 Inefficiencies and weaknesses of the present structure

Most waterways stakeholders recognise that the present structure of the inland waterways is seriously flawed. It is cumbersome with significant inefficiencies and weaknesses:

- the sector is fragmented and under-resourced;
- many of the smaller navigation authorities lack management resources and specialist skills;
- management of the largest authorities is hampered by government financial constraints;
- many navigation authorities have little engagement with local authorities or with the private sector;
- the two largest navigation authorities are heavily dependent on public funds and this level of public funding is not secure.

A fragmented system

The individual parts of the sector are managed as discrete entities with no continuity of style, approach or outcome. This leads to many practical problems, including:

- different management approaches to particular waterways where sections have different ownerships;
- inconsistency of policies between different parts of the inland waterways sector;
- inability to prioritise the need for financial support other than within each organization; and
- duplication of effort particularly in the provision of support services.

Under-resourcing of the sector

Funding gaps are difficult to estimate but in broad terms are about £30 million pa currently for BW and about £12 million in the operations of EA's navigations. The Broads Authority is also apprehensive that it might not have the funding to undertake the dredging that will be necessary in the coming decades.

On the other hand the smaller authorities admit to being short of specialist knowledge in areas like engineering and legal services. Whilst the smaller authorities in particular receive invaluable help and

support from bodies such as AINA, the task of managing a small network of waterways can be complicated and time consuming.

Management of any authority requires not just specialist knowledge on the technical aspects of managing waterways but also requires a wide range of financial, human relations and commercial skills. Many authorities cannot justify the cost of employing such specialists in their management teams and hence often have to rely on the best endeavours of general managers to cope with all the different challenges they confront.

Financial management constraints

The largest navigation authorities are all in the public sector and, under existing rules, are subject to limits imposed on external borrowing as part of the overall control of public expenditure. BW, for instance, has a balance sheet which shows some £550 million of equity and only £10 million debt. The scope for additional borrowing against the value of its assets is potentially significant and BW's income streams suggest that in normal times and under more sympathetic institutional arrangements it would have little difficulty in servicing such debt.

Navigation authorities manage vulnerable systems and are sometimes required to find large sums of money to repair breaches and attend to other emergencies. A limitation on borrowing denies the four largest navigation authorities the financial flexibility to cope with such events.

Little engagement with local authorities

The waterway corridor is an important part of the landscape and amenities of many local authorities. Close cooperation between the navigation authorities and local authorities is essential to ensure that each community derives maximum benefit from its waterway. Unfortunately close cooperation tends to be unusual.

There is a great variety of involvement of other public sector bodies in the different authorities in the sector. There are some outstanding examples of effective partnerships, including the River Thames Alliance and the Chesterfield Canal Partnership. IWAC's conclusion is, however, that a large number of navigation authorities, including BW, gave too little attention to close engagement with local authorities.

Little engagement with the private sector

IWAC's study recorded that in total over the two years, apart from contracts with utility companies and the like, the private sector contributed only £70,000 of funding, and this sum went entirely to EA. Anecdotal evidence suggests there may be other forms of engagement with the private sector on some waterways, but it is clear that few navigation authorities give it serious thought, and the smaller navigation authorities are unlikely to have the resources to be able to present themselves in a way that would encourage private sector interest or participation.

Dependence on public funding

Taken together the two largest navigation authorities, BW and EA, have received over £70 million in Grant in Aid (GIA) per annum for England and Wales. If the income from non-operational assets is also taken into account the figure rises to over £80 million.

Neither BW nor EA have the capacity at present to replace much of the public funding with income from other sources. This means that the waterways are extremely vulnerable to government decisions about GIA and, in BW's case, to decisions about the ownership of the property portfolio.

Section 5 of this Report establishes the strong case for continuing public funding of the waterways but there is little doubt that there would be greater security for the sector if the largest navigation authorities had a wider range of income sources.

Insecurity of public funding

The current level of public funding is neither guaranteed nor based on a framework of funding principles. The amount of each year's GIA is typically decided by reference to the level of GIA in the previous year, and this figure is modified to reflect the UK government's prevailing views of public expenditure. This short term approach provides little stability for waterways funding and makes the

waterways vulnerable during periods like the present when government decides that, for macro economic reasons, a reduction in public expenditure is necessary.

Conclusions

The 5,090kms of fully navigable inland waterways in England and Wales are managed by 21 navigation authorities which vary enormously in size, the biggest, British Waterways being responsible for about 2,615kms of waterways, with the smallest being responsible for only a few kms.

Ownership and management also varies greatly. BW is a public corporation; EA is a non-departmental public body; the Broads Authority (BA) has many features of a National Park; the Middle Level operates mainly as a drainage board; eight navigations are owned or managed by local authorities; two are operated by charities; two are private companies.

Revenue for the sector in England and Wales for the 2007 and 2008 period covered by the review was £225 million pa, of which 85% is attributable to BW

There is great diversity in the way the sector is funded, ranging from EA's very high dependence on public funding and the substantial dependence of BW through to some small navigations that receive no public funding of any kind.

The sector as a whole is under-funded at present with the two largest navigation authorities having a funding gap of over £40 million pa.

The present structure of the inland waterways is seriously flawed. It is cumbersome with significant inefficiencies and weaknesses:

- the sector is fragmented and under-resourced;
- many of the smaller navigation authorities lack management resources and specialist skills;
- management of the two largest authorities is hampered by government financial constraints;
- many navigation authorities have little engagement with local authorities or with the private sector;
- the two largest navigation authorities are heavily dependent on public funds and this level of public funding is not secure.

Section 4

The Implications of Cuts in the Public Funding for the Sector

4.1 Introduction

The Government plans to cut the funding of Defra, probably by about 25%. There is little doubt that Defra, as the department that sponsors BW and EA, will institute substantial cuts, perhaps of a similar amount, in the public funding of both navigation authorities. Cuts of this order will present BW and EA with a massive and unprecedented challenge. In this Section the likely effects of substantial cuts in funding are assessed, not just in the short term but against a background where cuts of this magnitude could cause permanent damage to the inland waterways network.

Waterways are expensive to maintain involving substantial liabilities and significant duties in respect to public safety. Additional regulatory requirements, further reservoir and other work on the assets and possibly inflation in the costs of construction will tend to increase costs. BW and EA will no doubt be pressed by Defra to cut costs and to increase efficiency, especially in terms of overheads, and some progress is being made. However, as a 2008 KPMG report into the financing of BW explained, the response of investing to replace outdated equipment is not as readily available as in conventional service organisations because navigation authorities manage heritage assets that must be conserved. Current projected growth in costs and self-generated revenues do not envisage the closing of BW's funding gap in the foreseeable future. Much the same can be said for EA's navigation responsibilities.

After overheads have been reviewed, the likely source of cost savings will be navigation assets. Complete closure of some canal and river sections - those which are located at the margin of the networks for which closure would be least disruptive to the system and users - would save on maintenance costs after the costs of making safe have been incurred. As a result, the status of these marginal navigations would generally be downgraded although this would be a slow process. In the case of BW the downgrade would be from cruising to remainder status. However, those closures which potentially have implications for loss or removal of riparian and other rights will require an implementation process and hence are unlikely to be rapidly effected. After compensation claims have been dealt with, the cost savings - at least in the foreseeable future - might be modest.

It would seem, therefore, that cuts in government GIA funding can only be accommodated on any scale on the existing network if the receipts foregone are substituted from other sources. There is uncertainty attached to potential sources of income but it is evident that for increases in income to be achieved there would need to be a change in ownership and governance arrangements for the institutions concerned.

4.2 The benefits of the inland waterways network

The network provides numerous and diverse benefits. Some of these benefits can be measured approximately by reference to the income they generate, but for many there is no "capture" through pricing and charging and so no direct measure of their worth. As a result, the total value of benefits of the inland waterways network is not well understood. Moreover, there is little correlation between different types of benefits across waterway sections. For example, BW data on usage suggest that in general canals have, on average, a higher density of boat usage on those sections where densities of walkers, anglers and cyclists are lower, and vice versa; that is, the correlation between numbers of boat users and of other users is negative. It is also the case that levels of flood defence benefits, values of cultural and heritage assets, regeneration opportunities and social policy benefits are distinct and at this time impossible to measure on a consistent basis and so should be assessed separately.

Much of the total benefit of the waterways is public benefit by its very nature. So, it is worth noting that the Government has confirmed that it will build upon the initial work that Defra, with IWAC support, has

carried out into quantifying the benefits (which means, in essence, the public benefits), as far as possible in monetary terms, so that they may be compared with the associated costs. Thus, the underlying conceptual framework for the determination of expenditure, and hence income requirements, continues to be cost-benefit analysis as set out in the official guide, the HM Treasury *Green Book*.

4.3 Cost cutting within the existing institutional framework

Overheads will very likely be an early target for cuts. BW's activities seem from the accounts to carry a head office cost of 15%. This is high in comparison with many businesses that provide local services and should be scrutinised. EA's navigation activities are charged less than 8% for head office services and this is the result of internal negotiations in a large and diverse organisation and is unlikely to be trimmed further.

BW is already aiming to increase engagement with local stakeholders and this will lead to a change in the balance of expenditure. The Chelmer and Blackwater navigations in Essex are owned by IWA and comprise some 22km of rivers and canals. The company is well regarded by local residents and by the County and District Councils. It employs only 4 staff (3 full time equivalents). Like many other small navigation authorities, the Company accepts that it is under-resourced in certain areas and has, for instance, too little legal and engineering support. Nevertheless the Chelmer and Blackwater navigations' provide an instructive insight into how some localised waterways could be run in the future.

The spotlight will also fall on so-called non-essential services provided by BW and EA. In reality cuts in these areas will mean that services to the general public will decline. For example, there will be fewer publicity materials and less information, response times will be slower, fewer promotions will be planned and environmental initiatives are likely to be cut back or shelved.

It would be necessary for BW and EA to prioritise by targeting specific assets for cuts in maintenance. The principle that management is likely to use is straightforward: cut expenditure where the costs of maintenance and other activities are highest and the benefits from that expenditure are lowest. In practice, this is a difficult action to take. On the costs side of the equation, of course, there are good data available and, anyway, the variation in cost for different navigable sections with similar status is usually modest. But there are often non-transparent interactions between parts of the network. Cutting maintenance in canal 'x' may have implications for the usage of canals 'y' and 'z' which are located some distance away.

However the bigger problem is the measurement of benefits. As explained in 4.2 above this is problematic, the research to establish estimates of benefit values has not been completed and the findings will take some time to emerge fully. So any management attempt to target areas for expenditure cuts based on an assessment of where public benefits will be least badly hit will, at best, be approximate and to some extent arbitrary.

Even where management believes that data on usage are sufficiently robust for a reasonable estimate of public benefit to be made, the fact that different categories of user favour different parts of the network will present management with difficult decisions. It happens that there tends to be high boat usage on many stretches of waterway with a relatively low usage by recreational walkers, cyclists and anglers and vice versa. So in practice management will have to choose which categories of users to safeguard and which categories of users should bear the brunt of the cuts.

There is a tolerance with most capital assets in respect of maintenance and repair activities and the implications of a cut back in maintenance spending will not be immediately obvious. Managers estimate that there might be a three or four year time period before adverse consequences appear in any substantive way. Many of the effects will be also lagged so that even if maintenance expenditure increases after a period of cuts, the deterioration of assets will continue for some time until catch-up is achieved.

With so many complex judgments to be made it is difficult to say where the cuts impacts will occur and this, in any event, is a matter for the navigation authorities in their corporate planning. Some commentators have drawn attention to locations where BW canals sections have comparatively low levels of boat usage and which are either on the fringe of the network or would cause lesser amounts of disruption to the network as a whole. These locations include selected branches in the West Midlands and the North West, upper reaches of the Lee Navigation, sections in Shropshire and in the East Midlands. However these possibilities would need to be scrutinised as there may be other factors to

consider, and they would need to be compared with other parts of the system before they could be regarded as candidates for cuts.

Serious events such as breaches, tunnel collapses and floods are by their nature unpredictable but based on recent cases they are usually expensive to repair and rectify. In the context of a regime of cutbacks the navigation authorities might not be able to find the money for reinstatement. As a matter of policy, therefore, serious failures might be left unrepaired and abandoned once the locality has been made safe. If a canal section is forced to close due to a breach or tunnel collapse the impacts on users, depending on the precise location, could extend over many more canals in the network than the one where the event occurred.

There is little doubt that the managers of the BW and EA navigations will do their best to minimise the effects of the cuts on users and on the public in general. The management will inevitably rely on experience and judgement in applying the cuts programme. Unfortunately the size of the cuts may well make much of that experience irrelevant. In respect of maintenance cuts, the short term effects on systems which are very old are likely to be determined randomly to a considerable extent. If serious events occur and the funding for repair cannot be found, there is a risk that parts of the network might deteriorate into a spiral of decline resulting in permanent loss.

EA and BW are likely to be pressed by Defra to cut staff numbers. The disadvantages of a rapid reduction in staff are well known. Morale usually drops sharply and, while necessary attention is given to staff that leave, those who remain can feel undervalued. Often the staff with the most easily transferable and specialist skills are the first to go and they will be the most difficult to replace when an upturn comes. As teams reduce in size, effective work partnerships are broken and relationships suffer.

There is significant and justifiable public and political pressure to increase the recruitment of volunteers. However, during a period when members of staff feel insecure, managers should resist the temptation to try to replace employees with volunteers. This is likely to be extremely damaging when maximum cooperation is needed from employees. It is much better to regard working with volunteers as an opportunity to widen horizons, to develop new income streams and increase the range of public benefits.

4.4 The impact of cost cutting on the network

Unfortunately the current level of government funding is insufficient, when taken with the other income generated by the two largest navigation authorities, to maintain the network in good order. BW has devised an asset management model (which is described in the recent report by Consultants KPMG, *British Waterways Status Options Review*) to assist with the calculation of the costs of maintenance of its existing network to a standard that prevents long-term decline. In 2008 this model produced a figure showing that an additional £30 million was needed to maintain the current network to this standard. Similarly, in 2008, the EA estimated that it has about £12 million shortfall in maintaining a physical steady state and a backlog of capital works to waterways structures of about £30 million.

The current level of public sector funding therefore, means that the inland waterway networks operated by BW and EA will slowly decline in physical terms or in services provided unless alternative sources of funding can be found, and such sources are sustainable. Obviously cuts in public funding add to the risks to the network.

Network decline in this context, therefore, means:

1. reduced standards of service provided to users, such as deterioration or loss of towpaths as footpaths; and/or
2. reduced levels of maintenance, for which the national dredging programme would be a prime candidate since it is a particularly expensive part of maintenance activity; and/or
3. reduced network size, whereby sections are taken out of the navigable system.

Most critically, any failure to repair or reinstate any part of the network following significant damaging events such as tunnel collapses, flood damage and breaches as a result of insufficient funds would be extremely damaging to the local community affected. The scale of these incidents can be very significant as was seen in the case of the breach on the Monmouthshire and Brecon canal in 2007 which cost BW about £7.5 million to repair and reinstate.

Conclusions

The current level of public sector funding already means that the inland waterway networks operated by BW and EA will slowly decline in physical terms or in quality of services unless alternative and sustainable sources of funding can be found. Cuts in funding will increase the risks to the network.

If Defra makes cuts of 25% or so in public funding of the waterways, BW and EA will have great difficulty in maintaining their navigations in good order.

The conventional option of cutting costs by investing to replace outdated equipment is not readily available because navigation authorities manage heritage assets which must be conserved.

Cuts in overheads and client service provision will not be sufficient to achieve large reductions in costs and navigation authorities will have to make substantial cuts in maintenance, including a significant cut-back in dredging.

The value of the benefits of the inland waterway network is not well understood. So targeting of areas to make expenditure cuts based on an assessment of where public benefits will be least badly hit will, at best, be approximate and to some extent arbitrary.

Substantial reductions in funding will have a long term, detrimental impact on the condition of the network and will probably lead to the loss of some existing waterways and reduced standards of service provided to users, such as deterioration or loss of towpaths as footpaths. This bleak outcome is particularly likely if serious breaches and network failures occur and the funding for repairs cannot be found.

Section 5

Public Funding based on Defined Principles

5.1 The present position

Figure 1 in Section 3 showed that public funds contribute about £90 million pa, most of which is Grant in Aid (GIA) from central government. This includes public funding of over £63 million for BW and £14 million from national government for EA's navigations. However the level and basis for public funding has varied significantly over time and has not succeeded in closing the funding gap which exists for most of the navigations at the existing network size and desired standards.

As indicated in Section 3.4, public funding allocated to the inland waterways has fluctuated, with periods of increase often followed by periods of decline. There was an increase in levels of funding in the five years between 1998/99 and 2003/04 but this has been followed by five years of reduction. However, in spite of these fluctuations, the general trend of public funding over the longer term has been flat, with UK governments tending to match the increase in general price inflation but resisting claims for real term increases in public funding.

When cuts have been applied it is noticeable that these, as in 2010, have been driven by a pressing need for national fiscal restraint and by economic downturn rather than by a considered reflection of what is an appropriate level of funding for waterways. In the four decades and more since the 1968 Transport Act established BW broadly in its present form, and through the life of the National Rivers Authority and its successor, the EA, successive UK governments have failed to develop any framework of principles for the funding of the main navigation authorities. The amount of each year's GIA is typically decided on the basis of the previous year's allocation, modified to reflect the governments' prevailing views of public expenditure in general. Similarly, and as far as can be ascertained, funding has never been explicitly linked to the types of public benefits that the waterways provide. This means that the prospect of cuts has tended to bring forth an impassioned response from interested parties, stressing what would be lost or put at risk but, because the detailed information on costs and benefits has not been available and because there is no framework of funding principles to guide decisions, the debate often contains more propaganda than substance.

5.2 The case for public funding

There are two over-arching justifications for UK government action in any policy area which are spelt out in the HM Treasury's *Green Book*,³ namely where:

- there is some inability by the private sector to provide the services and goods for which there is clear demand from the public, and hence either no or only limited opportunity for applying the principle of beneficiaries pay; and,
- government wants to give redistributive advantages to some specific groups in society, often groups which are disadvantaged.

Waterways as public goods

³ Discussion of principles in this section of the report relies on: HM Treasury, *The Green Book: Appraisal and Evaluation in Central Government* and in particular on its Section 3; and, on Chapter 1 of the book by Anderson, on fundamental principles of public finance (see References at the end of the report for details)

Failure to capture benefits through inability to charge beneficiaries on a beneficiaries pay basis is sometimes referred to as a “market failure”, which reflects the absence or limited development of a market. In such cases public sector action is required to provide a service for which there is clear demand. In these cases, government is said to be providing a public good.

The inland waterways provide many services and benefits of this kind. Examples include flood defence, drainage, landscape enhancement, heritage conservation and footpaths. These services and benefits of inland waterways, or some of them at least, need to be funded from the public purse if they are to be provided at all.

A consequence of the current system is that while Defra is the sponsoring department, many public benefits of the waterways fall outside Defra’s remit. While the Treasury will no doubt insist that all GIA would have to be routed through the sponsoring department, it should nevertheless be possible for other departments to fund projects relevant to their own policy targets. This possibility should be pursued through the Inter-Departmental Working Group.

Box I: Waterways – A “Public Good”?

Many of the benefits of using inland waterways are “public goods” – that is those who fail to pay for the maintenance of the asset cannot be excluded from enjoying (some of) its benefits and one person’s enjoyment of the waterway does not diminish the capacity of others to enjoy it too. Markets do not automatically provide the right type and quantity of public goods because of the limited returns on investment in relation to the amount of benefit that can be captured from the beneficiaries through, for example, toll revenues or users’ fees. In this respect, the provision of public goods represents the response to the most common form of market failure.

There are several ways in which this principle of a public good arising from market failure is applicable to the waterways. It is clear from BW statistics that there is considerable recreational use of the towpaths by walkers but there is no obvious way in which recreational walkers can or should be charged for the benefit they receive. So without the benefit of the public sector support the towpaths would not be opened up and maintained for the benefit of walkers, and other users. Other goods and services provided by the waterways authorities – such as their contributions to landscape quality, the heritage, eco-systems and flood risk management - are public goods.

But not all waterways goods and services are true public goods – some are better considered as private goods which for various institutional reasons may be provided by the public sector. For example, houses built for sale along the side and enjoying the waterside landscape benefits of the canal are private goods even if the developer is the waterways authority, or a joint venture involving a public authority. The definition of what constitutes a private or a public good has little to do with the sector of the provider. The definition has more to do with the extent to which the benefits can be captured as revenues by the provider – public or private.

Redistribution objectives

Redistribution of income and wealth in favour of some groups in society on grounds of equity constitutes the second of the over-arching reasons for public intervention in any particular policy area. Because of the multi-dimensional nature of the benefits that inland waterways provide, waterways tend to be strong candidates for a wide variety of government policy interventions on equity grounds. Social cohesion and regeneration fall within the broad definition of distributional objectives.

The National Community Boats Association supports the use of the inland waterways to combat the effects of social exclusion. Member organisations, staffed largely by volunteers, work with disabled people, children with troubled backgrounds, offenders and disadvantaged ethnic minority groups. Because of the importance of this work, it is highly desirable that these organisations should benefit from the reforms proposed in this report.

Restoring and improving inland waterways has helped to regenerate many cities, towns and rural communities and provide wider economic benefits within disadvantaged areas and regions.

Non-user benefits

Public expenditure decisions in relation to cultural and historical assets will also wish to distinguish “users” and “non-users” of their amenities and services. In respect of the waterways, users for example

are boaters, anglers, ecologist etc. A method of measuring the benefits of the waterways is by establishing what people would be prepared to give up to secure the benefits when the assets are used. This is the principle of willingness-to-pay. Non-users, in contrast, do not use the assets or do so only rarely. They benefit by virtue of the existence of the assets and the fact of their enjoyment by users. They too are willing to pay for the upkeep of the assets despite not using them. Research in other sectors suggests that non-users are often an important group in the overall assessment of the public benefit of historical, cultural and natural assets.

5.3 The international experience

The international study, *Funding and Income Sources for Overseas Waterways*, undertaken by IWAC in November 2009 in eight countries in Europe and North America drew a number of conclusions from overseas experience in governance change management in the recreation waterways sector. It found that while there is no obvious single funding or governance model or solution which ensures sustainability, recreational waterways are almost always supported from the public purse. Many waterways have been moved from the private to public sectors, from government to public corporations and from national to regional and local government. But while the burden of ownership and operation remains firmly in the public sector funding is ultimately a question of political motivation, whatever changes are made in the level of authority.

The international study found that:

- political motivation is supported by perceived benefits;
- there are wide ranging benefits of waterways as a living heritage;
- decentralisation spreads the burden as well as the benefits; and
- decentralisation can, nevertheless, introduce uncertainty with loss of integration.

Box II: International Funding Examples

Waterway/ Location	Km length	Total Operating Costs p.a.(£m)	Operating Income per km (£)	% coverage of costs by operations	
Rideau Canal, Canada	187	4.36	23,300	3,100	13.4
Canal de Roubaix, France	44	0.99	22,500	4,100	18.2
Brittany Canals, France	339	4.10	12,100	470	3.9
Finow Kanal, Germany	44	2.52	57,200	330	0.6
Shannon-Erne Waterway, Ireland	69	1.23	17,800	310	1.7
Drenthe Canals, Netherlands	195	2.09	10,700	180	1.7
Gota Canal, Sweden	219	4.62	21,100	13,940	66.1
Erie Canal, United States	791	48.57	61,400	1,210	2.0
British Waterways	3,540	n/av	n/av	54	62.6

Source: IWAC, *Funding and Income Sources for a Selection of Overseas Inland Waterways*.

Sterling (£) equivalent values at 2009 currency exchange rates.

As in any infrastructure network the busiest and most profitable sections help to fund remoter and less well used parts. After regionalisation this often no longer applies and neighbouring authorities often have different perceptions of the benefits of maintaining each section of the network.

The international study also collected data on funding of examples of recreation waterways. Box II summarises the findings. It is striking that public funding of recreation canals still amounts to between 80-99% of coverage of costs in nearly all cases investigated. Only the Gota Canal, where the canal's history as a commercial undertaking lives on as a public corporation of the Swedish Ministry of Enterprise, comes close to the model of BW by earning up to two-thirds of operating income.

5.4 The present funding gap

It is well established that, at present, there is a funding gap between the long-term self-generated revenues of the waterways and the expenditure required to maintain, operate and invest in the current networks for safety and their "viability". A few parts of the waterways do generate more by way of revenue than costs incurred and there are examples amongst navigation authorities where there is no funding gap to be bridged by public funding. Taken as a whole, however, self-generated revenues of the waterways agencies do not cover costs nor are likely to be able to do so in the foreseeable future.

Box III: Dissecting Departmental Expenditure Limits

The 1998 Comprehensive Spending Review (CSR) introduced a framework involving Departmental Expenditure Limits – spending which is planned and controlled on a three year basis in the Spending Reviews – and Annually Managed Expenditure – expenditure which cannot reasonably be subject to firm, multi-year limits. These add up to Total Managed Expenditure which represents the current and capital spending of the public sector.

Departmental Expenditure Limits (DEL)

In the Spending Reviews, firm DEL plans are set for departments for three years, with separate budgets for current (or resource) and capital expenditure. Departments may carry forward unspent DEL provision from one year to the next and, subject to some caveats, this may be drawn down in future years. This procedure is intended to encourage departments to plan over the medium term. There is a small centrally held DEL Reserve which is intended to be available for unforeseeable contingencies. The scope for departments to shift spending between different areas of spending is rather opaque, but the Treasury tends to insist on pretty clear guidelines on the division of spending within the overall total and on its agreement to any significant changes.

Annually Managed Expenditure (AME)

AME is not subject to the same three year expenditure limits as DEL, but is still part of the overall envelope for public expenditure. AME typically consists of programmes which are large, volatile and demand-led, and which cannot reasonably be subject to multi-year limits. The biggest single element is social security spending. Other items include tax credits, Local Authority Self Financed Expenditure, Scottish Executive Spending financed by non-domestic rates, and spending financed from proceeds of the National Lottery. AME is reviewed twice a year as part of the Budget and Pre-Budget process. The Pre-Budget Report is normally scheduled for November prior to the year in question.

DEL + AME = Total Managed Expenditure (TME)

TME therefore represents the current and capital spending of the public sector, made up of central government, local government and the public corporations.

Currently some £90 million of public money flows into the sector, made up of:

- GIA from UK government and the Scottish government to BW;
- GIA from UK government to the navigation arm of EA;
- small navigation payments from UK government for the Broads Authority;
- specific grants from local authorities to some of the smaller navigation authorities;
- very small payments from regional development agencies and from European funds.

There is a shortfall between existing revenue, including public funding, and existing network requirements of more than £40 million pa. Over time this will accumulate into a significant deficit with serious implications for the condition of the network.

Box III summarises the procedures by which governments determine the expenditure to be incurred on particular policies or policy areas at departmental level. It indicates that there is considerable scope at departmental level for variations in expenditure between policy areas. The system endeavours to achieve some stability in the planning and execution of expenditure decisions through the system of three-year departmental expenditure limits.

5.5 Research to identify and measure public benefits

As noted by the Efra Sub Committee in its 2008 report and as emphasised by IWAC on many occasions, too little is known about the extent and value of the public benefits provided by the inland waterways. This gap in reliable information reduces the quality of decision making. Government has no clear idea of the public benefits that a particular level of public funding can provide. With better information an increase or a reduction in users' services, maintenance standards and network size could be related to the public benefits that would increase or reduce in magnitude as a result of the expenditure change.

To meet these needs Defra, with the support of IWAC have sponsored research on the identification and measurement of the benefits of inland waterways to establish as far as possible their monetary value. This research has identified the long list of benefits that accrue and has begun to identify the beneficiaries, whether specific users, local communities, non-users or society as a whole and to measure the magnitude of these benefits in case studies. This research, as its results unfold, should be used to help to allocate the responsibilities for funding the waterways, including the size of contributions where relevant, according to the benefits that are directly or indirectly received.

There are some groups, like boaters and anglers, who derive particular benefits from the waterways for which it is a practical possibility to charge. As users, these groups should continue to make a separate and additional contribution towards the cost of the benefits that they receive. Other groups' benefits are not easy to capture, either because charging mechanisms do not exist for them as a practical proposition (such as towpath walkers), or the beneficiaries are difficult to identify (such as with flood relief), or some other reasons.

Not all of the public benefits are of national importance and a distinction could be made between those benefits that should be funded nationally and those where regional or local funding would be more appropriate.

5.6 Recommended principles for public funding of the waterways

This brief discussion of the case for public funding, and of the considerations that government should have in mind when determining the level of funding, suggests the following set of funding principles:

1. Local, regional or national governments should fund public goods functions of the inland waterways where there is an inability to capture benefits through charging mechanisms, and research should continue to be undertaken to inform the level of these public benefits in monetary terms.
2. Government should fund the provision of facilities and services for the benefit of the socially deprived or the excluded where inland waterways offer solutions on cost-effectiveness grounds either as good as or superior to other government programmes with similar objectives.
3. Local or national government should fund inland waterways based regeneration where it can be demonstrated that individual projects are worthwhile in comparison with alternative schemes in economic, social and environmental terms.
4. Government should fund inland waterways activities where they contribute significantly to the achievement of the government's political priorities even if they can not otherwise be wholly justified by the underlying principles of economic efficiency and/or redistribution.
5. Government should fund inland waterway expenditure on environmental improvements, broadly defined, to secure net gains.
6. Within the current level of operations of the inland waterway network the resources used should provide best value for money for the taxpayer.

7. An allowance in the determination of funding levels should make provision for benefits for “non-users”, which could in part be funded by private contributions to societies, charities etc, but which would also come from the public purse.

These funding principles should be used to help guide the allocation of public money to the waterways. If this process is followed, a good deal of the mystery and secrecy that surrounds the allocation of GIA will be dispelled.

5.7 Funding principles and the cuts programme

Section 4 of this Report demonstrated that substantial cuts in public funding are likely to have long term and damaging effects on the waterways managed by BW and EA. The Government’s intention to apply cuts in public expenditure in the immediate future does not relieve it of the responsibility to preserve the important national asset in the long term. The best way to reconcile these two policy objectives is for the Government to make a distinction between the long term public funding needs of the inland waterways and its declared and immediate intention to cut public spending.

The principles in this Section should be used to establish the basis and trajectory for long term public funding. Immediate economic pressures might well mean that Defra is unable to follow this trajectory for much of this Parliament. However if the waterways are to be sustained, Government will need to return public funding to this trajectory as rapidly as possible. Any other policy would involve accepting that parts of the inland waterways will sink into long term and probably irreversible decline. This approach should be the basis of the funding settlement made between Defra, BW and EA. Subsequent structural changes, as contemplated in Sections 7 and 8 of this report, might lead to modifications in the settlement but the principle of a funding trajectory based on a clear framework of funding principles should be preserved.

Conclusions

Public funds of various kinds contribute about £90 million pa to the financing of the inland waterways. However the current annual shortfall in funding for the existing network as a whole is estimated to be over £40million. Without remedial action this deficit will accumulate and lead to a significant deterioration in the condition of the network.

The case for public funding for part of the cost of maintaining the waterways is strong and convincing.

Paying GIA from one sponsoring Department should not prevent other departments from funding waterways projects relevant to their own policy targets.

The absence of agreed funding principles which can be used to plan the public contribution to the funding of the inland waterways represents a serious policy limitation of successive governments spanning more than four decades.

Not enough is known about the extent and value of the public benefits provided by the inland waterways and this gap in reliable data reduces the quality of decision making.

The absence of transparency in the process of reaching funding decisions and the dearth of detailed information on the benefits of the inland waterways have inhibited rational debate about the best means of achieving sustainable funding of the sector.

The Government should complete its research into the value of public benefits.

Government should adopt the seven funding principles set out in this report as the basis for determining future levels of public funding for the waterways.

The Government should make a distinction between a long term public funding settlement for the inland waterways based on the framework of funding principles and its declared and immediate intention to cut public spending. The funding settlement with BW and EA should define a trajectory for public funding and, taking account of the intention to apply cuts in the immediate future, should restore public funding to this trajectory as rapidly as possible.

Section 6

The Potential for Increasing Self Generated Income

6.1 Introduction

It is a fundamental requirement that all parts of the sector and, in particular, BW and EA should aim to increase their income from sources other than GIA. This Section examines whether more income could be generated. The possibilities are grouped into six categories:

- Local authorities
- Users
- Individuals
- Companies
- Commercial income
- Volunteers

It is also recognised that the initiative currently underway to create Local Enterprise Partnerships (LEPs) will be relevant to the waterways. LEPs will take on some of the roles of the current Regional Development Agencies at regional and sub-regional levels. Local authorities will be key partners in setting up LEPs, together with the private and voluntary sectors. Once the role of LEPs is fully understood, navigation authorities should examine how best to work in partnership with the new organisations.

6.2 Income from local authorities

The inland waterways provide many benefits to local communities and this has led to proposals that local authorities should take more responsibility for funding the waterways. In its most thoroughgoing form this argument is used to support the introduction of a local authority precept so that the waterways are funded in a manner similar to the fire and rescue service or to some municipal waste facilities. There are attractions of a funding system that appears to provide an increase in resources with greater security. However the problems are formidable. Local authorities are prohibited for the time being from increasing council tax and in these circumstances the task of explaining to local tax payers the justification for a new precept would not be welcomed; in short, a new precept cannot be justified. In any event local authorities could scarcely be called on to raise money to fund an organisation over which they have no control.

So a transfer of financial responsibility would have to be accompanied by substantial structural change to give local authorities strategic and possibly management control over the inland waterways system. IWAC's Report, *Funding and Income Sources for Overseas Waterways*, also studied the experiences in a number of other countries where such a transfer has taken place and the political and financial problems that are involved were noted. In Britain such a transfer is also likely to result in significant regional and local variations in the standards of service to users and in the importance given to waterways issues.

Another option would be to give local authorities responsibility for managing those parts of the inland waterways corridor that are most relevant to local communities, while leaving the river or canal to be managed by a navigation authority with the appropriate skills and focus. The waterway paths that typically run alongside rivers and canals provide opportunities for green travel and recreational use. They are most valuable when they connect with other paths and route ways in the area and local authorities are best placed to ensure the appropriate connectivity and to promote maximum use.

Waterway paths are sometimes in a poor condition and are under-used. Although many waterway paths are maintained by navigation authorities, they have no statutory responsibility to do so. Similarly, many local authorities help to maintain waterway paths but often they also have no statutory responsibility.

Giving local authorities the responsibility for managing waterway paths has obvious advantages but could also deprive BW in particular of the income from the running of utility pipes and cables under the surface of the tow-paths.

Defra urges navigation authorities to work closely with local authorities and suggests that this partnership working can unlock more funding for the waterways. Indeed, there are many important partnerships involving local authorities that have been formed to promote the waterways. One of the most important partnerships of this sort is the River Thames Alliance. Other partnerships have been formed to restore and develop waterways such as the Cotswolds Canal Trust and the Chesterfield Canal Trust. IWAC has recently published a good practice guide, *Working Together – Effective Waterway Partnerships*, which advises stakeholders how best to set up and sustain such partnerships.

The 2009 IWAC study of the funding of navigation authorities found only one example of local authorities contributing significantly to the running costs of navigation authorities that they did not own or manage. In this case Essex Waterways Ltd., which manages the Chelmer and Blackwater Navigation, has worked extremely hard to identify the priorities of local councils and to ensure that there is real synergy between the work of the navigation authority and of the local authorities. The lessons from the Essex Waterways experience should be applied by other navigation authorities.

6.3 Income from users

Navigation authorities need as much freedom as possible to manage their affairs and to increase their income. Most navigation authorities, including BW, have the right to charge boat owners for the use of their waters. However a few navigation authorities either have no statutory right to do so or have that right so constrained by archaic legislation that a reasonable charge cannot be levied. The most obvious example of unreasonable restriction is the case of the Middle Level; legally the Middle Level Commissioners can make no charge for recreational boating and the charge that can be made for freight traffic was fixed in the nineteenth century. Secondary legislation should be used to remove this and similar restrictions.

The level at which licence fees for boaters are set is a matter of continuing controversy. In the recent past both BW and EA put in place a series of staged changes intended to increase the real value of the fees. Research carried out for EA demonstrated that the number of boaters who would stop boating if fees increased for three years at twice the rate of inflation was quite small, and in any event when these increases were applied there was no significant rise in the number of boaters who failed to renew their licence.

However the two navigation authorities soon concluded that, although the policy of large annual increases caused enormous conflict with boaters, it did little to reduce the deficits of either BW or EA. Indeed to eliminate the deficits would require licence fees to increase not by a few percentage points above inflation each year but to double or treble. Increases of this magnitude would almost certainly reduce boat registration numbers and might start a downward spiral with the navigation authorities chasing fewer and fewer boaters for higher and higher fees.

IWAC's Report, *Funding and Income Sources for Overseas Waterways*, showed that the percentage of waterway costs met by boaters in Britain was generally in line with the proportions in other countries. IWAC's conclusion is that licence fees should keep pace with inflation and should reflect cost rises within the navigation authority, but a policy of increasing licence fees well above inflation for several decades is not an effective way of closing the funding gap.

6.4 Income from individuals

BW believes that a significant number of private individuals are prepared to contribute to the upkeep of the waterways by charitable donation. A recent poll conducted by BW suggested that the number might be as high as 650,000 individuals contributing between £10 and £20 a year. This research supports BW's estimate that, with a change in structure and a move into the third sector, an annual income of about £15 million a year from private donations might be achievable within a decade or so.

Much of the momentum behind the proposal from BW's managers to change the status of the organisation from a public corporation to a third sector body comes from BW's belief that private individuals are unlikely to donate to an organisation that is publicly owned. Therefore, access to

donations and legacies would require BW to move out of the public sector. If BW's assumption is correct, the other under-funded navigation authorities that remain in the public sector, including EA, the Broads Authority and Middle Level, will have little success if they appeal to the public for donations and legacies. BW's proposals for a move into the third sector and the implications for changing funding sources are analysed in more detail in Section 7.2 below but it should be noted that if private donations are to contribute significantly to sustainable funding for the waterways the massive nature of the change needs to be recognised.

6.5 Income from companies and organisations

In the medium term there could well be scope for sponsorship agreements with private companies and relevant organisations. Britain's canals and navigable rivers are well suited to a range of sponsorship opportunities and the approach need not be particularly intrusive. Signage and interpretation boards on a particular reach of a river or a section of canal could carry the logo of the relevant organisation or company, and the sponsorship could be acknowledged whenever the relevant stretch is mentioned in public. Depending on circumstances, the financial sponsorship could be reinforced by agreements to develop volunteering arrangements with the sponsoring organisation or company's staff. Providing the sponsoring partners are chosen with care and providing the agreements are carefully drafted, using skills that the navigation authorities will need to acquire, the relationship could generate substantial revenue.

6.6 Commercial income

Section 3.3 and Figure 2 provide details of income from different sources. On average in the two years 2007 and 2008 BW earned 18% of its total income from property in its ownership and a further 10% from utilities, mostly by permitting the laying of cables and pipes on its land. This represents an annual income of about £58 million. Other potential sources of commercial income produced much lower sums. Franchises and subsidiaries earned only £6.25 million and retail activities only £4.2 million. Together these two sources produced only 5% of total income.

EA earns very little from commercial activities. During 2007 and 2008 EA recorded that it earned an annual average of only £600,000 in commercial income, all of which came from property. According to the data supplied, EA earned nothing from utilities, franchises or retail activities. In order to fill its navigation funding gap, EA decided in 2006 that it needed to raise its commercial income to £6 million a year by 2014. However this figure included significant earnings from the sale of lockkeepers' houses and EA has subsequently changed its policy in this regard and the earnings are likely to be lower, and come later.

Low figures for commercial income are partly the result of the way in which navigation authorities are constituted and their purpose. BW has been encouraged by government to concentrate on securing income from property development and has either franchised out its other commercial activities or created opportunities for other businesses in the local economy. EA regards itself primarily as a regulator. The Broads Authority considers that its main function is managing a national park. EA recruited a commercial team to identify money making projects but that team has now been disbanded. The Broads Authority has not recruited employees with commercial skills and experience. The other navigations are typically small with little capacity to develop new income streams.

Government encourages the three largest navigation authorities to promote the waterways to potential users and to increase visitor numbers. An increase in boaters provides extra revenue to the three largest navigation authorities through additional license fees and tolls. However an increase in walkers, cyclists, horse riders and other non-boating visitors adds to wear and tear on the waterway paths and associated infrastructure, but produces almost no extra revenue for the navigation authorities.

The number of visitors to the waterways is very large. BW claims a total of 12 million visitors each year to their canals and visitor destinations; the Broads Authority claims 11 million visitors; a survey by the EA produced the result that half the people who live within 5 miles of the Thames had made a recreational visit to the river in the previous year. This large number of visitors can either be regarded as a business opportunity for the navigation authorities to sell goods and services and thereby to reduce the funding gap or it can be viewed as a public service working to increase business opportunities for

others. Either view is valid but the need for extra revenue suggests that marketing possibilities need to be taken much more seriously.

It is not essential for the navigation authorities, big or small, to recruit specialists to develop and operate commercial projects. Some facilities might be run directly, others through carefully controlled franchises. Whatever the method, the objective should be to ensure that the navigation authorities derive direct financial benefit from the efforts that they make to increase the use and enjoyment of the waterways.

6.7 Volunteers

Most of the smaller navigations enhance their engagement with their local communities by working extensively with volunteers. Of the larger navigation authorities the Broads Authority has a record of encouraging and working with volunteers, BW's willingness to work with volunteers has varied from region to region and EA has worked with volunteers in only a few locations. However within the past five years both BW and EA have clarified their respective policies and have become significantly more enthusiastic.

IWAC commissioned a study to discover whether organisations outside the sector have lessons which the inland waterways can usefully learn. Results published in the Report, *Volunteering and Inland Waterways: How to Attract, Integrate and Retain Volunteers*, suggest that an organisation must be carefully structured to work with volunteers successfully and that an organisation with a conventional hierarchical structure which tries to "use" volunteers is unlikely to achieve more than marginal success. Navigation authorities should use the IWAC Report to audit their current activities and to improve their performance.

It is not desirable to attempt to cut costs in any significant way by replacing employees with volunteers. As IWAC's study demonstrates, the substitution approach undermines the morale of staff, destroys trust in management and leads to damaging conflict between staff and volunteers. In the best organisations volunteering is regarded differently, as an opportunity to develop new income streams and deliver a widening range of public benefits.

Conclusions

Much of the legislation which governs those waterways that are not operated by BW is archaic and restrictive. Government should use secondary legislation to create a legal framework that permits all navigation authorities to manage their operations efficiently and to levy reasonable charges.

Increases in licence fees should reflect cost rises within the navigation authority. However, on the basis of past practice and from an examination of international experience, it seems that a continuing policy of large above inflation increases in licence fees is not an effective way of closing the funding gap.

The success of the waterways in delivering public benefits requires very close cooperation between navigation authorities and local authorities. To achieve this level of cooperation, navigation authorities should give a much higher priority to engagement with local authorities.

Once the role of LEPs is fully understood, navigation authorities should examine how best to work in partnership with the new organisations.

Navigation authorities should consider developing sponsorship agreements for parts of the network with private companies and other relevant organisations.

The level of retail and franchise revenue earned by navigation authorities is too low and marketing possibilities need to be considered much more seriously in future.

Some of the smaller navigations provide instructive lessons in how waterways might be run at low cost and the larger navigations should open dialogue with the most cost effective smaller navigations to discover what lessons can be learnt.

Volunteers have a very important role in helping navigation authorities to improve the quality of life of communities and to deliver valuable benefits. Navigation authorities should use IWAC's Report on volunteering to audit their current activities and to improve their performance in recruiting and retaining volunteers.

Section 7

Structural Change: Current Proposals

7.1 Introduction

BW's announcement in April 2009 of its "20:20 Vision" contained a very explicit recognition that fundamental change was needed in the governance and management of the inland waterways. However BW's proposal to move into the third sector was intended not as a solution to the structural weaknesses of the whole waterways sector but as a response to BW's own problems. So, whatever the merits of BW's third sector proposal, it understandably leaves many of the weaknesses described in this report unaddressed and unresolved. Developed intelligently, the third sector proposal could become the first stage in the necessary reform programme for the whole waterways sector. It would be a great disappointment and a significant missed opportunity if the BW proposal were to be regarded as an end in itself.

7.2 Moving British Waterways into the third sector

At the launch of the "20:20 Vision", BW explained that its wish to move into the third sector was seen as a way of resolving its funding difficulties. Since then, of course, the prospect of more substantial cuts in government grants means that BW's funding problems are likely to become significantly worse.

The move to the third sector could bring many potential advantages. As a public corporation, BW is subject to a number of restrictions and disabilities. It cannot independently borrow money against its assets and, as a publicly owned corporation, it is badly placed to raise money from the public by way of donations and legacies. A newly created third sector organisation could model its governance structure to give greater influence to local authorities and other potential partners. There are several important examples of third sector organisations acting as steward for the nation in operating and conserving great national assets and it is reasonable to conclude that, given enough time and resources, the new third sector organisation for the waterways could be just as successful.

In June 2010 Richard Benyon, the Parliamentary Under-Secretary of State for Environment, Food and Rural Affairs, made a statement to the House of Commons giving the Government's position:

"The Government considers civil society has a very valuable role to play in delivering public services as part of our commitment to creating a Big Society. We will therefore be continuing to look in detail at whether a third sector model would be appropriate for British Waterways, including the possible inclusion of the Environment Agency's navigations as the other navigation authority grant aided by Government. My department will be engaging a wide range of stakeholders in this work (and liaising with the Scottish Government). However I must make clear that, given the Government's overriding objective of reducing the financial deficit, no decisions on such a change will be taken until after the forthcoming Spending Review."

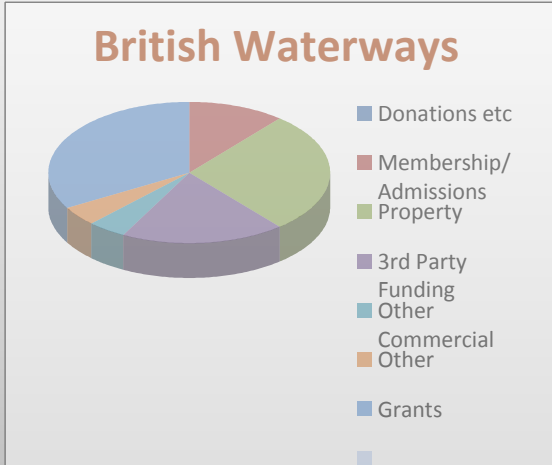
The Minister and many stakeholders, supported by IWAC, have insisted that simply moving BW in the third sector is not an acceptable way forward. The Government's declared aim is to create a new third sector body with a new financial structure, new systems of governance and with a much closer engagement with local communities. However of the many challenges facing the new third sector body, the greatest will certainly be the need to establish a reasonable level of financial stability.

Box IV: A National Trust for the Waterways?

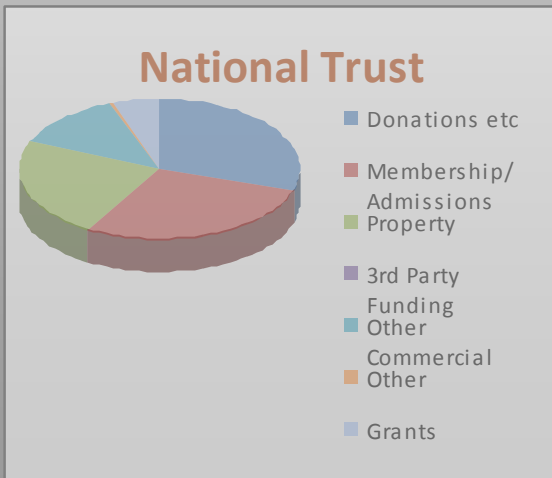
To turn BW into a “National Trust for the waterways” will require a massive transformation in the finances of BW.

BW receives about 33% of its income from public grants while the National Trust receives less than 6% from these public sources. Most of the National Trust’s income comes from donations and from membership and admission income. Only 11% of BW’s income comes from these sources.

There are clear regulatory and management reasons for these differences. The National Trust can raise subscriptions from members by offering free entry to its extensive portfolio of properties; BW has no similar opportunity. The National Trust does not usually accept major properties into its care unless the property comes with a significant endowment; BW needs to find endowments to meet the liabilities of its existing network.



The National Trust has massive land holdings which produce a large income from leases and tenancies; BW’s landholdings are more modest and there is no guarantee that they will all remain under BW’s control.



Senior managers of BW have stated that their aim is to create a “National Trust for the waterways”. The image of a waterways organisation that looks and operates like the National Trust or some other well regarded third sector body is compelling and many commentators and users have supported this aspiration. But the massive nature of the change needs to be recognised.

Comparison of the sources of income of BW with the sources of income of the National Trust, RSPB and the Royal Palaces shows that the differences between BW and these three third sector bodies are considerable; see, for example, Box IV. Most of the income of the National Trust, RSPB and the Royal Palaces comes from donations and much of the remainder from membership and admission income. Income from grants is less than 6% in all three cases. By contrast BW receives about 33% of its income from grants and only 11% from donations, membership and admission sources.

BW has concentrated heavily on the possibility of the new third sector body securing donations from the public and believes that an annual figure of some £15 million is achievable after ten years of fund

raising. Many supporters of the move to the third sector might have expected a more rapid improvement in BW's income but even this estimate is highly uncertain. In many charities, fund raising success has been built over many generations and requires skills that BW does not possess.

Fund raising on the scale suggested by BW is not easy. Donors often direct their money towards a favoured project which may not accord with the national strategy. Indeed BW might be advised to follow the example of the National Parks where money is specifically raised for local amenity. However this requires the resolution of complex and time consuming problems that BW has not faced and, in turn, requires a massive transformation in finances and structure. In short, there is little prospect of the move to the third sector leading to an early and rapid increase in income.

Most importantly however, the implication of a slow growth in donation income raises serious doubts about the financial stability of the new third sector body if the Government cuts back its funding by an amount greater than the rather modest expectation of donation income. If that happens, the new third sector body, which is likely to begin life in a weak financial position, faces a bleak future..

The key question is whether governments will support the change in BW's status by committing the appropriate level of funds. For some time the Treasury has tended to focus on the property portfolio as a solution to this problem and the Minister's parliamentary answer of 24 June 2010 offered some reassurance on that particular issue:

“For the third sector model to work, British Waterways will have to have access to its estate, or a large proportion of it, for it to gear up funding for sustainable funding in the future. I can assure him that it will not proceed unless it is locked in, in that way. Those are the negotiations that we are taking forward with British Waterways.”

This would appear to be a positive approach by the Government. However, the Minister's statement did little to contradict the widely held assumption that the Government's preferred outcome is for BW to retain the property portfolio but to lose, year on year, an increasing part of its GIA. This would mean that the new third sector body might need to sell part of its property portfolio each year to make up for the lost grant. But of course this would reduce its opportunity to earn development income in the future and the structural deficit would rise as the property portfolio shrinks.

Unless income is increased, the current funding deficit will accumulate to at least £200 million by 2020. This figure could well become higher if GIA is reduced during the same period. So a move to the third sector is not a complete and secure solution to even BW's present funding difficulties. And of course BW's plan does nothing to resolve the funding and structural problems faced by the rest of the inland waterways sector.

7.3 The merger of British Waterways and the Environment Agency's navigation activities

On several occasions in the past twenty years, the UK government has considered the possibility of merging the navigation responsibilities of the EA with BW. After the publication of *Waterways for Tomorrow* in June 2000, Defra carried out a formal review which eventually concluded that EA should retain its navigations and that a merger policy should not be pursued. In the light of that decision the EA Board made a series of policy commitments aimed at maintaining high standards on its navigations.

Recently, however, Defra has again started to consider the option of transferring the navigation responsibilities of EA to the new third sector organisation when that new body is set up. The Minister confirmed that this transfer was under consideration in his reply to a parliamentary question on 24 June 2010:

“We will be looking in detail at options for a third sector model that will be appropriate for British Waterways, including the possible inclusion of Environment Agency navigations.”

Although the prospect of a merger is currently being discussed in the context of the proposed move of BW into the third sector, it is sensible to consider two separate issues:

- is there a good case for a merger and, if so,

- should a merger be timed to take place as part of the transformation of BW into a third sector body?

The case for a merger

At first sight there appear to be financial advantages in bringing the two largest navigation authorities together. The new organisation could be expected to achieve some economies in administrative costs and the advantages of integration of responsibilities.

However BW and EA navigations operate in different parts of the country so there is little overlap and duplication in operational staffing and the potential for a proportionate lowering of head office costs is reduced by the fact that the EA's navigations are already part of a large organisation and the head office costs carried by EA's navigations are already substantially lower than those of BW. Nevertheless, based on figures in other amalgamations of this nature, savings in the combined administrative costs of the two organisations of about 10% should be achievable.

Impediments that stand in the way of a successful amalgamation are significant. User service standards including the staffing of all locks on the non-tidal River Thames are higher than provided on the BW navigations and any reduction in standards would be difficult to accomplish. An attempt by the EA in 2008 to reduce the number of residential lock keepers on the Thames was strongly opposed by users and by MPs, and the Agency eventually withdrew the proposals.

The EA is able to sustain the high cost operation because, as an organisation which manages all aspects of the river catchment, its flood risk management budget meets the cost of operating and maintaining the Thames weirs. A new merged organisation would have no access to flood defence money and would either have to fund a high standard, high cost operation out of its normal revenue or would have to negotiate some arrangement for control and funding of the weirs with EA.

IWAC's conclusion is that although desirable to bring greater coherence to the inland waterways sector, the merger would be difficult to achieve and is likely to bring only modest benefits in the short term.

The timing of a merger

The transformation of BW from a rather centralised public sector organisation into a decentralised third sector body within which local managers will be expected to take full account of the wishes and needs of local communities, will be difficult. To expect BW to manage this transition at the same time as merging with EA navigations would place great burden on managers at all levels in the new organisation. It is also important to appreciate that no senior EA manager is likely to transfer to the new organisation at the time of an amalgamation so the EA navigations in the third sector body may need to be managed by staff unfamiliar with EA's rivers. This in turn will increase the pressure on the new organisation. Any attempt to handle both these complex issues at the same time could lead to a lengthy period of dislocation and perhaps even confusion.

One argument advanced is that amalgamation with EA's navigation interests would help to change the culture of BW. This is highly doubtful. If no senior EA manager transfers to the new organisation, the BW approach to managing and directing its business is likely to prevail for some considerable period and little change in culture is likely to result from the merger.

Views have been expressed by some boating organisations that the transformation of BW into a third sector body should take place and that if and when that change programme is successfully accomplished the amalgamation with all its organisational, political and financial implications might then be reconsidered and addressed. This seems to be a sensible approach.

7.4 Asset ownership

There are many policy issues which need to be resolved before final decisions on the way forward with a third sector body can be taken. One key issue is who would own the assets? Day to day responsibility for the management of the assets would lie with the Trustees of the new body but, in the absence of primary legislation, the UK government would remain as the asset owner. At present this seems to be the favoured option.

An alternative would be to transfer ultimate responsibility and liability from government to the new, third sector body. Were this to happen, the nature of Trusteeship and the responsibility of the Trustees

would change significantly. For example, the risk of cost escalation arising from breaches, tunnel collapses and floods is substantial. Without the support of government the role of the Trust and the position of the Trustees would be unsustainable.

This difficulty could be ameliorated by highly supportive contractual arrangements between the government and the new third sector body. However the question is: would government chose to contract with an independent, third sector body to provide sufficient comfort to protect the long term stability of the sector? In the absence of this level of guarantee, IWAC concludes that there is little merit and many risks in a model which involves the transfer of assets to the third sector organisation.

7.5 A model for the future

Whatever decision the Government makes about the future of BW, it should aim to ensure that any new structure can be adapted to achieve a wider purpose. This report has demonstrated many inefficiencies and weaknesses in the current structural arrangements. Any restructuring of BW should take account of the need to address the wider problems of the inland waterways sector and should be a step towards a more comprehensive solution. Section 8 below suggests how a more comprehensive reform programme might be constructed and how it might be implemented.

Conclusions

The proposal to create a new third sector body to replace BW has significant potential advantages but will not resolve many of the current funding problems of BW and will do little to address the inefficiencies and weaknesses in the structural arrangements of the inland waterways sector as a whole.

Even if new sources of funding were to be found for the third sector body which replaces BW, it will take time before significant income is built up, and the cumulative deficit could well grow so large as to have a very damaging effect on the condition of the assets managed by the new body.

The change in BW's status and culture will be difficult to achieve and requires considerable management skill. The new third sector body would need to be supported by public funding at a substantial level during the transitional period in order to maintain the network in a sustainable condition.

The merger between BW and EA's navigation interests would be desirable to bring greater coherence to the inland waterways sector, but would be difficult to achieve and is likely to bring many problems and only modest benefits in the short term.

. To expect BW to manage a merger with EA navigations at the same time as BW is moved into the third sector will place great burdens on managers at all levels in the new organisation and could lead to a lengthy period of dislocation. The less risky approach would be to make the move to the third sector first and, providing the transformation is successful, plan the merger for some time later.

IWAC expects the ownership of BW's assets to remain in the public sector and can see little merit and many risks in a model which involves the transfer of assets to the third sector organisation.

Any restructuring of BW should take account of the need to address the wider problems of the inland waterways sector and should be a step towards a more comprehensive solution.

Section 8

Structure and Governance: Comprehensive Proposals for Reform

8.1 Introduction

This Section looks beyond the current proposals for BW and seeks to design a new and comprehensive structure for the waterways sector as a whole. Ideally a reformed structure should address the considerable weaknesses and inefficiencies in the current arrangements and provide a worthwhile basis for improvement in the future. The reformed structure proposed in this Section is not designed primarily to meet the challenge of the cuts programme but to ensure that the sector as a whole is fit for purpose through the next decade and beyond.

In view of the many weaknesses that arise from the fragmentation of ownership and management, the new structure should have the potential to embrace and involve all parts of the sector. However it must be recognised that some organisations would prefer to continue to operate on their own under their present arrangements despite the benefits which could accrue from being part of a reformed structure. Any development plan must include this element of flexibility.

BW would not necessarily need to be in the third sector for the reforms discussed here to take place. Clearly BW would have a role to play in assisting government in achieving a new body or bodies, but this aspect of BW's role in the process of reform is not dependent on any particular precondition concerning its status.

The need for a greater level of engagement with local communities, local authorities and local businesses suggests that the new structure should be highly decentralised. The design must also avoid giving smaller organisations any impression that their identity would be lost in the new reformed structure.

A structure designed on the basis of the principles outlined below will have a good chance of delivering a waterway system that meets the needs of local communities and the nation as a whole, while retaining the commitment and engagement of existing stakeholders and partners.

8.2 Main elements of a reformed structure

Although the sector as a whole, with expenditure of well over £200 million in England and Wales, is a large business by most standards this should not necessitate adopting an over complicated organisational structure. The reformed structure should be as simple and as transparent as possible.

So the structure should have:

- few layers of direction and management;
- clearly identified roles and responsibilities; and
- maximum delegation of responsibilities to local level within a simple framework of accountability.

The structure should:

- be easy to deal with at local level;
- facilitate partnership working with a wide spectrum of interested parties from both the public and the private sector; and
- have the potential to reduce the sector's dependency on government funding.

Taking account of these principles, IWAC proposes that the reformed structure should consist of the following elements:

Local business units

Creating locally based business units is at the core of the proposal. The local business units would manage the use of the waterways and associated facilities within defined areas. The proposal aims to harness the strong desire in the waterways communities for local decision making based on close engagement with the local community. It is broadly consistent with BW's forward plans. The local business units would have responsibility for both operational and financial performance assessed against pre-determined, agreed objectives. Built into the local management's key performance objectives should be the requirement to gain and retain the support of the local community.

IWAC's publication, "*Working Together - Effective Waterway Partnerships*" stressed the importance of partnership working in local communities. This aspiration is the key to the concept of locally based business units charged with maintaining and promoting the waterway in a particular area.

The local business units would seek to involve key local stakeholders in the affairs of the Unit. Involvement is intended to achieve active participation in the direction, management and operations of the business by all key players in the locality both from the public and private sector. The philosophy of the new reformed organisation is that involvement will yield substantial benefits to the whole network. The initiative by the current Government to establish Local Enterprise Partnerships would also link into the local business units proposal with the commitment to involve the voluntary and private sectors locally.

The task of dividing England and Wales into manageable local business units is beyond the scope of this report. However the guiding principle should be that the local business units should be small enough to ensure a sense of local identity and to allow considerable local engagement. This suggests that they might be rather smaller than those currently contemplated by BW.

The non-core specialist businesses

In any decentralisation plan, there is a risk that indirect overheads are replicated in each area, increasing costs and leading to variations in quality. To avoid this mistake it is proposed that a number of centralised specialist businesses be established which could provide support services to all local business units. It is suggested that there could be three different types of non-core, shared and specialist businesses:

- Engineering
- Property
- Support services, like human resources and legal.

The primary objective of each specialist business should be to provide services to all parts of the inland waterways network. The specialist businesses should be a standalone profit centre/business with agreed targets for performance and for profitability. They should be empowered to take on work outside the sector as a means of generating additional revenue but this should only happen where it is commercially prudent to do so. Consistent with the policy of decentralisation, the non-core businesses should have responsibility for both operational and financial performance assessed against agreed objectives. The aim should be to make each specialist business into a centre of excellence.

Each specialist business should be required to tender for service provision both for the Local Business Units within the network and for any potential external customers. The Local Business Units may choose to obtain other competitive quotes.

The non-core specialist businesses would be required to bid for an allocation of available funds along with the Local Business Units. Funding would also come in part at least from the profits of the business. Subject to reasonable systems of accountability and stability of ownership, the specialist businesses should also be empowered to raise funds from external sources.

A Strategic Authority

Overseeing the local business units and the non-core businesses would be a compact Strategic Authority. The staffing of the Authority would be kept low. The functions would not include operations. It would develop a strategic plan for the inland waterways sector in England and Wales as a whole after full consultation with stakeholders.

The Strategic Authority would receive and distribute all public funding. It would be responsible for agreeing business plans with Local Business Units and with the non-core businesses. It would monitor performance against these business plans. It would not be the function of the Strategic Authority to manage the implementation of the plan on a day to day basis. That responsibility would be delegated to the Local Business Units and to the non-core specialist businesses.

8.3 Other Issues

The museums

Subject to agreement The Waterways Trust Museums (TWT) could also be included in the overall structure. Because their business is distinct from the management of the waterways it is proposed that the TWT museums are managed in a separate body sitting alongside the non-core businesses. The organisation of this business unit could be determined at the appropriate time in the implementation process. Independent waterways museums should also be given the option of being included in the overall structure as part of the new Museum body.

The community boat organisations

There are currently 71 community boat organisations registered with the National Community Boats Association. They are predominantly voluntary organisations and registered charities and represent an important group of users of the inland waterways in England and Wales undertaking valuable work directed towards increasing social cohesion. It is important that these organisations are supported by the new structural arrangements outlined in this report. How this is to be achieved could vary from region to region but the management of the new reformed organisation should welcome and encourage their involvement and participation.

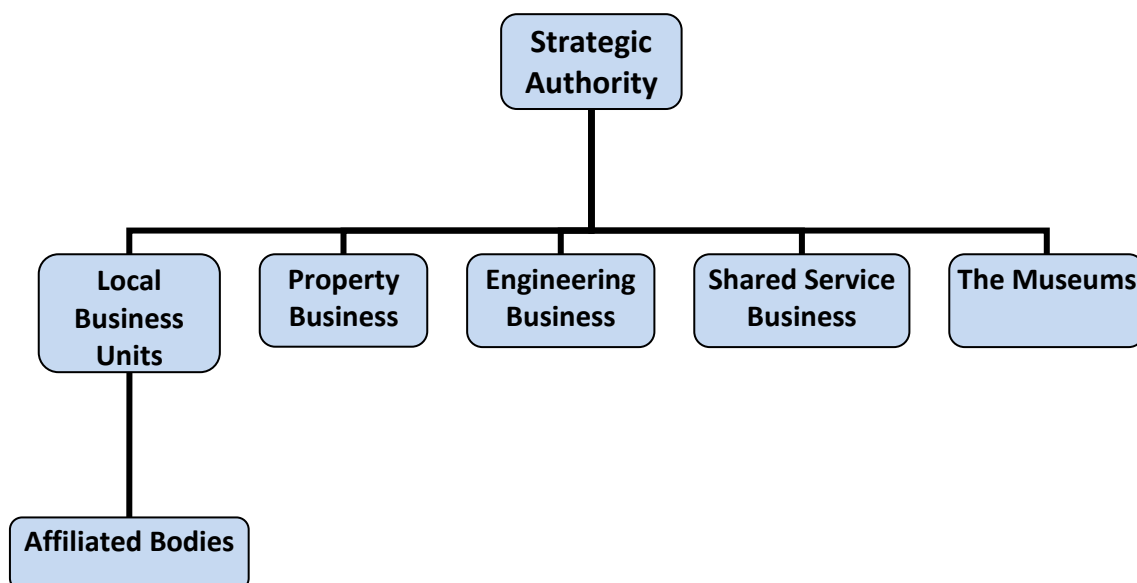
Affiliated bodies

In the introduction to this Section it was recognized that some existing organisations may have concerns about becoming absorbed into this new and large organisation. It is to be hoped, however, that such bodies would not feel precluded from an involvement with the new body. It would be essential to ensure that there was open, two-way communication between both parties primarily through affiliations with the local business units. It would also be important that those bodies not joining the new structure should have access to the services which the new body could provide.

Scotland

This report is about England and Wales. The option, however, is structured in a way that would enable the Scottish waterways network to become associated with the new authority if that were the will of the Scottish Government.

The following diagram illustrates how the reformed organisation would be structured:



8.3 Governance of the reformed structure

Whether the new reformed structure should be located in the public sector or should be part of the third sector will be a political judgment. IWAC believes that either could be successful provided long term funding arrangements are secured. However, whatever the aspirations at the outset, there is a danger that managers in the new reformed structure may tend to slide back into conventional business behaviour unless the principles of decentralisation, local engagement and stakeholder participation are reinforced by suitable governance arrangements.

If the new reformed organisation is located in the public sector, IWAC proposes that at least three user and stakeholder representatives are appointed to the Board of the Strategic Authority. At least one of these Board members should represent local authorities. In addition, each local business unit should have an Advisory Committee with representatives drawn from the local community and from users. It would be advisable about twice a year for the Chairs of the Advisory Committee to meet the Board of the Strategic Authority to review arrangements and accountabilities.

If the new reformed organisation is located in the third sector, IWAC proposes that the Governing Council is made up of users and stakeholders, including local authorities, and is responsible not only for appointing and dismissing the Trustees but also for discussing and approving the Corporate Plan.

8.4 The benefits of the new reformed waterways structure

It is IWAC's view that the new reformed waterways structure has the potential to deliver substantial benefits in terms of:

- adopting a more cohesive approach to managing the sector;
- grasping the opportunity to achieve improved operating efficiencies through economies of scale;
- spreading best practice to all parts of the sector;
- strengthening the long term financial position of the sector; and
- establishing a single culture across the sector appropriate to the management and development of a great national asset.

Although not all the benefits can be identified and evaluated at this stage, as currently envisaged the new reformed structure should deliver the following significant benefits:

- a simplification of the organisation of the sector by bringing all parts into one overall body yielding a significant reduction in central administrative and back office costs. It is estimated that these costs could at present be as high as 15% of total expenditure, or an annual figure of £40 million. Experience in other relevant organisations would indicate that a restructuring of the nature described in this option should yield net savings of 15/20%. This would put the annual benefit from reduced central administrative costs in the range £5 to £10 million:
- the creation of an organisation large enough to employ, directly and indirectly, the specialist skills necessary to develop the commercial opportunities described earlier in this report;
- the creation of an organisation which has the authority and skills to market the inland waterways as an important part of the visitor economy;
- a strong local focus which is well placed to raise funds from individuals and companies in local communities;
- the provision of a commercial focus to non-core specialist businesses enabling them to generate additional funding;
- the encouragement and involvement of a wider range of individuals in the management of the business making use of specialist knowledge and providing an understanding of the local environment, issues and opportunities;

- the enablement of local government to be actively involved in all parts of the sector leading to a greater commitment for support from this part of the public sector and access to a wider spread of funding; and
- greater potential for the involvement of volunteers and of the voluntary sector.

The benefits are not limited to the financial. By creating a new environment with all parts of the sector working together with local communities, a new sense of enthusiasm and energy can be created which will engender important long term social benefits, including community engagement and social inclusion.

8.5 Implementation issues

The objective of creating a comprehensive organisation for the waterways requires a stage by stage approach which enables the many difficult obstacles to be overcome in a considered manner without placing unreasonable burdens on the management of the new organisation.

BW, EA, Middle Level and the Broads Authority are public sector bodies and Parliament has the power to decide how they should be constituted and managed. Whether or not BW stays in the public sector or is transformed into a third sector body, it should move closer to local communities and to users. This culture change will be difficult whether in the public or the third sector but it is vital that the change is made. To this end Government should set BW challenging objectives and Defra should ensure that they are achieved within a reasonable timescale.

Membership of the new reformed waterways body must be attractive to the smaller navigation authorities because their involvement can only realistically be achieved by agreement. To encourage the process of cooperation, a small central services agency could initially be established to provide engineering, legal, administration, and human resource services to all navigation authorities. The expertise should be supplied by BW and EA and, with a reasonable cap on time and resources, could be accessed free by all other navigation authorities. The central services agency could be given the task of driving efficiency by the promotion of best practice.

Once BW has demonstrated to government, users and stakeholders that it is achieving the transformation that is required, the navigation responsibilities of EA and then the Middle Level should be combined with BW to create the reformed waterways body in embryo form. At this stage the central services agency should become part of the newly created Strategic Authority and the non-core businesses should be constituted.

On the basis of discussions that have taken place in the past, it can be anticipated that a number of smaller navigation authorities will wish to join the new reformed waterways body. Others, perhaps including the Broads, may wish to remain independent. To maintain momentum and to achieve the greatest level of integration consistent with harmonious relations between navigation authorities, the concept of affiliation, described above in 8.3, should be developed. An affiliated navigation authority would have the right to attend the appropriate Advisory Committees, be regularly briefed by local business unit management, and would have access to the central services. This would give the affiliated authority considerable support and an insight into the workings of the reformed waterways organisation. The timing of the start of a process of formal joining on the part of the smaller organisations would be deferred until such times as the administration was in place and working, which would depend on overall progress with the package of reforms.

It is not envisaged that affiliation would continue indefinitely. At some stage each affiliated navigation authority would need to decide whether to remain independent or to become fully involved in the reformed waterways organisation. If it decided to remain independent it would then be expected to pay for any services which it receives at reasonable commercial rates.

The reformed waterways body should remain close to independent navigation authorities and, where the opportunity arises, should work in partnership with them. Further amalgamations can only be achieved by the reformed waterways body demonstrating by its actions that integration brings more benefits than separation. If the reformed waterways body stays true to its core principles, the new body is likely to be viewed as a safe haven for navigation authorities that want to combine a greater measure of financial security and specialised support with local engagement and decentralised management.

Conclusions

There is the opportunity to achieve long term stability and financial security, not just for BW but for the inland waterways as a whole, by the creation of a new structure and new governance arrangements which:

- **have the potential to include all parts of the sector;**
- **address the inefficiencies and weaknesses in the current system;**
- **are highly decentralised;**
- **facilitate the involvement of stakeholders;**
- **actively engage with local authorities;**
- **create a single culture based on the principles of participation and stewardship; and**
- **preserve the identity of the smaller organisations.**

The key element in the proposed new reformed structure would be the creation of locally based business units charged with operating, maintaining and promoting the waterway in a particular area.

Engineering, property, support services and museums would be established as non-core specialist businesses serving the locally based business units.

A compact Strategic Authority would be formed to set objectives, give strategic direction and to receive and distribute public funding.

The principles of decentralisation, local engagement and stakeholder participation should be reinforced by suitable governance arrangements.

Implementation of this new structure could be by a stage by stage approach, involving amalgamations and the use of the concept of affiliation to provide smaller navigation authorities with short and medium term benefits while paving the way for the longer term integration of the sector.

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Glossary

AINA	Association of Inland Navigation Authorities
BA	Broads Authority
BW	British Waterways
Defra	Department for Environment, Food and Rural Affairs
EA	Environment Agency
Efra Committee	Environment, Food and Rural Affairs Select Committee of the House of Commons
GIA	Grant-in-Aid
IWA	Inland Waterways Association
IWAC	Inland Waterways Advisory Council
LEP	Local Enterprise Partnership
NCBA	National Community Boats Association
PLA	Port of London Authority

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* These reports are available on the IWAC website, www.iwac.org.uk