P.2025/25

**THE STATES OF DELIBERATION**
**of the**
**ISLAND OF GUERNSEY**

**STATES' TRADING SUPERVISORY BOARD**

INCORPORATING OUR TRADING BUSINESSES

The States are asked to decide:-

Whether, after consideration of the policy letter 'Incorporating Our Trading Businesses" dated 13th February, 2025, they are of the opinion:-

1. To agree in principle that Guernsey Water, Guernsey Ports and States Works should be incorporated as States' Trading Companies under the provisions of the States Trading Companies (Bailiwick of Guernsey) Law, 2001;

2. To agree that Guernsey Water should be the first business to be incorporated in accordance with Proposition 1 by 31st December, 2027, and to direct the States' Trading Supervisory Board to initiate a project to do so, reporting back to the States of Deliberation as necessary on the detailed practical and legislative requirements;

3. To direct the States' Trading Supervisory Board to continue investigating the incorporation of Guernsey Ports and States Works, taking into account the further considerations set out in section 5 of this policy letter, and to report back to the States with the results of those investigations by 31st December, 2026; and,

4. To note that the funds required to undertake the works required in Propositions 1 to 3 above are provisionally estimated not to exceed £500,000, which will be funded by the businesses themselves.

The above Propositions have been submitted to His Majesty's Procureur for advice on any legal or constitutional implications in accordance with Rule 4(1) of the Rules of Procedure of the States of Deliberation and their Committees.

**THE STATES OF DELIBERATION**
**of the**
**ISLAND OF GUERNSEY**

**STATES' TRADING SUPERVISORY BOARD**

INCORPORATING OUR TRADING BUSINESSES

The Presiding Officer
States of Guernsey
Royal Court House
St Peter Port

13th February, 2025

Dear Sir

## 1. Executive Summary

1.1 Since its establishment in 2016, the States' Trading Supervisory Board (STSB) has applied a more commercial and customer-focused approach to the management and operation of the States' unincorporated trading businesses, these being: Guernsey Ports; Guernsey Water; Guernsey Dairy; Guernsey Waste; States Works; and, the CI Lottery. In doing so, it has sought to strike the right balance between commercial considerations and the wider public interests and needs of Islanders, recognising that the primary purpose of the businesses is to deliver essential services to the community.

1.2 The STSB has adopted a range of organisational arrangements for the businesses to enable effective and efficient management and operations. Whilst the businesses are now operating with a stronger commercial focus, it has nevertheless continued to consider whether current operating models are inhibiting them from developing their full potential. Having considered the recommendations of a review that it commissioned by Interpath, a Deal Advisory and Restructuring specialist, it has concluded that incorporation of Guernsey Water, Guernsey Ports and States Works as wholly-publicly owned companies is the key to fully unlocking that potential.

1.3 Incorporation offers a significant opportunity to increase accountability and autonomy within the businesses for their effective and efficient operation, which will drive a more commercial, agile and customer focused approach. It will empower them to improve and diversify services and performance and better enable them to exploit the assets at their disposal by providing them with fiduciary responsibility and autonomy in areas such as:

- Infrastructure planning and funding, with investment decisions informed by long-term asset management plans and tariff strategies that transcend political electoral cycles;

- Staff terms and conditions of employment, enabling these to be tailored to the businesses' specific commercial needs and providing more agility and flexibility to adjust business models in response to changing market dynamics and commercial opportunities that arise from time to time;

- Pay awards, noting that pay costs account for over 40% of the businesses' total costs, but that pay awards are currently outside of their control; and,

- Corporate services (such as finance, information technology and human resources). These critical functions are provided by the States' shared service corporate functions and, as such, are outside of the businesses' direct control and are not tailored to their specific operational and commercial requirements.

1.4 Incorporation will reduce political involvement in operational decision making, leaving the companies' Boards and management freer to operate more commercially and dynamically. However, political influence can continue to be exerted by the States through an active shareholder function responsible for setting clear objectives for the businesses that are aligned with the Island's wider economic, social and environmental policies. In this manner, incorporation is a step that can be taken without compromising the businesses' public service ethos and responsibilities. The STSB believes that, as incorporated companies, they can continue to act in the long-term best interests of Islanders. Whilst acting more commercially, they can and must continue to recognise the critical role they play in supporting the delivery of the States' policy objectives.

1.5 In short, incorporation is intended to enable the businesses to continue providing essential public services to the Island, but in a manner which is more commercial, self-sustainable and customer focused and which minimises future requirements for States' funding.

1.6 The STSB supported Interpath's conclusion that neither the Guernsey Dairy nor Guernsey Waste were suitable for incorporation. The review identified factors that meant the Dairy's viability as a standalone entity was low and that the focus should be on continuing to improve performance as an unincorporated business. With Guernsey Waste, it noted that its strategic objective was to reduce waste volumes and, in doing so, the income that it can earn commensurately. In any event, its main purpose is to act as a commissioning body for waste management services, functions which are better suited to continue within government.

1.7 Whilst this policy letter is proposing that incorporation be agreed in principle for Guernsey Water, Guernsey Ports and States Works, it acknowledges that this will entail a significant programme of work across multiple different workstreams. In the case of Guernsey Ports and States Works, it will also be contingent on a number of external policy matters. These include understanding the impact that land transfers to the Guernsey Development Agency might have on the Harbours' real estate and its associated commercial potential and considering whether States Works will continue providing the Islands with an emergency support service to assist the Island in recovering from unplanned incidents or emergency situations. Work also needs to continue with a Business Improvement Programme initiated by the STSB in 2024 that is intended to return all three businesses to a sustainable financial position within three years.

1.8 However, the STSB does believe that Guernsey Water is in a sufficiently mature state of organisational readiness such that the States can agree now to initiate a programme of work to incorporate that business, noting that the process itself is unlikely to be completed until the end of 2027. There will be lessons to be learned from that process and the advantage of a phased approach, with Guernsey Water moving first, is that those lessons can be applied to the incorporation of Guernsey Ports and States Works at a later date.

## 2. States' Trading Businesses

2.1 Upon the recommendation[1] of the States' Review Committee (SRC), the STSB was first established in 2016 and, within a framework of policies and guidance established by the States from time to time, is responsible for:

- Firstly, acting as shareholder of the States' incorporated trading companies, these being: Guernsey Electricity (GEL); Guernsey Post (GPL); Aurigny Air Services (formerly Cabernet); and, Jamesco 750; and,

- Secondly, for ensuring the efficient management and operation of the States' unincorporated trading businesses, these being: Guernsey Ports; Guernsey Water; Guernsey Dairy; Guernsey Waste; States Works; and, the Channel Islands Lottery.

2.2 The SRC recommended the STSB be established to provide focused, active and prominent political oversight of the States' trading activities. In doing so, it was agreed that the Board's constitution should draw together both Members of the States and individuals independent of the States with appropriate commercial skills and experience of corporate governance, board and shareholder responsibilities, strategic and operational benchmarking etc. As such, the STSB's

[1] Billet d'Etat XII of 2015 – States' Review Committee – Organisation of States' Affairs

constitution includes up to two voting members who are not States' members.

2.3 The STSB's aim is to ensure that the trading businesses will be a group of well-managed, efficient companies that deliver a return in the long-term best interests of Islanders. Within this context, returns are not measured just in financial terms, but also against the contribution that the businesses can make to the Island's social, environmental and economic objectives. Accordingly, the STSB has sought to ensure its businesses deliver cost-effective and innovative services, whilst operating responsibly in the best interests of the community. Its aims have been:

- to harness the advantages of public ownership and control of critical infrastructure, whilst applying a more commercial and customer focused approach to operations and service delivery; and,

- to strike the right balance between commercial considerations and the wider public interests and needs of Islanders, recognising that the primary purpose of the businesses is to deliver essential services to the community.

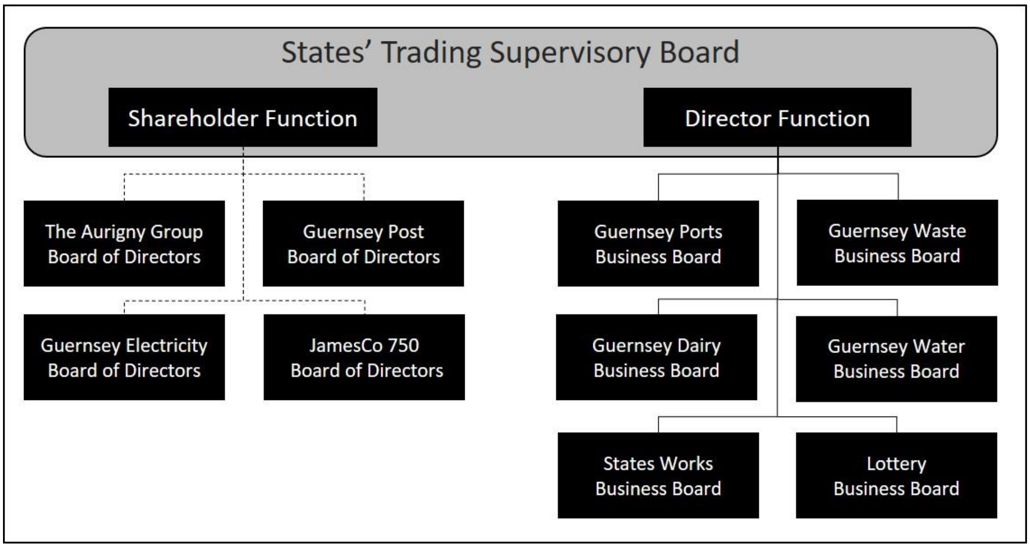
2.4 The current governance arrangements adopted by the STSB are as follows:

- In the case of the unincorporated businesses, it has established "company boards" for each business. Each board's role is to challenge established practices and assumptions and to develop long-term business plans for subsequent approval by the STSB. The boards are also responsible for ensuring the efficient and effective leadership, management, operation and maintenance of the businesses and ensuring they are aligned with the States' wider strategy and policy framework.

  These boards operate as sub-committees of the STSB and include a number of experienced business leaders, who serve in a voluntary and advisory capacity and bring with them additional commercial and private sector expertise. They operate within a scheme of financial and operational delegations that allow decisions to be delegated down to the lowest level possible, enabling quicker decision making;

- In the case of the incorporated businesses, the STSB has adopted an active role as shareholder, including the establishment of formal and regular reporting arrangements with representatives of their Boards of Directors. The focus is on reviewing and approving their strategic plans to ensure they are aligned with those of the States, engaging with them on financial matters and holding them to account in terms of performance against those plans and their agreed shareholder objectives.

The diagram below illustrates the current organisational structure for the STSB and the businesses for which it is responsible:




## 3. Incorporation - Background

3.1 The States last considered the possibility of incorporating more of its trading businesses in 2012. After considering reports[2] from the from the former Public Services Department (PSD), the States resolved that the PSD should carry out further investigations into establishing Guernsey Airport and Guernsey Harbours (now Guernsey Ports) and Guernsey Water as incorporated trading companies.

3.2 Those resolutions were superseded by the States' decision to establish the STSB in 2016 and by the governance arrangements that were subsequently put in place to drive a more commercial approach within the unincorporated businesses for which it is responsible. The States rescinded[3] the resolutions in 2021, albeit it was noted at the time that the STSB would continue to keep under regular review the most appropriate corporate governance structures for each of its businesses.

3.3 Therefore, the STSB has remained mindful of the arguments that have previously been put forward in support of incorporation, including those presented by the PSD in 2012. The general theme of those arguments was that incorporation would provide increased accountability and autonomy for performance at the business level which would, in turn, drive a greater commercial focus. Specific examples included:

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[2] Article 10 of Billet d'Etat III of 2012; and, Articles 11 and 14 of Billet d'Etat V of 2012 – Future Business Environment(s) for Guernsey Water & Guernsey Wastewater, Guernsey Airport and Guernsey Harbours (respectively)

[3] Resolution 7 of Billet d'Etat VI of 2021 – Government Work Plan – Stage 1

- Allowing the businesses to determine their own bespoke terms and conditions for the employment of their staff, rather than those determined centrally by the States. The concern was that the current centralised "one-size fits all" arrangement effectively disenfranchises the businesses and could inhibit the more efficient and flexible deployment of staff and the exploitation of commercial potential;

- Providing the businesses with direct control over periodic pay awards. Pay costs account for circa 44%[4] of the businesses' total costs, but pay awards are determined centrally by the States. Whilst the STSB is consulted on such matters by the Policy & Resources Committee, it remains the case today that its businesses have no direct control over the pay awards that drive a substantial part of their cost bases;

- Allowing the businesses to bring "in-house" a range of corporate services currently provided to them by the States (at cost, but currently without Service Level Agreements). These include human resource (HR), finance, legal and IT functions. The focus of attention demanded of these functions by a trading business differs to that required by a States' policy Committee. However, it can be difficult to achieve that level of focus when competing for the limited available shared resources; and,

- Allowing the businesses to adopt procedures, protocols and systems of corporate governance that were more aligned to the private sector, rather than the public. This could enable them to be more "fleet of foot" when taking advantage of opportunities to better realise their commercial potential.

3.4 The STSB has also noted the case[5] made in Jersey in 2014 for incorporation of their Ports. This included the following rationale and arguments, consistent with the above and those being set out later in this policy letter:

- It would provide the business with the ability to respond to opportunities and challenges and react to market dynamics in a commercially agile, focused and timely manner;

- It would provide greater commercial freedom and, with appropriate incentives, performance could improve significantly;

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[4] Based on 2025 budgets for unincorporated trading businesses. Excludes HR, IT, Hub, Legal and Finance services provided to the businesses centrally by the States' shared corporate functions, for which a separate charge is paid by them to the States.

[5] Ports of Jersey - The Case for Incorporation

- It would enable the agility, focus and capability required to deliver commercial development projects on the Ports' estate to build cash reserves that could be utilised to address the long-term capital requirements;

- With the (then) States of Jersey retaining 100% ownership of the business, safeguards could be put in place to ensure alignment between the government and the company on forward strategic direction.

The case in Jersey cited a review of incorporated governance arrangements for Ports in other jurisdictions, which highlighted benefits including: the adoption of a more commercial approach to the development of the entire asset base; an increase in autonomy resulting in more dynamic decision making; a stronger focus on business and customer satisfaction and on sustainability and improved productivity; and, more agility to develop and deliver commercial initiatives.

3.5 Any discussion about incorporation must also acknowledge that the process would, by definition, reduce political involvement in operational decision making, with the companies' Boards of Directors and management freer to operate more dynamically and commercially. That can occasionally result in tension between the business and the States. The successful management of such tension relies on the establishment of the following: a clearly established strategic policy framework within which to operate (such as the Electricity Strategy); clearly articulated shareholder objectives for the company (such as those established by the States for Aurigny[6]); and, a clear and documented understanding of how the relationship between the States and the company will operate, including delegated levels of decision making authority (the STSB has already put in place Memoranda of Understanding with the incorporated businesses for this purpose).

3.6 The STSB does believe that the unincorporated businesses are now operating with a stronger commercial focus and acumen. However, given its previous commitment to monitor the optimum corporate structures for the businesses, it has commissioned a review of different operating models, including incorporation, to assess whether these would offer up opportunities to develop further their commercial potential, but without compromising their public service ethos. This policy letter sets out the results of that review, the intention being to provide a full assessment for the States of the pros and cons of incorporating some or all of the unincorporated businesses, including further analysis of some of the arguments above that have historically been put forward in support of doing so.

[6] Article 12 of Billet d'Etat XX of 2021 – The Aurigny Group – Financial Sustainability

## 4. Trading Businesses – Review of Operating Models

### 4.1 Scope of Review

4.1.1 In 2023, the STSB commissioned Interpath to undertake a strategic review of the five unincorporated trading businesses (excluding the Channel Islands Lottery). Interpath is an independent advisory business, which supports businesses, their investors and stakeholders across a broad range of specialisms spanning deals, advisory and restructuring capabilities. The purpose of the review was to determine whether incorporating some or all of the businesses, either on a standalone basis or in combination with another, could deliver better outcomes and value for the public, the States and for the businesses themselves. The review included consideration of the following:

- **Strategy** – Understanding the key strategic objectives of each business and their future ambitions;
- **Financial** – Reviewing financial performance, including any potential capital funding requirements;
- **Operational** – Reviewing operational procedures in areas such as corporate governance, organisational structures and human resources;
- **Options** – Identifying potential options for improving performance, either under "business as usual" conditions, through incorporation or through other business combinations;
- **Further work** – Identifying what further work was required and next steps.

4.1.2 Given that the primary purpose of the businesses will remain the provision of essential critical services and infrastructure for Islanders, the STSB did not extend the scope of the review to include the possibility of privatisation. Its firm belief is that the States should retain full strategic control and oversight of the businesses if a recommended option is to incorporate. In that event, shares in the company would be wholly owned by the States, which could continue to leverage ownership of them to ensure their business plans supported the delivery of the States' related social, environmental and economic policies. Any profits would then be available for reinvestment in the businesses for the benefit of the Island, rather than for distribution to shareholders. By way of example, the STSB has previously established Shareholder Objectives for Guernsey Electricity that require it to ensure its activities are fully aligned with the States' Energy Policy and Electricity Strategy and that it develops a strategic plan that enables the delivery of the outcomes set out therein.

4.1.3 An Executive Summary of the report from Interpath is attached as Appendix I to this policy letter. The key themes, conclusions and recommendations arising from the report are set out below.

4.2 Key Challenges for the Trading Businesses

4.2.1 Interpath identified a number of challenges that affected all of the States' trading businesses, both incorporated and unincorporated, but which tended to have a more substantial and adverse impact on the latter.

4.2.2 The review identified that there has been a history of underinvestment by the States in the unincorporated businesses. There has been a depletion of their cash reserves in response to the returns target established under the Medium-Term Financial Plan adopted by the States in 2017 and, more recently, as a result of the COVID pandemic and the high inflationary environment. In the cases of Guernsey Water, Guernsey Ports and Guernsey Dairy, forecast capital investment requirements now exceed current operating surpluses.

4.2.3 Accessing capital to invest in infrastructure is critical to the sustainability of all the unincorporated businesses. The States' ability to prioritise the allocation of capital funding to the businesses is understandably constrained by many competing demands. However, the businesses have less ability to seek out alternative sources of funding given their unincorporated status. Investment decisions need to be informed by long-term asset management plans and tariff strategies that transcend the political electoral cycles and the shorter-term focus that they can entail.

4.2.4 The review noted that there has not been a consistent approach to asset management planning, with practice in this function operating at varying stages of development and maturity across the businesses. The STSB has been taking steps to address this and continues to invest in the asset management functions across its businesses. The aim is to reduce the risk of assets having to be replaced or repaired reactively when they fail and to ensure that proactive provision is made for their replacement as part of clear long-term capital investment plans. As its most asset intensive businesses, the focus of a lot of this work has been at Guernsey Water and Guernsey Ports. For example, whilst Guernsey Water has a well-established asset register, it has needed to invest in both the capacity and development of its personnel to ensure investment programmes and strategies for its different asset classes are fully integrated into its business planning processes. Guernsey Ports is investing in new IT facilities to support its asset maintenance and management systems. This will provide a central repository for all asset data, replacing a number of disparate systems that historically existed before the Harbour and Airports were integrated and enabling a more efficient and consistent approach to be taken to asset management in future. An ongoing challenge is recruitment, with Guernsey Water reporting challenges given the highly competitive nature of the employment market for asset management professionals, particularly where an infrastructure planning specialism is required.

4.2.5 Inflationary pressures have adversely affected the businesses' cost bases. A sustained improvement in their financial performance will require a combination of: improved cost efficiency; exploitation of commercial opportunities; and, increased tariffs. To that end, the STSB has already initiated a 3-year Business Improvement Programme across its businesses to place them on a more sustainable financial footing. However, public sector terms and conditions of employment leave the businesses with less agility and flexibility to adjust their business models to respond to those cost pressures. Increases in tariffs will usually require the introduction of legislation (Statutory Instruments) and, whilst that is rightly subject to political and public scrutiny, the reduced autonomy entailed results in uncertainty about future income levels.

4.2.6 The extent to which the businesses can leverage and respond to commercial opportunities is dependent on their freedom to operate and their ability to leverage the assets they manage. However, the review noted that their ability to react to such opportunities in a timely and agile manner is limited by the internal States' processes that can be involved in approving business cases. Additionally, extant States of Guernsey policies or legislation, coupled with sometimes conflicting commercial and political objectives, impinged upon the businesses' ability to operate more or wholly commercially. On the one hand, the businesses were being asked to apply a more commercial and customer focused approach, but on the other, they were still expected to operate within the operating parameters of the public sector. It can be unclear whether providing 'best service' should be of greater priority than, for example, operational efficiency or commercial success.

4.2.7 The review highlighted the challenge of recruiting and retaining key staff within a small Island community. Whilst this is not unique to the businesses, the inability to determine terms and conditions of employment that are tailored to their specific commercial needs rather than the wider States does compound the problem. More autonomy and flexibility to shape recruitment and compensation strategies would afford them greater opportunity to meet their talent requirements effectively.

4.2.8 Interpath acknowledged that the businesses benefitted from experienced and skilled operational delivery teams that were effective at ensuring the delivery of existing services. However, as a consequence, the risk was that they prioritised service delivery over commercial considerations. Successful commercialisation would require greater clarity of purpose and significant cultural change throughout all levels of the businesses, the latter being likely to take some time to embed. That process would need to acknowledge various "public service obligation" functions they are currently providing, but which would otherwise not be regarded as being a core or commercially viable parts of their trading activities (for example, the coastguard service provided by Guernsey Ports).

4.2.9 A wide range of services are provided to the businesses by the States' shared corporate functions. These are provided at cost, but currently without service level agreements (SLAs), and include financial, information technology, HR and legal functions. Whilst these are critical functions, the absence of SLAs mean that they are not within the businesses' control and nor are they tailored to their specific operational and commercial requirements. The businesses have only limited ability to influence the quality and speed of such services, despite how essential they are to effective decision making and efficient operations. The STSB believes it is important for the businesses to have direct responsibility and accountability in these areas in order to drive improved performance. A priority would be to develop an autonomous HR function for the businesses that would be able to prioritise its resources on ensuring that terms and conditions of employment and wider HR practices are fit for purpose and directly support the needs of their business plans, rather than the "one-size fits all" approach to HR that can be a feature of the States' centralised system.

4.2.10 In considering the challenges faced by the unincorporated businesses, the review also reflected on the experience of the incorporated businesses and what lessons might be learned from them. A recurring theme is that their greater autonomy has brought with it increased accountability for performance, which in turn drives a more commercial mindset. In the case of GPL, for example, that has underpinned the company's ability to work with its employees to respond swiftly to changes in market conditions, such as the loss of Low Value Consignment Relief, electronic substitution of traditional mail and the growth in parcel traffic. Experience with the incorporated businesses has also demonstrated the importance of their being provided with clear and focused shareholder objectives. The States' decision in 2021 to set new objectives for Aurigny Air Services provided a clear framework of outcomes that the new management at the airline was expected to deliver. Shareholder objectives must also be considered within the context of the States' wider policy framework and, in the case of GEL, the adoption by the States of an Energy Policy and Electricity Strategy provides a much stronger basis and clarity of purpose upon which to develop its strategic business plans.

4.2.11 Broadly speaking, the review observed that commercial and incorporated businesses have more agility and flexibility to respond to the challenges they face. Incorporation would not necessarily eliminate the challenges identified above, but they could help to mitigate or partially address them.

4.3 Assessment of Future Options

4.3.1 Three distinct options were considered for the future of the unincorporated businesses:

- Firstly, retaining a business as an unincorporated one, but identifying opportunities to: firstly, unlock 'current state' operational improvements; secondly, drive cost efficiencies, whilst improving revenues where possible; and, thirdly, utilise the improved financial performance to contribute towards the business' future funding requirements;

- Secondly, incorporating the business on a standalone basis and, in doing so: firstly, unlock its commercial potential; secondly, provide greater business autonomy and agility, including the opportunity to consider alternative ways of funding capital investment programmes; and, thirdly, remove restrictions regarding terms and conditions of employment to improve capability and retention; and,

- Thirdly, combine two or more of the businesses and then incorporating the combined entity and, in doing so: firstly, realise potential synergies and remove duplication of cost; and, secondly, improve economies of scale.

4.3.2 The analysis undertaken as part of the shortlisting process included a number of distinct stages, including the following:

- A review of historical financial operating performance to fully understand the main cost and revenue drivers;

- A sensitivity analysis of the 2024 budgets and a confidence review of their underlying assumptions;

- Identification of a range of potential improvement opportunities to grow/diversify revenues and reduce costs;

- The development of up to 4 scenarios for operating surplus/deficits. These were: firstly, a baseline scenario based on the 2024 budget; secondly, a "downside" scenario that downgraded the baseline on the assumption that some risks to costs and revenue did materialise; and, thirdly, one or two "upside" scenarios (depending on the business) that upgraded the baseline to reflect cost and revenue improvements at a lower and higher end of the range of opportunities identified. The result of that work was a range of forecast operating surpluses or deficits for each business;

- A review of forecast capital expenditure between 2024-26 and identification of the potential funding gap for the business, expressed as a range depending on the aforementioned operating surplus/deficit scenario in play.

4.3.3 Interpath adopted an objective scoring framework to enable it to systematically evaluate the potential options that it identified for the five unincorporated businesses. The design of that framework was underpinned by a range of core, commercial and public sector principles (see Appendix II). Initially a longlist of 25 options (see Appendix III) was established and then filtered against a range of macro, legislative and legacy factors. The process also applied a risk factor to reflect the inherent risk in making change. The longlist was reduced to a shortlist of 7 options that are set out in Table 1 below:

| **Table 1: Options Assessment – Shortlisted Options** | |
|---|---|
| Guernsey Ports | Incorporate (combined Airport and Harbour). Consider different BUs within. |
| Guernsey Ports | Split Airport and Harbour and incorporate one/both separately. |
| Guernsey Water | Incorporate as a standalone. |
| Guernsey Water | Combine with Guernsey Electricity. |
| Guernsey Water | Combine with States Works. |
| States Works | Incorporate as a standalone and scale up. |
| States Works | Combine with Guernsey Water. |

4.3.4 In the case of Guernsey Dairy, the review concluded that its viability as a standalone commercial entity appeared to be low. It identified the following factors in reaching this conclusion:

- Firstly, the Dairy's dual role, serving not just as a producer of milk for the Island, but also as a means by which funding is provided to help ensure Guernsey's unique rural environment and the Guernsey breed are maintained and protected. The current producer price is designed to support farmers to make sufficient profits to sustain their operations and their wider obligations under the farm management contracts, which constrains the Dairy's potential to operate as a self-sufficient trading entity;

- Secondly, the sub-scale nature of the Dairy business. Even without the above constraint, other dairy facilities rely on volumes or significant proportions of by-products to be viable, none of which are likely to be achieved in Guernsey at the scale required to cover fixed overheads and capital investment requirements.

Its recommendation is that the Dairy should remain unincorporated, with the focus on opportunities to improve current performance, including: potential efficiencies through the development of a new dairy facility; and, reviewing the use of the producer price paid by the Dairy to farmers as the means by which support is provided to the industry.

4.3.5 In the case of Guernsey Waste, the review observed that its strategic objective is to reduce waste but that, in doing so, the income that it earns reduces commensurately. Opportunities to counter this by increasing scale are not feasible in Guernsey, whilst options to reduce costs are constrained by its obligation to ensure facilities are available to manage all of the Island's different waste streams, even if uptake is low. Guernsey Waste's principal function is not to trade, but to commission waste management services. Rather than incorporating the business, the review recommended that it would be more beneficial for it to continue as a commissioning organisation within government.

4.3.6 The shortlisted options were then assessed against 10 critical success factors, which are summarised in Table 2 below:

| **Table 2: Shortlist Assessment – Critical Success Factors** | | |
|---|---|---|
| **Strategic** | **Financial** | **Operational** |
| Does the option allow the business to meet all its business objectives? | Does the option result in financial benefits / efficiencies? | Does the option alleviate operational risks / constraints? |
| Does the option align with the business' future ambitions? | Does the option result in significant additional financial costs? | Does the option provide improved value to customers? |
| Does the option enable the business to improve long-term financial performance? | Does the option enable the entity to become financially self-sufficient? | Is the option likely to succeed given the entity's ability to respond to changes? |
| | Does the option enable the entity to fund capital requirements? Does it pose a financial risk? | |

4.3.7 Having assessed the businesses against the above, Interpath recommended that Guernsey Ports, Guernsey Water and States Works should each be incorporated because of:

- the increased agility it would provide to leverage assets for commercial use;
- the increased financial autonomy and independence it would provide; and,
- the improved operational agility it would achieve.

4.3.8 In the case of Guernsey Ports, it recommended this should be incorporated as a single entity without splitting the Harbours and Airport. This option scored more highly than separating the Harbours and Airport because it provides better opportunities to use the size of the combined business to drive economies of scale and to attract talent. It also provides leverage to negotiate better terms for commercial opportunities that span both operations, such as car hire or duty-free concessions operating at the Airport and Harbours. The review concluded that retaining the combined entity would involve significantly less business change risk and would encourage shared working for complementary services, resulting in greater efficiencies and higher chances of success. Incorporating Guernsey Ports as a combined business would provide the most appropriate platform to unlock commercial opportunities. In the interests of transparency, Guernsey Ports' accounts already include separate financial statements for both the Airport and Harbours and that would continue under an incorporated model.

4.3.9 Consideration was given to combining Guernsey Water with GEL or States Works, recognising that this would provide opportunities for efficiencies and increased collaboration. However, those benefits needed to be balanced against the likely integration costs and risks of business change. The option of combining it with States Works was discounted because of the risk of change arising from Guernsey Water having to absorb a diverse set of new functions. A combination with GEL was discounted given the period of significant change that GEL is embarking on as a result of the Electricity Strategy and the work that it has to undertake to improve its financial sustainability. Accordingly, the review concluded that Guernsey Water should be incorporated as a single entity, noting that it has the potential to achieve good surpluses in future. Whilst the STSB accepts that it is not currently the right time to combine Guernsey Water with GEL, it has not discounted doing so in future and will keep the matter under review.

4.3.10 As a consequence of the above, the conclusion was also that States Works should be incorporated as a single entity. This recommendation was made on the basis that it would be allowed to scale up its operations to enable growth, for instance by competing for new private work in the market to drive growth and improve commercial performance. Incorporation would encourage States Works to be more cost efficient and could enable it to generate more revenues through better recruitment and retention of talent.

4.3.11 Summaries of Interpath's findings are set out in Tables 3, 4 and 5 below:

<table>
<tr><th colspan="5">Table 3: Guernsey Ports – Recommended Model:  Incorporate as a combined entity (Harbours & Airport)</th></tr>
<tr><td colspan="5">Rationale:<ul><li>Unlocks commercial opportunities and enables efficiencies of scale.</li><li>Aligns with other small self-sufficient air and seaport operators.</li><li>Combined entity minimises disruption of organisational change and potential dissynergies.</li></ul></td></tr>
<tr><td colspan="5">Current Key Constraints / Challenges:<ul><li>Significant capital requirements, including backlog maintenance.  Upcoming high priority & cost projects include QE2 Marina Gates replacement.</li><li>Historical operating deficits due to the impact of COVID on the travel industry.</li><li>Current operating deficits result in inability to self-fund all capital projects.</li><li>Large regulatory compliance burden, resulting in higher fixed baseline costs.</li><li>Challenges with recruitment into skilled/specialised roles under current States’ terms and conditions of employment.</li><li>Limited financial autonomy, with approval required from the States for capital projects exceeding £2m and for increases in fees and charges</li></ul></td></tr>
<tr><td colspan="5">Potential Opportunities & Further Considerations:<ul><li>Increasing commercial opportunities.</li><li>Venturing into new income sources through diversification and new revenue generating initiatives.</li><li>Investment in assets provides an opportunity to increase income streams.</li><li>Efficiency review to identify further potential cost efficiencies.</li><li>Further prioritisation of capital requirements to refine the funding gap.  Significant initial funding will be required.</li></ul></td></tr>
<tr><td>Financials – 2024-26:</td><td>Scenario 1 – Baseline</td><td>Scenario 2 – Downside</td><td>Scenario 3 – Upside (Lower)</td><td>Scenario 4 – Upside - Upper</td></tr>
<tr><td>Operating Surplus/Deficit (£)</td><td>(0.1m) - 2.7m</td><td>(1.1m) - (0.7m)</td><td>1m – 3.1m</td><td>2.8m – 3.2m</td></tr>
<tr><td>Funding Gap (£)</td><td>7m – 23m</td><td>13m – 29m</td><td>4m – 20m</td><td>3m – 18m</td></tr>
</table>

| Table 4: Guernsey Water – Recommended Model: Incorporate as a single entity | | | | |
|---|---|---|---|---|
| **Rationale:**<br>• Promotes commercial mindset to drive delivery of strategic ambitions, with least organisational change and associated cost.<br>• Ability to act more dynamically to macro-events. Ability to leverage assets to attract external funding.<br>• Well placed to balance objectives to deliver commercial viability and provide essential services to customers.<br>• Discounted combining with GEL given the change and market uncertainty GEL is facing under the Electricity Strategy. | | | | |
| **Current Key Constraints / Challenges:**<br>• Cesspit emptying service is loss-making and is cross-funded by Wastewater services.<br>• Limited income levers – tariffs are a key lever, but increases must be balanced with customer affordability.<br>• Legislative constraints on ability to differentiate tariffs between different users. Limited growth opportunities.<br>• Increasing cost pressures are eroding operating surpluses. Some recruitment challenges under current States' terms and conditions of employment.<br>• Limited financial autonomy, particularly over shared services and funding sources for its capital programme.<br>• Significant capital requirements, previously funded by the States of Guernsey bond, but which may not be available in future. | | | | |
| **Potential Opportunities & Further Considerations:**<br>• In-sourcing of cesspit emptying service from States Works, resulting in cost savings.<br>• Broadening of tariff rates, including introduction of commercial tariffs (subject to customer affordability considerations)<br>• Recruitment of additional resources required to deliver the capital programme.<br>• Ongoing refinement of capital requirements through bottom-up forecasting work.<br>• Potential access to private debt, albeit limited by the amount Guernsey Water can service.<br>• Could require independent regulation. Potential to merge with Guernsey Electricity in future. | | | | |
| **Financials – 2024-26:** | **Scenario 1 – Baseline** | **Scenario 2 – Downside** | **Scenario 3 – Upside (Lower)** | **Scenario 4 – Upside - Upper** |
| **Operating Surplus/Deficit (£)** | 5.4m – 6.8m | 5m – 5.7m | 5.7m – 9.8m | n/a |
| **Funding Gap (£)** | Zero – 9.3m | Zero – 11.2m | Zero – 3.6m | n/a |

<table>
<tr><th colspan="4">Table 5: States Works – Recommended Model:  Incorporate as a single entity and scale up</th></tr>
<tr><td colspan="4">Rationale:<br>• An opportunity to provide services to the Island in a self-sufficient way by expanding its current managed services model, improving value for customers.<br>• Priority to States of Guernsey’s needs, but leveraging capacity and skillset to provide leading services to other stakeholders.<br>• Allows States Works to be competitive in attracting and retaining talent.<br>• No obvious combination candidate.</td></tr>
<tr><td colspan="4">Current Key Constraints / Challenges:<br>• Recruitment challenges, particularly for skilled and semi-skilled trade roles.<br>• Increased fixed costs from maintaining a minimum service level of resource to deliver emergency support services.<br>• Historical operating surpluses have led to a high cash balance, but the potential loss of income from Guernsey Water’s in-sourcing of cesspit emptying services would reduce operating surpluses.</td></tr>
<tr><td colspan="4">Potential Opportunities & Further Considerations:<br>• Scaling up of services to compensate for potential lost income from cesspit emptying services by competing for alternative private sector contracts.<br>• Consider the perception of a States’ entity competing more within the open market.<br>• Investment of available cash required to unlock cost efficiencies may allow States Works to compete more effectively with the private sector.<br>• Consider future provision of emergency support services, which are currently provided at cost.</td></tr>
<tr><td>Financials – 2024-26:</td><td>Scenario 1 – Baseline</td><td>Scenario 2 – Downside</td><td>Scenario 3 – Upside (Lower) Scenario 4 – Upside - Upper</td></tr>
<tr><td>Operating Surplus/Deficit (£)<br><br>Funding Gap</td><td>2.1m – 2.2m<br><br>Zero</td><td>1.8m – 1.8m<br><br>Zero</td><td>As States Works has made historical surpluses and has positive cash balances, it is able to self-fund its capital programme, subject to one-off costs of cesspit transition to Guernsey Water.</td></tr>
</table>

## 5. Further Considerations and Next Steps

### 5.1 Common Considerations

5.1.1 Appendix IV to this policy letter summarises some of the key issues common to each of the above businesses that would need to be addressed and resolved as part of an incorporation process. That will include ongoing review of their capital requirements and determining future debt/equity arrangements and associated limits.

5.1.2 Within the context of the above, the STSB acknowledges that the work undertaken by Interpath identified a broad range of both profit & loss performance and funding gaps for the businesses, which are summarised in Tables 3 to 5 above. It is stressed that the above data was based on forecasts prepared in mid-2023 for the 2024 Budget, this being the only information available to Interpath at the time. Inevitably, both the data and some of the assumptions that underpin it, are now outdated. Furthermore, they do not reflect the early results of the Business Improvement Programme initiated by the STSB in 2024 and, as such, they should be treated with caution and used for indicative purposes only.

5.1.3 Accordingly, more detailed and additional analysis of the businesses' financial performance is required to support the incorporation process and to narrow down the range of financial projections. That will include:

- Ongoing refinement of profit & loss, cash flow and capital expenditure forecasts to reflect: firstly, refinement of the sensitivity testing that has been applied to the forecasts; and, quantification of the financial benefits of the various opportunities for improvement that Interpath has identified;

- Ongoing refinement of the prioritisation and sequencing of capital expenditure programmes; and,

- Extension of the forecasts for at least five years beyond 2024 to enable a longer-term view of financial requirements to be developed.

This work will result in the recalculation of funding requirements and, importantly, will enable the States to better understand the extent to which the businesses' capital requirements in future can be funded from their own surpluses, through debt finance (either public or private) or with grant funding from the States. These capital expenditure requirements will need to be funded regardless of whether or not the businesses are incorporated. However, the scenario analysis undertaken by Interpath demonstrates that incorporation offers opportunities to fund some of that expenditure through stronger commercial performance. It would also provide the businesses with alternative sources of debt finance that are currently not available to them.

5.1.4. Whilst the STSB has applied a more commercial approach to the unincorporated businesses' operations, it has to do so within a framework of legislation adopted by the States. This can limit the extent to which it is able to drive commerciality or innovation within the businesses. A specific concern relates to legislation that limits the flexibility it has to restructure their fees and charges. For example, the Water Supply Law does not allow Guernsey Water to introduce new categories of charges that would enable it to differentiate between commercial and domestic customers. In the cases of Guernsey Water and Guernsey Ports, many of the fees and charges that can be levied have to be set by Statutory Instrument and that process can be prolonged and uncertain, given the States' ability to annul them. The incorporation process will necessitate a review of such legislation.

5.2 Business Improvement Programme

5.2.1 The trading environment in which the unincorporated businesses operate was negatively impacted by BREXIT, the COVID pandemic and the Ukraine War. In the case of Guernsey Ports, its accumulated cash reserves were exhausted and it became reliant on General Revenue funding support by 2024.

5.2.2 The STSB was acutely aware of the need to address the consequential deterioration in its businesses' financial performance and, as such, it set them the challenge to return to financial sustainability within three years. The budgets for 2024 and 2025 were therefore built with that aim in mind. In this context, the term "sustainable" was defined as being able to generate sufficient surpluses to fund their future capital expenditure programmes, either through the accumulated reserves or through debt finance. This is a precursor to incorporation.

5.2.3 Successful completion of the programme requires a combination of: exploitation of commercial opportunities to generate new income streams; cost control and efficiency initiatives; and, increases in existing fees. For example, Guernsey Ports is targeting recurring efficiency savings of £1.2m per annum by 2026 and has identified potential new income streams of £720,000 per annum. Guernsey Water is targeting efficiency savings of £600,000 per annum by 2026/27.

5.3 Business-Specific Considerations

5.3.1 There are a number of other specific workstreams of relevance to the individual businesses that will have a bearing on any incorporation process and, in particular, the timeframe and sequencing of the process.

5.3.2 In the case of Guernsey Ports and, following their consideration of the 2025 Budget[7], the States have agreed that a study should be undertaken into the provision of a potential subsidy for Guernsey Airport. Given the subscale nature of the Airport and the challenge that this then presents for it in breaking even, such a subsidy would be a means of recognising the broader economic value and contribution it makes to the Island.

5.3.3 A further key consideration for Guernsey Ports will be the extent to which the evolving plans of the Guernsey Development Agency (GDA) will require the transfer of land and property assets from the Harbours to support its delivery of coordinated and comprehensive development along Guernsey's east coast. The Interpath report has identified opportunities for the Harbours to maximise the commercial potential of their real estate. Therefore, it will be necessary to understand how the inclusion or exclusion of such assets from the Harbour's own portfolio in future will impact that potential. Accordingly, the STSB acknowledges the agreement by the States[8] of a Land Transfer Policy that will set out the process for agreeing such transfers between the STSB and the GDA, which will be essential to defining the future scope of the Harbours' real estate and understanding the impact that such transfers might have on potential commercial opportunities at the Harbours and, accordingly, on its financial sustainability.

5.3.4 In the case of States Works, the business could face a material change given the decision by Guernsey Water to consider in-sourcing the cesspit emptying service. Whilst this could be expected to generate material savings for Guernsey Water, there would be a consequential reduction in States Works annual operating surplus. Interpath's recommendation to incorporate States Works was subject to the caveat that the business would have the opportunity to "scale up" its operations in the private sector and find cost efficiencies in order to compensate for that loss.

5.3.5 Therefore, further work is required to quantify the potential opportunities for States Works to expand the scale of its operations and understand the implications of doing so. That process will also require a review of the existing arrangements for the provision by States Works of an emergency support service to assist in the recovery from unplanned incidents or emergency situations.

5.4 STSB Conclusions and Recommendations

5.4.1 The STSB has concluded that it supports in principle the incorporation of Guernsey Water, Guernsey Ports and States Works. However, at this point, it is

[7] Resolution 24 of Article 1 of Billet d'Etat XIX of 2024 - The States of Guernsey Annual Budget for 2025
[8] Resolution 3 of Article 7 of Billet d'Etat XXII of 2024 - Guernsey Development Agency Update

only recommending that the States agrees to proceed with incorporating Guernsey Water for the following reasons:

- Under the Business Improvement Programme initiated by the STSB, there is a clearer pathway under which Guernsey Water will return to profitability and a sustainable financial position by the end of 2026, albeit one that is not without risk. Interpath concluded that, given the financial maturity of the business, it could be an early candidate for incorporation;

- Guernsey Water has developed a range of mature enterprise management IT systems that support its core business processes. These include: Navision, which supports customer and supplier account management, stock management and financial reporting; and, Agility, its computerised asset maintenance system. Its systems mostly operate independently of those of the States, which will make its transition to an incorporated company less complex than will likely be the case for Guernsey Ports and States Works, where a number of systems are more integrated with the States;

- The business-specific issues relating to Guernsey Ports and States Works set out in section 5.3 above need to be addressed before a final decision can be taken on when to proceed with their incorporation; and,

- More work is required to develop the maturity of Guernsey Ports' financial models to better understand its long-term capital funding requirements.

Notwithstanding the above, the STSB anticipates that the work entailed in preparing Guernsey Water for incorporation (see Appendix IV) means that the process is unlikely to be completed until the end of 2027. Inevitably, there will be lessons to be learned from that process. The advantage of taking forwards Guernsey Water for incorporation first means that those lessons can be applied in developing the process for Guernsey Ports and States Works at a later date.

## 6. Incorporation – Future role of STSB

6.1 Incorporation of Guernsey Water and, potentially, Guernsey Ports and States Works, would necessitate changes to the mandate and role of the STSB. Presently, the STSB's mandate includes a requirement for it to ensure the efficient management and operation of those businesses. At the point of incorporation, those responsibilities would transfer to and sit directly with their new individual Boards of Directors and the STSB's future role would be to act as shareholder on behalf of the States for the new companies.

6.2 The STSB already has an established shareholder function for its responsibilities in respect of GEL, GPL, Aurigny Air Services and Jamesco 750. An extension of that function to include Guernsey Water in the first instance would be straightforward.

6.3 In due course and, in the event that they are incorporated, inclusion of Guernsey Ports and States Works within the shareholder function would also be feasible. However, before doing so at that point, the STSB believes there would be merit in evaluating a potential evolution of the model that would involve the establishment of a single holding company. This would own shares in all of the States' incorporated businesses and would be responsible for their oversight. The States would own the shares in the holding company and, as such, would still need to maintain a shareholder function. However, that would be rationalised, given that the States' direct relationship would be with the single holding company, rather than multiple individual ones.

6.4 The STSB believes the advantages of this evolution could include the following:

- The holding company could take a "group wide" view of all capital funding requirements and use the strength of its balance sheet to leverage and access better financing and borrowing terms. It would be responsible for driving economies of scale by making more effective use of shared assets and exercising group purchasing power;

- The rationalisation of the shareholder function might mean it could fit quite manageably within the mandate of an existing Committee of the States. This would, of course, be subject to appropriate arrangements also being made for the future of Guernsey Waste and Guernsey Dairy and for the statutory functions that the STSB currently undertakes as the Waste Disposal Authority.

6.5 The STSB is only identifying this as an option for future consideration in the event that Guernsey Ports and States Works are also incorporated. It will evaluate the option more fully and report back on the matter as part of any such proposals to do so.

## 7. Incorporation and Independent Regulation

7.1 The proposals set out in this policy letter are based on the premise that the States will retain 100% ownership in its newly incorporated trading companies.

7.2 Within the above context, the STSB has considered whether there is a need to establish independent sector-specific economic regulation of those companies once they have been incorporated. Based on its previous experience with Guernsey Electricity and Guernsey Post, the STSB has taken into consideration the following factors:

(i) Given the small scale of the markets within which the businesses operate, there is a material risk that the cost of regulation, which ultimately has to be met by the companies' customers, will be disproportionate and will outweigh the benefits to the community. In the event that there was an appetite to introduce additional regulation, this should first be the subject of a full cost-benefit analysis that addresses not just the regulator's costs and regulatory fees payable, but also the administrative and operational compliance costs of meeting the requirements of the regulator; and

(ii) Whilst the States will be interested in the financial returns its companies can provide, as a public body its sole interest is not in maximising those returns. Through their ownership of the companies, the States can act to protect against profiteering and are also in a unique position to balance financial interests with broader considerations. These include a recognition that the businesses exist as economic enablers for Guernsey and that they have an important role to play in delivering the Island's wider economic, social and environmental objectives. The States is in a position to set shareholder objectives for the companies that can achieve an appropriate balance between these differing interests and, in so doing, negate the need for additional sector-specific independent regulation.

7.3 Provided that the States establishes clear direction for the companies, underpinned by shareholder objectives and measurable performance targets, the STSB has concluded that independent economic regulation is unlikely to be necessary and, indeed, is unsuited to businesses that are effectively operating as social enterprises. The balance between consumer and other interests can be resolved and enshrined by the States through its active shareholder role and the establishment of clearly articulated shareholder objectives. The STSB believes that the purpose of regulation in this environment should be to regulate competition within the wider marketplace under existing legislation, rather than to regulate individual businesses. That can be achieved under the Island's existing competition legislation, which includes the prohibition of practices that are either an abuse of a dominant market position and/or are anti-competitive, including those involving the imposing or fixing of prices.

7.4 The above arrangements could be reinforced by enshrining within each company's Articles of Incorporation a duty on the Directors to balance the protection of customers and the wider community with obligations around financial returns.

7.5 Essentially, this approach would result in implied regulation through political and shareholder oversight of the companies' business plans, which internalises within the business the need for efficiencies and increasing revenues by means beyond just the raising of tariffs.

7.6 As such and, provided that the States retains full control of the companies, it does not believe that there is a requirement to introduce independent economic regulation as part of the proposed incorporation process. Existing regulatory arrangements for quality or safety standards, such as those overseen by the Office of Environmental Health and Pollution Regulation or the Office of the Director of Civil Aviation, would continue unchanged, albeit there is likely to be a requirement to update the relevant legislation to reflect the fact that the regulated entity would in future be an incorporated company rather than a States' department. Any such changes would be identified as part of the project workstreams identified in section 8 below.

## 8. Project Implementation & Scope

8.1 A project to pursue incorporation of Guernsey Water and, potentially, Guernsey Ports and States Works will entail the completion of multiple workstreams. Appendix IV to this policy letter summarises some of the key issues common to each of the above businesses that would need to be addressed and resolved as part of an incorporation process and include: human resources, including TUPE and pension arrangements; financial management, including the businesses' capital structures; the need (or otherwise) for independent regulation of the businesses; legislative amendments and requirements; and, governance and corporate service functions.

8.2 That process will require the submission of further policy letters to the States, in particular where more detailed drafting instructions are required for legislative amendments that may be required. For example, incorporation of Guernsey Water will likely require amendments to the Water Law.

8.3 The STSB is intending to establish a Project Team to undertake this work. Over a two-year period, that team will need to commission technical support and assistance, most likely from outside the States given their resource constraints, in a number of areas, including: commercial, employment and company law; legislative drafting; corporate governance; financial accounting; human resources; and, industrial relations. The STSB's current estimate is that that support is likely to cost no more than £500,000 and will be funded by the businesses.

8.4 It is anticipated that there will be many parallels and synergies between the work that will be required to incorporate Guernsey Water and the work that could be required in future to incorporate Guernsey Ports and States Works. As such, it is not expected that all these costs will be re-incurred should a decision be made to proceed with the latter.

## 9. Compliance with Rule 4

9.1 Rule 4 of the Rules of Procedure of the States of Deliberation and their Committees sets out the information which must be included in, or appended to, motions laid before the States.

9.2 In accordance with Rule 4(1):

(a) The Propositions contribute to the Strategic Portfolios set out in the Government Work Plan 2023-2025 and, specifically, the maintenance of public service resilience, security and governance by ensuring the businesses have the resources needed to work effectively in the future to provide the essential public services and infrastructure for which they are responsible;

(b) The STSB has consulted with the Policy & Resources Committee;

(c) The Propositions have been submitted to His Majesty's Procureur for advice on any legal or constitutional implications;

(d) The financial implications to the States of carrying out the Propositions are set out in Section 8 of this policy letter.

9.3 In accordance with Rule 4(2):

(a) The Propositions relate to the STSB's duties to ensure the efficient management, operation and maintenance of the States unincorporated trading concerns;

(b) It is confirmed that the Propositions accompanying this policy letter are supported unanimously by the STSB.

Yours faithfully

P J Roffey
President

C N K Parkinson
Vice-President

N G Moakes
M Thompson
S J Thornton

**APPENDIX I**

# INTERPATH REPORT – EXECUTIVE SUMMARY

# Executive Summary

# Executive Summary: Project Context

This report is an assessment of 5 of the current unincorporated entities (UE) as to whether incorporating them, either as standalone businesses or under potential new combinations, could deliver better outcomes and value for the public, the States and the businesses, or whether they should remain as UE.

### Current Context of the States' Trading Supervisory Board (STSB) and the Trading Businesses

- A key aim of the STSB is to ensure its trading businesses are well managed, efficient businesses that deliver a social, environmental, economic and financial return to Islanders
- The STSB has sought to create a commercial, customer focussed mindset whilst maintaining the advantages of public ownership and control of critical infrastructure
- Whilst improvements have been made under the STSB's stewardship, current challenges remain with the UE, where commercial potential is not yet maximised
- Common themes of strategic misalignment , governance difficulties, operational frustrations, financial challenges, particularly with regards historical underinvestment in capital, are noted
- Alongside this, business specific challenges exist in each of the five in-scope businesses

**States' Trading Supervisory Board**

- **Shareholder Function (Incorporated Entities)**
  - Guernsey Post
  - Guernsey Electricity
  - JamesCo 750
  - The Aurigny Group
- **Director Function (Unincorporated Entities)**
  - Guernsey Ports
  - Guernsey Dairy
  - States Works
  - Guernsey Waste
  - Guernsey Water
  - Lottery Business Board

*Entities in scope*

### Project Scope

- Supporting Management in their assessment of five of the six unincorporated businesses, excluding the Lottery

The report includes:

- Strategic context and objectives
- Financial performance review
- Funding gap appraisal and options to fill
- Analysis of current operations
- Assessment of future options, including:
  - BAU improvements
  - Potential incorporation
  - Business combinations
- Further work required and next steps

### Project Approach

1. Discovery and collection of data
   - Programme of interviews with key business and STSB stakeholders
   - Assessment of available financial information
2. Review and analysis
   - Historical and budgeted financial performance
   - Current and future capital requirements
   - Cost sensitivities and commercial opportunities
   - Engagement of specialist Debt Advisory team
3. Reporting and stakeholder engagement
   - Engagement throughout with Management teams and the STSB to iterate the report to the final state

### Project Limitations

- There is an assumption that information provided by the STSB is complete and accurate
- The quality of financial information, both with regards to the operating performance budget and capital requirements, varies by entity; the analysis performed is therefore constrained by the information that exists; no auditing or due diligence was performed
- Financial data utilised in the analysis is referenced to the 2024 budget
- The report includes recommendations based on analysis, but do not amount to Management decisions
- Created to support Management's options evaluation

# Executive Summary: Key Challenges

Most of the UEs included in the assessment require significant future capital expenditure, have challenges with recruitment and retention, regulatory burdens and inflationary cost pressures, as well as restricted financial autonomy. Incorporation may improve the ability of the entities to respond to these challenges and alleviate constraints.

| Challenge / Constraint | Description | Impact |
|---|---|---|
| **Capital Requirements** | • Guernsey Water, Ports and Dairy all have forecast capital investment requirements far in excess of operating surpluses in the coming years, both to fund backlog maintenance and any required enhancements to their existing assets. | • The capital requirements for Guernsey Water, Ports and Dairy exceed the potential forecast operating surpluses, meaning there could be a funding gap of £7m to £32m based on the FY24 budget forecast. This could be funded through private debt, however the Dairy may require additional support from States of Guernsey (SoG). |
| **Recruitment and Retention** | • All UEs must conform to public sector pay structures and other T&Cs of employment. This can result in difficulty recruiting and retaining skilled roles (including trade roles, industry-specific roles etc.). | • The challenges to recruit for certain roles has resulted in unusual contracting workarounds, increasing risk (e.g. contracting as a consultant on certain roles in Ports), or inability to retain and recruit. The cost of labour has increased at States Works due to 'market supplement' payments being paid on top of existing pay. |
| **Regulatory Compliance Burden** | • The UEs all have significant regulatory requirements they must comply with. For example, Guernsey Ports must maintain a certain minimum resource for emergency services / regulatory compliance. | • This regulatory burden results in a high level of fixed costs – for instance, Ports must always employ a certain number of emergency personnel and vehicles, regardless of if they are incorporated or not.<br>• It also increases the complexity of the capital plan, as the priority of capital requirements may be altered if new regulations come into force. |
| **Cost Pressures** | • All entities are forecasting increased costs, largely due to inflationary pressures. All entities are expecting to increase tariffs in 2024 to address increasing inflation costs. | • To ensure sustained improvement in financial performance, increased tariffs are required in addition to achieving cost efficiencies. Guernsey Water's assessment of cost efficiencies is the most mature of all the entities. Ports is currently embarking on an efficiency review exercise. |
| **Reduced Autonomy** | • All UEs have limited financial autonomy. For instance, any increase in statutory fees and charges for all entities will need to be set before the SoG, who have the opportunity to annul these increases.<br>• Ports also requires approval from the SoG to spend >£2m. | • The reduced autonomy over increases in statutory fees and charges could result in uncertainty over future income (e.g., currently an issue for the marina).<br>• Moreover, given the size of Ports' forecast capital expenditure, ability to flex capital spend in-year could help to ensure the forecast capital programme is delivered. |

# Executive Summary: Options Assessment

We have considered a long-list of several potential options for each UE, which we have filtered through an options assessment framework and application of critical success factors. Our recommendation is to incorporate Ports, Water and Works, while leaving Dairy and Waste as UEs.

## 1 Potential Options Considered

Three distinct options considered for the future operating state of unincorporated businesses:

- **Retain as an Unincorporated Entity**
- **Incorporate**
- **Business Combination *(assumed an incorporated entity)***

## 2 Options Assessment Framework

A detailed list of options was established for each entity, then filtered down based on strategic, financial and operational selection criteria.

A risk of change adjustment was applied to filter down to 7 remaining options, with Dairy and Waste considered differently due to their unique characteristics.

| Short-Listed Options | |
|---|---|
| Ports | Incorporate (combined Airport and Harbour); consider different BUs within |
| Ports | Split and incorporate separately* |
| Water | Incorporate as a standalone |
| Water | Incorporate (combine with Electricity) |
| Water | Incorporate (combine with Works) |
| Works | Incorporate as standalone and scale up |
| Works | Incorporate (combine with Water) |

## 3 Critical Success Factors

Remaining options for each entity were assessed against 10 Critical Success Factors across strategic, financial and operational lenses to narrow down to 1 single recommendation.

| Strategic | Financial | Operational |
|---|---|---|
| Does the option allow the business to meet all its business objectives? | Does the option result in financial benefits / efficiencies? | Does the option alleviate operational risks / constraints? |
| Does the option align with the business' future ambitions? | Does the option result in significant additional financial cost? | Does the option provide improved value to customers? |
| Does the option enable the business to improve long-term financial performance? | Does the option enable the entity to become financially self-sufficient? | Is the option likely to succeed given entity's ability to respond to changes? |
| | Does the option enable the entity to fund capital requirements? Does it pose a financial risk? | |

## 4 Recommendation

| Recommended Option | |
|---|---|
| Ports | Incorporate (combined Airport and Harbour); consider different BUs within |
| Ports | Split and incorporate separately* |
| Water | Incorporate as a standalone |
| Water | Incorporate (combine with Electricity) |
| Water | Incorporate (combine with Works) |
| Works | Incorporate as standalone and scale up |
| Works | Incorporate (combine with Water) |

Final recommendations involve incorporating Ports, Water and Works, while leaving Dairy and Waste as unincorporated entities.

We set out in later slides the potential further considerations, including funding requirements and governance structures for each entity.

# Executive Summary: Outcome

Incorporation could allow Guernsey Ports and Water to address some of their current challenges and provide a platform to unlock future income or cost efficiency opportunities. However, based on current operating performance and capital requirements, up-front funding is likely required to set these businesses up for success. The drivers to implement changes in the near-term are to address an increasing backlog of capex, mitigate funding challenges and realise benefits of incorporation.

| Entity | Key constraints / challenges currently faced | Potential financials 2024 - 2026 | Recommendation | Potential opportunities / further considerations |
|---|---|---|---|---|
| GuernseyPorts<br>YOUR GATEWAYS TO THE CHANNEL ISLANDS | • **Significant capital requirements**, including backlog maintenance. Upcoming high priority projects include QEII Marina gate replacement which could cost c.£8.6m<br>• **Historical operating deficits** due to the impact of COVID-19 on the travel industry<br>• **Operating deficit** of c.£0.1m forecast in 2024 (driven by a deficit in airports offsetting a surplus in harbour), resulting in an inability of Ports to self-fund capital projects<br>• **Large regulatory compliance burden**, particularly for airports resulting in a higher fixed cost burden<br>• **Challenge with recruitment** into skilled / specialised roles | **Operating surplus / deficit range:**<br>£(2.1)m - £3.2m<br><br>**Funding gap range:**<br>£3m - £29m | **Incorporate as combined entity**<br><br>*Rationale: Unlocking commercial opportunities and enabling scale efficiencies of remaining combined, while minimising disruption of organisational change* | • **Increasing commercial opportunities** and venturing into new **income sources**, such as:<br>– Rent / concessions income – both for airports, and also harbours<br>– Property / rental income – including potential opportunity to maximise the real estate portfolio around the Marina<br>– Channel Islands Control Area (CICA) income<br>– Workboat services<br>• **Efficiencies review** to identify further potential cost efficiencies<br>• Further **prioritisation of capital requirements** to refine the funding gap |
| GuernseyWater | • **Cesspit emptying service is £2.5m loss-making** in 2022 and is cross-funded by wastewater services<br>• **Limited income levers** – tariffs are a key lever, however increases must be balanced by customer affordability constraints<br>• **Increasing cost pressures causing erosion of operating surplus**, particularly costs of SLAs with States Works, electricity costs, shared services costs etc.<br>• **Significant capital requirements**, previously funded via the SoG bond which is unlikely to be available for further borrowing | **Operating surplus / deficit range:**<br>£5.0m - £9.8m<br><br>**Funding gap range:**<br>£0m - £11.2m | **Incorporate as separate entity**<br><br>*Rationale: Promotes commercial mindset to drive delivery of Water's strategic ambitions, with the least organisational change and associated cost* | • **In-sourcing of cesspit emptying service** from States Works, resulting in cost savings of c.£0.8m<br>• Potential **broadening of tariff rates**, including commercial tariffs (though limited by customer affordability)<br>• Recruitment of **additional resource** required to deliver the **capital programme**<br>• Further **refinement of capital requirements** through bottom-up forecasting work (already commenced)<br>• Potential **access to private debt funding**, albeit limited by the amount Guernsey Water can service |

# Executive Summary: Outcome Summary

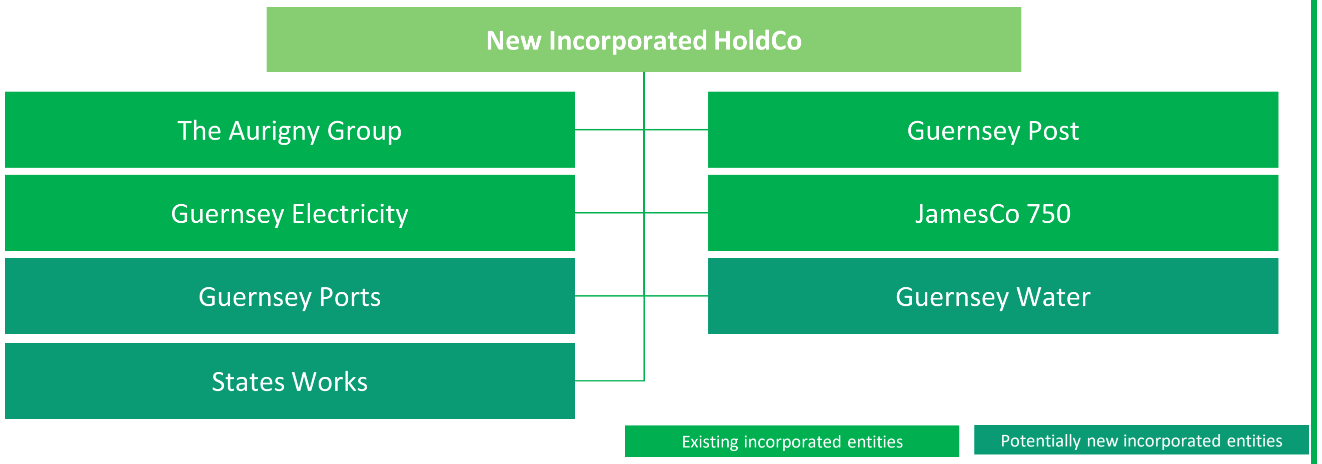
Incorporation is recommended for States Works as it aligns with States Works' current service delivery model. Further consideration is required to determine the future governance of all incorporated entities, both new and existing. A potential structure is to establish an incorporated central body, or 'HoldCo', to oversee all incorporated entities.

| Entity | Key constraints / challenges currently faced | Potential financials 2024 - 2026 | Recommendation | Potential opportunities / further considerations |
|---|---|---|---|---|
| States Works | • **Challenge with recruitment**, particularly for skilled and semi-skilled trade roles<br>• Potential challenge to **retain garage staff** recruited from previous competitor Rabeys<br>• **Increased fixed costs** from maintaining a minimum level of resource to deliver emergency services<br>• Although historical operating surpluses have led to a high cash balance**, potential loss of income** from in-sourcing cesspit emptying service to Water, reducing States Works' operating surplus by £0.3m | **Operating surplus / deficit range:**<br>£1.8m - £2.2m<br><br>**Funding gap range:**<br>None | **Incorporate as a separate entity**<br><br>*Rationale: Extension of current managed services model, allows States Works to scale up services and continue to be financially self-sufficient, improving value for customers* | • **Scaling up of services** to compensate for lost income from cesspit emptying services by competing for alternative contracts from the private sector<br>• **Investment of available cash to unlock cost efficiencies** – for instance impending works in Burnt Lane to increase cost efficiencies – which may allow States Works to be more competitive in the private sector<br>• **Provision of emergency services** would need to be considered further as these are currently provided at cost |

**Future Governance Considerations**

The three entities (Ports, Water and Works), which appear most suitable to incorporation, could be structured as a group, together with the other four existing incorporated entities. A new incorporated 'HoldCo' could be established to oversee these trading entities, acting as one central body for the shareholder (SoG) to engage with.

This structure could enhance ability of trading entities to act commercially and potentially attracting cheaper debt. However, this model could add to labour costs and perpetuate the perception that some entities are "subsidising" others. Further work is needed to assess the viability and attractiveness of this operating model compared to other options.



# Executive Summary: Outcome

Due to the inherent constraints of the Dairy and Waste businesses, we recommend these remain unincorporated. Further potential considerations include the redeployment of these entities to other government departments, and investment in a new Dairy facility.

| Entity | Key constraints / challenges currently faced | Potential financials | Recommendation | Potential opportunities / further considerations |
|---|---|---|---|---|
| GUERNSEY DAIRY | • **The primary function is to support the local farming industry,** not just to produce Dairy products<br>• **Sub-scale nature of the Dairy** which reduces the level of scale efficiencies to be unlocked, in contrast to other comparators<br>• **High purchase price and gate price of milk**, which can be amended only if strict conditions are met, to ensure financial viability and sustainability of farms, and does not lend itself to being a commercial entity<br>• Operating at near breakeven historically, **and forecast deficit of £0.2m in 2024**, with limited cash to fund capital investments<br>• **Ageing Dairy facility**, with operational challenges and limited opportunity for cost efficiencies, without significant investment | **Operating surplus / deficit range:**<br>£0.2m - £1.8m<br><br>**Funding gap range:**<br>£14.2m - £35.2m<br>*(2021 prices)* | **Retain as an unincorporated entity**<br><br>*Rationale: Viability to operate as a standalone commercial entity is low due to constraints faced by the Dairy* | • **Investment in a new facility** – consider funding through external debt or sale and leaseback of the Dairy building, (neither will be sufficient to cover the full requirement based on information provided) – may help to unlock operational and cost efficiencies<br>• **Subsidies –** Adopting subsidies for farmers, similar to the UK, could enable the Dairy to lower purchase prices while maintaining farmers' sustainability<br>• **Greater flexibility on the pricing of by-products**, with more regular price changes to take advantage of market movements<br>• **Industry specific advice** from an experienced professional to gain valuable insight on further commercial opportunities to exploit |
| Guernsey Waste | • **Strategic imperative** of reducing waste will likely **impede ability to be financially self-sustainable**<br>• **Forecast operating deficit of £0.5m in 2024, with limited levers to improve income.** Increasing tariffs cannot compensate for falling waste volumes in the long-term<br>• **Regulation and requirements to provide a minimum level of service** increase Waste's fixed cost base | **Operating surplus / deficit range:**<br>(£0.5)m<br><br>**Funding gap range:**<br>£0.5m* | **Retain as an unincorporated entity**<br><br>*Rationale: Not envisioned to be a commercial entity, as plays role of commissioning group* | • Transfer to another government department may allow for **greater linkage between policy and delivery**<br>• **Governance arrangements** between Waste Disposal Authority (WDA) and Guernsey Waste would require further consideration |

* Low maturity of capital programme means funding gap could be 2-3x higher than stated

# Executive Summary: Finance Options

While the borrowing capacity of each entity in the private debt market is high due to the credit worthiness of the States of Guernsey, borrowing should be limited to a level that can be serviced and repaid based on the operating performance of the entity. The Dairy is likely to require funding from the SoG for a new facility, regardless of the funding option pursued.

| | Holdco Level Borrowing | Entity Level Borrowing | Specific Considerations - Dairy |
|---|---|---|---|
| **Key Considerations** | ✓ Increased efficiency by keeping 'in-house' for both cost and time, scale of financing likely to be more attractive to potential lenders<br>✓ Improved credit profile due to portfolio effect<br>x Increased public scrutiny over the use of funds in a challenging macroeconomic environment | ✓ Steps towards driving financing independence<br>x Higher cost of financing when compared with direct borrowing from the SoG Government<br>x Multiple guarantees likely required from SoG<br>x More restrictive | Options include:<br>a. Access to external debt market for **loan of £35m** to fund entire requirement<br>b. Gift a private investor the land; private investor would build the facility and lease the building to Dairy. **£14.2m funding required** for equipment from other sources |
| **Range of Debt Capacity*** | See Holdco table below | See Entity table below | a. Using indicative potential interest rate of 5.5% (if backed by SoG), **£6.4m - £14.5m** cashflow required for servicing, depending on amortisation profile<br>b. Assuming 25 year lease, annual lease payment of **£3.2m to £3.5m** |
| **Example** | With £7.5m annual free cash flow (FCF), a Holdco may potentially be able to service £47.5m over 20 years, increasing to £127m in a scenario where £20m FCF existed. This may be insufficient for some of the largest one-off capital projects. | | |
| **Specific Factors for Further Consideration** | • An intermediate Holding Company would potentially increase the appetite of prospective lenders<br>• Portfolio effect benefits when lenders perform their credit assessment; synergies from combining working capital cycles<br>• The figures quoted above may be in addition to existing borrowing at incorporated entities, provided that the Cash Flow Available for Debt Service is viewed <u>after</u> the servicing costs of existing debt<br>• There would be a single set of financing documents, a single set of legal fees etc. | • Water business generates stable, predictable cash flows and has a strong asset base of long dated assets<br>• Water may be able to support borrowing with a lower headroom to the debt service cover ratio (up to 1.2-1.3x without a material impact on pricing), but we have modelled 1.5x above<br>• The Ports provide an integral service to Guernsey in the business and tourism industry, which has potential to increase revenue generation by leveraging assets<br>• The Harbour real estate portfolio could present further opportunity (not factored into the above) | • Regardless of option chosen, the Dairy's potential operating surplus of c.£1.8m per annum would be insufficient to access and service the loans required<br>• Some SoG support would likely be required for Dairy to remain operational under either option outlined above<br>• If option a was chosen, the Dairy is likely to achieve a lower cost of financing and potentially more flexible terms<br>• If option b was chosen, the Dairy will likely incur a higher cost of financing, however this option will require less up-front funding |

**Range of Debt Capacity – Holdco Level Borrowing**

| Cash Flow Available for Debt Service (£000s) | Amortisation profile (years) 5 | 10 | 15 | 20 |
|---|---|---|---|---|
| 7,500 | 19,500 | 32,250 | 41,000 | 47,500 |
| 10,000 | 26,000 | 43,000 | 54,750 | 63,250 |
| 12,500 | 32,500 | 53,750 | 68,250 | 79,250 |
| 15,000 | 39,000 | 64,500 | 82,000 | 95,000 |
| 17,500 | 45,750 | 75,250 | 95,750 | 111,000 |
| 20,000 | 52,250 | 86,000 | 109,500 | 126,750 |

**Range of Debt Capacity – Entity Level Borrowing**

| Cash Flow Available (£000s) | Amortisation profile (years) 5 | 10 | 15 | 20 |
|---|---|---|---|---|
| 7,500 | 2,500 | 4,000 | 5,000 | 5,750 |
| 10,000 | 5,000 | 8,000 | 10,100 | 11,500 |
| 12,500 | 12,500 | 20,000 | 25,250 | 28,750 |
| 15,000 | 18,750 | 30,250 | 37,750 | 43,250 |

*Based on indicative potential interest rate of 5.5% (if centralised borrowing / Holdco level) or 6.5% (entity level), debt service coverage ratio of 1.5x and interest cover ratio of 3.0x

# Executive Summary: Next Steps

The transition to incorporation presents a range of risks to address. Immediate considerations include refining the accuracy of financial forecasts and scenarios (including significant capital expenditure requirements), refining the scope and perimeters of operating models to transition / remain, putting in place transitional arrangements for shared functions and planning and sequencing transition to incorporation.

| Topic | Key risks | Immediate next steps | Post-transition next steps |
|---|---|---|---|
| **Governance and Structure** | • Lack of clarity on strategy / objectives<br>• Slow adoption of 'commercial mindset'<br>• Significant delays to realising incorporated benefits | • Consider future redeployment of remaining unincorporated entities (Dairy, Waste, Lottery)<br>• Appoint key leadership positions for entities to be incorporated<br>• Consider future role of STSB<br>• Set up project governance to oversee the transition | • Finalise business strategy, goals and objectives for each newly incorporated entity<br>• Set up new reporting lines |
| **Financial** | • Significant range in capital expenditure and therefore funding requirements – need to narrow down to enhance value for money<br>• No tracking of benefits / growth opportunities | • Extend forecasting period and refine forecasts based on sensitivities proposed<br>• Further validate sensitivities to include unquantified costs / growth opportunities highlighted<br>• Identify and value assets to be included in new entities and agree what is to be transferred with the new entities<br>• Identify costs and benefits of transition to enable tracking<br>• Register for tax, set up business bank accounts etc. | • Hire new finance team (if moving away from shared services)<br>• Set up financial processes and controls<br>• Agree reporting process into 'HoldCo' if relevant<br>• Agree how Management information on progress of incorporation is tracked<br>• Launch funding round process, if decided upon |
| **One-off Funding Requirements** | • Potential underestimation of funding requirements | • Refine prioritisation and sequencing of capital forecasts<br>• Re-assess funding gap based on updated financials<br>• Consider optimal funding strategy (public vs. private)<br>• Develop financial / cash flow model | |
| **Legal / Regulatory** | • Inability to operate due to non-compliance with legal / regulatory requirements<br>• Lack of alignment with trade unions | • Check compliance with regulatory requirements during transition<br>• Check staff transfer requirements from public to private sector and open dialogue with trade unions in advance were possible | • Set up new legal team (if moving away from shared services)<br>• Ensure familiarity with any regulations / requirements |
| **Operational (including HR, IT)** | • No replacement for shared functions (HR, IT, Finance, Legal) resulting in slowdown / inability to operate<br>• Too much business change at one time | • Define 'terms of separation', including how any shared services will be provided during and after transition<br>• Consider staggering incorporation (e.g., one entity at one time) to de-risk level of business change | • Set up new HR / IT functions as required<br>• Decide new pay structures, T&Cs of employment etc.<br>• Manage any redundancies, as required |
| **Communication & Change Management** | • Inertia / inability to move away from 'public service culture'<br>• Staff or public dissatisfaction over lack of communication | • Manage drafting of Policy Letter<br>• Set out clear communications plans for all stakeholders (including staff, public etc.)<br>• Build in time to embed new processes and cultural change | • Communicate new business strategy, goals and objectives to both staff and the public<br>• Open channels of feedback  to ensure staff 'buy in' |

**APPENDIX II**

## OPTIONS ASSESSMENT – KEY PRINCIPLES

Interpath adopted an objective scoring framework to enable it to systematically evaluate the potential options that it identified for the five unincorporated businesses. The design of that framework was underpinned by a range of core, commercial and public sector principles. These are set out in the table below.

| Core Principles |
|---|
| • Options considered must ensure long-term value for Islanders;<br>• Value is not just measured in financial terms, but through service standards and customer experience, as well as wider economic and social impact on the Island and its residents. |
| **Commercial Principles** |
| • Enable the pursuit of operational and financial synergies to drive innovation;<br>• While financial performance is not the sole gauge of success, entities should pursue efficiency and strive to attain sustainable self-sufficiency, including unlocking commercial opportunities to support the long-term viability of the business;<br>• Ideally, entities will have clear and strong balance sheets to access better funding and borrowing terms;<br>• Establish clear accounting for cross business activity, as well as treatment of business assets;<br>• Clear performance accountability. |
| **Public Sector Principles** |
| • Service standards and customer experience are central to delivery;<br>• Recognition of the crucial role services play in Islanders' lives;<br>• Establish an agreed route to deliver Public Service Obligations (PSOs);<br>• Organisational simplicity and absolute States' ownership. |

**APPENDIX III**

**OPTIONS ASSESSMENT – LONGLIST**

| **Guernsey Ports** | |
|---|---|
| 1. | Remain unincorporated and together and improve operational effectiveness. |
| 2. | Remain unincorporated (split Airport and Harbour). |
| 3. | Incorporate (combined Airport and Harbour). Consider different BUs within. |
| 4. | Split and incorporate separately (this may include incorporation of both Harbour and Airport or just Harbour. |
| 5. | Split, combine Airport and Aurigny, and incorporate Harbour separately. |

| **Guernsey Water** | |
|---|---|
| 1. | Remain unincorporated and improve operational effectiveness. |
| 2. | Incorporate as a standalone. |
| 3. | Incorporate (combined with Guernsey Electricity). |
| 4. | Incorporate (combined with States Works). |
| 5. | Incorporate (combined with Guernsey Electricity and States Works). |
| 6. | Incorporate (combined with Guernsey Dairy, Guernsey Electricity and States Works). |

| **Guernsey Dairy** | |
|---|---|
| 1. | Remain unincorporated, establish financial improvements and develop a credible capital programme, including funding a new Dairy facility. |
| 2. | Leave unincorporated, but seek a private investor to build a new facility to lease and the Dairy to operate. |
| 3. | Incorporate as a standalone. |
| 4. | Incorporate (combined with Guernsey Water, Guernsey Waste and States Works. |

| **States Works** | |
|---|---|
| 1. | Remain unincorporated and improve operational effectiveness. |
| 2. | Incorporate as a standalone and scale up. |
| 3. | Incorporate as a standalone and scale down. |
| 4. | Incorporate (combined with Guernsey Water). |
| 5. | Incorporate (combined with Guernsey Water, Guernsey Waste and Guernsey Dairy). |

| **Guernsey Waste** | |
|---|---|
| 1. | Remain unincorporated and improve operational effectiveness. |
| 2. | Incorporate as a standalone. |
| 3. | Incorporate (combined with States Works). |
| 4. | Handover to the Committee *for the* Environment & Infrastructure. |
| 5. | Incorporate (combined with Guernsey Water, Guernsey Dairy and States Works). |

**APPENDIX IV**

**INCORPORATION PROJECT – KEY WORKSTREAMS**

| INCORPORATION MODEL – GOVERNANCE AND LEGISLATION |
|---|
| Under the States Trading Companies (Bailiwick of Guernsey) Law, 2001, the States can by Ordinance: designate a company as a States' trading company (STC); determine the corporate governance arrangements for a STC; and, transfer parts its existing undertakings into an STC. The States Trading Companies (Bailiwick of Guernsey) Ordinance, 2001, sets out these provisions in respect of Guernsey Electricity and Guernsey Post and includes the following arrangements (not exhaustive):<br><br>• The holding of the shares by the STSB on behalf of the States;<br>• The appointment and remuneration of Non-Executive Directors of STCs;<br>• The submission of the STCs' strategic plans and publication of annual reports and accounts;<br>• The guidance that the States may give to the STSB in exercising its role as shareholder;<br>• Details of the businesses (including assets and liabilities) transferred from the States to Guernsey Electricity and Guernsey Post at the point of incorporation.<br><br>At the time of Guernsey Electricity's and Guernsey Post's incorporation, the electricity and postal sector legislation was reviewed and updated to reflect the new operational and organisational models, including: provision for regulation and licensing of services; rights to recover expenditure, fees and charges; technical, safety and environmental matters; and, maintenance of universal service obligations by each company.<br><br>Key tasks:<br><br>• Preparation of legislation to designate and establish businesses as STCs and identify/transfer the relevant undertakings and assets from the States. Review and update the States Trading Companies Law as necessary;<br>• Prepare Memorandum and Articles of Association for each new STC, including a mechanism that places duties on the Board to |

both follow the strategic direction of the States and to balance the protection of customers and the wider community with obligations around financial returns;

- Establish Memoranda of Understanding between the shareholder and each company setting out: shareholder objectives; key performance indicators; dividend policies; reporting arrangements; a scheme of delegated authorities (to include pricing and tariff decisions and authorities) and other related governance;
- Refine strategic/business plans, including identification of any Universal Service Standards/Obligations to be maintained by the businesses post-incorporation;
- Review and, if necessary, update sector specific legislation, including the need (or otherwise) for new regulatory arrangements systems and arrangements for introduction of changes to fees and charges;
- Establish shadow Boards of Directors (as an evolution of current company boards).

**Stakeholders:** STSB, Policy & Resources Committee; Committee *for* Economic Development; Law Officers; GCRA; Office for Environmental Health & Pollution Regulation; Director of Civil Aviation.

**HUMAN RESOURCES**

Incorporation of the businesses as States Trading Companies (STCs) will require the transfer of their employees to the new entities. Effective transfer arrangements will be critical to protect employee rights, retain key employees and preserve continuity during the process. Early and extensive consultation will be required with affected employees and their representatives/unions.

The STSB believes an Ordinance made under the Transfer of States Undertakings (Protection of Employment)(Guernsey) Law, 2001 (TUPE), will provide the best mechanism to enable a transfer. Such an Ordinance was used for the transfer of employees of the States to Guernsey Electricity and Guernsey Post in 2001. This would enable the transfer of employment contracts to the new STC in a way that preserves employees' terms and conditions of employment. TUPE only applies at the point where the employee moves across to a new employer and does not give any more protection to an employee than they would enjoy if they had continued to be an employee of the States. However, after the change in employer, it would be the STC that was responsible for fulfilling and negotiating any changes to terms and conditions.

A decision will therefore need to be taken on whether existing employees would remain in the Public Servant Pensions Scheme (PSPS) and, if so, an enabling amendment would need to be agreed by the States. At the time of their incorporation, employees of both Guernsey Post and Guernsey Electricity remained within the PSPS. Subsequently, Guernsey Post negotiated with all its staff for them to exit the PSPS and Guernsey Electricity has closed membership of the PSPS to new employees, offering them an alternative scheme.

Key tasks:

- Consultation with employer, employees and employee representatives/unions;
- Preparation of Ordinance under TUPE legislation for transfer of existing employees to the STCs;
- Confirmation of future pension arrangements.

**Stakeholders:** Employees; Employee Representatives/Unions; Policy & Resources Committee; STSB; Law Officers.

**FINANCIAL MANAGEMENT AND ADMINISTRATION**

Incorporation must result in improved financial transparency in the operation of the business, in part arising from the need to identify and account for any corporate (or other) services that may continue to be provided to the businesses, combined with full disclosure of and accounting for PSO activities undertaken by the businesses on behalf of the States.

Key Tasks:

- Identify, document and agree assets and liabilities to be transferred from the States to the incorporated businesses;
- Identify all PSO activities undertaken by the businesses on behalf of the States and agree basis on which any such activities are to be undertaken in future;
- Undertake review of the businesses' capital requirements and determine future debt/equity arrangements and limits;
- Identify options/solutions for capital funding of future strategic investments required to support the Bailiwick's long-term needs;
- Agree income tax arrangements for newly incorporated businesses;

- Review of future arrangements for the Ports Holding Account;
- Identify implications for preparation of audited financial accounts in accordance with Financial Reporting Standards (IPSAS);

**Stakeholders:** STSB; Policy & Resources Committee.

**CORPORATE SERVICE FUNCTIONS**

Identify arrangements for future provision of corporate functions currently provided by the States' shared services, including: financial management, legal, IT and human resource functions.

Key Tasks:

- Identify all "internal" services provided to the businesses by the States' corporate functions. Prepare service level agreements (including charges) for future provision of services to be retained by the incorporated businesses;
- Define "terms of separation" and agree how any shared services will be provided both during and after the transition;
- Subject to the above, establish new corporate service functions within the businesses to ensure compliance with legal, accounting and regulatory requirements (and recruit accordingly).

**Stakeholders:** STSB; Policy & Resources Committee; Law Officers.