



OFFICIAL REPORT
AITHISG OIFIGEIL

Public Audit Committee

Thursday 29 June 2023

Session 6



The Scottish Parliament
Pàrlamaid na h-Alba

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PUBLIC AUDIT COMMITTEE

20th Meeting 2023, Session 6

CONVENER

*Richard Leonard (Central Scotland) (Lab)

DEPUTY CONVENER

*Sharon Dowey (South Scotland) (Con)

COMMITTEE MEMBERS

Colin Beattie (Midlothian North and Musselburgh) (SNP)

*Willie Coffey (Kilmarnock and Irvine Valley) (SNP)

*Craig Hoy (South Scotland) (Con)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Kersti Berge (Scottish Government)

Stephen Boyle (Auditor General for Scotland)

Joanne Brown (Grant Thornton UK LLP)

Alison Cumming (Scottish Government)

Alison Irvine (Transport Scotland)

Bill Kidd (Glasgow Anniesland) (SNP) (Committee Substitute)

David Signorini (Scottish Government)

Mark Taylor (Audit Scotland)

CLERK TO THE COMMITTEE

Lynn Russell

LOCATION

The James Clerk Maxwell Room (CR4)

Scottish Parliament Public Audit Committee

Thursday 29 June 2023

[The Convener opened the meeting at 09:00]

Decision on Taking Business in Private

The Convener (Richard Leonard): Good morning. I welcome everyone to the 20th meeting in 2023 of the Public Audit Committee. We have apologies from Colin Beattie and I am pleased to welcome Bill Kidd in his place. The first item of business is for members to agree on whether to take agenda items 4, 5, 6, 7 and 8 in private. Are we agreed?

Members *indicated agreement.*

Section 22 Report: “The 2021/22 audit of Scottish Canals”

09:00

The Convener: We have two principal items on our agenda. The first is consideration of evidence on “The 2021/22 audit of Scottish Canals”. I welcome our three witnesses: we are joined by Stephen Boyle, the Auditor General for Scotland; Mark Taylor, the audit director at Audit Scotland; and Joanne Brown, who is a partner at Grant Thornton UK LLP.

We want to put quite a number of questions to you but, before we get to those, I ask the Auditor General to make a short opening statement.

Stephen Boyle (Auditor General for Scotland): Many thanks, convener, and good morning, committee. I have prepared this report under section 22 of the Public Finance and Accountability (Scotland) Act 2000 on the 2021-22 audit of Scottish Canals. My report brings to your attention on-going issues with Scottish Canals’ valuation of its assets and the completeness and accuracy of its records. Those issues are so significant that they have resulted in the auditors issuing a disclaimer on Scottish Canals’ financial statements for the second year in a row.

The committee might recall that, in February of last year, I reported on similar issues that were raised through the previous year’s audit of Scottish Canals. The issuing of a disclaimer of an audit opinion is a serious matter, which indicates that the auditors have been unable to provide an opinion on the financial statements due to insufficient appropriate audit evidence. In this case, there is a lack of public assurance over Scottish Canals’ financial position and performance, and the regularity of its transactions.

The basis for the disclaimer is Scottish Canals’ valuation of its property, plant and equipment assets. Scottish Canals has faced significant challenges adapting to the financial reporting and accounting framework that is required of it as a non-departmental public body—specifically, to the way it now has to value those assets. It has taken steps to address the auditors’ concerns but progress has been limited by the quality of its underlying documentation and data.

Scottish Canals now needs to develop an effective plan to ensure that it can meet its financial accounting responsibilities as a matter of urgency. Scottish Canals needs to work together with Transport Scotland, in its role as Scottish Government sponsor division, to ensure that the implications of the accounting rules that Scottish Canals must work to are fully understood and reflected in its planned response. They should work together to ensure, too, that Scottish Canals has the capacity and expertise to deliver the

improvements that are now needed. Those issues will be a central focus for the incoming external auditors during the 2022-23 annual audit. I will continue to monitor Scottish Canals' progress and report further as necessary.

As you have noted, convener, I am joined by Mark Taylor, who has led on the preparation of the section 22 report, and by Joanne Brown, from Grant Thornton, who is the appointed external auditor for 2021-22. We look to answer your questions.

The Convener: Thank you very much for setting the scene with that opening statement, which had a great deal of similarity with the evidence that we took around this time last year.

We will go straight to questions. I invite deputy convener Sharon Dowey to begin.

Sharon Dowey (South Scotland) (Con): This is the second year in a row that the auditor has issued a disclaimer on the audit opinion. Is it correct to state that, in 2020-21, the auditor's concerns arose from assets that had not been valued and that this year's concerns are related to a lack of audit evidence to support the valuations that have since taken place?

Stephen Boyle: Yes, that is largely the case. I will pass over to Joanne Brown, who can set out for the committee the judgments that she arrived at in issuing a disclaimer of opinion, but first I will quickly give some additional context.

Last year's section 22 report highlighted issues around the availability of evidence. Scottish Canals, in its evidence to the committee, set out its intention to undertake a full valuation exercise. As we note in our report, that is evidence of some progress. However, Scottish Canals has not yet been able to provide robust evidence to support the valuation numbers and disclosures that were set out in its accounts, in order to satisfy the external auditors that those were complete and accurate to allow them to issue an audit opinion.

Joanne can set out her judgments for the committee.

Joanne Brown (Grant Thornton UK LLP): There was a series of issues in 2021 that led to the disclaimer, but the principal issue concerned the accounting records that supported the valuation in 2021. That included evidence of the existence of assets, the record keeping within the fixed-asset register and a number of other issues around accounting for property, plant and equipment.

The exercise in 2021-22 was very complex. Scottish Canals had a project plan and sought to get a valuation. In doing the valuation in 2021-22, it also made a decision that it would value the canal itself as an asset; that was not something

that it had done in the 2021 accounts and it included a number of complex judgments and estimates. While we agreed, and could see, that the valuation model in 2021-22 was reasonable, Scottish Canals still lacked underlying data and evidence around some of the significant material judgments and estimates in the accounts. We saw some similar themes in 2021 around evidence of the existence and ownership of assets, record keeping, and the data that supported the cost information that Scottish Canals proposed to feed into the valuation model. It is very complicated and Scottish Canals did a lot of work but, unfortunately, the underlying records do not support some of the material numbers in the financial statements, which led to the disclaimer of opinion.

Sharon Dowey: Would you say that Scottish Canals is in a worse position this year than it was last year?

Stephen Boyle: Joanne Brown will have a view on that, having been the auditor for a number of years.

As we looked to set out in the report, there are signs of progress. Scottish Canals sought to undertake a complex programme of valuations. What it has not yet done is address all the clear evidence that is required, not just to satisfy the auditors; the accountable officer and the board, given their responsibilities, will also want to be satisfied on those same points.

As the section 22 report sets out at paragraph 15, a number of steps are still required in order to meet the requirements of an external auditor in order that they can issue a clear opinion on the annual report and accounts. There is some progress that we would want to recognise, but there is quite a bit of a way to go.

The other rationale that we arrive at in the report is that Scottish Canals, together with its sponsor division, needs to have a clear plan as to how it will arrive at a valuation methodology that can allow it, and its auditors, to see the evidence that is necessary to satisfy accounting requirements.

Sharon Dowey: How unusual is it for a public body to have a disclaimer on the audit opinion that is issued in respect of its annual accounts for two consecutive years?

Stephen Boyle: It is very, very unusual. I do not think that there are other examples that we can think of in which an auditor has issued a disclaimer of opinion. I will ask Joanne Brown to set out her experience.

The committee may also be interested to know that when auditors issue opinions, they have a range of options. The most common opinion that you will see is an unmodified—what is known as a

clean—audit opinion, which says that the auditors are satisfied that it presents a true and fair view: there are no material misstatements and no concerns about the regularity of expenditure. There are then gradations from that, of which the disclaimer of opinion is the most serious. Joanne Brown will have an additional perspective on that, as a practising external auditor.

Joanne Brown: From our perspective, as the Auditor General outlined, a disclaimer of opinion is highly unusual. A disclaimer of opinion arose because we were unable to get assurances that the financial statements did not materially misstate the valuation of Scottish Canals. The balance sheet shows £407 million of assets. As an auditor, we work to a materiality level. We have set that level, from assets, at £4 million and, based on our audit work and testing, we were unable to conclude the nature of the errors. We identify and believe that there are errors in the accounts, but we have not been able to quantify those errors and that is why we have the disclaimer of opinion.

When organisations have a disclaimer of opinion, it is quite difficult for them to get a clean opinion the following year. We discussed that with Scottish Canals in relation to its project plan and the amount of work that it was undertaking. It is not impossible, but for Scottish Canals to have moved away from a disclaimer we would have had to reaudit the 2020-21 numbers, which included the prior year misstatements. We opted not to do that reaudit, given the number of errors that we were accounting in the 2021-22 audit, because we were not confident that those prior year restatements were going to be materially correct.

We undertake our audit work as we would if we were to give a clean opinion. We considered whether Scottish Canals would be able to take the number of actions that we outlined for it to take and on what timeline, and whether it would be sensible for us, as auditors, to wait until those actions had been taken before going back to conclude our audit of 2021-22. However, our auditor judgment was that the time that that would take would be too long for us to hold the 2021-22 audit open and that is why we then issued the disclaimer of opinion.

Sharon Dowey: The report explains that

“The issuing of a disclaimer on the audit opinion, means that the auditors cannot provide assurance on the use of public money by Scottish Canals during 2021/22.”

As a disclaimer was also issued for the 2020-21 accounts, what are the wider implications of not having assurance on Scottish Canals’ use of public money over the past two years?

Stephen Boyle: The first point that I will emphasise is that it is a very serious matter. Public bodies that receive funding from the Scottish

budget are required to lay their accounts in the Parliament. As Auditor General, I have the option to consider whether to accompany the laying of an annual report and accounts with a section 22 report. As the committee is aware, I do that on a number of sets of accounts over the course of the year, to highlight matters emerging from the annual audit.

For those other sets of accounts, the assumption is almost always that they are accompanied by an unmodified opinion. However, because of the circumstances, we are highlighting in today’s report that there is not the assurance that the Parliament would typically receive on the contents of the annual report and accounts, because there is a disclaimer of opinion. The implications and the seriousness were very much part of our thinking in bringing that to the Parliament’s attention. It is not as if there is a qualified opinion, which is one of the interim steps that an auditor can take. A qualification is usually on a specific aspect of an annual report but, because a disclaimer extends much wider than that, it says that the committee and, therefore, the Parliament, does not have assurance in totality over that annual report and set of accounts.

Sharon Dowey: In your view, has Scottish Canals already failed to meet its public accountability responsibilities to comply with the financial reporting manual requirements in the 2020-21 and 2021-22 reporting years? Is the same conclusion of failure likely to be reported for the current financial year?

Stephen Boyle: I will take those points in reverse order. As Joanne Brown said a moment or two ago, it will be difficult to resolve all the issues in a short time. However, I do not want to pre-empt that entirely. It is important that the incoming auditors, together with the Scottish Canals leadership team and the sponsor body, have a clear understanding of their intentions to move forward and address some of the issues that are highlighted in today’s report. It is clear, however, that it will be challenging. These are complex issues and it will take careful consideration from Scottish Canals and Transport Scotland to come up with a clear plan to have the assets valued and reported in a way that will satisfy audit responsibilities.

09:15

I am paraphrasing slightly, but your other point was about understanding and ownership. The accountable officer of Scottish Canals sets out clearly in the annual report and accounts their responsibilities, one of which is overall compliance with the requirements of the financial reporting manual as it relates to assets and other matters. The committee might wish to explore further with

Scottish Canals its understanding of those requirements.

Sharon Dowey: What are the consequences for Scottish Canals if it continues to fail to meet its public accountability responsibilities?

Stephen Boyle: That is less clear. Ultimately, Scottish Canals is primarily funded by grant in aid from the Scottish Government through the budget setting arrangements. It will be important for the Scottish Parliament, as it considers future budget setting arrangements, to be satisfied that the funds that are allocated to Scottish Canals are being spent properly. Most typically, that assurance comes from regular audit assurance and recognition of accountable officers' responsibilities in the accompanying accounts. When that chain is broken by a disclaimer of audit opinion, it is effectively saying that the auditors cannot give the Parliament the typical assurance that it would expect from the awarding of public funds through the budget act.

The Convener: Paragraph 4 of the report is pretty damning, is it not? It says:

"the auditors were unable to conclude whether:

- the annual report and accounts give a true and fair view
- expenditure & income were regular ...
- the Annual Report & Accounts are free from material misstatement
- adequate accounting records have been kept."

That is a fairly heavy charge sheet, is it not?

Stephen Boyle: It is, convener. We cannot overstate the seriousness of an external auditor disclaiming their opinion and the ramifications of that: not having "a true and fair view" that the regularity of expenditure—the amounts spent by a public body—was consistent with legislation and budget acts. Joanne Brown's annual audit report, which accompanies the section 22 report, sets out many examples of where documentation and data were not available to support the valuation figures that were presented to her by the leadership of Scottish Canals. Joanne might want to give the committee more detail behind that, but paragraph 4 sets out a significant set of circumstances.

Joanne Brown: On that point, as auditors we look to management to provide suitable underlying documentation to support the balances within the financial statements and show that they are fit for audit purpose and that they tie back into the trial balance and the actual accounts. As our external audit report outlines, we encountered a number of difficulties in doing that. In particular, we had challenges in reconciling certain information through the valuation report back into the draft accounts. That did not reconcile in a number of draft account versions that we received. We had

concerns about additions, and whether those were treated in the right financial year. We had concerns about whether there was duplication of additions and about assets under construction and, within that, whether some of those assets that had been capitalised were in fact not assets and should have been put through the revenue account.

There were many examples of what we felt were potential errors in not just the valuation but the accounts as a whole. The reason for our opinion being a disclaimer is that the size of those balances is very large in the accounts of Scottish Canals; the property, plant and equipment balances touch on a number of areas in the accounts, including income and expenditure, the depreciation charge and the revaluation reserve. We felt that those errors were pervasive across the financial statements. The reason for the opinion on the wider annual report and accounts being caveated is that, when you read the annual report and accounts, the front-end narrative includes a number of balances that we are unable to give assurances on in the financial statements.

The Convener: Before I move on to Craig Hoy, I note that when we took evidence last year from Transport Scotland, it described the situation as it was then as "a fairly narrow point" and, again, said:

"it is a narrow point about the evaluation of assets."—
[*Official Report, Public Audit Committee, 24 March 2022; c 14.*]

Is that how you would characterise it?

Stephen Boyle: No, it is not. Stepping back for a second to look at the purpose of Scottish Canals, I would highlight that one of its core responsibilities—its strategic objective—is to maintain the canal network, part of which is about its associated value, the cost of maintenance and the records that go alongside that. So, no, I would not agree that this is a narrow technical point. Grant Thornton has reached the opinion that the valuation of the assets affects so much of the running of the business and the disclosures of its performance over the course of the year, and that that pervasiveness suggests that the matter is central to the activity of Scottish Canals.

Mark Taylor (Audit Scotland): Perhaps I can add a little to what the Auditor General has just said and say something that I think goes to the root of your original question, convener. We have issues with valuation and the result is that there is no assurance across anything in the accounts. That is our fundamental concern in terms of the disclaimer: there is no assurance here for the Parliament or, I have to say, the accountable officer in the Scottish Government, Transport Scotland, the Treasury and, indeed, the whole system when it comes to the confirmation that the

audit process provides to everybody about the robustness of a set of accounts. That is the fundamental concern here.

The Convener: Thank you. That was very clear and we appreciate that. Craig Hoy has some questions.

Craig Hoy (South Scotland) (Con): I do not want to repeat or, perhaps, to labour some of the points that the convener has already made, but I note that paragraph 5 of the report says:

“The auditors reported that they had not received all information and explanations required for their audit in relation to the property, plant and equipment balances. The auditors also raised concerns about the overall quality and timeliness of Scottish Canals accounting records and working papers. This has led to significant delays to the audit process.”

I can second guess what you are going to say, given your responses to Mr Leonard, but is it safe to say that your concerns go far wider than the issues related to the property, plant and equipment balances?

Stephen Boyle: Yes. If the committee finds it helpful, Joanne Brown can set out in a bit more detail the nature of some of the interactions that she and her team had with Scottish Canals, but your question speaks to a couple of other issues that we touch on elsewhere in the report about the capacity that exists in the leadership and finance team of Scottish Canals. There has been significant turnover in the finance team, and there has also been a change of leadership in the organisation, with the recent appointment of a new chief executive.

Those issues are relevant to the circumstances in which we find ourselves today. It has been challenging for Scottish Canals to prepare a complete set of annual report and accounts. Joanne might well refer to this, but in the version that she was originally presented with for audit, a number of significant elements that should have been in a set of annual report and accounts were missing. Some to-ing and fro-ing and a number of iterations then followed.

Before I pass over to Joanne, I also want to highlight not just the quality of the accounts but their timeliness. Public bodies are required to lay their accounts before Parliament by the end of the calendar year, or nine months after the end of the financial year. Those accounts were finally laid just a few weeks ago. Timeliness is relevant to scrutiny, so that Parliament can be satisfied. As a consequence of that, we are many months after the laying date.

As Joanne Brown said, we are now already not in the financial year to be audited but the next one, so there is a risk that we could experience a backlog over a number of years. That is another

reason why there needs to be a clear and comprehensive plan between Scottish Canals and its sponsor division for where it goes next in order to resolve the issues. Joanne can say a bit more.

Joanne Brown: On the financial statement audit work, which commenced in July, given the challenges that Scottish Canals had with valuation, we agreed that we would look at doing our audit work, excluding valuation, earlier in the process, so in July we were working off a trial balance. During the course of our audit, which concluded in May this year, we received seven or eight different trial balances from Scottish Canals. We received the first draft of accounts, which was not a full draft of accounts for audit, in January, and it was missing primary statements and key notes to the accounts.

We highlighted in our external audit report the need for better-quality accounts, better review of the accounts and better working papers that support the balances in the accounts. As the Auditor General said, the Scottish Canals finance team is very small and, during the financial year in question, there was significant turnover in that finance team, which resulted in a loss of corporate knowledge of Scottish Canals and made it difficult for the team to provide suitable explanations and working papers to auditors to support the numbers in the accounts. Individuals who prepared those accounts and worked to prepare the accounts were not there throughout the audit period. The organisation has some challenges around what records are held physically and what records are held electronically.

One of the key challenges, specific to property, plant and equipment, relates to the data and records that were held by the engineers in the project management system and the inability to reconcile them with the fixed-assets register. A lot of work was done and progress was made during 2021-22 to do that reconciliation, but the engineering records and the project records do not support some of the cost information that has been used in the valuation to inform the financial statements. We identified a number of issues that were wider than property, plant and equipment, and we have an action plan for Scottish Canals to take forward. Principally, I want the organisation to improve the quality of the accounts and the working papers that sit underneath them.

Craig Hoy: Regardless of the size of the team, that sounds pretty poor, given that we are talking about the public purse. The report states that auditors did not receive all the information or explanation that was sufficient for the audit in terms of property, plant and equipment balances. Did you get the impression that the staff who were there were fully engaged with the process, and were they open and transparent with you?

Joanne Brown: I would not flag any concerns about openness and transparency. The organisation has a very small team, and one of its particular challenges has been the capacity, skills and experience that are required to do the valuation work. The team highlighted that risk, but the core finance team needed significant time to work with the consultants to produce the valuation and to answer the consultants' questions on underlying data and so on. That directed the team away from the financial statements, but we would still look to it to be able to do that work. Regardless of its being a small team, it should have been able to do a self-review of accounts and it should have had records that produce a good set of accounts with the underlying data. The team should have been able to answer effectively the auditors' questions and to provide the data to support the balances. That was very challenging, over the period.

Craig Hoy: Obviously, accountability is linked to capacity and competence. Do you get the impression that there was some failure of past or present leadership in the organisation?

09:30

Joanne Brown: Personally, I think that Scottish Canals underestimated the challenge of the valuation in terms of the time commitment and the data that it would need to support the valuation work and, within that, the skills that would be needed in, for example, capital accounting. Although the organisation looked to the consultants for the valuation, it underestimated the skills and experience that it would need internally to be able to produce a set of accounts and information that would support the consultants in the valuation exercise.

In 2021-22, Scottish Canals focused on the point that was made in the prior year about valuation, but did not necessarily pay enough attention to the underlying records and the points that were raised in the prior year audit that it did not manage to address, which, in turn, supported another disclaimer this year.

Craig Hoy: You have produced a disclaimer in two years. On the basis of your engagement to date and looking at the present situation, would you say that Scottish Canals now has the bandwidth, capacity and competence to ensure that we will not be doing the same thing again this time next year?

Stephen Boyle: That question is probably for me, Mr Hoy. We cannot yet give you that assurance. As Joanne Brown set out, her audit has just finished; it has been only a few weeks since she disclaimed her opinion. The incoming auditors will have a handover, review her

judgments and take their own view about the adequacy of records.

I repeat my remark that it will be challenging to resolve all the issues that are set out in last year's report and today's in time to satisfy the requirements for a clean audit opinion. However, I stress that I do not want to pre-empt that audit, and that it will be for the independent external auditors to arrive at their views.

The Convener: Bill Kidd has some questions.

Bill Kidd (Glasgow Anniesland) (SNP): Ms Brown has already given us the background on the circumstances of the valuation of assets. During an evidence session with Scottish Canals in May last year, the then chief executive and the director of finance and business confirmed that the organisation aimed to undertake a new valuation process by the end of last year. They described that as being an ambitious target and had concerns that they would be unable to meet the deadline. Did Scottish Canals meet the deadline to undertake a new valuation on the canal infrastructure estate in its entirety during 2022?

Stephen Boyle: Good morning, Mr Kidd. I can start, then Joanne Brown can say a bit more about that.

The answer is twofold. As we say at paragraph 13 of the report, Scottish Canals "progressed work" to complete the valuation, but has not aligned the progress on it with clear underlying records and data to support the valuation that was presented for audit.

The matter is complex. I do not wish to understate that complexity to the committee. We are talking about very old and, in some cases, potentially heritage assets that have not been valued in that way before. Engineering records were used and the judgments of management experts were used alongside them. However, it proved to be difficult for auditors to validate that information. Therefore, we do not have sufficient evidence to support the valuation on the basis on which Scottish Canals made it. There were other factors, too, which Joanne Brown can set out for the committee.

Joanne Brown: Scottish Canals developed a project plan that sought to help it to address the disclaimer and to undertake the valuation for 2021-22. The board approved that project plan. There were some slippages, but in that time period, following the prior year disclaimer, the organisation undertook an exercise to procure consultancy support and worked with the consultants from June to November 2022.

By November 2022, the valuers that Scottish Canals appointed had given additional insight into the valuation and a valuation report, which was

then the subject of an audit and to Scottish Canals reflecting that in the unaudited accounts. In that period, Scottish Canals worked hard to componentise the assets. Part of the exercise was to understand what assets Scottish Canals holds—on what basis, the type of asset, whether they could be put into components and how they could be grouped. That was a significant piece of work, so Scottish Canals has certainly progressed that element. It was an ambitious project plan but, obviously, I was not able to sign the accounts until a couple of weeks ago.

Bill Kidd: To what extent, if any, have the issues around valuation of assets impacted on the ability of Scottish Canals to prepare a medium-term financial strategy? Will it be able to do that?

Joanne Brown: Scottish Canals has an initial financial strategy. The work on valuations in 2021-22 took up a significant proportion of the finance team's time, which meant that some activities were, in effect, put on the back burner while the team focused on the valuations and annual accounts. Scottish Canals has done an initial outlook for the next three years, and it has made a commitment to produce a more detailed financial strategy that will take into account the decision on the VAT element and the recent pay award. Scottish Canals is committed to that—it is part of an action in our external audit report, which has a deadline of October this year for completion.

Bill Kidd: That covers what I was going to ask next. Thank you very much.

The Convener: I will now bring in Willie Coffey, who has a suite of questions to ask.

Willie Coffey (Kilmarnock and Irvine Valley) (SNP): Good morning, Auditor General and colleagues. I will continue with examination of the historical data side of the problem.

You have identified that valuations for some of the assets were based on cost data that was provided by the management and drew on, for example, estimates of historical project costs. Is the fundamental issue that we just do not have records of what the assets were worth in the past? Is that what we are dealing with, principally?

Stephen Boyle: The situation is, undoubtedly, very complex. It has been challenging to value assets in a different way from how that was done previously and, in doing so, to find reliable records. You mentioned engineering records. Joanne Brown can say a bit more about the methodology and approach that Scottish Canals took with the consultants that it used to support the valuation. That is very relevant. Undoubtedly, however, we are talking about an exercise that was really challenging but which was consistent with the methodology and valuation approach that Scottish Canals was required to follow, in

conjunction with the accounts direction from the Scottish Government on the methodology to be employed and reported in the annual report and accounts. That complexity, together with dealing with very old assets and historical records, make valuation very difficult to achieve. Joanne Brown can say a bit more.

Willie Coffey: Yes—please do.

Joanne Brown: Scottish Canals determined that, on the whole, the assets are networked specialised operational assets, which requires them to be valued on a depreciated replacement-cost basis. In some instances, it worked closely with the consultants, where third-party cost data was easily available to indicate that something was a suitable measure—for example, lock gates. There were a number of assets for which we were able to substantiate the consultants' judgment and the data that the consultants used in order to benchmark the costs and the replacement costs of the assets.

One of the largest challenges during the audit was the canals themselves. In the 2021-22 accounts, they had a value of around £137 million. That was based on assumptions about the lengths of the canals and the costs per metre to replace lengths of canal. That was very judgment based and estimate based. We had some information from engineers who were, unfortunately, no longer with Scottish Canals. The judgments and estimates that they set out had not been fully articulated or documented.

The canals go back 200-plus years, so there is not the usual cost data available: valuing them is not as easy as valuing a road. There is a lot of data about what the cost of a replacement road would be, but similar data is not available for canals, so it was very hard to support the judgments and estimates in the accounts.

Willie Coffey: Given all that, how will we ever resolve things to the satisfaction of external audit if there is a real difficulty in establishing the original valuations of assets or even in benchmarking those values against similar assets elsewhere? Is that the journey that we are travelling on? Are we trying to benchmark the whole asset portfolio against similar assets elsewhere and being comfortable that that is a fair and reasonable assumption? Is that where we are? That sounds like an impossible task to me, but is that where we are going?

Stephen Boyle: I think that that is largely where we are. Mark Taylor might want to say a bit more about the alternative options. It is not for us as auditors or for Joanne Brown as the external auditor or even the incoming external auditor to say how a public body should value its assets. That is for that public body together with the

sponsor body, the Scottish Government—with a degree of flexibility, but not that much. It depends on the judgment on what the assets are for. In the case of Scottish Canals, as Joanne has set out, the assets are operational assets. That drives a particular valuation methodology. However, there are other categorisations of assets. Across the public sector, there is a range of categorisations. Scottish Canals is not the only body that has very old assets. In some places, they are valued differently.

That takes us back to one of the key judgments that we made in the report. Scottish Canals, together with its sponsor department, have to say what its plan—its route through this—is so that the accountable officer and the auditors can be satisfied that there is enough evidence to support valuations, given their centrality to the annual report and accounts.

Mark Taylor: I absolutely recognise the challenge that Mr Coffey set out. The starting point for what we said in the Auditor General's section 22 report is essentially having a broader look at what the plan should be. It might be that the work and the approach that has been set out and which Scottish Canals, with the support of Transport Scotland, has determined is the right thing to do should carry on. There are challenges there, but there is also an opportunity to have a broader look and ask, "Are we going about this in the right way? Can we reframe how we are looking to do this?" It is not for us, as the auditors, to say what the solution is in there, but there is a broader opportunity to say, "We are where we are. We've got the history that we know about. We've seen this coming since 2012. We've had a go at it. Is more of the same the right solution, or is there a different solution?"

Willie Coffey: Thank you for that.

Auditor General, you also raised in the report issues relating to ownership, rights and obligations, which probably further complicate the whole mix. How much have those issues in the background impacted on the ability to produce and prepare accurate statements on the valuation of assets?

Stephen Boyle: That is a good example of additional complexity in this year's audit. Joanne Brown can say more about what she and her team encountered. Fundamentally, auditors have to satisfy themselves when they look at any sets of accounts of public bodies or elsewhere. If a body is disclosing assets, the auditor has to say, "Prove to us that you actually own them." They might have the title deeds or associated evidence of ownership. Grant Thornton did not see all that from the sample testing that it did. However, Joanne is best placed to set that out.

Joanne Brown: From our perspective as an auditor, we are looking for evidence that Scottish Canals has rights and obligations and therefore ownership of the assets to enable it to account for them on its balance sheet. One of the challenges is the nature of the asset base. Within that, there are a number of towpaths, some of which are Scottish Canals towpaths and some of which are bordering local authority towpaths. It had to go back to look at land registry data from Registers of Scotland. Scottish Canals did not have that data; it had to look for it to be able to evidence the existence and ownership of the assets.

09:45

In our sample testing, there was at least one item where, although Scottish Canals had included it in its fixed asset register, it was not owned by Scottish Canals, and it had to adjust that. That was in a relatively small sample of the total population. Given the nature of Scottish Canals and how much work it does in partnership with other bodies, which includes receiving additional third-party funding, we recommended in the external audit report that, when undertaking partnerships and funding agreements with the likes of Sustrans, Scottish Canals should determine who owns what asset and what the asset is. That would help Scottish Canals to properly account for the asset, if it is its asset. Scottish Canals just did not have the controls in place in the past to be able to properly evidence for audit purposes.

Willie Coffey: Is Scottish Canals making sufficient progress in the area to reconcile that? Is it making good progress or any progress towards that? Disentangling all that is really complex. Is that being done?

Joanne Brown: From what we saw, a huge effort was made during the audit process to get evidence of the existence of assets. Scottish Canals understands the importance of having evidence of rights, obligations and the existence of assets, and it has endeavoured to get that evidence for all assets that ultimately go into the final fixed asset register. In some respects, that part, although it is complicated, is easier than some of the judgments and estimates on, for example, the cost data around canals' length.

Willie Coffey: My final query is on the comment that you made earlier about errors in the accounting statements. I will read this bit so that I get the wording correct. The report states:

"the reconciliation of the reconstructed closing balances to the figures in the draft accounts identified several errors."

Will you just flesh out for us a wee bit what those errors are and what has been done to correct them?

Joanne Brown: In our external audit report, we highlight about 10 pages of adjustments to the unaudited accounts. Some of those adjustments relate to identified errors. For example, there was a valuation report that did not reconcile to the TB. There were reconciling differences, so Scottish Canals needed to adjust for that.

Willie Coffey: What is the TB?

Joanne Brown: Sorry—it is the trial balance. In effect, the trial balance drives the accounts, and that is the financial ledger. Scottish Canals made some changes there.

We identified a number of errors, which comes back to the nature of the disclaimer opinion. We knew that there were errors and that, extrapolating from those—given that we sample tested—they were highly material. Some of the errors were in the categorisation of assets under construction and additions that Scottish Canals had put through in 2021-22 that should have been in the prior year's accounts. When you have something as an addition, if it is already in operation, it should be valued, and those obviously had not been valued. Scottish Canals had made a decision to retain an asset at historical cost, and we were not clear about the judgments on that. We felt that that should have been included in the valuation.

There was a challenge about the residual value of canals and what time period should be involved. Some of those are highly material. Scottish Canals judged that a canal would have a residual value for 12 years, but it did not necessarily have evidence to support that judgment. If that changed even to 10 years instead of 12, there could be a £30 million difference in the accounts.

There was a series of errors. There are known errors that Scottish Canals will need to correct, and there are other errors that it needs to investigate to ensure that it puts forward a complete and accurate accounting record.

Willie Coffey: That sounds to me like plain and simple accounting errors and lack of awareness of accounting practice. Could you give us any assurance that that is being addressed, and that that kind of error rate will not be seen in the next set of accounts?

Joanne Brown: Some of that comes back to the earlier points about the skills and capacity of the finance team, plus the turnover in the team.

I am aware that Scottish Canals has effectively done a restructure of its finance team and has introduced two new posts to increase the capacity and skills in the team. That recommendation is in our external audit report, which Scottish Canals management have signed up to take action on. By strengthening that team, the quality of the

accounts and the evidence for audit should improve.

Willie Coffey: If you are involved, will you be keeping a close eye on that next time?

Stephen Boyle: That will be Joanne Brown's final audit report on Scottish Canals, but a new team of auditors will do just that.

I will add to a couple of Joanne's points. She said that there were 10 pages of errors reported in the external auditor's annual report that accompanies the accounts; that is most unusual. We rarely see an auditor's report with that number of reported errors or requested changes. Bear in mind that that is based on sample testing. Auditors test samples of transactions or assets and then apply judgment or models to see what that means for the population. That brings us back to the range of factors that Grant Thornton built into its judgment that a disclaimer was the most appropriate opinion on the accounts.

The Convener: One of the points in the report is that Scottish Canals needs to consider the value for money of its approach to valuations, including whether it is getting value for money from the consultants that it engages. Have you seen any evidence that it is doing that?

Stephen Boyle: We refer to the fact that Scottish Canals has spent £500,000 on consultants to support the asset valuation activity in year, and it planned to spend a further £100,000 in the 2022-23 financial year that has now concluded.

We also note in the report that, in commissioning the work from the consultants, Scottish Canals does not retain ownership of the valuation model. Scottish Canals should consider whether that was a good decision to make, given the importance of the model and how it connects to a fixed asset register. Having an operational fixed asset register was not part of the overall commission. We have not arrived at a view on that, but we think that it is a relevant factor for Scottish Canals to consider.

I emphasise the point that Mark Taylor made earlier about whether it is the best approach to plough on and get to a conclusion on the methodology, or whether there are other routes to arriving at a true and fair set of accounts. It is relevant that there are still considerable sums of public money being invested in consultants to support an approach that has not yet borne fruit.

The Convener: I will move on to a different question, which is about the leadership of the organisation. We are aware that the former chief executive of Scottish Canals left and that, as recently as May this year, a new chief executive started. Was there a gap before that position was

filled and, if there was a gap, has that contributed to some of the difficulties?

Stephen Boyle: I will ask Joanne Brown to set out the timescale, and then I will come back in.

Joanne Brown: The previous chief executive left the organisation in December. That was a planned exit, in effect, given that she had been chief executive of Scottish Canals for five years. It took steps to appoint an interim chief executive, who was the chief operating officer of Scottish Canals. He had been with the organisation for many years, and he was very familiar with Scottish Canals. He filled that role on an interim basis until the new chief executive started last month.

I do not think that that contributed to the difficulties. The interim chief executive was within the organisation in the prior year, when the disclaimer was there, and he was a member of the board that supported the project plan. There was knowledge and experience in Scottish Canals and the challenge of the valuation and what the organisation was attempting to do was well known across the leadership team, so the change in chief exec did not, in my view, impact on the situation.

Stephen Boyle: Joanne Brown has made a fair assessment. However, there is a significant onus on the new chief executive to take his own view about the approach that he has inherited and about whether that approach will produce the result of a valuation methodology that leads to a compliant annual report and set of accounts.

The question also links to the wider, strategic purpose of canals. Are canals an operational asset? Is there an alternative approach? Part of that wider strategy of the organisation incorporates the maintenance of the canal network alongside, as Joanne mentioned earlier, some of the other activities that Scottish Canals has engaged in over the past 10 years.

The Convener: My final question is about the relationship with the Scottish Government sponsor division. We were told in evidence last year that Transport Scotland attends board meetings of Scottish Canals and that it—this is the expression that was used—“sits hand in glove” with Scottish Canals. Is that a characterisation that you recognise?

Stephen Boyle: Certainly, we recognise that Transport Scotland attends board meetings. I will leave the phraseology for others to describe. It brings us back to one of the judgments that we have made in the report, which is that the sponsor team at Transport Scotland will have an important role in working with Scottish Canals to determine the way forward and to arrive at a valuation approach and strategy that can be fit for purpose to deliver a clean set of audit opinion in future.

The Convener: Mark Taylor mentioned earlier that there had been a risk warning about this being a possibility as far back as 2012; we are almost a decade on and auditors are still issuing disclaimers. Some fundamental problems still exist, such as turbulence in the finance team and the leadership of the organisation, and so on. Why is Transport Scotland not injecting some stability into that equation?

Stephen Boyle: I will take that in reverse order. Stability is an important question for Transport Scotland in relation to its views on the way forward.

On the chronology, Scottish Canals became a public corporation in 2012-13, and I know that the committee has engaged with the Office for National Statistics on elements of its history. The Scottish Government, in discussion with the ONS and Scottish Canals, recognised that “public corporation” was not the best descriptor of the core purpose and activities of Scottish Canals. As we know from last year’s evidence and as is reflected in today’s report, that recognition has led to Scottish Canals becoming a non-departmental public body and having to adopt different accounting practices. There is a great deal of history behind the point that we have reached. However, we need to take the opportunity that exists now, with the new leadership of Scottish Canals and the sponsor team, to say what the best way forward is that will deliver value for money and a clear, compliant set of annual reporting accounts.

The Convener: Thank you. We have run out of time, so I will draw this part of this morning’s session to a close.

I thank the Auditor General for his evidence this morning, as well as Mark Taylor and Joanne Brown, who has been moved on, which is a routine thing—it is not because you have done anything wrong, Joanne, is it?

I thank you all for your evidence, which has been very illuminating. We will need to consider our next steps as a committee in response to the evidence that we have heard this morning. I now propose to suspend the session in order to allow for a changeover of witnesses.

09:59

Meeting suspended.

10:02

On resuming—

Major Capital Projects

The Convener: I welcome everyone back to this morning's meeting of the Public Audit Committee. The second principal item on our agenda is consideration of major capital projects. I am delighted that we have four witnesses from the Scottish Government to help us with our inquiries on major capital projects: Alison Cumming is the director of budget and public spending; Alison Irvine is the chief executive officer of Transport Scotland; David Signorini is the director of environment and forestry; and Kersti Berge is from the directorate for energy and climate change. You are all very welcome.

We are particularly interested in focusing on the Government's approach to net zero and the whole agenda around climate change targets. We are a little pressed for time, so there will be no opening statement—we will go straight to questions. Bill Kidd will ask the first couple of questions.

Bill Kidd: I thank the witnesses for being here today. With regard to the Scottish Government's "Infrastructure Investment Plan 2021-22 to 2025-26: Progress Report for 2022-2023", to what extent do the budgetary challenges impact on the delivery of programmes under the net zero and environmental sustainability theme?

Alison Cumming (Scottish Government): I will take that. If colleagues want to come in on anything specific afterwards, please do.

We manage the entirety of the capital programme across all portfolios. Members will be aware that, last year, we had an emergency budget review that necessitated some capital savings. Given the nature of that review, one element involved considering what savings were practically possible in-year and another element involved applying a strategic lens to protect the areas of greatest priority and greatest potential impact.

The capital position overall has been impacted by the overall fiscal position. The capital funding outlook is very challenging. We had negative consequentials in 2022-23, which means that we often have to prioritise in-year. However, ministers are clear when taking decisions about prioritisation that projects that support net zero are one of the top priorities and should be protected to the extent possible, but they are subject to the considerations that I gave about in-year savings. Sometimes, we have to consider what can practically be paused or halted at that point in the year.

Bill Kidd: On the basis of what you have said, we assume that those financial issues and others

are the reason why interim emissions targets have been missed so far. Will delays to delivery of, or scaling back, the net zero and environmental sustainability programmes have a further impact on the Scottish Government's ability to meet emissions reduction targets?

Alison Cumming: I invite my colleague to respond.

Kersti Berge (Scottish Government): I will build on what Alison Cumming has said. Budgetary challenges are very real, and they come at a time when we need to invest significantly in the net zero transition for pay-off well down the road. That said, the Scottish Government has increasingly invested in the net zero agenda. In the capital spending review back in 2021, there was a significant step-up in our net zero-related investment. In the revised CSR allocations that Alison Cumming talked about, there was a commitment to invest £5 billion in rail infrastructure, because investment in public transport is a critical component of the net zero transition. We have also committed to investing £1.8 billion in heat in buildings, and there is additional funding on top of that.

We recognise that this is a challenge. You are correct that we missed the most recent emissions targets—it was a fairly narrow miss, but it was a miss nonetheless. We will continue to focus closely on net zero as we work out capital funding allocations.

Public sector funding plays an important role, but we are increasingly looking at how we can even more effectively leverage in private sector funding to support the transition.

Bill Kidd: It was a narrow miss but a miss anyway. The latest analysis shows that emissions from transport and buildings increased during 2020-21. How will the use of that information impact plans for future infrastructure investment to tackle such problems?

Kersti Berge: Our three biggest emitting sectors in Scotland are transport, industry and buildings. If you look at our capital spending allocation, you will see that we have more devolved powers in areas such as transport and buildings, which are the areas on which our capital investment in net zero is significantly focused—our spend is targeted at those areas. As I said, there is £5 billion for rail infrastructure and £1.8 billion for decarbonising our buildings, which represents a significant step-up in this parliamentary session compared with previously.

It takes time to deliver the investment and for the investment to have an impact on emissions reduction. A lot of what we are doing—not everything—has substantive lead times before emissions reduction will be delivered.

Bill Kidd: Like most people, when I think of emissions, I think of transport—vehicles and suchlike. Most people do not think too much about emissions from buildings. A lot of buildings—the majority, I suppose—are not under the direct control of the Scottish Government. In what ways can the Scottish Government have an impact on addressing emissions from those buildings?

Kersti Berge: I will take that question, too, as it is still in my area.

That can be done in a number of ways, partly through regulations and partly by providing support for individuals and businesses. Again, we must leverage private sector finance where we can.

We have just laid regulations to require zero-emission heating in new builds. Subject to those regulations being passed, that measure will have a significant impact. We also intend to consult this year on a bill to regulate for improved energy efficiency and zero-emission heating for homes and domestic buildings. That gives a sense of the kinds of things that we are doing on the regulatory front. Using the regulatory tools applies across many areas of emissions reduction. We will need regulation, along with financial support. On financial support, as I mentioned, we have committed to investing £1.8 billion overall in the current parliamentary session.

I can go into detail about how we will achieve the emissions reduction in buildings, although I do not need to do so now. In Scotland, it will be done mainly through heat networks and heat pumps. We have a number of loan and grant schemes to support individuals, companies and housing associations to decarbonise their buildings.

Bill Kidd: I was wondering about help for private citizens to enable them to address these issues.

Kersti Berge: Shall I say a bit more about those schemes now?

The Convener: We are a bit pushed for time, so we cannot go into too much detail about particular projects. We have questions about specific projects, so we will come back to those in the course of the discussion over the next three quarters of an hour.

Willie Coffey has some questions.

Willie Coffey: Good morning, everyone. Could you make a few comments on the impact that the current economic situation is having on the programme? I am thinking in particular of issues with supply chains, inflation and so on.

Alison Cumming: As we reported in the medium-term financial strategy that was published in May, the Office for Budget Responsibility has

forecast that we will have a 7 per cent real-terms reduction in our capital funding between 2023-24 and 2027-28. That is what we expect.

We have seen significant pressures from construction inflation, which peaked at 25 per cent last summer. It is still high, although it is coming down, and we are now finding that the higher price levels are, in effect, baked in—we are not going back to pre-shock levels. That will undoubtedly have an impact on our ability to deliver the infrastructure investment pipeline as originally intended, to the original timescales.

That is why ministers intend to do a further reset of the capital spending review, which will be published alongside the budget for 2024-25. That gives us an opportunity to reset the pipeline and to extend it by one year, to 2026-27, in recognition of the fact that things will take longer to deliver. As flagged in the policy prospectus, that will enable us to direct our capital investment at the Government's top priorities, including reaching net zero and sustaining public service infrastructure.

The inflationary environment, with the impact flowing through into the UK Government's funding decisions, is having a significant impact on the extent of what our investments can achieve in Scotland and the pace at which that can be delivered.

Willie Coffey: What might be the impact on those programmes? You have said that the Scottish Government will try as best it can to protect and prioritise net zero projects. Is that the expectation? Can members take that as an assurance that net zero projects in the capital programme will be given priority as far as possible?

10:15

Alison Cumming: They will be given priority. We have budgetary tools that will help us to provide advice on prioritisation. Net zero is a priority alongside public service infrastructure, so we cannot direct the whole capital budget to net zero; there needs to be a balance. As Kersti Berge said, we are looking at the range of measures and models that might be available to help to maximise investment from different sources across the range of projects and programmes in the infrastructure investment pipeline so that we can supplement the public capital that is going into them.

Willie Coffey: Are you able to give the committee any hints about the potential projects that might suffer from delays, pauses or even cancellation? Can we draw you on that to give the committee an inkling of what that might look like?

Alison Cumming: It will probably not surprise you that I cannot be drawn on specific projects this morning, because the decisions have not yet been taken. We are working through that prioritisation with ministers and bringing them the evidence about which investments can have the greatest impact on emissions reduction and other priorities.

Willie Coffey: When will the Parliament see all that?

Alison Cumming: It will be when the draft budget is presented to the Parliament. The Deputy First Minister and the Finance and Public Administration Committee are engaging on the date for the draft budget. It will depend on when the UK's budget statement is given in the autumn. I expect it to be roughly the same time as it was last year, which was December, but it is subject to the UK's timings.

Willie Coffey: Many thanks for that.

The Convener: Craig Hoy might also have some questions on this area.

Craig Hoy: Before I delve into detail about a couple of infrastructure projects, I want to go back a bit. The Cabinet Secretary for Finance has said that there will be a prioritisation exercise in relation to infrastructure spending. You have said a little bit about how you will approach that in relation to net zero and public services. Is it therefore safe to say that road projects will be given less prioritisation than perhaps net zero? Can you see a conflation of the two in relation to road infrastructure helping to achieve net zero objectives?

Alison Cumming: My colleague Alison Irvine might want to say a little bit about roads. Overall, there is no presumption against investment in roads in the prioritisation framework that is coming out soon. There is still a clear need to invest in road projects, and ministers have made some specific commitments in that regard. We will look across the piece at net zero and other areas of our public service infrastructure in which we must continue to invest.

As I said, Alison Irvine might want to say a bit more about the planned investment in roads projects.

Alison Irvine (Transport Scotland): There are various reasons why we will want to invest in transport infrastructure. Ministers have been clear about their net zero ambitions and the prioritisation that comes with that, which is why we spend more than half of our transport budget on public transport and other sustainable modes of transport. That is all set out in the investment hierarchy that we adopt.

In that context, people still need to get about, and there are other reasons why we might want to invest in our road network. I am thinking about

road safety, severance issues, air quality and connectivity issues in particular.

Craig Hoy: Has that prioritisation exercise changed since the Bute house agreement?

Alison Cumming: The Bute house agreement contains some specific commitments in relation to investment, particularly in net zero schemes. The infrastructure investment plan and the original capital spending review predate the Bute house agreement and have net zero as a clear priority. We will look at the full range of projects in the pipeline and the Bute house agreement as part of the prioritisation that lies ahead of the capital spending review reset.

Craig Hoy: My next question might be one for Alison Irvine. You will be aware, particularly in relation to South Scotland residents in the Scottish Borders, West Lothian, East Lothian and Midlothian, of the £120 million planned potential intervention at Sheriffhall roundabout to relieve congestion at what is now a very congested pinchpoint. In 2020, it was held up quite significantly by a campaign that was led by the Green Party, with a local public inquiry getting under way earlier this year.

Do you have a revised timetable for the Sheriffhall intervention? Is it perhaps one of the areas for reprioritisation? After all, at any given time of the day, cars can be sitting idling in huge tailbacks, which will be having an environmental and economic cost. Where does something like Sheriffhall fit into the broader prioritisation exercise, given that one party in the coalition is clearly opposed to such interventions?

Alison Irvine: I will deal with the specific issue of Sheriffhall and then talk in more general terms about the rest of your comments.

We have completed the public inquiry work on Sheriffhall and are awaiting the response and the decision that has been made. Because we are in that position, we are not able to determine a programme at this point in time.

More generally with regard to Sheriffhall and a number of other projects that we have in the transport portfolio, I go back to the comments that my colleague Alison Cumming made at the start of the evidence session about the squeeze on the capital budget. The prioritisation exercise will need to come through before we are able to say anything one way or the other about a whole range of projects in the transport sector as well as in other sectors. I am sorry if that does not answer your specific question, but it is probably as clear as I can be at this point in time.

Craig Hoy: As far as the presumption of priorities is concerned—and given the 7 per cent reduction in the capital budget that you have

talked about—would it be safer to say that you can see investment flowing away from those sorts of projects towards public transport, net zero and public services? With regard to managing my constituents' expectations, is that the kind of expectation management that we should be engaging in?

Alison Irvine: Perhaps I can take you back to one of the very first questions that your colleague Mr Kidd asked in relation to the climate change targets. Transport is the sector with the biggest emissions in Scotland, and it was one of the sectors in which we saw quite a significant rebound from the previous year, because activity levels had been vastly subdued during the pandemic. You can see how stubborn—if I can use that word—transport emissions are and how challenging it is to reduce them.

This is not just about the infrastructure—although that, as well as giving people alternatives, is really important—but about changing behaviours and drawing other policy areas into the mix. I am thinking, in particular, of how transport interacts with land use planning. All of that needs to come together. I would not want us to think that we will be able to solve the transport climate emissions challenge purely through infrastructure, because a whole number of dynamics play into it.

Craig Hoy: That is fine.

My final question is on oncology-enabling projects at the Edinburgh cancer centre, which have been delayed by approximately a year, with the cost probably 10 to 15 per cent over budget. Can you flesh out the reasons for the delay and the increase in budget?

Alison Irvine: I am sorry—I do not have that detail to hand today, but we can write to the committee with that information.

Craig Hoy: No problem. Thank you very much.

The Convener: We are trying our best to be strategic this morning and not to get too much into pork-barrel politics, Mr Hoy.

I call the deputy convener.

Sharon Dowey: Good morning. In the third year of the IIP timeframe, reported spend on the programmes under the net zero and environmental sustainability theme appears to represent only around 13 per cent of total planned expenditure. Is spending expected to reach the amounts that were envisaged when the IIP was published, even with a one-year extension to the programme?

Alison Cumming: In overall terms, I reinforce the point that the decisions that were taken by ministers in the 2023-24 Scottish budget reflect

£2.2 billion of low-carbon investment in Scotland, which is the highest amount spent on low-carbon capital investment to date. I am just highlighting, by way of illustration, that the decisions that have been taken up to now show the commitment to increasing investment in low-carbon capital.

We cannot comment on specific sums today, because the prioritisation exercise is still under way, but, through that prioritisation, we are seeking to focus on the outcomes that can be delivered through particular programmes and to look at how those programmes can maximise the impact on net zero objectives, in particular—in due course—around emissions targets.

Sharon Dowey: Which specific programmes are likely to experience lower than expected spend or to require extended timeframes to achieve delivery on the scale that was originally anticipated?

Alison Cumming: Those issues are being considered by ministers at present. The outcomes of those decisions will be presented to the Parliament in the capital spending review reset alongside the draft budget.

Sharon Dowey: Has progress on net zero and environmental sustainability programmes been affected by lower than anticipated uptake among private sector and local authority partners? If so, what is being done to address that?

Alison Cumming: We have encountered underspends on particular schemes where demand has not picked up quite as quickly as we anticipated that it would when we set the budget using our original projections.

Kersti Berge: I can say a couple of things on buildings decarbonisation. This was in the period when we still had a bit of Covid overhang. When it comes to people looking to get folk in to install a heat pump or energy efficiency measures, there was a period when that was a bit slower than we had hoped that it would be.

Some of these initiatives are fairly new. In relation to the scale of investment and support for the heat network fund, it takes a little while to get the pipeline up and going. To go back to the capital funding programmes that deliver heat decarbonisation and energy efficiency measures in people's homes, we have seen a steady uptick in take-up. Last year, there was a significant increase on the previous year.

On decarbonising homes, we are increasing our public awareness and marketing work to increase uptake. Taking buildings as an example, there is a clear upward trajectory in those areas.

Sharon Dowey: I have a quick question about target setting. When you set targets for transport or any kind of infrastructure, who sets the targets

and ensures that they are specific, measurable, achievable, relevant and time bound, rather than being pulled out of thin air? I am looking at some of the figures—for example, it was initially planned that £495 million would be spent on bus priority investment but, so far, only £26 million has been allocated. I know that you say that you are still reviewing things to see where you can make savings.

On housing, there seems to be an 11-year plan to build 110,000 houses by 2032, which works out at about 10,000 houses a year. According to that, it looks as though we are 12,517 short, although I recognise that we have still to get to the end of this financial year. Are there workings in the background that show how many houses you expected to build each year? Is there more information that can be shared so that we know where we are in the investment programme?

Alison Cumming: Overall, for any capital investment programme, there is a business case to support the investment decision and, alongside that, a delivery plan that is subject to internal governance. Ultimately, ministers take decisions on where targets are set, based on the advice and evidence presented by civil servants.

If the committee would like additional information on the affordable housing supply programme, we can provide that. As you said, it is a 10-year-plus programme. There are plans for how the investment will be phased over the period, and I understand that we remain on track to deliver the overall target at the end of the period.

The Convener: I will pick up on that theme. Sharon Dowey mentioned the bus priority improvements under the future transport fund. I presume that that involves building bus lanes and ensuring that buses get priority in traffic, even across the Sheriffhall roundabout.

When we look at the budget headings, we see that the planned expenditure on that was £495 million, but only £26 million has been spent. There is £300 million in the budget for Scotland's heat network, but only £6.4 million has been spent. There is £26 million in the budget for the low-carbon manufacturing challenge fund, but only £750,000 has been spent. There is a planned spend of £180 million on the emergency energy technologies fund, but only £10 million has been spent.

I do not want to miss out Mr Signorini. The peatland underspend has been a bit of an issue as well, has it not? I know that Rhoda Grant has written to the cabinet secretary, who has confirmed that the underspend on peatland restoration in 2020-21 was £12 million and that it was £7.4 million in 2021-22. Why is there such slow progress in those areas?

10:30

Alison Irvine: Shall I kick off?

The Convener: Sure.

Alison Irvine: Let us talk about the bus priority fund. I will relate this answer back to the question that Ms Dowey asked about the role of other actors.

When the bus priority fund was launched, the £495 million was to set a signal of ambition from ministers about how important buses, bus priority and the bus sector are to the people of Scotland and the contribution that buses make to the transport offer. Since the scheme was launched, we have found that there have been fewer schemes that have been what I would describe as ready for construction than we had hoped.

A lot of work is currently going on with local authority partners, the Confederation of Passenger Transport UK and the Convention of Scottish Local Authorities throughout the country that involves looking at a whole range of business cases. That is predominantly where the £26 million that has been allocated is going to. It is anticipated that that will give us a pipeline of projects that we can start to roll out.

I will stop there.

The Convener: To go back to Sharon Dowey's point, I presume that those figures were not just plucked out of thin air. I presume that they were informed assessments of what was likely to be needed in order to help to meet the Government's target.

Alison Irvine: Absolutely—they were informed. We are now, with all the various partners, trying to pull together the evidence base and the business cases for all the offers that we have on the table to ensure that the outcomes are delivered. That might seem painful in terms of the timescales, but it is really good governance.

As you all know as politicians, once you try to take away road space, whether that is for bus priority or active travel, quite a lot of community consultation and engagement and views need to be taken on board. That is the right approach, because we need to bring people with us as part of the journey to overall climate emission reduction.

The Convener: I get that, but I also take cognisance of the fact that the previous First Minister declared that we have a climate emergency. That suggests that some fairly urgent action should be taken rather than a gradualist approach.

I do not know whether Mr Signorini can speak a little about what is happening with peatland restoration and why there is a hold-up there.

David Signorini (Scottish Government): I am happy to do that.

In summary, peatland restoration is in a phase of trying to build capacity, create demand and get to the delivery levels that it needs to get to. We are in the early stages of a 10-year programme. It is about the generation of demand for projects; a good process to get those projects assessed and approved, and the due diligence done; and the people, equipment and skills.

We have made progress in the past year. Some 7,500 hectares have been restored. That is 38 per cent up on the previous year, so there is a step change. We are building contractor capacity. It is quite a skilled operation. Machinery is needed, and we are investing in training and capacity building. The fact that we can say that the programme is a 10-year one gives the private sector confidence to invest in those skills and that machinery.

I acknowledge that we are below where we would want to be, but we have made progress in the past year, and we have confidence that we have the right analysis of the situation.

The Convener: Okay, but to again go back to Sharon Dowey's point, why set a target if it is not an informed target that is realistic and achievable? I think that that is a legitimate question that we are posing this morning.

Another area relating to the restoration of nature is the investment in woodland, forestry and so on, which again is not quite meeting the target. Does that take the shape of grants to private landowners and to some of the equity funds that are involved in the carbon offset racket?

David Signorini: Forestry is perhaps a more mature operation, but it has plateaued over the past three or four years and, to meet the targets, it needs to increase again.

As part of the climate change plan, the statutory targets for emissions reductions are turned into individual targets. They are very ambitious, but they have to be achievable.

On forestry, there is a lot of read-across to the peatland restoration. It is about skills, capacity and the process of application for and approval of grants. Last week, the cabinet secretary announced a whole set of actions and investments in that skills and capacity area.

The Convener: I turn to Alison Irvine for a particular area of interest, which is the whole question of net zero targets and what we are doing on transport. As you rightly say, that is first and foremost about getting people on to public transport. However, one of the other goals that the Government has set is on electric vehicle charging networks and so on. I noticed recently that an

announcement was made that the Government was withdrawing from the EV charging network ChargePlace Scotland and leaving that to the private sector. Is that correct?

Alison Irvine: Those would not be the words that I would use.

The Convener: Choose your own words, Ms Irvine.

Alison Irvine: If I may, I will choose my own words.

I cannot remember which member asked about the role of various actors in that aspect. There is a role for Government and, particularly on EV charging, Scotland has a good track record of leading the way, which is why we have the most EV charging points per head of population in the four UK nations. However, there comes a point when the role of Government is to give other actors the space to invest because, as is well recognised, the Government cannot afford to do this on its own, and should not do so, so there are opportunities there.

The work that we are doing on EV charging is about enabling. We recognise the great work that has been done and the great work that ChargePlace Scotland is doing, but we realise that, to get the pace and scale of investment that we need on EV charging, we must change the way that we do that. That work is under way now. At the moment, ChargePlace Scotland's network of chargers is a mix of those that Government has funded, those that local authorities have funded and those that are privately funded. It is now about working with local authorities or, depending on the area, in a regional context, to understand the needs and demands across the various types of EV charging—whether that is retail or residential—and to produce a plan that gets us to the point where we have the EV charging network that we need.

We are in a kind of transition—that is how I would describe it.

The Convener: It is reported that £65 million of public expenditure has been invested in the EV charging network. What happens to that? Do we get it back?

Alison Irvine: That is the level of investment that gives us the EV charging network that we have on the ground. I would describe that as pump priming. I do not think that it is as simple as saying that we will get it back. It is about where Government is best able to use its investment capabilities and its legislative and direction capabilities to effect behaviour change.

The Convener: Who will own those charge points in the future?

Alison Irvine: I cannot answer that question, but I am happy to write to you if I am able to give you the detail.

The Convener: Thank you—fair enough. Just one other thing from me before I go to Bill Kidd again, and that is a question about the assessment and cost benefit analysis that is made on road improvement projects such as on the A83 or whatever it is. How do you reconcile that with the net zero targets? What criteria is used in order to say, “Yes, that’s going ahead,” or, “No, that is not going ahead.” What criteria is used in order to say, “Yes, that’s been prioritised,” or, “No, that’s been deprioritised?”

Alison Cumming: Prioritisation takes place at different levels. At the overall Scottish Government level, we will take into account prioritisation of large-scale projects in relation to determining the allocations that go to different portfolios. Then, at portfolio level, there will be further more detailed prioritisation taken on the projects in that area. Alison Irvine may want to say more on the strategic transport projects review 2—STPR2; I hope that I got the letters in the right order—and the work that has gone into Transport Scotland’s very detailed methodology of looking at transport projects overall.

Ranking projects across different policy objectives is obviously not an exact science. Based on the recommendations of the Infrastructure Commission for Scotland, we are investing in developing a new investment hierarchy and prioritisation approach for the next capital spending review, and the Scottish Futures Trust is working with us to develop that. In the meantime, we are looking at individual value-for-money assessments through the business cases that are produced for different projects. Ultimately, there will always be an element of political prioritisation of the projects that are considered to be value for money.

The Convener: I have a request, which I am really making on behalf of the clerks and the Scottish Parliament information centre, which is to do with the fact that quite often these programmes have a change of name, especially in the domestic marketplace—Kersti Berge knows exactly what I am talking about. The request is, can you make sure that we can follow the thread of where different programmes go when their name changes, so that, when you produce these major capital projects updates for us, we can see what is what?

I invite Bill Kidd to ask a couple more questions.

Bill Kidd: On the basis that you get nothing for nothing, there has got to be funding for all that infrastructure. The IIP progress report noted that

“The Scottish Government is committed to sustainable deployment of revenue financed investment and capital borrowing to ensure there is no undue financial burden on future policy choices.”

Does the Scottish Government intend to make greater use of its capital borrowing powers to support infrastructure investment in the face of a declining capital budget, and are there any plans for any of the programmes under net zero and environmental sustainability to make use of revenue financing?

Alison Cumming: Taking the first point on capital borrowing, our capital borrowing policy is set out each year in the medium-term financial strategy. The fiscal framework that was agreed with the UK Government allows us to borrow up to £450 million in any year, but there is also an aggregate limit on the outstanding debt at any time of £3 billion, which means that we cannot borrow at that full amount every year, remain sustainable and have borrowing available to us.

The policy has determined that borrowing £250 million a year over a 15-year term is the sustainable level at which we would never breach that £3 billion ceiling. Our policy is to anticipate up to £450 million each year when we set the capital funding envelope for the budget, £250 million of which would come from borrowing, and £200 million of which would be to recognise that there may be some other flexibilities in the year—for example, from consequentials from UK Government funding changes—so that if they do not come to pass, we still have the scope to increase borrowing.

The Government is, within the terms of operation of the fiscal framework, making full use of its capital borrowing powers in planning its capital expenditure. The capital borrowing framework will be subject to consideration in the fiscal framework review that is under way between the Scottish and UK Governments.

10:45

Overall, given the financial challenges that I outlined earlier in the session, we will need to look creatively at what approaches—that, importantly, represent good value for public money—can be deployed to support the available capital funding, given that our capital funding, subject to borrowing, is essentially determined by UK Government decisions.

At the moment, I would not rule anything out in relation to looking at different funding models, whether those are revenue-financed models or, as my colleagues have referred to, they are ways of incentivising more private capital investment in some areas within the net zero investment space.

All those matters will be weighed up and considered at part of the capital spending review.

Bill Kidd: That includes the plans for any programmes under net zero and environmental sustainability being covered in the same way.

Alison Cumming: Yes, in exactly the same way.

I would add that ministers will, obviously, be very thoughtful of the learning from previous revenue-financed capital schemes, and taking into account value for money will be at the heart of any decisions when it comes to using different funding or financing models.

The Convener: Willie Coffey has got another question.

Willie Coffey: Thanks very much, convener, for letting me come back in here.

The convener asked about the A83 and how you balance investment in things like road infrastructure against an overall gain for net zero, and how you demonstrate that. Am I right in saying that the Rest and Be Thankful is on the A83, and that, in 2020, that section of the road was shut for 200 days? If you are investing in a repair, an upgrade, a programme, a project or whatever to solve that problem, are you ultimately able to demonstrate that there is a net zero gain because there would not be a 59-mile detour for vehicles for 200 days in a given year? Do you do that kind of balancing? Can you demonstrate to the committee that that is what is going on?

Alison Irvine: The A83 is a really good example of how, in the transport appraisal process and decision-making process, you need to draw on a range of factors to help inform decisions. As you rightly said, the A83 has been subject to quite significant landslides. That is a result of climate change—we are seeing increased rainfall, which is effecting the stability of the mountainside. I note that that road is fundamental in providing access to vast swathes of Scotland, so there is an impact any time that it is closed.

All those factors are drawn into the appraisal—the business case, effectively—to help ministers to make informed decisions. Ultimately, the decisions on how they prioritise that are for ministers. That is how that is done. Yes, the climate impact that is associated with a road improvement programme is part of that mix, but it is not the only part.

The Convener: Thank you. That was very helpful.

Can I ask each of you if you have got any reflections on the recent Audit Scotland report that spoke about the extent to which there is joined-up working across Government in pursuit of net zero targets?

I will read out a couple of the conclusions from the report. The Auditor General said:

“The Scottish Government does not routinely carry out carbon assessments or capture the impact of spending decisions on its carbon footprint in the long term.”

He also said:

“The Scottish Government does not assess how far the policies outlined in the Climate Change Plan Update will contribute to net zero.”

Finally, he said:

“The Scottish Government does not know how much the policies proposed in the current Climate Change Plan Update will cost”.

Do you think that that is a fair assessment? We will start with Alison Cumming.

Alison Cumming: I point to the work that is under way in the joint budget review, which is looking at how we can improve the transparency of the decisions that we make and at the supporting evidence on how decisions are taken on allocation of resources—both capital and resource budgeting—in relation to impact on climate change and emissions. We are starting to make progress on implementing the recommendations of that review.

We have introduced a dedicated climate change narrative to the budget, and we are developing an enhanced taxonomy of Scottish Government spend to support the Parliament and others in scrutinising decisions.

We are making significant progress on how we can take the evidence base in to support the decisions that are taken in the budget, on applying that across all portfolios and on looking at ways in which the investment decisions that are taken—be they in the health, justice or net zero portfolios—can have the maximum impact on our emissions targets.

Kersti Berge: I will add two things to what Alison Cumming said. One is that this is genuinely hard and no country does it well, so there is not a template out there that we could take and deploy for our purposes. The work that Alison described is ours, and we look at what people are doing internationally to improve our methodology for assessing the carbon impact. Willie Coffey's example of the Rest and Be Thankful is a good example of the detailed challenges that are involved.

The second thing that I will say is in response to the question about the Audit Scotland report on costs and the impact assessment.

We got new, really ambitious climate change targets in Scotland back in 2019. They were voted for by all parties; there was cross-party agreement on it. The year after that, we agreed to publish an

update to our climate change plan. We are required by law to produce a climate change plan every five years, but given the increased ambition for our targets, we thought that we had better get on and set out how we plan to meet them. Normally, it takes a good two-and-a-half years to produce a full climate change plan, given that the climate change plan covers everything. That was an update, a sort-of interim climate change plan, and in the time available we were not able to set out very detailed information on costs and the specific emissions impacts.

We are now in the middle of our next full climate change plan—I am sure that we will be back at the committee to discuss that. The intention is to lay that in Parliament in November this year, and it will be scrutinised then. In that plan, which includes the work that we are doing currently, we will set out information on costs and emissions impact of the policies.

We are doing that work alongside the work that Alison Cumming described about how to improve our assessment of the emissions impact of our policy decisions—not only in the climate change plan, but also when we publish budgets and when we make policy decisions.

David Signorini: I can talk about the peatland and forestry aspects. To paraphrase Kersti Berge, it is hard, but we are making progress.

There is a lot of really good science on forestry and peatland. There are a lot of models around the carbon capture elements of our projects and the emissions that are avoided because of them. Again, we are at the start of that; we are in the learning phase. We are understanding and thinking about economies of scale as we scale up, so we are gathering a lot of evidence and data on emissions and the costs per hectare or per tonne of carbon. We are feeding into Kersti Berge's climate change plan to support decision making.

Alison Irvine: To add to the “it's hard, but we're making progress” theme, we have updated our appraisal guidance to make the climate aspects of appraisal more explicit. That was done shortly after the last climate change plan. It also reflects our commitment to the 20 per cent reduction in car kilometres, so that that is taken into account. There is progress on that.

I have a couple of other things to add. Some of the technologies, particularly those in transport, do not exist at this time or they are very embryonic. It is therefore hard to work out how much the necessary action will cost. It is hard to know what it will look like and how quickly it can be ramped up, but we know that that is the area of innovation that we need to be in place in order to drive a degree of change, so we are doing everything we can, as Kersti Berge and Alison Irvine outlined.

The Convener: Okay, thanks. When we return after the summer recess, we are going to take more evidence on that with the director general for net zero, so we will get his assessment of that.

Data, measurement and assessment are really important to the Public Audit Committee, as is the word that Alison Cumming used: “transparency”. With that, I thank Alison Irvine, David Signorini, Alison Cumming and Kersti Berge for being transparent and giving us their time and empirical observations about how things work in Government on those questions that are important for all of us; it is greatly appreciated.

10:56

Meeting continued in private until 11:21.

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Published in Edinburgh by the Scottish Parliamentary Corporate Body, the Scottish Parliament, Edinburgh, EH99 1SP

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