OFFICIAL REPORT
AITHISG OIFIGEIL

Public Audit Committee

Thursday 16 January 2025

Session 6

The Scottish Parliament
Pàrlamaid na h-Alba

Thursday 16 January 2025

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PUBLIC AUDIT COMMITTEE
2nd Meeting 2025, Session 6

CONVENER

*Richard Leonard (Central Scotland) (Lab)

DEPUTY CONVENER

*Jamie Greene (West Scotland) (Con)

COMMITTEE MEMBERS

*Colin Beattie (Midlothian North and Musselburgh) (SNP)
*Stuart McMillan (Greenock and Inverclyde) (SNP)
*Graham Simpson (Central Scotland) (Con)

*attended

THE FOLLOWING ALSO PARTICIPATED:

John Boyd (Audit Scotland)
Stephen Boyle (Auditor General for Scotland)
Dharshi Santhakumaran (Audit Scotland)

CLERK TO THE COMMITTEE

Katrina Venters

LOCATION

The James Clerk Maxwell Room (CR4)

Scottish Parliament

Public Audit Committee

Thursday 16 January 2025

[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 second meeting in 2025 of the Public Audit Committee.

The first agenda item is a decision on whether to take agenda items 3, 4 and 5 in private. Do members agree to take those items in private?

Members *indicated agreement.*

Section 22 Report: "The 2023/24 audit of Ferguson Marine Port Glasgow (Holdings) Limited"

The Convener: Agenda item 2 is consideration of the Auditor General for Scotland's section 22 report on the 2023-24 audit of Ferguson Marine Port Glasgow (Holdings) Ltd.

Before we start, I remind everyone of my voluntary entry in the register of members' interests in relation to trade union interests.

I welcome our witnesses. We are very pleased to be joined by Stephen Boyle, the Auditor General, alongside Dharshi Santhakumaran, senior manager, and John Boyd, audit director, at Audit Scotland.

We have quite a number of questions to put. Before we get to those, I invite the Auditor General to make an opening statement.

Stephen Boyle (Auditor General for Scotland): Many thanks, convener.

This morning, I am presenting my report on the 2023-24 audit of Ferguson Marine Port Glasgow (Holdings) Ltd under section 22 of the Public Finance and Accountability (Scotland) Act 2000.

The appointed external auditor, John Boyd, has issued an unqualified opinion on Ferguson Marine's financial statements for 2023-24. At the time of the audit, however, the Scottish Government had not yet confirmed funding for FMPG beyond 2024-25. The auditor therefore highlighted a material risk to FMPG being a going concern—as noted by Ferguson Marine Port Glasgow (Holdings) Ltd's management in its performance report in the annual report and accounts. Since then, the Scottish Government has confirmed that it intends to continue to provide financial support to FMPG during 2025-26—subject, of course, to parliamentary confirmation of the budget.

Nonetheless, there remain significant risks to the long-term financial sustainability of FMPG. As the committee will have seen, the Glen Sannox entered service this week and according to the FMPG's most recent submission to Parliament, the Glen Rosa is due to be handed over in September 2025. However, FMPG has secured limited work beyond the completion of Glen Rosa. It will need to work closely with the Scottish Government to ensure that it is able to compete successfully for work and therefore secure its viability.

In my previous report on the 2021-22 audit, I raised concerns about governance and oversight arrangements in relation to performance-related bonuses for senior officers. There continue to be weaknesses in FMPG's governance and internal control arrangements. Although FMPG recognises that, and has made changes following the findings of an internal management investigation into contractor payments, it remains too early to say what impact those changes will have in the medium term.

There have been significant changes in leadership over the past year, and the committee will be aware of the difficulties that the yard has had in securing a permanent chief executive. That lack of stability in leadership has not helped FMPG to stabilise its governance or scrutiny arrangements. For example, my report refers to the internal audit service not completing its annual programme of work.

John Boyd, Dharshi Santhakumaran and I will do our utmost to answer your questions this morning.

The Convener: Thank you very much, indeed. We have a large number of questions, as I said, so I will immediately ask the deputy convener to put some questions to you.

Jamie Greene (West Scotland) (Con): Good morning, Auditor General and guests. Thank you for your opening statement.

Your report paints quite a stark picture of the long-term viability of the yard. You mention in points 1 and 2 of your key messages that there are significant risks and uncertainty around the yard's long-term financial sustainability—a point that you have just reiterated. Could you elaborate on why you have come to that conclusion?

Stephen Boyle: Certainly.

I will bring in John Boyd, as the external auditor, to frame that for the committee and explain what that has meant for the audit and for his reporting, in particular in relation to one of the triggers for today's section 22 report, which was, firstly and most importantly, the disclosure that the management of FMPG themselves made in their annual report and accounts.

It is probably best for John to set this out, but I will touch on it briefly. As I mentioned in my opening remarks, the accounts are not qualified. The real reason for that is that the management has, in the auditor's view, made a very clear disclosure: it has set out the risks to the financial sustainability of the yard. The primary risk is that, although there are letters of comfort from the Scottish Government and funding arrangements in place in terms of both capital investment and letters of comfort from the director general economy, as I mentioned in my opening remarks, there is no pipeline of work beyond the completion of Glen Rosa to support the viability of the yard.

I will pause there and pass to John to elaborate on that. It is important that the committee hears directly from him on the assessment that he made.

John Boyd (Audit Scotland): As the Auditor General outlined, the annual audit report and opinion are unqualified. In the annual audit report, we have included what is called an "emphasis of matter", which is, in essence, the opportunity for the external auditor to draw the attention of the reader to a matter of significance that is highlighted in the accounts. In the case of Ferguson Marine, it is about the assumptions around its being a going concern.

As part of our audit work, we consider management's assessment of a business being a going concern. Within the annual accounts, the directors have disclosed the key risks and uncertainties associated with the financial sustainability of the yard. As the Auditor General outlined, a key aspect of that is that there is no contracted work beyond the MV Glen Rosa. The five-year business plan outlines opportunities for Ferguson Marine, including the small vessels replacement programme. However, at the time of the signing of the accounts, there was no contracted work in place. Therefore, we have highlighted the material uncertainty around Ferguson Marine being a going concern and the wider risk around the long-term financial sustainability of the yard.

Jamie Greene: In essence, you are making that assertion because the management and the leadership team at the yard have made that assertion—you are not making an external judgment on the yard based on the evidence that you have been provided with, but repeating what they are saying in their own audit of the business.

There is a lot of auditing legalese in the report—you talk about disclosures and points of emphasis and so on. What effect does it have on the business when directors make such announcements? Is there a legal necessity for directors make such a disclosure in the reporting of the accounts? It is a profound announcement, given that it is such a big business.

Stephen Boyle: I will start, and then John Boyd can come in.

For clarification, I note that it is not a flow-through. That the management of the yard has made that disclosure is very significant and has implications; however, had it not made that disclosure, it would not be the case that the auditor would automatically have said nothing. It would have thrust it on to the audit team to make a judgment and it could have come to a different view, based on other sources of information, and on John Boyd's assessment of the sources of funding and the business plan.

In circumstances where there is a disagreement between management and the external auditor, it can give rise to a qualification of the accounts, which is something of an escalation of the auditor's view. That the management and the auditor are in agreement is a positive thing. It is an indication of the directors taking their responsibilities seriously.

To touch on your second point, this is a very serious matter. Directors of a non-departmental public body have a responsibility to make fair and open disclosures under the Companies Act 2006 because of its appointment as a public body, as does the accountable officer, which is also set out in the annual report and accounts.

I agree that it is a really serious matter, but we think that it has been set out transparently in the annual report and accounts.

Jamie Greene: That is helpful. Can we drill into some of the numbers that sit behind the conclusions that have been drawn? It is probably worth saying for the record that no one is comfortable with talking about the yard in this context. However, we are reflecting on what is in the section 22 report, so we have to talk about it.

When the report was issued, it was your understanding that, at the time, there was no financial underpinning from Government for the year 2025-26. However, since then, a draft budget has been produced, in which a budget line is allocated to FMPG. Can you perhaps talk me through what your understanding is?

Let us assume that the number in the draft budget is the final one. It might change, of course, but for the purposes of today's meeting, let us work with what we have in the public domain. Is it your understanding that that is money that has been allocated for the next financial year by the Government to keep the yard on its feet and to fund operational costs? Is it for staffing costs? Does it include any investment or upgrade allocation? Alternatively, in your understanding as an auditor, is that money simply for finishing the job of completing the second vessel that the yard is still responsible for? From reading the papers, it is a bit unclear how we follow that money.

Stephen Boyle: We are happy to do our best to provide a bit of clarity. You are right that some of it is about the timing of the publication of the section 22 report and the completion of the accounts and so on.

There are several different funding streams here, some of which relate to funding that is set in the budget. The £47.9 million is the figure that is included in the 2025-26 draft Scottish budget. There is a further proposed investment of £14.2 million, which is identified as being for supporting modernisation activity, to help the yard to be better positioned and to support its intentions to grow its order book. Those are headline levels.

John Boyd will set out what that means for business plan submissions and letters of comfort and so forth.

To address the question that you are asking about certainty and security, because of the letters of comfort and the figures in the draft budget, our assumption is that the yard had certainty for 12 months beyond the date on which the accounts were signed. That is the assessment that we are required to make following the assessment that the management of the yard has made.

Jamie Greene: Mr Boyd, one of the things that it would be very helpful for us to understand is whether the draft budget line of £47.9 million includes or excludes any of the additional £14.2 million that was announced separately for investment. That might be a question for ministers rather than for you, but I presume that you looked at that in the whole anyway.

John Boyd: I am happy to pick up the questions that have been raised. For the year ended 31 March 2024, there was budgetary approval of £76.8 million. There was budgetary approval for the year 2024-25 of £62.7 million. That was before the recently announced budget for 2025-26 of £47.9 million.

When auditing the financial statements for the year ended 31 March 2024, the date of signing is where we focus, and we have the forecast around what the next period of 12 months will look like. At that point in time, the 2025-26 budget information was not available, so we had only what was formally committed, which was £62.7 million for the year ending 31 March 2025. That would take the yard only up to March of the following year.

09:15

When we are considering the ability to continue as a going concern up to October, the letter of comfort from the Scottish Government provides assurance to the yard around continued support. The £47.9 million was not part of that focus in the audit work because it was unknown at that time. What we have outlined in the annual report is the projected costs and cash flows—at that time—for the completion of vessels 801 and 802.

With regard to the question about the 2025-26 budget information, I do not have the information about whether the announced £14.2 million of capital support would be included in that. At the time of the audit, that information had been announced, but no formal information had been reported to Ferguson Marine about what that funding would look like.

However, the business case that I mentioned, in relation to the five-year business plan, included how Ferguson Marine would utilise the £14.2 million to invest in the yard and transform it into a commercially viable business.

Jamie Greene: I will go back to that issue separately, but, before we do so, let us look at page 8 of your section 22 report, where you make some assumptions. I am trying to get my head around the fact that, for the year 2025-26, there will be a number of variables.

How much money will be required to keep the doors open, to keep the staff there and to keep the yard functioning as a going concern for that financial year? That will come at a cost, and there will be a number associated with that—presumably, there will also be a cost to finish the Glen Rosa, either separate to or included in that number. Additional moneys could be required, for example, for capital investment to upgrade infrastructure in the yard—technology, machinery and so on—to secure future business. From reading the papers, it is not clear to me whether what is in the draft budget for 2025-26 will cover all that. That is where I am looking for risk. Perhaps that is a question that you do not know the answer to.

Stephen Boyle: In short, there are variables that probably limit our ability to give you the assurance that you are looking for today. The most significant variable is the position of Ferguson Marine Port Glasgow's business plan, which was predicated on the assumption of the direct award of the small vessels replacement programme.

As the committee is aware, the Government, following legal advice, decided to take an alternative route that required FMPG to tender, and that process is currently on-going. With regard to the various cost streams, 802 has been the most significant and largest on-going project, based on evidence that the yard has given in writing to the Net Zero, Energy and Transport Committee. It is currently due to submit its updated projection to that committee by the end of this month.

Clearly, there are different funding streams. There is the £47.9 million that is set to be in the draft budget for 2025-26, the capital investment, and also the costs assumed for the completion of 802, which straddle two financial years. There are a number of variables still to tease out, but it is for the yard or the Scottish Government, rather than us, to be absolutely precise about those numbers.

Jamie Greene: Indeed, and those are questions that we can ask through due process.

You talked a little about the business plan and some of the assumptions that it makes about securing other work. Obviously, none of us wants to prejudice those decisions in any way, but we know that there is that potential, which was very much part of the plan, and investment is relevant to that.

Was there was any evidence of any other business outside of the small vessel replacement programme? Did you, in any of your auditing, come across any presentations or disclosures from the business team at the yard about other business that it was seeking? Was it commercially sensitive and so the team was unable to disclose it? Obviously, as it is a publicly owned and publicly funded business, one would hope that there would be an element of transparency there. Is it the case that all the eggs are simply in the one basket of the small vessel replacement programme? If that were not to go ahead, where would that leave the yard?

Stephen Boyle: I will start, and I will bring John Boyd in to say more.

As you allude to, some of that will be commercially sensitive and in the midst of negotiations, but equally, as you quite rightly note, it is a public body, and, especially given the context of the section 22 report that draws attention to financial viability risks and the management's assessment of the ability of the yard to continue as a going concern, that absolutely ought to be discussed.

I will hand over to John to talk about the business plan, but before I do that, I draw the committee's attention to the relationship that the yard has with BAE Systems and the work that it is doing with that organisation—that came up in evidence the last time that you considered FMPG. John Boyd can clarify the detail, but the yard's accounts refer to a £1.5 million revenue stream in relation to a three-unit build for BAE.

I do not think that the yard is solely focused on the small vessel replacement programme. I think that other sources are being explored, but I will pass to John to set that out in more detail, as much as we are able to.

John Boyd: On additional work, as part of our audit we have regular engagement with management and the directors, as well as scrutinising what their business plans look like. The five-year financial plan identifies other potential opportunities for the yard, and we are mindful of some commercial sensitivities around those. Although the small vessel replacement programme underpinned the five-year business plan, working opportunities for specific vessels and a pipeline of potential work were identified.

The yard has been actively involved in discussions with third parties about securing additional work outside the small vessel replacement programme. As the Auditor General mentioned, an example of that is the work with BAE Systems. That work spanned the past two financial years and demonstrated a commitment to deliver work outside of 801 and 802, using the yard's different skills and expertise. Right now, there is no contracted work with BAE, but those relationships have been built up from the delivery of previous activity.

Jamie Greene: The five-year business plan is predicated on the award of the small vessel replacement programme, so a significant risk would be posed to the plan and, de facto, the long-term future of the yard if that award was not granted to Ferguson Marine. If it goes elsewhere, there is very little outside of that to underpin the running costs and keep the yard going at its current rate with the amount of people who work there. Are all the eggs—not all of them, but most of them—in that basket, and does that pose a risk?

Stephen Boyle: Very much so. What is clear is that, as things currently stand—subject to events that might unfold over the next few months in terms of future orders—that financial underpinning is not there at the moment. Without that award in place, we agree with the assessment of the external auditors that there are doubts about the ability of the yard to continue as a going concern if it is not able to generate new orders. That is probably self-evident.

Graham Simpson (Central Scotland) (Con): I will follow on from the line of questioning about Ferguson Marine's business plan. According to you, the plan

"assumed the direct award of the contract for the Small Vessel Replacement Programme".

It was wrong to make that assumption, as it cannot be assumed that the firm is going to get that work. Indeed, it later transpired that the firm is now one of six firms in line for that contract, so there is no guarantee that it will get it. Does that not fatally hull the business plan?

Stephen Boyle: There has absolutely been a material change of circumstances. John Boyd might have insight into how FMPG initially arrived at that assumption and how that was then changed. I am not sure that that should be a criticism of the yard, given what seems to be a change in the legal advice about the ability of the Scottish Government to make a direct award. There is a complex set of circumstances in terms of the state aid arrangements, which affect the Government's ability in that regard, and there is also UK legislation on that.

There is no question but that that material change in circumstances was one of the direct contributors to the change in the management's approach in its annual report and accounts to the disclosure of issues around FMPG's viability and the circumstances around the ability of the yard to continue as a going concern.

Graham Simpson: Before John Boyd comes in on that, can you say whether there has there been any attempt to change the business plan in light of the new development that means that the firm has to compete for the work? I think that it was entirely predictable that that would be the case. Has Ferguson Marine done any revision to the business plan?

John Boyd: On the business plan's assumption that there would be a direct award, although the decision not to make a direct award was a fundamental and material change, it was the management's view that some of the underlying assumptions around the timing of contracted work and revenue streams would not materially change based on whether it was a direct award or a tender process, because the timing of the work would stay the same. Therefore, some of the assumptions about when the revenue would be generated would essentially remain the same.

The decision has led to engagement with some other providers around additional work, as I mentioned earlier, and that is identified in the business plan. The business plan includes scenarios on what the future of the yard would look like, and sets out how the Government's £14.2 million investment could be used to support the yard.

Stephen Boyle: The £14.2 million investment is an important component of the yard's future. The yard has identified that, in order to be competitive and viable in the future, it will have to modernise. It has to invest in its facilities to allow it to be able to be competitive and credible, and for its cost base to support its pace, efficiency, productivity and so forth. That investment is clearly set out in the Government's intentions, but it is just as important that, alongside that, there is a future order book to support the viability with which any modernisation might help.

09:30

Graham Simpson: I completely agree with that. Mr McMillan and I have been in meetings in which we, and others, have argued that the yard needs investment to modernise in order to be able to compete for orders, and ultimately to return to the private sector, which was the Government's ambition for the yard. It needs to modernise—I am in no doubt that that is required.

However, if the yard does not win any of the small vessel replacement programme work, how much extra work does it need to be able to continue?

Stephen Boyle: That is probably a question that the yard itself would be better placed to answer. There is no distinction between ourselves and the yard in our growing attention to the fact that there are doubts about the yard's viability. It is not a stretch to say that it would cause significant challenges either if the yard was unsuccessful in securing work through the small vessel replacement programme or if, in that case, the shortfall was not backfilled by other awards or avenues that the yard is currently pursuing.

Graham Simpson: I will express it in another way. Let us say that the yard gets to September and it has finished the Glen Rosa, which is off and sailing, and carrying passengers, and there is no further work. How long can the yard continue, in your view, without extra work?

Stephen Boyle: I think that that depends on the engagement that the Government will have with the yard. The Government is currently the yard's primary funder, and it will be a matter for the Government if it chooses—through budget submissions to Parliament, of course—to continue funding the yard. What there will not be is an alternative revenue stream that is generated through building ships.

I cannot say that, if the yard was unsuccessful in winning that work, that would result in no revenue or the closure of the yard, because that would be a matter for the Government, as the funder of the yard.

Graham Simpson: Yes, but at some point, the Government is going to have to make a decision on what it does about the future of the yard.

I have a couple of other questions. At paragraph 7 of your report, you mention "Under Recoveries funding". Can you tell us what that is? According to your report, it amounts to £1 million per month.

Stephen Boyle: I will bring in John Boyd, because he has the precise context and detail of that.

John Boyd: The underrecoveries funding is essentially funding that has not been directly attributable either to commercial activity—so, recharged to commercial activity for the likes of BAE work—or to the completion of the Glen Sannox or work on the Glen Rosa. The majority of the spend would be work around tendering for new business, development of a business case or business planning.

For the year ending 31 March 2024, the level of underrecoveries was not material to the financial statements. We highlight in the annual audit report and in the Auditor General's report, however, the point that those underrecoveries are due to increase; the current projections forecast that they could rise to as much as £1 million a month. That touches on the point that you made earlier, Mr Simpson, with regard to long-term funding for the yard if additional work is not secured. That is what the consequence would be. Where additional work is won, the level of underrecoveries would be reduced.

Graham Simpson: So, those are basically costs that the yard has but cannot charge for. It is not getting that money back but it potentially amounts to an extraordinary figure—£1 million a month.

Stephen Boyle: As John Boyd outlined, underrecoveries will generate a future revenue stream in the yard's commercial activities and its operations to secure future work. If we have it, we can share the detail of what that is made up of. The yard will, of course, give you that detail, but it is probably illustrative of the need for real investment in modernisation and commercial activities to secure the future order book.

Graham Simpson: I have one more question. Others will cover other areas, but I want to ask you a question about something that is not covered in your report. Will you bring us up to speed with your efforts to scrutinise Ferguson Marine Engineering Ltd's accounting records?

Stephen Boyle: I will say a word or two and then bring in Dharshi Santhakumaran, who has been tracking the matter from our perspective.

The committee will recall that there is a forensic accounting investigation into the revenue and costs of Ferguson Marine Engineering Ltd, which was the private body to which the Scottish Government had provided financial support before it entered administration and subsequent nationalisation and became FMPG Holdings Ltd.

The Scottish Government, rather than Audit Scotland, is leading the forensic accounting review because, given that FMEL was not a public body, we do not have the powers to undertake such activity. Tendering is under way. I will bring in Dharshi to say where we are and what the likely timeline is. You will recall, Mr Simpson, that I have committed to producing my own complementary reporting on the matter at the completion of the forensic accounting analysis to support its consideration by the Public Audit Committee.

Dharshi Santhakumaran (Audit Scotland): The position before Christmas was that the Scottish Government had not yet completed the procurement exercise. There had been some issues with two firms being close, so the Government was getting some advice and hoped to complete the procurement before Christmas or early in the new year. However, we have not had confirmation of whether that has been completed yet.

The Scottish Government hopes that the analysis will be a two-stage process, with a general overview and then, depending on what that throws up, potentially some more detailed work. The Government hopes that that will be published in the spring, but it will be better placed to give you the detail of the timescales if it has completed the procurement exercise. However, as the Auditor General said, once the analysis is complete, we will review the outcome and the Auditor General will prepare his own review of it.

Graham Simpson: If a detailed report is necessary—I hope that we get a detailed report—do you expect to see that in the spring?

Dharshi Santhakumaran: I am not sure about the timings of the two stages of the work. At the moment, there is a bit of uncertainty about exactly what records there are, the volume of records and, therefore, the amount of work that it will take to go through them and what the investigators will be able to find in them. The first stage needs to be assessing what is there—whether it is paper, whether there are digital records and what scale the investigators are dealing with—before they can assess what else they can do with it.

The Convener: Before we leave the business plan, I will ask you a couple of quick—I think that they are quick—questions on the small vessel replacement programme.

The FMPG board is attended by strategic commercial assets division representatives. In the most recent published minutes that are available on the Ferguson Marine website, which are from the board meeting of 30 May 2024, FMPG directors clearly indicated that they had obtained legal advice that supported the case for a direct award. Do you know anything about the dynamics of that?

Stephen Boyle: I suspect that there will always be alternative legal views, depending on the circumstances. In essence, I am not terribly sure that it matters if FMPG had legal advice. Ultimately, the Scottish Government is required to make decisions based on its own legal advice, and that led to the change in position, which was that it was not able to make a direct award. I am fairly sure that the matter would have been influenced by post-Brexit United Kingdom legislation. John may have further insight.

John Boyd: As the Auditor General outlined, the business case refers to the guidance and advice that the FMPG board obtained, and it includes the board's consideration of the suitability of the direct award.

That is the case on FMPG's side, but I have not been privy to the Scottish Government's advice on the matter. The decision rests with the Scottish Government as it is the procuring body.

The Convener: For the record, is the procuring body the Scottish Government, or is it Caledonian Maritime Assets Ltd, which the Scottish Government is the sole shareholder in?

Stephen Boyle: My assumption is that it is CMAL, but I am happy to check our records and correct the record if I am incorrect.

The Convener: It would be interesting to see whether that legal advice was given to the Cabinet Secretary for Transport, the board of CMAL or both.

My other question on the small vessel replacement programme is whether a single bundle has gone out to tender, meaning that the winner takes all, or could there be different configurations to how that work is awarded?

Stephen Boyle: It is common to see both approaches: as you say, it is a package of work, but the contract can be delivered in different lots. It is for the yard to clarify the subcontracting arrangements, but there could still be alternatives, and I am sure that that will be factored into its business planning preparation, even if it is unsuccessful in one or the other. If we have the detail, John can share it; if not, I am sure that the yard is better placed to share it.

John Boyd: The assumption in the business plan is that it is a single award for a number of vessels. That being said, there is an expectation that there will be future awards as part of a wider vessel replacement programme, but the current one in the business plan is a single award.

The Convener: Okay, thank you. I am conscious of the time, so I will move on. Colin Beattie has some questions to put to you.

Colin Beattie (Midlothian North and Musselburgh) (SNP): I would like to look at some of the changes that have taken place in senior management and on the board. You highlight that significant changes were made in 2023-24. You also note that a review of governance arrangements has been completed.

The chief executive of an organisation is usually also the accountable officer. Can you expand on any concerns that you have about the impact of those changes and whether that ensures that there is stability in the leadership? The chief financial officer is now the accountable officer, which is a bit of an odd sidetrack. Can you comment on that?

Stephen Boyle: I am happy to do so, Mr Beattie. Again, I will pass to John Boyd if there is anything that he wants to add.

I do not have any concerns per se that the chief financial officer is the accountable officer, although I recognise that, as you rightly point out, it is more typical for the chief executive officer to take that role. Given the circumstances of the changes, the interim chief executive officer—who I am sure is able to speak for himself—is primarily focused on the completion of the delivery of vessel 802, the Glen Rosa, as part of his role, as well as on the future business plan and so forth. It was deemed, through engagement with the Scottish Government, that the chief financial officer could undertake the running and discharge of accountabilities. Those are still interim arrangements.

09:45

Should the Government and FMPG make an assessment through the chair of the board that those arrangements have proven to be sub-optimal, there is capacity to change them. Given the circumstances that FMPG has found itself in, with the need for some pace around the appointment of an interim chief executive following the departure of the permanent chief executive last spring, I do not think that it was unreasonable to designate the chief financial officer as accountable officer.

However, in relation to the wider point that you made about there having been a lot of turnover and change, both on the board and in executive level positions, there is a need for stability and for clarity around roles and responsibilities. We are happy to explore further with the committee the circumstances around the deficiencies in internal control and governance in the organisation during the year. Those need to be addressed and the necessary improvements solidified.

Colin Beattie: Continuing on the review of governance, you state that

"FMPG should assess whether the existing cohort of board members provides sufficient capacity to support the updated committee structure."

By "capacity", are you referring to skill sets or the sheer number of members on the board to support the committees? How many committees are there, and what do they do?

Stephen Boyle: We mean the latter, rather than to question the skills of the board. That statement refers to the fact that it is quite a small board. I will bring John Boyd in to talk about the number of committees and the new committee arrangements.

Essentially, with a small board, there is a risk of members being spread thinly across the various committee and governance activities. Consideration has been given to the need for effective governance improvements to the workings of committees, but it will be for the Government, through the chair of the board, to assess whether they can discharge all those responsibilities and governance arrangements effectively under the new set-up. I will pass to John to elaborate.

John Boyd: As the Auditor General outlined, FMPG is a relatively small organisation with approximately 320 to 330 full-time staff. The board reflects that—it is a small body. With the establishment of the remuneration committee and the audit and governance committee, together with the board having quite an operational focus—as you would expect, given that its key priority is the delivery of the two vessels—there has been a lot of emphasis on and asks of the non-executive members of the board.

Colin Beattie: Can I interrupt you there and ask how many people are on the board?

John Boyd: I would need to double-check the accounts. I think that there is a total of six members: two executive members—the chief executive and the director of finance, who is also the accountable officer—and four non-executive members, but I need to double-check the accounts.

The Convener: There are six non-executive directors in the listing in the minutes for 30 May last year.

Colin Beattie: So far, you have not described a plethora of committees. They are the sort of committees that you would expect to see: the human resources committee, the audit committee and so on. Why is that putting so much pressure on the board?

Stephen Boyle: Our position does not touch on the skill set of the members. If you look at the members' biographies, you can see that they come from a range of different backgrounds that are relevant to supporting the delivery of the organisation as a non-departmental public body.

On capacity and the range of committees, you will find that members sit on more than one committee, and their ability to do all that with the extent of change that has just happened is a challenge, and the chair of the board needs to be satisfied, after a period of time, that the capacity of the board is sufficient to discharge its responsibilities. Bearing in mind the significant event of the completion of vessel 802 and all the commercial requirements to get a new business plan in place, it clear that much is going on in the organisation. With the governance arrangements and weaknesses that are touched on in the report, the chair should be satisfied that the new model is working appropriately.

Colin Beattie: Unless I am missing something, the number of committees still does not seem to be excessive. Two committees plus the board should not really be taxing the members that much.

Stephen Boyle: John Boyd can talk about what is required of the non-executives in committee and in other contributions.

We are clear that we are not saying that there is insufficient capacity, but it will probably take the next six to 12 months for the chair to be satisfied that there is sufficient capacity and that, with the volume of change, deficiencies in governance, and four new members coming on to the board in a short period of time, the model is working effectively. History shows that governance has not been effective in FMPG, so the chair will want to be satisfied that the changes are making the necessary improvements.

Colin Beattie: As you said earlier, FMPG is not a big business or a big company. Looking from the outside in, it does not seem to me to be that complex. Why is there so much pressure on the members?

Stephen Boyle: I take this opportunity to restate that we think that there needs to be a period of assessment for the new board. There are four new members and the committee structure has been changed. Because of the history of weakness in governance, people will want to be satisfied that there is adequate capacity on the board. Although on the face of it, the company's set up might not appear to be complex, with its limited order book to complete vessel 802, more certainty about viability in the future will mean that the complexity will increase.

If I can put it in these terms, Mr Beattie, it is a holding statement that the board, the chair and the Scottish Government, as the shareholder, will want to be satisfied that the capacity is appropriate and that the governance improves.

Colin Beattie: The construction of the vessels is an operational issue. The human resources committee is not involved in the building of the vessels; the company has it own structure for what that involves, and we can all get our heads around what that would be. The audit committee is not operationally committed either; it deals with the internal circumstances of the company, as in any other business. I am struggling to see the additional operational pressure on the HR and audit committees because of the construction of vessels.

Stephen Boyle: Perhaps what they do is not directly related to the vessels but I would argue that they are still fundamental to the effective running of the organisation. The previous section 22 report touched on the role of the HR committee and highlighted governance as it related to the award of performance-related bonuses. Today's report also touches on the completion of settlement agreements without the visibility of effective governance in relation to the HR committee. Those areas are to be addressed. Whether that means more input, better papers or more clarity about roles and responsibilities for the HR committee is one factor. On the audit and risk committee, we set out that there were deficiencies in internal control in the yard in 2023-24 and an internal audit programme was not completed.

Of the risks that the internal auditors highlighted over the course of the year, there were 10 high-risk recommendations and 19 medium-risk recommendations. Undoubtedly, there is work for a board and its committees to do to get a handle on these issues.

I am not disagreeing with you, Mr Beattie. Although on the face of it, it is clear what the organisation is there to do, its governance has not been good enough. Improving that will require either clarity of roles and responsibilities, or more capacity. The report that we are discussing today and John Boyd's annual audit report are clear that it needs a period of close review.

Colin Beattie: Are you satisfied as to the competencies of the board members?

Stephen Boyle: There has been a change of board members, and that has brought in what looks to be an appropriate skill set. However, that judgment is for the chair of the board and the Scottish ministers, through the public appointment process. They need to be satisfied about the skills and competencies of non-executive appointments.

Colin Beattie: Okay. I will leave that subject for the moment.

A few minutes ago, you mentioned settlement agreements and the HR committee's handling of them, and this committee has been interested in such agreements in the past. Are you aware of whether a financial package or settlement agreement was offered to the former chief executive when his contract was terminated?

Stephen Boyle: We can share some detail on that. Some of it is set out in the report. There was a settlement agreement for the former chief executive.

To step back for a second, there were three settlement agreements during the year. Two were for members of management who were not senior managers. Of those three, only one received Scottish Government approval, and that was the one for the former chief executive, which was in respect of payment in lieu of notice.

Colin Beattie: So that was approved by the Scottish Government.

Stephen Boyle: Yes, it was.

Colin Beattie: Okay. Let us move on. We have talked about risk management and governance arrangements. The thing that stands out in the audit report is where you state that there were

"significant delays to the commencement and completion of reviews that were agreed within the 2023/2024 internal audit plan."

In paragraph 19 on page 9 of the report, you say that

"internal audit was unable to complete enough reviews to provide an opinion on the overall risk management, control and governance arrangements".

That is pretty sweeping. Could I get a bit more information on that, to get a better understanding of where the issues arose? Was it a capacity issue in FMPG, an issue with the auditors, or a combination of both? How did that come about?

Stephen Boyle: I will bring in John Boyd in a moment to speak to that latter point and explore why internal audit was not able to complete the review, but, first, I will offer a view.

The internal audit function is a fundamental plank of the assurance and internal control arrangements of any organisation, especially one that spends public money. It is a requirement of the Scottish public finance manual that public bodies have an internal audit service. To go back a few years, the creation of Ferguson Marine (Port Glasgow) as a public body brought internal audit into its arrangements—I think that I am right to say that it had not previously had an internal audit service when it was a private company.

Nonetheless, the firm of auditors set out a programme of work for the year—an annual plan—which was considered by the audit and risk committee. However, it is significant that it was not able to complete that consideration. That means that the committee—and, then, the accountable officer—did not have all the information at its disposal to make a rounded assessment of the adequacy of controls and how well public money was being spent.

As I mentioned a moment ago, in the reviews that the internal auditors were able to complete, it is a matter of significance that they identified 10 high-risk areas and that there were 19 further medium-risk recommendations to be implemented.

Reviews were not completed and the auditors were not able to complete the whole plan. There is a gap in the control environment. As the external auditor, we are concerned about that; I am concerned about it; and I am sure—not to speak on your behalf—that the Public Audit Committee is concerned, having had it brought to your attention today. I am sure that some of the reasons behind it will be about capacity rather than a deliberate attempt to thwart the work of the internal auditors.

10:00

John Boyd: On the internal auditors' ability to complete the work, internal audit was appointed in May 2023. The committee may be aware that the lack of an internal audit function, and its importance in the framework of internal governance and controls, was previously highlighted.

On the reasons for the delays, internal audit itself outlined key challenges in its annual audit report. It was essentially the first year that the organisation had had an internal audit function, so it had been getting up to speed with the presence of an internal audit review.

One of the key challenges was the change in senior management within the organisation. As we outlined, there was a change in key officers, including the chief executive officer and the chief finance officer—two senior positions in the organisation—who would essentially act as sponsors for internal audit. That was one of the reasons for some of the delays affecting the ability to complete the whole audit programme for the year and, ultimately—as the Auditor General outlined—to provide an overall opinion on the internal control and risk environment.

Colin Beattie: You said that internal audit could not do sufficient reviews to give a proper audit opinion. Can you boil that down to a percentage? Did you get half or a quarter of the reviews done, or is it that, across the board, the reviews were not really completed?

John Boyd: Three reviews were completed and reported, covering information technology, risk and payroll. In each of those reviews, the internal auditor concluded that it had limited scope. It is up to the internal auditor to give an opinion on whether they have undertaken sufficient work to provide an independent opinion and assurance to the board. They concluded that they had not undertaken sufficient work within the organisation to enable them to issue such an opinion. That is a matter for internal audit's professional judgment.

Colin Beattie: The report says that it is important that the FMPG management engages with internal audit. The implication is that it is not engaging with internal audit. Is that correct?

Stephen Boyle: I do not think that it is an either/or. We found that they have engaged with internal audit for the reviews that have been undertaken.

As I mention in paragraph 18 of the report, and as John Boyd just referred to,

"Internal audit highlighted that changes in senior management and the loss of key management personnel, as well as a focus on the delivery of vessels,"

have meant that it has not had the time or access to complete the entirety of its programme.

I would expect that, during the current financial year—it is a rolling programme—the planned reviews for 2025-26 would remain or be prioritised; the ones that were not completed would also be done in the current financial year.

Access and capacity issues and the focus on the delivery of the vessels have all restricted internal audit's ability to deliver its agreed programme, which would have been agreed with the audit and risk committee to support the delivery of assurance for FMPG. We expect to see progress and catch-up this year.

Colin Beattie: So the programme was signed off by internal audit, or at least by the audit committee.

Stephen Boyle: By the audit and risk committee. That is how the internal audit works. The board will share a rolling three-year—and sometimes five-year—plan with the audit and risk committee. For the year in question, it will give details of the scope for review and that will be shared with the audit and risk committee, which would have signed it off.

Colin Beattie: I have one final question on the matter. I can understand that for an organisation that had not, in its existing culture, had an internal audit function, there would be difficulties in adjusting to and taking part in that.

Are you satisfied that sufficient progress is being made in order that the 2025-26 internal audit function will deliver what is required?

Stephen Boyle: I will ask John Boyd to pick that up, as he will have some insight into that.

John Boyd: The latest update for the financial year, or the audit year if you like, actually spans the year end. Often, internal audit functions will be reporting right up to June to align with the process for the preparation of financial statements, and to provide assurance for the publication of the accounts.

In the latest update that we had, there was a number of on-going internal audit reviews, so it is difficult for us to form an opinion as to whether the work will be completed this year. However, there has been a clear commitment from Ferguson Marine, and from the audit and risk committee, around the importance of the role of internal audit, and a commitment to complete the work in sufficient time to provide an independent opinion for 2024-25.

Colin Beattie: But is there an indication of sufficient progress being made, and sufficient commitment, to ensure that reviews going forward will be completed?

John Boyd: I would say that, from the latest update, it is quite early in the company's audit year for us to form a judgment as to whether it will complete the reviews. However, I do not have concerns, based on the latest update, that it is not committed to getting the internal audit programme completed.

The Convener: Before I invite Stuart McMillan to put some questions to you, Graham Simpson wants to put to you a very specific question on that area.

Graham Simpson: Mr Boyle, you mentioned that the internal audit had picked up 10 high-risk areas. Can you say what they were, or at least tell us what some of them were?

Stephen Boyle: If we have that detail, we will share it. For completeness, those areas spanned internal audit reviews on risk management, payroll and IT controls. I am not trying necessarily to link that with issues that we have already covered this morning, but in the section 22 report that we are considering today, we touch on deficiencies in some of the human resources governance with regard to settlement agreements. That is perhaps an example that shows that internal audit needs to be taken very seriously by any organisation, especially one that is reporting 10 high-risk recommendations.

The Convener: Okay—thank you for that. I now invite Stuart McMillan to put some questions to you.

Stuart McMillan (Greenock and Inverclyde) (SNP): I have a couple of very brief questions on some issues that came up earlier, to get a bit of clarity. In your main report, which was published in October, at paragraph 25 on page 15, you touch on

"the loss on BAE contracts".

Bearing in mind the earlier questions from Jamie Greene regarding the future and the business plan for the yard, I would assume that there would be further contracts included in that. Can you tell the committee what the financial loss was on the BAE contracts in the past?

Stephen Boyle: I will bring in John Boyd on that. Mr McMillan, can you repeat the paragraph reference?

Stuart McMillan: Sure—it is paragraph 25 on page 15 of the main report.

Stephen Boyle: That is the 2023-24 annual audit report.

Stuart McMillan: Yes.

Stephen Boyle: Thank you.

Stuart McMillan: It is the bullet point at the top on page 15.

Stephen Boyle: Thank you—I will bring in John Boyd to set out a bit of detail.

Earlier in the discussion, I referred to drawing on Ferguson Marine (Port Glasgow)'s annual report and accounts, in which it set out £1.5 million revenue from the three-unit build with BAE Systems. Clearly, the revenue from that transaction is just one side of the balance sheet, in terms of its financial contribution in the round. John Boyd can put that in a wider context for you.

John Boyd: The paragraph that is being referred to essentially explains what the level of capital contribution funding was, where there was a requirement for the Scottish Government to provide funding.

We have included a number of different aspects in our report. The total reported loss for the year made by Ferguson Marine (Commercial) Limited, which is one of the subsidiary companies that BAE activity is going through, was £300,000. That includes aspects of tendering and planning for future work; it is not necessarily just because of the BAE contract ending.

Stuart McMillan: I do not think that that actually answers the question. I am looking for a specific figure with regard to the financial loss that the yard had to deal with because of the work that it undertook for BAE.

Stephen Boyle: We may need to come back to you with the detail on that point. We will look at our papers now, but if we do not have the figure before the end of the session, we can come back to you in writing.

Stuart McMillan: That is fine.

My second brief question is in relation to Colin Beattie's questions on board meetings and governance. The board meets only six times a year. Bearing in mind the challenges that have been well documented by you and others, is six times a year enough for a board to get on top of all the challenges and risks that it faces?

Stephen Boyle: I point to two factors. First, it is for the board and its chair to determine the frequency with which it needs to meet to discharge its responsibilities. The other relevant factor is that governance is not just discharged through the board, which probably speaks to the growth in the committee structure. That point was a feature of the governance review.

It is also a reasonable position to take that the board could consider the specific parts that are required for the delivery of effective governance, whether it is audit control, HR matters or, particularly in this context, health and safety. It is absolutely a topic that should be kept under close review, and it is not one that should just fall into a rhythm, which may or may not be satisfactory. The chair should test regularly in order to be satisfied whether the frequency with which the board is meeting is right, but that is for the board to judge at the moment.

Stuart McMillan: Okay. I am sure that I will have the opportunity to take that point further in the future. Thank you for answering my questions on those areas.

I have some questions about public sector pay policy and exit packages. Colin Beattie asked about the previous chief executive's exit package. As the section 22 report touches on, there were a couple of pay-offs that did not go through the correct procedures.

The report says that, although

"FMPG is not required to comply with public sector pay and conditions",

there is an expectation that it

"will align with the principles of public sector pay policy."

Can you provide further detail on what the implications are if FMPG does not ensure that it is complying with the framework agreement and the relevant sections of the SPFM?

Stephen Boyle: You are right—in paragraph 24 of the report, we say that FMPG is not bound by the requirements of public sector pay policy but that there is an expectation that it will "align" with those. That reference is generic and slightly vague, but it affords FMPG flexibility. This committee and other committees have heard about the yard's need to secure sometimes high-cost, specialist skills in leadership positions, which has been a challenge. The need to address that is reflected in the framework agreement that you mentioned, which gives the yard flexibility.

On the implications of FMPG not complying with public sector pay policy, ultimately, the circumstances that are set out mean that it does not have to comply with that, so what would happen if it does not reference public sector pay is a bit of a moot point.

The more serious point that we set out in the report is that settlement agreements were entered into without the approval that is required by the Scottish public finance manual. Ultimately, it is for the Scottish Government, as the shareholder, to take a view on the significance of that.

10:15

The committee will be familiar with the situation from its consideration of other public bodies' settlement agreements. We again have an example of the Scottish Government not giving either prospective or retrospective approval. If I may put it in such terms, that is an indication of the dim view that the Scottish Government has taken of the process that was followed in the awarding of settlement agreements. The governance process was not appropriately followed and, as we set out in paragraph 28, FMPG did not have appropriate documentation either. Those are all indications of poor processes, poor governance and decisions not being taken properly. It will be for the Scottish Government to express a view on what it made of that.

Stuart McMillan: Did Ferguson's seek approval from the Scottish Government?

Stephen Boyle: John Boyd can clarify that. However, as we set out, the fact that the Scottish Government did not provide retrospective approval is an indication that such approval was sought.

Stuart McMillan: The threshold for settlement payments is £95,000. You have said today and in the report that there has been significant turnover of senior staff. As you are aware, I am the constituency MSP. I grew up in Port Glasgow and I still live in Inverclyde. I know a lot of folk who work at the yard and I hear a lot of different things from various people there. For some time, I have consistently heard that there is a revolving door of people coming and going, which chimes with what you have said today. I have heard examples of people coming into Ferguson's for maybe two or three months and then leaving with a package. I assume that those packages were payments of less than £95,000. However, I assure you that it is greatly frustrating for the workforce who have been there for many years to see people coming and going and leaving with fairly hefty settlements because their time in the yard has not worked out.

Have you seen information on how many people have come and gone with settlement payments that were under the £95,000 threshold? Can you indicate the annual total quantum of those settlements?

Stephen Boyle: I will comment on that first and then John Boyd can provide more detail. The circumstances that you outline are largely reflected in the disclosures that the yard has made in its annual accounts. For example, it has disclosed that there is a turnover rate of 22 per cent and that there were 21 exit packages during the financial year at a cost of £440,000. That is perhaps illustrative of a significant volume of change of personnel. It maybe also speaks to the point that we have discussed this morning about access to the right people, the change of senior leadership for internal audit and other factors.

Given that this is the only nationalised shipyard that we audit, I cannot say whether that position is comparable and reflects an industry standard. However, it is a sufficient indication that there is a volume of change happening at the yard. The underlying reasons for the change will be varied, but the information probably supports the insight that you have gained from your local presence.

John Boyd: I understand that 10 of the 21 individuals who exited in year did so due to ill health. As you would expect, given the nature of the industry, the organisation provides regular health assessments and has minimum health criteria, so there is a degree of in-year turnover. As auditors, we make a year-on-year comparison. In the previous year, seven individuals left, which is a significantly lower number. The year 2023-24 saw quite a high number of exit packages, which we have not observed at Ferguson Marine in the past.

Stuart McMillan: I probably know the answer to my next question. In undertaking your audit work, you will be in the office at the yard to look at the facts and figures and at the information that is presented. Do you ever go to talk to the folk on the shop floor to gain knowledge and understanding from them, too?

John Boyd: As part of our on-site audit visit, we undertook a tour of the vessel that was under development, which was in the yard at the time. As part of that visit, the audit team interacted with staff. Generally, our focus is predominantly on the finance team, payroll personnel and those who are involved in governance.

Stephen Boyle: You will see from the annual report and accounts the various parts of what John Boyd and his team do and what the audit covers. They are specifically required to look in detail at the staff disclosures, which means the exit packages, the remuneration of senior officers and the governance arrangements. However, in totality, auditors are required to understand the business. Our work is framed by auditing standards, and that understanding is one of the central elements. This goes back to the deputy convener's earlier point. It is not just a straight flow-through. We cannot be confident in giving an opinion without making an independent assessment and judgment in order to meet the requirements that we are held to.

Stuart McMillan: That is helpful. We have discussed the requirements of the Scottish public finance manual, the £95,000 threshold and the internal mechanisms at the yard. Were the settlement agreements for the 21 individuals who left in 2023-24 all signed off by the board or would that have been an operational matter?

John Boyd: As we report in the annual audit report, there was not visibility through the remuneration committee in relation to the sign-off of those agreements.

Stephen Boyle: We make quite a stark judgment on that in paragraph 28 of our report, where we say that there was an absence of compliance with the Scottish public finance manual, that appropriate documentation was not held and that there was not the visibility that we would expect through proper governance channels. More typically, the packages would be dealt with through the HR remuneration committee. However, it is a significant weakness that exit packages for senior officers were not visible in governance terms, especially where exit packages and the resultant settlement agreements were in excess of the £95,000 threshold.

Stuart McMillan: Clearly, you will know the quantum for each of the two packages that the Scottish Government did not provide the guarantee for. Can you share that information with the committee?

Stephen Boyle: I ask John Boyd to answer that if we have that detail.

John Boyd: One of the packages was £96,000, which is slightly above the threshold, and I think that the other one was £106,000.

Stuart McMillan: Okay. I will not proceed further on those questions, convener.

The Convener: Thank you. I want to pick up on a couple of points relating to Stuart McMillan's questions to you. Back on 1 June 2023, Mr Miller, the chair of the board of FMPG, had an exchange with the committee in which we asked him about the performance bonuses that seemed to prevail at the time, particularly among the senior management team. He said that they were not performance bonuses but retention payments. I suppose that there are two ways of looking at that. Is it the case that there is no longer a retention payments regime so people are leaving the business en bloc, or does some kind of performance bonus system still exist that applies to members of the senior management team at FMPG?

Stephen Boyle: I ask John Boyd to set out the disclosures in the remuneration report and also the annual report and accounts. However, I recall the exchange that took place between the committee and the chair.

John Boyd: We followed up the recommendation as part of our annual audit report, and that is included in the appendices. During the year, as part of a review following the audit findings and the section 22 report, we reviewed the incentives package for senior personnel. We found that there is no longer a bonus payment or retention payment scheme at the yard.

The Convener: Auditor General, would you like to add to that?

Stephen Boyle: Just for completeness, convener, that is reflected in the remuneration and staff report on page 13 of Ferguson Marine's accounts. The last retention payment was made to the former chief executive in the 2022-23 financial year. There are no disclosures of retention payments in this year's accounts.

The Convener: Okay. Thanks for clearing that up.

I want to go back to the cases involving settlement agreements. You said that there had been three that were above the threshold and two had not been approved. The Scottish Government had clearly taken a dim view of those, and indeed

"has not provided retrospective approval".

Can I take you to the case that it did approve? In paragraph 14 of your section 22 report, you say that the former chief executive's employment was terminated "citing unsatisfactory performance". However, paragraph 14 of the Scottish public finance manual says quite clearly that

"Settlement Agreements should not be used to deal with poor performance",

so why would the Scottish Government approve such a settlement?

Stephen Boyle: Convener, you are right that both of those things are the case. For clarity, it was the board rather than Audit Scotland that cited poor performance on the part of the former chief executive. The board took that decision, having engaged with the Scottish Government and received approval for the settlement. We have not seen the circumstances of the settlement request that was put to the Scottish Government, or the detail of it. However, I agree that those appear to be contradictory statements.

What we draw attention to, and where we make a comparison, is that, in addition, process was followed in respect of the termination of the former chief executive's employment, in contrast to the circumstances of the two other settlement agreements that were entered into.

The Convener: I accept that process was followed, but the Scottish public finance manual has a certain status, does it not? The situation is probably a reflection on previous inquiries, including those that this committee has conducted, into situations where people have performed badly and, to use a colloquialism, have been rewarded for bad behaviour. They have walked out of a public sector organisation with a large amount of public money by way of a settlement agreement when, in most objective observers' eyes, they should not have received some kind of reward but should have left with no extra payments other than those that they were contractually due.

Stephen Boyle: I think that those are the circumstances that we have here. They were contractual payments in lieu of notice rather than additional payments to facilitate someone's exit. That is our understanding, convener—that the payment reflects a payment in lieu of notice.

The Convener: Okay. Do we know whether a non-disclosure agreement was attached to it?

10:30

Stephen Boyle: The yard would need to confirm that. What I can say is that non-disclosure agreements have been a feature across the range of exit packages. The yard's understanding—John Boyd can confirm this—is that non-disclosure agreements have been used because of the competitive, commercial nature of some of the activities. However, the committee will be familiar with the fact that such agreements should be used only sparingly and where appropriate, rather than there being a presumption that they will be included in any departure arrangements.

The Convener: Absolutely.

One of the things that stands out in the report is the case of somebody who was brought in from CMAL on a secondment basis. According to your description of it, they were originally engaged on secondment on a contract with a salary of £36,000 a year, which was then uplifted to £54,000 a year. Instead of being paid as a salary payment, the money was paid into a limited company, of which the employee was the sole director. That is quite extraordinary, is it not?

Stephen Boyle: There is no doubt that those circumstances are very unusual. As is clear from what you quoted from the report, that situation is illustrative of a breakdown of controls and approval processes within FMPG, because the level of governance was insufficient to support such a decision. In mitigation, awareness of the situation came about through the work of the accountable officer. On taking on that designation, he initiated a review into the contractual payments that the yard was making, which highlighted how deficient the arrangement was.

I will make an additional point about the numbers that you have quoted. When a person is operating through their own company, HM Revenue and Customs requires the paying body to be satisfied with the off-payroll arrangements, including whether they are a proxy for payroll and the resultant tax arrangements. In this case, that led to FMPG having to pay HMRC £48,000 for pay as you earn and national insurance payments that had not been made.

It should be pointed out that FMPG was proactive: it quickly engaged with HMRC, made the necessary disclosures and thus avoided any penalties. However, the fact that such arrangements were allowed to be put in place reflects the existence of a poor set of circumstances and highlights FMPG's poor controls and governance processes.

The Convener: To recap the figures involved, the person was originally engaged on a salary of £36,000, which then rose to £54,000. However, what the report documents is that, in the period from February 2023 to March 2024, FMPG was invoiced by the individual's company for £144,000. That is quite a leap in payment, is it not?

Stephen Boyle: Yes, the growth in payments from £36,000 to £54,000 and then to £144,000 is somewhat exponential. John Boyd can give a bit more detail on that. We are satisfied that there was an increase in the time commitments that FMPG expected of the secondee, but the growth in payments is absolutely stark. I am concerned that those circumstances were allowed to materialise without there being proper checks, balances and controls.

The yard wants to make it clear that it has arrangements in place to avoid any repeat of that situation. We have seen plans for improved controls, segregation of duties and necessary approvals so that that cannot happen again.

John Boyd can set out the detail behind what took place.

John Boyd: First, it is worth clarifying that the sum of £36,000 was for the salary, which excluded national insurance and tax contributions. Therefore, the day rate that was set under the contract factored in those additional costs that it would be the responsibility of the employing body to cover.

Another contributing factor to the significant increase in the total cost, as the Auditor General alluded to, was the increased number of days that were covered. At the completion stage, the individual involved was entitled to significant annual leave from their employing body, CMAL, and an agreement was reached that the individual would, in essence, work those days at FMPG at the increased day rate. Therefore, the volume of activity that the individual was involved in and the number of days that were recharged increased significantly.

The Convener: If the individual was seconded from CMAL, I presume that CMAL was party to those agreements.

John Boyd: Convener, you might have seen the evidence that the chief executive of CMAL gave to the Net Zero, Energy and Transport Committee last week—

The Convener: Mr Hobbs.

Stephen Boyle: Indeed. CMAL was party to the initial secondment. However, through John Boyd's audit work, I am clear that CMAL was not sighted on the totality of the arrangements, and Mr Hobbs described it as an "odd" set of circumstances. Therefore, I am not clear that CMAL was aware of all the arrangements, particularly the move from a secondment to an arrangement with the private company of the individual concerned.

The Convener: I want to be clear about what Mr Boyd said. He said that the original £36,000 was the net salary figure. We are looking at the other figures. I presume that the invoice for £144,000 did not take account of the fact that there was going to be a tax liability of £48,000.

Stephen Boyle: You are right that that was in addition to the sum of £144,000. When FMPG engaged with the company payment arrangements, its position—at the time, although this has since been rectified—was that payroll tax arrangements were a matter for that company as a supplier. However, it failed to take account of the IR35 regulations, which mean that, when an arrangement looks like an off-payroll arrangement, the paying company must make a more rounded assessment of whether that is actually akin to a situation in which someone should be on the payroll and, therefore, paying tax.

For absolute clarity, the sum of £48,000 for underpayment of tax was in addition to the sum of £144,000.

The Convener: A framework agreement has been put in place between the Scottish Government and FMPG in an effort to clear up some of these matters and to ensure that we have good governance arrangements. One part of the framework agreement is headed "Staff Management", and bullet point number 1 is:

"the recruitment of its staff"—

that is, FMPG's staff—

"is based on fair and open competition and equal opportunities".

The case that we have just been discussing is not likely to pass that test, is it?

Stephen Boyle: I will perhaps not express a direct judgment on that, because my understanding is that the arrangement related to specialist skills that FMPG required to access. I do not know whether that would allow it some flexibility or mitigation. However, that does not detract from the overall principle that is set out in the framework agreement and which, of course, any public body would be bound by—namely, that it must follow proper recruitment, selection and employment practices.

The Convener: We might pose those questions to the Scottish Government and to FMPG representatives.

The framework agreement sets out portfolio accountable officer responsibilities. This goes to the point about governance arrangements that you have been addressing for much of this morning. The portfolio accountable officer in the Scottish Government is the director general economy. The framework agreement says that the company must

"conform to the requirements both of propriety and of good financial management."

Do you have any reflections on whether those criteria have been met, and to what degree there is an element of responsibility for the accountable officer in the Scottish Government?

Stephen Boyle: There are enough examples in today's section 22 report and the annual audit report to show that there were deficiencies in governance and internal control, especially in relation to the management of the settlement agreements. Those will have to have been reflected on by the portfolio accountable officer—who, as you rightly say, is the director general economy—in his submission to the principal accountable officer at the Scottish Government, the permanent secretary, for completion.

You are right: it is a matter for the director general economy to express his view on the circumstances. However, there is enough evidence in the reports that it is relatively clear that there were deficiencies in those areas, which ought to warrant the attention of the director general economy.

The Convener: Thank you. Graham Simpson and Stuart McMillan have a final few short questions.

Graham Simpson: Thank you, convener—my question follows on from some of your earlier questions.

Auditor General, from reading your report and hearing the evidence today, in which we have heard about big payments being made without permission, it seems to me that the situation at FMPG has a bit of a Water Industry Commission for Scotland feel to it. You know about the work that we have been doing on money that was being spent without approval at WICS.

The convener asked about the case of the secondee who ultimately set up a limited company. That fact was discovered by the accountable officer. Was it discovered before the previous chief executive was sacked?

Stephen Boyle: John Boyd can give an insight into the timeline of those events. You are right that they were discovered on review by the new accountable officer; I am not quite sure how the timelines overlap or marry up. I suspect that the yard will be able to give the committee that level of detail on which events took place when.

I will pass the question to John to give you the clarity that you are looking for.

John Boyd: When the review was initiated, it was originally a review of underlying contracts. At that time, the director of finance was relatively new to the organisation and he wanted to understand where the organisation was spending its money and what its contractual commitments were. As part of that review, he identified the contract with the secondee, and he undertook an investigation. That work was undertaken between March and April 2024, and the final report was concluded in April 2024. The new accountable officer then concluded the findings from that investigation.

Graham Simpson: I cannot remember when David Tydeman was fired. To save me looking it up, was that before or after the report was concluded?

John Boyd: It was during March that David Tydeman left the organisation. The review was undertaken during March. I cannot give an exact date for when the review was initiated, but the formal report was not concluded until April.

Graham Simpson: Was it Mr Tydeman who approved the arrangement?

John Boyd: Yes.

Stephen Boyle: Yes, that is my understanding.

Graham Simpson: Was it also Mr Tydeman who approved the other payments that were above the £95,000 threshold, which the Scottish Government has not given approval for?

John Boyd: One of the payments was approved by the former accountable officer, and the other was approved by the former interim director of finance.

Graham Simpson: So it was not Mr Tydeman.

John Boyd: No, it was not Mr Tydeman.

Graham Simpson: So those two payments were approved by different people.

John Boyd: One was approved by Mr Tydeman, and one was approved by the former—

Graham Simpson: So one was approved by Mr Tydeman.

John Boyd: Yes.

Graham Simpson: Right—and one was approved by somebody else.

John Boyd: Yes.

10:45

Graham Simpson: Okay. Do you think that there is any connection between those discoveries and Mr Tydeman being asked to leave the organisation?

Stephen Boyle: I would rather not speculate without absolute clarity on the timeline. It would be for the board to provide the committee with any further detail that it can share about the circumstances that allowed it to publicly state its dissatisfaction with Mr Tydeman's performance and which led to his departure from the organisation. That is how we arrived at our position on that.

Graham Simpson: Those are obvious questions to ask, but we are still not clear. I guess that if board members appear before us, the committee can ask them what the poor performance consisted of. However, you are saying that you do not know.

Stephen Boyle: Again, the detail is a matter for the board. I think that the business plan and future projections and viabilities were factors in its consideration. However, beyond that, our understanding is that those are matters for the board to go into.

Graham Simpson: Okay. Thank you.

The Convener: Stuart McMillan has the final question.

Stuart McMillan: It is about contractors—not so much the individuals concerned, but the subcontractor organisations. Did the chief financial officer's review that we have just discussed include the subcontracts for the various suppliers that came in to do work?

John Boyd: Yes. The aim of the review was to understand where the contracts were and what spend the organisation was undertaking. As the committee might imagine, the majority of the contracts that Ferguson Marine has in place are with large-scale suppliers. However, there was one contract that was unusual. On further investigation, Ferguson Marine identified the underlying scenario and took action to address it.

Stuart McMillan: Are you content with the work that has been undertaken in that regard, and in particular that on the larger contract organisations?

John Boyd: As the committee might imagine, as part of our review, we examined the work that was undertaken by the accountable officer to ensure that there were no other such circumstances and potential risks. We are comfortable with the completeness of the work that was undertaken.

Stuart McMillan: Okay. Thank you.

The Convener: I thank all our witnesses for their evidence.

Before we move into private session, I remind everyone that this is our final Thursday morning meeting. We will switch to Wednesday morning meetings from next week onwards.

10:48

Meeting continued in private until 11:15.

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