# FINANCE COMMITTEE

Tuesday 13 May 2008

Session 3

£5.00

Produced and published in Scotland on behalf of the Scottish Parliamentary Corporate Body by RR Donnelley.

# CONTENTS

## Tuesday 13 May 2008



## FINANCE COMMITTEE
**13th Meeting 2008, Session 3**

**CONVENER**

*Andrew Welsh (Angus) (SNP)

**DEPUTY CONVENER**

*Elaine Murray (Dumfries) (Lab)

**COMMITTEE MEMBERS**

*Derek Brownlee (South of Scotland) (Con)
*Joe FitzPatrick (Dundee West) (SNP)
*James Kelly (Glasgow Rutherglen) (Lab)
Liam McArthur (Orkney) (LD)
*Tom McCabe (Hamilton South) (Lab)
Alex Neil (Central Scotland) (SNP)

**COMMITTEE SUBSTITUTES**

*Roseanna Cunningham (Perth) (SNP)
Ross Finnie (West of Scotland) (LD)
Murdo Fraser (Mid Scotland and Fife) (Con)
Peter Peacock (Highlands and Islands) (Lab)

*attended

**THE FOLLOWING GAVE EVIDENCE:**

Jon Ford (British Medical Association)
John Swinney (Cabinet Secretary for Finance and Sustainable Growth)
Dave Watson (Unison)
Ken Wimbor (Educational Institute of Scotland)

**CLERK TO THE COMMITTEE**

Susan Duffy

**SENIOR ASSISTANT CLERK**

Mark Brough

**ASSISTANT CLERK**

Allan Campbell

**LOCATION**

Committee Room 6

# Scottish Parliament

## Finance Committee

*Tuesday 13 May 2008*

[THE CONVENER *opened the meeting at 14:00*]

## Efficient Government Programme

**The Convener (Andrew Welsh):** Good afternoon and welcome to the 13th meeting in 2008 of the Finance Committee in the third session of the Scottish Parliament. I ask members, witnesses and the public to turn off their mobile phones and pagers. We have apologies from Liam McArthur and Alex Neil. I welcome Roseanna Cunningham, who is here as the committee substitute for the Scottish National Party.

Agenda item 1 is to take evidence on the Scottish Government's efficient government programme. I welcome John Swinney, the Cabinet Secretary for Finance and Sustainable Growth; Craig Russell, head of efficient government delivery in the Scottish Government; and Fiona Montgomery. We also have with us David Bell, who is our budget adviser.

The previous Finance Committee took a keen interest in the Scottish Executive's efficient government initiative and we agreed to continue the practice of taking evidence on it at appropriate junctures. We signalled in our report on the 2008-09 draft budget that we wanted to take evidence on the Scottish Government's efficiency programme once detailed plans were produced. The plans were produced in April, so we invited the cabinet secretary to be with us today to consider the efficiency programme in more detail. I invite the cabinet secretary to make an opening statement.

**The Cabinet Secretary for Finance and Sustainable Growth (John Swinney):** Thank you, convener. I will make a brief opening statement. The committee will be familiar with the Government's determination to pursue a programme of continuous improvement in the delivery of our public services, which involves a sustained approach to efficient government. By ensuring that the public sector is as efficient as possible, we will deliver savings that will be reinvested to make a real difference to people's lives in Scotland. We have therefore set a target for the Scottish public sector to deliver incremental, cash-releasing efficiencies of 2 per cent each year, applied to a baseline of the 2007-08 departmental expenditure limit budget, which will give rise to savings of £1.6 billion in 2010-11. That is a challenging but essential target, given the tight financial settlement from the United Kingdom Government.

The efficiency programme is about enhancing value for money, improving public service delivery and raising productivity. The first set of efficiency delivery plans, setting out where we expect to make the required efficiency gains for 2008-09, were published on 15 April 2008. As promised in my response to the committee on 29 January 2008 in relation to the draft budget, copies of the plans were sent to committee members at that time.

The efficiency delivery plans confirm that public sector bodies have identified potential savings in 2008-09 of £601 million, against a target of £534 million. The extra savings were found by the public sector itself identifying ways in which to increase efficiency. I welcome the commitment that public sector bodies have demonstrated to being as efficient as possible. My officials continue to work with colleagues across the public sector to identify further efficiencies, to ensure that those that are identified are robust and to monitor their delivery. Further iterations of efficiency delivery plans will be published at the end of this month and in September. I confirm to the committee that the outturn report, setting out what has been achieved in the 2005 to 2008 programme, will be published in October 2008.

**The Convener:** Thank you.

Are there contingency plans, should efficiency targets not be achieved? How will the Government ensure that they are delivered? What sanctions are in place for areas of the public sector that do not deliver on their efficiency targets?

**John Swinney:** I will address those three points. First, the Government is clear that its plans must be delivered. There is no element of the plans that cannot be delivered, as they are an integral part of the decisions that we have taken on the spending review and of our approach to improving the efficiency of public sector service delivery in Scotland. In all the guidance and direction that ministers provide to Government departments and relevant agencies, it is implicit that our plans must be implemented.

The team that Mr Russell leads has responsibility for undertaking regular monitoring of all programmes throughout the Scottish Government. Annual reporting will take place in each of the three years of the forward programme. As the previous Administration undertook to do, we will publish annual reports that substantiate the efficiency gains.

Your question about sanctions is the flip side of your first question, which was about whether we expect efficiency savings to be made. We require those savings to be made. Our approach, which is that there is no part of the public sector that cannot address the efficient government agenda, is supported and reinforced by the actions and interventions of ministers and senior officials who are responsible for management of the programme.

As members will see from the detail of the efficient government programme, we specify the accountable officers who are responsible for the delivery of particular efficiency savings. Invariably, they are senior Scottish Government officials. A portfolio manager in Mr Russell's team will examine carefully each of the savings, and defined project managers in the relevant organisations are responsible for progressing the heart of the efficient government proposals.

**The Convener:** On a positive and linked note, how can incentives be built into the system to encourage greater efficiency?

**John Swinney:** Essentially, the process is about encouraging in the public sector the mindset of looking for more efficient and sustainable ways of delivering public services. We are motivating people who deliver our public services by encouraging them to look for more efficient ways of delivering those services. There have been excellent examples of how that has been done, which we want to encourage across the public sector.

As regards incentives, the organisations concerned have the opportunity to deploy resources in different ways to meet different priorities. That is an integral part of a system that has been designed to encourage a mindset that is about delivering continuous improvement in public service delivery.

**Roseanna Cunningham (Perth) (SNP):** I apologise if my question covers an issue that has already been dealt with by the committee. Efficiencies are sought across the public sector, with one big exception: Scottish Water. I am sure that there is a good reason why Scottish Water appears to be excluded from the efficiency process, but it would be interesting to hear what it is.

**John Swinney:** Far from being excluded from the process, Scottish Water's efficiency savings are captured by the approach to pricing that the Water Industry Commission for Scotland takes. As part of the financial arrangements for charging customers, the financial health of the organisation and its investment programme, the WIC specifies what efficiency savings it requires Scottish Water to make. As the Cabinet Secretary for Finance and Sustainable Growth, I cannot specify Scottish Water's efficiency programme. It is specified by the WIC and, essentially, it is captured in the envelope of Scottish Water's pricing and investment strategy.

**Roseanna Cunningham:** Does the WIC specify along the same lines as you do for the rest of the public sector, or is it left entirely to the WIC?

**John Swinney:** If my memory serves me right, the WIC is pursuing a more aggressive stance than we are and has done so for a considerable time.

**Derek Brownlee (South of Scotland) (Con):** If my memory serves me correctly, you have increased the target beyond the one that you said you would set before you came into government. What drove you to the conclusion that a target of 2 per cent rather than 1.5 per cent is credible and achievable?

**John Swinney:** We were driven to undertake the move from 1.5 per cent to 2 per cent by the nature of the financial settlement, which created an imperative to increase the pace of public sector efficiency by that factor. In my view, the target remains credible. The track record over the past few years suggests that, in the broadest sense, an annual efficiency saving of about 1.5 per cent was delivered by the previous Administration. Given that that has been achieved and that a climate and culture of the continuous pursuit of efficiency is beginning to develop, we take the view that gains beyond 1.5 per cent are credible and deliverable. We have therefore settled on the figure of 2 per cent.

**Derek Brownlee:** Is there scope to go beyond 2 per cent?

**John Swinney:** The first reporting of identified efficiency savings suggests that some organisations have gone beyond that and have levels of achievement that exceed 2 per cent, so we are looking at reported plans that look much closer to the achievement of savings of £600 million than the £534 million that would be achieved by efficiency savings of 2 per cent. There is clearly scope for that process and you will understand that the Government will not complain about organisations delivering greater performance on efficiency than we envisage.

**Derek Brownlee:** I understand that you would not complain about it, as it would be a nice problem to confront. However, from an institutional perspective—this ties in with the convener's point about incentives—if the perspective within an organisation is that a saving that equates to 2.5 per cent might be deliverable, is it not more likely that, knowing that the Government's 2 per cent target will be applied year after year, the organisation will manage savings so that it meets the target year after year, rather than being more ambitious in year 1 and running the risk that it might not meet the target in subsequent years? Is one issue not how you incentivise the people who have to deliver the targets to ensure that they can be more ambitious if the opportunity exists?

**John Swinney:** I am certainly willing to consider further how we might incentivise organisations to exceed the minimum level of efficiency savings that the Government envisages. I would be happy to consider that and report back to the committee on how we might achieve that. This is not only an exercise in numbers; it is about a mindset that focuses on improving the efficiency of public services. When I look at much of the available information on the reconfiguration of public services, I am struck by the examples that are emerging of how local authorities and other public sector organisations, through being encouraged to work together on single outcome agreements, are identifying ways in which they can deliver services more effectively at a local level. Essentially, they are putting on the table the service design that is deployed by a range of organisations and we are finding duplication and overlap. We want to encourage public servants to make the process meaningful by leveraging out resources that can be deployed on other priorities.

14:15

**Elaine Murray (Dumfries) (Lab):** I am sure that the cabinet secretary remembers the discussions that we had in the past about local authorities not being treated in the same way as departments of the Executive. Will all portfolios be allowed to keep their efficiencies? Will they make decisions about how those efficiencies will be redeployed?

**John Swinney:** As I have made clear on a number of occasions, within the arrangements that we have arrived at, local government is being allowed to retain all its efficiency savings. In terms of the overall financial calculations that I have made about the budgets that are relevant and required for individual areas, certain elements of efficiency savings will be deducted at source. Efficiency savings beyond 2 per cent should be retained by the organisations concerned. Obviously, that has an element of the incentivisation that the convener and Mr Brownlee were looking for.

**Elaine Murray:** But the other portfolios will not be retaining their efficiencies. Or will they be retaining part of their savings?

**John Swinney:** Some parts of the efficiency savings have been deducted at source as part of the overall calculations of budgets, but we have taken the view that local authorities should retain their efficiency savings. Any performance in excess of 2 per cent should certainly be retained by the organisations concerned.

**Elaine Murray:** In the reporting of efficiencies, will it be reported how much other portfolios kept and how much went back to the centre?

**John Swinney:** The reporting of efficiencies is based on the baseline of the 2007-08 DEL budget. I am pretty sure that the committee will have the numbers for the breakdown of the financial targets for individual portfolios totalling up to £534.4 million. Clearly, we will report whatever we have got to report on efficiency savings—portfolios will identify that for us. We will report against the target of £534 million. If there is anything in excess of that, it will form part of the reporting into the bargain.

**James Kelly (Glasgow Rutherglen) (Lab):** One of the prime objectives of the Government is economic growth; indeed, it is for economic growth in Scotland to match the United Kingdom level. Obviously, you see efficiency savings as contributing to that policy objective. As the local government budgets have unravelled, it has been suggested in some quarters that what is happening in some cases is cuts as opposed to efficiency savings. If there were cuts, that might undermine the Government's policy objective of efficiency savings contributing to economic growth. If you felt that a local council was making a cut rather than an efficiency, would you act? In addition, what role do you take in monitoring local government?

**John Swinney:** There are a number of points in there. First, there is the status of local authorities, which are self-governing institutions that conduct their own affairs. There are certain circumstances in which I, as a minister, can intervene, but it is more in extremis than Mr Kelly's question implies. My ability to interfere in the affairs of a local authority is, quite appropriately, very limited.

My second point is about how changes in local authority budgets are reported. If a local authority wants to report a cash-releasing saving, the definition of what that constitutes is clear in section 17.1 of the Government's efficiency plans, which says:

> "Cash-releasing efficiencies are achieved by delivering an actual resource efficiency because the organisation or function delivers the same service at a reduced cost which might be demonstrated by delivering the same outcome(s) or output(s) for a reduced input … or delivering a reduced unit cost allowing an increased volume of service for the same cost."

That it is the same service is crucial. The definition of an efficiency saving is a pretty tough one and any reporting has to be consistent with the definition of a cash-releasing efficiency. Those are the factors that we have to look at when reporting to the committee and a wider audience about what constitutes an efficiency saving by a local authority.

**Roseanna Cunningham:** My question follows on from Derek Brownlee's. I notice that non-recurring savings are now to be included in efficiency savings. Will such savings be a realisation of assets through, for example, sales of land and buildings? I do not have a particular concern about it, but it might be seen in some places as quite an easy way to reach the 2 per cent target. It is a finite point because one can realise assets only so far and not everybody will be able to. Will you keep an eye on that, to ensure that you do not get too many efficiency savings through that method rather than efficiencies in administration?

**John Swinney:** A change of criteria is implicit in the programme that we discussed with Audit Scotland, whose view is that we are taking a sustainable and robust approach to include an asset sale, for example, as an efficiency saving. However, such sales can be included only once. If, for example, an authority plans a £10 million efficiency saving in year 1, £20 million in year 2 and £30 million in year 3, it might manage year 1, but it would have one heck of a distance to travel in year 2 to go from zero to £20 million. Realising assets might sort a short-term issue, but the day of reckoning would come very quickly because in year 2 the authority would have to deliver double what it—

**Roseanna Cunningham:** It depends on how many spare assets it has lying around.

**John Swinney:** Yes. Such words of caution are well placed because if the programme is to be delivered as we intend as a sustainable programme to improve the efficiency of public service delivery, measures must have a longer life cycle than just making an impact in one year with no impact in year 2. Obviously, we are looking for a transformational programme that runs through that process.

**Tom McCabe (Hamilton South) (Lab):** I can only agree with you, cabinet secretary, that the use of one-off generations of finance to fund on-going services will ultimately mean a day of reckoning, but that is perhaps further down the line.

I see that time-releasing savings do not form part of the 2 per cent but can be counted for anything in excess of that target. Some people were sceptical about time-releasing savings, but I see that they still play a part in the programme. How do you intend to measure those savings in the future?

**John Swinney:** I agree with Mr McCabe about one-off savings, which are convenient as a one-off, but if a programme is predicated on such savings, it will not be sustainable. Those are wise words of caution that the Government will bear in mind in the monitoring of the programme.

On time-releasing savings, I cannot think who on earth Mr McCabe could be referring to—

**Tom McCabe:** It slips my mind too.

**John Swinney:** I am glad that we are all becoming forgetful as we mature, Mr McCabe. Time-releasing gains can be made. There is a hard element to the Government programme, which is predicated on cash-releasing efficiencies. However, into the bargain, we want to retain the ability to encourage and motivate public servants to make time-releasing savings.

On the tabulation of those time-releasing savings, we want to undertake an element of data capture that will allow us to show how processes have changed to release time. That can best be delivered at programme level within public services to identify what the time-releasing efficiencies have been. We will report on time-releasing savings in a different way from the way in which we have reported the hard information on cash-releasing savings.

We have said in the documents that the time-releasing savings will be defined as measures that allow for the delivery of better services with the same amount of money through making better use of people's time and activities. We are all aware of various elements of our public services in which we have seen some of those benefits come to the fore in the past.

**James Kelly:** In your answer to Roseanna Cunningham, you spoke about the importance of managing assets efficiently. The committee has been interested in asset management in another area of its activity. Of course, asset management is important in making efficiency savings. The guidance note says that asset management plans were due to be submitted for all relevant parts by 30 April 2008. What progress has been made on that?

**John Swinney:** This is an area in which I think there are significant gains to be made. I am thinking not just of one-off disposals of assets. Various elements of the Scottish Government are occupying buildings on a rental basis. We have limited occupancy in one bit, another bit around the corner with limited occupancy and yet another bit further round the corner with limited occupancy. What has horrified me is that there has been a certain reluctance in the past to see that as an issue about which it is fair to take a corporate view. Each organisation might be taking forward its own accommodation strategy regardless of the corporate concern. That is unacceptable.

We have just taken steps on asset management. In central Glasgow, we have the

Atlantic Quay building, which is occupied by Scottish Enterprise; the Meridian Court building, which is occupied by the Scottish Government; and the Europa building, which is occupied by Government officials. We are merging all those functions into the one building at Atlantic Quay. That is sensible asset management. We will reduce the number of locations at which we have people based and, as a consequence, we will generate efficiencies.

We have now turned some important corners in breaking down the unwillingness of organisations to take a corporate view. We have made good progress on the asset management review. We have a much better tabulation of information about what assets we own, what assets we use, and what assets we do not use fully. We are in the process of working our way through the asset management plans to ensure that we have the right approach to the use of those assets. The situation in Glasgow that I cited is a vivid example of how we can secure benefits from the process.

**James Kelly:** My follow-up question is a technical question, so it might be one for the officials. You have a large asset base of £5 billion. I am interested in the accounting methodology that you use. Do you use historical cost accounting or current cost accounting?

14:30

**John Swinney:** In the absence of a volunteer rushing to my aid, I offer to write to the convener and members of the committee on that point.

**The Convener:** That is much appreciated.

**Tom McCabe:** I will continue on the theme of asset management, without mentioning accountancy. Clearly, the management of assets will be very important to your programme. Are you satisfied that in the organisations involved, especially local government, sufficient distinction is made between the compilation of an asset register, which is the number-crunching element, and proper use of assets? Asset registers have not always been professionally compiled. There is more emphasis on that today, but it is important for us to go a step further and to ensure that there is professionalism in the use of assets.

**John Swinney:** Mr McCabe is absolutely right. There are two elements in the process. First, we must have an up-to-date, tabulated register of the assets that are in the ownership or under the control—I stress the difference between ownership and control—of an authority. It is not fair to single out local government. Local government will be part of the debate, but so will non-departmental public bodies, executive agencies and the Scottish Government. Since coming into office, we have applied pressure to ensure that there is clearer tabulation of the assets that are held by the Government and by agencies. As I indicated in my response to Mr Kelly's question, I do not have that locus in local authorities, but we can argue for such tabulation through the best-value process, of which it is an elementary part.

Stage 1 is to tabulate the asset base, including assets that are either in the ownership or under the control of authorities. The next stage is the decisions that flow from that with regard to whether we are securing optimum use of assets. I readily concede that there is bound to be scope for progress and efficiencies to be made as a result of that set of decisions. We cannot take those decisions until we have the information from stage 1. Once that has been put together in the form of an asset register, it would be ridiculous of us not to take decisions on the use of assets.

That brings us on to other ground. For example, is it appropriate for ministers to say to executive agencies or NDPBs that they disapprove of those bodies' locations and that they should be located on a floor of a Government building? What on earth is the point of our occupying only 85 per cent of a building and having 15 per cent spare capacity, when NDPBs down the road are separately incurring facilities management costs, have separate rental streams and so on? That is part of the work on asset management that we have undertaken. What we have done in Glasgow is an example of how we have recognised the advantages of co-location and brought together the Government and NDPBs in order to save resources on a long-term, sustained basis. I have no doubt that there will be many more such examples across central Government, the agency and NDPB sector and local authorities.

**Elaine Murray:** I have a further question on the issue of asset management, which seems to be exercising all members. The guidance that you have made available to us states:

> "It should be noted that accounting rules require capital receipts to be used only for 'expenditure of a capital nature'."

How can that be tracked? If the disposal of assets by portfolios counts towards their efficiencies, but some of those efficiencies have been deducted at source, how can you prove that they have not used capital receipts as revenue to fund service delivery rather than for

> "expenditure of a capital nature",

as they should have done?

**John Swinney:** In essence, that will be done by separate processes. Portfolios will have revenue and capital budgets, and they will be able to secure the authorisation of expenditure only if they have the revenue budget cover for the revenue item or the capital budget cover for the capital item. That is the control of capital and revenue in that one box.

An asset sale may allow portfolios to undertake a greater amount of capital activity, or it could be offered into the central facilities of my finance portfolio to be traded elsewhere in the Government. Although they do not crop up terribly often, there are circumstances in which bodies have more revenue than they require and not enough capital. Invariably, it is the other way round, but there are circumstances in which we can swap some of the capital items or facilities. However, I emphasise that revenue expenditure can be incurred only when there is revenue cover within the portfolio. It is a separate process, but it is absolutely robust in giving the assurance that only revenue cover can be used.

**Elaine Murray:** So it will not be possible to flog off the family silver to pay for services.

**John Swinney:** The finance portfolio will watch that very carefully.

**James Kelly:** As we touched on earlier, monitoring is very important in seeing whether targets have been met. A strategic board will review and report quarterly on performance against targets. Will any other body review and report on a more regular, perhaps monthly, basis?

**John Swinney:** On a daily basis, Craig Russell and his team look at the performance of different portfolios and deal with inquiries from them about the initiatives that they suggest or consider as possible efficiencies. That daily interaction is encouraging. Organisations are thinking along the process of efficiency and are in dialogue with the Government about what is being considered and what qualifies as part of an efficiency programme. That dialogue continues daily.

There is regular reporting of progress on the performance and efficiency programme to me, as the relevant minister. I see that monthly. The report goes formally to the strategic board, which is chaired by the permanent secretary and involves the directors general and other non-executive directors of the strategic board. In essence, they consider over a three-month period whether the performance targets are likely to be delivered. They have operational control. As members will notice, most of the directors general are cited as accountable officers in the programme, so they are immersed in the reporting. They will take decisions on the programme based on whether it is on track at different stages during the year. Obviously, I will keep a close eye on all developments to be assured that an integral part of the Government's agenda is being delivered at that level.

**James Kelly:** As part of the programme, there is a traffic light assessment tool, with green, amber and red lights. Those projects that are red and have fallen more than £5 million outwith the target are flagged up for investigation. What about projects that do not fall within that definition? What will happen if a project has a red light against it but is only £3 million outside the target? How will such exceptions be handled?

**John Swinney:** I would not want the committee to think that we wait for a red or an amber before we take action. Issues are examined regularly to ensure that progress is being made. Given the type of programmes that we deal with, we need to be assured at all times that appropriate progress is being made. I am sure that the committee will readily understand that, if we reach December and we have a collection of reds on the efficiency programme, the likelihood that we will be able to deliver the efficiency savings by the end of the financial year will be slim.

We have been in the current financial year for about six weeks and monitoring of the programmes is already under way. That will ensure that detailed progress emerges so that we can be confident that we can substantiate the efficiency savings that we envisage.

**James Kelly:** To clarify what you said in your previous answer, you expect the lower-level work, whereby things are monitored daily or monthly, to flag up any difficulties so that you can take action to correct them.

**John Swinney:** If an issue reaches a level at which it has to be reported to the strategic board, we will have reached a pretty sorry state of affairs. Many interventions will be made to ensure that programmes are delivering long before we get anywhere near a three-monthly review. If a programme is not performing three months into the financial year, the room for manoeuvre will have reduced by 25 per cent. We must be acutely aware of the demands so that we can guarantee that progress is being made.

**The Convener:** How will the reporting of cash-releasing savings overlap with or relate to the reporting of single outcome agreements with local government?

**John Swinney:** The reporting streams will be distinct. The single outcome agreements will be published and they will be reviewed during the year. They will certainly be reviewed after the end of the year to determine how much progress has been made.

Actions might arise from the formulation of the single outcome agreements. Increasingly, we are finding that the single outcome agreements are emerging from discussion and debate with a variety of public sector providers—health boards, enterprise organisations, local authorities, the police, the fire service and so on. They might throw up efficiencies that can be considered as part of the reporting of efficient government.

There will be two full, but quite distinct, reporting streams.

**James Kelly:** What will be Audit Scotland's role in reviewing progress? How will it report to the Parliament?

**John Swinney:** That is not a question for me to answer. We have been in dialogue with Audit Scotland about the formulation of the programme and we secured its agreement to the changes to the definitions that the previous Administration agreed with Audit Scotland—one change that comes to mind concerns the disposal of assets.

On interrogation of the data, or reporting, I simply say that the Government will facilitate whatever approach Audit Scotland wishes to take. If it wants to undertake a review at the close of the first financial year, or whenever, the Government will of course make information available to assist in the process.

**The Convener:** I thank the cabinet secretary and his departmental officials for their evidence. I wish the department well in its quest for more efficient government.

We will have a short suspension to allow for a changeover of witnesses.

14:44

*Meeting suspended.*

14:55

*On resuming—*

## Methods of Funding Capital Investment Projects Inquiry

**The Convener:** The fifth evidence session in the committee's inquiry is to hear evidence from organisations that represent people who work in key public service facilities that have been procured and funded by different methods. I welcome Jon Ford from the British Medical Association, Dave Watson from Unison, and Ken Wimbor from the Educational Institute of Scotland. I will give each of you an opportunity to make a brief opening statement.

**Jon Ford (British Medical Association):** I am the head of health policy and economic research at the BMA in London. We are a United Kingdom organisation, by which I justify my presence here.

The BMA's hostility to private finance initiatives and public-private partnerships is quite well known. At our annual meetings of representatives, we have passed numerous resolutions opposing the concepts. In this introduction, I do not intend to go into any of the reasons for that opposition—we can perhaps explore the reasons later.

Our members tell us that they prefer public procurement. That said, we have had reason, once PFI facilities have been built, to ask our members what they think of them. They are more ambivalent than the committee might expect. One reason for my being here today is to pass such information on to the committee and to elaborate on it where appropriate.

**Dave Watson (Unison):** As colleagues will know, Unison is a long-standing critic of PFI, largely on the grounds of cost and poor value for money. We believe that PFI undermines the public service ethos and team delivery, and that it is inflexible in delivering services. We are equally sceptical about non-profit-distributing models. They are not non-profit and they retain many of the weaknesses of the PFI model.

It is important that the committee focus on the way ahead. Governments of all colours have attempted to get a free lunch out of capital financing and have come up with various ways of doing so. Each successive Government has tried to achieve that unachievable goal. In our written evidence, we have set out a plan that we believe will ensure that we can deliver capital infrastructure in Scotland much more cost effectively and within the spirit of the public service ethos.

**Ken Wimbor (Educational Institute of Scotland):** I thank the committee for inviting the

EIS to give evidence. In the late 1990s, it was estimated that between £2 billion and £4 billion was required to bring schools up to an acceptable standard. The subsequent concentration on PFI/PPP projects as "the only show in town" led to the neglect of other procurement options.

A significant body of evidence supports the view that PFI/PPP schemes are not the most cost effective. In a survey that was carried out jointly three years ago by the EIS and the Royal Incorporation of Architects in Scotland, only 30 per cent of our members believed that PFI/PPP new schools or refurbished schools delivered value for money.

**The Convener:** A submission from the unions says that PPP/PFI is not good value, and Unison says that the focus should have been on conventional borrowing using the prudential borrowing regime where possible, because that represented better value for money. However, we have heard that the investment required is much greater than could be afforded through conventional borrowing. How do the unions think the problem could be overcome?

**Dave Watson:** As I suggested, there is no way of funding capital infrastructure without cost. If you can afford to pay the unitary charge payments of a PFI scheme, you can afford to pay the prudential borrowing costs through conventional borrowing. As our research has demonstrated, PFI schemes incur billions of pounds of additional costs. The revenue cost of borrowing has to be met, whichever way it is done. Prudential borrowing will work in a way that PFI does not.

**Jon Ford:** That is pretty much the BMA's opinion. The advantages to the Government and the Exchequer of postponing capital investment into an income stream over 30 years or so are obvious because it postpones accountability and so forth, but the sums of money that are involved outweigh the sums that would normally be expected in a conventional up-front approach to capital investment.

At a time when we are talking about stringency in trusts and hospitals, it does not seem sensible to pre-empt income so far down the line. In fact, the advantage of paying up front through a conventional procurement mechanism is that it is hypothecated and does not impact on services later in the timescale. In itself, that is a strength of paying up front, which PFI does not have.

15:00

**Ken Wimbor:** I have nothing much to add, except that I concur with my two colleagues' views and with those that the Scottish Trades Union Congress expressed in its written evidence, which I think members have seen.

**Elaine Murray:** Dave Watson has answered in part the question that I will pose. We have been taking evidence on a number of different models of funding; for example, the Borders railway is to be funded under non-profit-distributing mechanisms. I would like to hear your views on the use of the NPD model in public sector investment.

In addition, there has been a Government consultation on the Scottish futures trust, and we have had evidence that suggests that some of the difficulties could be resolved by its being funded by the private sector. What are your views on that?

**Jon Ford:** To some extent, the NPD model and the Scottish futures trust as it is now envisaged—as opposed to how it was originally envisaged—are little different from the PFI arrangements, because profit will still be taken from income streams. The difference seems to be that there will be less profit at procurement level because the economies of scale mean that it will be possible to drive a harder bargain when borrowing the money. However, I presume that there will be more profit downstream for the contractors, who will obviously take profit from the income streams, as they do under PFI. It seems to us that there is almost just a semantic change from the PFI model, whereas the original Scottish futures trust bond route, which I know is not available for a variety of reasons, seems far more attractive to us and is much more akin to what we would like to be used.

**Dave Watson:** We argue that the NPD model retains the higher borrowing costs of PFI and will still include the extraordinary costs that are attached to risk transfer. We added those up and they total about £3.6 billion in Scotland—the most expensive insurance policy in living history, I should think. Further, the NPD model includes the inflexible contract provisions that are inherent in PFI. Of course, NPD is not non-profit, because the profit is simply taken at contractor level.

On the SFT, we had less difficulty in principle with the original Scottish National Party policy paper of 2006. We concurred with its analysis of the weaknesses of PFI, and we had little difficulty with the idea that the SFT might collect all its funding through bonds, but we were sceptical about whether the SFT could be delivered under devolved powers. Frankly, the new proposal for the SFT bears little relation to the 2006 paper and seems to us to be simply PFI under another heading. We are disappointed by the current consultation document. However, in fairness, it is a broad document, and people would like to see a lot of detail before coming to a conclusion.

**Ken Wimbor:** We felt that the NPD model and the Scottish futures trust as originally envisaged represented a distinct move away from existing procurement through PFI/PPP. However, recent developments suggest to us that there remains a problem regarding borrowing costs and the continuation of private profit.

**Joe FitzPatrick (Dundee West) (SNP):** We have heard a number of times—particularly from people who, I suppose, benefit from the PFI/PPP system—that that model provides more security for asset management for the future. Can you give us some ideas about how we could achieve that security without the PFI/PPP model?

**Dave Watson:** Frankly, good asset management has little to do with who provides the cheque. At the end of the day, good asset management has been a developing learning experience over probably 100 years or more, and practices develop and improve. There is nothing inherent in PFI that could not be developed in the standard model; in fact, there is nothing in it that is not being used in the standard model. The asset management policies of most public authorities and of the Scottish Government have been refined over the years to improve the way in which conventional finance is delivered. The important point is that there is nothing magical about getting money from a bank at great expense that means that assets are managed any better.

**Jon Ford:** There is a presumption that the private sector manages assets better than the public sector, but I do not know whether that is borne out by evidence. It seems to be an article of faith, rather than something that can be argued based on evidence. I agree with Mr Watson on that score.

**Tom McCabe:** I stay in Lanarkshire. My mother died in Hairmyres hospital, which was an appalling place—there were holes in the walls that had been there for years. That did not really suggest to me that the asset was being well managed, and many of the people who passed through it did not think it was well managed. In the light of that, how can Dave Watson support his last statement?

**Dave Watson:** Nobody is against having new buildings. Part of the problem with the argument about PFI over the years is that it has been presented as, "Either you have a new hospital and build it our way or you don't get a new hospital at all." The finance of capital infrastructure has been weighted and biased in favour of one scheme—it has been the only game in town because it is the only scheme for which Governments have given money.

The Hairmyres hospital building has had its problems under PFI but, in fairness, they are not solely because of PFI. Other buildings have problems as well, but the reality is that PFI has not delivered anything that a conventional build would not have delivered. It is a good hospital—that is fine–but it would have been a good hospital had it been built under conventional funding. It would have been a new, bright, shining hospital with all the advantages of a new hospital.

**Tom McCabe:** In the 1970s, a raft of schools were constructed that were, in design terms, a disaster, cost a fortune to maintain and were often poorly maintained, which resulted in children learning in environments that were below the standard that we consider acceptable. With the introduction of PFI, those buildings were replaced at a rate that was previously inconceivable. If PFI produces "nothing magical", why are the new buildings being maintained far better than buildings were under conventional public sector procurement?

I have been a member of this Parliament for nine years and was a council leader for about nine years before that, so I have been involved in a lot of discussion on procurement of schools. I have yet to meet a single one of Mr Wimbor's members who was anything less than enthralled by their new school and the rate of replacement of the schools in their area. That does not square with his approach. Is he representing his members accurately?

**The Convener:** As a former EIS representative, I call Mr Wimbor.

**Ken Wimbor:** I am representing our members accurately. In 2004, we conducted a survey with the Royal Incorporation of Architects in Scotland. Although a number of teachers expressed some pleasure at the new schools that had been built, a significant number of problems were identified, particularly in relation to facilities management, basic maintenance and basic janitation. For example, 30 per cent of our members did not believe that the refurbishment or new school that was delivered represented value for money. I have already made that point, which is provided for in the survey that we conducted in 2004.

**Tom McCabe:** I have known headteachers who retired in frustration at their inability to get a school maintained; for example, to have a piece of broken glass repaired or a leaking roof properly fixed. Did you ask the people who had experienced the previous system how it compared with the system at the moment?

**Ken Wimbor:** I am not for a minute denying that the schools that were built in the 1960s and 1970s now have significant problems or that there are significant problems with maintenance. I am saying that the new schools that have been developed are showing the same problems at a much earlier stage.

**Jon Ford:** To answer the question about ageing infrastructure, Tom McCabe is quite right, of course, that most hospitals that have been replaced by PFI models were woefully undermanaged, but that is because of lack of finance, not because of the method of procurement. When we did qualitative research among some of our members on the state of hospitals post PFI, many said that one reason why they were so happy with what they had got was that they had been waiting 20 years or more for the replacement. We cannot blame that on the procurement method—it was because of the unavailability of funds and the Government's attitude to investing in public infrastructure. Regardless of the method of procurement, that money was never going to come forward.

Now, for the sake of putting the onus of that expenditure on future generations, buildings are coming on stream much more quickly, but had the Government made the proper investment up front at that time over 20 years, it would not have been necessary to do that. We are talking about the desire of Governments to postpone expenditure, whether by doing nothing or by spreading it over 30 or 60 years. The same principles apply. In the case of Hairmyres hospital and some schools, the expenditure was postponed by doing nothing.

**Tom McCabe:** If I take out a mortgage for my house, am I deliberately postponing expenditure or am I facing up to the fact that I do not have £250,000 there and then?

**Jon Ford:** Yes—that is entirely what you are doing. However, if you were spending countless millions more than you would on a conventional mortgage, which is what happens with PFI, that would be a very different question. If you spend hundreds of millions of pounds on something for which the up-front investment would have been only £20 million or so, the order of magnitude is very different from that of a conventional mortgage, which might cost twice the price of the house.

**Dave Watson:** The mortgage analogy is not accurate. It is much more appropriate to conventional finance—it is essentially what conventional finance is. I accept the fact that there has been bad design in conventionally financed buildings; however, there has been bad design in PFI buildings, too. The reality of the funding issue is that the maintenance costs are built into the price of a PFI building. What is needed are new, modern asset-management approaches to conventional finance that build the same maintenance cycle into the funding of conventionally financed buildings. It does not matter where the money comes from: the only differences between PFI buildings and conventionally financed buildings are that PFI buildings cost a lot more and there is a lot less flexibility because the partners are tied into 30-year contracts.

**Elaine Murray:** I disagree with the idea that PFI has been the only show in town—it has not. It has been part of a mix. We have heard that around 85 per cent of public investment is made by traditional methods, through the Public Works Loan Board, prudential borrowing or the sale of assets. PFI has not been the only show in town. In my constituency, five new schools are going to be built by PFI but three are going to be built by conventional methods. It is not the case that the Government has refused to fund in any way other than PFI.

However, we have heard in evidence that around 80 per cent of PPP/PFI projects are delivered to budget and on time, whereas 70 per cent of publicly procured projects are not delivered to budget and on time. If you want to get rid of the option of PPP/PFI, how will you ensure that the traditional methods deliver to budget and on time?

**Jon Ford:** It is right that the PFI model appears to deliver on time and to budget, which is a major plus. Why is the public sector so bad at project management that it does not deliver on time and goes over budget? The same companies are building and designing the structures as under PFI. What is it about public sector procurement that lets building companies and contractors get out of control when they are not allowed to get out of control under the PFI model? It is all about project management.

I do not know what the solution is apart from government buying in the appropriate project management or ensuring that it has better project management. There is no logical reason why a company that is building a hospital under the PFI model should treat the project differently from how it treats a hospital that it is building under the public procurement model. Something goes wrong, which I suspect is to do not with procurement but with the attitude of contractors to the people who commission them.

**Dave Watson:** The figure that Elaine Murray cites was highly disputed. It was produced by a firm of consultants that had—to say the least—a strong bias in favour of PFI.

I agree that there is "nothing magical" about PFI in terms of asset management. In terms of global government spending, Elaine Murray is correct that PFI has not been the only show in town. However, for many public authorities that have been considering purchase of certain buildings—schools, in particular—it has been the only show in town: they were clearly told that if they did not use PFI they would not get funding. What is—laughably—in Scotland called "level playing field funding" was allocated only if the authorities went down the PFI route. In England, the funding was called PFI credits, which is a much more accurate description. It is a subsidy. It cannot be said that there was a genuine choice between the conventional model and PFI when public authorities were told that they would not get funding unless they opted for PFI. In that context, it has been the only show in town.

**Ken Wimbor:** All the new builds and school refurbishments that were covered by our 2004 survey were PPP/PFI projects. The question is about the standard and quality of project management. It is not inherent in the procurement method, whether that is PPP/PFI or more traditional methods.

15:15

**Elaine Murray:** The evidence that we have received so far suggests that a range of options is available, of which PPP/PFI is one. It has been suggested that some methods of funding are more appropriate for some types of projects than for others. Why do you want to take out one model? I am not trying to argue that PPP/PFI is superior for all projects because clearly it is not. Some projects are far better funded by more traditional routes of public procurement. Why should PPP/PFI be removed from the public sector?

**Dave Watson:** Our plan does not say that PPP/PFI should be removed; rather, it says that a level playing field should be created. We have been there—we have done the design and we have been part of the evaluation. If there was a level playing field, most projects would not touch PFI with a barge pole. There would be no subsidy, a proper value-for-money assessment would be done and the project would end up being done using conventional finance.

It is argued that some PPP/PFI schemes are better than others, but the list gets whittled down. Originally, PFI was considered fine for everything. We then had bundling, before the Institute for Public Policy Research told us that PPP/PFI should perhaps not be used for the health service. We are now told that maybe it is appropriate only for very large schemes.

I say one word to the committee: Metronet. Your colleagues at Westminster have a clear view on the matter. Big projects that have been done using PPP/PFI have gone very wrong. Big projects are particularly risky ones on which to use PFI, but the industry does not want the little ones. Once we take out the incentive for public authorities to pick PFI over conventional finance, I am not sure what the market will be for PFI.

**Jon Ford:** I go along with that. When we compare the traditional procurement route and the PFI route, the costs in the public procurement route are heavily influenced by the factor that is attached for cost and time overruns. Obviously, historical precedent is brought to bear on that rather than what might happen in the future. If we were to improve project management, that would not happen. We could take that out of the equation and create a level playing field.

Secondly, as we know, the transfer of risk under PFI never occurred. What has happened is that once the contract was signed and there was the 30-year guarantee, there was refinancing and the risk vanished. In effect, the Government was paying too much for PFI. My objection to PFI is that there is no level playing field and the Government ends up paying more than it should.

**Ken Wimbor:** We are not persuaded that the transfer of risk compensated for the additional costs that have been associated with PPP/PFI projects. To add to the Metronet example, there is an example closer to home. The buyout of the West Lothian College PPP cost the taxpayer in the region of £27.7 million. That is an example of the problems that can occur.

**Joe FitzPatrick:** It is reasonable to assume that most of the panel would support projects being funded by conventional funding whenever possible, and would welcome the announcement about the new hospital in Glasgow, which will be funded that way. However, it is clear from the evidence that we have gathered so far that that will not be possible every time, and that other methods need to be considered. One of the methods that the Government is inclining towards is the non-profit distributing organisation model. Will the panel comment on the fact that the NPDO model appears to reduce the overwhelming equity profits that we see in the PPP model? In using PPP for a hospital you get, in effect, one hospital for the price of two. Maybe it is not the ideal, and you would prefer the conventional route, but is the NPD model much better than the traditional PPP/PFI model?

**Dave Watson:** Equity finance is one of the advantages of the NPD model. However, there are other costs. The committee has heard evidence from other colleagues who are concerned that although you may save a bit on the NPD model, there are costs in other areas. The question you really need to ask is this: why bother? Why create what is essentially PFI lite, with all the inflexibilities and costs of NPD models, when you have another route called prudential borrowing? That route provides the flexibility without the additional costs. Everyone tries to solve the previous problem with finance: the Conservative Government introduces a model, then Labour plugs some of the gaps and now it seems that the new Scottish Government is trying to find another gap to plug. Forget it. Start from scratch and use prudential borrowing. That is our advice.

**The Convener:** Would prudential borrowing address the problem, given its size?

**Dave Watson:** No form of financing can do that. Scotland's ageing infrastructure requires more money than we will be able to provide at any one time. Even if we could provide the money required, it would probably be outwith the capacity of the Scottish construction industry to meet those demands. The industry's capacity is estimated to be about £1 billion a year, almost half of which is taken up by Scottish Water alone, before we mention schools or other projects. The reality is that we do not have the money or capacity to sort out all the problems associated with our ageing infrastructure as quickly as we would like. However, we can decide how to finance what we can do, given the capacity that is available to us. All the evidence demonstrates that conventional finance, using prudential borrowing, is less expensive than the unitary charge and revenue costs of PFI schemes. If we use prudential borrowing for projects, we will know that we can afford them and that it will be within the capacity of the economy to cope with them.

**Derek Brownlee:** We are all wrestling with the issue of how we can format an objective comparison of different financing and procurement methods. Whatever the criticisms that can be made of PPP—we have heard many in the course of the inquiry—it highlights explicitly the total cost of a project. I know that questions have been asked about how transparently that figure is arrived at, but it is accepted that PPP highlights the total cost. Is not part of the problem with conventional public sector financing that the life-cycle costs of a piece of infrastructure and the services that it provides are not transparent or readily available, which makes it difficult to compare financing methods objectively?

**Jon Ford:** You have raised the issue of life-cycle costs. The further down the road we go, the less what we expected to find corresponds to reality. In the public sector, especially the health service, things change rapidly, as we found to our cost when using private finance. Many costs do not emerge until you are too far down the road to do anything about them. For example, the presumption that hospital throughput would be at 85 per cent, or thereabouts, of capacity was stretched almost immediately during the first phase of projects by the national health service plan, and the emphasis on waiting lists meant that the service had to crank through many more operations. At that stage, people did not realise that, under the private finance option, higher throughputs lead to financial penalties, not to mention the higher costs that are associated with doing more operations in infrastructure that is not designed for it because there are not enough beds and so on.

It is not immediately obvious to me that costs are transparent over the entire life cycle of PFI projects, because things change rapidly in the health service. I am not an expert on schools, but I suspect that the same is true there. In my experience, things seem to change rapidly in education these days. [*Interruption.*]

**The Convener:** You are being heckled by a mobile phone. I ask the person to whom it belongs to turn it off.

**Joe FitzPatrick:** It is off.

**The Convener:** We have found the culprit. I am sorry for interrupting you.

**Jon Ford:** The transparency of the entire cost cycle cannot be apparent from the outset. The evidence from our members on the ground seems to be that the public procurement route is more flexible, given the changes to which I have referred, than an arrangement that locks us in for 30-odd years.

**Dave Watson:** The one thing that PFI is not is transparent. For a long time, my staff have been trying under the freedom of information regime to get contracts out of the previous and the current Scottish Government. Every method possible has been used to try to prevent us from getting the documentation—in some cases, the last-ditch defence was that the Government did not have it. The total cost of PFI projects is not transparent. During a 30-year contract, a lot of variation orders can be placed by contractors. That is linked to the issue of life-cycle costs. I accept that a figure for life-cycle maintenance costs is provided at the beginning of PFI schemes, but we must recognise that few public buildings will look the same or be subject to the same demands in 30 years' time, let alone 60 years' time, which is the length of some schemes.

Hospitals provide a good example of that. If we had sat down 10 or 15 years ago to design a hospital, would we have anticipated the degree of day surgery that is done today? The design and bed complement of hospitals are entirely different today. Given such change, it is difficult to achieve flexibility. Without recourse, we are over a barrel in negotiations with the company that owns the hospital.

**Ken Wimbor:** Commercial confidentiality is often given as a reason for not providing information about projects. That results in a lack of transparency about existing PPP schemes that has become evident to us.

**Derek Brownlee:** The health service provides a good example—we all accept that priorities change and that clinical advances affect services. I am sure that that applies to other parts of the public sector, too. However, some such changes would happen anyway and, under conventional public financing, the cost of changing to prioritise waiting lists rather than another aspect, for example, is not as explicit. Is not one issue that no one can say what the cost to the health service of doing X is, whether under private or public finance?

The service changes over time and the reality is that the problems under PPP concern how a project has been contracted rather than the fact that it is contracted. Even in a public setting, if a hospital is built on an incorrect assumption about how services will look 10 years down the line, something will have to change—for example, construction might be needed. Some such costs are not specific to PPP/PFI—they relate to changing views about what is required or desirable. Is it not the case that the cost of changes to service design, whatever the procurement method, has not been readily identifiable?

**Dave Watson:** The task is difficult, because we do not have a crystal ball to show what the changes in 10 to 15 years' time will be. The difference between conventional procurement and PFI is that, under PFI, we are stuck with the contract. The client has signed up to a deal for 30 years or more and the contractor always gets his or her money under such a deal—it is ring fenced under Treasury rules. The reality is that the client does not have flexibility. Under a conventional build, people sit down to work out the design changes and approach the health board or local authority to say, "Look—things have changed. We need to do this. You make the changes." That does not involve a commitment to the other 15 years or however long a private contract is. Under PFI, we negotiate with someone who has got us over a barrel, because he or she has that contract in their pocket.

**Derek Brownlee:** You raise an important point. If, because of falling school numbers or a different view on health services that should be provided centrally, services were reconfigured, which led to reduced demand for buildings or staff, are you seriously suggesting that the members whom your organisations represent would not be at least as strongly capable of influencing the Government of the day as would be contracts that were signed with PFI providers?

**Jon Ford:** I am not sure what point you make.

**Derek Brownlee:** You represent an organisation that has been incredibly successful at negotiating for its members.

**Jon Ford:** Thank you.

**Derek Brownlee:** I do not think that that is particularly controversial—you deserve credit for that. If proposals could undermine the interests of members of the BMA or other trade unions, a significant amount of political influence could be exercised—we have evidence that it has been exercised in the past few years—to apply pressure outwith the contractual sphere. Even without PPP/PFI, would not significant inhibitors on service change exist?

**Jon Ford:** The intention of the first phase of PFI and some of the subsequent contracts was to reduce dependence on the hospital sector and increase dependence on primary care. However, the reduction in dependence on the hospital sector did not occur. The number of beds in the first phase of PFI hospitals was too low for the throughput, but that was not to do with the actions of our members; it was more because the Government had different priorities and wanted faster throughput to bring down waiting times.

In addition, the Government did not invest in primary care at that time; it did so subsequently, as you rightly point out, and we negotiated new contracts for general practitioners on the back of that. Because it did not invest in primary care at the time, half the equation was missing. I do not think that that was to do with our members. There was a desire to move resources out of the acute sector into primary care; it is simply the case that the money did not follow. When you have predicated your entire model for a 30-year expenditure stream on the basis that there will be a shift of resources into primary care but such a shift is not funded, you are bound to have problems, regardless of the procurement route that is followed. However, I suspect that it is possible to get out of such a situation more quickly under public procurement than under PFI.

15:30

**Dave Watson:** I suggest you look at a PFI contract, or even a final business case. The appendices at the back of those that have been disclosed show how such contracts are costed out over the 30, 40 or however many years for which they last. The problem with PFI is that the unitary charge is costed on the basis of the initial assumptions.

Let us take pupil numbers as an example. If a school PFI is costed on the basis that the school is for 500 pupils, that assumption remains in place for the 30 years of the contract. In all fairness to private contractors—I am not often fair to some of them—if they have costed their model over a 30-year period but the authority says after 10 years that it wants a school of only half the size, their lawyers will tell the authority to take a running jump. There is an element of rigidity with PFIs. Service change is always challenging and difficult, but there is not the same degree of inflexibility with conventional procurement.

**Tom McCabe:** But if the same situation arose with a conventionally procured resource and the authority told the union that it needed only 250 workers, for example, and that a certain number of job losses were necessary, surely you would resist that.

**Dave Watson:** We cope with service change all the time. You have been a council leader; you have sat round the table—

**Tom McCabe:** Would you resist it?

**Dave Watson:** We would and we would not—it is not true that we resist every service change. There are many examples of the service change that has taken place in Lanarkshire over a long period of time. We do not resist all service change. We certainly want service change to be managed and planned in such a way that our members are not made redundant, which involves retraining people and moving them to new places. That happens with all local authorities and health boards, and in Government. All that we are saying is that under a PFI scheme, you are stuck.

There is a good example of that in Lanarkshire, where there are three major hospitals, two of which are PFI funded. I remember warning MSPs that it was self-evident that Monklands hospital would come under pressure because of Treasury rules, whereby funding for the other two hospitals was ring fenced. It was obvious that that would happen, given the rigidity of PFI contracts.

**The Convener:** The more closely we examine such problems, the greater the complexity that we find. We are talking about a moving target. Issues of timing are involved, and there are changes in tasks and societal needs as regards education, health and so forth. The unknowns result in problems with the methods of finance. If we have not got it right, who has got it right and why?

**Dave Watson:** A number of models are available. It is possible to pick out bits of different international models for the financing of schemes. Our view is that the starting point is good asset management. An organisation should work out its capital infrastructure plan and what it can afford—in other words, it should consider the revenue consequences of any project. Once sound asset management has been put in place, it is necessary to find the cheapest way of financing the project, which is, essentially, through conventional finance.

I am not sure that anyone has got it absolutely right. I have seen studies of how projects are financed in some of the Nordic countries, the USA and elsewhere, and there are bits of those schemes that one would pick. All that we would say is that our experience indicates that the best way forward is conventional finance within a competent asset management regime.

**Jon Ford:** Those who get it right are probably those who integrate their services most fully. Those who get the flexibility built in are those who have the most integrated systems. We do not yet have an integrated system. We have not integrated primary care and secondary care to the extent that I and our members would like us to have done. I would not hold up the US as a classic example of how to run a health care system, but some bits of its system are integrated. For example, the Kaiser Permanente model seems to work better than others.

The better integrated the systems are, the more likely we are to get the flexibility that we need to run such projects properly. If the systems are not integrated, we will not get that flexibility. Taking a large chunk and parking it with one provider for 30 years does not work.

**Ken Wimbor:** I have an example of where flexibility is important. The previous Administration, like the current Administration, was committed to reductions in class sizes, which have consequences for both teacher numbers and accommodation. Our members' perception is that PPP projects have not delivered the required flexibility in accommodation.

I am not answering your question directly, with an example of good practice, but I agree that future flexibility is important.

**The Convener:** It strikes me that the matter is about medium to long-term planning, but, unfortunately, competence and foresight can be scarce commodities.

Would our witnesses like to make any final comments?

**Jon Ford:** As I said at the outset, the experience of those of our members whom we consulted about PFI projects has been positive in some respects. They got the new hospitals that they wanted. They have the shiny new facilities and the capital investment that they wanted for 20-odd years. However, as the projects have unfolded, the criticisms have become manifold.

The message is that, if you predicate something on a certain pattern of service for a long time, sooner or later the deficiencies will come to light. That is what has happened. Increasingly, our members tell us that facilities that they thought were fit for purpose have turned out not to be so, particularly in the light of recent deficits. In the NHS in England, the focus of the deficits is the hypothecation of large expenditure streams to PFI projects, which has been to the detriment of clinical services. Obviously, doctors are concerned about that. The more money we wrap up in such projects, the more likely it is that services will feel the pinch.

I echo what Mr Watson said about reconfiguration. Our members' view is open to challenge, but their perception is that PFI facilities are the least likely facilities to be closed when services are reconfigured. It does not necessarily follow that those facilities are the ones that should stay open. It is just that there is an income stream to which one is committed for a long time and it makes sense not to prejudice that. Other facilities are vulnerable, but they should not be.

**Dave Watson:** The arguments against private financing have been well rehearsed. The committee has heard all of them during its evidence-taking sessions.

Our view is that you should not try to put a flawed model right by playing with it. That will not work. You should start again, which in our view means providing a level playing field between conventional finance and private finance. You should do that by ensuring that the prudential borrowing framework is available both to local authorities and to other public bodies. That approach is the way ahead. It will deliver a flexible and cost-effective capital infrastructure that meets Scotland's needs.

**Ken Wimbor:** The existing PPP scheme is a flawed model. We believe that it is important to have a level playing field. Our members reported to us four major areas of concern about the schemes that they have experienced: consultation levels; health and safety when a school is not closed during refurbishment; facilities management; and future flexibility, particularly in relation to reductions in class sizes.

**The Convener:** Thank you for your important evidence, which is appreciated by the committee. If you wish to raise any further points, do not hesitate to put them to the committee in writing.

15:39

*Meeting continued in private until 15:50.*

Members who would like a printed copy of the *Official Report* to be forwarded to them should give notice at the Document Supply Centre.

No proofs of the *Official Report* can be supplied. Members who want to suggest corrections for the archive edition should mark them clearly in the daily edition, and send it to the Official Report, Scottish Parliament, Edinburgh EH99 1SP. Suggested corrections in any other form cannot be accepted.

The deadline for corrections to this edition is:

**Wednesday 21 May 2008**

PRICES AND SUBSCRIPTION RATES

OFFICIAL REPORT daily editions

*Single copies: £5.00*
*Meetings of the Parliament annual subscriptions: £350.00*

The archive edition of the *Official Report* of meetings of the Parliament, written answers and public meetings of committees will be published on CD-ROM.

WRITTEN ANSWERS TO PARLIAMENTARY QUESTIONS weekly compilation

*Single copies: £3.75*
*Annual subscriptions: £150.00*

Standing orders will be accepted at Document Supply.

Published in Edinburgh by RR Donnelley and available from:

**Blackwell's Bookshop**

**53 South Bridge**
**Edinburgh EH1 1YS**
**0131 622 8222**

**Blackwell's Bookshops:**
243-244 High Holborn
London WC 1 7DZ
Tel 020 7831 9501

All trade orders for Scottish Parliament documents should be placed through Blackwell's Edinburgh.

**Blackwell's Scottish Parliament Documentation Helpline may be able to assist with additional information on publications of or about the Scottish Parliament, their availability and cost:**

**Telephone orders and inquiries**
**0131 622 8283 or**
**0131 622 8258**

**Fax orders**
**0131 557 8149**

**E-mail orders**
**business.edinburgh@blackwell.co.uk**

**Subscriptions & Standing Orders**
**business.edinburgh@blackwell.co.uk**

**Scottish Parliament**

**RNID Typetalk calls welcome on**
**18001 0131 348 5000**
**Textphone 0845 270 0152**

sp.info@scottish.parliament.uk

All documents are available on the Scottish Parliament website at:

www.scottish.parliament.uk

**Accredited Agents**
(see Yellow Pages)

and through good booksellers

Printed in Scotland by RR Donnelley