

PUBLIC AUDIT COMMITTEE

Wednesday 21 January 2009

Session 3

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PUBLIC AUDIT COMMITTEE

2nd Meeting 2009, Session 3

CONVENER

*Hugh Henry (Paisley South) (Lab)

DEPUTY CONVENER

*Murdo Fraser (Mid Scotland and Fife) (Con)

COMMITTEE MEMBERS

*Willie Coffey (Kilmarnock and Loudoun) (SNP)

Cathie Craigie (Cumbernauld and Kilsyth) (Lab)

*George Foulkes (Lothians) (Lab)

*Stuart McMillan (West of Scotland) (SNP)

*Nicol Stephen (Aberdeen South) (LD)

*Andrew Welsh (Angus) (SNP)

COMMITTEE SUBSTITUTES

Derek Brownlee (South of Scotland) (Con)

*James Kelly (Glasgow Rutherglen) (Lab)

John Farquhar Munro (Ross, Skye and Inverness West) (LD)

Sandra White (Glasgow) (SNP)

*attended

THE FOLLOWING GAVE EVIDENCE:

Mr Robert Black (Auditor General for Scotland)

Angela Cullen (Audit Scotland)

Barbara Hurst (Audit Scotland)

Mark MacPherson (Audit Scotland)

Stewart Stevenson (Minister for Transport, Infrastructure and Climate Change)

CLERK TO THE COMMITTEE

Tracey Reilly

SENIOR ASSISTANT CLERK

Joanna Hardy

ASSISTANT CLERK

Jason Nairn

LOCATION

Committee Room 1

Scottish Parliament

Public Audit Committee

Wednesday 21 January 2009

[THE CONVENER *opened the meeting at 10:00*]

Decision on Taking Business in Private

The Convener (Hugh Henry): Good morning. I will start the meeting, as I know that the minister is running to a tight schedule. I welcome everyone to the second meeting in 2009 of the Public Audit Committee.

I ask everyone to ensure that mobile phones and other electronic devices are switched off. Apologies have been received from Cathie Craigie. James Kelly is substituting for her. I welcome the staff of Audit Scotland, the minister and his team, and members of the public.

Under the first item on the agenda, I ask members to agree to take items 4, 5 and 6 in private.

Members *indicated agreement.*

Section 23 Report

“The First ScotRail passenger rail franchise”

10:01

The Convener: The second item on the agenda is a section 23 report. Last week, we started our discussion on the extension of the First ScotRail franchise. Today, we will take further evidence from the Minister for Transport, Infrastructure and Climate Change, Stewart Stevenson MSP. We will then hear from Robert Black, the Auditor General for Scotland. Minister, I welcome you to the committee. I am aware that you need to attend another committee, so we will try to stick to our agreed time. I invite you to make introductory comments.

The Minister for Transport, Infrastructure and Climate Change (Stewart Stevenson): I apologise for the change of supporting personnel, which is due to illness. I hope that that does not influence the committee—I do not believe that it should. Thank you for the invitation to be here.

I very much welcome the report's findings on train performance. More trains are running on time, passenger numbers are well ahead of expectations and passenger satisfaction is up. Those findings reflect Transport Scotland's effective and efficient management of the Government's single biggest contract. The report also recognises the benefits that the franchise extension has secured for passengers and taxpayers.

I noticed the committee's comments on the provision of information that was substantially analysed both internally and externally and that allowed me to make the decision to extend the contract. I am also aware that our approach to stakeholder consultation and Transport Scotland's management of interests relating to the extension are matters of interest to the committee. I am happy to answer questions on any issues relating to the franchise or the extension process, although the point relating to the management of interests was comprehensively covered last week by both Transport Scotland's chief executive and the permanent secretary.

I will remind the committee why we took the decision to extend the franchise. The original contract, which was let by the previous Administration, contained a revenue share mechanism that, given the unforeseen levels of performance by the franchisee, was set at a level such that First ScotRail had become financially incentivised to make cuts—something that would have resulted in a poorer service to passengers

and a loss of employment in the rail industry. The original contract also contained an extension clause without any awarding criteria. This Government, along with Transport Scotland, developed those criteria. By developing the criteria and then awarding an extension, the Government has ensured that we have a best-value deal and a guaranteed return that is based on growth assumptions that are challenging in the current economic climate.

In extending the contract, the Government has ensured that First ScotRail remains incentivised to grow our joint business. We have increased value for money by putting improvements in place without any subsidy uplift and we have improved the performance of trains as the franchisee attempts to meet testing new delivery targets. In addition, not only have we secured growth in the size of the First ScotRail workforce, we have enabled that growth to continue as our further rail developments are delivered.

The Convener: Thank you, minister. I have a couple of general questions to ask before I open up the discussion to other members of the committee. Were you aware that investigations were being undertaken by Transport Scotland into complaints about Mr Houston in relation to other contracts and other pieces of work?

Stewart Stevenson: I was not aware of that.

The Convener: Okay. Did you or Mr Swinney make known at any time to senior civil servants or to senior officials in Transport Scotland that you believed that Mr Houston should leave?

Stewart Stevenson: I am not prepared to discuss that subject, convener. Matters to do with the employment of civil servants are for the permanent secretary, not for ministers.

The Convener: I understand that. I am not trying to pursue any line of inquiry into the employment contract; I am asking whether you or Mr Swinney indicated to senior civil servants or Transport Scotland that you, as ministers, believed that Mr Houston should leave his post.

Stewart Stevenson: The beliefs of ministers are quite irrelevant to the employment situation of any civil servant.

The Convener: That is as may be, but I am asking whether you indicated either to civil servants or to Transport Scotland that you thought that Mr Houston should leave.

Stewart Stevenson: Convener, I am simply not going to be drawn on a subject that is a matter for the permanent secretary.

The Convener: No, I am not asking about the permanent secretary's decision. I am asking what you and Mr Swinney said in your capacity as

ministers either to civil servants or to Transport Scotland in relation to Mr Houston's employment. Did you indicate that you, as ministers, felt that he should leave his post?

Stewart Stevenson: Convener, ministers have absolutely no evidence to suggest that any malfeasance occurred to justify action being taken to force that man to leave office. I am not going to discuss the matter further, as employment matters are for the permanent secretary.

The Convener: But Mr Stevenson, I am not asking about employment matters. I realise that such matters are the responsibility of officials. I am merely asking whether you or Mr Swinney indicated either to senior civil servants or to senior officials in Transport Scotland that Mr Houston should leave his job.

Stewart Stevenson: Convener, I am going to keep repeating that we had no evidence of any malfeasance or dereliction of duty that required us to make comments to the civil service. At the end of the day, the performance and employment status of civil servants are entirely matters for the permanent secretary and others in the civil service. If I may say so, convener, we are heading into very dangerous territory if we are suggesting that ministers—or members of the Scottish Parliament, for that matter—should be involved in any way in the employment status of civil servants. The separation between the political decision-making process and the employment of civil servants is important, and I think that, like me, people in this room wish it to be preserved.

The Convener: I agree entirely, and I do not suggest that there is any evidence of malfeasance. I am asking a simple question: did you or Mr Swinney indicate either to civil servants or to officials in Transport Scotland that you believed that Mr Houston should leave his job?

Stewart Stevenson: I am not prepared to put myself in the position, in any answer to this committee, of suggesting that there were any grounds for taking action to cause that man to leave employment. I am simply not prepared to respond further in any way that would suggest that there were grounds for terminating the employment of any civil servant.

The Convener: I note what you are saying, Mr Stevenson, and I will seek further advice on your unwillingness to reply to the specific question that I asked. I am not trying to draw you into any of the wider areas to which you referred. I will leave it there for the moment.

Nicol Stephen (Aberdeen South) (LD): The convener's raising of that point with Mr Stevenson reminded me a lot of the Jeremy Paxman interview with Michael Howard. As you will recall, he was asked repeatedly whether he played any

role in the sacking of a senior civil servant. I would have thought that this situation—

Stewart Stevenson: Excuse me, convener.

The Convener: Can I let Mr Stephen—

Stewart Stevenson: No. Convener, if I may—

The Convener: Mr Stevenson, I am chairing the meeting. I will let Mr Stephen finish, then I will allow you to respond.

Nicol Stephen: Everyone on the committee understands your point, minister, which is that ministers should not play a role in issues relating to the contract of employment of a senior civil servant, whether disciplinary action has to be taken or whether there requires to be a dismissal. However, as we all know, ministers may state their views and opinions, and they may raise issues with senior civil servants. You have gone out of your way to emphasise your belief that there should be no ministerial involvement in such matters. I would think that it would be very easy to give a direct and honest answer when the convener asks you whether you or Mr Swinney got involved, played any role or expressed an opinion on the removal from office of Mr Houston.

So far this morning, you have been unable to give a direct answer. I know that, ultimately, Mr Houston left office of his own free will—he resigned from employment—so it should be even easier to answer the hypothetical question. Did you wish any action to be taken against Mr Houston?

Stewart Stevenson: In his remarks, Mr Nicol Stephen used the words

“the sacking of a senior civil servant”

and

“the removal from office of Mr Houston.”

The use of those phrases in this context is precisely why I am not going to comment further on the matter, because it potentially impugns, without a shred of evidence, someone's reputation, which they are entitled to have protected. Forgive me, but that is why I will not be drawn further on the subject. It is clear that we would start to use entirely inappropriate language in the circumstances. If I may say so, we have already crossed that very important and dangerous line.

The Convener: I entirely accept what you say about impugning anyone's integrity. However, if you could assure us that neither minister was in any way involved, there would be no need to explore the matter further.

Nicol Stephen: Exactly, convener. Mr Stevenson could simply state, “No, ministers did not get involved in any way and did not seek to

influence the civil servants.” If you were able to give the simple, straightforward question a simple, straightforward answer, Mr Stevenson, the matter would be resolved. The problem is that you seem unable to give such a straightforward answer—in the same way that Michael Howard was unable to answer the question that Jeremy Paxman asked 13 times over. I do not understand why you cannot give that simple assurance this morning. Unless you can explain that, I will continue to be bemused by the matter.

Stewart Stevenson: I hope that I can be direct and unambiguous. A former minister of Mr Stephen's experience should understand that the employment status of any civil servant is entirely a matter for the civil service—ultimately, it is for the permanent secretary. I have already seen the real dangers of our opening up this discussion in any way, shape or form, given Mr Stephen's use of the words

“the sacking of a senior civil servant”

and

“the removal from office of Mr Houston.”

I must apologise to you, convener, if you think that it is discourteous, but I am simply not going to cross that line.

The Convener: We will reflect on that.

Stewart Stevenson: No discourtesy is intended, convener—please accept that.

The Convener: I do accept that.

Murdo Fraser (Mid Scotland and Fife) (Con): Good morning, minister. You can perhaps appreciate the committee's difficulty. When we took evidence from him last week, Malcolm Reed of Transport Scotland put up a robust defence of his actions and the actions of Transport Scotland in relation to the way in which the renewal of the ScotRail franchise was handled and in relation to Mr Houston's role. Mr Reed was quite clear in his evidence, which is all in the *Official Report*, when he said:

“there was no conflict and ... Guy Houston was not involved in decision making”.—[*Official Report, Public Audit Committee*, 14 January 2009; c 821.]

Mr Reed was clear that there was no problem with that. However, when the matter became public, Mr Houston left the employment of Transport Scotland. The committee is unable to find out the terms on which he left, because that is deemed to be confidential information. To any impartial observer, that sequence of events appears curious. It appears to be more than a coincidence that the two things should happen at the same time.

One of the purposes of the Public Audit Committee of the Parliament is to ensure that

public money is properly accounted for. You will appreciate our concern that public money might have been used in the departure of Mr Houston from Transport Scotland and that that was in some way connected with the renewal of the ScotRail franchise. It is immensely frustrating that the committee, which is supposedly here to safeguard the public purse, is unable to discover whether or not that was the case. Can you appreciate committee members' frustration? Surely you, as Minister for Transport, Infrastructure and Climate Change, with ultimate political responsibility, share that frustration.

10:15

Stewart Stevenson: I absolutely acknowledge what Mr Fraser says. I must say that I have absolutely no knowledge of the decision-making process that was involved in the departure of a senior member of Transport Scotland staff. The answers that were given by the permanent secretary must stand on the record.

Murdo Fraser: But, as minister with responsibility for transport and for Transport Scotland, would it not be a matter of concern to you if civil servants who were involved in that agency's employment matters were using public money as, for example, a pay-off to a member of staff who had become an embarrassment?

Stewart Stevenson: I can make no comment whatever on any financial issues around this matter. I have no knowledge of them. Ministers are responsible and accountable for the decisions that are made. That is the proper responsibility of ministers. Issues of employment are, of course, a matter for the permanent secretary.

Murdo Fraser: Surely matters involving public money are of concern to you, as minister.

Stewart Stevenson: Of course money is a matter of concern to me, as a minister, but I have absolutely no knowledge of the circumstances of the departure from Transport Scotland on which you are trying to draw me. The person of whom you could ask the question is the permanent secretary. You did that last week, and his answers are a matter of public record.

Murdo Fraser: Indeed they are. You appreciate my concern: we are dealing with public money, yet nobody is prepared to give this committee of the Parliament an answer as to whether or not public money was spent in this connection.

Stewart Stevenson: I have no knowledge of whether any money was involved at all. It is entirely a matter for the civil service.

Murdo Fraser: So you deem it acceptable that the matter is entirely secret, and that there is no public transparency at all about how public money may or may not have been spent.

Stewart Stevenson: It is an issue that you must pursue with the permanent secretary.

Andrew Welsh (Angus) (SNP): We are all trying to seek out what actually happened. I am uneasy about this situation. Are we in danger of asking you, as minister, to breach confidentiality? Is that the basis of your reluctance?

Stewart Stevenson: You have to understand that I know nothing of the circumstances of the departure of an individual from Transport Scotland. That is a matter of his employment status with the civil service, and all questions on that matter must be directed to the permanent secretary. However, you are correct: if I were aware of the circumstances, I would be bound by the same laws to which the permanent secretary referred when he spoke to the committee last week.

George Foulkes (Lothians) (Lab): I do not want to ask about the circumstances of Mr Houston's departure, but when did you first become aware that he had shares in FirstGroup, the holder of the ScotRail franchise?

Stewart Stevenson: It was a matter of public record. I signed off the annual report for Transport Scotland, which indicated that such a declaration had been made.

George Foulkes: So you knew that he had shares in FirstGroup. Because of that, did you worry at all about his involvement in the discussions on the franchise extension?

Stewart Stevenson: As has been made clear, Mr Houston's involvement post-dated the decision.

George Foulkes: Were you worried about it at all? I would have been if I were in your position.

Stewart Stevenson: Given that it post-dated the decision, no.

George Foulkes: Not at all?

Stewart Stevenson: No.

George Foulkes: Why not?

Stewart Stevenson: Because the decision had been made without Mr Houston's involvement.

George Foulkes: But he was around. He was part of the establishment and the structure at the time. Did you not think that it was strange that he was taking part in discussions and procedures around the extension of the contract?

Stewart Stevenson: You were told last week by the chief executive of Transport Scotland that Mr Houston played no part in the decisions.

George Foulkes: But I am asking you—

Stewart Stevenson: Forgive me, Mr Foulkes, but you are asking me whether I was worried

about something that did not happen. I was not worried about it, because it did not happen.

George Foulkes: Imagine the public perception of the situation: a senior executive of Transport Scotland has shares and share options in FirstGroup and you, as minister, know that the franchise is being discussed. The public perception would be that that was strange. Did you not feel that perhaps you should have taken some action and intervened in some way?

Stewart Stevenson: Given that Mr Houston was not involved in the process, no action required to be taken. In addition, I think that ministers are entitled to rely on the existing proper process for managing interests in the civil service, just as in Parliament.

George Foulkes: Did you inquire at the time whether he was taking part in the process?

Stewart Stevenson: It was very clear that he was not taking part in the process.

George Foulkes: How was that very clear?

Stewart Stevenson: It was very clear because the work was being done in a different functional area of Transport Scotland from the one that Mr Houston worked in.

George Foulkes: But he was still involved very much in the work of Transport Scotland in relation to the rail franchise, was he not?

Stewart Stevenson: No.

George Foulkes: Not at all?

Stewart Stevenson: That was the responsibility of Bill Reeve.

George Foulkes: So he had no part whatever in the franchise extension.

Stewart Stevenson: Until the decision was made, he had no involvement.

George Foulkes: Although he was a member of the investment decision-making board.

Stewart Stevenson: I simply have to go back to the evidence that the chief executive gave you last week. I think that there is no evidence whatever of Mr Houston's involvement in the decision-making process. In any event, there were processes within Transport Scotland, as there are throughout the civil service, for managing interests. I note that the Audit Scotland report does not suggest in any way, shape or form that Mr Houston was involved in the decision-making processes. That is something upon which we should rely, together with the existence of the appropriate processes and the public declaration of interests that ensured that the information was in the public domain.

George Foulkes: Given all the answers that you have just given me, were you not surprised when Mr Houston resigned?

Stewart Stevenson: It is not a matter for me to be surprised or unsurprised about the employment status of any member of the civil service. If you will forgive me, I will not comment further on that subject.

George Foulkes: But I have heard you comment on so many other things about your brief. All I am asking you is, when you heard about his resignation or read about it—or however you found out about it—what was your reaction?

Stewart Stevenson: My brief does not include responsibility for the employment status of a single civil servant.

George Foulkes: I am not asking you about your responsibility. You must have had a reaction. Were you surprised, pleased or shocked? Did you take any action as a result?

Stewart Stevenson: I am not going to respond to questions about the employment status of a civil servant.

George Foulkes: You say that you regret feeling discourteous to the committee. I put it to you that you are not being discourteous; you are being evasive.

Stewart Stevenson: I am not supplanting the proper role of the permanent secretary in civil servant employment. I do not have that role. It is not for me to take over any of the responsibilities of the permanent secretary in that regard. I do not think that anyone is suggesting that I should do so. Given that that is the case, you should simply accept that it is not for me to make the kind of comment that you wish me to make.

The Convener: I want to pursue one issue. You say that there is no evidence of any malfeasance and you state categorically that Mr Houston was not involved in the franchise extension in any way and therefore did not influence the decision in any way. Given all that, would you agree that there was probably no reason for Mr Houston to leave his post with Transport Scotland?

Stewart Stevenson: People leave posts for a huge variety of reasons, and I have no knowledge whatever of Mr Houston's thinking when he left Transport Scotland.

The Convener: Yes, and I presume that the decision was his, without any influence or interference from elsewhere. However, my point is that there was no reason relating to the franchise extension for Mr Houston to leave his post. If he had other reasons to move on, that is entirely for him, but, as far as the franchise extension is concerned, there was no reason for him to leave his post.

Stewart Stevenson: I am entirely unaware of any such reason.

Nicol Stephen: Can you confirm that the first that you knew of Mr Houston's shareholdings in FirstGroup was through Transport Scotland's annual report?

Stewart Stevenson: I do not want to give false certainty. I was certainly aware of the issue at that stage. I cannot recall it being brought to my attention prior to that.

Nicol Stephen: When you were asked to sign off the annual report, for how long had Mr Houston been in office?

Stewart Stevenson: Again, I do not wish to give false certainty. I simply say that I believe, based on what I have read elsewhere, that Mr Houston had been in office since 2006.

Nicol Stephen: When were you asked to sign off the annual report?

Stewart Stevenson: Again, I cannot give an absolute date. We can get the publication date for you. I certainly would have signed off the annual report in advance of that, for rather obvious reasons.

Nicol Stephen: I understand that.

Stewart Stevenson: It would have been early autumn at the latest.

Nicol Stephen: I presume that you can provide the dates to the committee.

Stewart Stevenson: Oh yes, we can certainly do that.

Nicol Stephen: Either before signing off the annual report or subsequent to it, were you at any point given advice on how to handle Mr Houston's interest? For example, it would obviously have been inappropriate for you to raise issues with him relating to FirstGroup. Were you given any such advice?

Stewart Stevenson: It would not have been appropriate for me to be given such advice because, under the civil service code, it is for the person who has an interest to handle their interest, just as members of the Parliament have responsibility for handling their interests. The responsibility is an individual one within a framework that is set down.

Nicol Stephen: So in any meeting at which Mr Houston was present, you would have expected him to raise the issue if you strayed into areas of discussion that involved FirstGroup, which you could normally and innocently have done. Is that how you would have expected the situation to be handled?

Stewart Stevenson: Any civil servant or member of the Parliament must recognise when they are at a point at which an interest has to be declared or other action taken. I would expect that to be the case with any civil servant and any member of the Parliament.

Nicol Stephen: My difficulty is that the civil service code does not state that. It makes it clear that it is for the individual to declare the interest—

Stewart Stevenson: Yes, that is my point.

Nicol Stephen: But it goes on to say that the department should take appropriate steps to handle that interest. I would have thought that a fairly obvious appropriate step to take would be to ensure that a minister was informed of an interest, and that it would be inappropriate to discuss with an individual the interests of a significant transport company if he had a shareholding in it. Will you confirm that that did not happen in this case? Nothing was explained to you and you did not set down at ministerial level a procedure or protocol for handling the interest.

10:30

Stewart Stevenson: It is not for me to handle the interest; it is for the individual, just as we as MSPs handle our interests.

Nicol Stephen: As I just explained, that is not the case under the civil service code, which makes it clear that the department must respond to the interest and decide whether, for example, shares should be sold—that is an option under the ministerial code—or whether other action should be taken. What other action were you aware of Transport Scotland taking in relation to Mr Houston's interest? It is clear that Transport Scotland did not require the shares to be sold.

Stewart Stevenson: The committee questioned Transport Scotland's chief executive and the permanent secretary on the subject last week. Their answers described the processes and procedures that were in place to deal with civil servants' interests.

Nicol Stephen: Are you concerned that the first that you knew of that important interest was when you were asked to sign off the annual report?

Stewart Stevenson: It is important to return to the point that there is absolutely no evidence that the existence of an interest had a material effect on anything. It is also important that civil servants at all levels—who may have a huge variety of interests—take responsibility for managing their interests. The situation would be impossible if they did not have individual responsibility for which they were accountable.

Nicol Stephen: I am surprised that your view continues to be that the matter was solely for the civil servant involved. I am trying to find out whether you are concerned by any aspect of the situation, but I am not receiving clear answers.

How were you informed of Mr Houston's departure? What were you told and who informed you?

Stewart Stevenson: I was informed of the fact of his departure, but I do not recollect in what circumstances or who told me.

Nicol Stephen: Am I correct in saying that you can provide that information to the committee?

Stewart Stevenson: I expect so, but I do not want to give false certainty. I think that the issue came up in conversation in another context, rather than in a formal notification to me. I am preparing the ground in case I cannot provide absolute certainty, but I can say with certainty that I was informed that Mr Houston had left Transport Scotland.

The Convener: That information would be helpful. I assume that, irrespective of whether the issue came up in conversation, Transport Scotland formally notified the permanent secretary or ministers of the position.

Stewart Stevenson: I cannot comment on what the permanent secretary was told—that is a matter for him.

The Convener: We can find that out.

Stewart Stevenson: I would not normally expect a formal notification to ministers, but I accept that it is clear that ministers were told about the position in this case. A formal note to ministers is not normally provided on such a subject. As the former ministers in the room know, civil servants leave all the time, and I do not think that there has ever been a formal process for making ministers aware of that. When another senior civil servant left I was told about it, but I do not believe that I received formal notification.

The Convener: If you can check e-mails and letters, that will be fine.

Stewart Stevenson: We are content to do that.

Andrew Welsh: Surely ministers should know about an official's declarable interest. We are talking not about any official but about a key official and about the finance for and organisation of a major project. The minister will understand our concern. We keep hearing that the director of finance and corporate services played no part in decision making, but he was present at meetings at which decisions were discussed, so he was privy to confidential information.

Surely the normal practice in any organisation would be for such an official to declare an interest and leave. The official declared a financial interest in FirstGroup, but surely he should not have been present at any meetings at which the matters in question were discussed and decided.

Stewart Stevenson: I simply fall back on what the chief executive said to the committee last week, which was that the organisation recognised that it had to consider the recording of people's presence or absence at particular points in meetings.

Andrew Welsh: I suggest that ministers should know about such interests because they may end up in front of a parliamentary committee, being answerable to Parliament—as is happening to you. That issue should be thought about deeply.

Stewart Stevenson: Ministers will always take tent of audit reports and what the committee has to say.

The Convener: Andrew Welsh makes a valid point. What we are saying today and what we said last week is not a criticism of you or your actions per se; it is a concern about a system that puts ministers in an invidious situation. To some extent, whether ministers were involved in other matters is neither here nor there—we can pursue that. The important discussion is about the implications of the role of the individual concerned and how that clouds the wider issue. We have raised our concerns with the permanent secretary, but I hope that you will convey to the Cabinet Secretary for Finance and Sustainable Growth and the First Minister the concerns that we have articulated so that the process is given some consideration to ensure that ministers are not placed in such a situation in future.

Stewart Stevenson: It might be useful if I say to the committee that it can be absolutely assured that this minister, the cabinet secretary and all members of the Government will take very seriously what a senior committee of the Parliament—it is appropriate to describe the Public Audit Committee in those terms—might say. As with all reports, we will ensure that, if opportunities emerge for us to improve and tighten procedures, we will seek to do that.

The Convener: Thank you, minister.

James Kelly (Glasgow Rutherglen) (Lab): I would like to clear up one issue in regard to Mr Houston's role. The minister stated that Mr Houston had no input on the franchise extension until that decision had been made. We should bear it in mind that an extension was being considered because the existing arrangements were no longer fit for purpose. When new arrangements were considered, an appraisal process would have had to take place that

involved analysis of the financial impacts for Transport Scotland and included a review of performance-based payments. Are you telling us that Transport Scotland's finance and corporate services division had no input into that process?

Stewart Stevenson: As the Audit Scotland report says in paragraph 71:

"the director of Finance and Corporate Services has no vote on any decision-making relating to FirstGroup, and was not involved in the review process, including development of the options".

That is an important conclusion. The fact that the rail part of Transport Scotland took independent external advice provides a high level of assurance that the figures that were used were a correct basis for the decision making, which did not involve Mr Houston.

James Kelly: Are you stating that Transport Scotland's finance and corporate services division had no input into the process? Are you trying to separate Mr Houston's role from that of the division?

Stewart Stevenson: I am being asked about Mr Houston and I am making it clear that the Audit Scotland report reinforces what has been said by others: Mr Houston played no role in the decision-making process. It was for the rail part of Transport Scotland to pursue the issue and it did; it also engaged external consultants to assist it.

James Kelly: Do you not agree that in pursuing the issue it would have had input from the finance department and that, as the director of finance and corporate services, Mr Houston would have been responsible for that input and therefore involved in the process?

Stewart Stevenson: It was a matter for the rail part of Transport Scotland. The directorates involved were rail delivery, and strategy and investment—neither of which was the responsibility of Mr Houston.

Willie Coffey (Kilmarnock and Loudoun) (SNP): Convener, we have spent 41 minutes asking basically the same question on the same subject, and we have limited time in which to ask the minister other questions. As you know, some of us arrived in plenty of time before the meeting to prepare for the session; it is a wee bit discourteous that the agenda has been, to an extent, grabbed by members who came in very late and have used up valuable time asking the same question.

The Convener: Mr Coffey, the time at which members arrived at the meeting is irrelevant to the questions that they have asked. Given your concerns, you could put your question now.

Willie Coffey: I will focus on the business case. The Audit Scotland report stated that

"Transport Scotland did not provide the Minister for Transport, Infrastructure and Climate Change with a fully documented business case",

but Dr Reed said last week that a detailed business case, business plan and rigorous appraisal process was gone through, which was sufficient to enable you to come to the decision. Will you give us your take on that and tell us a wee bit more about the nature, quality and volume of the information that led you to make the decision?

Stewart Stevenson: Paragraph 56 of Audit Scotland's report states:

"Transport Scotland's appraisal process was rigorous and has resulted in a guaranteed £73.1 million investment by First ScotRail".

Ministers—myself in particular—were involved in looking at a range of figures related to the proposal over quite a period. The figures changed as we involved the external consultants and as officials engaged with the company. When ministers sat down to make the decision at the end of the process, it was against a backdrop of their having been involved in looking at the options—some of which appeared and disappeared during the process.

The important thing was for ministers to have confidence in the process that Transport Scotland had undertaken. Its internal processes for looking at the economics of the matter, and the use of external consultants meant that ministers were well placed to understand the alternative options that were available and to make the right decision. Audit Scotland's report is clear that huge benefits arose from the decision that ministers made.

Willie Coffey: It was suggested that the presentation to you was no more than a set of slides, but Audit Scotland's report described the appraisal process as "rigorous". It is difficult to see where the middle ground may lie between those two positions. What was the nature of the documentation and so on that you were given to enable you to make the decision?

Stewart Stevenson: It is true that a set of high-level slides was used to focus the discussion at the decision-making meeting, but you should be clear that the meeting was by no means the first engagement of ministers. As you would expect, given my personal interests, detailed figures had been examined at various stages. Ministers have looked at a number of the underlying assumptions and workings over a period of time. The presentation at the decision-making meeting pulled together the key facts that had been drawn out from the work of Transport Scotland and the external consultants, so that ministers could see that the decision that they were about to make was sensible.

10:45

Stuart McMillan (West of Scotland) (SNP): Paragraph 73 of Audit Scotland's report states:

"Transport Scotland did not consult on the franchise review".

It goes on to say:

"Transport Scotland did not secure separate advice on this point",

which refers to the lack of consultation, the influencing of market activity and the breach of financial regulations. Is that normal practice for such a large project—in financial terms—in the public sector? Was it a legitimate course of action for Transport Scotland to take?

Stewart Stevenson: It was a legitimate course of action. In my professional life I have become extremely familiar with the issue of market sensitivity, as have other members of my family who have worked in financial services. It was no surprise to me personally, as a minister, when that issue was raised as something that inhibited our ability to go public at that stage.

In making the decision, ministers relied on the substantial consultation that had been undertaken around the publication of "Scotland's Railways" and in letting the franchise and drawing up the contract that made the provision for the extension. We created a window within which it would be possible to consult on the proposals for spending the £73.1 million that was derived from recasting the contract and extending the franchise. We also retained a window within which we could go back to market and retender in 2011, if that was the appropriate thing to do. We have not fully analysed the results of the consultation on the franchise extension, but it is clear from the input that we have examined that there is widespread support for what the extension has delivered.

Stuart McMillan: I accept much of what you say, particularly with regard to the financial regulations that are in place, but we are discussing a large project that involves a large sum of public money. Are there any other instances within your department or other Government departments in which further external information or advice has been sought before awarding a project?

Stewart Stevenson: Projects come in all shapes and sizes. On Friday, for example, we signed a £320 million contract for the 11-mile M80 extension, and we have also signed a contract worth more than £400 million for the M74. Each project is dealt with in the most appropriate way.

The project that we are discussing, which will deliver money to the public purse to improve Scotland's railways, was aligned with the consultation on rail policy that the previous Administration carried out and to which we have

continued, essentially, to subscribe. Substantial consideration was given to the contract that provided for the extension and, given the market sensitivity, we had to carry out the consultation post hoc rather than ad hoc. The consultation that we have now carried out justifies the choice of that particular approach in that particular circumstance.

The Convener: James Kelly has a question about the role of the Cabinet.

James Kelly: You have acknowledged that the contract was significant. What role did the Cabinet play in taking the decision?

Stewart Stevenson: The decision was made by ministers.

James Kelly: Did the Cabinet have sight of the documents relating to the contract? Did it authorise the decision?

Stewart Stevenson: The decision was made by me.

James Kelly: So the matter did not go to the Cabinet—the decision was made by you, as the Minister for Transport, Infrastructure and Climate Change.

Stewart Stevenson: The decision was made by me.

The Convener: Without any discussion in Cabinet?

Stewart Stevenson: That is correct.

George Foulkes: You mentioned that, before you made the decision, you considered alternative options. What were they?

Stewart Stevenson: There were three main headings. One was simply to do nothing, which is a standard option that one would expect to consider in such circumstances. The second was to seek to renegotiate the contract as it stood, with the franchise running to 2011. We saw that in 2006-07 First ScotRail had looked to reduce spending on advertising, for example, so there were already warning signs that the approach of the point at which 80 per cent of new revenue would be returned to the Government was starting to change behaviour in the company. That was a key issue in turning us away from doing nothing.

The next question to be considered was what value we could derive from seeking to renegotiate the contract. If we had sought to renegotiate it without having something to offer, there would not have been much incentive for the company. Ultimately, it was clear that there was substantially more value to be extracted from extending the contract, for which provision had been made originally. In particular, we were driven by consideration of the risks that would be factored into any bids by a new franchisee in 2011. A

number of substantial rail projects, for which a new franchisee would want to add risk pricings, will be on the go by that date. Several different considerations led us to the option that we chose. I have outlined the three main headings, below which were a range of subheadings and options.

In 2002, Iain Gray suggested that a 15-year franchise would achieve maximum stability. We ended up with a seven-year franchise, with the option of a three-year extension. The franchise contract was signed weeks after the collapse of Railtrack, when there was huge uncertainty. That was part of the reason for the way in which the contract was structured, which took us to the decision point.

George Foulkes: You seem reasonably confident that your decision was robust. Why did you rush out the announcement during recess, instead of making a statement to Parliament?

Stewart Stevenson: The original franchise was also announced during recess. We looked at the processes and procedures that were followed at that time, and we followed them to the letter. We were concerned about commercial confidentiality. Today's newspaper reports that an Edinburgh company has been fined by the Financial Services Authority in relation to disclosure—disclosure of a different character, I hasten to add. We thought that there was no reason to delay and that there was a reason to proceed. We followed exactly the same processes that were followed when the original franchise was announced during recess.

George Foulkes: In retrospect, do you not think that it would have been better for you to have made the announcement to Parliament and answered questions on it?

Stewart Stevenson: I did answer questions on it, and there was also a statement. I have seen nothing to suggest that we should not have announced the decision when we did—immediately before the start of the new financial year, which was a matter of some importance for decision making.

George Foulkes: I have a related question. Are the procedures of Transport Scotland different from those of any other department of Government?

Stewart Stevenson: I am not sure that I am equipped to answer that very general question. It is perhaps a question that the permanent secretary could more readily answer, although individual departments will clearly have to do certain things in different ways. I do not think that I can be more specific than that unless you make your question more specific.

George Foulkes: Well, can I just ask—

The Convener: Sorry, George, but the minister has to leave. Nicol Stephen has another question, but we do not have time—

George Foulkes: I have another question, too.

The Convener: If we have further questions, minister, we will put them to you in writing. I am aware that you have another parliamentary commitment and that we need to conclude our questioning. We will reflect on your earlier comments and your unwillingness or inability—however you want to describe it—to answer the questions. I acknowledge some of the points that you have made, but we will have to seek further advice on the matter. Thank you for your time and evidence this morning.

Stewart Stevenson: Thank you, convener.

The Convener: I suspend the meeting for a minute to allow a changeover of witnesses.

10:56

Meeting suspended.

10:58

On resuming—

The Convener: The next part of our discussion on the First ScotRail passenger rail franchise will be with Robert Black, the Auditor General for Scotland. He is accompanied by Barbara Hurst, director of public reporting at Audit Scotland; Angela Cullen, assistant director of public reporting; and Mark MacPherson, portfolio manager.

Last week, we heard from Dr Malcolm Reed, who made a number of comments about the process and the role of Audit Scotland. Somewhat unusually, we decided to invite the Auditor General and his team to respond to the committee. There are, I think, legitimate questions arising from the session that we had last week.

Mr Black, are there any preliminary remarks that you want to make?

Mr Robert Black (Auditor General for Scotland): It might be helpful to the committee if I quickly touch on the issues that arose in Dr Reed's evidence. I would be happy to answer the committee's questions on those issues, and this might help your consideration of them.

11:00

I echo the minister's remark this morning that many of the key findings in the report are positive, for example about the performance of First ScotRail. The report says that Transport Scotland is managing the contract effectively and that, as I told the committee in December, it used a rigorous

process to review the contract and to develop the options that led to the agreement of the extension. However, the report notes that there are some areas for improvement around consultation, the provision of information to stakeholders and some of the performance measures that are relevant to passengers and to the wider Government priorities. In the second part of the report, we also comment on the governance arrangements and suggest that some aspects of those arrangements could have been better.

If you do not mind my doing so, I think that it is important for me to restate the overall context and the high-level messages coming out of the report. In taking its evidence, the committee has, so far, concentrated on the governance arrangements. During last week's evidence session, Dr Reed expressed concerns about the content of the report and the information that I supplied to the committee. I have considered Dr Reed's comments carefully, and there are a few issues that I would like to clarify with you if I may.

In his opening remarks, Dr Reed mentioned the process of agreeing the facts in the report. The Audit Scotland team went through its usual procedure, and I assure you categorically that everything in the report is factually accurate. However, in his opening remarks, Dr Reed suggested that some issues were introduced late in the audit process. The only issue in that category relates to the shares and share options in FirstGroup that were held by the director of finance and corporate services. That was the only issue that came in relatively late in the process.

My report says that that information about the shareholding and share options was known to Transport Scotland. It is included in both its register of interests and its annual accounts. However, that interest was not drawn to the attention of the audit team who carried out the review. It would have been, frankly, much preferable for Transport Scotland to have alerted the team to the issue much earlier in the process. In his evidence, Dr Reed appeared to question whether the shareholding was a material interest. When the shareholding was drawn to my attention, I was in no doubt that it was an important matter of public interest that needed to be included in the report, and I instructed the Audit Scotland team to do that.

The second issue about which Dr Reed expressed concern was the business case. I remind the committee of what the report says. It says that Audit Scotland found that Transport Scotland used a rigorous process to review the options and that the team that was carrying out the review reported regularly to Transport Scotland's senior management. In short, senior management

were able to make decisions on the basis of full information supported by a rigorous procedure.

However, the report notes—as the committee has also acknowledged during its evidence sessions—that a fully documented business case was not provided to the minister. I will clarify the significance that I think should be attached to that. I fully acknowledge and accept the point, which was made by Sir John Elvidge to the committee, that ministers, suitably advised by senior civil servants, should be seen as the best judges of whether they have sufficient information to make a decision, depending on the circumstances. However, the First ScotRail franchise is a very big contract that is worth about £2.5 billion over the 10-year life of the contract. I am in no doubt that a fully documented business case should have been brought together to provide a clear basis for supporting the formal decision to commit a very significant amount of public funds. However, a fully documented business case was not readily available to the Audit Scotland team during the course of the audit.

The last issue that was raised by Dr Reed related to the role of non-executive directors in what was called the investment decision-making board. Again, I refer to the report, which explains the difference between Transport Scotland's board and the investment decision-making board, which supports the chief executive in making decisions. Transport Scotland's main board is an advisory body, not a legal entity. It is the investment decision-making board that makes the key decisions. The report notes that Transport Scotland agreed that its non-executives should not be part of the investment decision-making board and therefore should not be involved in the franchise review.

At last week's meeting, Dr Reed appeared to be concerned that, at the meeting on 10 December, I might have suggested to the committee that non-executives were excluded from the board. Having reviewed the *Official Report*, I can say that I did not use that term.

As I think I mentioned to the committee, as part of our work programme I have asked Audit Scotland to undertake a project that will look at the operations and procedures of boards across the whole of Government. I have asked it specifically to ensure that the review includes executive agencies and non-ministerial departments. Some interesting analysis might come out of that.

I have no further comments. Thank you for the opportunity to make my remarks. With my team, I am happy to do my best to answer any questions or concerns that you have.

The Convener: Thank you for that helpful clarification of the clearance process for the report.

For absolute clarity, I take you back to Dr Reed's comments. He said that, just before going to print, "significant further revisions" were made to the report that had not been discussed previously. Is that the case?

Mr Black: The only issue that arose was the matter relating to the shares and share options that were held by the director of finance and corporate services. That issue was not brought to the attention of the Audit Scotland team as they were doing the work; it emerged relatively late in the process when the team were doing the due diligence check of everything around the project. The team drew my attention to the fact that there was a declaration of interest accompanying the accounts. The Audit Scotland team discussed that with Dr Reed and his colleagues. I took the view that it was most certainly a material interest and therefore required it to be introduced into the report. It is factually accurate and the judgment to include it in the report was mine.

The Convener: So, had Transport Scotland made your team aware earlier of those facts, there would have been no need to make a revision to the report.

Mr Black: That is correct. Had the Transport Scotland people drawn the attention of the Audit Scotland team to the matter earlier on, it would have been in the draft report that went for clearance at an earlier stage and it would have been in the draft report that came to me.

The Convener: Once you decided to make the revision, was there any discussion with Transport Scotland about it?

Mr Black: Yes, there was. Barbara Hurst, the director of our performance audit programme, had conversations with Dr Reed and possibly some of his colleagues.

The Convener: How do you or your colleagues respond to the claim made by Dr Reed that Transport Scotland did not have the opportunity to engage fully with Audit Scotland on the matter?

Mr Black: I am satisfied that it had a full opportunity to engage, but I would be happy for Barbara Hurst to fill in the background to that more fully.

Barbara Hurst (Audit Scotland): Dr Reed is absolutely right that the late revision to the report concerned the shares and share options of the director of finance and corporate services. We discovered the situation late in the process when Mark MacPherson was reviewing Transport Scotland's annual accounts. I need to say to the committee that, when we discovered that, our immediate thought was, "We cannot publish a report without including this in the report." That was before we had spoken to the Auditor General.

We were all clear that it was a significant issue—I could rerun the movie of when we discovered it, but I will not do that because I am sure that members are not interested. It was so significant for us that we knew that we had to tell the Auditor General.

We told the Auditor General about it the next day and we agreed that I would need to go back to the chief exec to tell him what had come to light, that we needed to include it in the report and that we would give him the paragraph that we were going to include. Although it had not gone through the formal clearance process, he would have a chance to see what was in it. At that time, the chief exec asked me to deal directly with him on the whole issue, which I subsequently did.

The Convener: So, on Transport Scotland's behalf, the chief executive had a clear opportunity to have a discussion on that point.

Barbara Hurst: Absolutely. We had several discussions on that point. In addition, I alerted Dr Goudie's office to the fact that our report would include a paragraph that made reference to the shares and share options of Transport Scotland's director of finance and corporate services.

The Convener: Is Dr Goudie the accountable officer?

Barbara Hurst: He is director general for economy within the Scottish Government.

Murdo Fraser: I seek a little more clarity on this issue as—my wife is the auditor in our family—I do not fully understand the audit process. It would be helpful to hear a little more explanation on how the audit process works. At what point would one normally expect a client to disclose material information such as a shareholding? Barbara Hurst said that Mr MacPherson discovered Mr Houston's interest when looking at the annual report. Would one normally expect a client to be proactive in disclosing such material information to the auditors?

Barbara Hurst: Given that we thought that the shareholding was of such significance, we would have expected it to have come up very early in the day. Our initial meetings were with the director of finance and corporate services. We should remember that we were involved in an unusual project. When we kicked off the project, it was about the management of the rail franchise. Halfway through, we added in an objective about the rail franchise extension, which was announced while we were undertaking the audit. There were a number of occasions on which the interest could have been disclosed, but we picked it up only from the annual accounts.

Murdo Fraser: The point that I am trying to get at is this. In the normal course of events, would

one expect a client to be proactive in disclosing such a material piece of information?

Barbara Hurst: Personally, I think yes.

Mr Black: Let me just support Barbara Hurst on that point. The answer to that question is unequivocally yes. We expect audited bodies in Scotland to operate to the highest standards of governance, which they generally do. I would reasonably have expected the Transport Scotland team to draw our attention to such a significant matter, not least because I know that a number of the conversations and exchanges that took place with the Audit Scotland team were with Mr Guy Houston.

The Convener: Before I bring Nicol Stephen into the discussion, I want to clarify something. We have been told by Transport Scotland and by the minister that Mr Houston had no involvement in the franchise process. Why was Audit Scotland discussing a report on the franchise with Mr Houston?

Mr Black: As part of the process of undertaking an audit, the general practice in Audit Scotland is to have a point of contact—or perhaps a series of points of contact—with the audited body with whom the auditors can engage as they do the work. Mr Houston was one of the people with whom the audit team engaged.

Barbara Hurst: When we kick off an audit, the director of finance is often our initial starting point, just because that is the process—

The Convener: Before Barbara Hurst goes any further, let me say that I understand that that would be the normal process. However, we are not talking about a normal contract or a normal process. We are talking about a situation in which, according to Dr Reed, the individual was specifically excluded from the franchise process. If he had no part in the process and no knowledge of what went on, why was he involved in the discussion?

Mr Black: That question is best answered by Transport Scotland. As I hope we have indicated, we certainly had no knowledge of the director of finance's particular private interest in the issue. That would certainly have affected how we suggested to the Transport Scotland team that they should engage with the auditors.

The Convener: I think that we need to follow that up with Transport Scotland, but—

11:15

Barbara Hurst: I should clarify that, after the discussion with the director of finance, he immediately passed us on to the people from whom you have taken evidence: the rail franchise team dealing with the issue.

The Convener: Okay. Did he at any point say anything about his shareholding?

Barbara Hurst: No.

Nicol Stephen: Convener, as your questions have covered the issues that I wanted to begin by asking about, I will ask a couple of follow-up questions. With the benefit of hindsight—or at least with the benefit of the knowledge that you now have about Mr Houston's shareholdings—do you think that it was appropriate for him to be involved in the initial meetings?

Barbara Hurst: That is a hard one to call. We would have expected Mr Houston to have said something at that point. As I think Mark MacPherson can confirm, he was not involved in the detailed discussions that were undertaken as part of the audit.

Mark MacPherson (Audit Scotland): That is correct. We had no real dealings with Guy Houston beyond the very initial meetings.

Nicol Stephen: So there were several meetings.

Barbara Hurst: During an audit, there are lots of meetings with different individuals.

Nicol Stephen: But there were several meetings with Mr Houston.

Mark MacPherson: I am not sure that I can offer you a certain answer to that, because I was not directly involved at that stage. There might have been one meeting; there might have been a couple. I can say for certain that Mr Houston was not involved in the meat of the process.

Nicol Stephen: Given that Mr Houston attended at least one of the meetings, given that you, as auditors, were unaware of his investments in FirstGroup, and given the adjustment that you made to the report—which you say was the only substantive change that was made and was not one of a series of changes—were you shown during the final stage in the process or have you since been shown the conflict of interest arrangements that Transport Scotland put in place as a result of Mr Houston's shareholding?

Barbara Hurst: I refer the member to paragraph 71 of our report. In my conversations with Dr Reed, I explained the significance of the issue and why we felt that it needed to go into the report. I asked him about the arrangements that Transport Scotland had in place to ensure that the director of finance and corporate services was not involved in the decision making. I realise that English is a very rich language, but we were very careful with the language that we used to reflect that in the report. You should remember that we were at a late stage of the process; we made it clear that the issue had to go in and Dr Reed told me about the systems

that Transport Scotland put in place. In paragraph 71, we very specifically used the phrase

“Transport Scotland’s chief executive has stated that”.

We have not gone back on that. Indeed, I do not think that we could have done so. For example, although we knew from some of the minutes of the meetings that the director of finance and corporate services had attended them, we did not know what happened at those meetings.

Nicol Stephen: Did you see a written version of the arrangements, or did you receive only a verbal explanation of them from Transport Scotland?

Barbara Hurst: It was a verbal set of arrangements. It might well have been included in some of the e-mail traffic—I do not remember—but we did not see a formal document. *[Interruption.]* Sorry—my colleague has just reminded me of the register of interests, which is the key document.

Nicol Stephen: As you probably understand, I am looking beyond the register of interests, which is what triggered the knowledge, to the next stage. What action did the agency take with regard to this interest? Was it set down in writing for you, or was it simply explained to you verbally by the head of Transport Scotland?

Barbara Hurst: I will unravel that a bit. The issue was verbally explained to me by the chief executive of Transport Scotland. We have not seen a formal document saying, “This is the arrangement,” but I am not saying that such a document does not exist.

Nicol Stephen: I understand that. We asked for that document last week and were told that we would be given it. I am just trying to clarify that it was never shown to you as part of the audit process.

Barbara Hurst: No, but you must remember that we raised the issue with Transport Scotland pretty late on in the process.

Nicol Stephen: I understand that and the explanation that you have given.

Murdo Fraser: I seek some clarification to ensure that we are absolutely clear about all this and that it is on the record. Is it the case that, until Mr MacPherson came across the reference to Mr Houston’s interests in the annual report during his stage of the audit process, the information had not been drawn to your attention by anyone in Transport Scotland—and specifically not by Dr Reed?

Barbara Hurst: Yes, that is the case. What I have learned from this experience is that I should pay a bit more attention to organisations’ annual reports, which, I have to say, I do not drill down into in great detail when they cross my desk.

The Convener: When you discussed with Dr Reed the late revision to the report, did he think that the comment should be included, or was his preference that it should not be put in?

Barbara Hurst: I remember that I did not want to make the phone call because, as you will appreciate, I knew that the conversation was going to be difficult. However, it was not as difficult as I had expected; I think that Dr Reed understood where we were coming from. You will need to ask him whether he would have preferred the comment to have been put in or left out.

The Convener: But he did not express any preference to you.

Barbara Hurst: Not at that stage. Later on, he said to us what he said to the committee, which was that he did not think that this was a material issue.

The Convener: He indicated to you that, as he did not think that it was a material issue, it should not be included.

Barbara Hurst: I think that he was very keen for the wording to be very precise if we were going to include it. I understood his reasons for that, which is why we shared the wording with him.

Willie Coffey: My questions are on the same theme, as it is of concern to members. The role of the director of finance and corporate services is discussed in paragraphs 70 and 71. I realise that you have probably answered this question many times now, but did Transport Scotland receive the text of those paragraphs for its response, or was there simply a discussion of the issue?

Barbara Hurst: I can categorically tell you that Transport Scotland got those paragraphs. I sent them directly to the chief executive by e-mail and received a response acknowledging that e-mail.

Willie Coffey: That clearly raises an issue, convener, because Ms Hurst’s response conflicts with what Dr Reed said last week. I should say, though, that Dr Reed was not specific or clear about the issues that were being raised at a late stage; he simply said that significant issues were raised at a late stage that he had not been given an opportunity to discuss. If this was not one of those issues, what were they?

Mr Black: On a general point, the procedure that I expect Audit Scotland to follow—and which has stood the test of time and received the support of the Public Audit Committee and the former Audit Committee ever since we started in this business—is that a draft of a report, including all the key findings, goes to the accountable officer no less than three weeks before we want to commit to publication. In other words, accountable officers have three weeks to consider the report. We also try to ensure that there are no surprises.

The department, the agency or the organisation in question has a general indication of how the process is moving along, which should make the clearance process easier.

The important point about the clearance process is that it is essentially about confirming matters of fact. I take personal responsibility for the findings that come out. We are clearly willing to take into account the thoughts, views and preferences of the accountable officer and the team on the wording but, at the end of the day, I also sign up to the wording in the report. After all, it is my report, so it is my wording. However, we give accountable officers the opportunity to comment, which is what happened in this case.

I am satisfied that the Audit Scotland team handled the issue properly right to the end. As Barbara Hurst said, the chief executive had the opportunity to see the wording that is in the report. I think that the wording is accurate, true and fair.

Willie Coffey: Helpfully, Audit Scotland always produces a summary document as well as a main document. I see the issue discussed in paragraphs 70 and 71 of the main document—I mentioned them a moment ago—but I see no mention of it in the key messages in the summary document. Is there a reason for that? Was there a timing issue?

Mr Black: It is always difficult to get the right balance in an executive summary. Over the years, we have found that people welcome the publication of an executive summary, but it tends to be more challenging to produce one when we are considering matters of governance.

The degree of attention that is given to the issue in the main report reflects the fact that, although I was convinced that we had to mention the issue clearly in the report, its significance in relation to the high-level messages was that there was no evidence of anything improper, that robust procedures had been followed, and that decisions had been taken on the basis of proper information. That is the high-level message that we included in the executive summary.

Nothing has been suppressed. I made a point of drawing your attention to the matter in the presentation that I gave you when I introduced the report.

Andrew Welsh: Audit Scotland has a duty to report all significant issues to the Public Audit Committee and to Parliament without fear or favour. The case that we are discussing is a surprise because, for the first time, basic facts are being questioned by the audited organisation. Audit Scotland has always been involved in a two-way, detailed process with the organisations that it audits, and its reports are always produced with great care about the wording. Perhaps the case is

a wake-up call for us to remember what the committee and indeed Audit Scotland are about. To my mind, important issues have been raised, including the accuracy and efficacy of the advice that is given to ministers and the Government and openness in decision making.

A fundamental concern is whether the business case was fit for purpose. I seek Audit Scotland's advice about that. Did adequate criteria exist in the business case? Was the process that was used to develop the criteria sufficiently robust? Were the criteria—and any approval of them by Transport Scotland—sufficiently well documented? Those questions go to the heart of what we are all about, which is seeking best practice and value for money.

Mr Black: I ask Angela Cullen, who is closer to the detail of the audit, to answer that.

Angela Cullen (Audit Scotland): As we say in paragraph 68, the original contract did not specify the criteria. Transport Scotland told us that criteria had been established and approved, but we could find no formal record of who had approved the criteria or when.

Mark MacPherson: I will add a little more detail on that. There is clear evidence from our review that criteria were developed. All that we are saying is that it is not clear at what stage and by whom they were approved. That fits in with our assessment that there was a rigorous appraisal process and that management had all the information that we considered they would need to make the decisions that they made.

Andrew Welsh: There are lessons for us, lessons for the Government, and lessons for every organisation that is audited by Audit Scotland about the standards of conduct that we should all expect in looking for best practice and value for money. Our ultimate duty is to the public of Scotland.

I do not have a question, but I wanted to make that statement.

George Foulkes: The minister and all our witnesses from Transport Scotland said that all Mr Houston's involvement was post hoc—after the event—so why are you worried about it?

11:30

Mr Black: Dr Reed has given us assurances that Mr Houston did not take part in the vote on the project—I think that that was the phrase he used. Given the insufficiency of the records, on the basis of the evidence available to us, the audit team cannot provide a positive assurance on that.

George Foulkes: Why do you not accept Dr Reed's assurances?

Mr Black: Because it is the nature of the audit process for us to proceed on the basis of the evidence that is available to us. That is the robust basis on which all our work is undertaken. I am not sure whether you have the report in front of you, but exhibit 10 on page 20 sets out the project's timeline. We know for a fact—because it is documented—that on 19 March, Transport Scotland agreed the proposal to seek ministers' views and that Mr Houston was present at that meeting. I understand from the briefings that I have had from Audit Scotland that, prior to that late stage, the documentation was not all that it should have been. Therefore, we do not have a reliable record of which meetings took place, which of them Mr Houston was present at, or what role he played. As I record in the report, we have had to rely on the assurance of the chief executive, Dr Reed, on those matters.

George Foulkes: The committee was caught somewhat flat-footed, because we pressed very hard on the impropriety of Mr Houston's involvement, and we got repeated assurances from Dr Reed that Mr Houston was not involved in any way in any of the material decisions, the vote or any considerations, and the minister backed that up. Are you still worried—because you, as auditors, do not have the evidence—that Mr Houston may have been involved?

Mr Black: I am afraid that I must say that I have nothing to add, because we have stated all we can on the basis of the facts that are available to us. We have also recorded the advice that we received from Dr Reed on the matter.

George Foulkes: Are we therefore justified in being suspicious about this, given the nature of Mr Houston's departure from Transport Scotland?

Mr Black: That is a judgment that you must make in light of the difference of view that exists between Dr Reed and me about the material significance of the shareholding that Mr Houston had at the time.

George Foulkes: The other issue that we pursued strongly was the business case, to which my colleague Andrew Welsh has just referred. We had some discussion about the difference between a business plan and a business case—which I did not quite understand. Stewart Stevenson made a convincing argument today that he was involved in a whole process, that he was being briefed continually and that, therefore, when the final decision-making meeting—as he called it—took place, he did not necessarily need to have a business case document. Is that not a valid defence from the minister?

Mr Black: Absolutely. I fully accept that. I think I said in my opening remarks this morning that I fully accept the position taken by Sir John Elvidge

at your previous meeting, which is that it is for the minister to determine what information he or she feels is absolutely necessary to take a decision. However, as we have all said this morning, the contract is very large indeed—it is one of the biggest contracts in Scotland. It is worth up to £2.5 billion and the extension alone was worth about £900 million. Therefore, I think it entirely reasonable to expect, at an early stage in the process, but well after the ministerial decision had been taken and the contract had been announced, that the Audit Scotland team would be immediately offered a document that contained the full business case.

It is essential that a contract of this magnitude is underpinned by clearly documented material that brings everything together in the form of a business case that sets out the aims and objectives, the options being considered, the evidence base used to assess the options and the financial management arrangements. I would expect to see the business case supported by a documented risk assessment, with an indication of how the contract would be terminated in the public interest, if it required to be terminated early. There must also be a clear plan of how the project should be monitored and evaluated. Not for a moment would I necessarily expect a minister to go through all that, but I would expect that, when the auditor comes along some time afterwards, such a document would be readily available to them. However, that was not the case.

George Foulkes: I have a final question. The minister did not understand, and I had no further time to pursue the question because he had to disappear—allegedly—to give evidence to another committee immediately, but—

The Convener: No, he did.

George Foulkes: Well, I have just had a look at the timetable. Let us find out when he actually gave that evidence before we conclude on that either way.

Our perception is that Transport Scotland is different from other civil service departments that have boards, votes and that kind of thing. However, I am beginning to wonder whether that is fiction, because it seems that all the decisions that we hear about are made by Sir John Elvidge, or go up to him because he has responsibility and then go to the minister, just in the way that they would go from a health directorate or another directorate.

A new chief executive has just been appointed to Transport Scotland—David Middleton, who was head of the Scotland Office—through a normal civil service process. There seems to be a move away from the kind of business operation through which Malcolm Reed was brought in from the

outside. Does that not indicate that there has been a change in the nature of Transport Scotland and that it is reverting to being increasingly just a normal civil service department?

Mr Black: I am sorry, but I do not think that I can help the committee with that. The audit did not look more widely at those issues.

I will expand on my previous answer and say again to the committee what I have said several times. Although the documented business case was not brought together in one place so that the auditor could sit down and examine it, at the end of what was a really challenging and complex audit examination, the team was satisfied that, having reviewed lots and lots of paperwork, in totality it was a robust process that was based on sound analysis and appropriate evidence.

The Convener: Just before I bring in Nicol Stephen, can I clarify something that you said? You mentioned a meeting on 19 March.

Mr Black: Yes.

The Convener: When was the actual deal struck, to use Dr Reed's phrase?

Mr Black: Our report records that the minister approved the extension on 27 March. There was a meeting the day after of the investment decision-making board to confirm the extension.

The Convener: I just want to clarify something. Dr Reed said that Mr Houston was a participant only at a very late stage in the process. He attended two meetings after the deal had been struck, one of which was to discuss handling the contract. The second meeting was held after ministers had taken the decision to proceed with the extension. Was the meeting of 19 March held before the deal was struck and before the decision was made?

Mr Black: I ask Angela Cullen and Mark MacPherson to help you with that. I believe that they might also wish to say something about my earlier comment.

Angela Cullen: I will clarify the earlier comment. Going back to the minister's evidence this morning around on-going dialogue with ministers throughout the process, I do not dispute that that happened. My point of clarification is that, again, Transport Scotland did not inform us of that or provide us with any evidence that that had happened.

Mark MacPherson: That was my understanding of the internal process in Transport Scotland. Notwithstanding Dr Reed's comments at last week's committee meeting, my understanding is that the relevant members of the senior management team had been involved throughout the process and had been given documents and

information throughout to allow them to make a decision at the end of the process, without necessarily having to have a huge pile of papers in front of them. Therefore, they had done all the work up to that point.

The Convener: I return to the issue of the status of the meeting of 19 March. Was that before the deal was struck?

Angela Cullen: Our understanding is that the minister approved the extension at the presentation that was made to him on 27 March.

Mr Black: The report, including the exhibits, has been cleared factually with Transport Scotland.

The Convener: So Dr Reed may have been mistaken when he told us that Mr Houston attended two meetings after the deal had been struck.

Barbara Hurst: Mr Houston may have attended those meetings, but we know from the minutes that the director of finance was at the meetings of 19 and 28 March.

The Convener: Okay. We need further clarification of whether Mr Houston was involved in any meetings to discuss the issue before the deal was struck and, if so, why.

Another issue has come up in your contributions, Mr Black. You used the word "vote". Is there any evidence of whether Mr Houston participated verbally in any of the meetings?

Mr Black: My understanding—I am sure that my colleagues can assist you further—is that the phrase

"the director of Finance and Corporate Services has no vote on any decision-making relating to FirstGroup"

was cleared specifically with Dr Reed. He intimated to us that such language was appropriate.

The Convener: So it is possible that, notwithstanding the fact that Mr Houston did not vote, he may have participated in the discussion and contributed to the meeting.

Barbara Hurst: It is possible, but we do not know that from the minutes. We know only that he was there.

The Convener: The minutes provide you with no evidence. We need to clarify the matter with Transport Scotland. It is unfortunate that its minutes do not record whether Mr Houston participated in the meeting, but that is as may be.

Nicol Stephen: Angela Cullen clarified the process of briefings in Transport Scotland, which kept individuals informed of the progress of the extension negotiations. You suggested that that information was provided to ministers and senior officials. Is that correct?

Mark MacPherson: No. My understanding is that the process was internal to Transport Scotland. It was not brought to my attention that there was on-going engagement with ministers. I was aware—as Transport Scotland indicated last week—that Transport Scotland had briefed the new Administration when it came into office and had made presentations to ministers in December 2006 and March 2008. Other than that, I was not made aware of on-going dialogue that may or may not have taken place.

Nicol Stephen: The minister referred to such on-going dialogue this morning. Is that your recollection?

Mark MacPherson: I was not made aware of that.

Mr Black: It is important to distinguish between information that was supplied to us and the assurance that you have received from the minister. All that we are saying is that Transport Scotland did not advise the Audit Scotland team explicitly of what may have been done as the weeks and months rolled by to keep the minister in touch with developments. We would not necessarily expect it to provide us with that level of detail.

Nicol Stephen: So you do not know whether communications were recorded; if they were, the information was not provided to you. Is that a fair summary of the position?

Mr Black: That is correct, but I urge you to be cautious about attaching too much significance to the issue. It is probable that senior civil servants brief ministers regularly on all sorts of matters. There would be no difference from any other major on-going project in that respect.

Nicol Stephen: Indeed. I understand that regular verbal briefings are absolutely normal. I just wanted to clarify the issue of recording and what information was provided to you.

The second issue that I will ask about is confidentiality. As you said, we are talking about a £900 million contract extension. Transport Scotland and the minister referred to the importance of confidentiality and to market sensitivity to knowledge about the contract extension negotiations. Did you discuss that with Transport Scotland? Do you understand the confidentiality argument and the reasons for it?

11:45

Mr Black: I did not discuss the matter with Transport Scotland, other than in the context of the initial announcement that the contract would be extended. The committee has asked me whether I knew about the extension before the announcement and I have said that I did not.

The significance that is attached to commercially sensitive issues in the contract is a matter for Transport Scotland's professional judgment. We are not in a position to second-guess or challenge that judgment.

Nicol Stephen: The minister came up with the concept of post hoc consultation. Every committee member prefers prior consultation, if that is possible and appropriate. We need to understand better whether openness and transparency about the contract extension might have been possible. You say that you feel unable to give direct advice on that.

Mr Black: That is correct.

Nicol Stephen: To enable us to respond more authoritatively, could we obtain advice on that from another source?

Mr Black: I do not wish to dissuade the committee from doing so, if it feels that that is essential, but whether financial sensitivities require to be observed is a matter of judgment on the basis of the best professional advice. Unfortunately, we cannot advise you further.

Nicol Stephen: On market sensitivity, if disclosure and consultation had occurred, and if consideration of extending the contract with FirstGroup had been announced to the stock exchange, could the process have been adequately managed and appropriately defended?

Mr Black: I am not sure whether I am in a position to help you. If I were in such a situation, I would wish to take the best advice that I could before making the decision. The answer depends on the circumstances.

Nicol Stephen: My final point is perhaps the most important. Andrew Welsh was right to emphasise that the issues are serious and important. Was any aspect of the evidence that we heard last week misleading or inaccurate?

Mr Black: I simply refer back to my opening statement this morning. The report is accurate in all factual respects. There might have been two or three issues of emphasis and interpretation that I required to correct but, beyond that, I have nothing to add.

James Kelly: The meeting on 19 March is crucial to determining Mr Houston's involvement. The minister told us that Mr Houston's involvement post-dated the agreement on the franchise extension, but we have established that Mr Houston attended the meeting on 19 March. Transport Scotland's chief executive said that Mr Houston did not vote in any part of the process. How do the minutes that Audit Scotland has seen record any decisions that were taken on 19 March? Does a record exist of who had a vote at that meeting?

Mr Black: I ask the team to help.

Mark MacPherson: There is no record of any vote. The decisions that were made were reflected in terms of action that was to be taken.

Stuart McMillan: Paragraph 73 in the report makes the point that Transport Scotland did not take external advice on the contract extension. Mr Black, your office has produced many reports in the past eight or nine years. Do you have examples of other public bodies securing advice from external sources before major decisions were taken to spend public money?

Mr Black: There are many, many projects in which decision takers in Government seek, and might rely on, expert advice from outside the organisation. In relation to paragraph 73, I recall Dr Reed saying to the committee that he felt that there was no need for separate advice, because he had many years of experience in the business. He was clear in his mind about the commercial sensitivities relating to the contract extension. I must acknowledge that that is his professional judgment and I do not wish to take issue with it.

Stuart McMillan: I fully respect Dr Reed's experience and background and agree that the judgment was for him to make. However, bearing in mind the cost implications for the public purse and the size of the project, personally, I think that it might well have been a good idea to take external advice. Can Audit Scotland point to another project in the past eight or nine years in which a public body has taken external advice before committing to major expenditure of public money?

Mr Black: I cannot help you with that one. We must realise that the contract is fairly unique, as it is a service provision contract that is worth £2.5 billion, which is different from most other contracts. I offer one additional thought, which is that, in Transport Scotland, there is a great deal of expertise in that field. At last week's meeting, one of the people supporting Dr Reed discussed Transport Scotland's concerns about the impact that knowledge of the contract process might have had on FirstGroup's share price and how that might have made it more difficult to negotiate the best deal for the public sector. I have to respect that view and I have no comment to make on it.

Willie Coffey: I return to the issue of a business case or plan. You have said several times that you did not see a business case or plan. Is that correct?

Mr Black: That is correct. When the Audit Scotland team engaged with Transport Scotland in the early stages, although after the contract had been let, Transport Scotland did not offer to Audit Scotland a fully documented business case brought together between covers that would

explain, in the terms that I have outlined, everything from the aims and objectives through to a plan of how the project should be managed. I know from the team that it took a considerable amount of work to analyse the process and reach our finding, which is that the process was robust and based on good evidence.

Willie Coffey: I am coming to that. If you did not see a business case, what led you to the conclusion that a rigorous process had been gone through? What paperwork did you see that led you to that conclusion but then to comment that a business case or plan should have been presented? What would have been the difference, if rigour had been applied—

Mr Black: I will answer the second part of the question, and I must repeat what I said earlier. For a contract of this magnitude, there is absolutely no doubt that good practice requires the agency to have a documented business case, brought together in one place, which an auditor could sit down and examine. In this instance, that was not done.

However, a great deal of work was undertaken by the Audit Scotland team to examine all the documentation that was available in order to provide the analysis and findings that are contained in my report. I invite the team to come in on that point.

Mark MacPherson: I go back to what the report says about the provision of the business case to ministers. Notwithstanding the comments that I made earlier about whether we were aware of the on-going dialogue, when we undertook the review we were, ultimately, provided with a range of documents that, when taken together, could provide us with assurance. They reflected all the issues that the Auditor General spoke about earlier, and on which Transport Scotland made some points last week. All the information was available, but it would have been very helpful to us to have had it available in a single volume, instead of having to spend time putting it together.

Willie Coffey: That is what I am trying to get at. All the information was available. Are we arguing about whether it was all clipped or stapled together in a document? Was there actually anything missing? It seems to me, from what everyone has said, that there was a sufficiency of preparation and analysis of information—it just was not clipped together in a single document. Are we splitting hairs about that?

Mark MacPherson: I repeat what we said in our report: there was a rigorous process, which was backed up by a great deal of evidence. We said that a single document was not provided to the minister.

The Convener: Could Mr Black comment on that point from Willie Coffey about splitting hairs? You emphasised earlier that you accepted that rigorous work had been done.

Mr Black: That is correct.

The Convener: You also emphasised, however, that, from an audit perspective, it would be best practice to have a business case put together. Do you think that it is a matter of splitting hairs?

Mr Black: No, I do not. For a contract of such a magnitude, it should be possible, after the event, for the auditor to go in and look at the documented business case containing all the critical information—the aims and objectives, the options that were being considered, the evidence that was being used to develop those options, the financial management arrangements, the risk management arrangements, how the project was to be monitored and implemented, and the exit strategies. That would be best practice. Perhaps that is a high test, but I am in no doubt that, in order to safeguard the proper use of public funds, the expectation was not unreasonable.

Willie Coffey: I think that you are saying that such a business plan does not exist. What on earth, then, was the rigour that was derived from the process? You have said that a rigorous process was gone through. Were processes not carried out? Whether multiple documents were presented is neither here nor there as far as I am concerned. In your view, were any actions or processes that should have been carried out not carried out? For example, was a risk assessment not carried out?

Mark MacPherson: I reiterate the point: as we have said, a business case was not provided to the minister. Dr Reed said last week that a business case was “available”. However, it was not made available to us at the point of our review. Therefore, we had to draw the information from a range of other documents, which, had they been placed together, could have constituted a business case.

The Convener: I intend to draw the discussion to a close there. For the record, the minister started his evidence to the Local Government and Communities Committee at 11 o'clock, which was immediately after he left here.

I thank the witnesses for giving evidence. We will return to the matter later on our agenda.

Section 23 Report: Response

“A performance overview of sport in Scotland”

11:59

The Convener: Item 3 is a response from the accountable officer on the Auditor General for Scotland's section 23 report, “A performance overview of sport in Scotland”. There are no comments or questions from members. It is a fairly useful response and, if no one is otherwise minded, I suggest that we simply note it.

Members indicated agreement.

The Convener: With that, I close the public part of the meeting.

11:59

Meeting continued in private until 12:43.

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