PUBLIC AUDIT COMMITTEE

Wednesday 25 February 2009

Session 3

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PUBLIC AUDIT COMMITTEE
4th 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 ALSO ATTENDED:

Mr Robert Black (Auditor General for Scotland)
Nick Hex (Audit Scotland)
Barbara Hurst (Audit Scotland)
Mark MacPherson (Audit Scotland)
David Watt (KPMG LLP)
Kirsty Whyte (Audit Scotland)

CLERK TO THE COMMITTEE

Tracey Reilly

SENIOR ASSISTANT CLERK

Joanna Hardy

ASSISTANT CLERK

Jason Nairn

LOCATION

Committee Room 5

Scottish Parliament

Public Audit Committee

Wednesday 25 February 2009

[THE CONVENER *opened the meeting at 10:04*]

Decision on Taking Business in Private

The Convener (Hugh Henry): Welcome to the fourth meeting in 2009 of the Public Audit Committee. I ask members to ensure that all electronic devices are switched off. I welcome to the meeting members of Audit Scotland, the press and the public.

This will be the last meeting that Stuart McMillan attends before moving to pastures new. I thank him for his contribution to the committee and wish him good luck in his new abode.

Stuart McMillan (West of Scotland) (SNP): Thank you, convener. I thank all committee members, past and present, for their assistance over the past 22 months, which have been an interesting period. There have been some funny moments—it has not all been dull. [*Laughter.*] It is audit, after all. I offer particular thanks to the clerking team. Sometimes the work that the clerks do—not just for this committee, but for all committees—goes unnoticed.

Finally, I thank the team from Audit Scotland. My colleague Andrew Welsh speaks highly of Audit Scotland at practically every meeting of the committee, and his comments are extremely valid. The work that Audit Scotland does for the public in this country is first class. Its reports ensure that there is now more scrutiny of where the public pound goes. The Parliament would be a duller place if we did not have Audit Scotland.

The Convener: Thank you. It is good to know that there are shafts of interest to brighten up the tedium in your life from time to time. No doubt Anne McLaughlin will be expected to continue your sterling work of picking up typographical errors—someone will have to assume that responsibility.

Do members agree to take in private items 6, 7 and 8 on our agenda?

Members *indicated agreement*.

Section 23 Report

"Asset management in the NHS in Scotland"

10:07

The Convener: Item 2 is consideration of a section 23 report. We will receive a briefing from the Auditor General on the report "Asset management in the NHS in Scotland".

Mr Robert Black (Auditor General for Scotland): With your agreement, convener, I invite Barbara Hurst to introduce the report.

Barbara Hurst (Audit Scotland): My challenge is to make asset management less than dull for Stuart McMillan's last meeting.

Our report on asset management in the national health service was published in late January. The NHS's main assets are land and buildings, information technology, medical equipment and vehicles. In 2007-08, the health service held assets worth almost £5 billion, of which the estate made up around four fifths. There is significant investment in those assets—£3 billion is planned between 2003 and 2011.

The report looks at three issues and is especially concerned with the importance of managing assets well. First, it focuses on the strategic role that the Scottish Government health directorates play. Secondly, it examines how the health service is planning and managing its assets. Thirdly, it looks in a bit more detail at the estate, because that accounts for four fifths of the value of the assets.

The health directorates are responsible for overall policies and guidance on the management of assets and for monitoring how those are implemented locally. There are a collection of policies and guidance on the estate, IT and medical equipment, but some of them need updating. There are no national policies or guidance on vehicle management. That is an issue, given the number of vehicles that are used in the health service.

National monitoring of the way in which bodies manage their assets is limited. There are some mandatory performance measures for the estate, and NHS bodies are required to produce estate strategies that are updated annually. However, there is no routine collection or monitoring of those performance measures and strategies.

The oversight of major capital projects—those above £5 million—is more rigorous, with detailed reviews of business cases for major capital investment. NHS bodies are required to undertake post-project reviews and post-occupancy evaluations to assess whether projects have achieved their objectives, but there is no checking of whether reviews have been done.

Part 2 of the report examines how the health service is working with other partners to develop the public sector estate as a whole. At the time of our review, only NHS Grampian had a joint estate strategy with its public sector partners, although 12 other bodies had strategies in development.

I move to part 3 of the report. Local asset strategies should link with clinical strategies to ensure that assets are in place and properly maintained to support the delivery of health care. However, we found that only five NHS boards have comprehensive asset strategies that are explicitly linked to their clinical strategies. Most of the other boards have strategies for their estates and IT, but fewer have them for medical equipment and vehicles. Most bodies also have basic information on their assets, but they are less likely to know the maintenance needs or conditions of the assets.

Given the value of the estate, we looked at estate management in more detail. Based on information from 11 boards, we found that the majority of the estate is of satisfactory quality, although just under a third will require major upgrading in the coming years. That is not surprising, given the age profile of the estate, which is shown in exhibit 12 on page 21 of the report. Exhibit 14 on page 23 provides a more detailed breakdown of the quality of the estate against four key criteria, including physical condition.

We found that the health estate has a maintenance backlog of in excess of £512 million. That figure is likely to be an underestimate, because it excludes NHS Greater Glasgow and Clyde and NHS Western Isles. Exhibit 17 on page 25 shows that the amount that NHS bodies spend on maintenance of the estate that they own—as opposed to private finance initiative-funded estate—varies, but we found no direct link between the amount that NHS bodies spend on maintenance and the size of their backlog. We also found little evidence that NHS bodies are budgeting to meet the long-term planned maintenance costs of the estate, otherwise known as whole-life costing.

Not all the estate meets disability discrimination legislation requirements. That is a particular challenge, given the age of some of the estate. We found that all NHS bodies consider equality and diversity issues when planning and implementing capital estates projects, but that does not always include consultation with people with disabilities.

As usual, we are happy to answer any questions that members have.

The Convener: Thank you. In paragraph 11 of your key messages report, you highlight the fact that

"Five NHS bodies did not know the condition of their medical equipment."

Is that not rather worrying?

Barbara Hurst: It is very worrying. Several years ago, we published a report on medical equipment and made a number of recommendations, a key one being that NHS bodies need to know where their equipment is, what condition it is in and what the maintenance programme is. The finding to which you refer is not good.

The Convener: Despite what you said to health boards previously, five health boards still do not know the condition of their medical equipment.

Barbara Hurst: That is correct.

The Convener: We will want to reflect on that.

Murdo Fraser (Mid Scotland and Fife) (Con): I will continue the convener's line of questioning. Exhibit 10 on page 19 shows whether information is held electronically, in paper records or not at all. The bar chart for vehicles suggests that one NHS body has no record at all of the number of vehicles that it holds. Is that correct?

Barbara Hurst: Yes.

Kirsty Whyte (Audit Scotland): The figures for each category do not always add up to the total number of boards, because not all boards responded to all questions.

10:15

Murdo Fraser: But the left-hand side of the "Vehicles" table in exhibit 10 shows that 16 NHS bodies hold their records electronically, none has paper records and one has no records at all. It seems utterly extraordinary for an NHS board to have no records of the number of vehicles that it has, nor of their location—not to mention information on their condition, replacement plans or work that has been done on them. It seems extraordinary for a public body to run a vehicle fleet without having any records about it. I am not missing something, am I?

Kirsty Whyte: The one body concerned is the national waiting times centre, which does not own an awful lot of vehicles. It might be that it did not answer the question.

Murdo Fraser: Ah—okay.

The Convener: Which were the five NHS bodies that did not know the condition of their medical equipment?

Kirsty Whyte: They were NHS Fife, NHS Shetland, NHS Tayside, the state hospital and the Scottish Ambulance Service.

Andrew Welsh (Angus) (SNP): The fact that NHS bodies did not know the condition of their medical equipment strikes at the heart of treatment. Surely tracking and monitoring are required to solve the problem, and nowadays those have to be done using IT facilities. Is there any indication that action is either likely or imminent on those issues? Do action plans exist, or are they being planned? In other words, what will be done about the situation?

Kirsty Whyte: A national e-health strategy was published just last year, and I know that boards are working with the Government to develop the initiatives that were contained in it around information management and technology. That includes the monitoring of equipment, patient records and the use of different software.

Andrew Welsh: So the issue is recognised and is being looked into.

Kirsty Whyte: Yes.

Barbara Hurst: We will be following up work that we have done on IM and T. We will consider the matter in the work that we do this year.

Willie Coffey (Kilmarnock and Loudoun) (SNP): One of the very positive opening comments in the Audit Scotland summary recognises the tripling of the investment that is coming along. Given members' comments so far, I think that we have a golden opportunity to correct some practices and ensure better practice for the future.

One or two of the comments in your report stick out. First, there does not appear to be any correlation between the condition of the estate and the amount that is spent on it. A further comment was that the overall percentage of spend on maintenance is actually decreasing. Those are worrying trends, if they are allowed to continue. However, I am pretty confident from the report before us that, once it is shared with the NHS throughout Scotland, we will begin to correct some practices.

I see that one of my old favourite issues has appeared yet again; I refer to the recurring theme of post-project evaluation—or the lack of it—which can be used to learn and share good practice. That has been a recurring message at the Public Audit Committee. Why should that be? Is it something that the public sector is just not very good at? I suppose that the answer to that is yes. What can the Audit Scotland team say about ensuring that that theme is taken up far more seriously in the future?

Barbara Hurst: We expected you to ask about post-project evaluation, partly because of our major capital projects report in which that came through as a theme. We do not know whether the health service is not routinely doing such evaluation, but we know that it is not monitored. We genuinely do not know whether the NHS is doing that or not. However, the issue is important, because it concerns health care facilities and we need to evaluate whether they are meeting needs. I think that Kirsty Whyte will support me on this: there is a lot of evidence that, if buildings are well designed, that can enhance the health care experience. We want to pick up on that with the Scottish Government health directorates to ensure that such evaluations are happening across the health service.

Willie Coffey: That is very encouraging. I am similarly encouraged and delighted to see that you have picked up the north-west Kilmarnock area centre as a case study on page 13. Located in my own dearly beloved Kilmarnock, the centre is a fantastic resource for the community, which combines lots of health services with housing, community and police services all under the one roof. It is a fantastic example and I am certain that, should the committee wish to see examples of good practice, it would be made very welcome down in Kilmarnock. It is lovely to see that resource being recognised. Although I recognise the comments that were made about the lack of post-evaluation analysis, I am certain that the work that is being done in that centre is delivering positive results for the community.

Mr Black: That is a good example of why we include case studies in the report. We would expect such a report to be read carefully and seriously by board members and senior officials. Other boards should be interested in a case study like the one that has just been mentioned and would want to explore whether there is anything that they can learn from it.

Stuart McMillan: Paragraph 17 of the key messages report says that

"Almost a third of the estate will need major upgrading soon",

and recommendation 5 in that document talks about the new hub initiative. When more information comes to light and more proposals are signed off in the future, will you do any further analysis work to ensure that any developments that take place are of the highest order?

Barbara Hurst: We will probably follow that up in about 18 months or a couple of years, to give the recommendations a chance to bed in. There are also some issues coming up through the annual audit process around capital investment, which we would be likely to highlight in our overview report on the health service.

Nick Hex (Audit Scotland): We highlighted the fact that there is a lack of performance information. The development of the performance management system that the Government is committed to producing this year should help in that regard, as it will standardise the information that is available across all the boards and make it much easier to monitor.

Stuart McMillan: With regard to case studies, last year the Justice Committee went to Peebles, where there is a hub centre for the Scottish Court Service, Lothian and Borders Police and the community justice partners. Other examples, in the health service and in other areas of the public sector, could provide useful examples of such arrangements.

George Foulkes (Lothians) (Lab): When the NHS boards decide to dispose of property assets, it always seems to be a long time until that property is transferred to someone else and used for another purpose, during which time the property deteriorates and the value goes down. Did you look at the process for the disposal of assets, with regard to the time that it takes to do so and the resultant costs?

Nick Hex: No. We examined the disposals process and discussed it with the Government, and we understand that the disposals programme forms part of the capital investment programme for each board, which is planned over a number of years. As our report says, not a lot of information is gathered annually. However, one of the elements that are gathered annually by the Government is each board's capital investment, which includes all the plans for disposals over not just the coming year but succeeding years.

George Foulkes: I am surprised that you did not examine that issue. In my old role in South Ayrshire, I constantly heard complaints about the fact that, after the health board built a new hospital, Ayr hospital, Ballochmyle hospital and all the others that were surplus to requirements were empty for years, which led to huge extra costs. Surely Audit Scotland ought to examine that issue.

Nick Hex: We examined things in a strategic way. We considered at a global level the functional suitability of the estate—whether the estate is suitable and how it is being used—but we did not examine individual disposals of assets.

George Foulkes: Might you consider doing that? I am sure that a lot of money is wasted through property lying unused. I understand that there is a long, complicated procedure whereby the property must be made available to other public bodies before it can be disposed of on the private market. Is that correct?

Barbara Hurst: Public bodies are supposed to get the best value that they can when they dispose of land or buildings. An issue that might be coming up now, given the financial climate, concerns the fact that assumptions that were made about the extent to which land disposal can contribute to capital might prove to have been overoptimistic.

George Foulkes: That is a separate issue, really. My worry is that properties can become less valuable when they are left to deteriorate.

Page 27 of the report mentions various matters that must be considered. Rather low down the list—too low, in my view—you mention

"how energy efficient the estate is".

Having had a look at the new buildings, I do not think that anyone has paid any attention to that. There seems to be no indication of any work having been done to make them energy efficient. Have you detected anything that has been done to ensure that the buildings have as low a rate of energy consumption as possible and that they use all the new techniques for improving energy efficiency?

Barbara Hurst: The report on energy efficiency that you will consider later on your agenda examined that, to an extent. The health service is better than some other parts of the public sector in the attention that it pays to that issue. I believe that it has a target for energy efficiency in health service buildings.

George Foulkes: I am surprised by that. That is not my experience, but there we are.

Willie Coffey: On acquisitions and procurement, is there any evidence that NHS boards are trying to partner up with regard to services or materials? I note that there is a national database for something or other—I am not quite sure what, though; perhaps it is just for vehicle tracking.

Barbara Hurst: We are doing some work on procurement at the moment. I cannot remember exactly the publication date that we have planned, but I believe that we will bring a report on procurement in general across the public sector to the committee in the early summer. That will explain what is being done in the public sector to establish the sort of shared approaches that you are talking about.

Kirsty Whyte: There are a couple of initiatives that are quite specific to what you mention. Public sector bodies should be entering their properties into the United Kingdom-wide electronic property information mapping service—e-PIMS—so that public bodies that are looking for buildings can see what is available in certain areas. That enables the most efficient use of the space. The service has not been well used in Scotland so far, but the Government is working on promoting its use.

The Government has begun piloting the new hub initiative as part of the Scottish Futures Trust. That should increase efficiencies around the procurement of buildings, as public bodies can come together to procure large-scale contracts.

Cathie Craigie (Cumbernauld and Kilsyth) (Lab): On page 21, exhibit 13 demonstrates that acute hospitals and non-acute hospitals account for the majority of the NHS estate. On page 5, the report reminds us that there is a

"shift … from a hospital focused service to one that is community based".

Is there any indication that, in managing the estate, NHS boards are investing for the future to deliver on that community-based agenda?

10:30

Kirsty Whyte: Yes, I think that there is a recognition of that among health boards, particularly given the scale of the capital investment that is being made. All boards have major investment programmes that are linked to shifting the balance of care from a heavy focus on acute services to community centres.

Andrew Welsh: It seems that the focus of the Scottish Government health directorates is to look to future policy, but they do not seem to look at the existing situation. The report gives a warning signal about future problems unless the estate is dealt with. Should the focus of the SGHDs include not just existing policy but the existing estate, given that the estate is deteriorating and the health directorates do not seem to know exactly how bad the situation is? Is a switch in focus, or an additional focus, required?

Barbara Hurst: The report certainly recommends that there needs to be better monitoring nationally so that we know what the current situation is. We do not suggest that the health directorates should manage the local assets, but they certainly need to know what the picture looks like across Scotland. Without a proper picture of the estate, they cannot know what the capital investment should be for the future. That is an important point.

Andrew Welsh: They might be storing up future problems.

Barbara Hurst: Yes.

The Convener: If members have no further questions, I thank the Audit Scotland team for coming along—

George Foulkes: What happens now?

The Convener: We will decide what to do with the report under a later agenda item.

George Foulkes: Will that item be taken in private?

The Convener: Yes.

Section 22 Report

"The 2007/08 audit of VisitScotland"

10:32

The Convener: We move on to agenda item 3. I invite the Auditor General to brief us on his report "The 2007/08 audit of VisitScotland".

Mr Black: At its meeting on 4 February, the committee asked for further background information on VisitScotland's involvement with eTourism Ltd. I asked Audit Scotland to do a bit more work with the external auditor to provide a further briefing, so I am pleased that we are joined today by Mr David Watt of KPMG LLP, which is the appointed auditor for VisitScotland. As the briefing paper is very much based on the work that David Watt and his team undertook, he will be in a position to help members with any matters of fact that are of concern to them. I understand that the briefing has also been shared with VisitScotland, which has confirmed that it is factually accurate. The briefing has not been through the normal extensive clearance process, but it has been through a process of open sharing with VisitScotland.

As members can see from the briefing paper, we thought that the committee identified about seven key areas of interest. Unfortunately, some of those questions either run outside the scope of the work that we have been able to undertake to date, or are constrained by timing issues because they relate to on-going or future matters. Therefore, the briefing paper concentrates on the first two areas: the business case for developing eTourism Ltd, and VisitScotland's monitoring arrangements and associated actions. I am sure that members have taken the opportunity to read the paper, but I will provide a brief summary of its contents as it contains quite a lot of detail. Of course, committee members are welcome to follow up on any matters of detail that they wish to pursue.

The first point is that VisitScotland prepared an outline business case and a full business case. Both business cases considered all the relevant issues. They identified options and included criteria that were to be used in appraising the options, they contained financial and economic appraisals and the proposed procurement strategy, and they identified and assessed risks and proposed the mitigating actions that would be put in place. The business cases were subject to formal approval, which was obtained.

On monitoring arrangements and associated actions, evidence shows that VisitScotland and TourCo Ltd—the company that was established to represent the interests of VisitScotland and the area tourist boards in eTourism Ltd—regularly considered eTourism's performance.

The auditor's review identified that concerns about eTourism's business plan were expressed early, but those initial concerns were about the level of detail in and the timing of the plans. More significant concerns began to emerge in 2005. They related mainly to eTourism's financial performance and focused on the company's overall financial position, on the conversion rate of website visitors to bookings and on continuing concerns about eTourism's business planning.

The main route by which VisitScotland and TourCo could raise concerns was through their representation on the board of eTourism. As I said in my section 22 report and at the committee's previous meeting, eTourism is not an organisation that I audit and the auditor had no access to the board's minutes. As I also mentioned at the previous meeting, I have asked VisitScotland's external auditors to continue to monitor developments.

I am happy to attempt to answer any questions from members, with support from the team.

The Convener: Thank you for the detailed briefing paper, which helps to clarify the process that developed. Your paper says that, in September 2005,

> "visitscotland.com had risen to 20th most visited travel, destination and accommodation site—achieving more visits to the site than both visitengland.com and the equivalent Irish site. However, there remained a 45% drop-off rate from people visiting the site to people booking accommodation."

We heard about that in our previous discussion. Do we know what the equivalent conversion rates for England and Ireland were? Although their sites had fewer visitors, were they more successful at converting those visits into bookings? Do we know what the problem was or is with the VisitScotland site?

Mr Black: We do not have that information—I am sorry that I cannot help you with that. As you will appreciate, we concentrated on preparing a briefing that related to VisitScotland. I am sure that such questions could be adequately answered by VisitScotland's management, who will know their business.

Murdo Fraser: You talked about VisitScotland's monitoring of the situation and the action that was taken, to which paragraph 30 of the briefing paper refers. You said that, in 2005, VisitScotland and TourCo started to express concerns about financial performance and the conversion rate, yet matters were not drawn to a close until the end of 2008. To an outsider, that is an extraordinary length of time to allow problems to remain unresolved. Can you comment on that? Was the approach of VisitScotland and TourCo dilatory?

Mr Black: Appended to the committee's briefing paper is a table that helpfully itemises major interactions with eTourism and assessments that VisitScotland and TourCo undertook of eTourism's performance. As you can see, there is a narrative that shows an increasing level of concern. There is a fairly critical point round about 2005 when it seems that VisitScotland was becoming increasingly concerned about overoptimistic business targets. However, at the same time, according to VisitScotland's assessment, eTourism Ltd was developing a reputation for working well with the industry. It was containing the costs well and, as the convener just mentioned, performing well in terms of visits to its site. The picture was mixed. Concern about the failure to convert the visits into bookings and, therefore, to generate the additional income that was necessary to deliver on the business plan arose progressively only over the subsequent years.

Murdo Fraser: Thank you for that. I note from the calendar of events that, in July 2007,

"TourCo Limited's directors considered a six month financial report … and concluded that there had been no material change in eTourism Limited's trading position."

That was subsequent to a range of other concerns having been raised, and agreements that there would be careful monitoring. However, it took more than a year from July 2007—until August 2008—before an attempt was made to bring matters to an end. I am concerned that there seems to have been a lack of attention on the part of VisitScotland and TourCo and that matters should have been progressed more quickly.

Mr Black: I understand that concern. All that we, with support from David Watt, can do in the report is present the facts as we understand them. What underlies the timeline and the pattern of events is a question best asked of VisitScotland.

Murdo Fraser: We can pursue that with VisitScotland.

Andrew Welsh: Internet site visits are one thing, but eTourism Ltd's business was delivery. Surely the problem was previewed. You said that outline and full business cases were prepared, but how realistic were they? For example, how realistic was the £10 million payment that was expected from eTourism Ltd "regardless of … performance"? The risk assessment warnings appeared quite early, but the go-ahead was given on the outline business case. It strikes me as a shaky foundation for a £10 million revenue assumption. Were there flaws in the original assessments?

Mr Black: I hope that the section 22 report and the additional briefing paper give members independent assurance that the procedures that VisitScotland used to put the project together were appropriate and fit for purpose. In particular, it had an outline business case and a full business case. All the key elements that one would expect to be in a business case were in those.

We are not in a position to comment on whether the assumptions and analysis in the business case were appropriate—you would have to explore that with VisitScotland. However, as I think I mentioned at the previous meeting, the project has been in development for 10 years, in effect—since the first idea came through—and the market and use of the internet have changed enormously since then. It is important to understand the context within which the project has operated over the years. It appears that some of the risks have materialised in the ways that we have outlined in the report.

Andrew Welsh: Is it reasonable to expect that those points would have been picked up? Should the performance problems have been picked up earlier rather than in hindsight? There were concerns about the adequacy of the business plan for eTourism Ltd over four years and about its financial performance in converting site visitors into bookings. That sounds a bit like drift rather than sound business practice, especially because warnings were made early in the process and there were continuing doubts about performance. Is it not reasonable to expect that something would have been done about that earlier?

10:45

Mr Black: It is important to recognise that the VisitScotland people are the best people to answer those questions. I remind members that the company was performing quite well in many respects. It was attracting many visitors to its site, which in itself represents a significant benefit to the Scottish tourism industry. According to the papers that the auditors have seen, it was doing reasonably well to contain its costs.

The issue that was of major concern was the conversion rate into bookings. Given that serious concerns were being expressed from 2005, roughly speaking, we must also recognise that there would be a turn-around period. There would not be an instant solution. That is not to take away from the concerns that Mr Welsh has expressed, but it is important to understand the context. However, if members wish to pursue the matter further, it might be more appropriate to do so with the management of VisitScotland.

Nicol Stephen (Aberdeen South) (LD): I would like to talk about VisitScotland's acquisition of shares in eTourism Ltd in December 2008. Can you give us a little bit more detail about how the share price was negotiated and agreed and whether any independent valuation was carried out to support the acquisition?

Mr Black: Perhaps Mark MacPherson can help with that.

Mark MacPherson (Audit Scotland): We did not consider that matter in detail, because the section 22 report relates to the 2007-08 accounting period, which was well over by the time the acquisition was made. The auditing work on VisitScotland and the background to the matter did not include a detailed review of the process by which the figure in question was negotiated. However, I think that the price would be based on a book value and negotiations with the other partners to establish a reasonable price.

David Watt (KPMG LLP): It was essentially a matter of negotiation between VisitScotland and TourCo Ltd and the other parties to the shareholdings—Tiscover and Partnerships UK—with a view to securing VisitScotland's full control. VisitScotland subsequently engaged financial advisers to assist it in the valuation of the company and to support the restructuring that is taking place.

Nicol Stephen: So VisitScotland subsequently engaged financial advisers, but did not engage advisers at the time. Is that right?

David Watt: Perhaps it would be better to use the expression "in parallel".

Nicol Stephen: I am interested in the final page—page 13—of the Auditor General's further briefing. Paragraph 10 on that page reminds us that VisitScotland decided to write off an

"original loan of £1.85 million and unpaid interest due on that loan of £900,000 in its 2007/08 accounts."

Was no thought given to shifting that loan into capital?

Mr Black: Again, I look to David Watt to help us with that question. Part of the issue is that there was unfinished business at the time of the report, because the values of debts and so on are not terribly clear until there is a business plan for the future. VisitScotland now has complete control of the company in question and is, as we speak, working on alternative options for the future that will then settle into its business plan. The size of the outstanding debt will become clearer as a result of that work. Therefore, I am not sure whether we can fully answer your question at the moment.

Nicol Stephen: I hope that you understand what I am driving at. If a company is lent £1.85 million and then another £900,000 and all that money is lost, nothing will be received in return and there will be no transfer of loan to equity. There will then be a technically insolvent company. Am I correct?

Mr Black: Yes.

Nicol Stephen: So, a company was lent about £2.6 million or £2.7 million, then all that money was written off, and there was a technically insolvent company. How much more was paid to acquire shares in the company in December 2008?

David Watt: The shares were £64,000, at a nominal value of £1 per share. There was a subsequent capital injection to allow an element of the loans from the other parties to be repaid.

Nicol Stephen: How much was that?

David Watt: It was £1.25 million.

Nicol Stephen: So £64,000 was paid for the shares and a further £1.25 million went, in effect, to repay the debt of the previous shareholders. That does not look like a good deal for the public sector. The partners who received the £64,000 for their share capital for an insolvent company and those who received the £1.25 million in loans back, would have walked away with happy smiles on their faces. Compare that to the public sector, which so far has paid more than £2.6 million to write off loans and has injected a further £1.25 million simply to repay the previous partners, as well as paying £64,000 for shares in a company that was technically insolvent. In the current environment, quite a few shareholders would be pleased to get £64,000 for shares in a company that was bust. The issue needs close scrutiny. I am astonished that professional advice was not given to VisitScotland during the negotiations. I seem to be hearing that professional advice was not given. Is that correct?

Mr Black: We acknowledge Mr Stephen's comments. The principal reason why I made the report to the committee was because of the concerns about the matter and the exposure for the public sector. However, those questions and concerns are best answered by the management of VisitScotland.

George Foulkes: You have said that five times.

The Convener: I want to clarify an issue with Mr Watt. He said that, subsequent to the purchase of the company for a nominal value of £64,000, loans were repaid to other parties. How much was repaid to the other parties?

David Watt: It was £1.25 million, which was not the full value of the loans.

The Convener: I understand that. To return to Nicol Stephen's point, £64,000 was used to purchase, at a nominal value, the full worth of a company that was technically insolvent. Others were then given £1.25 million from the public purse for loans that they had made. In the retail trade recently, a company with which Sir Tom Hunter was associated went into liquidation but, subsequently, another part of his business empire purchased some shops that it wanted to retain. That meant that, in effect, all those who were owed money by the initial company received nothing. That seems to be a fairly common business practice in the private sector just now. I make no comment on whether that is right or wrong, but I struggle to understand why the public sector would recompense others for loans that were given to a company that is technically insolvent. Can anyone answer that, or should we take that up with VisitScotland as well?

David Watt: To echo what the Auditor General said, that is a matter for the management of VisitScotland. The view was that, although the company was insolvent, putting it into administration was not in the best interests of VisitScotland and its work to promote tourism in Scotland.

The Convener: You have expertise in the financial and legal aspects of business. If the company had been put into administration, would it have been technically possible for VisitScotland and/or another body to repurchase an interest in the company—almost like a management buy-out or whatever we want to call it—in the way that seems to happen in the private sector?

David Watt: That would have been technically possible, yes.

The Convener: It would have been technically possible but, for whatever reason—it is not your responsibility—those who were involved decided that that was not in VisitScotland's or someone else's best interests and chose to handle the situation in a way that ended up with the public purse repaying £1.25 million of debt to others.

Murdo Fraser: I am interested in the £1.25 million that you are talking about, Mr Watt. On page 2 of our briefing paper there is a helpful flow chart that shows the make-up of the shareholding. The principal shareholder in eTourism Ltd was SchlumbergerSema, which was in the private sector. However, the other 40 per cent of the company was owned by the public sector—by TourCo Ltd, which was itself a joint venture between VisitScotland and the area tourist boards, and by Partnerships UK, which is also a public sector vehicle. Do you know how the £1.25 million loan repayments that you have talked about were split between the various partners?

David Watt: Yes. The flow chart under paragraph 4 of the Auditor General's paper shows the structure as it was originally established and not the final shareholding. The committee may recall that, in 2006, there was a reorganisation of shareholdings and interests in eTourism Ltd. At that time, SchlumbergerSema ceded most of its shareholding and another partner, Tiscover UK, was introduced. The loan repayments were £250,000 to Tiscover UK, £800,000 to Atos Origin IT Services—which is now the parent company of the company that was SchlumbergerSema—and £200,000 to Partnerships UK.

Murdo Fraser: So, there was £1.1 million in payments to the private sector partners. Is that correct?

David Watt: Yes.

Nicol Stephen: Is Partnerships UK not now a privatised entity? Has it not been spun out?

The Convener: We can look at that later.

Andrew Welsh: My concern is that lessons should be learned. What we have heard so far has not exactly been about getting value for money, and the concern is that it might be a continuing saga. VisitScotland is currently considering alternative business models to secure the future sustainability of eTourism Ltd and its website operations. Has anything changed? How viable are eTourism Ltd's operations?

Mr Black: I am sorry, but we cannot answer that question. It is a matter that VisitScotland is considering at the moment.

Stuart McMillan: Do you know the value of bookings in December 2008? If, at that time, the £1.25 million was not put in and the £64,000 not paid for the shares—if VisitScotland had gone bust and stopped trading—how much would have been lost to the public purse?

Mr Black: I am sorry, but we do not have that information.

Nicol Stephen: I would like David Watt to clarify the role that he has been playing in all this. I assume that your role is as auditor of the company—is that correct?

David Watt: I am appointed by the Auditor General as the auditor of VisitScotland.

Nicol Stephen: Did your company play any role in providing an advisory service to VisitScotland in relation to any of the issues that we are discussing separately from the audit?

David Watt: Not that I am aware of, no.

Nicol Stephen: Are you aware of any other corporate finance or advisory services that were provided to the company in relation to this saga?

David Watt: What period are you talking about? As the earlier paper from the Auditor General indicates, there have been advisers at different stages of the project.

11:00

Nicol Stephen: I am focusing most on the final stage, when the shares were acquired by VisitScotland, the debts were paid off by VisitScotland and the option of administration—where the company could have continued trading, with administrators in position—seems to have been set aside.

David Watt: VisitScotland appointed legal advisers and engaged financial advisers in connection with the project. My understanding is that the financial advisers' role was essentially in relation to certain aspects of the accounting and restructuring of eTourism Ltd in the context of VisitScotland.

Nicol Stephen: So, is it your understanding that there were legal and financial advisers on the evaluation of options in relation to share values, the amount of debt to be repaid and other options, including administration? Alternatively, was the legal advice, corporate financial and other financial advice on different matters?

David Watt: I think that the advice was on what Mr Stephen is calling "different matters".

Nicol Stephen: So, it may be that VisitScotland conducted all these negotiations without appropriate professional advice?

Mr Black: We are not in a position to answer that, convener.

The Convener: Okay. We can ascertain that separately. We will reflect on what we have heard so far later in the meeting. I thank the Auditor General and Mr Watt for their contribution to the discussion.

Section 23 Report: Responses

"Improving energy efficiency"

11:01

The Convener: The next item on the agenda is a section 23 report. We have responses from the accountable officers to the Auditor General for Scotland's report, "Improving energy efficiency". Are there any comments?

George Foulkes: Are you seeking comments from members of the committee?

The Convener: Does the Auditor General want to say anything before I invite comments from members?

Mr Black: No.

George Foulkes: I do not know whether it is just me, but I find the reply from dear Sir John astonishingly complacent. One of the most amazing phrases under the heading "Barriers to improvement" on the second page is:

> "We believe the most significant barrier to improving energy performance in public bodies is achieving senior level buy-in".

In other words, all his directors will have nothing to do with it. That is my interpretation of it. Is it not astonishing that the Government is saying that improving energy performance is a top priority, but Sir John Elvidge cannot get his directors to do anything about it? Am I misinterpreting what he says in the response?

The Convener: The comment is quite astonishing. Given the commitment that ministers have made to tackling this issue, they could reasonably expect all senior officials to respond to the policy directives.

George Foulkes: The very last paragraph of the response says that 20 per cent of public bodies did not even reply to Audit Scotland's survey. How on earth are we going to get energy efficiency in the public sector if 20 per cent of public bodies do not reply when the issue is raised with them? That is astonishing, given that we are trying to improve energy efficiency. We are all being told to improve our energy efficiency. I have just had cavity wall insulation put into my house because I was so inspired by the Government to go and do something, and yet we find that the public sector is doing bugger all—if that is not an unparliamentary expression. Surely we ought to do something about that? Mr Salmond is down in London saying that he cannot find any efficiency savings in the budget. Surely he should get these people who are sitting on their behinds mobilised. If he was able to achieve "senior level buy-in"—to use that wonderful phrase from the response—he might be able to get some efficiency savings.

Andrew Welsh: There is a sense of frustration, as we have just heard. The Government was asked:

"What actions will you take to assess the quality and effectiveness of energy efficiency plans as they are developed across the public sector?"

In its response, it made reference to an internal group and an external group, but the external group has not yet met. There is frustration because, although action is needed, instead of being told what action will be taken, we have simply had references to various groups.

The Convener: Okay. We can reflect on what we want to do. We could refer the correspondence to the Economy, Energy and Tourism Committee, which is conducting an energy inquiry; we could note it; or we could engage in further correspondence. We could even invite the accountable officer or officers to give evidence. I am in the hands of the committee.

Nicol Stephen: It would be valuable to refer on the work that has been done to the Economy, Energy and Tourism Committee.

However, I agree that there are aspects of the reply that are complacent. I would have thought that, at the very least, we should suggest to John Elvidge that he obtain a response from the 20 per cent of organisations that failed to respond and that he make those responses available to the Economy, Energy and Tourism Committee.

The statement that

"We shall use the mechanisms aimed at ensuring senior level buy in, which I have described above, to raise awareness of the importance of the issues among the 20% or so of public bodies … which did not provide a response"

is mandarinspeak for not doing very much at all. It is quite a serious issue that one fifth of the public bodies ignored a request from Audit Scotland to provide information on such an important area. That situation should not be allowed to continue.

The Convener: Is that generally agreed?

Members *indicated agreement*.

The Convener: Does Willie Coffey have anything further to suggest?

Willie Coffey: The second part of the "Barriers to improvement" section of the permanent secretary's reply mentions the barrier of not being able to access resources to deliver energy efficiency. Not getting the £500 million cut that we face next year would be a great help in that regard, and would greatly encourage participation.

You might remember that we asked the Scottish Parliament to have a wee think about the issue, too, and I am greatly comforted by the fact that

"the Parliament has a combined heat and power plant with the capability to generate 80 kW of electricity and all water required for flushing the toilets is provided by on site boreholes"—

whatever that means.

The Convener: We will not go there, nor will we get into a discussion about how the present Administration will use the increasing budgets that it will receive year on year. We will leave all that for others to consider.

Cathie Craigie: It should be easy to find the necessary resources from the extra £2.6 billion that will be provided over the next two years.

The Convener: We agree with Nicol Stephen's suggestion.

Stuart McMillan: I return to the fact that 20 per cent of public bodies did not respond to Audit Scotland's request for information. That is an issue that the committee could consider at some point in the future, even if some of us might not still be on it. It is important that some public bodies do not think that they have to respond to genuine and serious requests. The role of public bodies is to represent the public and to provide public services. Given that the energy situation is high up on the agenda of the public and of Governments, the fact that the bodies in question just did not bother to respond is an example of a lack not only of co-operation but of understanding.

The Convener: It raises issues for senior officials in the civil service with regard to how they manage. George Foulkes has already raised the issue of the failures in that regard. In our letter, we will exhort more effective management.

George Foulkes: Will we pass the responses to the Economy, Energy and Tourism Committee, along with our remarks that we are concerned about Sir John Elvidge's comments?

The Convener: Yes.

Principles of Public Audit

11:10

The Convener: We have a consultation paper from the Auditor General and the Accounts Commission on the principles of public audit. I invite comments from the Auditor General.

Mr Black: I will be brief. The Accounts Commission and I feel that the document is necessary. It is an attempt to capture, in plain English and within a reasonably short document, the elements of how we work together and how we expect the audit process to be undertaken in the public interest, while balancing the expectations of all our stakeholders—including this committee—that we undertake the process of holding to account robustly and seek to improve it.

Section 5 of the document is a reminder of our respective roles and of how we work together. In section 6, we have tried to capture the five fundamental principles of public audit that we think are important for the public interest. Those are perhaps of particular interest and relevance at the moment, in view of the recent events in the private sector—in the banking sector in particular—and the concerns that have been expressed about the effectiveness of oversight and assurance in the private sector.

In the public sector, the first principle is that the public auditor should be independent from the bodies that are being audited. In other words, they are appointed by me for audits in the larger part of the public sector—David Watt, who is here this morning, is a case in point.

The public auditors are remunerated through a system that is independent of the body that is being audited, which is a good thing. The audit is also much wider in scope than is the case with the auditing of private companies or private organisations. It does not involve only an audit of financial statements; we consider issues of legality and standards, and the arrangements that public bodies have in place to prevent and detect fraud. The committee has received reports on that area of our work in the past. The public auditors make a contribution to the audit of value for money and best value and to performance audit. I just wanted to capture that for the committee.

We have put the document out for consultation, in order to provide our principal stakeholders with a high-level statement of how we undertake the work and how we attempt to ensure that it is robust, independent and fit for purpose. It is a bit of an abstract document but, nevertheless, it is right that the committee is made aware of it. We will be pleased to receive any comments between now and the end of March.

The Convener: It is a very useful document—it sets out some important principles.

You commented that the auditors are fully independent from the organisations that are being audited. In a country as small as Scotland, there is often overlap, and many of the large accountancy companies, in the way in which they now operate, have arms other than just audit functions. Is there a danger—notwithstanding the fact that the auditors may be separate from the other parts and activities of those companies—that there could be a degree of compromise if the same holding company is doing other work for an organisation that is being audited by the auditors from that company?

11:15

Mr Black: My Audit Scotland colleagues and I are very much aware of the importance of ensuring that independence, which is why it is a first principle. I will explain how we do that. Appointments are offered every five years. In the course of that exercise, Russell Frith, our director of audit strategy, conducts a pretty robust review of the interests and the other work that they do in audited bodies of any companies that might express an interest in working with us. A great deal of care is taken in audit appointments to avoid such conflicts of interest. To put it bluntly, if a company provided high-level consultancy or advisory services to a public body, there is no way that that company could become the external auditor.

Scotland is of a sufficient scale that we can keep an eye on such things. It is a matter that we take extremely seriously. We expect the auditors to operate to a code of audit practice, which is explicit and robust on what they are expected to do. I can give the committee an assurance that, in all the years that I have been doing this work, there has never been an instance when I have felt that an audit opinion or audit analysis has been compromised in any way.

George Foulkes: There is a very important point here. I accept what Robert Black has said. However, when the mutuals were demutualised and investment banks and other banks were brought together, a lot of people expressed concerns about conflicts of interest, but they were all brushed aside and pooh-poohed—everything was apparently okay. Look what has happened, however.

The convener has made a very good point. Accountants used to be auditors who got on with financial matters. Now, they are involved in a whole range of things. They bid for public sector contracts and do a range of consultancies and so on. We ought to look into that. I accept Robert

Black's assurance, but we should consider that area rather more carefully in the future.

As I said, the convener made a very good point: there could be a conflict of interest. KPMG, PricewaterhouseCoopers and other firms say that they have Chinese walls between the people who do accountancy and those who do consultancy, but it is easy for such Chinese walls to become—what is the word for when things pass through?

Murdo Fraser: Porous?

George Foulkes: That is right—porous. We really need to look into that. I am not sure how we do that, but the convener has fired an important warning shot.

The Convener: We now have a statement from the Auditor General on the record that that does not in fact happen—and, I presume, will not happen.

Mr Black: Yes, you have my assurance on that.

I recognise the concern that is being expressed, which is entirely reasonable. We are due to go to a retendering of the audits in a couple of years' time. I shall make a note of the matter and I shall ensure that—if the committee is interested—Russell Frith is able bring you a paper at some stage, describing how the process operates. That might provide the assurance that you are seeking.

The Convener: That would be useful. Thank you.

Andrew Welsh: The convener's comments remind us that eternal vigilance is required. We all rely on the integrity and judgment of Audit Scotland. As far as I am concerned, there should be no no-go areas for Audit Scotland in its sphere of operation. Quite rightly, it seeks neither fear nor favour. What the committee has heard further underlines the fact that Audit Scotland is the auditing exemplar that other organisations are following. We owe it a deep debt of gratitude for that.

Willie Coffey: I have a question about the audit function. As I understand it, it tends to stop short, at recommendations to the public sector or whoever. Is there a case for revisiting and strengthening the powers that the Auditor General has—with powers of compulsion, for example? Over the past 22 months, as I think Stuart McMillan mentioned, there have been many examples from across the public sector of non-compliance and of not following up on audit recommendations—and even of not responding to surveys. That must detract from the Auditor General's good work. Mr Black, have you a view on whether you should have more powers of compulsion—an ability to instruct or require bodies to act and follow up on the recommendations that you painstakingly make?

Mr Black: I acknowledge the concern. As you can imagine, my colleagues and I occasionally—more than occasionally—feel a degree of frustration. If we bring reason and light to an issue, and improvement does not happen when one thought that it would, that can be frustrating for us. However, I have a very clear view on this: the auditor must not take over the role of management in any circumstance whatsoever. We may have particular skills in analysing evidence, but we are not accountable for the running of health bodies, local authorities or bodies such as VisitScotland. Those bodies have their own management to do that. It would seriously compromise auditors if their recommendations on public bodies were mandatory.

One of the strengths in having the Scottish Parliament is that, as Stuart McMillan said, scrutiny is more open and more robust. This committee is particularly well placed, as you have demonstrated on many occasions, to hold senior public sector managers to account if they decline to take up recommendations that you and we feel would lead to better public service.

The audit process is not the whole story. We are part of an accountability process. We provide what we hope is robust and objective evidence, information and analysis, and then we pass the torch to you.

Stuart McMillan: A few moments ago, George Foulkes mentioned a couple of companies. Those organisations, as well as others, are global players in the accountancy and audit fields. I assume therefore that the situation in Scotland is replicated in other European countries, small and large. Does Audit Scotland consult its partners in other countries on the processes that you use, before you bring companies in to do work for you?

Mr Black: I offer a qualified yes to that question. There is great benefit to us in having partnership arrangements with firms, subject to the constraints and checks and balances that I described earlier. The firms have experience across the whole of the United Kingdom and beyond. It has on occasion been very helpful indeed to be able to draw on their knowledge of work in, for example, England. That has been especially helpful when we have been working in the performance audit sphere. In future, it will be increasingly valuable for both parties to compare performance and systems in England and Scotland.

The Convener: With that, I draw this part of the discussion to a close. I thank the Auditor General for his contribution.

11:23

Meeting continued in private until 12:17.

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