FINANCE COMMITTEE

AGENDA

4th Meeting, 2003 (Session 1)

Tuesday 11 February 2003

The Committee will meet at 2.00 p.m. in Committee Room 1 to consider the following agenda items:

1. **Scotland’s Budget Documents 2003-04:** The Committee will take evidence from—
   - Peter Peacock MSP, Deputy Minister for Finance and Public Services;
   - Richard Dennis, Scottish Executive Finance Co-ordination;
   - Richard Wilkins, Scottish Executive Finance Co-ordination.

2. **Budget (Scotland) (No. 4) Bill:** The Committee will consider the Budget (Scotland) (No.4) Bill at Stage 2.

3. **Outcome Budgeting:** The Committee will take evidence from—
   - Peter Peacock MSP, Deputy Minister for Finance and Public Services;
   - Richard Dennis, Scottish Executive Finance Co-ordination;
   - Richard Wilkins, Scottish Executive Finance Co-ordination.

   *Not before 3.15 pm.*

4. **Scottish Parliamentary Corporate Body – Report on the Scottish Parliament Building Project:** The Committee will consider a report on the progress of the Holyrood Project and take evidence from—
   - Paul Grice, Clerk and Chief Executive, Scottish Parliament;
   - Robert Brown MSP, Member, Scottish Parliament Corporate Body;
   - John Home Robertson MSP, Convener, Holyrood Progress Group;
   - Sarah Davidson, Project Director, Holyrood Project Team.
5. **Visit by the House of Commons’ Modernisation Committee:** The Committee will consider an invitation to a Member of the Committee to attend a lunch with the Modernisation Committee.

6. **Cross-Cutting Review (in private):** The Committee will consider a draft report on its cross-cutting expenditure review on Children in Poverty.

David McGill
Clerk to the Committee

The papers for this meeting are:

**Agenda item 3**

Paper by the Clerk
Submission from the Scottish Executive

**Agenda item 4**

Letter from Sir David Steel
Letter from Robert Brown MSP to the Convener

**Agenda Item 5**

Paper by the Clerk

**Agenda Item 6**

Paper by the Adviser
PRIVATE PAPER
FINANCE COMMITTEE

CONSULTATION RESPONSE TO MOVING TO OUTCOME BUDGETING

Background
This paper has already been issued to Members, for the Committee’s meeting of 8 October 2002. At that meeting, it was agreed that the Executive would be invited to submit a written response to the Committee’s consultation on Outcome Budgeting. Following receipt of that response, the Executive has now agreed to provide oral evidence to the Committee. This paper is being reissued to Members as an aide memoir, listing the questions asked in the consultation exercise and highlighting the main issues which arose.

Introduction
At the Finance Committee’s meeting of 22 May 2001, Members agreed to submit a bid for external research on outcome based budgeting to the Conveners’ Liaison Group (CLG). The research aims and objectives were as follows:

- To investigate the feasibility of outcome budgeting for the Scottish budget;
- To identify areas where it could be applied; and
- To develop practical proposals to assist Committees in measuring outcomes in the analysis Scottish budget.

Having secured agreement to the bid from the CLG, Norman Flynn was commissioned to carry out the research and his final report “Moving to Outcome Budgeting”, was published on 16 May 2002.

The Consultation
A consultation exercise on the final report was initiated immediately after publication. A total of 68 organisations were asked to provide their views on the research, using the following questions as a structure for their responses:

1. To what extent do you feel that the report has made the case for more extensive use of outcome budgeting?
2. On the evidence presented in the report, do you feel that outcome budgeting (as opposed to input or output budgeting) represents the best possible form of budgetary control? What do you see as the advantages and disadvantages of outcome budgeting?
3. To what extent has outcome budgeting been adopted by your organisation? Where appropriate, what have been the advantages and disadvantages?
4. Is there now a more efficient and effective system of budgetary control in place as a consequence of the introduction of outcome budgeting?
5. What effect, if any, has it had on the identification and realisation of policy aims? What other changes has it led to in your organisation?
6. If your organisation has not adopted outcome budgeting, what scope do you think there is for it to move towards such a system? Do you feel that
such a move would lead to improvements in the way policies and objectives are pursued?

7. Would a move to outcome budgeting improve monitoring and accountability in your organisation?

8. What impact, if any, would the Scottish Executive moving to outcome budgeting have on your organisation?

9. Do you feel that setting specific policy targets - and allocating resources according to these - may lead to unexpected outcomes?

10. Do you think it is likely that outcome budgeting will be more widely adopted in future?

11. Are there any other comments you would like to make?

It is worth noting that of the 64 organisations asked to comment, only 25 responded. Moreover, not all of the respondents answered fully the questions outlined.

The Response

This paper highlights some of the key messages to have emerged from the consultees’ responses. Before doing so, there are caveats worth stressing. Outcome budgeting, as is acknowledged in Norman Flynn’s report, is a method of accounting that has not, as yet, been adopted on a widespread basis by any government. Rather, a few governments have made limited progress on moving towards outcome budgeting, particularly through the inclusion of outcomes in the budget process. Secondly, a move towards outcome budgeting is likely to be a complex process, which may be achievable only over a lengthy period of time. Again, this is something that was mentioned in Norman Flynn’s report. As these two concerns were repeatedly stressed by respondents, it is worth putting their concerns into context.

The analysis below, showing what the respondents perceive to be the more specific benefits and drawbacks of outcome budgeting, appears to show that opinion is almost equally divided. However, it would be more accurate to state that most respondents had serious reservations about the introduction of outcome budgeting. These reservations do not amount to outright rejection; there is a consensus that outcome budgeting is something that is worthy of greater consideration and research than has been the case until now. Moreover, in the limited cases where an attempt has been to move towards a method of outcome budgeting, this has been done in tandem with existing budgeting methods. This reinforces the message that outcome budgeting is a long term development, since, at this stage, it is a system that is not currently seen as a replacement method, but rather, as a complementary method of budgetary control.

A final point of note is that there may also be differences in interpretation as to what outcome budgeting actually means; SEPA, for example, challenges the definition of outcome budgeting provided, preferring instead “a budget process that makes resource allocation and control decisions based on the results of expenditure”. It also appears from some of the responses received...
from different NHS organisations, that what is considered outcome budgeting in one area, is a definition not necessarily held by all NHS Boards and Trusts.

With this in mind, some of the main benefits or drawbacks of outcome budgeting suggested by the consultees can be summarised as follows:

**Benefits of outcome budgeting**
- Most useful when used to communicate information regarding the deployment of funds for specific outcomes (SEPA)
- Allows organisations to clearly demonstrate the benefits of money being spent in specific areas or on specific projects, making the organisation more accountable to its public and its stakeholders (SEPA)
- Gives primacy to performance measures that are more meaningful in terms of people’s lives (Communities Scotland)
- Could achieve improved integration between the process of agreeing priorities and desired outcomes and that of allocating resources (Communities Scotland)
- Provides focus, and even impetus to challenging option appraisal as part of a process of strategic decision making (Communities Scotland)
- May lead to increasingly effective organisations and encourage multi-agency working (Highlands and Islands Enterprise)
- Could mean a move towards longer term planning and target setting which will provide stability and strategic clarity for the public sector (Highlands and Islands Enterprise)
- May enable local flexibility in delivery to support consistent national priorities (Scottish Enterprise)
- Could encourage the strategic direction of economic development in Scotland to be based on longer term economic impact rather than short term issues such as expenditure (Scottish Enterprise)

**Difficulties of outcome budgeting**
- Could complicate decision making process (SEPA)
- Does not provide management with accurate cost analysis or audit trail, which is essential to maintaining strong and robust financial management (SEPA)
- If there are financial penalties for under-performing services, what happens to the service still to be delivered? (ADES)
- Main difficulty is capturing a robust measurement methodology that supports the process (NHS Grampian)
- Would the level of realised benefits be commensurate with the level of resources required to implement the process, including the information requirements? (Shetland NHS Board)
- Identifying a clear link between the resources provided and the outcome achieved can be difficult with outcomes potentially emerging several years after the input (Highlands and Islands Enterprise)
- Outcomes can be the result of the combined impact of several different agencies, and the specific contribution of each agency may be difficult to identify and quantify (Highlands and Islands Enterprise)
Conclusion
While the response to Norman Flynn’s research has expressed serious concerns about the practicalities of implementing outcome budgeting, only one organisation (NHS Highlands) has come near to actually rejecting the idea entirely. Many of the responses were critical of some of the principles of outcome budgeting and expressed scepticism about its effectiveness, but also acknowledged that fact that it may become a more realistic prospect in the future, providing further development work is carried out.

As many of the potential benefits and drawbacks identified above are rather theoretical, it may appear more instructive to examine the experiences of the three organisations that indicated in their responses that they have taken some steps towards an outcomes based method of accounting. However, the experiences of Highlands and Islands Enterprise, NHS Lanarkshire and Greater Glasgow NHS Board, illustrate that there is a mixed message in terms of the benefits of this approach:

Highlands and Islands Enterprise
“HIE (has) establish(ed) some very specific outcome indicators and links these to specific longer term objectives, project outcomes and consequently resource inputs. One of the main problems encountered and currently being reviewed is the fact that a specific investment in a single project may in reality result in several outcomes being achieved, however, it is not possible to discriminate between the specific financial investment and each of the outcomes.”

NHS Lanarkshire
“A number of Outcome Budgeting approaches have been tried for the Health Service over the years, e.g. management budgeting. These have never had any real success and the traditional approach of setting budgets based on staff, premises etc, as a method of allocating resources within health organisations has continued.”

Greater Glasgow NHS Board
“We currently use outcome budgeting for new funding like waiting times, Discharge Planning, Winter Issues, Cancer, etc, as well all the work on the national priorities. Advantages are apparent in the greater control and the direct link to results. Disadvantages would include the time taken up by the consultation and monitoring process, etc.”
On 18 June 2002 Des McNulty wrote to me about outcome budgeting. Des McNulty’s letter asked for answers to several specific questions relating to Norman Flynn’s research called *Moving to Outcome Budgeting*. Apologies for the delay in replying.

My answers to the questions raised in the letter are as follows:

1. This report makes a very useful contribution to the understanding of outcome budgeting in particular. It clearly identifies the constraints that we will have to overcome to make progress.

2. The evidence is persuasive, the real questions are establishing the causal links between outputs and outcomes, and the practical issues surrounding information, analysis and possible overload.

3. Our approach follows an outcome budgeting framework focussing on what outcome is required before beginning to consider the pure public expenditure aspects of the budget. From our perspective the major advantage is the strategic focus. The disadvantages are set out in Question 2.

4. It is difficult to assess the comparative efficiency and effectiveness of different budgetary approaches. We think that outcome budgeting brings something additional and worthwhile.

5. It has brought a greater focus on the end product.

6. We have moved towards outcome budgeting because we think it worthwhile. Pure outcome budgeting is probably unachievable by large, complex organisations.

7. The more strategic focus with the associated improvement in objective and target setting has improved monitoring, and hopefully Parliamentary accountability.

8. The causal link between input, output and outcome is not particularly well specified in all circumstances and there is always the possibility of an unexpected outcome.
9. I think the benefits of outcome budgeting are quite clear and this will drive organisations towards it. Whether we will ever be able to fully implement the full system of "outcome budgeting" is open to question as there are a number of outstanding difficulties in both principle and practice.

I hope that you find this response helpful, and that it will allow the Committee to take forward its work in this area. If you or the Committee have any further questions about this, or require any additional information, then you are very welcome to contact me.

Yours

Dr P S COLLINGS
Principal Finance Officer
HOLYROOD PROJECT

Giving evidence to the Committee in December, the SPCB was acutely conscious of the frustration caused by the apparent continuing uncertainty surrounding the Project completion date and consequently the final cost estimates. We shared that frustration, which was at least in part due to the unavoidable timing of the meeting, immediately prior to receiving the results of significant reviews of both programme and cost.

At that time, we anticipated that by January we would be in a position to report more confidently on the expected time-scales and budgetary requirements to completion. We have now met with the Construction Manager and the Cost Consultant and we were anxious to let you have the resulting information as soon as possible.

Programme

The programme review undertaken in late December/early January assessed the ability of individual package contractors to meet the time-scales required of them within the overall programme. It also took into account other outstanding risks which could affect programme – issues such as co-ordination of services; resolution of window installation; completion of outstanding design details etc.

This review concluded that package contractors were performing well on site; that there was the desired degree of construction momentum and that the spend profile was significantly improved.
Given this, the Construction Manager is able to say with confidence that the construction and internal fit-out of the majority of the complex (the MSP Building, Queensberry House, the Towers and the Canongate Building) should be complete between the end of August (the programme 6B target date) and the end of October. However, the review also confirmed that the remaining elements, (the Debating Chamber and Boundary Walls) are unlikely to be complete by that time.

Mindful of the Committee’s views and of the SPCB’s own concern to secure a realistic handover date, we have discussed this issue in some detail with the Construction Manager. Taking into account the remaining risks, he has assured us that he has a very high degree of confidence that the building will be handed over in its entirety in November 2003 at the latest.

Clearly no programme is risk free, but we took from the Construction Manager a good deal of comfort that the remaining risks to this programme are now well understood and continue to be managed appropriately. For our part, we continue to send a very strong signal to the Construction and Design Teams about the importance of resolving all outstanding issues as speedily as possible and securing the best possible, (i.e. earliest) completion date.

**Cost**

When we reported to the Committee in December, an estimated total project cost of £310.5m was discussed. This figure was made up of the £294.6m reported on the basis of the previous Risk Review in May and the cost consultant’s provisional estimate of the likely costs of the extended programme, (£15.9m). We indicated that the forthcoming Risk Review would assess the accuracy of this estimate as well as quantifying the other variations and delays to packages which had increased costs since the last full Review.

Following the December Review, the cost consultant has confirmed that his initial estimate for programme related costs remains unchanged. In addition, a number of individual packages had increased in expected cost since the last Review, totalling £6.5m gross. There has also been an increase to site running costs and fees of £6.9m.

These additional figures result in a revised overall target figure of £323.9m, (of which £7.8m is the remainder of the original project contingency sum intended to provide for as yet unforeseen, but common on-site problems.) The budget for the landscaping scheme is of course separate from this total.

At this stage in a project, programme uncertainty is the biggest threat to costs. The significantly increased programme certainty we are now discussing allows the cost consultant to be similarly confident about the accuracy of his current estimates and he has assured us that he is comfortable that this estimate of £324m represents the funding now required to complete the project in the light of known risks and the Construction Manager’s expected completion dates.
Conclusion

It is accepted that 100% certainty about cost and programme at this stage is not within the gift of the Construction Manager or the Cost Consultant, let alone the SPCB. Nonetheless, we welcome the increased certainty which has emerged from the recent review and will continue to monitor progress closely over coming months.

I hope that the information contained in this letter is of assistance to the Committee and we will of course update Members should that become necessary. I am conscious that there were a number of other matters of detail which witnesses undertook to pursue following the meeting on 17 December and we will also write to you on these as soon as possible.

Given the considerable general interest in this matter, I am sure you will understand why I feel that it would be appropriate to release the text of this letter to the press tomorrow.

David Steel
Finance Committee Undertakings

The Presiding Officer’s letter to you of 16th January addressed the principal matters outstanding after our last meeting with the Committee, namely those of cost and programme certainty. However, there were also a number of technical points raised at the 17th December Finance Committee meeting, on which we undertook to revert to the Committee. That is the purpose of this letter.

Risk management

In discussing cost and programme issues, the Committee asked a number of detailed questions about the extent to which individual works packages were still perceived to pose risks either in budgetary or time terms. While I think that these issues have largely have been addressed in the generality by the PO’s letter of 16th January, I would like to pick up on one or two specific points.

The SPCB met the Construction Manager in mid-January and pressed him on precisely this issue of outstanding risks. He indicated that there were no difficulties currently running which he perceived as being very significant problems. There are certainly a number of smaller detailed construction design issues to be resolved on a range of packages, (including Debating Chamber Roofing, Specialist Glazing, Windows, Stone Cladding and Fit-Out), but the Construction Manager does not see these as extra-ordinary and they are all manageable.

Each key package encounters risks on a daily basis, in addition to those risks associated with complexity of the design and the logistics of a tight programme and confined working environment. All of these risks change from day to day and are continually being managed by the Construction Manager and Design Team. One of the risk management actions currently being taken is a comprehensive analysis of all...
the outstanding design information that is required. This will be a valuable tool in enabling the whole team to prioritise the completion of outstanding detailing in line with the programme requirements and thereby significantly reduce the outstanding exposure of the programme to risk.

I have discussed Dr Simpson’s request that the full risk register be made available to the Committee with Paul Grice and the Project Team. I have concluded that, for obvious reasons of commercial confidentiality, this cannot be done at this sensitive stage in the project. However, I can reassure the Committee that both the SPCB and the HPG have had meetings with the construction manager and cost consultant in order to address detailed issues arising from the risk review. It was the conclusions reached at these meetings that led directly to the greater certainty expressed in the Presiding Officer’s recent letter to you. All of the risks described in the above paragraphs were accounted for in the cost and programme advice which was contained in the PO’s letter of 16 January.

Insurance

At column 2431 Margo Macdonald asked about insurance cover obtained by the Design Team. As Paul Grice indicated in giving evidence, I can confirm that the SPCB is protected from negligence or failings within the design team by a requirement for each of the designers to provide Professional Indemnity Insurance to a level of £5m for each and every claim.

Non Payments

Margo Macdonald also asked how claims for payments are assessed and processed. Before the Project Team receives requests for payment a lengthy checking process is carried out by the Construction Manager in conjunction with the Quantity Surveyors, the Architect and the Project Team's Senior Project Manager. This process certifies that the work for which payment is requested has been done in accordance with the terms and conditions of the Trade Contract. All construction payment requests are therefore subject to rigorous evaluation and are only passed to the Project Team if payment is in order. The Project Team has never refused a recommendation for payment.

Acceleration

We were also asked about the amount of spend that had at that time been made from the £7m (net) figure provisionally identified for acceleration measures in the Presiding Officer’s letter to you of 10 December. It is probably most helpful if I respond to that question as the situation presently stands which is that around £1.1m has been committed for acceleration, essentially for off-site manufacture relating to Specialist Glazing (£20k), Rooflights (£97k), Assembly Windows (£500k) and Stone Cladding (£500k). The cost consultant’s advice continues to be that the remainder of this £7m sum will require to be spent in order to maintain the current momentum on programme.
Flour City

You will recall that we were asked a number of questions in relation to the terminated contract with Flour City.

I can confirm that the Construction Manager did obtain 5 supportive references in respect of the performances of Flour City Architectural Metals Ltd in the USA, the Philippines and in Asia. Those references were, of course, provided in confidence, but it should be understood that such references are no guarantee that the company in question will not, subsequently, go into receivership.

In relation to the other substantive point raised by Fergus Ewing, I should also make it clear that no companies, Scottish or otherwise, were prevented from seeking to compete for the MSP building Cladding contract. Any company was entitled to submit an expression of interest in any of the contracts, which were all advertised in the Official Journal of the European Community (OJEC). That is the stage at which the extensive pre-qualification exercises are undertaken. I understand that the Construction Manager and the Design Team did consult with some Scottish companies during the normal information gathering processes on the MSP building Cladding contract, but that no guarantees were given, or could have been given, concerning the award of the contract.

As Mr Ewing is aware, these local companies would have required to have been successful in being engaged as sub-contractors to one of the potential bidders for the composite MSP cladding package. The Construction Manager did attempt to promote the cause of such Scottish companies by passing on their details to the package contractors but neither Bovis nor the client was at liberty to apply any more pressure than that.

Migration

Paul Grice undertook to give the Committee an update of the migration cost estimates at column 2440. At the last meeting in December it was reported that the SPCB had set aside migration budgets of £2.7m for 2002-03 and £3.3m for 2003-04. The later building completion date means that not as much will be spent in the current year on migration activities. The current forecast for migration costs in 2002-03 is less than £0.9m with some of the underspend from this year now falling into 2003-04. End year flexibility will again allow the remainder to roll forward into the following financial year’s budget. We expect the overall costs of migration to be contained within the £6m across the two years.

Penalty Clauses

At column 2441 Dr Simpson asked about ‘penalty clauses’. The nature of Construction Management prevents a predetermined level of damages being ascertained for each individual work package and as a consequence, no liquidated
damages exist within any of the Trade Contracts. Instead, the Contract allows for the actual costs of a trade contractor delay or failure to be recovered unilaterally.

For reasons of commercial confidentiality, we cannot give specific details of instances where damages or costs have been sought from Trade Contractors. However, it should be noted that it is the responsibility of the Construction Manager and the Cost Consultant to ensure that any legitimate costs are recovered.

**Conclusion**

Finally, I extended an invitation to Committee Members to visit the site, and I would strongly encourage Members to take up that invitation, to see construction progress at first hand, and gain a better visual understanding of some of the practical issues involved.

Robert Brown
Visit by the Select Committee on Modernisation of the House of Commons

On Tuesday 4 March, the Rt Hon Robin Cook, MP, Leader of the House of Commons and Chairman of the Select Committee on Modernisation of the House of Commons will visit the Scottish Parliament along with other members of the Committee. The purpose of the visit is to examine and discuss:

• The role of Committees in handling draft legislation (pre-introduction)
• Petitions and the role of the Public Petitions Committee
• The role of the Presiding Officer
• Electronic voting

As part of the programme for the visit, the Presiding Officers will host a working lunch for the members of the Committee. The lunch, to which the Conveners of all Committees are invited, will be held at 1pm on 4 March in the Signet Library. As the Convener is unable to attend, the Committee is asked to nominate another member to attend in his place.

A note of the remit and membership of the Committee on Modernisation is attached.

David McGill
February 2003
Remit of the Select Committee

The Select Committee on Modernisation of the House of Commons was appointed on 16 July 2001 to consider how the practices and procedures of the House should be modernised.

Membership of the Select Committee

Mr Robin Cook (Chairman, Lab, Livingston)
Ann Coffey (Lab, Stockport)
Mrs Lorna Fitzsimmons (Lab, Rochdale)
Barbara Follett (Lab, Stevenage)
Mr David Kidney (Lab, Stafford)
Mr Greg Knight (Con, East Yorkshire)
Mr Andrew Mitchell (Con, Sutton Coldfield)
Anne Picking (Lab, East Lothian)
Mr Peter Pike (Lab, Burnley)
Joan Ruddock (Lab, Lewisham & Deptford)
Mr Martin Salter (Lab, Reading West)
Mr Richard Shepherd (Con, Aldridge-Brownhills)
Mr Andrew Stunhill (Lib Dem, Hazel Grove)
Mr Paul Tyler (Lib Dem, North Cornwall)
Sir Nicholas Winterton (Con, Macclesfield)