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Dear Kenneth,

ANNUAL UPDATE ON CONTINGENT LIABILITIES

The Session 5 agreement between the Scottish Government and the Finance and Constitution Committee was updated, by agreement, on March 2021 to include a commitment that the Scottish Government will provide “an update annually, normally in September, of outstanding contingent liabilities, including any costs incurred”.

This is the first such update and I apologise that the intended timetable was not achieved. The choice of September was to coincide with the usual timing of the completion of the Scottish Government Consolidated Accounts. There is a natural read across from the information reported in the Accounts to the Committee’s more specific interest in those matters, which have come to it as part of the specific Committee process.

Unfortunately, the pandemic has impacted on the timing of financial reporting and auditing across all sectors. Annual accounts have met the statutory deadline, which is the end of December, but timings have slipped against the normal timetable: the Scottish Government Consolidated Accounts for 2019-20 and 2020-21 were both laid and published in December. Consideration of the scheduling of 2021-22 process is underway and it is hoped that timelines will advance but this is unlikely to restore to pre-pandemic timings for 2021-22 Accounts.

We have not agreed a particular format for this update and will be happy to review and revise the approach taken going forward following feedback from the Committee.

The Committee is invited to consider the information in the paper below and to seek any clarification or additional information that would be helpful.

Scottish Ministers, special advisers and the Permanent Secretary are covered by the terms of the Lobbying (Scotland) Act 2016. See www.lobbying.scot

The Committee is also invited to note that the relevant chapter in the Scottish Public Finance Manual (SPFM)¹ will shortly be reviewed. The Committee is welcome to suggest areas for the review to consider and views in particular on the following points, which have already been identified for improvement and are relevant to this report process:

- there is not presently a single log of all matters brought to the Committee under these provisions. Within the Scottish Government, it is for the relevant business area, or body, to follow the appropriate procedure; the annual accounts consolidate the accounting disclosures across the Scottish Government; a register maintained for the Committee would help to provide direct read across to the parliamentary reporting.
- in relation to matters which should be notified to the Committee, the SPFM could be clearer about when notification should take place; specifically when is notification via the annual report process deemed sufficient.

As the Committee is aware, certain contingent liabilities have been considered and approved by the Committee in private sessions or in private correspondence.

The Scottish Government remains committed to transparency as part of our Open Government Action Plan. The need for transparency is balanced against the need for commercial confidentiality in order to protect both Scottish Government, and our counterparty's, interests and to ensure that the Scottish Government can operate as a credible party to any future transactions.

On that basis, as certain contingent liabilities remain commercially sensitive, we request that Committee respects the confidential nature of the updates provided in relation to these instances and ensures that the information is kept **strictly private and confidential**.

I hope that the Committee finds this update helpful.

KATE FORBES

¹ [Scottish Public Finance Manual - gov.scot \(www.gov.scot\)](http://www.gov.scot)

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ANNUAL UPDATE ON CONTINGENT LIABILITIES

Background

1. The authority of the Parliament is required before the Scottish Government can grant a guarantee or indemnity which would, in effect, bind the Parliament into providing future funding in the event of the guarantee or indemnity maturing. This approvals process does not apply to a guarantee or indemnity which is granted under a statutory requirement to do so or is of a standard type and arises as an unavoidable feature of an activity authorised by statute.
2. The Written Agreement between the Scottish Government and the Finance and Constitution Committee sets out:
 - the Scottish Government's undertaking to submit to the Committee in advance, any proposals to grant any guarantees or indemnities in excess of £2.5 million (including those without limit),
 - the process for the consideration by the Committee.
 - and an undertaking to notify the Committee of all contingent liabilities between £300,000 and £2.5 million.
3. The Committee has considered a number of such proposals and this report fulfils the new requirement for the Scottish Government to provide "an update annually, normally in September, of outstanding contingent liabilities, including any costs incurred".

Specific reporting on contingent liabilities considered by the Committee

4. This report provides updates in relation to the contingent liabilities previously considered and approved by the Committee.
5. **Annex A** provides information in respect of each of the following matters considered by the Committee which are not commercially sensitive and confidential:
 - Lochaber Aluminium Smelter
 - Winchburgh Housing Development
 - Solheim Cup
 - UCI Cycling World Championships
6. **Annex B** provides information in respect of contingent liabilities which the Committee has considered in private and where the information remains commercially sensitive and confidential.

Reporting of Contingent Liabilities in Annual Accounts

7. The annual accounts of the Scottish Government and other bodies are prepared in accordance with the Government Financial Reporting Manual which applies International Financial Reporting Standards to the central government context. The accounts contain:

- disclosures about contingent liabilities that meet the accounting standard definition and
 - information about other liabilities arising from indemnities and guarantees which are included for parliamentary reporting and accountability purposes (in accordance with the Scottish Public Finance Manual).
8. Note 19 to the accounts provides information on Contingent Assets and Liabilities in accordance with accounting standards (International Accounting Standard 37). **Annex C** shows the detail of the 2020-21 Accounts disclosure.
9. Note 17b provides information for parliamentary purposes on guarantees, indemnities and letters of comfort, confirming that none of the items listed there meets the definition of a contingent liability within IAS 37, because the likelihood of a transfer of economic benefits in settlement is assessed as too remote. **Annex D** provides the analysis of the 2020-21 Accounts disclosure.
10. The full accounts are available at: [Scottish Government Consolidated Accounts: year ended 31 March 2021 - gov.scot \(www.gov.scot\)](https://www.gov.scot/Information/Accounting/Scottish-Government-Consolidated-Accounts-year-ended-31-March-2021). Equivalent information is available in the accounts of prior years.¹

Additional Information - updates to the 31 March 2021 accounts position

11. The regular in year financial management practices include reviewing any movements or expected changes to the contingent liabilities. A recent review was carried out in advance of the 31 March 2022 year end. In view of the elapsed time since the 2021-22 accounting period, Annex E provides some additional information on changes expected to the contingent assets and liabilities accounts log in the current financial year. SG Accounts for 2020-21. These will be confirmed or amended via the accounts preparation and audit process for the 2021-22 accounts disclosures.

¹ [Government finance: Financial reports and accounts - gov.scot \(www.gov.scot\)](https://www.gov.scot/Information/Accounting/Scottish-Government-Consolidated-Accounts-year-ended-31-March-2021)

Update on contingent liabilities

Lochaber

In December 2016 the Scottish Government entered into a 25-year financial guarantee relating to the hydro plant and aluminium smelter at Lochaber. This involved guaranteeing the power purchase obligations of the smelter if the business does not fulfil its obligations to pay for contracted power. The guaranteed annual amounts vary between £14m and £32m over the life of the contract. The Scottish Government receives an annual fee in return for the guarantee.

The Committee approved the contingent liability on 22 November 2016.

The Scottish Government's contingent liability is protected by a series of cross-guarantees and a comprehensive security package.

The Scottish Government has security over the smelter, the Fort William hydro-electric power station and substantial land holdings in support of its guarantee. This means that in a potential default scenario, the Scottish Government would be able to utilise these assets to recover any amounts it had required to pay.

The Lochaber guarantee exposure has been assessed in line with a HM Treasury Green Book analysis, concluding that the value of the security granted to the Scottish Government exceeds the present value of the payments guaranteed.

The net present value of the remaining power purchase agreement revenue stream over the remaining 20 years is £284.2 million (as at 17/01/2022), while the companies' valued the assets at Fort William at £438 million in their 2019 accounts.

In light of the current position of the GFG Alliance group, the Scottish Government reviewed the level of provision required with regards to their guarantee as part of the 2020/21 annual accounts process. The provision in the Consolidated Accounts increased from £37 million in 2019/20 to £161 million as at 31 March 2021. The Auditor General has confirmed the approach taken is reasonable.

There has been no call on the Government's guarantee and no public expenditure under the guarantee. All payments due under the guarantee – that is, fees to Government and PPA payments due to bondholders – are up-to-date.

Winchburgh Housing Development

As part of the Winchburgh Housing Development there is a potential liability in relation to loan repayments for the construction of Winchburgh Primary School. The housing development is due to pay the council as houses are sold.

The Scottish Government have entered into an arrangement to cover final costs if the developer cannot pay which can be called upon after 31 March 2026. The current value of potential liability as per the Scottish Government's most recently

published annual accounts for 2020/21 is £15m (2019-20: £15m).

The Committee approved the contingent liability on 13th September 2018. There has been no call on the guarantee to date.

Solheim Cup

This contingent liability was in respect of the Solheim Cup which Scotland hosted in 2019.

The Solheim Cup is a biennial golf tournament for professional women golfers contested by teams representing Europe and the United States. The event is owned by the Ladies' European Tour (LET).

The bid itself represented a contingent liability for the full costs of hosting the event – up to £19.2 million estimated at the time. There were also additional liabilities associated with the cancellation of the event once a formal contract was entered into. It was agreed at the time that the liabilities would be no more than €8 million. The particular scenarios under which these clauses would be invoked included material breach of the contract or negligence or inability to provide the venue for the event.

The Finance Committee approved the contingent liabilities associated with the Scottish Government's bid for the Solheim Cup 2019 on 13th August 2015. The Finance Committee also took evidence from the Minister for Sport, Health Improvement and Mental Health on 2nd September 2015 and further correspondence was submitted by the Minister in follow-up to this session on 23rd September 2015.

The event has now successfully concluded and this no longer represents a contingent liability. I can confirm there was no call upon the contractual contingent liabilities.

Union Cycliste Internationale

This contingent liability is in respect of the inaugural 2023 UCI Cycling World Championships that are to be held in Scotland in 2023.

This is a new event that will be held every 4 years and will bring together existing world championships of 13 different cycling disciplines to be held from the 3rd to the 13th August at a range of locations across Scotland. The event will be organised and delivered by a partnership involving the Scottish Government, EventScotland, Glasgow City Council, UK Sport and British Cycling.

The rights for the Cycling World Championships are held by the international governing body of the sport, the Union Cycliste Internationale ('UCI'), based in Switzerland. On behalf of the partnership and as principal funder and underwriter of the Championships, the Scottish Government signed a Long Form Agreement which represented a contingent liability.

The contingent liability relates to circumstances whereby the UCI incurs financial loss arising from the early termination of an agreement with one or more of its commercial sponsors as a result of a material breach in the Long Form Agreement by the Scottish Government and its hosting partners. The liability would also relate to the recovery of any 'wasted expenditure' or additional costs arising from the early termination of the Long Form Agreement as a consequence of a material breach by the Scottish Government and its hosting partners. The total liability in those circumstances is capped at 13.2 million Swiss Francs.

The contingent liability was approved by the Finance Committee on 11 August 2019.

I can confirm that there has been no call to date on the contingent liabilities contained within the Long Form Agreement to date.

Contingent Asset and Liability disclosures within 2020-21 SG Consolidated Accounts

19a. Contingent Assets disclosed under IAS 37: Provisions, Contingent Liabilities and Contingent Assets

The definition of a contingent Asset under IAS 37: Provisions, Contingent Liabilities and Contingent Assets is a possible asset, arising from past events, whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the entity's control.

NHS Employer's Liability estimated at £2m (2019-20: £2m).

Grants repayable as a result of sales of Housing Association Properties to tenants or as a result of conditions of grant being breached. Grants become repayable when conditions of grant cease to be met. It is not possible to predict the level of activity in future years.

Repayments of grant from the Open Market Shared Equity Scheme which allows people on low income to buy a share in a property, the balance being owned by a housing association and funded by grant from the Scottish Government. If the property is sold or an increased share is purchased by the owner, the grant becomes repayable. It is not possible to estimate the level of future receipts.

Grants repayable from Edinburgh Council Rent Guarantee - Project Resonance. Grant becomes repayable if either (a) projects do not proceed as planned, where it is repayable immediately, or, (b) projects are sold on privately up to 10 years from now. Timing and values are uncertain as to when events giving rise to the contingent asset are likely to occur.

There is an expectation of a secured creditor distribution to Scottish Ministers from Ferguson Marine Engineering Limited Administration. The net amount due to be recovered by the Scottish Government is yet to be confirmed.

19b. Contingent Liabilities disclosed under IAS 37: Provisions, Contingent Liabilities and Contingent Assets

The definition of a contingent Liability under IAS 37: Provisions, Contingent Liabilities and Contingent Assets is:

- a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control; or
- a present obligation that arises from past events but is not recognised because it is not probable that a transfer of economic benefits will be required to settle the obligation; or
- the amount of the obligation cannot be measured with sufficient reliability.

Only contingent liabilities above the threshold of £1m, which have to be reported and authorised by the Scottish Parliament in accordance with the written agreement between the Finance Committee and the Scottish Government, are included in the consolidated annual accounts.

NHS related

Clinical and Medical compensation payments of £394m (2019-20: £396m).

NHS Employer's Liability estimated at £4m (2019-20: £3m).

Housing related

The Mortgage Indemnity New Home Scheme (MI New Home) allows credit-worthy borrowers, locked out of the market by high deposit requirements, access to 90% to 95% LTV mortgages. The scheme is supported by a SG guarantee which sits behind cash indemnities set aside by participating house builders (for each house sold under the scheme). The guarantee valued at £7m (2019-20: £7m) can only be called upon once the indemnities are exhausted and lasts for 7 years. The guarantee scheme ended for applicants in 2015, therefore the potential calls on this scheme will end in 2022.

National Housing Trust guarantees of £4m (2019-20: £4m) which the Scottish Government are committed to giving but are not active until construction has been completed. The risk of a call on the guarantee is rising in line with the current COVID-19 crisis. We do not expect a call on the guarantee in the near future but we are monitoring each development closely through the Scottish Futures Trust to understand if tenants are continuing to pay their rent and thereby allow the loan debt to be serviced. This situation is subject to change.

As part of the Winchburgh Housing Development there is a potential liability in relation to loan repayments for the construction of Winchburgh Primary School. The housing development is due to pay the council as houses are sold. The Scottish Government have entered into an arrangement to cover final costs if the developer cannot pay which can be called upon after 31 March 2026. Current value of potential liability is £15m (2019-20: £15m).

Justice related

Claims against former independent Conveyancing and Executory Practitioners in Scotland. This is a contingent liability relating to an agreement to meet any valid claims arising from the acts or omissions of past independent conveyancing and executory practitioners, as defined by the Law Reform (Miscellaneous Provisions) Scotland Act 1990. The amount and timing of any outlay is uncertain.

COPFS has been subjected to several civil and damages claims. COPFS is opposing these claims but continues to review each case individually for liabilities that may arise as the legal process progresses. The value of these claims has yet to be finalised.

In a July 2020 Treasury response to an Employment Tribunal decision, it was held that benefits payable to male survivors should be equal to the categories of other survivors. Estimates of £2m (2019-20: £nil) have been obtained for any potential future liabilities.

Claims have been received for part-time sherriffs who may have been temp-sherriffs prior to 2000 with regard to their pension rights. Claims are being reviewed and there is an expectation that further claims may be received. The value of these claims has yet to be finalised.

The Redress for Survivors (Historical Child Abuse in Care) (Scotland) Bill was passed in Parliament in March 2021 and received Royal Assent on 23 April 2021. The Act provides for the functions of Redress Scotland and for Scottish Ministers to make arrangements for the establishment and operation of the redress scheme which will progress when the Provisions of the Act come into force.

Once operational, individuals will submit applications and the new independent body, Redress Scotland, will consider applications and make determinations, which may include an offer of a redress payment to be made by the Scottish Government. It is not possible to determine the number of applicants or the level of payments likely to be made under the scheme.

Rural related

The Supreme Court found that an element of the Agricultural Holdings Act 2003 breached the European Convention of Human Rights -Art 1 P1. Remedial legislation was enacted to resolve this and a small group of tenant farmers have taken SG to Court of Session seeking compensation for breach of their rights arising from the Remedial legislation. The court has issued initial judgement but litigation is still live and more court activity is required to resolve. The amount and timing of any outlay is uncertain.

EU CAP audits can result in future disallowances and a number of audits are in progress relating to CAP for scheme years 2015, 2016, 2017, 2018 and 2019. The level of late payment penalties from the EC to the UK member state and the split of penalties attributed to administrations are still to be formally concluded for CAP Pillar 1 scheme year 2015. The amount and timing of any outlay in relation to these two items is uncertain.

Sports events

In certain circumstances a payment of up to 13m Swiss Francs (£10m at 31 March 2021 exchange rates) (2019-20 restated: £11m) would be due to the UCI (the Union Cycliste Internationale) in relation to the UCI Cycling World Championships to be hosted in Scotland in 2023.

Decommissioning of offshore renewable energy installations

Functions under the Energy Act 2016 in relation to decommissioning offshore renewable energy installations in Scottish waters transferred to Scottish Ministers on 1st April 2017. This also means that the Scottish Government is now the funder of last resort in cases where the developers/owners cannot meet their decommissioning obligations. As the size of the Scottish portfolio of offshore energy projects grow so does the cumulative value of the decommissioning obligations and contingent liability. The value of the contingent liability to date has been reviewed in line with guidance issued by the Department of Business, Energy and Industrial Strategy entitled 'Decommissioning of offshore renewable energy installations: guidance notes for industry' published in March 2019.

The value of the contingent liability to date relates to 5 constructed and operational projects:

- Beatrice Offshore Wind Farm (Moray Firth) (c. £100m);
- Hywind Energy Park (Aberdeenshire) (c. £20m);
- Aberdeen Bay Wind Farm, also known as European Offshore Wind Deployment Centre (Aberdeenshire) (c. £20m);
- Moray East Offshore Wind Farm (Aberdeenshire) (c.£235m);
- Kincardine Offshore Floating Wind Farm (Aberdeenshire) (c. £20m)

And to 2 partially constructed projects:

- Nearth na Gaoithe Offshore Wind Farm (NNG) (Fife) (c. £100m)
- Orbital o2 (Orkney) (estimate not yet available)

Other

The Scottish Government occupies a number of leased properties which have dilapidations clauses in the leases. These properties are maintained in excellent order, but there is a potential liability to reinstate the internal layout of these buildings to their original floor plans. These costs will be subject to negotiation and the monetary impact is not reliably estimable.

Accountancy in Bankruptcy has recognised one contingent liability in their accounts. Further advice is being sought in order to assess the likelihood of any financial implications (31 March 2020: nil).

Education Scotland has recognised one contingent liability in their accounts. Further advice is being sought in order to assess the likelihood of any financial implications (2019-20: £nil).

As part of Transport Scotland's normal course of business, the Forestry Commission grants the right to use a forestry track as an emergency diversion route on the A83 Rest and Be Thankful on the understanding that Transport Scotland has the liability for any incidents that may occur whilst the track is being used for this purpose. The potential obligation is estimated at £5m (£2019-20: £5m) but it is considered unlikely that any liability will occur.

Guarantees, Indemnities and Letters of Comfort disclosures within 2020-21 SG Consolidated Accounts

17b. Guarantees, Indemnities and Letters of Comfort

The Scottish Government entered into the following guarantees, indemnities or provided letters of comfort. None of these is a contingent liability within the meaning of IAS 37, *Provisions, Contingent Liabilities and Contingent Assets*, since the likelihood of a transfer of economic benefit in settlement is too remote. They are included for parliamentary reporting and accountability purposes.

Only guarantees and indemnities above the threshold of £1m, which have to be reported and authorised by the Scottish Parliament in accordance with the written agreement between the Finance Committee and the Scottish Government, are included in the consolidated annual accounts.

Guarantees

Guarantee to Lothian Pension Fund in relation to the admission of Scottish Futures Trust Ltd.

Guarantee to Lothian Pension Fund in relation to the admission of The Scottish Homes Pension Fund.

Guarantees for 10 local government pension schemes, as a result of Visit Scotland taking on the staff from the local area tourist

Guarantee to Lothian Pension Fund in relation to the admission of The Scottish Legal Complaints Commission.

Guarantee to Lothian Pension Fund in relation to the admission of The Scottish Agricultural College.

Guarantee to Lothian Pension Fund in relation to the admission of Youthlink and Scotland's Learning Partnership.

Guarantee to Fife Council in relation to the admission of The Scottish Agricultural College to the LG Pension Fund.

Guarantee to Dumfries and Galloway Council in relation to the admission of The Scottish Agricultural College to the LG Pension

Guarantee to Highlands and Islands Enterprise in relation to their pension scheme.

Guarantee to Strathclyde Pension Fund in relation to admission of Scottish Canals.

Guarantee to Shetland Council Pension Fund.

Guarantee to Orkney Islands Council Pension Scheme.

Guarantee to Highland Pension Fund.

Indemnities

At the beginning of the year there was an existing indemnity relating to objects lent under the National Heritage Act 1980 and the National Heritage (Scotland) Act 1985. The year-end balance depends on new acquisitions and the number of exhibitions that these pieces are included in during the financial year, and at 31 March this was £1,277m (2019-20: £1,277m)

Existing indemnity for local museums and galleries dependent on the number of new acquisitions and number of exhibitions that these pieces were included in during the financial year, valued at £17.2m (2019-20: £17.2m) at 31 March.

A specific indemnity has been agreed with the Australian Museum Trust with regard to the Tyrannosaurus Exhibition hosted by the National Museum of Scotland.

Indemnities provided by the former Scottish Homes to mortgage lenders £0.5m (2019-20: £0.5m).

Letters of Comfort

None

Additional Information - Financial Year 2021-22 potential changes

New Items - None

Closed items

Contingent Liability	Held by	Update
Claims have been received for part-time Sheriffs who may have been temp-sheriffs prior to 2000 with regard to their pension rights. Claims are being reviewed and there is an expectation that further claims may be received.	Justice	Sponsor team received invoice for costs of Back-Stop issues standing at £840k in November. Four additional claims are looking to be settled which have an estimated cost of around £2.3m subject to calculations to be carried out by MOJ/XPS. These claims will be processed by the end of the financial year
Transport Scotland had received a claim in respect of damage to a commercial property, Oak Mall Shopping Centre Greenock, purported to be caused by rainwater passing from the bridge over the property that carries the A78 trunk road that Transport Scotland is responsible for maintaining.	Transport Scotland	The mall has since been sold and no obligation has been passed to the new owners.

Pension Funds	Held by	Update
Guarantee to Lothian Pension Fund in relation to the admission of The Scottish Legal Complaints Commission	SG Core	The last employee left in 2019-20. The final payment to the fund has been agreed and the balance of £67k will be paid back in 2021-22.