Minister for Business, Trade, Tourism and Enterprise
Ivan McKee MSP

Scottish Government
Riaghaltas na h-Alba
gov.scot

T: 0300 244 4000
E: scottish.ministers@gov.scot

Kenneth Gibson MSP
Convener
Finance and Public Administration Committee
The Scottish Parliament
Edinburgh
EH99 1SP

1 December 2022

Dear Kenneth,

LOCHABER GUARANTEE CONTINGENT LIABILITY

With the laying of the Scottish Government's Consolidated Accounts for 2021/22 in Parliament I wanted to draw the Committee's attention to the reduced accounting provision relating to the Lochaber Guarantee and, as I did previously on 16 December 2021 in respect of the 2020/21 accounts provision, give reassurance to the Committee that this does not impact the Scottish Government's funding position.

The previous accounting provision was assessed at £161 million for the 2020/2021 accounts. The new accounting provision has been assessed as £114 million, a reduction of £47 million. The provision is calculated using the requirements of IFRS 9 (International Financial Reporting Standards) for Financial Guarantee Contracts. The Auditor General has stated that the Scottish Government's approach to setting the level of provision against the potential exposure through the guarantee is reasonable.

The provision is informed by a technical assessment of a range of credit risk scenarios carried out by independent advisers. The change in provision is an accounting adjustment only and has no impact on Scottish Government spending. The Guarantee has not been called and the Scottish Government continues to earn the expected income in the form of Guarantee fee payments from the GFG Alliance which are up to date.

The provision is not a forecast of likely outcomes in respect of the Guarantee.The provision remains under annual review and is therefore subject to change.

For planning rather than accounting purposes, the Scottish Government assesses the Lochaber guarantee exposure in line with HM Treasury Green Book guidance.

However, international financial accounting standards require the Scottish Government to take a more prudent view on the calculation of the potential liability and the value of the underlying security.

The reduction in the provision has been influenced by the anticipated increase in the value of the primary asset while GFG Alliance has also continued to meet the power purchase agreement (PPA) payments due to bondholders.

Security

As previously advised the Scottish Government is the guarantor of the PPA revenue stream to the bondholders while the primary payment obligation rests on the smelter to pay for the power it consumes.

Should the Scottish Government require to make any payment under the Lochaber Guarantee and Reimbursement Agreement, it is thereafter entitled to recover the full amount of any such payment from other members of the Liberty / Simec Groups by virtue of a series of cross-guarantees.

The Scottish Government maintains security over the smelter, the Fort William hydro-electric power station and substantial land holdings in support of its guarantee. This means that in any potential default scenario, the Scottish Government would be able to utilise these assets to recover any amounts it had required to pay. The value of the Lochaber assets secured to Ministers is greater than the level of exposure.

Economic return

The Scottish Government's guarantee has helped to secure the future of aluminium and renewable energy production in Lochaber and supported many high-skilled jobs. The combined smelter, hydro-electric power station and estates businesses are operating profitably and have created 40 new jobs since 2016, increasing direct employment in the complex to around 200 jobs while supporting a valuable supply chain with hundreds of associated jobs.

It was absolutely right for the Scottish Government to provide the financial guarantee to protect jobs in the region, underpin additional investment at the site, and promote industry in Scotland.

Should the Committee require anything clarified further I would of course be happy to provide more information.

IVAN McKEE

St Andrew's House, Regent Road, Edinburgh EH1 3DG
www.gov.scot