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Mr Edward Mountain MSP
Convener,
Rural Economy and Connectivity Committee,
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The Scottish Parliament
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Dear Convener,

Inquiry into the construction and procurement of ferry vessels in Scotland

I refer to the publication of the Committee's report, following its inquiry into the construction and procurement of ferry vessels in Scotland. I remain grateful for the opportunity to present evidence to the Committee during its inquiry, recognising the public interest in the subject and Scottish Ministers' commitment to transparency on the matters raised. I would like to take the opportunity to thank the Committee members for their detailed consideration of what are broad ranging, complex and important issues.

There is value in the Committee's independent assessment of the issues raised before it, and my colleagues, particularly the Cabinet Secretary for Economy, Fair Work and Culture, and I have taken time to reflect upon its content. There are some conclusions in the report with which we do not agree, and some instances where it is not clear to us how the conclusion or recommendation made reflect the evidence presented to inquiry. However, recognising that in relation to the MV Glen Sannox and hull 802, the outcome has not been that for which we had hoped at the point of awarding the contract to FMEL, we remain receptive to constructive feedback regarding areas for improvement going forward. In this response, I focus upon those opportunities for improvement, rather than seeking to repeat the detailed and well supported evidence that has previously been provided by Scottish Ministers. I trust that the Committee recognises the transparent and constructive manner in which Scottish Ministers and officials working on our behalf have engaged with the inquiry to facilitate its consideration of the issues within its remit. I also trust that the Committee recognises that Ministers' own process of reflection and improvement is

already underway, as we described in our evidence to the inquiry to ensure we supported the Committee in preparing its report.

Decision Making Structure

Scottish Ministers remain fully supportive of our transport agency, Transport Scotland, of Caledonian Maritime Assets Limited (CMAL) and of CalMac Ferries Limited (CFL). The Committee highlights areas for improvement in relation to the “tripartite” relationship going forward. However, we believe a balanced view is required. I would like to record my own recognition of and gratitude for the services which have been and continue to be successfully delivered across the Clyde and Hebrides and Northern Isles networks, as a consequence of the hard work of the staff within these three organisations. It is of course important that we learn from occasions where outturns or experiences are not as intended and that we consider areas for continuous improvement and increased efficiency. But we must also recognise and safeguard those areas in which the tripartite arrangements already perform well.

Without prejudice to our thanks to and support for those three organisations, Scottish Ministers have already committed to review the current legal structures and governance arrangements around the provision of ferry services, which pre-date our taking office in 2007. The three organisations involved have committed to engage constructively in that review process and to reflect on any recommendations produced.

The purpose of this project is to reflect on whether the governance arrangements between the tripartite bodies remain fit for purpose having regard to the overarching objective of effective, efficient and economic delivery of lifeline ferry services.

We anticipate this will deliver reflections on positive aspects of the current arrangements, areas for improvement, and balanced recommendations for the optimal corporate structures and governance arrangements going forward. The project should identify any specific, practical recommendations to improve transparency of decision making.

Procurement for consultant advisers to support the project is already underway with the project due to commence in Spring 2021. It is our intention that interim findings and recommendations will be delivered in late 2021, informing work for 2021/22.

Community Engagement

As I set out in my evidence to the Committee, Ministers are committed to the principle that the views of those directly affected by decisions around ferry services are heard in the decision making process and that any engagement is meaningful. As the Committee itself found, there are often competing views from different groups around aspects of ferries policy and it is important to balance these in our decision making. We will improve transparency on how community views are taken into account in decision making, including providing a clearer explanation of why specific design decisions have been reached, and why on some occasions community or individual preferences have not been reflected in a bespoke design as the final

outcome of the design process, for example where a vessel has to be capable of providing a wider resilience role on a number of routes.

We have already begun the process of developing a revised communications and stakeholder strategy. I welcome the positive feedback on our most recent engagement on the new Islay vessel, provided to the Committee by the Calmac Community Board. We will continue to build on this in refining our processes.

Strategic Planning for Vessel Replacement

The report highlights a number of areas where more strategic and long term planning may be beneficial to support the replacement of the existing fleet and to give operators and communities more certainty over the programme for new tonnage. Scottish Ministers have already committed to undertake this work.

Building on our successive Vessel Replacement and Deployment Plans, we will produce and maintain a long-term plan and investment programme for new ferries and development at ports to improve resilience, reliability, capacity and accessibility, to increase standardisation where possible, to reduce emissions, to meet the needs of island communities, and to give confidence in our ongoing commitment to island connectivity. This will address vessels serving both the Clyde and Hebrides and the Northern Isles networks. To underpin the delivery of these plans, we will invest at least £580 million during the next five years, as set out in the Infrastructure Investment Plan.

That strategic policy development will not delay investment decisions in the interim.

Project design

The inquiry expressed some interest in the process for design of new vessels generally, and the process adopted in relation to 801 and 802 specifically. I trust that the evidence provided by Scottish Ministers has assisted the Committee with its understanding of what is a well- established process, with the parties' roles and responsibilities clearly set out in the international standard contracts to deliver the vessels.

I also trust that the evidence provided by Scottish Ministers has assisted the Committee with its understanding of the various considerations which must be balanced in the specification of any new vessel alongside what can be competing community views. We remain committed to the principles set out in our evidence to inquiry.

We will, as covered in our evidence to the Committee, continue to strive for greater standardisation, where possible. For example, current work on the new Islay vessel will introduce standardised bridge, engine room and safety equipment to be replicated throughout new vessels for the fleet. Careful consideration is being given to any port infrastructure upgrades required to support the introduction of new vessels as part of the overall investment decision making process, so that whole project costs are understood, and to ensure value for money. It is important to note that in some cases investment is required even if existing vessel were continuing to

operate due to the port asset having reached life expiry – as was the case with Brodick and we see at Kennacraig as set out in engagement for the Islay Vessel replacement programme.

We will continue to look at opportunities to reduce the emissions and carbon footprint of the fleet. This will include exploring all technologies, hull design and fuel type.

These considerations are not new, as previously outlined in our evidence to the inquiry. But we will reflect on the feedback provided to inquiry by third parties, and seek to better communicate to interested parties how these factors are balanced in future decision making.

Contract procurement and management

CMAL owns the vessels in the Clyde and Hebrides fleet and directly procures those vessels for its own ownership. I am satisfied that procurements in relation to 801 and 802 were undertaken fastidiously, in good faith and following appropriate due diligence. In reaching that view, I attach weight to the independent review undertaken in May 2018 as described in evidence to the inquiry and to which I referred in giving my won evidence.

However, CMAL is already introducing improvements to its own processes. These improvements should not be viewed as criticism of the process adopted in relation to 801 and 802, but build upon best practice exhibited in other areas, and the experience of the current Chief Executive Officer, who was not in post at the time of contract award for 801 and 802. These improvements include additional diligence to be undertaken on the financial standing of the preferred bidder, to be informed by independent advice. Financial monitoring will be undertaken prior to any contract award and continued at appropriate stages throughout the contract period. Going forward, CMAL proposes to obtain greater support from independent naval architects, to work alongside its in-house team when undertaking technical assessments during the procurement process.

CMAL will also give consideration to the frequency and level of milestone payments applied in the industry standard BIMCO contract. This must balance the need for appropriate contractor cash flow, the impact of payment terms on contract pricing, and the security and confidence in delivery to CMAL as the client.

I trust that these reflections provide the Committee with confidence that Scottish Ministers welcome the constructive challenge provided by the inquiry, and that we are already making progress on improvements going forward with some of this work already having progressed.

There are however some points in the Committee's report with which I cannot agree. I wish to retain a constructive and forward looking focus rather than to repeat the evidence which has already been provided to the inquiry, in form of a detailed rebuttal to the committee's report. However, there some points which warrant clarification. The following points of clarification are offered in the same constructive spirit as Ministers have sought to engage in the entire inquiry process.

Perceived failings in relation to 801 and 802

The Committee has sought to identify specific points of failure and areas for improvement in each of the design, procurement, contract award and contract management phases of projects 801 and 802. Those principally focus on the actions of Scottish Ministers acting through Transport Scotland and upon the actions of CMAL as procuring authority. I have set out in preceding paragraphs the steps which are already underway to make improvements in these areas.

I would however, respectfully, record some disappointment on our part that the report does not better reflect the contribution of the contractor's non-performance, contract management and financial management, described in independent evidence to the inquiry, to the outcomes in relation to 801 and 802. It remains our view that contractor failure has been a very significant factor in the difficulties we have seen arise in relation to delivery of hulls 801 and 802. On behalf of the Scottish Government, I would also take the opportunity to record our disappointment that the report does not fully reflect the extensive and proactive steps taken by Scottish Ministers and by CMAL to facilitate and negotiate a better outcome with the contractor, which are clear matters of public record.

While there are lessons to be learned, which we have acknowledged, we do not accept the Committee's description of a "catastrophic failure". In the face of contractor non-performance at the yard in relation to 801 and 802, the Scottish Ministers took action to secure the future delivery of the vessels to serve the island communities which rely upon them, to secure the employment associated with continuation of those vessel contracts, and to secure the future of the yard in Inverclyde. Scottish Ministers took balanced, informed decisions following appropriate diligence and independent advice. In reluctantly accepting increased cost and timescale for the delivery of the vessels, Scottish Ministers have acted and have secured hundreds of skilled jobs and wider economic activity. I do not regard those difficult decisions to represent a failure.

Commercial Loans

I note the Committee's concerns regarding the purpose of the commercial loans provided to FMEL by the Scottish Government and the sharing of information about them with CMAL. The purpose of the two loans is recorded in the contract documentation published on the Scottish Government's website (see Clause 2.2 of both the September 2017 and June 2018 loan agreements) alongside the conditions for utilisation and the financial and operational performance monitoring associated with loan drawdown.

We took great care to ensure a proper separation between the two contractual spheres: one relating to CMAL's ship building contracts with FMEL and a second relating to the FMEL's business plan and funding needs. The Scottish Ministers could not share FMEL's confidential commercial information with any of FMEL's clients, including CMAL, without breaching its duty of confidentiality to FMEL. However, Scottish Ministers did have a full understanding of the complex commercial and contractual issues at play when taking decisions.

Updates Sought

I note the Committee's request to provide an immediate update if it is anticipated that the pandemic is going to have any further significant impact on costs or timetable beyond those identified by the August 2020 update. Scottish Ministers are committed to being transparent in reporting progress on 801 and 802 and will ensure that the Committee is kept informed of progress at appropriate stages. Illustrative of this commitment, I note that Tim Hair, the Director at Fergusons, proactively wrote to the Committee on 19 January 2021 to provide an update on the impact of Covid 19 on production at the yard.

The Committee also asked for an update on measures being taken to mitigate impacts on communities due to the delays in bringing new vessels into the fleet as a result of the delays around 801 and 802. Scottish Ministers and CFL strive to ensure that the existing fleet is deployed efficiently and effectively and work with communities to consider improvements that can be delivered within available resources. Scottish Ministers have provided CMAL with additional funding of £4 million per annum in resilience funding over the past three years to enable improved monitoring and repair or replacement of older equipment on board vessels and to stockpile equipment to minimise any loss of service. CFL already has procedures around essential appointments for islanders to use at short notice which were put in place before the inquiry commenced. We are constantly looking at ways to maximise the use of existing deck, including improvements anticipated through the new booking system that CFL is working to deliver.

Audit Scotland

The Committee has indicated three areas that they have drawn to the attention of Audit Scotland – financial management of the ferries contract by CMAL, the role played by Scottish Ministers acting through Transport Scotland in relation to those contracts, and the agreement and payment of commercial loans to FMEL by Scottish Ministers.

Audit Scotland's has routine and full access to any financial and contractual information it requires from the Scottish Government. Officials routinely brief Audit Scotland on matters relevant to the Government's Consolidated Accounts. Any decision to undertake such further reviews as suggested by the Committee would, of course, be a matter for the Auditor General, but I would confirm that Scottish Ministers would welcome and fully cooperate in any review that the Auditor General determines should be undertaken.

I trust this information is helpful.

Kind regards



PAUL WHEELHOUSE

