



**Cynulliad Cenedlaethol Cymru
The National Assembly for Wales**

**Y Pwyllgor Archwilio
The Audit Committee**

**Dydd Iau, 12 Gorffennaf 2007
Thursday, 12 July 2007**

**Cynnwys
Contents**

- 4 Ethol Cadeirydd
Election of Committee Chair
- 4 Cyflwyniad, Ymddiheuriadau, Dirprwyon a Datgan Buddiannau
Introduction, Apologies, Substitutions and Declarations of Interest
- 4 Cyflwyniad i Gylch Gwaith a Gwaith y Pwyllgor Archwilio
Introduction to the Remit and Work of the Audit Committee
- 10 Cynnig Trefniadol
Procedural Motion
- 10 Diogelu Arian Cyhoeddus ym Mhrosiectau LG, Casnewydd—Rhagor o Dystiolaeth
Protecting Public Money in the LG Projects, Newport—Further Evidence
- 23 Cynnig Trefniadol
Procedural Motion

Cofnodir y trafodion hyn yn yr iaith y llefarwyd hwy ynddi yn y pwyllgor. Yn ogystal,
cynhwysisir cyfieithiad Saesneg o gyfraniadau yn y Gymraeg.

These proceedings are reported in the language in which they were spoken in the committee.
In addition, an English translation of Welsh speeches is included.

Aelodau Cynulliad yn bresennol
Assembly Members in attendance

Lorraine Barrett	Llafur Labour
Eleanor Burnham	Democratiaid Rhyddfrydol Cymru Welsh Liberal Democrats
Jocelyn Davies	Plaid Cymru The Party of Wales
Chris Franks	Plaid Cymru The Party of Wales
Janice Gregory	Llafur Labour
Lesley Griffiths	Llafur Labour
Irene James	Llafur Labour
David Melding	Ceidwadwyr Cymreig (Cadeirydd y Pwyllgor) Welsh Conservatives (Committee Chair)
Darren Millar	Ceidwadwyr Cymreig Welsh Conservatives

Eraill yn bresennol
Others in attendance

Gillian Body	Swyddfa Archwilio Cymru Wales Audit Office
Jeremy Colman	Archwilydd Cyffredinol Cymru Auditor General for Wales
Ian Gibson	Dirprwy Swyddog Cydymffurfiaeth, Swyddfa Gydymffurfiaeth y Cynulliad, Llywodraeth Cynulliad Cymru Deputy Compliance Officer, Assembly Compliance Office, Welsh Assembly Government
Jeffrey Godfrey	Cyfarwyddwr Gwasanaethau Cyfreithiol, Llywodraeth Cynulliad Cymru Director of Legal Services, Welsh Assembly Government
Gareth Hall	Pennaeth y Grŵp, Adran yr Economi a Thrafnidiaeth, Llywodraeth Cynulliad Cymru Head of Group, Department for the Economy and Transport, Welsh Assembly Government
Sharon Linnard	Cyfarwyddwr, Gweithrediadau a Buddsoddi Cymru, Llywodraeth Cynulliad Cymru Director, Operations and Invest Wales, Welsh Assembly Government
Ben Robertson	Swyddfa Archwilio Cymru Wales Audit Office
Ian Shuttleworth	Pennaeth Monitro a Gwasanaethau Proffesiynol, Gweithrediadau a Buddsoddi Cymru, Llywodraeth Cynulliad Cymru Head of Monitoring and Professional Services, Operations and Invest Wales, Welsh Assembly Government
James Verity	Swyddfa Archwilio Cymru Wales Audit Office

Swyddogion Gwasanaeth Seneddol y Cynulliad yn bresennol
Assembly Parliamentary Service officials in attendance

Dan Collier	Dirprwy Glerc Deputy Clerk
Dr Kathryn Jenkins	Clerc Clerk

*Dechreuodd y cyfarfod am 1.30 p.m.
The meeting began at 1.30 p.m.*

Ethol Cadeirydd
Election of Committee Chair

[1] **Dr Jenkins:** Good afternoon. The first item of business is the election of committee Chair, and I invite nominations from committee members.

[2] **Darren Millar:** I nominate David Melding.

[3] **Jocelyn Davies:** I second that nomination.

[4] **Dr Jenkins:** Are there any further nominations? I see not. Therefore, I declare that David Melding is duly elected Chair of the Audit Committee.

David Melding: I thank you for your trust in my abilities as Chair. That was an effortless transfer, as you can see, with the infrastructure coming in front of my microphone to declare me in this high office. I welcome all Members and officials to the first meeting of the Audit Committee in the third Assembly.

Cyflwyniad, Ymddiheuriadau, Dirprwyon a Datgan Buddiannau
Introduction, Apologies, Substitutions and Declarations of Interest

[5] **David Melding:** I will start by outlining the usual housekeeping rules, which some new Members will not have heard. These proceedings will be conducted in Welsh and English. When Welsh is spoken, a translation is available on channel 1, and anyone who is hard of hearing can amplify the proceedings by using channel 0. Please turn off all mobile phones and any electronic equipment, as they interfere with our broadcast and translation systems. In the case of an emergency, please leave via the nearest exit, and the ushers will assist you to leave safely.

I have received apologies from Karen Sinclair. If any Member needs to make a declaration of interest, now is the appropriate time. I see that there are none, and so we will move to our first substantial item, namely item 3 on the introduction to the remit and work of the Audit Committee.

1.31 p.m.

Cyflwyniad i Gylch Gwaith a Gwaith y Pwyllgor Archwilio
Introduction to the Remit and Work of the Audit Committee

[6] **David Melding:** We have received a paper, marked paper 1, and I will now ask Jeremy Colman, Auditor General for Wales, to introduce his paper. In welcoming him, I also extend our best wishes for a full and speedy recovery as he has broken his leg. News broadcaster-esque, you cannot observe the injury because he is seated, but I can assure you

that he had to hobble in, and we are grateful to him for putting his public duty first and putting up with the inevitable discomfort. Jeremy, would you like to introduce your paper?

[7] **Mr Colman:** Thank you, Chair. There will be an opportunity to sign the cast after the committee meeting. [Laughter.]

[8] The paper that I have circulated to the committee is—as you might think appropriate for an organisation that bases its work on evidence—a stock take of the past achievements of this committee’s predecessors, which is in part a stock take of the work that the Wales Audit Office and before that, my predecessor as Auditor General for Wales, had done. That paper is, essentially, for your reference; I do not propose to go through it now. However, I wish to talk about how the committee has conducted its business in the past. It is, of course, open to you to change things considerably, if you wish to do so. I will also talk about how we, in the Wales Audit Office, support the committee and what else we do, because we do other things that sometimes bubble up to the attention of the committee and sometimes do not. So, that is what I want to talk about.

[9] On the meetings themselves, the format that has been developed over the years is closely based on the practice of the Public Accounts Committee at Westminster with some differences—improvements, in my opinion. So, in preparation for a meeting, the first thing that you will see, if there is an evidence-taking session, is a brief on a report from my office. The brief will summarise the report and will suggest lines for questioning that the committee may wish to follow. In practice, the committee has wished to follow those lines of questioning, which is one of the areas in which it differs from the Public Accounts Committee. I think that that is a real strength, as it comes over to witnesses that the committee as a whole is pursuing a line of questioning. It is, of course, open to committee members to add questions, if they so wish, and it is sometimes quite helpful to us if they do so.

[10] So, a brief is circulated before the meeting. We have been in the practice of holding briefing sessions for the committee at various times in the run-up to the hearing, a day or two before. In practice, very few committee members have found time to come to those briefing sessions, and you may want to discuss what to do about that. Options range from not having briefing sessions at all to having them in some different form, place or manner. That is entirely up to you. We are at your service; it is not in any way an inconvenience for us to brief the committee and, in fact, we welcome the opportunity to do so. We can sometimes add a bit of background to the report. The reports are, of course, complete, but they are written in very formal language, and sometimes it is helpful if we can explain a little about what has been going on behind the scenes.

[11] You will then have the evidence session on the report and witnesses will attend. Invariably, the witnesses will be the relevant accounting officer, the senior civil servant with responsibility for that area of Assembly Government expenditure, and, occasionally, third parties are invited. In an NHS study, for example, the chief executive of a trust or local health board might be invited. A real third party, if you like, would be someone like the vice-chancellor of Cardiff University, for example, people from private companies, or recipients of funding.

[12] The session concludes when you have got through the questions and made any additions that you wish to make. This year—and I think I am right in saying that it is for the first time—we have included in the agenda an evaluation of the evidence-taking session, as we have done today. That is in private session at the end of the meeting. It has been a really useful innovation. It enables the committee to say what struck them about the witnesses and to make any points that they think are important—things that either were or were not said. That is a real help to us for the next stage, which is the drafting of a report that will be the Audit Committee’s report on that session. It takes a little while to put those reports together,

because they are very full and they cross-reference the evidence very closely. So, usually, two or three meetings after the evidence-taking session, you will get a draft report from me for you to agree. If anyone has comments on draft reports, it is helpful to have them before the meeting, because then we can take them into account, but, of course, we are at your service and we will take comments made at any stage into account, and the committee will agree a report—with recommendations.

[13] I emphasised the fact that committee reports contain recommendations, because the Assembly Government is required to respond to the committee's recommendations within a fixed timetable, and it is normal practice for me to advise the committee on how far the response can be judged to be satisfactory. That is sometimes less straightforward than you might think. In recent years, the Assembly Government has very helpfully enumerated the recommendations and then put the words 'agreed', 'rejected' or 'part agreed' next to them, which makes life a little easier. However, occasionally, it has said that it has agreed to recommendations when we have found, on closer reading, that it has not accepted them at all; on some occasions, it has claimed to disagree with the recommendations but, when reading its response closely, we have been found that it has accepted them in full. So, that points out the need for us to read what it says very carefully, and advise the committee on whether the response is satisfactory and what should then happen.

[14] There are a range of options, as far as the committee is concerned. It can do nothing—and that does not mean that we do nothing; we follow it up to ensure that the Assembly Government acts as it says it will and, if necessary, come back to the committee in due time—or, at the other end of the scale, if the response is completely unsatisfactory, it is open to the committee to have the witnesses back to ask them why they are unable to do what the committee has recommended. I do not suggest that the committee will want to do that every time, but once in a while it might be a good thing, if you have a case in which the committee's recommendations have not been wholeheartedly accepted.

1.40 p.m.

[15] So, that is the sequence of a committee hearing. Let us consider what happens before all of that. Clearly, the stimulus for a committee hearing is, generally speaking, a report from me. I consult the committee on how I might exercise my powers of reporting, and I have generally done that by presenting a very long list of ideas. In the past, committee members have been a very fertile source of further ideas, and have sometimes modified proposals that I have laid before them. I then think about what you have said. It is a consultation, but the decision on what I do is mine alone. It is not appropriate to use the word 'commission' in relation to what you ask me to do, though of course I would take very seriously indeed any requests that you make. However, technically, it is my decision. We then do the work—or my colleagues, mostly, do the work—and bring a report to the committee in due time.

[16] Let me explain how we do the work, as it goes through a number of stages. We follow a very specific methodology, which, among other things, is designed to produce reports that are very easy for readers to use. The first thing that we do is called an 'issue analysis': we consider which question the report will answer. We always like to focus on a single question, which might be: has the Government successfully implemented its policy to promote increased physical activity in Wales? That is a real-life example. We consider which sub-questions need to be answered in answering the main question, and so on. We create a logical tree of questions, to which we add the bits of evidence that we collect. That defines the fieldwork, my colleagues carry out the fieldwork, and we bring it all together in what we call the 'drawing-conclusions meeting', which is about constructing a different kind of tree—one which answers the questions. So, if the answer is 'not really'—and that is generally the answer—the next phase is to show why. We will say, 'Because of this, that and the other', and we will show why, pointing to this and that evidence, and so on. In that way, we grow a

tree of reasons that terminates in evidence, so that the conclusions are based logically and clearly on the evidence.

[17] You may ask how that makes a report easy to read. The answer is—and, unfortunately, you do not have one in front of you—that the contents page of our reports tells you the whole story. If you read nothing else, read the contents page. If you have time to read more than the contents page, read the first page or two of the summary; it will give you a little more detail. If you can spare a bit longer, read the whole summary. However, you do not even have to read the whole summary to understand the report. The first couple of pages will give you the question, the answer, and the reasons for the answer.

[18] **David Melding:** You are going to inculcate bad habits. With that warning, I will let you go on. [Laughter.]

[19] **Mr Colman:** If you are really enthusiastic, as I hope you always will be, you can read the whole report, which gives you all the detail, all the evidence, and so on.

[20] Perhaps I should have said that, in preparation for hearings, however much or little of the report you have read, should you have any questions at all, I would be absolutely delighted to answer them. We try to make the reports readable—readable to people who are very busy and are not necessarily experts in the subject. Of course, sometimes we deal with very technical subjects, and maybe we do not always achieve absolute clarity, but that is what we try to achieve, and we really welcome feedback if you do not understand any particular report, or if there is some issue that you think is missing. We have been known to miss issues, but not, I hope, very often.

[21] We go through a process of clearance before the report gets to you, and this is sometimes criticised and sometimes quite controversial. We show the draft report to the audited body, which, in your case, generally speaking, is an Assembly Government department. I ask the relevant accounting officer to agree, in writing, that the report is factually accurate, that the conclusions follow from the facts and that the facts are fairly represented. So, it is a very high standard of agreement that I seek. I seek it not because I do not want to offend important civil servants in the Assembly Government—I do not mind that at all, if any of them need to be offended—but to help the committee in the evidence session. The committee would be in a very difficult position, I suggest, if you had a witness who said, ‘The alleged fact on page 23 of the report is wrong’. That would be difficult. I would say, ‘Oh no it isn’t’, and he would say, ‘Oh yes it is’, and you could not resolve that. So, we carry out clearance with accounting officers to avoid arguments. It is not intended to lead—and I would be horrified if it did—to bland, wishy-washy reports with no hard conclusions. One has to be very vigilant and ensure that we get away from that, because we write reports that say unpalatable things. It is only natural for the civil servants involved to want us to cover those unpalatable things, if we have to mention them at all, in quite a lot of chocolate and fudge, and so on. Sometimes it can take a long time to go through that process. As I say, I do this to help the committee; there is no legal obligation to do it. So, if an accounting officer is, frankly, playing games—and I have known that to happen, but not in Wales—in order to delay things and spin things out, I can cut through that at any time and say, ‘Enough, I am going to report’, and I will report that there is disagreement, if necessary. So, that is clearance.

[22] If third parties are involved, clearance takes a slightly different form. If the third party, Cardiff University, for example, is quoted as a particular case, I will wish to be sure that it accepts that the facts are accurate. I do not quite apply the same standard of agreement on how the facts are presented, and so on; if they are accurate, that is fine.

[23] There is a third category, which relates to reports that might be regarded as being personally critical of named individuals. I regret to say that the technical term for the process

that I follow in such cases is called ‘Maxwellisation’, after the late Robert Maxwell. In the interests of natural justice, I am required to show those individuals what conclusions I am minded to draw and to listen to any representations that they may wish to make. I am not required to change anything as a result of those representations, but I have to give them an opportunity to comment. That was highly relevant last year in relation to the report on the ambulance inquiry. In any reasonable interpretation, the report was highly critical of the former top management of the trust, and we went through a process of Maxwellisation. That did not lead to any changes being made to the report, but we had to go through the process.

[24] I think that I have described the whole process by which an idea for a study gets into my portfolio of work and ends up in a report to this committee, which is followed by an evidence session and a report of the committee, which we then follow up.

[25] What else do we do in the WAO? We do a lot. I am directly responsible for auditing the accounts of the Welsh Assembly Government, the Assembly Government sponsored public bodies and NHS bodies, including local NHS bodies. I am responsible for appointing auditors to audit the accounts of local government bodies. The auditors, once appointed, even if they are my own staff, exercise their professional judgment independently of me.

1.50 p.m.

[26] However, in everything else, they might be my appointees or they might be firms. So that is the audit of accounts.

[27] I also have a variety of powers, because of the way in which the legislation is drawn up, which empower me or the appointed auditors, as the case may be, to undertake performance audit work. That can be local; that is, something that happens in a single local authority, or it can be across all local authorities, all NHS bodies, the whole public sector or bits of it. The powers, although they can be irksome in other ways, do not constrain the choice of the work that I can do. I can look across the public sector and cut it any way you like. I can also follow public money wherever it goes, including into the private sector. So, they are strong powers, stronger than those of any of the other audit bodies in Great Britain, which gives me a lot of choice in what I can do.

[28] There is a particular difficulty for this committee in that, if I am doing a piece of work in the local government sector, it is not constitutionally appropriate for the Assembly to hold a local authority to account, although it is perfectly appropriate for the Assembly to hold the Assembly Government to account for what it is doing in local government. I was talking to the Chair before you came in about a piece of work that will be published in a couple of months’ time and which began life as a study of home energy efficiency in local authorities. The work has been done, and it has led to a report in every local authority. However, we thought that we would put a national report together. When we did that, we found that all the recommendations are not recommendations for the local authorities, but for the Assembly Government. So that is a report that I shall be bringing to this committee—sometime in the autumn, probably.

[29] So, we have a variety of powers, including financial audit across the whole of the public sector, performance audit cut any way you like, and the whole reason for having a single audit institution in Wales is precisely to enable that work to be done straightforwardly. Another current project that is absolutely cross-cutting in every dimension is a study of delayed transfers of care in Cardiff and the Vale of Glamorgan, Gwent and Carmarthenshire. That will lead to a national report, again in the autumn. I think that that will provide a very interesting session for this committee.

[30] How is all this paid for? It is paid for by a variety of means. The audit of accounts

and the performance audit of individual bodies is paid for by fees that I levy on those bodies. I carry out work under the Wales programme for improvement, which is partly paid for by fees and partly by a grant from the Assembly Government. If there is a gap—which there is—between the total fee income and the total expenses, I present an estimate to this committee and, under the new procedures, the committee can vary that estimate if it wishes, and it then presents it and it becomes part of the budget resolution. So, it is no longer anything to do with the Assembly Government. The committee will approve, I hope, my requests for a grant to cover the gap. It is not precisely true that that gap is the cost of doing the work for this committee, as it is wider than that. So, for example, if, as is quite likely, some of the other scrutiny committees that have been set up seek work from my office, then that would be paid for in that way.

[31] I have been talking rather a long time, I am sorry, but I hope that it has enabled you to see how your work fits in with everything we do and the points at which you can intervene to stimulate further activity.

[32] **David Melding:** Thank you very much, Jeremy. I will take any comments that Members want to make. However, I have had a pre-meeting with Jeremy, and it might be appropriate for us to meet informally in September to talk about some of the blue sky things in terms of work that we think could be considered. Also, we could perhaps look at the finer points of the working methods then, rather than now. I do not want to cut off discussion, but we have a full evidence session to undertake.

[33] **Eleanor Burnham:** Is the work of the committee—perhaps this could be a clarification for people watching, because many people are interested in what we are doing—driven partly by your consideration of issues and also by requests from here?

[34] **Mr Colman:** Yes. As I said, we are completely at the service of the committee. One advantage that this committee has over other committees is that you have access to us in a straightforward way. If there is any topic that you are interested in pursuing, you can ask me to do some work in that area. If I agree to do so—which I generally will, I dare say—that will provide the committee with rich evidence on which to base inquiries. There are limits to what I can properly do and there are limits to what this committee can properly do in relation to policy. The law says that I must not produce reports that question the merits of policy objectives, which is a fine phrase—nobody quite knows what it means, but we know in general terms what it means.

[35] **Janice Gregory:** I thank Jeremy for that resume of what you do as a team. That has been useful not only for the new Members, but, as I said to Jeremy before, for those of us who have sat on the Audit Committee, but some time ago. I am sure that we have all taken something from that. As Chair of a scrutiny committee, I am particularly interested in the fact that you are not just the property, as it were, of this particular committee but that you can work with the whole range of committees, especially the scrutiny committees. I would welcome an informal discussion on what work we can do as an Audit Committee, and I am already thinking about on what I can engage with you in terms of the Communities and Culture Committee, so thank you very much.

[36] **David Melding:** Are there any comments? No? Thank you for that clear exposition, Jeremy, which I am sure helps us all, even if we have had some previous experience of the committee, but there are also new members.

1.57 p.m.

Cynnig Trefniadol Procedural Motion

[37] **David Melding:** I propose that

the committee resolves to exclude the public from the remainder of the meeting in accordance with Standing Order No. 10.37(vi).

[38] I see that the committee is in agreement.

Derbyniwyd y cynnig.

Motion carried.

*Daeth rhan gyhoeddus y cyfarfod i ben am 1.58 p.m.
The public part of the meeting ended at 1.58 p.m.*

*Ailymgynullodd y pwylgor yn gyhoeddus am 2.20 p.m.
The committee reconvened in public at 2.20 p.m.*

Diogelu Arian Cyhoeddus ym Mhrosiectau LG, Casnewydd—Rhagor o Dystiolaeth Protecting Public Money in the LG Projects, Newport—Further Evidence

[39] **David Melding:** While the witnesses are entering and making themselves comfortable in preparation for the evidence session, I will make a few introductory remarks so that they are on record. We are discussing LG projects following an evidence session in March before the Audit Committee of the second Assembly on the auditor general's report 'Protecting Public Money in the LG Projects, Newport'. At that hearing, some further information was requested from officials, which we have now received via the auditor general. Also, some legal advice relating to the way that the Welsh Office secured the commission's approval for the aid package has been released to the *Western Mail*, which quoted from it extensively in an article on 11 June. So, as well as giving us the opportunity to examine any issues that we so choose from the session at the end of the second Assembly, this is also a good opportunity to take stock of this additional information and to consider how this committee might reflect it in our report. That is the context of this witness session.

[40] I welcome Gareth Hall and his colleagues. We are pleased to see you this afternoon. It would help us if you would introduce yourselves and place those introductions on record.

[41] **Mr Hall:** We are the same team that gave evidence to the previous committee. I am Gareth Hall, Director of the Department for the Economy and Transport in the Welsh Assembly Government.

[42] **Ms Linnard:** I am Sharon Linnard, Director of Operations and Invest Wales.

[43] **Mr Godfrey:** I am Jeff Godfrey, Director of Legal Services.

[44] **Mr Shuttleworth:** I am Ian Shuttleworth; I head up the Professional Services Monitoring Team in Invest Wales.

[45] **David Melding:** Thank you and welcome to this session of the Audit Committee. I suspect that you are familiar with the procedure. We have a set number of questions that we would like to put to you and we will work our way around the committee members in putting those questions to you. There may then be supplementaries on particular topics from other

Members; I will direct those as appropriate.

[46] **Jocelyn Davies:** You will remember, in our last session, that a great deal was made of the contents of the official's diary. I thank you for letting us have sight of that. The diary runs from somewhere around 18 to 25 June 1996. There are some three references in total to the Secretary of State in that period. Would you like to tell us about the involvement of the Secretary of State in the negotiation process, or perhaps your knowledge is limited to what is contained in the diary? Would you like to tell us what would happen now if there was a project on this scale? What role would Ministers play?

[47] **Mr Hall:** Following our last appearance before the committee, we went back and researched the files. The documentation that was forwarded to you is the only reference on the files that we hold where specific reference is made to the Secretary of State. So, over and above this diary, we have nothing in the paperwork regarding the Secretary of State for Wales.

[48] On your second question, about how this would be managed now, with regard to the whole process of handling large-scale inward investment, we would follow the recommendations set out in this report, which we fully support. This time last year, we were involved with a potential project for the subject site and we involved all of the parties within the Assembly Government. That is one of the benefits of the merger: it was no longer the Welsh Development Agency ploughing a furrow answering to its own governance and board; it was an approach taken right across the Welsh Assembly Government. One of the other things that we have done, working with Jeff's department, is to set up a state aid unit, which advises not just my department, but all the departments in the Assembly Government. The Minister and the First Minister on that occasion were advised of what we were doing from the outset and were kept abreast of developments.

[49] It is also pertinent to say that we had tentative negotiations with the European Commission with regard to state aid. We involved the company we were working with from the outset. So, that is a different scenario from that with LG, and it follows the auditor general's recommendations.

[50] **Jocelyn Davies:** So, today, the Minister's involvement would be fairly limited?

[51] **Mr Hall:** Ministers would understand what the project was about, as they would have met the parties, because of the sheer scale of the project and its financial implications—it would have an impact on budgets.

[52] **Jocelyn Davies:** Yes, but obviously, according to this documentation, the Secretary of State took final decisions. Would that still be the case today?

[53] **Mr Hall:** Yes, because it would be above my delegations.

[54] **Jocelyn Davies:** Thank you. I am happy with that.

[55] **Lesley Griffiths:** It is apparent from the diary that negotiations were extremely difficult and, in order to secure such projects for Wales, compromises had to be made. The diary shows that the final deal was secured on the basis of the second phase for the electronics project, which would reduce the total cost per job to under £40,000. However, it did not have board approval and LG Electronics required a side letter allowing both companies to look at it again at the second phase after 2000. Does this not indicate that the company's commitment was lukewarm, at best, and that there was a huge risk that it would not materialise?

[56] **Mr Hall:** There was re-reading of the diary. I would echo the statement that you

made that it was a very difficult set of negotiations. It was not just that Wales was negotiating with LG; there were other interested parties as well, which were feeding information and other offers in. The negotiations changed over the period that you mentioned. There was, for LGE, always the intention for phase 1 to set up the electronics part; as for phase 2, you have described how the negotiations turned out.

[57] To give you a bit of background to the negotiations—it is documented in the diary—I think that it was a Mr Kim who initially carried out the negotiations, and he spelt out that he did not have board approval. The following day, his boss, a Mr Bay, came along and I think that it says—I am not quoting verbatim—that the negotiations were slightly more relaxed. I have been involved in negotiations with far-eastern companies, although I was not involved with LG, and the nature of the way in which business is done is hierarchical; there is a chain of command when you deal with far-eastern companies. That is why they were uneasy and is why they said that they had to get board approval. However, the ultimate deal was sanctioned by the president of LG who knew the bones and the detail of the deal before they went public on the announcement. So, it was ultimately endorsed from the very top of the LG organisation.

[58] **Lesley Griffiths:** It is apparent from the auditor general's letter that the Welsh Office agreed to limit the recovery provisions for the regional selective assistance grant to phase 1 only, and there is no record of any risk assessment or legal advice. Surely it was clear at that point that LGE was determined to avoid any commitment to phase 2. If phase 2 had failed to proceed, would the project have exceeded state aid levels?

[59] **Mr Hall:** When the negotiations were going on, there was a commitment to have an expansion of the LGE activities at Newport. I think that there was a reluctance on the part of the company to specify this, because the nature of electronic consumer goods is that you cannot project into the future what sort of products—particularly in the consumer electronics field—you are going to be producing x or y years hence. However, you can see from the diary that the company was very keen to start on the site. We were negotiating with the company when it came to assembling the site, to get the footprint of the site, on both projects, including phase 2. So, the land acquisition and the infrastructure were designed for a full second phase. If the company had no intention to go ahead, I believe that it would have accommodated phase 1 on the land that was available to get the project off the ground, because increasing the size and bringing in the extra services did delay the start of the project.

2.30 p.m.

[60] So, I would think from that that there was intent to go ahead with the future package. We also should appreciate that the semiconductor plant was the first facility to be built outside of the far east and that this was seen as the bridgehead for LG to produce product for the expanding European market.

[61] **Mr Godfrey:** To pick up the last point of your question, while the RSA agreement restricted recovery in the event that phase 2 did not go ahead, the developments described in that agreement still included both phases, which brings you back to the belief of the officials at the time that there would be a phase 2. However, they were not sure what its form would be and made the concession in negotiations. On the state aid point, it is true that, if phase 2 did not proceed, that would have led—as it did—to an overpayment of state aid, which was ultimately protected by a state aid recovery clause in the RSA agreement.

[62] **David Melding:** I realise that all these negotiations were in real time, and you get the breathless sense of how that was in the official's diary, but you started by being told that the board was not committed to phase 2, and then it wanted to frontload everything into phase 1. Why did that not set more alarm bells off?

[63] **Mr Hall:** I was not there at the time or party to it; I know no more than the to-ing and fro-ing that is recorded in the diary. This was a moveable feast.

[64] **David Melding:** It would set alarm bells off now though, would it not?

[65] **Mr Hall:** Yes, it would now.

[66] **Irene James:** I will look at the press release of 10 July 1996, which announced LG's investment in Wales. The press release does not state that the offer was subject to due diligence and that the project was in two parts. Why did it not stress that? Does that not indicate that this project was going to go ahead in any case?

[67] **Mr Hall:** The press release was issued the day after the framework agreement was signed. The framework agreement had no legal status, and, as you said, it was subject to due diligence and European approval. If a press release of this nature was going to be issued now, it would not say that it was announcing the project, but that the principle of an agreement or deal was being announced.

[68] **Lorraine Barrett:** I am looking at the article that was leaked to the *Western Mail*. It includes a press statement from the Welsh Assembly Government in response to the *Western Mail*'s coverage of the Slaughter and May advice. The Government's response to the article said that you did not rely on Slaughter and May's advice to assess the legal position on state aid anyway. So, where did that advice come from and how did that advice differ from Slaughter and May's advice?

[69] **Mr Hall:** I can give you the background and Jeff Godfrey can give you a detailed response. The Slaughter and May advice was commissioned by the Welsh Development Agency alone. I understand this—because we have not been able to find any letter of instruction to Slaughter and May in the files—from the tenor of its response. It was giving advice as regards the state aid implications and it was asked to talk about the situation not just for the WDA but also for the Welsh Office/Welsh Assembly Government. However, it was given access only to documentation held in the offices of the WDA; it had no access to any of the files of the Welsh Office or Welsh Assembly Government, and there was no consultation with officials from the Welsh Assembly Government. That is why, when you read its advice, you see that there are conditions and caveats. That gives you the context; Jeff will now explain what was happening in the Welsh Assembly Government.

[70] **Mr Godfrey:** It may help if I briefly reprise what the legal department, at least, was doing in relation to LG. We started work on the issues arising from the state aid overpayments in 2001. In 2001, we obtained two separate pieces of advice from leading counsel on state aids issues, and analysed these with our own former Counsel General, in terms of our negotiating position, in the event that it became necessary to take formal steps to recover moneys from LG. Thus advice from a number of sources had been obtained prior to the letter from Slaughter and May being sought by the Welsh Development Agency. As Gareth has said, the advice from Slaughter and May was taken purely from the WDA files: the letter's opening paragraphs stress the point that the advice had been provided on the basis of the documents made available to them, and should not be seen as a definitive review of the facts or an analysis of those facts.

[71] It may also be worth mentioning that, given the way in which the advice had been procured, there was no opportunity for Slaughter and May to speak to any of the officials who were involved in the negotiations with the European Commission. That is why the response in terms of the press statement is as it is: we had already got a lot of legal advice from a leading practitioner on state aids law, we had already instructed separate leading counsel on some of

the commercial issues arising, and we had already formulated a view and a negotiating strategy to deal with the company. You must bear in mind that the Slaughter and May advice arrived a matter of days before we departed for Seoul for the first round of negotiations about recovery. From there on, we continued to use our leading counsel and our in-house team to pursue the recovery.

[72] **Mr Hall:** I would add, Chair, that the press report refers to a secret Slaughter and May letter. That letter was on file and formed part of the deliberations of the auditor general when he formulated his report.

[73] **Lorraine Barrett:** That is fine.

[74] **Darren Millar:** This question, again, relates to the press release, because the Slaughter and May letter seems to indicate that there were some anomalies. I appreciate that you indicated that it saw only part of the picture, because it reviewed only the WDA's files; however, it does refer to the assurance that was given to LG that, even if the EC rejected the aid package, it would go ahead regardless, and there would be direct support from the UK Government.

[75] **Mr Godfrey:** I think that that was a reference to one of the letters that they had seen. First, the statement itself referred to moneys being made available by lawful means. What he was actually talking about was the package that the European Commission was considering.

[76] Going back to our last session here, one problem when the package was communicated to the commission was that a property development grant had been regarded by the Welsh Office, and the UK Government of the time, as not involving state aid, because it was what is called a gap-funding scheme. So there was an argument about whether it was state aid or not. Given that, in this case, the level of assistance provided was quite high, even for property development grants—that is, it went outside the norm—what the letter was referring to was that if it was not possible to award a property development grant in the amount that formed part of the communication to the commission then, effectively, the moneys would be switched to regional selective assistance. It certainly was not intended as a means of providing money out of sight of the European Commission, because that would have been unlawful, and the letter itself said that lawful means would have to be taken. So, it was a case of moving between the different grant schemes rather than avoiding the commission's process.

[77] **Darren Millar:** So, it is almost like bending the rules rather than breaking them.

[78] **Mr Godfrey:** I do not think that it was bending the rules—

[79] **Darren Millar:** That is the impression that it gives.

[80] **Mr Godfrey:** While the UK Government maintained its view that gap-funding schemes were not state aid, in order to progress this scheme, it was agreed on a without-prejudice basis that the commission would regard the property development grant as state aid in giving its approval. So, it effectively took account of all of the funding streams. They were all regarded as state aid.

2.40 p.m.

[81] **Darren Millar:** One of the other issues that Slaughter and May raised was the fact that the European Commission seemed to be giving negative responses when it was asked for updates on how successful the aid package would be, and that that did not reconcile with what the Welsh authorities were telling LG at the time. Perhaps you can tell us what did not

reconcile and why. If the rules were not being broken, why was there a different story on one side as compared with the other?

[82] **Mr Godfrey:** I do not know; I can only read the correspondence as the auditor general has, in preparing his report. The initial negotiations proceeded on the basis that the package was a mixture of property development grant that was not regarded as a state aid and other forms of assistance that were regarded as notified state aid—in other words, it did not need specific approval in its own right. When the issue went to the European Commission, that picture changed in two respects: first, they raised the problem that it needed an ad hoc notification, namely approval of the scheme as a scheme in itself, and, secondly, that the semi-conductor plant and the electronics plant were being split. Officials then had to go into a fairly difficult negotiation with the European Commission. What comes out of the correspondence, perhaps for understandable reasons, is that they were trying to send back encouraging noises to the company to the effect that the problems were capable of being resolved, which, ultimately, they were.

[83] **Darren Millar:** So, it was a half-full, half-empty sort of situation.

[84] **Mr Godfrey:** It did not help—and that is a lesson that comes out of this report—that, at the time, the officials, as part of a general UK Government approach, maintained confidentiality in the communications between the Welsh Office, through UK representation, and the commission. So, they felt constrained by the fact that they could not release the correspondence that was taking place. Not even the final notification, as the report makes clear, was released to the company at the end of the process. So, that creates a difficulty in terms of handling and how you demonstrate that you are resolving any problems that have arisen without sharing information that you regard as being confidential. That would certainly not happen when dealing with such large schemes today.

[85] **Jocelyn Davies:** This is probably an obvious question, but why would anyone commission a lawyer's advice without giving all of the information to the lawyer? Who would do that? It is a 33-page report; I imagine that it is quite a considerable, hefty document. Even in lawyer's language—even if there is a bit of Latin in there—it is still quite a long report. So, who would commission legal advice without giving the lawyer all the information?

[86] **Mr Godfrey:** The report has many strands to it; it sought legal advice on the recovery provisions in the property development grant, namely those agreements that were the Welsh Development Agency's responsibilities. Slaughter and May gave clear advice on those aspects. In undertaking that report, it also went on to look at the recovery under the regional selective assistance agreement and at the general state aid recovery position, which is regarded as being a Welsh Assembly Government responsibility. We already had our own internal legal advice, going back to 2001, as well as leading counsel's advice on that. So, I cannot answer the question as to why they sought legal advice on the Welsh Assembly Government side, other than by saying that this took place immediately before the visit to Seoul to start the recovery negotiations. Obviously, WDA personnel were part of the team that went out to Seoul. I can think only that they wanted their own view of the wider position, but the fact that they did not have access—

[87] **Jocelyn Davies:** But that would not have been of any value, because the lawyer would not have had all the information. It is just an obvious point to me.

[88] **Mr Godfrey:** We did not regard it as being of value in terms of informing; it was valuable in terms of sequencing the various documents. In retrospect, it proved helpful in that respect, because it brought together a lot of the factual information in one place, in the sequence of agreements. However, it was not particularly helpful to us in sorting out our negotiating position, because we were looking at additional information and were talking to

officials who were involved in the original notification and formulating our negotiating strategy from there.

[89] **David Melding:** In reading the documentation, it seems that officials expected a pretty quick response from the EC, but that was not forthcoming, and that just added to the pressure that officials were under, given that LG was getting pretty heavy.

[90] **Mr Godfrey:** It depends on your perspective; five months is quite a quick approval time, but, because the company did not expect the European Commission to become involved, it was getting frustrated about the process. At the time the original agreement in principle was struck, the Welsh Office officials believed that it did not require a state aid notification and approval. Having got to the point where it needed that approval, a lot of work had to be done—which was not a long time in terms of communications with the commission. However, from the company's perspective, it clearly was an awfully long time. That is where a lot of the tension that you can see in the background correspondence comes from.

[91] **David Melding:** My question is next. Slaughter and May's assessment, as reported in the *Western Mail*, indicated serious weaknesses in the Assembly Government's position that could have been exposed in any legal action. Did subsequent legal advice taken by the Assembly Government substantiate the fact that a serious counter-claim could have been made against us?

[92] **Mr Godfrey:** I think that the auditor general has given a fair summary of the legal advice in the report. We were alive to the possibility of a counter-claim, and saw that as a difficulty in the negotiating position. I do not think that we were as pessimistic as the Slaughter and May report was, but we did not disregard the fact that there could be difficulties. Ultimately, we were optimistic that a counter-claim would not be successful, not so much on avoiding a claim being made, but on the recoverability of any damages. Most of the damages that might be sought on the basis of any misrepresentation—if that were the basis on which the claim were made—were fairly remote in terms of the loss of the overall investment. The Slaughter and May report also did not pick up on the fact that, at the time of the commission's approval, while it was not provided with a copy of the decision letter, it was referred to the commission press notices, and so on, which clearly showed the £520 million figure. So, even though there was a discrepancy between the figure appearing in the commission's communication and the regional selective assistance agreement, it should have been alive to the difference, and would have been under an obligation of due diligence to satisfy itself that it was all in order.

[93] **David Melding:** It is fair to say that officials were aware of the potential difficulties in the legal case, and that this affected their behaviour in the recovery process.

[94] **Mr Godfrey:** Absolutely. Going back to the auditor general's report, if you look at paragraphs 2.40 to 2.41, you see that they canvass the fact that we were considering the difficulties that would be associated with legal proceedings. In the final event, because our calculation of the state aid overpayment and the interest which was due on it did not quite go as far as the commission's calculations, which use compound interest rather than simple interest, the sign-off from the commission was given to us in the light of the difficulties that we would have encountered—from a purely commercial perspective—had we gone into court proceedings, and the prospect that there may well have been a counter-claim of some type. So, we did not discount it.

[95] **David Melding:** What I am getting at is not how inconvenient it would have been to have a long drawn-out case in a foreign court, but, in your judgment, was there a weakness in our legal position, which could have been exposed and could well have affected recovery action? Or was it just the inconvenience factor that was the deterrent?

[96] **Mr Godfrey:** We were very close to the commission's figure, and our view was that it would cost between £3 million and £5 million if we had to go through expensive domestic proceedings and then take proceedings in Seoul against the parent company to recover the balance, not all of which would have been recoverable. So, on a purely commercial basis, I think that the commission accepted that there were risks associated with formal legal proceedings to go for the balance, and that it was a prudent decision to agree at the point that we did.

2.50 p.m.

[97] **Eleanor Burnham:** To follow on, paragraphs 2.40 and 2.41 of the auditor general's report describe the weaknesses in the Government's legal position during the recovery negotiations, which has already been alluded to, and which was discussed in the previous evidence session. As I am sure that you are well aware, the auditor general reports that officials at the time thought that there was a significant risk of a counter-claim from LG. How did the weakness of the Assembly Government's legal position affect the level of grant recovery that you were willing to settle for in negotiations? With £60 million lost, it is usually politicians who get the rap, and I am just interested to know whether any legal heads rolled. I realise that these events happened some time ago, but can you describe how that weakness in legal competence has been addressed and improved so that this does not happen again?

[98] **Mr Godfrey:** As other parts of the auditor general's report make clear, in terms of the contractual recovery entitlement, the only effective recovery power we had was under the RSA agreement, so we were looking at £34.6 million, which was the total amount of RSA that had been paid. We got £34 million, so were very close to recovering what we were contractually able to recover.

[99] On the state aids calculations, the external company, ourselves and the commission each had a different total, because of the way in which we were calculating interest. On our view, we were collecting all of the overpaid state aid, but on the commission's view, in terms of compound interest, we were slightly short. So going into the negotiations we effectively recovered what we had a contractual entitlement to recover.

[100] **Eleanor Burnham:** The general public would blame us as politicians, and would think that we had been very negligent in the loss of £60 million—and it is my understanding that that is the figure that has been lost.

[101] **Mr Godfrey:** The auditor general's advice, which we certainly agree with, is that there ought to be state aid recovery, and more effective recovery powers operating across all of the agreements. In this particular case, while there are a number of agreements under which either money or assets were provided, the effective recovery provisions were confined in the circumstances to the RSA agreement. I think that nowadays, particularly given that the WDA functions are now discharged by the Welsh Assembly Government, we would ensure that our recovery powers were fit for purpose.

[102] **Eleanor Burnham:** So basically, the weakness of the legal position has been addressed and competence has been improved?

[103] **Mr Godfrey:** It is not for me to say, but certainly on state aid we are considerably stronger than would have been the case back in the Welsh Office in 1997. We have put quite a lot of investment into training on state aid issues, and my colleague behind me here, and another lawyer within the department, have both worked at the European Commission in Directorate-General Competition. We consider ourselves to be very strong on state aid issues, and we have looked at many of these agreements in the light of LG and for other reasons,

looking to strengthen the recovery powers that we impose. Clearly, there is always a negotiation, and negotiations always have an element of compromise, but I do not think that you would see agreements of this nature arising out of any comparable investment made today.

[104] **Mr Hall:** Just to add to that, we propose by the autumn of this year to bring together all of the capital grants—not just RSA and the property development grant, but the section 4 tourism grant, the SMART grant, and other grants—seven grants will be brought together into a single investment fund with a single set of criteria, due diligence and legal conditions, so in a situation such as that of LG, in future we would have a single set of terms and conditions and legal requirements.

[105] **David Melding:** Thank you. I apologise, Eleanor, for cutting across some of your ground.

[106] **Eleanor Burnham:** That is okay.

[107] **David Melding:** Darren, you have something on this issue?

[108] **Darren Millar:** In your answer you spoke about the differences in the amount recovered being down to different calculations of interest, effectively, between the commission, the Welsh Office and the company itself, or the Assembly and the Welsh Office. Has that been mopped up in future deals in terms of how to calculate the recovery, because that has obviously been a major issue in this particular case?

[109] **Mr Godfrey:** In 2003, the commission published a notice to the effect that, in all cases, it would recover compound interest. Prior to that time, the commission had made different decisions in different cases, sometimes using simple interest and sometimes using compound interest. So, we had an historical agreement whereby it was not clear what type of interest would be payable. LG took the view that there was no interest; we took the view that there was simple interest up to 2003. From 2003 onwards, the position is beyond doubt because the commission has stated very clearly that, in all cases, compound interest is applicable. So, it is not a problem that would arise today.

[110] **Mr Millar:** So, it was just simply the interest that made up the difference?

[111] **Mr Godfrey:** We spent a long time during the negotiations in 2003 working to reach an agreement on the amount of the overpayment. So, I think that there was agreement about what the amount was, but we had a disagreement about the interest that was applicable to it, when it should be calculated from and what the method of interest should be. The method is not an issue now, because the commission recognised that there was uncertainty about it and announced generally in 2003 that compound interest is recoverable in all cases of state aid recovery.

[112] **Mr Millar:** I take it that it was difficult to agree on the amount of overpayment as there were lengthy negotiations on it. Is it easy now, in all agreements, to determine exactly what is the overpayment that might need to be clawed back, or not? Is that a simple exercise?

[113] **Mr Godfrey:** Calculating the overpayment would mean looking at what the eligible levels were and tallying up the money paid out to the relevant projects. So, that may take some accounting work, but it should be possible. As I said, in terms of the interest that is attached to it, the commission's approach should be reflected in documentation and there should not be any doubt as to how the interest should be calculated on any overpayment that has arisen.

[114] **Mr Millar:** I am sorry to labour the point, but if it is a straightforward exercise to calculate the amount that has been overpaid, why were there lengthy negotiations to agree on it?

[115] **Mr Godfrey:** It is straightforward if you have all the information. State aid is a proportion of the total investment, and during the first meeting in Seoul it became apparent that the company was referring to expenditure that it had incurred in connection with the project, which was not being accounted for by the Assembly Government in its calculations. So, a fairly lengthy exercise went ahead over that summer in which the company was accounting for its investment in the site. If expenditure was eligible, that would then be factored into the state aid overpayment calculation. Obviously, the more investment the company made, the higher the eligible level of public assistance that could be retained.

[116] **Mr Franks:** I wish to refer to paragraphs 1.15 to 1.17, which relate to the difficulties in substantiating the figures provided to the European Commission. According to the report, it is not easy to substantiate these figures. There is a danger that a charge can be made that these figures were misleading so as to avoid breaching state aid rules. What assurance can you provide that this was not the case?

[117] **Mr Godfrey:** In terms of the dialogue with the European Commission, the commission identified the difference that existed between the £520 million and £400 million or so in the initial agreement—there was a £96 million gap. Meetings were held and there was correspondence with the commission.

3.00 p.m.

[118] The officials attending, supported by external consultants, satisfied the commission that this was eligible expenditure. When we came back to look at the figures, there are doubts about some of the items that are in there—although not for the whole £96 million. You can identify some of it as being legitimate, such as the value of the land and some infrastructure works that were done around the site, but there was a lack of clarity over whether the building cost for phase 2 of LG Electronics had been double counted. I am not sure that there is an answer to that question, at least not from the files and from the officials who were dealing with it. They thought that there were building costs over and above the plant and equipment costs that the company had provided, and that was presented to the commission, which the commission accepted in its sign-off of the notification.

[119] **Chris Franks:** I see. So, does it still accept the figures as reasonable?

[120] **Mr Godfrey:** What the commission was dealing with, when we came to the recovery process, was whether we had maintained the development within the terms of the state aid approval. Clearly, phase 2 had not happened, whereas phase 1 had, and it had a level of public assistance that went beyond the state aid limits. So, the commission was really looking at the use of our contractual powers to recover the amount of state aid overpayment. They were not looking back to what was a historical process by that stage of how the original notification had been presented. It is an issue that cropped up as part of the recovery process, for the reasons that we discussed earlier, as to whether there would have been the possibility of a counter-claim of some kind by the company, because, in justifying the expenditure to the commission, calculations were being made of building costs and professional fees and so on, which were being provided by a mixture of the WDA and consultants employed by the WDA. They were not being provided by the company itself.

[121] **Jocelyn Davies:** Were they never discussed with the company itself?

[122] **Mr Godfrey:** No. Again, that is different to how we would deal with these things

now. There is a marked difference in approach.

[123] **Mr Hall:** If we were doing this now, those figures would be agreed with the company, and they would be known, because we would be presenting to the commission.

[124] **Jocelyn Davies:** I seek clarification on one point, Mr Godfrey. I have read over the transcript, as you would imagine that I would, of what you said last time. We talked then of the fact that those figures had not been discussed with the company. You said then that the company would have been aware, once the EU published its notice of approval. You mentioned earlier in this session that the company would have been referred to that approval. How does that happen?

[125] **Mr Godfrey:** The company would have been aware of the total figure, so it could have seen the difference—£520 million compared with £425 million. That happened because the solicitors acting on behalf of the company were referred to the commission's press notice. Effectively, when the commission—

[126] **Jocelyn Davies:** Who does the referring? That is what I wondered. What are the mechanics?

[127] **Mr Godfrey:** When the commission issues a notification, it publishes a notice to that effect in the official journal. So, there is a public notice of the amount, and as part of the correspondence in denying the company access to the decision letter, the solicitors were referred to the notice being published by the commission. The company would have therefore seen the headline amount, but would not have seen, and did not subsequently interrogate, how that difference was made up.

[128] **Jocelyn Davies:** And that would have been provided to the company by the WDA, would it?

[129] **Mr Godfrey:** It was referred by the Welsh Office to where that press notice could be found.

[130] **Janice Gregory:** Reading the report, you can see what a massive part state aid plays in all this, and I do not think that we should underestimate that. Listening to the answers that you have given puts more meat on the bones of this matter with regard to the difficulties, where the Welsh Office assumed one thing while the European Commission had a different view as to what actually constituted state aid. There are obviously differences of opinion with regard to training grants and so on, and I would like to know whether you are absolutely sure that you have complete clarity in terms of state aid rules. Can you go forward now with more certainty than before? I know that you touched on that in a reply to my colleague. Is everything now clear?

[131] **Mr Hall:** I mentioned that we have a dedicated state aid unit. Lawyers in Jeff's department have particular expertise on this. With the mergers, there will no longer be the anomaly of the right hand and the left hand not being exactly synchronised. I do not think that anyone could give an absolute assurance, because it is the nature of the European Commission that a precedent comes from cases that it is dealing with on an ongoing basis. However, as an organisation, we are far better informed now than we were back in the late 1990s. Also, we are not bound by this confidentiality issue of the UK Government and, of course, we will be doing it hand in glove with the company that we are working with and not separately.

[132] **Mr Godfrey:** Compared with then, the state aid rules themselves are a lot clearer now, because the commission has published a lot more information about that. While there

are undoubtedly areas of dispute in state aids law, I am confident that we have the skills to identify where a state aids issue is arising and to deal with it competently.

[133] **Janice Gregory:** Would that be identified very early on—right from the outset? Does state aid now form part of the equation, in being at the front end? Would you clarify issues immediately?

[134] **Mr Godfrey:** We have expert state aid lawyers in the legal department. There is also a state aid unit that deals with matters across the policy divisions. So, provided that a proposal is brought to their attention, I am very confident that state aid issues would be identified.

[135] **Mr Hall:** I referred to a project that we dealt with last year. In our first detailed meeting with the company, state aid was an agenda item and it was discussed from the word go.

[136] **Janice Gregory:** I do not know whether this is completely related, but it is state aid related. Will the state aid unit that Gareth said that he is setting up—and I welcome that; having seen the problems that this threw up, I think that it is vital—work across the piece in terms of local authorities? I know that they throw up a state aid rule every now and again on certain issues. Would that unit be of assistance? What I am trying to get at is whether it is just for economic development and the bringing in of inward investment or whether it goes across the piece.

[137] **Mr Hall:** This unit gives advice across the Welsh Assembly Government. Remember that, with any advice, you are ultimately accountable to the sub-accounting officer and the accounting officer. I take Jeff's advice on this. If you were going to give advice to another organisation, who would be bound by that information? You could inform but I do not know whether you could give categorical advice to a local authority because, ultimately, there would be an accounting officer in the local authority who would have to be satisfied that that advice was—

[138] **Mr Godfrey:** The primary purpose of the state aid unit is to advise the Assembly Government. There have been discussions around the extent to which it might give advice to the wider public sector. The lawyers in my department have provided seminars through the Law Society, to which local government lawyers, in particular, have been invited and we have managed to arrange for commission officials to come over to give presentations. So, it is very much an advisory role in relation to the wider public sector, because, ultimately, those bodies must satisfy themselves that they are acting within state aid law. However, we are conscious of the need to raise awareness more broadly.

[139] **Mr Hall:** And to share information.

[140] **David Melding:** With this project, once phase 2 was in jeopardy, clearly the state aid rule was going to be broken massively—and it was not close; it was way over the permitted amount of state aid, was it not? Presumably, when you are attracting investment, the amount of frontloading that you can deliver is important in negotiations. How are the risks involved in complicated projects that require quite a lot of frontloading managed now?

3.10 p.m.

[141] **Mr Hall:** The recommendations in this report from the auditor general are now being followed in all cases, to identify the life span of the project. Tests are done frequently. You can see in the graph in the report that—it goes above and then below the line—all the time that you are moving along the graph, you want to see how far you are above the line to ensure that it is compensated as you go forward. We have also acted on the recommendations of

other reports from the auditor general about ensuring that sensitivity analysis is factored into this when you are taking all of these issues into account.

[142] **David Melding:** My final question relates to the current culture. You need a certain speed in these negotiations, and there are many people competing for investments. However, it seems that there is a balance between not getting pushed by companies obviously saying that they are being bombarded—or whatever LG was saying—at any one stage and moving you to make decisions quicker than can be done with due diligence. Are you confident that the system is now more robust?

[143] **Mr Hall:** Yes. We have those checks and balances to ensure that it is never the case that you get that project at all costs. If you look back at the diary, there was a videoconference link with the then Secretary of State which says, ‘This is the limit that we are prescribing and do not go above it, even if it means losing the project’. That is very much part of the value-for-money criteria that the teams are constantly checking in their negotiations.

[144] **David Melding:** We are nearly at the end of the session, but Eleanor has indicated that she would like to ask a question.

[145] **Eleanor Burnham:** Bearing in mind that, politically, one would obviously want to get the best value for money and follow best practice—and you, as a department, are very far from these early days of losses—how would you balance that against not being seen as risk-averse? I am talking about the balance between getting the best value as opposed to being fleet of foot in commercial terms and being fairly responsive to the need to get a good deal and so on.

[146] **Mr Hall:** One of the checks and balances that we have in place is the independent Welsh industrial development advisory board. Any capital projects over a certain sum go to the board for consideration and the board then makes its recommendations to the Minister. That is one of the important checks and balances for projects over a threshold of £500,000, which is an important part of this process.

[147] **Eleanor Burnham:** That gives you a degree of confidence that you will not repeat some of the mistakes that were made in the past. It also gives you the flexibility of being ready to do good deals.

[148] **Mr Hall:** Yes, and to do it responsibly.

[149] **Mr Godfrey:** If you take the example of last year, which has been alluded to, the company coming in was aware of the state aid rules and the involvement of the European Commission. More than anything, it looks to you to give confidence that you can deal with it. I do not think that it is a case of being risk-averse, because, ultimately, if there is a state aid overpayment, the company has to repay the money with compound interest. So, companies tend to look for your competence to deal with state aid issues even to the point of dialogue with the commission rather than being put off by factors of that nature.

David Melding: Thank you. Your evidence has helped with the deliberations that we will now make. A transcript of this session will be sent to you for comment and, if necessary, amendment.

3.14 p.m.

**Cynnig Trefniadol
Procedural Motion**

[150] **David Melding:** Before we move to item 6, I propose that

the committee resolves to exclude the public from the remainder of the meeting in accordance with Standing Order No. 10.37(vi).

[151] I see no objections. Therefore, please clear the public gallery and could the technicians please ensure that the broadcasting system is switched off? Thank you.

*Derbyniwyd y cynnig.
Motion carried.*

*Daeth rhan gyhoeddus y cyfarfod i ben am 3.14 p.m.
The public part of the meeting ended at 3.14 p.m.*