

Audit Committee

Thursday, 11th December, 2014
6.00 - 7.50 pm

Attendees	
Councillors:	Colin Hay (Chair), Chris Nelson (Vice-Chair), Matt Babbage, Flo Clucas, Dan Murch, David Prince and Pat Thornton
Also in attendance:	Councillor Rowena Hay, Rob Milford (Head of Audit Cotswolds), Andrew North (Chief Executive), Bryan Parsons (Governance, Risk and Compliance Officer), Councillor John Rawson, Mark Sheldon (Director Resources) and Councillor Jon Walklett

Minutes

1. APOLOGIES

No apologies had been received.

2. DECLARATIONS OF INTEREST

No interests were declared.

3. MINUTES OF THE LAST MEETING

The minutes of the last meeting had been circulated with the agenda.

Upon a vote it was unanimously

RESOLVED that the minutes of the meeting held on the 24 September 2014 be agreed and signed as an accurate record.

4. PUBLIC QUESTIONS

2 public questions were received.

Questions from Anne Brookes to the chair of the Audit Committee, Councillor Colin Hay	
1.	It is the responsibility of the Borough Council, officers and elected members, to ensure that public money is safeguarded and properly accounted for, and the report to this committee regarding the overspend shows a complete failure of control throughout the project, and that even when completed, the actual details of the overspend remain unknown. If managed properly it would have been possible, at any time, to know why, where and how much the overspend was likely to be. The committee, if properly undertaking its duty and responsibility, should question why it is being asked to spend more public money on further audits to identify what was spent. A public interest report following the legal case against the former Chief Executive made recommendations concerning managing risk, yet these have been ignored. We are again in the situation where evaluations are only made after the event, and it seems likely that the overspend on the Art Gallery will be close to or

	<p>possible top £½ million of public money.</p> <p>What will the committee do to ensure that there is a proper process in place to minimise, at the very least, the risk to the council and public funds, and stop just accepting these hindsight reports promising to identify ways to prevent this happening in the future?</p>
	<p>Response from Councillor Colin Hay, Chairman Audit committee</p>
	<p>The statement made by Ms Brooks relating to responsibility is correct and the Council has always recognised this by putting in place a series of financial rules and internal controls. In addition to this the council provided a project team, led by a qualified and experienced Project Manager who was supported by an external Construction Project Manager. The Project team was governed by the Council's financial rules, controls and its Prince 2 based approach to project management, all of which are designed to ensure that public money is safeguarded and properly accounted for.</p> <p>The Executive Sponsor for the project reported to Council in February 2014 that the outturn cost of the extension to the Art Gallery and Museum had exceeded the budget by £360,000. As a result of this the Council agreed to commission Grant Thornton to carry out a review and to report back to Audit Committee on its findings.</p> <p>Grant Thornton's report was considered by the Executive Board and was tabled for consideration at the Audit Committee meeting on the 11th Dec 2014. However since then additional expenditure has been identified and the report has been put on hold until after a discussion by the Audit Committee this evening and to account for any additional work by our internal and external auditors.</p> <p>The Grant Thornton draft report contained specific recommendations and the management response has been that they will all be accepted and acted upon.</p> <p>When the work of the auditors is complete the Audit Committee will then be asked to consider how best to improve all of its policies procedures and working practices and to make recommendations to prevent this happening again.</p> <p>In a supplementary question, Anne Brookes asked how the Audit Committee would ensure that any measures were followed.</p> <p>The Chairman explained that Grant Thornton had been commissioned to look at this issue. When Audit Committee considered the recommendations and management response, they would no doubt be asking questions regarding whether financial regulations and procedures had been adhered to and if not, why not. The Audit Committee would then consider any lessons learnt and monitor implementation of any recommendations.</p>

<p>2.</p>	<p>In a project such as this, financial control throughout is inextricably linked to the practical project management function. It is not unusual for projects of this scale to go over schedule and over budget, but when public money is involved tight control is a duty and the committee should question the 'glib' statements made in the report about 'shared burden' and the overall success of the finished Art Gallery.</p> <p>When visiting the Art Gallery, the clean 'modern' finish is entirely spoiled by a very obvious 'error' in project management, where patches are evident in the large flank wall in two places when accessing the upper galleries. It would appear that after the wall was 'finished' it was necessary to knock into this wall for (I assume) some incomplete services. (I have attached photographs of these for the Committee) There are also issues that could be raised about the finish on the floor in the entrance atrium, and the holes left in the wall after what appears to be more than one attempt to install the hand rail going up the stairs. This makes a mockery of the back-slapping 'awards' list for this building, and in view of the high cost this should not have been accepted. This is a risk to the reputation of the town.</p> <p>Who was responsible for 'signing off' completion of this building, and why were the contractors not made to rectify this before the new building was opened and what measures are in place to make the contractors responsible, at their cost, for any ongoing problems that may occur, and over what period?</p>
	<p>Response from Councillor Colin Hay, Chairman Audit committee</p>
	<p>The 'signing-off' on the completion of certain areas of the building was undertaken by the Senior User both before and after the re-opening, this was after discussions and approval by the Architects and Design Team.</p> <p>There are a few defect issues still outstanding that need to be rectified and agreed with the architect and the contractor, the markings on the wall are one of these.</p> <p>It was not possible to rectify this issue prior to the opening of the AG&M, discussions over the identification of a possible solution are continuing.</p> <p>In a supplementary question Anne Brookes asked, what assurances could be given that the holes in the walls would be resolved, if not completely redone, how long this would take and who would pay for it.</p> <p>The Chairman asked that the Governance, Risk and Compliance Officer answer this supplementary question. He advised that as with all projects of this nature, there came a time when the final payment needed to be agreed. This often allowed 12 months, as a guide only, to rectify defects, a period known as the snagging period. The Council's property department had a list of snagging issues and discussions were ongoing with the contractor, whom would bear the cost. It could be that the solution was to undertake extensive work or indeed to do nothing. The Wilson was open to the public 7 days a week and disruption was a factor</p>

	for consideration. The marks that had been highlighted were only aesthetic and not structural.
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5. UPDATE ON AUDIT WORK IN RELATION TO THE WILSON ART GALLERY AND MUSEUM EXTENSION PROJECT

The Chairman explained that the discovery of the additional overspend at this late stage and the fact that, whilst Grant Thornton's (GT) report tracked the chronological order of various correspondence, it did not identify any key reasons for the failure, which he would expect from a report, both necessitated the need for further investigation. He was disappointed that the report was not available, as he was sure that other members would be, but he had felt that it was important that the committee met to understand the current situation and the reasons for it.

The Chief Executive introduced the report as circulated with the agenda and apologised that this was not the report that he had expected he would be presenting, the report for which the meeting had been convened. He explained that a report had been commissioned from forensic auditors at GT, to review the extension project at the Wilson Art Gallery and Museum (AG&M) after the project exceeded the previously agreed budgetary provision by £360,000 and was completed 12 months later than originally planned. This audit process took much longer than anticipated, however, on Friday 28 November 2014, just as the report was being finalised, it became apparent that the true extent of the overspend exceeded that which had been agreed in February 2014. Neither, the Chief Executive or any other senior officers had been aware of this additional overspend prior to this point. It had been identified at this time, as there was the matter of the contractor being paid the retention, but this was not what the overspend related to. The overspend had been incurred as a result of a number of extras which had been commissioned by the AG&M, but not logged on the council's financial system. Whilst the report to Council on 14 February 2014 had been prepared in good faith, this was incorrect and at this stage, Finance had a high degree of confidence that the additional overspend was of the order of £90,000.

He provided members with a brief history to the issue. Key individuals on the project had included, the Senior User, a senior officer at the Wilson, responsible for certain contractual matters, the Project Sponsor, the Director of Service, and the Executive Sponsor, an Executive Director who had since retired. The cost for the project was originally estimated to be £6.3million; a figure which Council agreed to underwrite, the authorised sum. At the end of the tendering process, ISG, who had submitted a tender for considerably less than the expected cost, were awarded the contract and the contract budget was revised to £5.6million. This was good news but from the outset this was considered to be a difficult build and the authorised sum was not reduced at this stage. At an early stage the projects structural engineer went into liquidation and upon appointment of a new structural engineer, a lot of work had to be repeated. A mistake during the pouring of concrete resulted in this having to be redone and there were a number of issues relating to the neighbouring building which had not been anticipated, and all caused delays and additional costs. Some of these were contractor risks and some were client risks. During the course of the contract, there were around 1000 change requests and it was because of this, in part, that the Council was in a less than favourable position in terms of finalising the

contract liability. There were discussions regarding claims, but advice was to settle and ultimately a settlement with ISG which (when other consultants' and contractors' fees are added) totalled £6.7million was reached in February 2014; £360,000 more than Council had authorised at that point and £1.1million more than the reduced budget. A report was prepared in good faith, for Council on the 14 February 2014, which sought approval for no more than £360,000 overspend.

It had been an extreme disappointment then to discover the additional overspend recently identified, so long after this time. He described how this overspend had occurred without the knowledge of the Senior Leadership Team or Cabinet. Essentially, the Council's purchase order system should be updated whenever anything is commissioned. The system allows for real time information on what had been spent and what expenditure had been committed to. Had this been used, there would have been no confusion about spend on this project; but the fact was, this system had not been used and therefore commitments were being made which exceeded the budget and which Finance had no knowledge of. It was noted that this issue was not confined to the Wilson, but that there were indeed other parts of the Council which were not using this system properly. He did not underestimate how disappointed members were to not yet have received the GT report but he reassured the committee that there was good reason for this; the report was out of date and therefore misleading, and the recommendations incomplete. The report acknowledged that there was a fairly thorough contract management process in place, with the build being directly project managed by the architect, Davis Langdon, which was normal practice and there was no suggestion that this had not been done properly. As well as the Senior User, Project Sponsor and Executive Sponsor, there was also a project team and project manager at CBC and thorough risk management had been built-in, with regular meetings of the project team. It seems from the evidence gathered by GT, that accurate and timely information was being presented to the Senior User, but that this was not being consistently passed on to the Project Team and/or the Operational Programme Board (part of SLT) or Cabinet. The blockage was localised to the Wilson itself, which was well documented in the GT report, but the report did not make it clear as to the reason(s) for these blockages and this had been an area for much discussion between the Council and GT, which had in turn caused delays. Before the decision to defer the report was taken it was envisaged that this would be supplemented with a brief by Internal Audit which would detail areas for further report. The overspend had been appropriately incurred and he suggested that the by the very nature of the build, a level of overspend would have occurred even if SLT and Cabinet had been aware, but the extent of it might have been managed and minimised. This may well have impacted the quality of the final product but because this information was not shared, there was no opportunity to assess this.

The committee would ultimately see the report, which outlined detailed evidence of who was told what and when. GT were of the opinion that they had completed their work, as the new information had come to light after they had concluded their investigation and drafted their report, but he hoped that they would be open to a partnership effort in looking at the new information, as the original report had not quite met expectations.

In closing, he urged members not to lose sight of the fact that this project had resulted in a fantastic, award winning building which attracted visitor numbers far in excess of what had been projected. He felt that it would be unfortunate for the success of the new building to be tarnished by this issue.

The Chairman invited questions on what the Chief Executive had said, as the GT was not available for consideration and reminded members that any matters relating to an individual would be dealt with by the Chief Executive, as Head of Paid Service and were not a concern for this committee.

The Chief Executive provided the following responses to member questions, with some assistance where necessary, from the Director Resources, Head of Audit Cotswolds and Governance, Risk and Compliance Officer;

- Though not closely involved in the tender process at the time, there was surprise at how keen the tender was from ISG. There was a concern from the outset that it would be a difficult build and in hindsight, the £600,000 contingency, which was quickly exceeded, was not enough.
- There were discussions with claims assessors and OneLegal regarding a possible claim against ISG when the extent of the initial overspend was uncovered. The advice was that because the contract was a standard form of building contract, any claim would more than likely result in a counter claim against the Council, on the grounds of the number of change orders that were issued and this would be considerably more than any penalty and arbitration. Legal advice was that the Council should come to terms with ISG, which the council did and settled on £6.7million total cost (including the cost of all other consultants and contractors. He was not aware of a bond with the original structural engineer company.
- Most of the 1000 (approximate) change orders were relatively small and not significant in themselves, but this gave the contractor a lot of leverage in achieving the settlement that it did. The question of whether these change orders had been properly authorised had been asked of GT and they had found that they were in accordance with the rules at the time.
- An opinion shared by GT was that it was not the system which had failed but rather that those operating within the system had not been doing as they should, not passing information on and not gathering all of the information required. This would be a matter for the committee once it had considered the report.
- Whilst Internal Audit and GT continued their review, the individuals that had fulfilled the role of Senior User and Project Sponsor (the Executive Sponsor had since retired) on the Wilson project, would not be involved in any similar roles for Cheltenham Borough Council, until all the facts had been established. There was a general question regarding how the Council managed performance and this was already a subject being considered as part of a review of the appraisal system.
- It appeared that there was a perception that the Council had to deal with project overspend/communication issues such as this on a regular basis and whilst perception was important, fact was more important, as this simply was not the case.

- The bid from ISG was believed to be the lowest but would have been assessed against price and quality. The Council relied heavily on expert external advice and made a reasonable decision based upon that advice. ISG was a national contractor and it would be odd for the Council not to accept a bid simply because it was low. It was important that members understand that this thread was not covered by the GT report.
- The structural engineer who went into liquidation shortly after work started would have been assessed as being a going concern as part of the contract process. At the time the economy was suffering its hardest period of many years.
- The person responsible for the delivery of the design and for administering the building contract, as with any project of this sort, was the architect. They are the experts and the change orders came through them. Council Officers may have had the expectation that the architects were responsible for more than they actually were. The Senior User at the Wilson was responsible for the budget and signing off any change requests for the Client. It seems that the Sponsor was not always aware of, or being made aware of, the level of detail that related to these changes, that they should have been.
- Upcoming projects for which lessons needed to be learned included hard landscaping to the town centre, accommodation and procurement at the crematorium. Any further projects would be decided as part of the budget and capital expenditure.
- The disquiet being expressed by members was also felt by officers and the Cabinet and members could be assured that neither were being complacent and a full explanation as to why these problems with the project had occurred was being sought by the Audit Cotswolds team.
- A brief would be produced which would set out what the Internal audit report will cover and members were invited to email specific questions to the Head of Audit Cotswolds for inclusion. A structure chart for this project would be produced as requested.
- The question of whether any claims can be made by the Council has been raised and whilst there have been discussions, there had not yet been a clear answer. It was not believed that the original structural engineer, who went into liquidation, had paid a bond, but the Council could make a claim to insurers if negligence could be proven. Members could be assured that all options were being considered.
- The additional overspend was not identified until this late stage as it was only as the matter of retention was being settled, a year after completion, that it was discovered that there was insufficient money to pay the retention. It is understood that this arose because the Senior User continued to commission contract without using the purchase order management system and without advising Finance of these commitments.
- The Project Initiation Document would have set out who was the budget holder, in this case the Senior User/Project Sponsor.
- The purchase order system, Agresso, was purchased two years ago and enabled budget holders to monitor expenditure as well as commitments, providing real time information. This new system had not previously been used and as such there was no insistence that teams/areas use it right away, however, anyone committing the Council to expenditure

must ensure that there is sufficient budget and that the finance team are made aware of outstanding commitments. There had been a gradual increase but this issue had identified that it now needed to be rolled out across the Council, but members were warned that this would take time and there was no instantaneous solution.

- A number of budgets made up the project and went into a specific area for a specific project. This was a complex project with a complex coding structure. Any expenditure/commitments against the project should have been coded against the project.
- £20,000 had been wrongly coded and this had needed to be amended by an Officer from Finance. An Officer had since looked again at all expenditure to identify and correct any errors. At this stage, no payments had been made over and above the agreed budget (i.e. towards the additional overspend of approximately £90,000).

In response to a statement made by a member, the Chief Executive gave assurances that he had answered all questions as fully and openly as he was able and did not dispute the seriousness of the current situation. He, along with his SLT colleagues and the Cabinet, wanted to establish exactly what had happened and why, so that lessons could be learnt and this issue avoided in the future. The purchase order issue was being addressed, with roll out to any areas or teams that were not using the system and training being provided.

With no further questions from members of the committee, the Chairman took the opportunity to make some observations. He reminded everyone that the contract was awarded during a recession and at a time when all tenders were more competitive than in the past, as there was less work available. In his professional opinion, as a builder himself, he explained some of the difficulties posed by old buildings when providing quotations; surveys often did not involve lifting floorboards, etc and unforeseen issues were often not identified until work had commenced. Getting a set price often meant getting an inflated price to cover the contractor against any unanticipated and additional works. He accepted that this in no way related to the issue of reporting, which was key in making decisions about how to proceed and to allow for budget management. It was important for the Council to learn lessons but without having seen the report from GT, members were speculating on what happened and why. He assured members that the report would be made available to them as soon as was practicably possible and it would address all of their questions as to why something adverse had or had not happened.

Officers anticipated being able to present the report to the next scheduled meeting of the committee (14 January), however, members felt that the agenda for this meeting was already fairly substantial and that consideration of this report would require a dedicated meeting. An extraordinary meeting would be arranged for a date after the scheduled meeting, but the Chairman was reluctant to set any timescales at this stage.

The Chair proposed that the committee consider the recommendations in light of the discussions that had been

Upon a vote it was unanimously

RESOLVED that;

1. **Additional audit work be carried out to investigate new information on the extent of the project overspend and to explore any failures which led to its late reporting be carried out.**
 2. **The decision as to what further work should be undertaken by Grant Thornton and/or by Audit Cotswolds be delegated to the Director Resources who will enter into contracts accordingly.**
6. **ANY OTHER ITEM THE CHAIRMAN DETERMINES TO BE URGENT AND REQUIRES A DECISION**
There were no urgent items for discussion.
7. **DATE OF NEXT MEETING**
The next meeting was scheduled for 14 January 2015. It was likely that another extraordinary meeting would be arranged in the weeks after this meeting. Democratic Services would contact members in due course.

Colin Hay
Chairman

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