

# APPENDIX 1

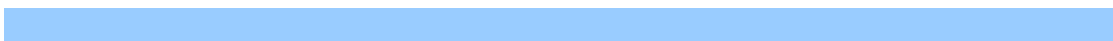


## SOUTHAMPTON CITY COUNCIL

### INTERNAL AUDIT INVESTIGATION REPORT 2005/06

### OVERSPEND ON THE WATERLOO ROAD HOSTEL IMPROVEMENT PROGRAMME

### EXECUTIVE SUMMARY



## 1 EXECUTIVE SUMMARY

### Scope of the investigation

- 1.1 The scope of the exercise was to investigate the reasons for the project overspending and to conclude on whether the Council's Financial Regulations and other processes have been properly followed.

### Background to the overspend

- 1.2 For a number of years the Council has included a budget for Hostel Improvements in the Capital Programme, with the anticipated annual spend being set at £50,000. This figure was set some years ago by the former Operations Manager's team within Housing Services. For 2004/05, Housing Management decided to advance the anticipated budget for 2005/06, and use the combined budget for the improvement of the hostel at 76 Waterloo Road, with a view to converting the premises from bed-sit accommodation to self-contained accommodation.
- 1.3 The core budget for the programme, £100,000, was augmented by £69,000 from the Decent Homes budget for 2004/05, and £15,000 from the 2004/05 Asbestos Works budget. Total budget provision for Waterloo Road was therefore £184,000, with the total contract sum being slightly lower at £164,800.
- 1.4 The "contract" for the Waterloo Road hostel improvement work was let to the Council's in-house Building Contract Services ("BCS") team within the Housing Services Division. The decision to let the contract was made by officers within Building Design Services ("BDS") on the basis that previous contract for hostel improvement work at Howards Road had been successfully delivered by BCS.
- 1.5 At the time of our investigation, the final cost of the programme had not been fully agreed, but is anticipated to be in the region of £356,400. This represents an overspend of around £172,400 or 94% against budget, or £191,600 (117%) against contract sum.

## Causes of the overspend

- 1.6 A number of primary contributing factors were identified during the investigations into the causes of the overspend. These included:-
- The failure to properly plan the project, in terms of design, intrusive survey, financial modelling, resources and prioritisation;
  - The adoption of CCT operational practices in relation to client/contractor split, where such a split was neither required nor appropriate;
  - The failure to properly apply procurement processes resulting in ineffective commissioning;
  - Reliance on multiple systems for the provision of financial information, none of which detailed full and robust financial performance details;
  - Lack of cost consciousness throughout, evidenced by the practice of manipulating financial information with the effect of masking cost overruns;
  - Poor project management and control; and
  - A general lack of active management

## Responsibilities for the overspend

- 1.7 A number of Divisions within the Council contributed to the Waterloo Road project. The Divisions are referred to in the context of their roles at the time of the Waterloo Road project, and have not been updated to reflect the recently implemented restructuring.
- 1.8 Under the previous CCT regime, a client/contractor split was a requisite part of these types of project. This project was ultimately delivered on a client/contractor basis so any reference to clients and/or contractors should be viewed in this loose context.
- 1.9 Contributing divisions performed the following roles:-
- Housing Services represented the client service;
  - BDS undertook design and surveying work and acted as the conduit between the client and contractor functions;
  - BCS undertook the role of contractor in delivering the work on site;
  - Finance Services were responsible for professional support and the provision of robust and timeous financial information to facilitate project monitoring and reporting to Members; and
  - Human Resources acted in a supporting role for recruitment, staffing and “acting up” decisions.

- 1.10 Responsibility for the overspend on the Waterloo Road hostel improvement programme does not lie with any single Division of officer of the Council. Instead, it resulted from a variety of operational, managerial, structural and cultural shortcomings which require to be actively addressed by management to reduce the risk of similar problems arising on future projects.
- 1.11 The table overleaf provides a summary of the failures showing the areas of weakness and the consequential effect.

Weakness	Effect
<b>Housing Services</b>	
<ul style="list-style-type: none"> <li>Decision to draw down budget from future years [para. 8.1]</li> </ul>	<ul style="list-style-type: none"> <li>Financial manipulation</li> <li>Assumption that budget would be there was presumptuous</li> <li>Silo approach to financial management</li> </ul>
<ul style="list-style-type: none"> <li>Lack of clear option appraisal to support decision to proceed with Waterloo Road proposal [para. 8.4-8.5]</li> </ul>	<ul style="list-style-type: none"> <li>Members unable to prioritise between projects</li> <li>Unable to make fully informed decisions</li> </ul>
<ul style="list-style-type: none"> <li>Failure to fully specify project and allocate project management responsibilities [para 8.4, 8.6]</li> </ul>	<ul style="list-style-type: none"> <li>Confusion over who was the project manager and who had overall responsibility for the success / failure of the project</li> </ul>
<ul style="list-style-type: none"> <li>Lack of acceptance of project management responsibilities [para 8.7]</li> </ul>	<ul style="list-style-type: none"> <li>Confusion over who was the project manager and who had overall responsibility for the success / failure of the project</li> <li>Failure to comply with job description</li> </ul>
<ul style="list-style-type: none"> <li>Failure to discharge responsibilities per job descriptions [para 8.9]</li> </ul>	<ul style="list-style-type: none"> <li>Project management responsibilities were not fully and demonstrably discharged in relation to the Waterloo Road project</li> </ul>
<ul style="list-style-type: none"> <li>Financial manipulation serving to mask overspends [para 8.25, 8.26]</li> </ul>	<ul style="list-style-type: none"> <li>Breach of Financial Procedure Rule B.28 to mask overspend</li> </ul>

Weakness	Effect
<b>Housing Services</b>	
<ul style="list-style-type: none"> <li>• Use of various budget heads to cover project costs [para 2.2, 8.71)</li> </ul>	<ul style="list-style-type: none"> <li>• Total cost of project is not transparent</li> <li>• Possible detrimental effect on other schemes</li> </ul>
<ul style="list-style-type: none"> <li>• Failure to engage in steering group principles [para 8.75-8.77]</li> </ul>	<ul style="list-style-type: none"> <li>• Lack of trust and confidence in BDS relationship</li> <li>• Poor communication between Divisions</li> </ul>
<ul style="list-style-type: none"> <li>• Failure to engage Members in approval of change to capital programme and provide full information to support decision making [para 8.89]</li> </ul>	<ul style="list-style-type: none"> <li>• Inability to make an informed VFM assessment</li> </ul>

Weakness	Effect
<b>Building Design Services</b>	
<ul style="list-style-type: none"> <li>• Lack of acceptance of project management responsibilities [para 8.7]</li> </ul>	<ul style="list-style-type: none"> <li>• Confusion over who was the project manager and who had overall responsibility for the success / failure of the project</li> </ul>
<ul style="list-style-type: none"> <li>• Failure to manage client expectations [para 8.16, 8.17]</li> </ul>	<ul style="list-style-type: none"> <li>• Poor communication between Divisions</li> <li>• Project seen as “low risk”</li> <li>• Pressures on staff to start project so initial work was rushed</li> <li>• Overspend not identified until late in process</li> <li>• Project delivered late</li> </ul>
<ul style="list-style-type: none"> <li>• Failure to discharge responsibilities per job descriptions [para 8.10]</li> </ul>	<ul style="list-style-type: none"> <li>• Project management responsibilities were not fully and demonstrably discharged in relation to the Waterloo Road project</li> </ul>
<ul style="list-style-type: none"> <li>• Lack of handover procedures on staff changes [para 8.37]</li> </ul>	<ul style="list-style-type: none"> <li>• Lack of continuity and consistency</li> </ul>
<ul style="list-style-type: none"> <li>• Financial manipulation serving to mask overspends [para 8.67]</li> </ul>	<ul style="list-style-type: none"> <li>• Costs transferred from one budget head to another without appropriate justification, back-up and authorisation</li> </ul>
<ul style="list-style-type: none"> <li>• Failure to manage client expectation in terms of delivery deadlines [para 8.53]</li> </ul>	<ul style="list-style-type: none"> <li>• Failure to comply with job description</li> </ul>

Weakness	Effect
<b>Building Design Services</b>	
<ul style="list-style-type: none"> <li>• Erroneous risk assessment of project based on flawed assumptions about financial success of previous project, failure to consider structural and site differences, and absence of site visits, structural surveys etc at outset [para 8.18, 8.19,8.20]</li> </ul>	<ul style="list-style-type: none"> <li>• Project plans based on previously failed scheme</li> <li>• Design approved without approver visiting site so unexpected problems were not identified</li> <li>• Problems identified after work had commenced therefore duplicate work done</li> <li>• Could not determine whether initial / amended schemes provided / continued to provide VFM</li> <li>• Inconsistent approach between this scheme and the one it was based on</li> </ul>
<ul style="list-style-type: none"> <li>• Lack of active project management and management of / communication with contractor [para 8.34]</li> </ul>	<ul style="list-style-type: none"> <li>• Variation requests not answered so unauthorised work carried out unbeknown to client</li> <li>• Failure identify / respond to potential overspend timeously</li> <li>• Failure to adequately address staff shortages and skills gaps</li> <li>• Project considered “low risk” so not given appropriate attention</li> </ul>
<ul style="list-style-type: none"> <li>• Lack of control over and authorisation of variations [para 8.35]</li> </ul>	<ul style="list-style-type: none"> <li>• Poor detail on clerk of works report resulted in lack of knowledge on physical progress</li> </ul>



Weakness	Effect
<b>Building Design Services</b>	
<ul style="list-style-type: none"> <li>Absence of suitably professionally qualified officers during periods of staff absence and lack of management intervention to resolve and support [para 8.40-8.42]</li> </ul>	<ul style="list-style-type: none"> <li>Lack of professionally qualified officers and due reporting process</li> <li>Lack of active management reaction</li> </ul>
<ul style="list-style-type: none"> <li>Lack of monitoring sheet to match physical progress with spend [Appendix 1, Objective 9]</li> </ul>	<ul style="list-style-type: none"> <li>Progress of scheme not overtly monitored</li> </ul>
<ul style="list-style-type: none"> <li>Making decisions on work variations without authorisation [para 8.34, 8.77]</li> </ul>	<ul style="list-style-type: none"> <li>Conflict over costs due to unapproved work being undertaken</li> </ul>

Weakness	Effect
<b>Finance</b>	
<ul style="list-style-type: none"> <li>Failure to identify and report on breach of Financial Regulations [para 8.28, 8.29]</li> </ul>	<ul style="list-style-type: none"> <li>Breach of Financial Procedure Rule B.28 which had the effect of masking the overspend on Howards Road</li> <li>Failure to actively manage overspends in a timeous manner</li> </ul>
<ul style="list-style-type: none"> <li>Colluding with Housing to raise journal entries [para 8.25]</li> </ul>	<ul style="list-style-type: none"> <li>Expenditure transferred from one scheme to another without following due process</li> </ul>
<ul style="list-style-type: none"> <li>Supporting culture of financial manipulation to mask overspends [para 8.65, 8.66]</li> </ul>	<ul style="list-style-type: none"> <li>Breach of Financial Procedure Rule B.28 which had the effect of masking the overspend on Howards Road</li> <li>Failure to investigate reasons for overspends and learn for future projects</li> <li>Lack of transparency / openness</li> </ul>
<ul style="list-style-type: none"> <li>Awareness of multiple financial systems and absence of commitment accounting, but limited intervention to resolve to support production of robust and accurate financial information (lack of capital budgets on Agresso and of use of commitment accounting) [para 8.59 – 8.64]</li> </ul>	<ul style="list-style-type: none"> <li>Lack of complete picture</li> </ul>
<ul style="list-style-type: none"> <li>Lack of exception reports on journals over £25,000 [para 8.70]</li> </ul>	<ul style="list-style-type: none"> <li>Failure to identify breaches of Financial Procedure Rule B.28</li> </ul>

Weakness	Effect
<b>Finance</b>	
<ul style="list-style-type: none"> <li>Lack of formal process for authorising journal entries [para 8.29, 8.69]</li> </ul>	<ul style="list-style-type: none"> <li>Expenditure moved from one scheme to another</li> <li>Expenditure on Howards Road journalised to have a detrimental effect on the costs for Waterloo Road</li> </ul>
<ul style="list-style-type: none"> <li>Poor quality of reporting to Members [para 8.87, 8.89]</li> </ul>	<ul style="list-style-type: none"> <li>Failure to identify Howards Road overspend</li> <li>Lack of transparency / openness</li> </ul>
<ul style="list-style-type: none"> <li>Lack of defined approach to capital programming, monitoring and reporting (e.g. Procedure Manual) [para 8.71, 8.72]</li> </ul>	<ul style="list-style-type: none"> <li>Lack of consistency detailing the approach and the requirements</li> </ul>

## Summary of recommendations

1.12 Our recommendations are detailed in Appendix 2 to the main report but can be summarised as follows:-

- Housing management should clearly define project deliverables, roles, responsibilities and monitoring arrangements at the outset of projects;
- BDS staff should aim to deliver to their stated responsibilities, deliverables and timescales and to manage client expectations;
- The need for active management of resources in the event of staff changes should be emphasised to BDS staff, and supported by training where necessary
- Proper planning should be an integral part of each project;
- Financial monitoring should include exception reporting of journals to reduce the risk of failure to comply with Financial Regulations and the associated culture of manipulation of financial information must cease;
- The entire approach to capital budgeting, monitoring, virement, control and management requires re-engineering
- HR policies require to be reviewed and consistently applied;
- Proper project management principles should be adopted on future exercises;
- Operational structure require to be considered at strategic, corporate level to address value for money issues;
- The format and content of Reports to Members should be revised to include an appropriate level of detail; and
- Officers should be reminded of the need to engage members in the approval of additional expenditure where budgets are likely to be exceeded.

## Value for money assessment

1.13 The extent to which value for money has been achieved through the use of the Council's resources on the Waterloo Road project has been considered in terms of economy, efficiency and effectiveness. The project significantly overspent and was delivered late. Certain costs were avoidable had the project been properly scoped from the outset and actively managed throughout. The value for money criteria of economy and efficiency were not therefore demonstrably met.





- 1.14 However, Housing Management confirmed that they consider the Waterloo Road hostel to be of a high quality and that, despite the operational difficulties encountered during the course of the project, the final product had been delivered to the correct quality standard. The effectiveness assessment in terms of value for money is therefore positive.
- 1.15 It is possible that, had the eventual costs of the Waterloo Road hostel improvements been anticipated, Members would still have approved the work. They should, however, have been provided with sufficiently robust financial estimates to allow them to make an informed decision on the matter.

### **Overall conclusion**

- 1.16 The overspend on the Waterloo Road Hostel Improvement programme has resulted from a number of institutional shortcomings, compounded by operational weaknesses within various Divisions of the Council.
- 1.17 These weaknesses, when considered in totality, are likely to have a significant negative impact on the Council's internal control arrangements, and ultimately on the assurance that can be relied on for the preparation and publication of the Council's Statement of Internal Control.
- 1.18 Lessons must be learned from these identified shortcomings.
- 1.19 In addition, while the ultimate outcome in terms of the hostel fabric is considered by Housing Management to be effective, the project did not demonstrably meet the remaining value for money criteria of economy and efficiency.
- 1.20 A number of major actions require to be undertaken by senior management and Members to resolve the matters which contributed to this overspend, both at Corporate and Divisional levels.
- 1.21 By addressing our recommendations, the Council should be in a position to implement a framework to achieve improved capital programme management, progress monitoring and project management in future capital works.