

Quantum Leap

Report

Shropshire Council

Audit 2011/12

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Introduction

1 In October 2011, local electors raised concerns with me in correspondence about the costs and value for money of the sculpture, Quantum Leap, a public work of art built to commemorate the bicentenary of Charles Darwin. The costs of which had risen from an original budget of £200,000 to exceed £1 million.

2 The sculpture was commissioned by Shrewsbury and Atcham Borough Council (SABC). Architects were appointed in April 2008 and planning permission was granted in September 2008 by SABC. The budget had increased to £388,090 in January 2009 when the firm of contractors responsible for constructing the structure were awarded the work by SABC with the appointed architects acting as contract administrators.

3 Work started on site in February 2009 with an initial planned completion date of June 2009. This straddled the transition date for local government reorganisation. A Transition Board was put in place to manage the local government reorganisation between Shropshire Council and all of the demising district councils in Shropshire. This agreed a further increase of £100,000 in the budget to re-orientate the structure to avoid the tree root preservation area.

4 As part of local government reorganisation, responsibility for the completion of the project passed to Shropshire Council in April 2009. Erection of the structure took place from April to July 2009 when it was found that there were problems in the construction of the arch. Practical completion was achieved in April 2010, some ten months after the original planned completion date. The delay resulted in significant additional costs, the liability for which was disputed between Shropshire Council and the contractor. In April 2011 formal dispute resolution was initiated and in July 2011 an independent adjudicator determined that liability for the additional work, other than some minor sums, lay with Shropshire Council. Following the settlement of this judgment the final total costs of the project, including external professional fees, were £1,015,090.

Audit responsibilities

5 External audit is an essential part of the process of accountability for public money. As the Council's external auditor, I operate within a statutory framework which determines the nature, level and scope of my work. My responsibilities under this framework, are to provide:

- an independent opinion on the Council's accounts; and
- an independent value for money conclusion as to whether the Council has put in place proper arrangements for securing economy, efficiency and effectiveness – including sound governance – in its use of resources.

6 I also have a responsibility to consider matters brought to my attention by members of the public. I can however only consider issues that are

relevant to an 'open' audit; that is where the audit certificate has yet to be provided.

7 At the time the concerns were raised with me and I undertook my enquiries only the 2011/12 audit at Shropshire Council remained open. The majority of the key decisions on the project pre-date 2011/12 and some were made by the now demised SABC. I have documented these decisions to provide the necessary context but I have only considered these matters, and where appropriate formed views and judgments, insofar as they may impact on Shropshire Council's arrangements and financial transactions in 2011/12.

Audit approach

8 I have considered the matters raised with me in the context of my responsibilities, as outlined above. As part of my audit work, I have reviewed available documentation relating to the planning and management of the project and liaised with Shropshire Council officers. Shropshire Council was unable to provide me with the documentation relating to the tender evaluation of the design and the appointment of the contract administrator, due to an inability to access Shrewsbury and Atcham BC documentation following local government reorganisation. This has limited my ability to understand in full the reasons for the additional costs. This report deals with my findings relating to the cost overruns on the project, insofar as they may impact on Shropshire Council's arrangements and financial transactions in 2011/12, based upon my review of the documentation provided and explanations received from Shropshire Council officers.

9 The appointment of the contractor administrator, awarding of the construction contract and the granting of planning permission by SABC took place 2008 and 2009 respectively. The audit of SABC's financial statements for 2008/09 has been certified as complete by its appointed auditor at the time. Some of the additional costs of the project were met by Shropshire Council in 2009/10 (£212,104) and 2010/11 (£33,718). The audits of Shropshire Council's financial statements for 2009/10 and 2010/11 have also been certified as complete. I therefore have no statutory power to consider any transactions or issues prior to 1 April 2011. There are, however, transactions relating to the Quantum Leap project reflected in Shropshire Council's 2011/12 financial statements, specifically the settlement of disputed costs with the contractor and other professional and adjudicator fees to the total of £539,871. These do fall within my statutory responsibilities and I have therefore considered these payments and related matters as part of my 2011/12 audit.

10 As noted above an independent adjudicator has already concluded that liability for additional work, other than some minor sums, lay with Shropshire Council. The adjudicator formed his view after a detailed consideration of the technical aspects of the design, review of evidence provided and following discussions with all parties involved. It is not my role, in this report, to review this judgement. Also, as the award of the contracts and the issuing

of contract variations for agreed work took place in closed years of account, there is no statutory basis for me, as Shropshire Council's external auditor, to carry out further work on this issue. I have, however, considered the actions the Council has taken in the management of the construction process, the reporting to Members and the Council's use of external construction advice following transfer of responsibility for the management and completion of the project to it in 2009, in so far as these relate to my statutory responsibilities. Having reviewed the project to completion I am of the view that there are some lessons to be learnt for future projects. I have raised recommendations in this report which have been accepted by officers.

11 I have also considered whether any formal audit action is required as Shropshire Council's appointed auditor for the financial year ended 31 March 2012 a result of my findings, including recognising that the matters are of local concern. I have discretion as District Auditor to determine whether the matters raised with me are of such significance that I should issue a report in the public interest under section 8 of the Audit Commission Act 1998. I have determined that this would not be appropriate in this instance. I believe a more appropriate and proportionate approach is to report my findings in this document to Shropshire Council's Audit Committee, the agenda (which will contain this report) and minutes of which will in due course become public documents.

Background

12 The sculpture was commissioned by Shrewsbury and Atcham Borough Council to commemorate the bicentenary of Charles Darwin. The project was agreed at its full Council in February 2008. Invitations to tender were issued and a shortlist of design teams was drawn up in April 2008. A public exhibition of the submitted designs took place and feedback was received from stakeholders. The winning bid from the appointed architects was agreed by a majority vote at the end of April 2008 and a standard form of contract drawn up. Planning permission for Quantum Leap was granted in September 2008 by SABC.

13 In January 2009 a firm of contractors were awarded the work in the sum of £263,216 with the appointed architects acting as contract administrators. Funding had been received for part of the work and some materials had been donated. Work started on site in February 2009 with an initial planned completion date of June 2009. This straddled the transition date for local government reorganisation. In March 2009 the project was delayed as equipment could not be put in place due to a tree root preservation order on the site. An additional £100,000 was agreed by the Transition Board (put in place to manage the local government reorganisation between Shropshire Council and SABC) as part of the 2009/10 capital programme. The additional sum was to cover the costs of the work to re-orientate the structure to avoid the tree root preservation area. This involved making changes to the foundations and piling. The additional funding came from SABC resources. The reserves transferred to Shropshire Council under

local government reorganisation were reduced by these amounts. The additional £100,000 included a contingency sum of £50,000 to address any future problems.

14 As part of local government reorganisation, responsibility for the completion of the project passed to Shropshire Council in April 2009. Erection of the structure took place from April to July 2009 when it was found that there were problems in the construction of the arch. The reason for the misalignment was disputed between the contractor and the contract administrator. On 27 July 2009 the contract administrator, after a visit to the site with Shropshire Council representatives, notified the contractor that the work was unsatisfactory. Further work was undertaken to correct the misalignment and the liability for the costs of the additional work remained in dispute. Practical completion was achieved in April 2010, some ten months after the original planned completion date, and after significant additional cost had been incurred.

15 Shropshire Council agreed the appointment of a quantity surveyor in December 2009 to assist the contract administrator in managing the risks due to the complexity of the project and reviewing liability for the disputed costs. In April 2011, formal dispute resolution was initiated by the contractor in accordance with the contractual procedures in place, and an independent adjudicator was appointed. In July 2011 the adjudicator decided that liability for the additional work, other than some minor sums, lay with Shropshire Council. The Council was required to pay the contractor the full costs of £457,819 associated with the delay and disruption. In addition, Shropshire Council incurred its own costs including:

- external professional costs;
- the cost of the adjudication process; and
- in-house costs such as the cost of legal and other officers' time.

16 The cost of the project was originally budgeted by SABC at £200,000. As a result of the issues identified above, the final total costs of the project, including external professional fees, were £1,015,090 (see table 1 below). The cost overruns have had a high public profile and were reported by the local press.

Table 1: **Budgeted and Actual Costs of Quantum Leap Project**

Budget	£	Actual Costs	£
Original SABC Budget	200,000	Final Contract Costs	861,268
Additional SABC funding 2008/09	55,000	Adjudicator Costs	6,392
Additional other funding 2008/09	133,090	Professional Fees	108,076
Additional funding from SABC reserves 2009/10	100,000	Other costs (including rock clock and signage)	39,354
Final budget following expected increase in costs for realignment	483,090	Total Costs	1,015,090

In addition to the above costs, a project sponsor provided materials for the sculpture. The estimated value of these materials was £150,000.

17 This report deals with my findings relating to the cost overruns on the project, insofar as they may impact on Shropshire Council's arrangements and financial transactions in 2011/12, based upon my review of the documentation provided and explanations received from Shropshire Council officers.

Overall conclusions

18 The final cost of the Quantum Leap project increased from an original budget of £200,000 to over £1 million. The majority of this cost overrun related to the difficulty in constructing the design. The liability for these additional costs remained in dispute for over a year until formal dispute resolution procedures were initiated by the contractor. Both parties made submissions to the adjudication process. The Council alleged that the costs had arisen due to deficiencies in the construction work. The contractor alleged that the design of the structure was flawed and additional work had therefore been required. The independent adjudicator, after reviewing the evidence provided, decided that the original design specification for the sculpture was at fault and required Shropshire Council to pay the contractor for the disputed costs of the additional work. This was contrary to the conclusions of the expert witness report commissioned by Shropshire Council to support its submission.

19 I have been informed that, as a result of their assessment of the specification, the matter was not considered by SABC to be of a high enough risk to require a quantity surveyor to review the design before the tender was awarded. Such a review may have identified the risks of additional time and increasing costs required by the challenging design of the structure.

20 The management of the project was made more complicated by local government reorganisation which took place in April 2009, as the construction of the project was beginning, and responsibility for the work moved from SABC to Shropshire Council as the successor body. However the reorganisation itself is not the reason for the cost overruns.

21 Shropshire Council inherited agreed contracts for design and contract administration of the project and the contractors had been appointed at the time of reorganisation. The Council reviewed the arrangements they had inherited. They allocated additional budget to address initial issues of siting the design and included a contingent sum intended to cover any further costs of construction. A project board was set up to monitor the construction of the design, regular meetings took place and a Council project manager reported to the project board. The board identified a number of risks with the arrangements they had inherited, most notably the low level of professional indemnity insurance in place that, in the case of a successful claim, would cover losses arising. Officers wrote to the contract administrators in May 2009, shortly after LGR, attempting to increase the level of insurance to the

levels required by Shropshire Council's arrangements and which would have been equivalent to an amount that would have covered the eventual losses on the construction of the design. This action was noted in the project board meetings, while the disputed additional costs were being incurred, but the Council were unable to increase the level of indemnity insurance. The Council is therefore not in a position to claim for the full amount of the losses incurred on the contract.

22 The majority of the additional costs arose from July 2009. At this point the arch had been completed. The construction contractor was of the view that the contractor administrator had approved the alignment and had therefore carried out work to finalise the structure. At a subsequent site visit a misalignment in the structure became apparent. The question of the approval of the alignment of the arch by the contract administrator was disputed and both sides argued that liability lay with the other party. Due to the stage of construction, a significant level of work was required to achieve final completion of the intended design. The project manager, a chartered surveyor, with significant experience in this role, took a report to the project board in August 2009 stating that this was a significant matter for the Council and that the scale of the costs was not known. The report recommended that the Board needed to seek legal and contractual advice to clarify the Council's current position and future action and to ensure that the Council's approach protected its interests.

23 Work was halted for a brief stage and a site meeting was held in August 2009. This meeting noted the need for a clear programme for going ahead without concluding liability for the additional work. The Council was balancing the risks of incurring additional delays and daily costs for revisiting the specification with the risks of continuing and rectifying the alignment. In my view, the decision to proceed without formally concluding where liability for any additional costs lay did expose the Council to the risk that it may become liable for them. The Council is clear that this decision was based upon advice that the contractor was at fault and that in situations of this type normal practice is to complete the works and determine liabilities afterwards. Improved documentation and transparency of this decision making process would have assisted in it being able to demonstrate appropriate governance arrangements were in place and operating.

24 In line with the contract conditions any disputed additional work to address the misalignment was not included in approved contract variation documents. As a result, the budget monitoring outturn position only included the agreed costs. Inclusion of the disputed sums within Project Board financial projection reports would have assisted in ensuring it had a clear understanding of the potential liability should the Council's advice that it would not be liable for the disputed costs have proven incorrect.

25 The Council has stated that it took advice from its officers and the contract administrator throughout the time of the project. An internal option appraisal in November 2009 identified that the main parties to the project were in a position of dispute in respect of delays and cost overruns. It concluded that adjudication was the likely outcome with the risk of

significant professional costs the Council in preparing a defence. Practical completion was not attained until April 2010 and in November 2010 a specialist structural engineer was appointed to provide advice when it was thought likely that the contractor would initiate formal dispute resolution. The advice supported the Council's view that that the design specification was adequate.

26 The Council received an offer from the contractor, before the final account had been agreed and the adjudication process entered into, to settle the dispute for a total contract cost of £600,000. The Council obtained professional advice which indicated that the Council was likely to be successful in its claim. I do not believe that its actions in obtaining this advice, or in taking part in adjudication, were unreasonable.

27 However, due to the complexity of the case, the costs of professional advice were in excess of what had been estimated. Other professional time of the contract administrator and other expert support was also required. Following the adjudication, these costs, and the costs of the adjudication process, represented over £114,000 of the total costs of the project. I believe that the Council, while pursuing what it believed to be the best course, based on the professional advice provided, could have done more to document its consideration of value for money in evaluating this initial offer for early settlement, for example, by estimating the possible additional costs of continuing with the adjudication process compared to the possible costs that the Council might have to meet should the adjudication process find against them in some areas.

28 The adjudicator formed his view after a detailed consideration of the technical aspects of the design, review of evidence provided and following discussions with all parties involved. It is not my role, in this report, to review this judgement. I have, however, considered the actions the Council has taken in the management of the construction process, the reporting to Members and the Council's use of external construction advice following transfer of responsibility for the management and completion of the project to it in 2009, in so far as these relate to my statutory responsibilities. Having reviewed the project to completion I am of the view that there are some lessons to be learnt for future projects. I have raised recommendations in this report which have been accepted by officers.

29 When conducting my investigations not all of the relevant information was available for my review. This was due to documents not being made available to Shropshire Council during handover arrangements from SABC, particularly in relation to the initial tendering and evaluation of the design of the sculpture and the appointment of the contract administrator. SABC is no longer in existence and the audit of its financial statements for 2008/09 and those for Shropshire Council for 2009/10 and 2010/11 have been certified as complete. I therefore have no statutory power to consider any transactions or issues prior to 1 April 2011. It is therefore not appropriate for me to undertake further work in this area, rather I have set out my conclusions below based upon the evidence I have at this time.

Tendering for Quantum Leap

30 The majority of the key decisions on the project pre-date 2011/12 and some were made by the now demised SABC I. I have documented these decisions to provide the necessary context but I have only considered these matters, and where appropriate formed views and judgements, insofar as they may impact on Shropshire Council's arrangements and financial transactions in 2011/12.

31 I have been informed by Shropshire Council that in 2006 a feasibility study was carried out by the Shrewsbury Public Arts Partnership to explore a lasting legacy to commemorate the bicentenary of Charles Darwin. Funding was provided by the Arts Council to produce a design brief and in February 2008 SABC'S Cabinet agreed the expenditure as part of their capital programme. This was approved by full Council on 13 February 2008. In April 2008 a shortlist of three design teams presented their designs to the selection panel. Feedback was obtained from a number of sources, including local residents, conservation, planning and environmental health. The winning architects were awarded the contract on 28 April 2008 by a majority vote.

32 Shropshire Council has informed me that SABC did not consider that an overview of the project by a quantity surveyor, to assess the design specification, was required as it was not considered sufficiently high risk. I am unable to determine what selection criteria for the design and the appointment of the contract administrator were in place and the checks that were carried out or the results of any checks. I am also unable to determine, due to lack of documentation:

- if SABC complied with its own standing orders and procedures;
- how SABC evaluated the specification against the budget allocated; or
- how SABC ensured that officers or other experts with sufficient technical expertise assessed the submitted design for any future risks, particularly the financial risks, of proceeding with such a complex project.

33 After the tender for the design of Quantum Leap and the appointment of the contract administrator by SABC was concluded, a further tender process to appoint a contractor to build the design was carried out by SABC. I have been provided with the tenders submitted but I have not seen documentation relating to the evaluation of the tenders. Four tenders were received and the winning tender was then awarded by SABC.

34 Shropshire Council's Internal Audit reviewed the awarding of the tender to the contractor in January 2010. Internal audit noted that there was a lack of evidence regarding the evaluation of the tender. Internal audit confirmed that the lowest tender was accepted, following some minor adjustments to amounts for additional works to be carried out. There were significant differences between the values of the tenders submitted. Internal audit noted that the documentation they reviewed did not contain evidence of any professional member of the tendering team at SABC querying if the winning tender was too low. Internal audit noted that a professional opinion would be

required to confirm the adequacy of design drawings and specification and did not comment further on this.

35 I have been informed by officers that the contract administrator was a company specifically formed to tender for the work required. No evidence has been made available to me to indicate how SABC evaluated if there were any potential, or increased, risks from such an arrangement and how these might be considered in terms of indemnities for a failure to deliver required services. Professional indemnity insurance was agreed with the contract administrator in the sum of £250,000, significantly less than the final costs of the project. Shropshire Council, as examined later in this report, noted early in their management of the project that this level of indemnity insurance presented a risk, and attempted to increase the level in line with their own procedures.

36 In July 2011, the adjudicator decided that the delays and cost overruns were due to an inadequate design specification (that Shropshire Council had inherited on LGR) and that the Council was liable for the additional costs of this project.

Project management of the contract

37 Shropshire Council inherited a number of capital projects at the time of local government reorganisation presenting a significant challenge in terms of project management. Arrangements were put in place on a timely basis to manage the construction of Quantum Leap, including the appointment of a project manager and a project board that met regularly to consider risks, progress and necessary actions. The project was not identified as high risk at the time of handover to Shropshire Council and at that point officers had no indication of the potential risks of the design. The only delays at the time of handover were issues relating to the location of tree roots. The contract administrator provided Shropshire Council with professional advice on the project.

38 The project board identified a risk relating to the level of professional indemnity insurance early in the project. Shropshire Council require a level of indemnity insurance at a minimum level of £1 million and an action was noted by the project board in May 2009 to review the £250,000 level of insurance that had been agreed with SABC. A letter was sent to the contract administrator in May 2009 requesting that the insurance level was increased to £2 million. The project board minutes, throughout the period from May to December 2009, including the period when the additional work was ongoing, repeat the action regarding the need to increase the level of indemnity insurance. Correspondence dated November 2009 between the Council and the contract administrator notes that a quote for £1 million indemnity insurance had been obtained and the Council asked the contract administrator to propose a sum for the Council to contribute to the cost of the additional insurance. The Council were unable to achieve successful resolution of this issue with the contract administrator and the level of indemnity insurance remained at £250,000 as per the original SABC contract which Shropshire Council had inherited.

39 Shropshire Council officers' view is that, in line with normal contract procedures, they were provided with advice by the professionals employed on the contract, including the contract administrator and a structural engineer. The Council has stated that it had regard to industry practice in managing this project. As no significant issues were identified at the time of transfer of responsibilities, officers maintained an 'arms length' overview of the situation in line with the project management principles used by Shropshire Council. In line with the procedures in place, the Council's project manager submitted an exception report to the project board in August 2009. The report notes the misalignment discovered in the final construction of the arch. The contract manager informed the contract administrator that this was unacceptable and the contractor was instructed to halt work to allow options to be considered. The report states:

'The issue regarding liability is a significant matter for the Council and the Board needs to consider whether legal and contractual advice is sought to clarify the Council's current position and future action.'

40 The August 2009 report notes that the scale of the additional costs was not yet known. The site minutes provided to me dated 10 August 2009 note the need for a contractual meeting to discuss liability for the current situation. The minutes then state 'there is still most of all a need for a clear programme for going ahead without concluding liability.' I have been informed that a meeting was held around this time between the project team and the Council's legal officers to assess the Council's options and which ultimately informed the report produced in November 2009 (see paragraph 45). The Council has not been able to provide evidence of this meeting or a record of outcomes. However, I have seen evidence that legal and contractual advice was being taken in October 2009, before the majority of the additional costs were incurred. Clearer documentation of how the Council considered the matter would have helped support the reasonableness and transparency of the decision-making process.

41 The Council has informed me that it operated at all times with the benefit of professional advice from the contract administrator, the quantity surveyor, following his appointment, and later, in the adjudication process, with the advice of specialist construction advice, all of which indicated that the Council was not at fault in respect of the misalignment, and therefore were not likely to be liable for the costs. It was also considered by the Council that work should continue as the structure was then partially complete and significant cost would be incurred if work was suspended for any length of time.

42 The Council was balancing the risks of incurring additional delays and daily costs for revisiting the specification with the risks of continuing and rectifying the alignment. In my view, the decision to proceed without formally concluding where liability for any additional costs lay did expose the Council to the risk that it may become liable for them. The Council is clear that this decision was based upon:

- advice that the contractor was at fault;
- that in situations of this type normal practice is to complete the works and determine liabilities afterwards; and
- that it was consistent with the contractual requirements.

Improved documentation and transparency of this decision making process would have assisted in it being able to demonstrate appropriate governance arrangements were in place and operating.

43 Standard industry practice is that where costs are being disputed, such as the additional work to correct the misalignment, these are not included in the standard process for approving variations to the contract. This process is used only for additional work that has been agreed between both parties. However, the adjudicator examined the issues of how the variations were issued and approved in respect of the additional work and considered that there was sufficient evidence of approval for the Council to be liable for the additional costs.

44 I have seen records of how other less significant variations were approved by the Council in line with procedures in place. The site minutes of 25 September 2009 note that a variation in respect of the rectification of the arch top was disputed and that details relating to a further variation regarding disruption of works would be provided on completion of the additional work. The additional disputed costs were included as a note to financial summaries of the project. However, due to their disputed nature they were not included in the budget summaries and details of under/overspends on the contract at that point. Whilst noting that this is standard Shropshire Council reporting practice, and that commercial confidentiality issues may have prevented such items being on the public agenda of meetings, in my view, the failure to formally recognise potential liabilities when reporting on performance against budgets meant that the potential position on the project was not clearly communicated to Members.

45 A Project Board meeting on 4 November 2009 recognised the need for a briefing note outlining the situation from a progress and budget position. An internal option appraisal was produced later in the month that was circulated to Directors, the Council Leader and the Portfolio Holder. This identified that the main parties to the project were in a position of dispute in respect of delays and cost overruns. It concluded that adjudication was the likely outcome with the risk of significant professional costs to the Council in preparing a defence.

46 The Council agreed to the appointment of a quantity surveyor in December 2009 to assist the contract administrator in preparing the final accounts and managing the risks due to the complexity of the project and reviewing liability for the disputed costs. The project board minutes and decisions made subsequent to this, and provided for my review, are not sufficient for me to understand:

- the discussions that took place regarding progress;
- to confirm the decisions that were made; and
- how the Council further considered its response to the legal, contractual and financial risks.

Until November 2010 when a specialist structural engineer was appointed to provide advice when it was thought likely that the contractor would initiate formal dispute resolution. I have found no evidence that the decisions reached by the Council were unreasonable but improved documentation would assist in improving the transparency of the decision making process.

Reporting to Members

47 As I have noted above, reporting to formal Member meetings during the period does not refer to the additional disputed costs that were being incurred. The internal option appraisal in November 2009 was used as the basis for briefing the Chief Executive, Leader and Portfolio Holder of the risks. A report to Cabinet in September 2010, after the completion of the additional work, but before the adjudication process began, informed Members that only retention payments remained in respect of Quantum Leap and that there was a remaining budget of £69,264 for this. No reports to formal Member meetings raised the risk that the additional costs might become payable by the Council.

48 The Leader was briefed on the adjudication process in April 2011. A report to Cabinet relating to the additional costs of Quantum Leap was made in September 2011. This was the first report available for public scrutiny and was after the conclusion of the adjudication process. This report informed Members of an additional budget increase for the project of £532,000 due to liability for costs having been apportioned to the Council. Whilst recognising that commercial confidentiality issues may have prevented disputed items being on the public agenda of meetings, given the high profile and financial risk of this matter, I believe that aid transparent decision-making Cabinet Members could have been informed earlier and more regularly by officers of the potential liabilities should the Council's advice that it would not be liable for the disputed costs have proven incorrect.

49 It is clear from the internal report produced in November 2009 that officers had identified the potential risks from the various ways a dispute with the contractor might be resolved. Despite the indications that the Council would be successful in defending its position at the time, my view is that improved documentation and transparency of the decision making process would have assisted in it being able to demonstrate appropriate governance arrangements were in place and operating, including formal reporting to Members. As noted above, the November 2009 internal report was used as a basis for briefing the Leader and Portfolio Lead and senior officers. I also understand from officers that other regular informal briefings to portfolio holders were taking place. Up until November 2010 the records of these meetings are incomplete but after this date they demonstrate that Members were regularly briefed on the possibility of formal dispute resolution and the progress of the adjudication. These reports continued until the adjudication decision was made in July 2011.

External construction advice for the adjudication process

50 Shropshire Council obtained external construction advice from a specialist construction firm to support their submission to the adjudication process. As noted, the Council's decision to take external construction advice was based on its view that the additional costs were due to the contractor and officers believed that specialist construction advice would support their submission to the adjudication process. The external construction firm's expert opinion was that the design specification was adequate. On this basis the Council was satisfied that its position was likely to be supported by the adjudication process.

51 The adjudicator's view was that, other than minor amounts, liability for the cost overruns lay with Shropshire Council. I have reviewed the detailed report of the adjudicator's investigation into how each of the additional costs arose. In summary, the adjudicator's view was that the additional costs arose from the inadequate design specification. This was contrary to the conclusions of the expert witness report commissioned by Shropshire Council to support its submission.

52 A briefing note prepared for Members on 30 November 2011 states that the contractor made a verbal offer to settle for a lower amount than the final award of costs (£600,000 compared to the final payment to the contractor of £861,268) and before other professional fees and adjudication costs were incurred. I have been informed that the offer was considered by officers, and a decision was made to proceed to adjudication as Shropshire Council believed that it would be successful in the adjudication process, based on the professional advice it had obtained from an expert witness report and its specialist construction advisers. The note confirms that Shropshire Council has limited experience of dispute resolution but provides no written decision or analysis of any considerations on the option to settle in the briefing note or other documents provided for my review. The Council should better document its considerations on such matters, based upon appropriate

professional and/or legal advice on the offer, in order to be able to demonstrate that it has reached a reasonable and transparent decision.

53 In my view it was not unreasonable, based on the balance of evidence before them, for Shropshire Council to obtain external construction advice to support their submission to the adjudication process, believing that their case was likely to be successful. However, the cost of the construction advice in the sum of £108,076 and adjudicator costs of £6,392 are a significant part of the total cost overrun, and are higher than Shropshire Council anticipated when this support was obtained and the adjudication process was commenced. Officers have told me that Shropshire Council disagrees with the adjudication decision but is unable to challenge the decision within the process in place, as the adjudicator's decisions are final and binding. Officers are evaluating options in respect of a claim against the contract administrator's indemnity insurance of £250,000 to recover some of the additional costs. However, their initial view is that this would require either arbitration or litigation with the potential for significant further costs.

Next steps

54 The Audit Committee needs to consider carefully the contents of this report and the recommendations I have summarised below. It then needs to agree the detailed actions needed in response and oversee their implementation. External audit responsibilities will be transferring to Grant Thornton for the 2012/13 audit year. I will be making a copy of this report available to them so that they can consider it when discharging their audit responsibilities.

55 Shropshire Council, as the successor Council, has a number of procedures in place that they believe would provide assurance if a similar capital project was undertaken:

- indemnity assurance level requirements are higher than those applied to Quantum Leap; and
- enhanced work on specification and evaluation of tenders is required as detailed in the Council's constitution.

I have no reason to believe that the issues noted in respect of indemnity assurance or awarding of tenders relating to Quantum Leap apply more widely to the Council's project management arrangements or capital programme.

Summary of recommendations

- R1** Ensure that documentation of the management of capital projects, particularly where PRINCE2 contact management is used, is sufficient to provide an audit trail through clear reporting of issues and actions taken.
- R2** Where contract design problems, additional works and cost are being incurred, or other issues are identified ensure that arrangements are in place to ensure:
- the risks are managed and action is triggered early even if the Council believes it will not be responsible for additional costs;
 - there is reporting and tracking of progress on all capital projects to formal Member meetings as soon as significant risks are identified; and
 - where the Council finds itself in dispute ensure appropriate arrangements are in place to consider and document the relative risks (ie financial, legal, professional, reputational) and any decisions on whether to pursue or settle them so that it can demonstrate how those decisions offer value for money to council tax payers.
- R3** Where the Council finds itself in dispute ensure:
- that where the PRINCE 2 project management clause is utilised on a project the appropriate variations are confirmed in writing with the Council before being issued;
 - where costs have been incurred but are in dispute that any potential liabilities are appropriately recognised in budget monitoring reports (using confidential agenda items if necessary); and
 - for major capital contracts the appropriate separation of duties is identified and recorded to ensure the 'employers' role in the oversight of arrangements and monitoring of performance is clearly set out and defined.
-

Appendix 1 Action Plan

Recommendations

Recommendation 1

Ensure that documentation of the management of capital projects, particularly where PRINCE2 contact management is used, is sufficient to provide an audit trail through clear reporting of issues and actions taken.

Responsibility	Area Director, North
Priority	Medium
Date	March 2013
Comments	Agreed

Recommendation 2

Where contract design problems, additional works and cost are being incurred, or other issues are identified ensure that arrangements are in place to ensure:

- the risks are managed and action is triggered early even if the Council believes it will not be responsible for additional costs;
- there is reporting and tracking of progress on all capital projects to formal Member meetings as soon as significant risks are identified; and
- where the Council finds itself in dispute ensure appropriate arrangements are in place to consider and document the relative risks (ie financial, legal, professional, reputational) and any decisions on whether to pursue or settle them so that it can demonstrate how those decisions offer value for money to council tax payers.

Responsibility	Area Director, North
Priority	High
Date	December 2012
Comments	Agreed

Recommendations

Recommendation 3

Where the Council finds itself in dispute ensure that:

- where the PRINCE 2 project management clause is utilised on a project the appropriate variations are confirmed in writing with the Council before being issued;
- where costs have been incurred but are in dispute that any potential liabilities are appropriately recognised in budget monitoring reports (using confidential agenda items if necessary); and
- for major capital contracts the appropriate separation of duties is identified and recorded to ensure the 'employers' role in the oversight of arrangements and monitoring of performance is clearly set out and defined.

Responsibility	High
Priority	
Date	December 2012
Comments	Agreed

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Audit Commission

1st Floor
Millbank Tower
Millbank
London
SW1P 4HQ

Telephone: 0844 798 3131

Fax: 0844 798 2945

Textphone (minicom): 0844 798 2946