

## VOTE 25. - ENVIRONMENT AND LOCAL GOVERNMENT

### 21. Controls over Local Authority Finances

The Local Government Audit service (LGA) is responsible for the audit of the accounts of all Local Authorities. In addition to the Local Authorities themselves, the LGA audit reports are submitted to the Department of Environment and Local Government as part of the controls exercised by the Department in relation to public expenditure by the Authorities. Some £624m was paid to Local Authorities by the Department in 1998. Copies of the audit reports are made available to me in my capacity as auditor of the Department. As at 1 July 1999, I had received copies of all 39 LGA reports for 1996 and copies of 31 of the 1997 reports.

In both my 1996 and 1997 Reports, I referred to certain critical comments included in the LGA reports about controls over Local Authority finances. These comments were common to a number of Local Authorities and had been adverted to in previous years' reports. My review of the 1997 LGA reports indicated that the matters reported in previous years continued to feature as audit concerns and included the following:

- Capital projects carried out by Local Authorities are usually financed by way of recoupment of the agreed cost from the Department. However, Authorities do not always recoup the full cost of projects, for example, when adding to their land banks for future housing development, or when engaged on projects not funded by departmental schemes. Such expenditure, where unmatched by receipts, is shown in the Authorities' accounts as Adverse Debit Balances on Capital Account. The LGA reports continue to highlight these balances, specifically drawing attention to the fact that many are unfunded. In those reports which I have examined, a total of almost £8m is highlighted as unfunded. The LGA reports also identify other debit balances of over £37m. It is not apparent in most cases how these balances are to be eliminated through funding from internal and/or external sources.
- Some Local Authorities continue to carry adverse Revenue Account balances with no provision for their elimination in the following year's estimates. Earlier than usual receipt of higher education grants gave a once-off boost to the 1997 Revenue Account balances of many Local Authorities. The total adverse balances identified in the LGA reports which I have examined amounts to £39m.
- The internal audit function is still not in place in many Local Authorities or, where an internal auditor has been appointed, the function is restricted in operation, in some authorities.
- Expenditure in excess of estimates should be approved beforehand by the Local Authority. Various programmes had expenditure exceeding that estimated without such approval, although retrospective approval was given in most cases in the following financial year. The situation showed some improvement over previous years, with a reduction in the number of cases where this type of incident occurred.
- The collection yield on Local Authority service charges and housing rent and annuities showed improvement in 1997, with the number of Local Authorities subject to critical comment on this matter being reduced in that year.



## 22. Cost Overruns on Fire Stations

Under the Department's reporting and budgetary measures for fire station projects, Local Authorities embarking on a project require the Department's approval at all stages, from preliminary to contract stage. At construction stage, the drawdown of project funds by the Local Authority is subject to control by the Department. The approval of the Department of Finance is also required for projects over £1m in value. In the course of audit it was noted that a number of projects had final costs significantly in the excess of the original estimate as outlined in Table 3.

*Table 3 - Cost of Fire Station Projects at Each Stage*

Project	Project Approval in Principle £	Design Stage £	Contract Stage £	Final Cost £	Grant Paid to Date £
Listowel	300,000 (1993)	365,000 (1994)	405,400 (1996)	422,500 (1997)	413,900 (1998)
Kells	300,000 (1990)	355,000 (1995)	355,000 (1997)	421,000 (1998)	355,000 (1999)
Kilrush	330,000 (1989)	337,100 (1993)	413,300 (1997)	436,900 (1998)	415,900 (1999)
Wicklow	250,000 (1992)	256,000 (1994)	319,300 (1997)	357,000 <sup>1</sup> (est 1999)	338,000 (1999)
Milford	300,000 (1990)	299,900 (1991)	336,400 (1996)	411,400 (1998)	330,000 (1999)
Kilbeggan	295,000 (1995)	277,000 (1996)	312,700 (1997)	331,370	300,000 (1999)
Kilkenny	96,600 (1990)	102,000 (1992)	227,400 (1996)	255,700 (1998)	255,700 (1998)

<sup>1</sup> *Estimated, pending receipt of final accounts from the Local Authority*

In response to my inquiries the Accounting Officer stated that, generally, the principal causes for cost increases were:

- The significant time lag of some 5 to 6 years between approval-in-principle stage and completion of the projects. This delay was due to the limited funding available to the Fire Services Capital Programme, (average £4.8m per annum in the period 1990 - 1998), and the high level of demand from the fire authorities for funding of capital projects. As a result, cost estimates were overtaken by building industry increases.
- Conditions in relation to design and finishes imposed by planning authorities.
- Statutory increases under the terms of a contract's price variation clause.

- Variations to works specified in original contracts and additional works carried out at the request of fire authorities. Where the fire authorities do not obtain departmental approval prior to, or at the time of incurring these additional costs the increases are examined fully by the Department at final account stage and a decision taken as to whether they qualify for fire services grant aid.

In an effort to minimise cost increases, and notwithstanding the comprehensive cost control procedures already in place, the Department has introduced further controls which, *inter alia*, require the authorities to:

- Submit updated cost estimates for approval before proceeding to invite tenders in the case of proposals that have been before the Department for some time.
- Seek fixed price contracts for projects.
- Reduce the number of Prime Cost and Provisional Sums in contracts (where possible the items involved to be measured and priced competitively by tenderers).
- Review projects where, on receipt of tenders, it is clear that the approved budget limit will be exceeded.

In addition, the Department is now capping grants at appropriate limits at project detailed design or tender stages, where it considers this action to be necessary. All costs in excess of such limits would be a matter for the fire authorities to meet from their own resources, thus placing an incentive on the authorities to exercise stricter cost control measures. The Accounting Officer also stated that although it is expected that these provisions will go some way to curb the increasing costs of fire stations, it has to be accepted that the predominant factor in relation to cost increases is the degree of competition prevailing in the construction industry.



### 23. Tara Street Fire Station

In August 1996, following a public competition, Dublin Corporation stated they had accepted a tender of £3.6m for construction, on a design and build basis, of a new fire brigade headquarters at Tara Street, Dublin. The design and build contract required the contractor to provide a finished building for purchase by the Corporation, which would be completed in every respect and suitable for the intended purpose. The successful tender included a provision for the contractor to purchase surplus land on the site for a private development, at £1.2m, bringing the estimated net cost of the Corporation's project down to £2.4m.

Although it had embarked on the project and accepted the tender without the Department's approval, the Corporation formally requested a grant of £2.4m in December 1996. The Department had earlier contributed £450,000 in grants and £200,000 in loans towards site costs at Tara Street, but turned down the Corporation's grant application in January 1997 and again in April 1998, as the project had not been approved. The Department noted that despite its refusal of grant assistance, the contractor was on site in January 1997. However, in December 1998, £1m was paid to the Corporation as a once off contribution to the project. The Department advised the Corporation that no further contributions would be forthcoming. The current estimated net cost of the project is £4.37m as against the initial estimated net cost of £2.4m.

In response to my inquiries as to why the Department paid £1m when the contract had originally commenced without departmental approval the Accounting Officer informed me that:

- Dublin Corporation had for a number of years been seeking to redevelop the site at Tara Street. In seeking Exchequer assistance, Dublin Corporation pointed out that the Tara Street Station was the headquarters of the largest fire service in the State serving one million people, that it was a Victorian facility unsuitable for modern requirements and standards, and that staff and unions were threatening to withdraw from working in the station.
- It was not possible, however, to give Dublin Corporation a commitment that the normal 100% Exchequer grant assistance would be provided because of the scale and cost of the project, the limited funding available for the fire services capital programme and the competing demands throughout the country. Dublin Corporation, accordingly, decided to utilise the site's designated area status under the Urban Renewal Scheme to achieve the twifold objective of having a new Fire Brigade Headquarters constructed while, at the same time, securing development on the surplus lands which had been derelict for many years.
- Against this background, Dublin Corporation decided to enter into a joint venture (Public Private Partnership) for redevelopment of the site to include the provision of a new fire brigade headquarters. The fire station was not a separate contract but part of an overall contract involving the development of the whole site, including an hotel and car park.
- The contract was advertised and awarded on a design and construct basis and the Department's procedures do not cater for this type of development. The Department was not included in the development of the fire station element of the project, as the project was not progressed in line with departmental financial and administrative procedures.



- In response to a request from Dublin Corporation in 1998, and as the original decision was considered to be somewhat harsh, the position was reviewed in the light of the different circumstances which then prevailed (the explicit support in Partnership 2000 for the concept of Public/Private Partnership) and a once off contribution of £1m was provided by way of Exchequer grant. As a high quality full-time headquarters fire station was being provided, this represented excellent value for money insofar as the Department was concerned.

## **24. Cost Overruns on Water Supply and Sewerage Schemes**

Capital expenditure on water supply and sanitation schemes by the Department of Environment and Local Government amounted to £185m in 1998. Estimated expenditure on such schemes in 1999 is projected to increase by 50% to £275m. Projects approved by the Department to commence construction in 1998 range in value from £20,000 for the Athlone Water Conservation scheme to £200m for the Dublin Bay (Ringsend) Sewerage scheme, which will be financed over a number of years to completion.

The guidelines on awarding contracts for public sector construction projects stipulate that, in order to avoid increased costs later, every effort should be made to ensure that all aspects of the design are finalised before a project goes to tender. Upper cost and work limits should be established at the outset and a detailed design brief should be prepared. The design brief should be sufficiently comprehensive to establish clearly the services required and the relevant standards and constraints to be followed. Proper supervision is essential at construction stage to ensure that the works are being carried out according to the specifications and within the time and cost limits for the contracts and the project should be subject to a detailed cost review at completion.

A final account is transmitted by the Local Authority to the Department, which retains 5% of the scheme grant pending its submission.

Despite the existence of strict approval, reporting and budgetary control procedures designed to ensure adherence to the above guidelines at local and departmental level, it was noted on audit in previous years that cost overruns occurred consistently on water and sanitation projects. My 1995 Value for Money Report on Regional Development Measures indicated that, generally, cost estimations at the preliminary report stage differed substantially from design stage costing, which in turn tended to increase at the tendering stage. In some cases, cost at design stage became irrelevant because the schemes were delayed for considerable periods of time. In general, final costs of projects were in excess of the agreed contract costings and the excess arose as a result of adverse ground conditions not identified during site investigations, the introduction of additional cost classifications and substantial increases in salary, administration and miscellaneous costs.

In 1998, in response to an inquiry from my Office, the Department provided information on certain water and sanitation projects which indicated that the tendency for a cost drift to occur between tender and completion stages was continuing, as outlined in the examples in Table 4.



*Table 4 - Water and Sewerage Schemes*

Scheme	Contract Price £	Final Cost £
Bailieboro Sewerage	839,768	1,075,718
Annagry Sewerage (Donegal)	495,000	644,629
Dunlaoghaire Water Supply Contract No.1	6,200,000	7,138,699
Dingle Sewerage	3,705,402	5,693,516
Killybegs Water Supply Contracts	10,900,000	17,695,950
Tralee Sewerage Contract No. 1	2,900,000	4,126,889

The Department indicated that the factors giving rise to these costs variations were the same as those outlined in my 1995 Value for Money report and that final accounts and material required to complete examination of the final accounts, such as construction drawings, engineers' reports, *etc.* are still, typically, received no earlier than 2 to 3 years after substantial completion of a scheme, with longer delays frequently occurring. As a result, few final accounts are received and fewer final payments are made each year on completed schemes.

It was also noted that revised project monitoring arrangements introduced in 1998 include, *inter alia*, a requirement for Local Authorities to seek an increase in the approved grant from the Department at the time the projected cost overrun is identified, rather than when the approved grant is exhausted, as had happened previously. New arrangements on final accounts in early 1999 provided for the introduction of an interim final report, giving an initial assessment of the project and a preliminary statement of final costs, to be followed not more than two years later by the final report which should include a full post-project review and the complete final account. The Department also introduced design and build contracts for suitable projects in early 1999 as one of the main fundamental principles of infrastructure development under Public Private Partnership arrangements. The monitoring, payment and reporting procedures would remain broadly similar to those in current use.

Due to the substantial increase in final costs, I inquired as to whether the Department had conducted any further review of the factors giving rise to the cost overruns. I also inquired as to whether cost overruns on EU co-financed schemes were borne solely by the State or co-funded by the EU.

The Accounting Officer stated that the type of factors that led to cost variations were:

- Uncharted and poorly mapped services causing delays and disruption
- Road structures in poor condition when trenches were excavated, and requiring additional work
- In some cases, better but more costly technology becoming available during the contract
- New requirements of other authorities being made known during the contract
- Delays caused by difficult ground conditions not identified by initial survey
- Difficulties negotiating wayleave agreements



- Delays arising on associated contracts
- Changes such as adjusted Value Added Tax rates.

He also stated that, in recognition of, and in response to, the factors influencing the cost of a scheme over its lifetime, the Department had taken steps to minimise their effects as follows:

*Measures taken by Department prior to Tender Stage*

- Current practice is that schemes are not approved to proceed to planning stage unless the Department is confident that the funding is in place to allow the schemes to progress through to construction in the short term. The Accounting Officer informed me that since 1997, the Department has published the list of schemes to advance through planning with the result that the time between completion of preliminary report and commencement of construction has been shortened.
- Since March 1997, the Department requires Local Authorities to give advance notice to the Department of the Marine and Natural Resources of proposed water services schemes.

*Measures taken by Department during Post Tender Stage*

- In June 1995, Local Authorities were asked to revise scheme costs as part of the Annual Capital Returns process and to submit a report to enable approved finance for the scheme to be reviewed. The report must outline the current scheme cost and itemise the elements giving rise to increases such as price variation clauses, certified claims, overruns and/ or approved extras. It should also incorporate a detailed statement from the County/ City Engineer on the scheme. In addition, it has been emphasised to Local Authorities that it is important that the information in claim forms is carefully checked and verified before they are passed to the Department for payment.
- Local authorities have been reminded of the need to institute value for money and cost control regimes. In particular, rigorous value engineering methodologies are applied to the larger schemes.
- A Steering Group, made up of Local Authority representatives, departmental technical and administrative personnel and the Consulting Engineers, to facilitate regular exchanges of information and early signalling of problems, must be established in respect of each project.
- Local authorities have been reminded of their responsibilities and obligations as contracting authorities to ensure that adequate site supervision, cost control and project management techniques are in place for all schemes. The Department must be notified immediately of likely increases in scheme costs and the factors giving rise to such increases must be fully documented. Local Authorities are generally required to apply for prior written approval before any commitment is entered into. Applications of this nature must also clearly state why the works were excluded from the original scope of the scheme.
- The Department has adopted a policy of limiting the Contingency Sum in contracts to a maximum of 2.5%.
- The Department issued a circular to Local Authorities in December 1997 dealing with the issue



of sound financial management and control systems on water and sewerage schemes. In particular, guidance was given on:

- recording of Local Authority capital expenditure
  - maintenance of scheme documentation
  - categories of eligible expenditure
  - Local Authority inspections of schemes
  - quarterly monitoring returns
  - preparation of audits
  - Local Authority audits and assessment of control systems
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- The introduction of the new administrative arrangements were notified to Local Authorities in December 1998 and, with effect from January 1999, the Department gave Local Authorities more direct responsibility, within approved cost limits, for the management of Water Service projects.
  - A Working Group has been established with representatives of the Department and the Department of Arts, Heritage, Gaeltacht and the Islands to deal with archaeological issues arising.
  - New arrangements have been put in place to ensure that site investigation works are carried out by specialist firms. In addition, Consulting Engineers are being asked to report to the Local Authority and the Department on the effectiveness of the site investigation contract where claims for extra cost due to ground conditions arise.
  - The Department has put in place a system whereby baseline costs for projects are established with a view to determining at final account stage the real increase in costs over tender prices.
  - The Department monitors the competitiveness of the sector by keeping track of the number of contractors bidding, and delays in start-up of jobs.
  - In February 1999, the Department set out revised procedures for carrying out post-project reviews for water services projects. The main objectives of the new arrangements are:
    - To provide an assessment of the management of the project
    - To allow for a full evaluation of the impact and effectiveness of the project, particularly in terms of the environmental and economic objectives set
    - To ensure that information is collected in a manner that facilitates the conduct of financial audits and the aggregation of national statistics
    - To meet the various requirements of the EU in relation to the draw down of EU aid
    - To determine the final outturn cost, and identify any cost increases over the original estimates and tender prices
    - To identify, explain and, if possible, correct any irregularities in the management of the project and recover any financial losses arising from identified financial irregularities
    - To ensure that the appropriate maintenance of the works in question and for the ongoing monitoring of their performance have been put in place
  - The Department is implementing a standard accounts system for the monitoring of expenditure on water services capital projects.



The Accounting Officer also stated that the Department had recently engaged a consultant to undertake an audit programme of interim certificates issued by consulting engineers to establish that these certificates reasonably reflect the value and efficiency of the work covered by them.

With regard to the funding impact of cost overruns in EU co-financed schemes, the Accounting Officer stated that there is no obligation on the European Commission to increase the maximum amount of assistance from the Cohesion Fund, the source of the majority of funding for such schemes. Nevertheless, he stated that, up to April 1997, in practice the Commission has approved most cost increases on individual projects but that since then has tended to disallow cost increases on water projects. The reason for doing so is stated to be due to Ireland's interpretation of Article 130 of the Treaty on European Union, *i.e.* the Polluter Pays Principle. Since that time also they have approved new water projects for funding at the lower aid rate of 80% (compared to a usual 85%) for the same reason.

In relation to a minority of schemes that benefit from Structural Funds and Interreg Funds, the Accounting Officer stated that the Exchequer bears any cost increases. However, he pointed out that no EU aid is lost to Ireland in this respect in view of the availability of schemes to be set against Structural Funds. In the absence of EU assistance, such schemes would be funded by the Exchequer in any event.