Vetting Prior to Procurement

We have agreed that the purpose of the special August meeting of the audit committee would be to appraise the vetting procedures and methods used in order to identify any weaknesses and propose potential improvements. That said, we cannot ignore the fact that there have been two significant apparent failures – Dawnus and Jistcourt. In both cases we do not know if it was a failure or shortcoming of the system used or of the data inputted into it. As you know we have already put some questions to officers specific to the Dawnus failure but the answers received raise further questions, (I have attached a copy of their response for your convenience). Putting these together with further questions arising from the Jistcourt situation, I think the meeting should explore the following and I think it would be fair and constructive to give the service advance notice of our challenge.

- Dawnus

  The vetting for Dawnus commenced in Feb 2018 prior to awarding the stage 1 contract for Bro Hyddgen school. The work was completed in February, report produced at the end of March and contract awarded in April. That assessment was made using the Dawnus Construction Holdings accounts for 2015 & 2016. There would have been no reason to reject the tender using that data. The response states that rumours about Dawnus viability reached the council in or just prior to July 2018 *'at this point the group accounts for 2017 and construction accounts for 2017 were requested and assessed to add to the 2016 assessment carried out previously.'*

  The 2017 accounts reflect the fact that at the end of that year Dawnus had involved consultants, its banks and the Welsh Government to advise and assist in their cash flow problems. Those accounts show a bank balance of zero, creditors at £52m (some 24 weeks of cost of sales) and an apparently liquid position maintained by an equally massive £58m of debtors – much of which a recent report from the administrator appears to have been overvalued. We will need to establish:

    - How the spreadsheet dealt with the extra year (2017) - the response states that it was 'included'.
    - Why such dismal figures when taken in isolation were apparently mitigated by the Q1 results requested and submitted also in July, there were, after all, rumours which should have prompted extra vigilance. We need to see those figures before the meeting, not the least because the bank and WG loans were made in that quarter.
    - By what criteria, to quote the 26th March report from the portfolioholder, did the assessment of the 2017 and 2018 (Q1) accounts show 'good financial health with just a small reduction in the maximum contract value'.
    - The Chattels mortgage taken out in 2017 was relatively small, however, the security for the March 2018 loans at some £7m were significant and should have been declared. I have not yet had a response on the issue of obligatory disclosure clauses.

- Jistcourt

  There is very little information available on Jistcourt. The latest accounts registered at Companies House is for the year ending 30th June 2017. The accounts for the 2018 year are overdue. However, the records do show that two secured loans were taken out by the company one in 2016 from Finance Wales and another from the Development Bank of

Wales in September 2018. The latter was at 9% presumably recognising the high risk to the loan. In a section of the directors report titled 'Going Concern' various current liabilities were discussed totalling £1.6m, the relevant paragraph ends:

> *The majority shareholder has provided a letter of support confirming that they will, if necessary, waive further repayments and/or support to the Group to assist the working capital of the Group for a period of no less than 12 months from the date of signing of these accounts.*

That period would have ended in March 2019. On that basis the directors felt able to adopt the going concern basis in preparing the financial statements.

Also shown is the resignation of the finance director and contracts director replaced, it would appear by family members. Also, somewhat curiously the financial year was shortened from the 30th June to 29th June! We therefore need, preferably before the meeting:

- an account of the data received for Jistcourt similar to that supplied for Dawnus.
- The circumstances surrounding the award of the contract without the bond being in place.

- General

I am totally mystified that investigation of Companies House records which include details of accounts, charges and directors is not an integral part of the due diligence vetting process. The last paragraph of the Dawnus note give me particular concern:

The Council did not have a tracker on Dawnus via companies house. In February 2018 and July 2018 we have appraised their accounts and there was not a significant concern which would lead us to place a tracker on the company. The Council understood also that Welsh Government were financially supporting the company though we were not aware what form that was.

In July 2018 officers had heard rumours of financial problems, also they were aware of the WG support, surely, in those circumstances, every information channel should be explored.

We shall also have to understand:

- The calculations made by the spreadsheet tool in order to assess its limitations since, on the face of it, some rather curious results have emerged particularly in the case of Dawnus. In particular, how the maximum contract value is calculated.
- The role of the SEWSCAP2 framework manager and why, given his responsibility to ensure that contractors continue to meet framework standards, no warnings were apparently received.
- The timing and scope of the Constructionline investigation.

Your comments, additions/deletions would be appreciated.

John