

CYNGOR SIR POWYS COUNTY COUNCIL

AUDIT COMMITTEE

7th August 2019

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**SUBJECT: Undertaking Economic and Financial Standing (EFS)
Procedures in Procurement**

REPORT FOR: Information

1 Purpose

- 1.1 The purpose of this report is to provide additional details to Audit Committee of the Economic and Financial Standing Assessments that were undertaken for Dawnus Ltd and Jistcourt Ltd which led to the awards of contracts for schools and Housing projects for the Council

2 Introduction

- 2.1 The reports seeks to show how the EFS procedures are undertaken in general together some specific elements related to the construction projects for schools and housing and also some shortcomings of any process applied to these assessments. Responses have also been provided at the end of the report have been provided to the specific questions raised by Audit Committee (Appendix 1) .

3 Economic and Financial Standing Assessments

- 3.1 Economic and Financial standing assessments as a principle is a process to a assess bidder's ability and capacity to undertake a contract alongside other criteria obtained as part of any procurement.
- 3.2 The criteria and information we assess against has to be specified upfront in any process and the Council will be unable to change or vary the criteria once bids or prequalification data is received. The questions asked and the evaluation criteria from recent tenders are included as Appendix 4
- 3.3 All assessments of bidders must be fair, proportionate, contract specific, flexible and not be overly risk averse whilst ensuring protection of public money and compliance with procurement law. The assessment should also avoid discrimination of small and medium enterprises.
- 3.4 The assessment is considered as part of the overall selection criteria. It may not on its own reflect a bidder's ability to deliver and other criteria should be considered including references from other clients, value of contracts currently undertaken, track

record and the type of organisations bidding (e.g whether part of a wider group of companies)

- 3.5 The public announcement of a change in circumstances may also be relevant for consideration. For instance in the case of Jistcourt Ltd, in May this year they announced that they were opening an office in Bristol because of their expansion plans which if considered alongside the specified assessment would give a more rounded picture of the current operation and direction of the company
- 3.6 The assessment is carried out for any major or high risk contracts by the Council by its financial team utilising criteria they have provided and have published in tender or prequalification documentation and this may also require companies to produce further information to support their accounts.
- 3.7 The set criteria have been utilised on many occasions and for many of Powys's contracts.
- 3.8 The EFS process is recognised to have some shortcomings. For example, information on a bidder's profitability, cash flow, liquidity and solvency and therefore its EFS and capacity can change. Financial assessments are also dependant on backward facing information which even in a period of downturn can subsequently (and quickly) improve or deteriorate without any client visibility and is very difficult to monitor until subsequent published information is available. The recommendations below are some consideration which may be possible to implement for any future high risk project.
- 3.9 Prequalification processes are undertaken for any procurement before tenders are issued or alongside or at the same time as a tender process. The prequalification envelope includes mandatory criteria (such as criminal offences, fraud etc) which are pass fail type criteria, technical and capability criteria and financial criteria including insurances and financial standing of the companies concerned. If a company fails on any mandatory question or fails on the financial then the companies will not be invited to the second stage unless further mitigation is provided. This was not the case for either Dawnus or Jistcourt at the time of assessments.
- 3.10 The process applied are in accordance with usual prequalification processes and in accordance with Welsh Government supplier qualification questions (SQUID) guidance used by many other public sector buying organisations in Wales.
- 3.11 The SEWSCAP framework which operated on behalf of 15 local authorities in Wales and provides a flexible framework for appointment of school contractors according to the value of each school. It provides for a speedy means of engaging contractors in accordance with our specific requirements and important contractual terms and conditions, some elements of pricing added value and community benefits have already been agreed. The way the SEWSCAP2 framework operated for financial vetting was that the financial checks were undertaken when appointments were first made to the framework but local authorities were expected to undertake their own due diligence/ prequalification at the point of any subsequent mini-competition for a project build. This has and was undertaken by Powys Council and because the procurement and construction process were two stage for Schools (stage 1 design development and costing, stage 2 Construction) the due diligence undertaken again before the construction element of the contract was commenced and after design had been undertaken. There was some anecdotal and rumour that there were issues at Dawnus but no information available publicly and the SEWSCAP team were also unaware of any difficulties.

3.12 The full financial assessment was also carried out for the Bowling Green Contract

3.13 Performance Bonds are a useful tool and obtained at contract award for an agreed percentage of the total contract, They provide some compensation if the supplier proven to have defaulted and some incentive for suppliers to ensure they carryout the contract efficiently and on time and an additional incentive on the supplier to perform well. However they are not obtained until contracts have been awarded and required within 7 to 14 days of award. The Bond market however in some case is requiring contractors to demonstrate a competed construction contract before providing the bond

4 Considerations and Recommendations

4.1 A new Policy Guidance Note has been issued by the government 'Assessing the Economic and Financial Standing of Suppliers' (Appendix 2) which will be used to review current practice and approach for the Council

4.2 As a result of the experiences in these two incidents the Council will be considering whether to include ongoing monitoring processes for all of its major or high risk contracts. This is not currently undertaken at present and requires access to forward information and predictions if available as well as ongoing published result as anniversary of publications occur. This is most likely best delivered via and electronic portal via a specialist provider such as Dunn and Bradstreet or Equifax.

4.3 Finance and Commercial Services are currently reviewing whether any market and company health analytic companies or providers who are able to electronically monitor changes or financial distress events, can provide these services to the Council. and provide alerts to the Council so that it can make decisions or put in place appropriate mitigation.

4.4 The Council will be considering whether it can include terms in its contract which may require providers to provide annual confirmation of compliance and notify the Council of any defined changes classed as financial distress factors (which would need to be specified) and consideration of the use of other tools and sureties to provide assurances to the Council on the financial health of all of its key suppliers.

5 The Council may also need to review it procurement documentation to ensure that any changes to the approaches are incorporated into pass/ fail mechanisms within documentation.

Recommendation:	Reason for Recommendation:
That Audit Committee notes the contents of the report.	To review the process for Economic and Financial Standing Assessment to provide the necessary assurance that new providers and current strategic/major suppliers have the financial Health to deliver its services and projects

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Responses to the Specific Questions Raised

Question 1

- *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 portfolio holder, 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.*

Response

Further response will be tabled prior to or at the Audit Committee

Question 2

- *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 tender process required bidders to be Constructionline registered with assessed work categories and category notation values relevant to the value of the contract. The Council reserved the right to request company accounts and to carry out a credit check and further financial analysis.

Jistcourt passed the requirement for both Constructionline work categories and notation values in excess of that required for the contract. As final due diligence prior to award, the Council requested their latest audited full accounts for year ending June 2018. The bidder was unable to provide audited accounts at this time due to the accounts being with the auditors, but were able to provide unaudited accounts. The resulting financial assessment of the 2 years worth of information available from these accounts resulted in the following assessment:

Financial Health - Strong
Risk of Failure – Higher than average risk
Maximum Contract Amount - £4.1 million

Following this assessment meetings advice was sought from senior managers on whether or not to proceed with the award of the contract. Following discussions, the award was agreed based on the following:

- The project was being ran under the Welsh Government's Innovative Housing Programme. The

Bowling Green had been designed on this basis and had a grant award of approximately £2 million. The grant terms stated that award was on the basis of entering into contract by the end of March 2019. Not awarding to the contractor would have meant losing this award, and potentially jeopardising the viability of the scheme.

- Unlike the contracts with Dawnus, where the contractor had been responsible for the initial designs, as well as construction, on the Bowling Green the designs had been developed by architects commissioned by the Council. It was seen that in the case of the contractor going into insolvency, it would be a more simple process to appoint a contractor to complete the construction of the building.
- The contract included for a performance bond of 10% of the total build cost, valued at £3.5 million. This was seen to give adequate protection to the Council in the event of the contractor going into administration.
- The contractor would be requested to put a Project Bank Account in place to give protection to local subcontractors in the event of the contractor becoming insolvent.

On the basis of the above points, senior managers agreed to proceed with the award of the contract to Jistcourt (South Wales) Ltd.

Question 3

The circumstances surrounding the award of the contract without the bond being in place.

The Employers Requirements documents stated a requirement for a Bond of 10% of total contract value. It was very clear in the documentation that a Bond was expected to be put in place with the contract award, during the 12-week lead in period to commencement. Contractors are unable to obtain a bond until after a contract is awarded and in some cases until the Construction contract has been completed. There was a dependency on awarding the contract, securing the site and make a meaningful start on site to secure a £2million grant from Welsh Government. Following award the Contractor did not produce the Bond and was in breach of its obligations. They were continuing to assure the Council that the Bond would be put in place. They were aware that they could not submit any Applications for Payment until the Bond was provided. No Applications were received by the Council and no payments were made.

Question 4

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.

Question 5

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.

Please see Appendix to follow

Question 6

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.

Was it SEWSCAP's responsibility to do ongoing checks?

The framework managers undertake these checks at the point of appointment of the companies to the framework. For the SEWSCAP2 Framework. Authorities are advised to undertake their own due diligence and prequalification checks at the time of undertaking a mini competitions for a specific project. This was undertaken for Dawnus in accordance with previous information.

However we understand that under the new SEWSCAP3 the Framework Management will be providing this service and have the facility to undertake annual checks with 6 monthly checks on management accounts.

Question 7

The timing and scope of the Constructionline investigation.

Carried out during the evaluation process, as part of the Qualification Assessment as a pass/fail.

The scope includes the Work Categories and Category Notation Values relevant to that which the contractors are being assessed against. For example, building schools and colleges, social housing. The Notation Values are calculated by looking at a contractor's financial ability and established track record for successfully delivering contracts in each work category to a certain value. This brings together the last reported annual turnover, net assets, and the average value of references obtained.

ASSESSING AND MONITORING THE ECONOMIC AND FINANCIAL STANDING OF
SUPPLIERS - Government Policy Paper

**FINANCIAL AND ECONOMIC INFORMATION REQUESTED AT PREQUALIFICATION
AND TENDER STAGE AND EVALIATION PROCESS**

APPENDIX 4

**REVIEW INFORMATION OF JISTCOURT FINANCIAL STANDING (*COMMERCIALY
CONFIDENTIAL INFORMATION REDACTED*)**