

Audit Committee (virtual meetings to commence from June 2020 due to Coronavirus)

Thursday 28 January 2021
10.00 am Virtual meeting



SUPPLEMENT TO THE AGENDA

To: The Members of the Audit Committee (virtual meetings to commence from June 2020 due to Coronavirus)

We are now able to enclose the following information which was unavailable when the agenda was published:

Item 7	SWAP non-opinion audit – Highway Maintenance: Duplicate Payment Requests (Pages 3 - 12) To consider this report.
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Somerset County Council
 Audit Committee 28 January 2021

SWAP non-opinion audit – Highway Maintenance: Duplicate Payment Requests

Cabinet Member(s): Cllr John Woodman – Cabinet Member for Highways and Transport

Lead Officer: Alyn Jones, Director of Economic and Community Infrastructure Operations

Author: Andrew Turner, Strategic Manager – Highways

<p>Summary</p>	<p>In recognition of a number of issues around the Application for Payment (AfP) process, and specifically the risk of duplicate payment requests which had been identified through the certification process, SWAP was commissioned by the Highways Strategic Manager in May 2020 with the objective to:</p> <ul style="list-style-type: none"> a) Establish the extent of duplicate payments applied for across the three-year contract period, through analysis of submitted AfP's; and b) Assess the extent to which both the internal and contractor processes are sufficiently robust to mitigate the risk of both duplicate payments being applied for and paid. <p>The non-opinion audit outcome identified seven key recommendations where changes were required to provide full assurance.</p> <p>This report sets out:</p> <ul style="list-style-type: none"> • the findings relating to the areas of concern raised by SWAP; and • provides assurance to the Audit Committee that the actions have been accepted and currently being addressed with timescales for resolution. <p>Follow-up audit(s) are planned for 2021 / 2022.</p>
<p>Background</p>	<p>Somerset County Council (SCC) awarded the Highways Maintenance Contract to Skanska Construction UK Ltd and the contract commenced in April 2017. It is valued at approximately £30m each year.</p> <p>Skanska submit a monthly AfP for all task orders relating</p>

	<p>to highways maintenance. A review of the AfP process was conducted by the Highways Service area for internal compliance in early 2020 and this highlighted two incidents amounting to £361k in value where Skanska had failed to accurately assess the previous paid sum prior to applying for payment. This triggered an Early Warning Notice to Skanska in which three critical questions were posed, to gain a better understanding of the process:</p> <ul style="list-style-type: none"> • What checks are currently being undertaken to prevent potential duplications reoccurring? • How did these duplications happen to slip through the current quality assurance processes already in place? • What improvements can be made to the current checks and balances to ensure that these occurrences are kept to an absolute minimum? <p>It transpired that Skanska had not undertaken checks for the full term of the contract. Discussions around this and the questions above informed the instruction to SWAP to undertake an audit.</p> <p>SWAP was commissioned by the Highways Strategic Manager in May 2020 with the objective to:</p> <ol style="list-style-type: none"> a) Establish the extent of duplicate payments applied for across the three-year contract period, through analysis of submitted AfP's; and b) Assess the extent to which both the internal and contractor processes are sufficiently robust to mitigate the risk of both duplicate payments being applied for and paid. <p>The approach adopted by SWAP was a Risk Based Internal Auditing (RBIA) which is recognised as best practice. A preliminary assessment of the risks relevant to the activity under review was completed as part of the initial planning process and engagement objectives reflect the results of this assessment. SWAP considered the probability of significant errors, fraud, non-compliance and other exposures when developing the engagement objectives.</p>
<p>SWAP audit conclusion</p>	<p>The SWAP audit report dated 2 October 2020 concluded Skanska's submitted AfP confirmed a significant number of duplicate payment requests made across the three-year contract period. Importantly though, SWAP identified</p>

	<p>these duplicate instances were in fact re-applied requests for payments that have previously been refused through the certification process.</p> <p>Due to data quality and visibility issues, it was not possible to confirm that there have not been any duplicate payments made in error. However, the audit itself did not identify any duplicate payments were made. Clearly there is further work in this area to gain further assurance and this is planned alongside the review and implementation of finding recommendations contained within the audit report</p> <p>SWAP established several complex root cause issues that relate to both operational process and the AfP certification process, which have given rise to the situation of repeat payment requests being submitted by the contractor.</p> <p>The most significant issue is a high differential between the ordered cost of works, compared to the actual cost applied for. There are further process and system issues, which are causing the amount of data within the AfP to be unnecessarily inflated, and therefore the certification process is less than efficient or effective. These combined issues increase the likelihood that a duplicate payment request could be overlooked and approved in error.</p> <p>SWAP also assessed the extent to which payment request and certification processes are sufficiently robust to mitigate the risk of duplicate payments being erroneously applied for and paid. This identified that whilst Skanska has recently implemented enhanced controls, the Highway Service is yet to secure approval for the required improvements on their side to be funded and priority action is needed. This will continue to be addressed through the Medium Term Financial Planning (MTFP) process.</p> <p>The requirements of the certification process are also beyond the capabilities of the current spreadsheet and a module added to the highway system would provide a better framework for such a high volume and complex process.</p>
Review activity and	Due to the significant value of highway maintenance

outcomes

payments and the lack of assurance that public funds can be effectively safeguarded via the current processes in place, SWAP made a series of recommendations to address the root causes.

Please note, the priorities set against the findings are:

Priority 1 - Findings that are fundamental to the integrity of the service's business processes and require the immediate attention of management.

Priority 2 - Important findings that need to be resolved by management.

Priority 3 - Finding that requires attention.

Finding 1 - There are high differentials between the ordered and actual costs in the Application for Payment.

Recommendations (Priority Score 1)

SWAP recommend that the Strategic Manager – Highways should:

- introduce a differential threshold above which, a variation order must be raised;
- introduce a requirement for accurate cost accounting, to address the issue of orders being raised for nominal £1 values;
- assess and address knowledge and skills gaps across operational staff teams. The outcome should be to ensure that all officers raising task orders apply the same interpretation of safety defect work measurements and the price list; and
- consider the optimum level of resource required to address these issues and seek to increase it where required.

Agreed Action

- Senior Quantity Surveyor (SQS) to review use of arbitrary figures used to raise Task Orders as part of process review. The intention to put an immediate cessation on procuring works of this nature. (General agreement that this cannot continue for budget management purposes);
- Skanska will need to be engaged on the process review, SQS to review how we address this with

Skanska; and

- Strategic Manager – Highways to review knowledge and skills gaps across Operations and consider optimum level of required resources.

Timescale

31 March 2021 (with implementation from 1 April 2021)

Finding 2 - Other issues with the cost visibility of orders in the Application for Payment may impact on the number of task orders refused for payment and re-applied for by the contractor.

Recommendations (Priority Score 1)

SWAP recommend that the Strategic Manager – Highways should work with the contractor to agree an improved approach to the use of explanatory comments in the AfP by both the client and the contractor. This action should seek to achieve a 'right first time' approach to certification, which will reduce the number of repeat requests. As part of this action, consideration should be given to introducing a differential threshold, above which comments are mandatory.

Agreed Action

- SQS to review use of explanatory/mandatory notes as part of the process review. (Acceptance there is a lack of commentary from SCC and Skanska on the cost differentials).
- Skanska will need to be engaged on the process review as this is likely to result in an amended / agreed process with Skanska.

Timescale

31 March 2021 (with implementation from 1 April 2021)

Finding 3 - The amount and scope of routine auditing of highway task orders is not commensurate with the total value of expenditure, or the financial risks associated with the outsourced maintenance contract.

Recommendation (Priority Score 2)

SWAP recommend the Strategic Manager – Highways

should seek to resource an increased amount and scope of routine auditing of task orders completed by the contractor, to confirm both the quality of works and the correct application of the price list. The approach to auditing should be reviewed to ensure that certifiers and contract auditors target the areas of highest financial risk.

Agreed Action

The Strategic Manager- Highways has developed a Contract Management Business Case indicating the requirement for more resource (this is currently subject to a revenue pressure bid and currently awaits financial approval through the MTFP process).

There is also a need for task order commissioners to undertake their own audit for payment purpose and record as such (this will be a process issue that will need to be factored in issues above).

Current audit activities to be re-focused on value and risk.

Timescale

January 2021 (following Full Council decision).

Finding 4 - The size and format of the Application for Payment exceeds the capabilities available from a spreadsheet and does not enable the certification process to achieve compliance with Financial Regulations. There is also a lack of cost visibility for certifiers.

Recommendations (Priority Score 1)

SWAP recommend the Strategic Manager – Highways should explore options for improving the architecture of the Application for Payment through either adoption of a highways system payment module, or a database to replace the current spreadsheet format.

Agreed Action

- SQS to review current support systems activity. Confirm on Demand appears to provide an opportunity to explore further.
- SQS to review the long-term aspirations of the AfP

review with a view to ensure the IT systems are aligned to support.

Timescale

31 March 2021 (with implementation from 1 April 2021)

Finding 5 - There is a lack of cohesion between the processes of the authority and the contractor that impact on the data quality of the Application for Payment.

Recommendation (Priority Score 2)

SWAP recommend the Strategic Manager – Highways should explore options with the highways system provider for streamlining system functionality that will remove differences between authority and contractor processes in respect of allocating task orders to specific parts of the highway.

Agreed Action

- Significance of Link & Sections to be reviewed to determine usage requirements and potential for streamlining system functionality.

Timescale

31 March 2021 (with implementation from 1 April 2021)

Finding 6 - The authority's highway maintenance payment reconciliation process does not include sufficient data to be effective.

Recommendation (Priority Score 2)

SWAP recommend the Strategic Manager – Highways should explore options for expanding the reconciliation process beyond the three-month dataset currently used.

Agreed Action

- SQS to review quarterly reconciliation process currently undertaken by Business Support Team; and
- SQS to discuss potential development of improved SCC reconciliation process.

Timescale

	<p>31 March 2021 (with implementation from 1 April 2021)</p> <p>Finding 7 - The Application for Payment process does not have a realistic completion timescale given the complexity of the certification process.</p> <p><u>Recommendation</u> (Priority Score 3) SWAP recommend the Strategic Manager – Highways should review the role of the Commercial & Procurement team in the Application for Payment process, to establish any benefits achieved through involvement and whether the Highways Operations team should assume responsibility for distributing the AfP.</p> <p><u>Agreed Action</u> This is to be reviewed as part of the review and implementation of the Contract Management Team (which is now subject to a Business Case and revenue pressure bid).</p> <p><u>Timescale</u> 31 March 2021 (with implementation from 1 April 2021)</p>
Actions to date	<p>The Strategic Manager – Highways commenced an internal service area review in response to the SWAP recommendations. This will be managed with representation from ECI Operations, Commercial and Procurement and Finance. It is noted that some early interventions have been achieved already, for example, removing notional low value task orders.</p> <p>Given that Skanska will be part of the solution, a separate work stream has been initiated with them to look at the end-to-end payment process; with specific inputs and focus on the SWAP recommendations. (It is noted that an abridged version of the full SWAP report has been shared with Skanska).</p>
Recommendations	<p>It is recommended that the Committee accepts the outcomes of the non-opinion audit and are assured that:</p> <ul style="list-style-type: none"> • the Highways Group is committed to fulfilling the agreed actions resulting from the findings; • The target completion for the majority of the findings is

	<p>by 31 March 2021 (with implementation from 1 April 2021); and</p> <ul style="list-style-type: none">• A follow up audit is planned in 2021 / 2022 and the Audit Committee will be updated as required.
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