

**AUDIT COMMITTEE  
THURSDAY, 24 OCTOBER 2013**

**ITEM 4 – PUBLIC QUESTION TIME**

**Note**

The time allowed for questions shall be limited to 30 minutes or a maximum of 20 questions, whichever occurs first.

The questioner at the meeting may ask one supplementary question to the original question, which will be answered without discussion.

**Ms Theresa Musgrove**

Can the Chairman offer me assurance, limited or otherwise, that the risks posed by the following financial transactions were properly assessed and authorised, and if not, will he ask the External Auditors to investigate the matter?

1. The council has paid Capita £14.7 million for an interim contract of which only £0.7m was spent, while £14 million is still awaiting refund to the council. Why has this 'interim' payment not been returned? Will we receive interest accrued during the delay?

**Response**

Of the money unspent in respect of the interim service agreement (ISA), some of this was offset against the capital payment, some of this is offset against on-going service charges, and £4.1m was returned to the Council on 20th October. The response to Contract OSC is provided below. The £4.1m was returned to the Council following a detailed reconciliation of amounts spent under the ISA in September. No interest payments are due to the Council.

2. Was there a risk assessment made before the council agreed to borrow £16 million to fund investment in the Capita contract, and why was this sanctioned when no such action had been mentioned before the contract was awarded? Is this lawful, and did the authority take legal advice before agreeing such a loan?

**Response**

The Council has not taken a loan out to fund this investment; this payment has been made from the Council's cash balances. However, the Council received legal and accounting advice throughout the procurement process, and can confirm that making payments for services provided under the CSG contract is legal.

3. At last week's Contract Monitoring Committee, the Capita Partnership Director in Barnet initially explained to Cllr Khatri that the £30 million given to Capita were 'interim' payments. Members of the public who were present disputed this, and he deferred to a Barnet officer, who would not respond, and said she would speak to the councillor out of the meeting. Does the Chair agree that such a lack of clarity over these enormous amounts of taxpayers' money is unacceptable, and in the interests of transparency, and accountability, can he confirm the details of any response given to Councillor Khatri?

## Response

The Head of Commercial has provided a detailed response to Councillor Khatri and the members of the Contract Monitoring Committee Overview & Scrutiny Committee on this matter and is replicated below in question 4.

4. Clearly such generosity has saved Capita a substantial amount of money by avoiding the payment of interest rates, but how does this represent good value for money for the taxpayers of Barnet? Does our External Auditor take a view on the probity of such a use of our money?

## Response

From the Council and taxpayers perspective, the payment of capital investment up front represents good value for money. It reduces the funding costs that would otherwise have been charged to the Council under the contract, ensuring that the Council receives the best possible deal. The contract saves the Council £125m over 10 years which is a substantial benefit to the tax payer in a time when government support for local authorities is being reduced substantially. Whilst the assets are owned by Capita, Capita is obligated to provide them back to the council upon contract termination at no further cost, and the assets are recognised in the council's accounts irrespective of how they are funded.

From our external auditor - *we have reviewed the management response and discussed it with the Chief Officers and do not have any concerns at this time. On the wider point of ensuring value for money (vfm) from the Capita contracts we have already agreed with management to incorporate coverage of this in our 2013/14 vfm audit.*

### **Capita Payments – response to Contract OSC:**

By way of context, it is worth setting out the rationale for the payments made to Capita for customer and support services, and associated risks. They are as follows:

- 1. Why did we enter into the interim service agreement?** The reason for this was that, due to the on-going uncertainty of the judicial review, it was becoming impossible to continue to run these services with such a significant level of vacancies and turnover of staff, particularly in customer services and revenues and benefits, and the ISA enabled the Council to increase staffing capacity and resilience. In addition, there were urgent pieces of work that the Council had to undertake, particularly in respect of updating ageing IT infrastructure. Further to this, it was important to undertake work that would enable the Council to realise financial savings. So for example, the project to replace the SAP financial system had to start, because if it is not completed by the middle of 2014, the Council would incur an additional £1.5m of spend with Logica to continue this service for another year.
- 2. Why did the Council fund the £16.1m up front?** The reason for this is that the Council benefits from as low as possible costs of funding investment within the deal. Under accounting guidelines, the assets are recognised in the Council's accounts irrespective of how they are funded, but paying the £16.1m up front reduces the costs of financing.
- 3. Why does the Council pay in advance for the service provision?** Again the reason for this is that this minimises the costs of funding investment within the deal.
- 4. What risk exists in respect of payment in advance?** For the first 6 months of the contract while assets are purchased, if Capita were to go bankrupt, it would owe the Council money for payments made up front (£8m in November, reducing to zero by March 2014). After that point, investment in the services through the contract are in excess of the payments made in advance. Regular financial

assessments have been made, and will continue to be made, on Capita's financial health to mitigate against this risk. This is in accordance with the Council's financial regulations.

In respect of the terms of payment for both contracts, these are contained within schedule 4, which is published on the council's website for CSG (see: [https://www.barnet.gov.uk/downloads/download/1244/schedule\\_4-payment\\_mechanisms](https://www.barnet.gov.uk/downloads/download/1244/schedule_4-payment_mechanisms)) and will be published by the end of the month for RE.

### **Customer and Support Group (CSG)**

The agreement in the CSG contract was that the council would provide **£16.1m** of upfront capital investment as part of a total of **£275m** of payments to Capita over the 10 year term. Ongoing service payments are quarterly in advance, with **£14.1m** due as payments for the first 6 months of service provision. The council agreed to fund the capital costs up front because the council benefits from a lower interest rates which keeps the overall cost of funding CSG as low as possible. The assets are Capita's, but Capita is obligated to provide them back to the council upon contract termination for at no further cost.

However, the delay caused by the application for Judicial Review meant that the council had to take out a separate interim services agreement with Capita in June 2013 to undertake essential work on infrastructure and systems replacement projects, as well as temporary staff cover for various services. This involved an upfront payment of **£14.7m**. The details of this decision can be found here: <http://barnet.moderngov.co.uk/ieDecisionDetails.aspx?ID=4818>

The signing of the CSG contract in August 2013 meant that the interim services agreement (ISA) was terminated and replaced by the CSG agreement, which commenced on 1 September 2013.

Of the total **£14.7m** paid under the ISA:

- **£1m** was paid in respect of services delivered in July and August (interim services for revenues and benefits and customer services, project management, procurement consultancy and management oversight and governance)
- A further **£4.0m** was in respect of mobilisation costs, the IS programme team, insight and wide area network projects. **£2.9m** of this was to have been paid as part of the first advance service payments for the first 6 months of service provision and therefore deductible from the first CSG payments. A further **£1.1m** was to have been paid in future service payments and will be deducted at this point.
- **£5.6m** was paid in respect of upfront capital costs, which was deductible from the larger CSG upfront contract capital contribution
- A rebate of **£4.1m** is now due for amounts paid and not spent under the ISA which has now been received.

That meant that when the CSG contract was signed, **£10.5m** was paid to Capita in respect of the capital contribution (**£16.1m** less the **£5.6m** paid under the ISA), and payments of **£4.1m** and **£7.1m** in respect of the first 6 months of service provision (**£14.1m** was the upfront contractual CSG payment for services, and **£2.9m** already paid under the ISA has been deducted from this).

So in total Capita has been paid **£14.7m**, **£10.5m**, **£4.1m** and **£7.1m** as set out above, totalling **£36.4m**, with **£4.1m** subsequently being repaid to the Council.

### **RE (Development and Regulatory Services)**

I have also set out below the payment structure for the joint venture for development and regulatory services.

The agreement in the Re contract is that the council provides **£1.7m** of upfront capital investment as part of a total of **£150m** of payments to Capita over the 10 year term. Ongoing service payments are quarterly in advance, with **£3.5m** due as payments for the first 3 months of service provision. The council agreed to fund the capital costs up front for the same reason as in the CSG contract and Capita is obligated to provide the assets back to the council upon contract termination at no further cost.

So in total, thus far Capita has been paid **£5.2m** for RE, as set out above.

5. Capita has already required Barnet Council to breach a contract with bailiffs, an action that has led to the threat of legal action against the authority: has the risk of this and similar legal challenges from other contractors displaced by Capita been assessed by the council, and if not, why not?

### Response

Capita has not required Barnet Council to breach a contract with bailiffs. As part of the mobilisation of Customer and Support Group (CSG), a number of contracts have had to novate from the Council to Capita. The only suppliers that have refused to co-operate in the novation process are those bailiff contracts referred to in the question. In this circumstance, the contracts include a novation clause which requires the contractor to novate the contract, so on that basis it is clear that the Council has not breached the contract. The bailiff contract is volume based and non-exclusive, so there is no financial implication to the Council in respect of the inability to novate. Furthermore, Capita have arrangements in place which means that there has been no disruption in service.

### Note

The following questions are not related to an item on the agenda. These questions relate to items best dealt with by either the Executive or Scrutiny Committees. However the responses have been provided. A supplementary question can be asked and will be noted by Governance Officers for response however the Chairman of Audit Committee will not be answering these questions.

6. The new recycling scheme has cost more than £4 million for the purchase of new wheelie bins and food bins. There are now allegations that these new bins are not compliant with regulations that will apply in 2015. Was the risk of non compliance assessed by the authority, and if not, why not?

### Response

For the benefit of the Committee, the question arises due to a recent letter from Lord de Mauley on behalf of Department of Environment, Food and Rural Affairs (DEFRA) on the 15th October 2013 on the separate collection of waste. The letter can be found here:

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/250013/waste-seperate-collection-201310.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/250013/waste-seperate-collection-201310.pdf)

The revised Waste Framework Directive (2008/98/EC) which came into effect from June 2012 requires member states to set up separate requirements for collections of paper, metal, plastic and glass, where separate collection is:

- 1) necessary to provide high quality recyclates, and
- 2) technically, environmentally and economically practicable.

Paper, metal, plastic packaging and glass collected from Barnet households is separated at the Materials Recovery Facility operated by Biffa at Edmonton. We are aware that glass separation can be more problematic than for other materials, however the council's view is that separate collection is not necessary to meet materials quality objectives, and that separate collection is not technically, environmentally and economically practicable for Barnet. By changing from a source separated collection to a comingled (mixed) collection of recycling it is expected that there will be economic savings of £1.2m by 2014/15 and £4.1m by 2016/17. It is expected that a significantly greater tonnage of material will be diverted from costly disposal, to recycling, with the proportion of household waste recycled, composted and reused projected to rise from 33% in 2012/13 to 41% in 2014/15 and 43% in 2016/17. If the previous source separated collection had been continued, these economic savings and environmental performance improvements would not be realised.

A recent judicial review (*UK Recyclate Ltd & Ors R (on the application of) v Secretary of State for Environment, Food and Rural Affairs & Ors*) demonstrated that the most sensible approach, and indeed the most effective approach to mitigating the risk of legal challenge, is to rely directly on the words of the Waste Framework Directive itself. Article 10 of the Directive clearly states that 'waste shall be collected separately if technically, environmentally and economically practicable and shall not be mixed with other waste or other materials with different properties.

Therefore we believe that the bins are compliant with the current law as it stands.

7. Is there, as required by Department for Environment, Food and Rural Affairs (DEFRA), an audit trail that meets the requirements of the new regulations, to provide evidence in support of an argument for exemption from the forthcoming changes?

## **Response**

DEFRA have advised that new regulations will be published this winter regarding the quality of materials produced by the Materials Recovery Facilities, and the council will ensure its compliance with these requirements following publication.

Lord de Mauley states in his letter – "local authorities should consult their own lawyers as necessary and keep an audit trail given the potential for legal challenge." We confirm that once the regulations are published we will review them in line with our current procedures in consultation with our lawyers. However we note currently case law prevails which notes "the obligation to set up separate collection of paper, metal, plastic and glass from 2015 is restricted by both practicality and necessity requirements that also restrict the obligation in Article 10(2) to collect separately for the purposes of recovery"

It is important to note that DEFRA's correspondence from Lord de Mauley has been recently (16th October) commented upon by the Local Government Association (LGA) in their letter to the Rt Hon Owen Patterson MP as an "unhelpful contribution to the debate and will only cause confusion amongst councils and the industry in their interpretation of the legal framework". LGA notes that it is "crucial that councils understand that the letter records simply the opinion of the Minister, and that it would be legally unsafe to allow it to guide Local Authority decisions in any way. The most useful advice in the letter is that Local Authorities should take their own legal advice, and make decisions in accordance with that advice locally."

LGA further state that the "most important thing is having in place systems that work locally, encourage recycling and are easy for people to use".