States of Jersey
States Assembly

États de Jersey
Assemblée des États

Public Accounts Committee

Reporting of Abortive Costs

Presented to the States on 19th March 2018

P.A.C.2/2018

Contents

Reporting of 'Abortive Costs' of Projects

1 Background

1.1 Members will know that the Public Accounts Committee's remit is slightly different to other Scrutiny Panels in that it holds Officers rather than Ministers to account. It also takes a retrospective look at whether public funds have been applied for the purpose intended by the States, and whether sound financial practices have been applied throughout administration of all States departments.

1.2 The PAC is firmly of the belief that there remains scope for States departments to improve their general approach to project management, and has been giving consideration to the issue of the reporting of abortive costs (definition below). It noted that, presently, there is no requirement on Accounting Officers to report or explain abortive costs of projects at the time, or soon after, such losses occur. Reporting of 'fruitless payments' (definition below) are duly noted in the end-of-year Financial Report and Accounts. However, this annual report is usually reported to the States Assembly in the second quarter of the following year, so potentially there could be a gap of 18 months from the incurring of abortive costs, to the reporting of them.

1.3 Exhibit A (Appendix 1) shows the relevant page of the Financial Report and Accounts for 2016, published in the second quarter of 2017. Fruitless payments are shown in a lump sum, with no breakdown of costs in respect of the projects (for which funding was voted by the States) and no reporting of the department responsible.

2 Purpose

2.1 The PAC considers that the Accounting Officer (or Principal Accounting Officer where applicable) of each department should identify, report on, and be held to account for, such abortive costs. It is certain that this would help to improve decision-making, ensure prudent use of consultants, and help clear planning and implementation of policy. The PAC considers that this in turn would encourage stringent accountability, a learning culture throughout departments and promote openness and transparency.

2.2 The PAC accepts that some losses on projects (for which funding was voted by the States) will inevitably occur and it is not seeking to reinforce a "blame culture" when things go wrong or projects are halted. It also accepts that value can be found even in a project which is not seen through to completion.

3 Current Situation

3.1 There are already requirements stemming from the Jersey Financial Reporting Manual (JFReM) regarding the reporting of fruitless payments and these are duly noted in the end-of-year Financial Report and Accounts. Fruitless payments for individual projects (for which capital funding was voted by the States), even if they amount to significant sums (£50,000 or more) are not currently required to be reported to the States Assembly at the time (or as soon as possible after) they are incurred.

3.2 In the UK and its devolved administrations, there is a statutory obligation to report such abortive costs to the respective legislature as public funds have not been applied for their intended purpose. However, the departments do not have to report losses of under

£300,000. In Jersey, the PAC would like to see reporting of lesser sums, for example, in the order of £30,000.

4 Example – ICR

4.1 An example where the PAC consider that it would have been appropriate to see 'abortive costs' reported more meaningfully was the Health and Social Services Integrated Care Records programme, which the PAC reported on in 2014.

4.2 Members may recall that in 2006, the Health and Social Services Department (HSSD) committed to an ambitious strategy of transitioning to fully integrated care records (ICR) via a single major programme and within a timeframe of less than 5 years. HSSD sought and obtained £12 million capital funding in support of its ICR programme, without having first produced an outline business case and without the Minister for Health and Social Services giving the States Assembly an accurate and meaningful summary of the intended use to which the £12 million would be put. The de-scoped ICR programme concluded in the summer of 2011, having overrun by some 18 months. £11.97 million of the total programme budget was spent. The primary objective – an integrated care record spanning all health and social care settings – was not achieved.

4.3 Some material service improvements and cash savings were achieved by the programme but the cash savings were negated by a significant overall increase in IT-related operating costs. The majority of planned non-cashable efficiency savings were not realised, and the ICR programme was not closed by way of a formal and thorough evaluation.

5 Treasury Commitments

5.1 The PAC considered whether to propose to the States, the introduction of legislation for reporting abortive costs of (capital and revenue-funded) projects to the States Assembly. The PAC wrote to the Treasurer on 9th February this year, and PAC members met with senior Treasury Officers at the PAC meeting of 19th February. The officers offered alternatives to a Report and Proposition, for making the reporting of losses more transparent, quicker and more detailed.

5.2 The discussion with the officers was helpful, in particular, the PAC considered the following points:

- Definitions of 'abortive costs' in a broader sense than when applied by the UK
- The proposed financial parameters to be applied in reporting those costs
- Reporting lines (and proposed changes to them) as per the draft 'Machinery of Governance' Report and Proposition[1]
- Treasury Department's current plans to update Financial Directions

5.3 The Treasury Officers committed to:

- Providing more prominence to reporting constructive losses and fruitless payments in the 2017 Annual Report and Accounts
- Planning to issue a financial direction on Major Projects by the end of August 2018

[1] http://www.statesassembly.gov.je/assemblypropositions/2018/p.1-2018.pdf

- Working with colleagues in other departments to improve corporate control and reporting of projects [2]

5.4 The PAC heard that the Treasury is currently drafting a Financial Direction that encompasses 'major' projects over £1 million, or where the risks involved with the project are such that greater scrutiny is deemed by the Accounting Officer to be required. The PAC would like to see that apply to non-Ministerial departments as well as Ministerial departments, and would like to see more stringent reporting on projects which incur losses of £30,000. It notes that Arm's Length Organisations such as Andium, Ports and SoJDC already have requirements upon them to report losses.

5.5 At the moment, the Financial Direction, as drafted, does not capture constructive losses and the PAC has urged the Treasury to explicitly include them.[3]

6 Treasury Concerns

6.1 For the sake of completeness, the PAC also notes Treasury reservations about the PAC approach.[4] For instance, they have advised that extending the definition of "fruitless payments and constructive losses" to include "all such expenditure" is not straightforward. They advise that simply because a project does not produce the predicted or anticipated benefits it does not necessarily mean that it would be reported within an extended definition of "constructive losses and fruitless payments" or "abortive costs". They have also told us that the organisation's systems for monitoring and reporting on projects are being improved, but that it is a work in progress and likely to take some time to bed in fully:

> *'… Improved processes as a result of structural and operational changes, including improved use of performance information alongside financial information, and the use of benchmarking, will develop that approach for all areas of spending.'* [5]

6.2 However the Officers have indicated they understand and share the aims of the Committee to identify instances of poor value for money in relation to project expenditure and have agreed to continue a dialogue with, and provide updates to, the incoming PAC to try and achieve that objective. The PAC is also confident that Accounting Officers are perfectly capable of making the common-sense differentiation between feasibility studies and preliminary research on whether to pursue a project, and 'abortive costs' of a project.

6.3 We have been assured there are no manpower implications as a result of this undertaking, it can be resourced from within existing departmental resources, and does not require changes to existing legislation.

7 Conclusions

7.1 The PAC urges the Minister for Treasury and Resources and the Chief Minister to monitor the progress on this matter. The PAC has specifically concluded that:

[22] Confirmed after the private meeting, by way of email to the PAC Officer, 12.03.2018

[3] Notwithstanding that Guidance to the JFReM includes constructive losses and abandoned capital projects within 'Fruitless payments', the Committee would like to see specific reference to capital and/or revenue project losses including constructive losses.

[4] Confirmed after the private meeting, by way of email to the PAC Officer, 12.03.2018

[5] email to the PAC Officer, 12.03.2018, from senior Treasury official

a) All States departments should maintain an up to date record of losses. The record should show:
   the nature, gross amount (or estimate where an accurate value is unavailable), and
- cause of each loss;
- the action taken, total recoveries and date of write-off where appropriate; and
- the financial year in which the expenditure related to the loss falls

b) A losses statement should be produced and reported by the Accounting Officer to the Treasurer and Chief Executive;

c) the Annual Financial Report and Accounts should list those projects for which the abortive costs are equal to, or exceed, £30,000 and should describe for each such project how expenditure was incurred (and the options which were not pursued); what steps were taken to recover the money, where possible; what value was gained; and what was learned;

b) In relation to projects for which the abortive costs exceed £100,000, the relevant States member with official responsibility should report those costs to the States Assembly at the earliest available States meeting, with the report to include descriptions of the project; how expenditure was incurred (and the options which were not pursued); what steps were taken to recover the money, where possible; what value was gained; and what was learned.

7.2 The PAC also concludes that (total) departmental constructive losses should be identified as such and noted in the Losses Statement in the annual Financial Report and Accounts.

7.3 The PAC further concludes that when departments identify losses of £30,000 or more, they should consult the Treasury, if they:

- involve important questions of principle;
- raise doubts about the effectiveness of existing systems;
- contain lessons which might be of wider interest;
- are novel or contentious;
- might create a precedent for other departments in similar circumstances;
- arise because of obscure or ambiguous instructions issued centrally

Where such losses are reduced by subsequent recoveries, this should be advised by the Accounting Officer to the Minister and Treasurer.

Follow-up

7.4 The PAC will be including this matter in its legacy report and would recommend that the incoming PAC monitors progress and follows-up if necessary.

8 Definitions for the purpose of this Report

Definition of Abortive Costs

8.1 The term is used to encompass constructive losses and fruitless payments (both defined below). Current Financial Directions do not address the issue of ‘abortive costs’. Although accountability reporting defines ‘losses and special payments’ which includes fruitless payments and constructive losses, the PAC is keen to ensure that the States

Assembly is made aware, on a timely basis, of expenditure incurred that does not give rise to the benefit anticipated. It would like to see UK concepts of fruitless payments and constructive losses reflected in the Jersey Financial Reporting Manual to cover all such expenditure.

8.2 However, it does not consider all project research and development or feasibility studies *per se* to be 'abortive'. The PAC recognises that preliminary studies on whether to pursue a project or not, are worthwhile and can save money in the longer term.

Definition of Fruitless Payments

8.3 A fruitless payment is a payment which cannot be avoided because the recipient is entitled to it even though nothing of use to the entity has been received in return. It is a payment for which liability ought **not** to have been incurred, or where the demand for the goods and services in question could have been cancelled in time to avoid liability, for example:

- forfeitures under contracts as a result of some error or negligence by the department;
- payment for travel tickets or hotel accommodation wrongly booked or no longer needed, or for goods wrongly ordered or accepted;
- the cost of rectifying design faults caused by a lack of diligence or defective professional practices; and
- extra costs arising from failure to allow for foreseeable changes in circumstances.

Definition of Constructive Losses

8.4 A constructive loss is similar to fruitless payments, but one where procurement action itself caused the loss. For example, stores or services might be correctly ordered, delivered or provided, then paid for as correct; but later, perhaps because of a change of policy, they might prove not to be needed or to be less useful than when the order was placed.

Definition of a 'Project'

8.5 In Jersey, there is a clearly defined resource allocation and reporting structure for capital projects (for example the Future Hospital or a School) but a less defined structure for revenue, or mixed capital/revenue projects (e.g. eGov). Sometimes a 'Project' is at least part-funded from existing base budgets rather than a specific, additional allocation. For the purposes of this report, a Project is defined as a piece of work that:

- has an identifiable start and end date
- is outside of a Department's recurring activities
- is being undertaken to achieve a specific goal
- has defined deliverables

8.6 In addition any activities funded through a Capital Head of Expenditure will be considered to be projects.

8.7 A Major Project is any project where:

- the estimated overall outturn cost of the project (including professional fees and all other non-contract costs) is greater than £1,000,000; or
- the risks involved with the project are such that greater scrutiny is required (as determined by the Accounting Officer)

8.8 Where several smaller projects are interrelated, for example forming part of an overall programme, the Accounting Officer must consider whether it is appropriate to combine these when considering whether a project is part of a major or minor project.

8.9 Individual projects within a Capital Rolling Vote should be considered separately against the definitions above, for example, a project costing over £1 million would qualify as a Major Project.[6]

[6] Definition provided by Treasury Officers via email of 20th February 2018

Appendix 1: Exhibit A: Losses and Special Payments reported in Financial Report and Accounts 2016

States of Jersey

Financial Report and Accounts 2016

STATES OF JERSEY TREASURY

9.36 Losses and Special Payments

	2016 £'000	2015 £'000
Losses		
Losses of cash		
Overpayment of Social Benefits	100	73
Bookkeeping Adjustments	27	(562)
Other Losses of cash	2	
Total losses of cash	**129**	**(489)**
Fruitless Payments		
Fruitless Payments	–	193
Total Fruitless Payments	**–**	**193**
Bad debts and claims abandoned		
Uncollectible Tax	1,848	2,147
Other Tax Receivables written off	305	929
Other claims abandoned	363	590
Total bad debts and claims abandoned	**2,516**	**3,666**
Damage or loss of inventory		
Write off of expired stock	(15)	82
Other inventory write offs	71	112
Total damage or loss of inventory	**56**	**194**
Other losses		
Other losses	–	–
Total other losses	**–**	**–**
Total Losses	**2,701**	**3,564**
Special Payments		
Total compensation payments	100	123
Total ex gratia and extra contractual payments	25	370
Total Severance Payments	3,970	5,938
Total Regulatory Payments	(30)	25
Total Special Payments	**4,065**	**6,456**
Total Losses and Special Payments	**6,766**	**10,020**