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PCC No 88/23

Copy No 21 of 21

MEMORANDUM TO PCC FROM THE DEPARTMENT OF THE ENVIRONMENT

REVIEW OF CONTRACTS POLICY

Following discussion at PCC, DoE was invited in February 1988 to consider measures which might help to reduce the scope for the diversion to paramilitary funds of money from Government construction contracts. The terms of reference are given at Annex 1. This paper deals mainly with procedures relating to the letting of contracts by NI Government Departments and the Property Services Agency (PSA). Further attention is being given to the private sector. The review has been carried forward by DOE, with the assistance of the range of Departments and organisations noted at Annex 2.

2. The recommendations which we make are directed primarily toward contracts for capital and maintenance works placed by NI Departments and the PSA. We expect that they would also be applied to contracts placed by the Education and Library Boards and by the Health Boards. The Housing Executive, by reason of the complexity of its operations and the extent of the measures against mal-practice which it has already undertaken, raises particular issues which merit further consideration. We do however consider that the Housing Executive should at the minimum join in the common arrangement for obtaining security assessments of contractors which is noted at 13a.

3. We have used a broad interpretation of paramilitary involvement and funding of paramilitaries and have taken into account fraudulent practices of a social security or tax nature perpetrated by individuals or by companies, on the understanding that the paramilitaries gain directly or indirectly from the proceeds of these frauds.

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Background

4. Various proposals have been considered by the Government in recent years to combat malpractice in the construction industry. The measures which are in present use were introduced in 1984. They amount to

- a. the restriction of building and civil engineering contracts let by Departments and the Housing Executive to firms which are in possession of a current 714 Tax Exemption Certificate (ie to firms which are in good standing with the Inland Revenue), and a requirement that contractors should check that their sub-contractors are in possession of valid 714 Certificates.
- b. exclusion from Government contracts for a period of 3 years of building and civil engineering firms which have been convicted of social security fraud.
- c. approval by NIO of the security firms which contractors may wish to employ.

5. These measures have been applied widely by NI Departments during the past 4 years. While they have relevance to the problem, their penetration is limited. Representatives of the construction industry regard them as inadequate, and there is little to suggest that the incidence of malpractice within the construction industry has decreased in recent years.

6. The review has identified a number of areas of risk and has concentrated on addressing these. These relate to (a) Government's relationship with main contractors (b) the problem of sub-contracting (c) enforcement of measures adopted.



Main Contracts

7. Our first concern has been to try to find means of limiting the risk that main contracts placed by the Government might become a major direct source of funding to paramilitaries. This could occur because of management compliance with paramilitary demands or through paramilitaries gaining not just influence but effective control over a contracting firm. While there is no evidence of paramilitary take-over of construction firms, this cannot be ruled out and it is known that paramilitaries have gained control of other business activities.

8. This concern brings into question the extent to which Departments' present arrangements for appointing contractors and monitoring their progress offer or can be adapted to offer the necessary safeguards. The most notable aspect of the practices in present use is their wide diversity. The procedures used vary not only as between Departments but also within individual Departments (see Annex 3).

A Unified Government List of Approved Contractors

9. This highly fragmented system of contract placement makes it difficult to take a global view of the situation, to identify 'suspect' contractors or to consider means of dealing with abuses. The problem of paramilitary influence and racketeering is a common one potentially affecting all contracting Departments. Measures to deal with it, if they are to be effective, should also be on a common basis. The very diversity of Departmental practices is inconsistent with the achievement of a common approach to the placement and monitoring of Government contracts. Therefore our first and basic recommendation is that Departments should move to some common basis of contract placement.

10. We consider that there should be general adoption of the approved list system. We recognise that there is no 'best' arrangement which is entirely appropriate to the wide span of Departmental involvements in construction. There



has however been increasing recognition of the value for money and presentational merits of the approved list system. This system offers a basis for the development of measures against malpractice, and we recommend that it should be adopted by all Departments. In order to avoid administrative overburden we suggest that Departments should continue to use their present practices in relation to smaller works valued at up to a level to be agreed but which could be in the region of £50,000.

11. It would be possible for separate approved lists to be drawn up and maintained by each Department (and even this would represent a degree of consolidation of the present situation). However there is strong advantage in moving to an omnibus Government list of approved contractors which would include all firms in Northern Ireland which are interested in tendering for Government construction projects.

A Central Unit for the Approved List

12. The assembly and maintenance of the Government approved list could be made the responsibility of a small central unit which would liaise with contracting Departments and with other interested parties eg RUC, DHSS and Inland Revenue. Only in this way is there likely to be the consistency of approach which is needed to deal with the issues, many of them sensitive, which will arise and to present a common reference point to all interests.

13. The function of the central unit in relation to the management of the Government approved list would be

- a. to obtain from the RUC an assessment of applicant firms and the extent to which they may be amenable to paramilitary influence
- b. to obtain information from contracting firms which will assist action against fraud (see 14 below)



- c. to process the information obtained under b, liaising with Inland Revenue, DHSS and on occasion with the RUC
 - d. to liaise with contracting Departments about the technical competence of applicants (eg DOE would judge the competence of firms to construct roads, DHSS to build hospitals etc)
 - e. to obtain financial assessments of applicant firms
- and perhaps also
- f. to check on possession of equal opportunity certificates
 - g. to establish that contractors are in possession of a health and safety policy statement.

14. An advantage of the approved list system is that it offers an opportunity to obtain from applicant firms information which is relevant to the action against fraud (and which is unlikely to be available in any other way). As a condition of admission to the approved list contractors might be asked to agree to provide as required

- a. access to their financial records as main contractors and those of their sub-contractors while employed on a particular project. Examination of records might on occasion reveal the possibility of a leakage of funds to paramilitaries. More probably it should be seen as having some deterrent value against the formation of relationships with paramilitaries.
- b. information relating to all persons working on site, whether they be in direct employment of the main contractor, or employees of sub-contractors. This would include names and addresses and the reference numbers of Tax Exemption Certificates. Such information would then be made available to Inland Revenue and DHSS for computer runs to check for illegal use of Tax Exemption Certificates or of social security fraud.



- c. to obtain access to construction sites for the purpose of site audits. This would be a reserve power, used on occasion to verify information and to check the identity of persons on site. In most cases site inspections would be made by the police, who place a great deal of importance on obtaining this as a general right of access to construction sites.

Sub-Contractors

15. The preceding paragraphs have considered the position of main contractors who are directly employed by Departments. Much of the actual value of work carried out for Departments is undertaken by sub-contractors to main contractors. In most cases these are firms of standing and many are on current Departmental approved lists.

16. The aspect of sub-contracting which gives most cause for concern is labour only sub-contracting (LOSC). This practice has developed extensively in recent years and is widely considered to lend itself to social security fraud and to tax evasion. Research has indicated that there are some 9,000 operatives engaged in LOSC in Northern Ireland, of whom some 4,000 are engaged in public construction work. In many cases these labour only sub-contractors have no corporate structure and in practice are no more than gangs of self-employed workers who travel from site to site.

17. We have considered whether it would be appropriate for Government contractors and nominated sub-contractors to be required to use only their own directly employed labour ie effectively banning LOSC on Government projects. We have decided against such a recommendation because it would be likely to increase construction costs, to reduce flexibility within the construction industry and would sit uneasily with Government's policy of encouraging enterprise. We are more attracted to the option of implementing a form of registration of labour-only sub-contractors and of requiring main contractors to Departments to confine themselves to employing registered firms or gangs. This could involve a considerable administrative effort, but against such an investment has to be weighed the refuted extent of this sector's involvement in malpractice. We are not yet in a position to make a firm recommendation on this aspect.



Practicability and Cost of Proposals

18. We are conscious that our proposals would introduce an additional element of bureaucracy and of regulation in Government's relationship with the construction industry. We have therefore considered carefully the practicability of the arrangements discussed above with, on the one hand contracting Departments, and on the other with the RUC, Inland Revenue and DHSS who would be involved in scrutiny and follow-up action. There has not been time for detailed consideration of all of the administrative processes, but the general view is that the proposals are relevant and workable. The main administrative chore would probably lie in the receipt of information relating to individuals on construction sites (14b). This information would be processed through Inland Revenue computers, and any follow-up enforcement action would fall to Inland Revenue in the normal manner. DHSS are prepared to act similarly, but because of the very large numbers involved not all potential social security claimants among construction workers could be screened at once. Both tax and social security procedures would be targetted initially on projects where some difficulty is perceived.

19. A main point of concern to Departments has been that they should be allowed to retain full responsibility for assessing the technical competence of contractors to undertake the various categories of work. The central unit would have no technical competence and in managing the approved list would reflect totally the judgement of Departments in technical matters.

20. It would not be appropriate to apply certain proposals eg the collection of personal information in the case of sensitive security-related works. We would expect that contractors for these works would in other respects comply with the conditions for entry to the approved list.

21. The RUC support the proposals. They are prepared to carry out the security assessments of contracting firms and to co-operate in on-site audits as necessary. They see particular advantage in working with the unit which would be dedicated to continuous responsibilities in relation to Government contracts and in the application of counter-measures to fraud.

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24. The work of the unit would clearly be of a sensitive nature and must be assumed that staff engaged in administering the proposals would be exposed to a degree of personal risk. This factor would need to be taken into account in deciding the location of the unit. We note that the PSA have made it clear that although they are prepared to have the procedures applied to the work for which they are responsible in NI, they are unwilling to have their staff involved in the administration of them. We take the view that the central unit should be housed in a secure location, and that its staff should not be associated with the Government's normal dealings with the construction industry. For this reason we recommend that the unit should be located not within any NI Department but should function in association with the ARU. Such an association would ensure that in dealing with measures against construction industry malpractice the unit would be operating within the wider perspective of the anti-racketeering effort as a whole. This could have significance if, as may be expected, successful curbs against malpractice in the construction industry tend to have the effect of deflecting racketeering into other areas and activities.

Legal Implications and Enforcement

25. Legal advice is that it would be a reasonable exercise of discretion for the Government, in support of a policy directed against malpractice, to require the sort of information and facilities for inspection which we recommend as a condition of the entry of firms to the approved list. The advice which we have received suggests that such decisions, being a matter of private rather than public law, would probably not be amenable to judicial review. Decisions to remove a firm from the approved list (once it had been accepted) on grounds of non-compliance with the conditions of entry or of exclusion on grounds of suspected involvement with paramilitaries would have to be approached carefully, and on the assumption that such decisions may be capable of challenge.

26. There are at present three main forms of contractual conditions used by NI Departments. We have considered whether some degree of standardisation would assist measures against paramilitary-related malpractice, as in the approach to approved lists. NI Departments tend to adopt the contractual conditions used by corresponding Departments in Great Britain, and the contractual conditions which are at use in present are regarded as being most apposite to Departments' requirements. We are not aware that the contract conditions which govern Departments' relationship with contractors have any relevance to the paramilitary involvement, and accordingly we do not consider that there is anything to be gained by disturbing the present systems used by Departments.

27. We have also discussed with legal advisers the situation which would arise in relation to a contractor who, having been accepted for the approved list and having been awarded a contract, did not honour the conditions of entry to the list eg by failing to provide information relating to persons present on the site. The advice which we have received is that the only practical sanction available to the Government in such a case would be the removal of the firm from the approved list and its exclusion from further work after the contract had run its course.



28. We have however taken legal advice on the possibility of introducing an additional clause into contract codes which would amount to a provision that contractors should not pay protection money. The difficulties attached to this are obvious: the means by which such payments are demanded and paid are myriad, and any attempt at definition is as likely to exclude as much as it would include. It may nevertheless be helpful to have a catch-all provision - if for no more than its possible deterrent value - which would state that if an employing Department is satisfied that payments have been made by a contractor in response to unlawful demands, such a contractor may be removed from the approved list or the particular contract on which he is engaged rendered null and void. We are discussing the implications of such a condition with legal advisers, and we are considering means by which it could be given appropriately wide and emphatic publicity eg by means of a statement in Parliament.

29. We have noted that there is likely to be a mixed response to the proposals from the construction industry. The majority of contractors who work for the Government at present or who are candidates for Government work may nevertheless be expected to co-operate to the best of their ability in applying the new conditions. There will, however, be problems with some contractors, either by reason of the attitude of their managements or because of particular difficulties relating to the location of certain projects. In such cases an exercise of political judgement will be needed, and a willingness to balance, on the one hand, the disadvantage of accepting delay to or even withdrawal from a project in order to security credibility in the Government's policy against paramilitary racketeering, and on the other the normal pressures for project completion.

Castlecourt Development

30. The recommendations which we make are directed primarily to firms which are, or seek to be in, a permanent contractual standing with the Government eg membership of an approved list. However Government departments occasionally enter relationships with firms outside the normal approved list procedures eg for the acquisition of property through purchase or leasing arrangements. The



Castlecourt retail and office complex in Belfast is such a case. We are concerned to ensure that the thrust of our recommendations for approved list contractors should be carried over into major agreements of the Castlecourt type. We have therefore taken legal advice on the possibility of introducing additional clauses in the proposed agreement with Laings, the promoters of Castlecourt, which would broadly reflect the conditions for approved list contractors which we are proposing in this submission. We have presented these clauses to Laings, who are considering them. There are some indications that the firm may find difficulty in complying. In taking this action we have had close consultations with the police, who advise that there is very good reason in the case of this development to seek whatever safeguards may be obtained against the leakage of public funds to paramilitary interests.

Private Sector Implications

31. The recommendations contained in this submission are confined to public sector involvement within the construction industry. Later we will be considering what might be done to discourage paramilitary malpractice relating to privately sponsored construction works. We are conscious that to the extent that efforts to constrain malpractices in public sector contracts succeed, there could be a deflection of paramilitary pressures to the private sector.

Summary of Recommendations

32. We recommend that

- a. Departments adopt the approved list system of contract placement, where this is not already used.
- b. A general Government approved list should be created, covering the involvement of all Departments.
- c. As a condition of entry to this approved list, contractors should be required to provide information and facilities.

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- d. The construction and maintenance of such a general list should be the responsibility of a central unit dedicated to this task.
- e. Further consideration should be given to a form of registration for labour-only sub-contractors.
- f. The present forms of contractual conditions employed by Departments need not be changed.

J Murray

J MURRAY

27 May 1988

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APPENDIX 1

CONTRACTS POLICY REVIEW GROUP

The Group's terms of reference are:-

- (a) to review urgently current procedures for the letting of contracts in the public sector and make such recommendations as are necessary to reduce the scope for paramilitary involvement;
- (b) consider what further practices and procedures should be introduced by the public sector on site management and control to reduce opportunities for exploitation and racketeering during construction work; and
- (c) consider in consultation with appropriate representatives of the private sector, what changes in procedures and supervision could be introduced within the private sector to achieve similar objectives.



CONTRACTS POLICY REVIEW GROUP

Prior to preparing the report and recommendations the Contracts Policy Review Group had discussions with representatives of the various Government Contracting Departments and other interested parties:-

1. Department of Health and Social Services
2. Department of Education
3. Industrial Development Board
4. Department of the Environment Water Service
5. Department of the Environment Roads Service
6. Department of the Environment Housing Division
7. Central Unit on Purchasing
8. Northern Ireland Office
9. Property Services Agency
10. Inland Revenue
11. Royal Ulster Constabulary
12. Northern Ireland Housing Executive
13. Northern Ireland Electricity Service