Northern Ireland Assembly

PUBLIC ACCOUNTS COMMITTEE

OFFICIAL REPORT
(Hansard)

‘Synergy e-Business Incubator (SeBI)’

20 May 2010

NORTHERN IRELAND ASSEMBLY

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Members present for all or part of the proceedings:
Mr Paul Maskey (Chairperson)
Mr Roy Beggs (Deputy Chairperson)
Lord Browne
Mr John Dallat
Mr Trevor Lunn
Mr Patsy McGlone
Mr Mitchel McLaughlin
Mr Jim Shannon

Witnesses:

Mr Mel Chittock	)	Invest Northern Ireland
Mr Alastair Hamilton	)	Invest Northern Ireland
Mrs Tracy Meharg	)	Invest Northern Ireland
Mr David Sterling	)	Department of Enterprise, Trade and Investment

Also in attendance:

Mr Kieran Donnelly	)	Comptroller and Auditor General
Ms Fiona Hamill	)	Treasury Officer of Accounts

The Chairperson (Mr P Maskey):

David, would you like to introduce your colleague who has joined us at the table?

Mr David Sterling (Department of Enterprise, Trade and Investment):

Joining us is Tracy Meharg, who is the managing director with responsibility for innovation.

The Chairperson:

Tracy, I welcome you to today's Committee meeting. We will move straight on to members' questions.

Mr Lunn:

At paragraph 11 on page 24, we see that two sets of consultants were engaged to appraise the incubator project, and they appear to have identified some relevant potential threats that later damaged the success of the project. I would have thought that the project required a high standard of risk management. Why did it not receive that standard of risk management?

Mr Sterling:

We accept that. We do not disagree with the general conclusion that the value for money achieved by the project was poor. It is worth noting that the incubator supported 15 companies against a target of 20, six of which are still operating.

On the issue of risk management, it is clear that this was an innovative project and that it was inherently risky. There was sufficient evidence to conclude at the time that the benefits of the project would exceed the risks, but we acknowledge that the risk management could have been better. However, effort was made to manage the key risks that were identified at the outset of the project. Those had been identified under four areas.

The first concern was that there may not be a sufficient number of people interested in becoming "incubatees", which is an awkward word. Nonetheless, ICL Fujitsu encouraged its workforce to start up a small business to avail of the opportunity. They ran seminars and there were monthly progress reports. Risks around the uncertainty over accommodation were flagged up. The fact that it was difficult to find a permanent site for the incubator was a major problem in the early days, but the industrial research and technology unit (IRTU) and the industrial development board (IDB) co-operated to find premises.

There were risks in and around private sector financing. The risk was such that no new private sector financing was available. We must acknowledge that, at the time, the project was a concept. It was expected that there would be much stronger growth of information and communications technology (ICT) business, but globally, the ICT business crashed post-2001, partly because of 9/11 and so on. That made it a much more difficult environment in which to operate.

We now know much more about what is needed and how to manage incubator-type projects. It is quite clear from analysis that has been done across Europe that most of those units require some ongoing private sector funding, and few of them generate profits. Nonetheless, efforts were made to address that particular risk and ICL, for example, seconded three of their executives to the incubator. Those executives would normally have been expected to generate four times their own salary for ICL. The benefit in kind to the incubator was around £700,000 from those secondments, and ICL also provided services.

Those were some of the ways in which risk was managed, but we acknowledge that there are lessons to be learned from the project. Those lessons are now being learned and applied.

Mr Lunn:
Mention has been made of the fact that six of those businesses are still in operation. That seems to be at odds to the report. Page 23 states that there were only five of those businesses on site when the incubator ceased to operate. Of those projects, one relocated to Jordanstown, two to the Northern Ireland Science Park, and the two that were left were experiencing trading difficulties. That is either five or three. Are you satisfied that there are still six in operation?

Mr Sterling:
Additional work has been done to track down those companies. Tracy will comment on that.

Mrs Tracy Meharg (Invest Northern Ireland):
One of the big issues that the Audit Office identified in the process was the absence of good information on the incubating companies. It was difficult to find that information. We have now been able to identify six companies that are still operating that came through the incubator, and we know what their employment is. I am happy to pass that information to the Committee after the meeting.

Mr Lunn:
Do you know how many people they employ? Can you tell us, or do you want to write to us?

Mrs Meharg:

I am happy to write to you on that. It is in the region of 40 people.

The Chairperson:

Can you tell us where they are based at the moment?

Mrs Meharg:

I will be happy to do that.

Mr Lunn:

It seems odd that there were only five companies on site when it closed down.

Mrs Meharg:

I have included in the six the synergy company, which was there at the start, and may be included in the Audit Office's numbers.

The Chairperson:

I take it that the report was agreed between the Audit Office and yourselves?

Mrs Meharg:

Yes, that is right.

The Chairperson:

You did not have the numbers either at that stage.

Mr Lunn:

In 2009, as you know, the Committee published a report on the review of assistance to Valence Technology. There is a big difference in scale, but there are parallels with the Valence Technology project when it comes to controls, in particular the question of approval by the casework committee. What does a casework committee do? Where does it sit in the overall function of Invest NI?

Mr Alastair Hamilton (Invest Northern Ireland):

I will answer the second part of your question first. Leaving the project under discussion aside for the moment, the casework approval process, in general, allows the client executive or the person responsible for the project to put together a case. The case is reviewed, depending on the value of the proposed support to the company, which, in turn, depends on the delegated limits within the organisation. The case is reviewed usually by a group of three people in the organisation to provide a peer review across the team. The casework needs to clearly identify what the project is, what the expected outcomes are, and the pros and cons, which takes us back to the Valence project.

It was said earlier that there was no upfront identification of the risks to the project. The casework must clearly identify those risks and identify the mitigation process against any such risks. This project came from the same era as Valence Technology, and, therefore, some of the systemic issues that existed at that time are visible in this case. Whether this project should have gone to casework is commented on in the report. The project was concluded under a programme called Foresight, which had single delegated authority and did not require casework. That does not justify what happened, but simply explains it.

Mr Lunn:
Was there no approval by the casework committee of this particular project? Was there a failure to reappraise the project when major changes occurred as it went along?

Mr A Hamilton:
There are two aspects to that. There was no casework for this project. The lessons that have been learned from other projects that are now in place mean that if this project was being done in this way today, a casework committee would oversee it. Again, there was a delegated authority level in the IRTU at that stage, and the proper delegated authority limits were enacted in this case. It was signed off at the right level with the right person. The lessons that have been learned across the organisation over the past 12 to 15 years in cases such as Valence means that all projects should have casework approval. That requirement has now been embedded in the organisation.

Mr Sterling:
The project was reviewed and certain actions were taken following the withdrawal of Fujitsu. There was a consultants' review of the management arrangements and changes to management structure were made as well as some other changes. However, we accept that the withdrawal of Fujitsu represented a material change to the project. It should have been formally reappraised at

the time. Such a thing would happen under current arrangements.

Mr Lunn:

You probably would not be amazed at how often we listen to people saying that lessons have been learned and mistakes will never happen again. That is what we are about. For all that, we hear about the same failings over and over again; that is the way it goes. I am absolutely in favour of Invest NI, and this type of project is fine. I would not be particularly critical. I have said it here and in other forums that if Invest NI never took a risk it would never have a failure; it would not be doing its job.

If one only backed racing certainties, there would not be many of them; so one has to take risks. That is fair enough. If we lose the odd few bob here and there from backing the wrong horse, that is fair enough, as long as we monitor them carefully. That is what seems not to have happened here. There is a parallel there with failings. This thing was allowed to run without proper control and monitoring. That is my problem with it. It is not the fact that you took the project in the first place, but rather that it was allowed to dribble away money and fade out of existence without proper control.

You can treat that as a question if you want.

Mr Sterling:

I will let Alastair address that. However, we accept that, whilst there was monitoring of performance on a regular basis, the weakness was that there was no monitoring of financial performance. That is something that now happens consistently on projects of this nature and on projects generally. There have been improvements in control arrangements. You have said that you hear that time and again. However, let me repeat that, in this project, that problem occurred some years ago. We are confident that procedures are now much stronger.

Mr Lunn:

That is exactly what we hear time and again. We should almost have a button on that desk, which, when pushed, plays out the words "Lessons have been learnt." I do not want to be too critical. I will leave it at that. The next questions might follow on from that.

Mr Beggs:
I want to pursue that further.

Without appropriate monitoring, how can you take calculated risks and decisions? That is one of the main failures in this episode. Mr Sterling, paragraph 35 tells us that DETI and Invest NI did not receive detailed financial and management information from Synergy Centre Limited or Synergy eBusiness Incubator.

The sort of things that I understand to have been part of the grant arrangement are: board minutes, spending forecasts and four-monthly reports, which I understand were irregular and from which information was missing. Statisical information was inconsistent. I see from paragraph 19 that there was no source data to support the figure of 53 jobs. How solid was that figure? Do you accept that without accurate detailed information, which you had requested as a part of the grant arrangement, you could not monitor performance?

Mr Sterling:
I do not want to repeat myself endlessly, but we accept that, whilst there was monitoring of performance, it was not sufficient. In particular, the absence of monitoring financial performance was a clear weakness in the management of the project. I acknowledge that.

Some of my colleagues may want to pick up on some of the more specific points.

Mr A Hamilton:
I will pick up some of the points as to the granularity of the detail. I do not want to repeat David's comments. Information was requested, but it was not provided in sufficient detail. That should have been fixed. My second point is that the programme under which this was supported did not require that financial information be provided, just information on the operational performance of the project. That has now been changed. All projects that we support are now required to provide financial information.

Another point made in the report is that we did not monitor the parent company. That was also a failing in the process, and we now monitor parent companies of all such projects.

My only point is about your reference to the board meetings. Let me be clear: we do not request board minutes from companies. We rely completely on the information provided in the annual report and accounts, any quarterly financial information requested and any operational monitoring reports.

Mr Beggs:

If there are companies, particularly start-up companies, that are so reliant on that one aspect of their business, why do you not go for detailed information? In 2003, I noticed that there was another company spin-out from the operation and another £2 million with regard to NITAP. There were big risk factors. Why were you not keeping a careful eye on how the company was performing before giving out further significant amounts of public money?

Mrs Meharg:

An economic appraisal took account of the financial performance of SCL before the NITAP money was given out. The economic appraisal was sent back three times because issues were found. The latest report was aware of the deteriorating financial position in SCL at the time. However, the report also looked at the changes that had been made post the restructuring in 2002 and concluded that, given the changes to the cost structure and the fact that the incubator was now part of the University of Ulster, it believed that it was sustainable in moving forward and that the cost structure should deal with the underperformance. An appraisal and a casework were done for the NITAP funding.

Mr Beggs:

Can you assure the Committee that if a similar situation were to happen today that the parent company's finances would be carefully monitored, particularly when the daughter company is closely related to it?

Mr Mel Chittock (Invest Northern Ireland):

We review the risk profile of a potential project as part of the assistance that we provide. That also takes into account the parent company position, which would be assessed at the front end of a project. We would then attach a series of conditions to any assistance, so there would be pre-conditions, general conditions and specific conditions. There is a division of responsibility to sign off on those conditions to ensure that, first, they are adequately monitored and, secondly, that they are signed off at the appropriate level. We do that as part of our normal control framework.

Mr Beggs:

I want to concur with some of the comments that my colleague Mr Lunn has made. I fully accept that risks are involved if one wants to achieve new businesses. However, it is a matter of trying to minimise the risks involved in doing that, and we try to maximise the use of public funding. I am encouraged to hear that 40 jobs remain today. Those 40 jobs have been provided for a considerable time and, hopefully, more jobs will come.

Mr Lunn:

On the question of risk and reward, could you indulge me as this is more of a comment than a question? A few years ago, I was part of a Lisburn City Council trip that visited Estonia to look at its economic development. We visited an incubation unit, which was a pretty ramshackle affair. Nevertheless, people were beavering away inside. I did not think much about it until I was told that Skype had started in that unit, so there is hope.

Mr McLaughlin:

You have given your clients far too good a quality of service.

An important point was made by Committee members about the risk, and I suppose that there is another risk here. If we engender a risk-averse approach, we will fall short of our targets and aspirations. The thrust of the Committee's view is that risk is part of the process, so risk management must also be part of the process. If the Committee is critical, it is on that basis. It is certainly not to discourage people from taking risks, given the step change that we are trying to achieve with the economy. We will certainly have to repeat the Skype success story at some stage.

My questions deal with the experience of not having the information to hand. Paragraphs 38 to 40 characterise the post of project evaluation as being delayed and lacking detail. The Committee has returned to that issue time and again, and it emphasises the importance of strong post-project evaluation and the lessons learned — to go back to Trevor's point again.
What improvements to procedures has Invest made since those events?

Mr A Hamilton:

I fully accept the challenges presented to our post-project evaluation, and I can outline exactly what the organisation does today. To ensure timeliness, we require an independent post-project evaluation to be completed within six to nine months of the end of the project. We rigorously enforce that timeline. I will not explain some of the problems and difficulties experienced with the company that we are talking about today.

Mr McLaughlin:

They are well described in the report.

Mr A Hamilton:

They are. To provide visibility of what we do annually, we evaluate individual projects such as this one and programmes under our umbrella of support for programmes, including research and development. In the year that we have just exited, 313 post-project evaluations (PPEs) were conducted in Invest NI on both projects and programmes. We currently have a rolling three-year process within which we evaluate every one of our more than 100 programmes. Therefore, there is an intensive process at project and at programme level to ensure that PPEs are done.

However, doing them differs slightly from doing something with them. I assure the Committee that what is learnt from those project and programme plan evaluations is ploughed back in. There are two examples today of programmes which are currently suspended because their PPEs highlighted issues that must be resolved before each programme, or a variant of it, carries on. In answer to Mr McLaughlin’s question: we have a very detailed process, 313 of evaluations were conducted last year and there is a rigorous process to ensure that derived learning is ploughed back into both projects and programmes.

Mr McLaughlin:

The Committee is encouraged to hear that, although, in this case, core data was not available to make its post-project evaluation particularly effective or successful. There are lessons in that as well, and I am giving Invest NI credit for responding to them. Recalling the action and the process is required to develop the type of risk management that can identify any potential value from post-project evaluation.

I reiterate that, provided that the process is rigorous enough, members defend Invest’s risk-taking ability and capacity. Politicians, who often get it in the neck from the media, could inhibit Invest’s manoeuvrability. Therefore, we must give each other confidence and support. Managing risk is key and I hope that that is reflected in both our approaches. It is not a matter of finding fault because, from start to finish, the project is challenging.

Paragraph 41 highlights a number of important areas in which SeBI could have been better appraised and managed. Will Alistair Hamilton assure the Committee and indicate to it how project management has changed to ensure that we good money is not thrown after bad?

Mr A Hamilton:

In response to your earlier comments, we welcome the fact that its members understand the challenges involved in trying to drive some of these policies forward. I fully understand, and the organisation takes seriously, the difference between risk avoidance and risk management to the point of project management, in which roles and responsibilities are clearly defined when a project is entered into.

Let me return to the casework: right up front in the casework, the risks of the project are identified, as are the mitigations against those risks. Immediately after a casework committee signs off a project, those risks are apportioned to an individual in the organisation and that information is tracked in our client contact management system. Therefore, the information is recorded so that individuals know exactly who is responsible for the ongoing management of that risk.

For high risk projects, we now ensure that monitoring meetings take place regularly, and that those meetings are minuted and recorded in that CCMS system, together with any outcomes of that. This refers to Mel's earlier comment about parent company guarantees, company liabilities or any of those issues that arise in response to that ongoing project management. If there are any issues, they are then highlighted up the management chain.

Mr McLaughlin:

Would we get an earlier response if there was shortfall or deficit in the job creation targets and the milestones that had been set out in the original business plan?

Mr A Hamilton:

All of that is now tracked on the CCMS system.

Mr McLaughlin:

It is not a matter of gathering the information; rather, we must use it.

Mr A Hamilton:

A decision will always be taken at a point where a project starts to go off track according to the delivery mechanisms. Let me give you an indication of the scale of the operation: currently, there are 7,000 live letters of offer in Invest Northern Ireland that are tracked and managed on that CCMS system.

Mr Sterling:

It is also worth recognising that any performance that is related to a Programme for Government target or public service agreement target flows from Invest NI to the Department and is reported to the Executive and ultimately to the Assembly in the PfG reporting mechanisms.

Mr Beggs:

This is addressed to Mr Hamilton. I note that, on pages 81 to 84 of the annual report for 2008-09 and in note 31 of the accounts, there is a long list of transactions with the client companies where Invest NI board members have declared a private interest. I have no doubt that Invest NI benefits from that private sector experience to add to the decision-making process. Can you explain to us how Invest NI manages those conflicts of interest? In a potential conflict of interest, it is important that the process is managed so that there is transparency and also public confidence in the decisions made.

Mr A Hamilton:

The current process that we use to manage the conflicts of interest is as follows. Twice a year, in April and October, all our board members are asked to declare their interests. They have to record all their interests and all the companies with which they are connected. The occasion in April is used for the compilation of our annual report. The transactions are all entered onto a system whereby we can hold all of that information together.

We then search across the Oracle database, which is our financial system for all the companies referred to in that database. I do not want to go back and start making excuses for some of the variants between the two questions, but some challenges are involved. Companies can be referred to in lots of different ways; for example, the Northern Ireland Science Park could be referred to as such, or as the “NI Science Park” or as the “NISP”. So there are some challenges that we must manage in that process.

Anyway, we match those companies, and the transactions we do with them, with the list of board members’ interests. They are then broken down into grant moneys and payments for services. You will see those separated in our report. That separation between grants and services is done on a manual basis. Someone goes through all those transactions and separates them. There is scope for human error in that process. A distinction is then made on the point that David Sterling made earlier, between beneficial and non-beneficial interests, and that too is a manual process. Those, too, are separated. People within the Finance Department audit all of that information to ensure that it is up to date and accurate, before it is entered in our report.

That is a part of the answer to your question: how conflict of interest is reported. The second part of the answer is how those conflicts are managed in our organisation on a day-to day basis. As you rightly say, we should get maximum value and benefit out of having private-sector and well-connected people on our board, but we must minimise any potential issue arising from interests. At the start of every board meeting, as you would expect, the chairman of the board asks board members to declare their interests. If any interests are declared that are relevant to the agenda of the meeting, the chairman will decide whether any board members need to leave for the entire meeting or for a section of it. Some board members are very well connected across the business community, which is great for us, because we sometimes find opportunities through the board members. However, in general, there is a clear process in place so that if a board member wants to engage with our organisation, they can do so through an MD. He or she must go to one of the four MDs in the organisation to ask them to pursue an opportunity with a company. All those contacts are kept at MD level.

Through all those recording and monitoring processes, and in managing conflict, that is what we do today.

Mr Beggs:

That is a very comprehensive answer. It is clear that those services are in great demand. It is appropriate that the organisation is managed as you have indicated. The public can benefit from your expertise.

I will turn to your employees' interests. Undoubtedly, Invest NI employees will need to have a high degree of interaction with the businesses that they support and the business community generally. Can you assure the Committee that Invest NI operates a watertight system in relation to employees' declarations of outside interests? In the past, there were problems with Northern Ireland Tourist Board funding. How is that process managed?

Mr Chittock:
We have a clear code of conduct, which means that all staff must avoid all conflicts of interest, whether real or perceived. All staff are required to declare all outside interests to the human resources function, which holds a central register of all interests that staff members have. In addition, all our contracts of employment have a condition that requires that they do not work, or are not employed, in any other business apart from the work of Invest NI. Any breach of that condition is grounds for instant dismissal. We take our staff members' interests very seriously.

Mr Beggs:
What happens when staff move on? Some time ago, an employee of the Department of Agriculture and Rural Development sat on a board and was transferred to a private company that had obtained considerable funding in the area in which that employee was working. Is there any protection against a situation in which, perhaps, a significant grant is awarded to a company, after which job opportunities arise for individuals who took the grant decision? Is there a requirement, particularly at senior decision-making level, that there would be a gap before an employee could transfer to a company that had benefited from significant public sector grants?

Mr Sterling:
Are you asking about senior civil servants or senior —

Mr Beggs:
I am talking about a situation in which a staff member who made a decision or who provided specific advice to a company that resulted in its obtaining a significant public sector grant, suddenly being offered a job by that company.

Mr Sterling:
There are rules that apply to people who leave the Civil Service or indeed the Senior Civil Service. There are restraints on the activities that they can do and the organisations that they can

join. I do not have the detail of that, but I am happy to write to the Committee with those details.

Mr Lunn:

You have a well-established system of checks and balances in relation to conflicts of interest. However, do you ever find yourselves in a situation in which you have to tell a board member that he either has to give up his interest in one of your client companies or his interest in the board? Is that too simplistic? There seems to be a recipe for clear conflict.

Mr A Hamilton:

As I have outlined, I believe that we can manage all the conflicts that exist. Let us bear in mind that board members' interventions in the day-to-day operation of Invest NI come in two ways: first, through monthly board meetings, and secondly, by way of casework, through which, by way of the delegated limit that I talked about earlier, board members become involved in higher-value projects. It is quite easy to ring-fence those projects, based on the expression of interest from the board members, and keep them away from projects in which they have an interest.

Mr Lunn:

"Keep them away" is a grey area, which would apply to employees, too. I do not see how somebody could have a financial interest in one of your client companies, and be a senior employee or board member. I heard what Mel said about the necessity to intervene at least at managing director level. I do not see what difference that makes.

Mr Chittock:

We have very clear rules. If employees have a financial interest in an organisation outside Invest NI, they are not allowed to have any contact with that company or any intervention from Invest NI. Therefore, they are not part of the management of that relationship.

The Chairperson:

The Committee has never advocated that the public sector should be risk averse. The Committee said that on a number of occasions, and it needs to be restated. It is unfortunate consistently to have to say that where there is risk in public sector activities, that risk needs to be identified, as Trevor and Mitchell said. When identified, the risk needs to be managed in keeping with the best practice guidance issued by the Department of Finance and Personnel.

The Committee recognises that risks have to be taken in areas such as Invest NI. There will not always be a successful outcome, but it is important that the risks are well managed and handled more professionally. The Committee supports well-thought-through and well-managed risk taking. Regrettably, if we are being honest, that is not what the Committee saw today.

Invest NI needs to ensure that all interests, including those of board members and staff, are recorded in a register of interests, which you said will be done. Obviously, the register will be updated regularly and properly reported. Conflicts of interest are to be managed effectively, or better still, in most cases hopefully, avoided altogether.

Mel, Alastair, David and Tracy, at this stage thank you very much.