

Norfolk County Councillors Andrew Boswell
and Elizabeth Morgan

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Anthony Boucher,
Local Transport Funding, Growth and Delivery,
Department for Transport,
Great Minster House,
33 Horseferry Road,
London,
SW1P 4DR.

September 3rd 2015

Dear Mr Boucher,

Department for Transport : Additional funding for Norwich Northern Distributor Road

We understand that DfT is shortly to decide whether to make a further funding contribution of £10m to the Norwich Northern Distributor Road (NDR). This would be under an arrangement where Norfolk County Council (NCC), New Anglia Local Enterprise Partnership, and the DfT each contribute £10m to fund a £30m hike in the project costs following contractor Balfour Beatty presenting a final target cost to the Council.

On Sept 2nd, Norfolk County Council decided to find an additional £10m. The voting was 59 in favour with 11 councillors not being in favour (8 against and 3 abstentions). We are two of the councillors who voted against.

We are writing to you because 1) the Norfolk County Council decision is unsafe as Councillors were misled, 2) to recommend that your department defers its decision pending further investigation of the financial details, and possible alternatives.

Problems with the Norfolk County Council decision

Councillors were provided with a 24 page agenda paper (attachment: 150902 County Council Agenda.pdf). This included financial information on the construction cost changes between 2013 and 2015 which comprise the £30m hike. The key message to councillors was that the construction cost inflation “aligned” closely with the Department of Business, Innovation and Skills (BIS) ROADCON TPI index for a similar period. Councillors were advised that it followed that the Council should proceed to Stage 2 of the Contract, and not seek to re-tender.

The relevant figures presented in the report to Councillors are 18.7% Construction Cost inflation (CCI), and 22% TPI Index rise (TPI). This gives a CCI/TPI ratio (our terminology) of 0.85.

Prior to the meeting (on August 31st and September 1st), we advised the Council that there were errors on both the above figures: the actual figures being 33.93% for the Construction Cost inflation (CCI) and 15.68% for the TPI Index rise (TPI). This gives a CCI/TPI ratio of 2.16. (We provide details of the two errors in Appendix A and Appendix B of this letter, showing both the correct calculations and how the errors were made in both case.)

However, the Appendix D of the Council agenda paper states that “the inflation allowance in the 2011 Development Pool bid to DfT was set at 2% per annum to 2017”. When the TPI Index rise is adjusted over the 9 relevant quarters to reflect this, the TPI Index rise becomes 11.18%. This gives a CCI/TPI

ratio of 3.03 (the corresponding ratio for a CCI of 18.7% would be 1.67). The calculation of these CCI/TPI ratios is given in Appendix C of this letter.

This means that far from being aligned, the Construction Cost inflation in the Balfour Beatty new pricing has risen to more to over 3 times the market rate given by the TPI index. (Even without the correction the Construction Cost inflation, given in Appendix B, it is 1.67 times the market rate).

Despite the information provided by us prior to the Council debate, the Council made no changes to the agenda papers and the financial briefing therein to Councillors. The Director responsible did however acknowledge within the meeting that our figure of 15.68% for the TPI Index rise was the correct one. It is our strong opinion that proper due diligence in making the Council decision was not followed. Within the debate, Cllr Boswell called on the Council to postpone the decision, pending clarification of the errors and misinformation, and the misleading recommendations following from it.

NEC3 contract with Early Contractor Involvement

A fundamental issue is that Councillors, the DfT, the Examining Authority at last year's DCO Examination in Public, and the public, have been led to believe by NCC that the NEC3 contract with Early Contractor Involvement (NEC3/ECI) was entered into to prevent exactly the sort of cost hikes now being made to the project.

The Development Pool bid (DPB) to DfT states that the NCC Design team had worked with the appointed contractor (then known as Birse Civils Ltd) on detailed design scope changes (attachment: NCC132459.pdf, page 24, section 2.3b). The DPB also has at Figure 4.1 (PDF page 38) a Quantified Cost estimate of the total outturn cost.

There are serious questions as to why the £10m for further "Design Development" (£5m) and "Design Standards" (£5m) have only been notified as of 6th August 2015, and no indication of these were submitted to the EiP, even before its closing date of December 2nd 2014. It is unacceptable for the £10m new Design Factors to be treated as notional 2013 costs: they are new costs in the 2015 figures.

Further, if increases with the supply chains were happening, why were these also not reported to the EiP?

The NEC3/ECI should have brought well developed target price early on with the provision to re-procure quickly and effectively if the contractor is not performing well, and this must include keeping on par with market pricing (ie BIS ROADCON TPI) having taken into account any inflation allowance originally agreed. We note that the Government say on NEC3/ECI for the HS2 project that a mechanism will be developed for quick and effectively re-procurement¹ between Stages 1 and 2, if necessary.

Issues for the Treasury/DfT decisions

Central Government appears also to be lined up to make up a further £10m via the New Anglia LEP as the LEP intend to make up their £10m contribution via future Growth Fund allocation rounds. So the real Whitehall contribution is likely to be £20m, even though only a £10m funding is under discussion.

The DfT/central government should undertake a serious scrutiny of the contract cost increase before agreeing to fund £10m directly, and £10m indirectly, of the contract shortfall. This scrutiny cannot be done by September 8th, and therefore the DfT should defer its decision to examine the issues in detail.

These include:

1. Given the 3 times TPI index cost increase, outlined here, should the contract be re-tendered for NEC3 Stage 2? If the Government believe it may be done quickly and efficiently on HS2, why not the NDR?
2. Should other alternatives be considered such as amending the Development Consent Order to build the

¹https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/377586/Early_contractor_involvement_ECI_guidance_Oct_2014.pdf

NDR to the A140 in the first instance? This is quite feasible, and relatively easy, legally now, following the enactment of the Infrastructure Act 2015. The contract may then either be renegotiated with Balfour Beatty, or NEC Stage 2 re-tendered, to construct from Postwick to the A140.

It is worth noting that the Government (DfT) funding has previously only been provided for the Postwick-A140 connection. The Government predicated making the NDR a National Significant Infrastructure Project (NSIP) on the strategic and economic aspects of this Eastern section. And it is also the section that relates to the Norwich North East Growth Triangle (NEGT) where new homes and economic development are primarily planned in the Joint Core Strategy (JCS). (The context here is that the ¾ NDR, now costed at £178.5m, comprises two main parts: Postwick-A140 (Airport) Eastern section, and A140 (Airport)-A1067 Western section.

3. As explained, the papers provided to Councillors contained errors and were misleading about the relationship between the Construction Cost inflation and market TPI indexes. Should the Government not defer its decision until after questions about the due diligence at the Norfolk County Council meeting have been investigated?
4. Appendix D contains some other more technical concerns

We further note that for the Government to make this £10m contribution today sends a poor message to the Construction market and industry. By accepting cost increases which are out of kilter with market indexes, the Government is giving the message that companies can hike their prices above market indexes and get away with it, for it will be get strapped-for-cash Whitehall departments and Councils who will cough up the funding shortfalls.

We strongly suggest that you defer making a decision on the £10m direct, further funding contribution to this project until the alternatives above have been properly assessed and appraised.

We look forward to your full response to these points.

Yours sincerely,



Councillor Andrew Boswell
Norfolk County Councillor and
Leader of the Green Party Norwich City councillors

Elizabeth Morgan, Norfolk County Councillor and
Vice-Chair, NCC Adult Social Services Committee

APPENDIX A

Error in the BSI ROADCON TPI index information provided to Norfolk County Councillors

The table below shows a spreadsheet of the BIS ROADCON TPI Index values used by the Council (data taken from spreadsheet provided to me by Jon Barnard, Norfolk County Council, by email 01 September 2015 17:07).

	Q1	Q2	Q3	Q4	Annual Increase based on Q1 figures	Accumulative Increase from 2010Q1	2015 Accumulative – 201N Accumulative
2010	157	163	168	N/a	11.46%	0.00%	
2011	175	169	175	176	2.29%	11.46%	36.31%
2012	179	180	179	185	7.82%	14.01%	24.84%
2013	193	194	198	204	8.81%	22.93%	22.29%
2014	210	216	213	213	1.90%	33.76%	13.38%
2015	214					36.31%	0.00%
2015Q1/ 2012Q4	15.68%						

1. The Council report focuses on the “late 2012 to early 2015” period ie: 2012Q4 to 2015Q1 (Attachment, Appendix D, page 16, bullets 5-7).
2. The correct calculation is given by the 2015Q1/2012Q4 ratio (Green square and yellow squares).
3. The Council’s erroneous calculation is derived by subtracting the 2012 “Accumulative increase from 2010Q1” from the 2015 “Accumulative increase from 2010Q1” (Orange square). There are two arithmetic problems with this:
 - a. The accumulative increases contain a compounding factor (similar to compound interest): it is not arithmetically correct to subtract one from another to calculate relative changes within the sequence (2015Q1/2012Q1=19.5% rather than 22.29%).
 - b. The 22.29% figure represents a change from 2012Q1 to 2015Q1 **not** 2012Q4 to 2015Q1

APPENDIX B

Error in the Construction Cost inflation information provided to Norfolk County Councillors

1. Appendix C of the Council report (Attachment, page 15) compares the NDR Project costs between the 2013 Q1 base year estimate and 2015 Q2 Current forecast. The Construction Cost subsection contains a breakdown of these factors: “Base Construction Cost excluding fee”, “Risk Allowance (Contractor)”, “Contractor fee”, “Inflation allowance to outturn”, and then a sub-total “Total Construction Cost” is given.
2. A further table (Attachment, section 2.2, page 6) indicates two further factors “Design Development” and “Design Standards”, each costed at £5m in the 2015 Q2 Current forecast. These were not shown in the Appendix C table.
3. I reproduce the Construction Cost sub-section here and calculate the inflation increases in the repricing from Balfour Beatty based on A) the Base Construction Costs and B) the Total Construction costs.

NDR Project Cost Comparison 2013 to 2015						
	2013 Q1 base year estimates	2013 Summary	2015 Q2 Current Forecast	2015 Summary	Percentage increase 2013- 2015	
	£m	£m	£m	£m		
Construction Costs						
Base Construction Cost excluding fee	66.4		93.5		40.81%	A
Risk Allowance (Contractor)	2.4		3.4			
Contractor fee	3		4.1			
Inflation allowance to outturn	6		3.2			
Total Construction Cost	77.8	77.8	104.2	104.2	33.93%	B

4. The correct figure based on the “Total Construction costs line” is 33.93%.
5. The Council explained to me their calculation of the Construction Cost inflation as follows (Jon Barnard, Norfolk County Council, by email 01 September 2015 17:07).

Q1: Please indicate how the quoted construction cost increase in the agenda document of 18.7% is calculated?

The reasons for change of construction costs has been covered in section 2.2 (page 5) in the report.
The resultant percentage increase was calculated as follows:-

2013 Q1 base estimate total construction cost £77.8m (Appendix C of the report)
Plus £5m Design development (Reasons and breakdown given in table 2.2 page 6 of report)
Plus £5m Design Standards (Reasons and breakdown given in table 2.2 page 6 of report)
This equals £87.8
Plus 18.7 % for Road Construction Inflation (reasons given in table 2.2 page 6 of report)
Equals 2015 Q2 Current Forecast of Total Construction cost £104.2 (as per Appendix C page 15)

6. This calculation corresponds to the following on the Council Report Appendix 3:

NDR Project Cost Comparison 2013 to 2015						
	2013 Q1 base year estimates	2013 Summary	2015 Q2 Current Forecast	2015 Summary	Percentage increase 2013- 2015	
	£m	£m	£m	£m		
Construction Costs						
Base Construction Cost excluding fee	66.4		93.5			
Risk Allowance (Contractor)	2.4		3.4			
Contractor fee	3		4.1			
Inflation allowance to outturn	6		3.2			
Total Construction Cost	77.8	77.8	104.2	104.2		
<i>Design Development</i>	5		0			
<i>Design Standards</i>	5		0			
NCC Calculation Sub- total	87.8		104.2		18.68%	E

7. The error here is that the two new in 2015 Design Factors (yellow squares) have been added into the 2013 figures.

APPENDIX C

CCI/TPI ratios

1. The Table shows the (CCI/TPI) ratio of the 2012Q4-2015Q1 BIS ROADCON TPI Index (see this letter, Appendix A) over the Construction Cost inflation (see this letter, Appendix B).
2. The A column shows the TPI Index as per the Council agenda papers, and the corrected value acknowledged by NCC.
3. The B column shows the same data but with a 4.5% correction corresponding to the contractual inflation allowance (as in the 2011 Development Pool bid to DfT) set at 2% per annum to 2017.
4. The C column shows the Construction Cost inflation as per the Council agenda papers and as corrected in this letter in Appendix B.
5. The D column shows the CCI/TPI ratios uncorrected for the contract inflation allowance, and E show CCI/TPI ratios corrected for the inflation allowance.

	BIS ROADCON TPI Index (TPI)	BIS ROADCON TPI Index (TPI) - 2%/yr over 9 quarters	Construction Cost inflation (CCI)	CCI/TPI	CCI/TPI (inc. 2% inflation adjustment)
	A	B	C	D = C/A	E = C/B
Council Agenda Papers	22.00%	22.00%	18.70%	0.85	0.85
Correcting the TPI Index, acknowledged by Council	15.68%	11.18%	18.70%	1.19	1.67
Correcting the CCI figure	15.68%	11.18%	33.93%	2.16	3.03

APPENDIX D

Other issues of concern

1. The Council state that Construction Cost increases are due to supply chain costs changing. Have the figures involved been forensically examined?
 - a. Are supply chain providers increasing their margin?
 - b. Were supply chain estimates too low to start with?
2. Why is there such an increase when the oil commodity market price have halved since 2013?
3. Why has the £8.3m budget line for “Statutory Undertakers”, not in the Sept 2011 Development Pool Funding Bid been introduced?