

Argyll and Bute Council

Internal Audit Report

May 2021

FINAL

Capital Monitoring

Audit Opinion: Substantial

	High	Medium	Low	VFM
Number of Findings	0	2	0	0

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1. Executive Summary

Introduction

1. As part of the 2020/21 internal audit plan, approved by the Audit & Scrutiny Committee in March 2020, we have undertaken an audit of Argyll and Bute Council's (the Council) system of internal control and governance in relation to Capital Monitoring.
2. The audit was conducted in accordance with the Public Sector Internal Audit Standards (PSIAS) with our conclusions based on discussions with council officers and the information available at the time the fieldwork was performed. The findings outlined in this report are only those which have come to our attention during the course of our normal audit work and are not necessarily all the issues which may exist. Appendix 1 to this report includes agreed actions to strengthen internal control however it is the responsibility of management to determine the extent of the internal control system appropriate to the Council.
3. The contents of this report have been agreed with the appropriate council officers to confirm factual accuracy and appreciation is due for the cooperation and assistance received from all officers over the course of the audit.

Background

4. Section 35(1) and (2) of the Local Government in Scotland Act 2003 determines that it is the duty of each local authority to determine and keep under review the maximum amount which it can afford to allocate to capital expenditure.
5. The Council's Financial and Security Regulations, and the Capital Programme Planning and Management Guide (the Guide) provide the framework for managing the Council's available capital resources. The Guide aims to ensure clear alignment of the Council's Capital Programme with the Council's governance and management structures, its key strategic plans and its budgeting process.
6. Audit Scotland reported on Asset Management for the Council in December 2016. The report highlighted the importance of elected members receiving adequate information on capital investment and individual projects to enable them to effectively scrutinise the performance of capital programmes.

Scope

7. The purpose of the audit was to assess the Council's capital budget monitoring procedures and controls to ensure they are working both efficiently and effectively.
8. The audit focused on the processes carried out by staff in Financial Services and Project Managers when completing the capital monitoring spreadsheet that informs the Capital Monitoring Reports provided to various Committees.

Risks

9. The risks to be considered throughout the audit are:
- **SRR02:** Infrastructure and asset base does not meet current and future requirements and is not being used or managed efficiently and effectively.
 - **ORR04:** Capital programme is not effectively managed
 - **Audit Risk 1:** The Council does not have Capital monitoring procedures and processes which align with the Council's Financial Regulations.
 - **Audit Risk 2:** Capital Monitoring is not carried out as per Council's procedures and processes.
 - **Audit Risk 3:** Initial profiling of capital expenditure spend is not robust.
 - **Audit Risk 4:** Capital Monitoring and Reporting arrangements do not provide sufficient information to allow effective scrutiny.

Audit Opinion

10. We provide an overall audit opinion for all the audits we conduct. This is based on our judgement on the level of assurance which we can take over the established internal controls, governance and management of risk as evidenced by our audit work. Full details of the five possible categories of audit opinion is provided in Appendix 2 to this report.
11. Our overall audit opinion for this audit is that we can take a substantial level of assurance. This means that internal control, governance and the management of risk is sound. However, there are minor areas of weakness which put some system objectives at risk and specific elements of residual risk that are slightly above an acceptable level and need to be addressed within a reasonable timescale.

Recommendations

12. We have highlighted two medium priority recommendations where we believe there is scope to strengthen the control and governance environment. These are summarised below:
- the Capital Programme Planning & Management Guide should be refreshed after the revised Capital Strategy is approved
 - a training programme should be developed to support officers involved in the management of the Council's capital programme.
13. Full details of the audit findings, recommendations and management responses can be found in Section 3 of this report and in the action plan at Appendix 1.

2. Objectives and Summary Assessment

14. Exhibit 1 sets out the control objectives identified during the planning phase of the audit and our assessment against each objective.

Exhibit 1 – Summary Assessment of Control Objectives

	Control Objective	Link to Risk	Assessment	Summary Conclusion
CO1	The Council has capital monitoring procedures and processes which are aligned to Financial Regulations and good practice.	SRR02 ORR04 Audit Risk 2	Reasonable	The Council has an approved Capital Programme Planning and Management Guide which is aligned to Financial Regulations and good practice however it has not been updated since 2018 due to the ongoing development of a new Capital Strategy. Officers are currently developing this Strategy and once finalised the Guide should be refreshed to ensure the two documents complement each other. It would also be beneficial to engage with relevant officers to identify training needs and develop a training programme aimed at addressing these.
CO2	Capital monitoring procedures are consistent with established procedures.	SRR02 ORR04 Audit Risk 2	Substantial	The monthly capital monitoring process is well established and there is evidence that staff in Financial Services have taken steps to update and enhance this process and actively engage with elected members and officers involved in project management.
CO3	Profiling of capital projects is based on a robust process and regularly reviewed	Audit Risk 3	Reasonable	In the past three years there has been significant slippage in the Council's capital programme and whilst some will be 'true' slippage it is also likely that an element is due to inaccurate expenditure profiling. There are also differences in the way project managers access and analyse financial information on capital projects and it would be beneficial if the revised Guide was clear about the reports which can be provided to project managers and what additional information can be provided on request.
CO4	Capital expenditure is monitored in line with budget monitoring arrangements and reported regularly to relevant officers and elected members.	SRR02 ORR04 Audit Risk 4	High	Capital monitoring reports are presented to a variety of committees and senior management teams by both project managers and financial services.

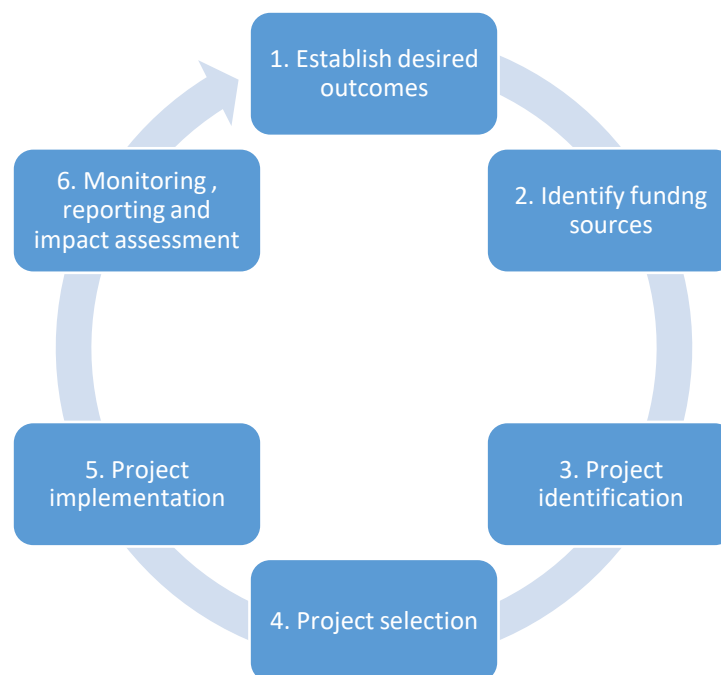
15. Further details of our conclusions against each control objective can be found in Section 3 of this report.

3. Detailed Findings

The Council has capital monitoring procedures and processes which are aligned to Financial Regulations and good practice

16. The Council has a Capital Programme Planning & Management Guide (the Guide) which was last reviewed in January 2018. It is aimed at Heads of Service and project managers and sets out a six stage Capital Programme Planning and Management Model as set out in Exhibit 2. Capital monitoring is included in Stage 6 of the model.

Exhibit 2 – Six Stage Capital Programme Planning and Management Model



17. The aim and purpose of the Guide is to:

- set out the capital programme planning and management arrangements
- clarify links with existing Council processes
- define roles and responsibilities for governance, management and implementation
- provide detail on processes and procedures to be followed in making the arrangements a success.

18. The Guide has not been revised since 2018 and requires a review to ensure it reflects current working practices. However the Council is currently developing a new Capital Strategy which is to be presented to the Policy and Resources Committee in August 2021. We recognise that a review of the Guide should be conducted after the Capital Strategy has been finalised to ensure the two documents complement each other and avoid unnecessary repetition. The Guide could also benefit from being linked to, or referencing, other relevant Council processes, in particular the Project Management section on the Hub.

Action Plan 1

19. A review of the Guide found it to be consistent with the Council's Financial and Security Regulations and that it is aligned to the Capital Strategy Checklist set out in CIPFAs Prudential Code for Capital Finance in Local Authorities and to Audit Scotland's Good Practice in Capital Monitoring Guide and Checklist.
20. Financial Services have taken steps to update and enhance the capital monitoring and reporting process including engaging with elected members and some officers involved in project monitoring. In particular:
 - an elected members seminar in February 2018 focusing on the Capital Plan
 - a further elected members session in August 2019 focusing on the format and content of the capital monitoring reports
 - a group development session with Roads and Amenity Services officers focused on the capital monitoring spreadsheet which informs capital monitoring reports
 - improved engagement at Strategic Asset Management Board where the Capital Plan position is presented and representatives from all services are given the opportunity to provide feedback or discuss issues. Historically Services provided their own individual updates which did not give an overall position of the programme and how their own areas of responsibility feed in to that.
21. As a result of these engagements the capital monitoring spreadsheet and capital monitoring reports have been amended.
22. Although there is no specific capital monitoring training programme, through discussions with officers, we confirmed that one to one engagement has taken place with other project managers during the process of completing the capital monitoring spreadsheet. Consideration should be given to the development of a cross service training programme aimed at officers who are involved in the management of the Council's capital projects to help ensure there is a consistent and robust approach to capital monitoring. It would be beneficial to engage with the various programme managers to identify where they feel training should be focused.

Action Plan 2

Capital monitoring procedures are consistent with established procedures.

23. Financial Services prepare a budget pack which is presented to full Council as part of the annual budget setting process in February. This includes the capital plan with the budget papers detailing the revisions proposed to the plan and recommending it be extended by a further year as it is a three year rolling plan.
24. The capital monitoring process involves Financial Services issuing a capital monitoring spreadsheet to all project managers requesting them to complete it by a specified date. Project managers are expected to provide comment on any issues, update the forecast spend and provide details of any slippage or acceleration of spending.
25. Financial Services monitor the return of these spreadsheets and follow up non returns and query those returned with either no comment or insufficient comment. This follow up can take various form, ranging from meeting requests, emails and calls to project managers or the project team contact.
26. Financial Services consolidate the returns to prepare a capital monitoring report which is presented to the Strategic Management Team (SMT) on a monthly basis and as a standard

agenda item to each meeting of the Policy and Resources Committee (except the May meeting). In particular the report highlights:

- financial indicators
 - i. planned current year spend and forecast spend for next two years
 - ii. year to date actuals vs budget spend
 - iii. total project spend
 - iv. details of slippage and acceleration
- non-financial indicators
 - i. comments and explanations for major variances for project which are 'off track'
 - ii. high level indicators of benefits expected; deliverability of project and project risks (traffic light system).

Profiling of capital projects is based on a robust process and regularly reviewed

27. To establish how project managers carry out capital monitoring we liaised with three project managers who manage, between them, 71 of the 151 projects contained in the Council's capital plan. These projects are split across three categories (Asset Sustainability, Service Development and Strategic Change).
28. The project managers questioned all complete the capital monitoring spreadsheet however the information used by them and the way they monitor projects differs. This may be due to the different project category but also the resource or departmental support available to enable them to carry out the financial monitoring and complete the capital monitoring spreadsheet. Across the three project managers interviewed:
- Piers and Harbours have a finance contact who supplies six detailed reports monthly and three departmental staff who are involved in aspects of monitoring multiple projects.
 - The CHORD team receives year to date transaction reports from Financial Services and run their own reports from other systems. The team use their own spreadsheets to monitor what are complex projects with multiple funders.
 - The Customer Services Property Design Manager runs his own reports and updates his own spreadsheets.
29. These varying approaches are not consistent with the Project Management Section on the HUB, which states:
- “project managers can have access (depending on the type of project) to three separate financial reports. These 3 financial reports used in conjunction with the Project Budget spreadsheet provide sufficient financial control for all but the very largest of projects.
- Payroll Report: allows you to check the project team payroll and expenses costs
 - Financial Summary: provides all the information needed to check the project's budget and spends (for a given project cost centre)
 - Transactions Report: Provides an itemised breakdown of all transactions for a given cost centre; most useful for managing Capital budget.”
30. Payroll reports are circulated by Financial Services Consolidated Team and the Financial Summary reports are provide by the Financial Services capital team. Whilst the Transactions

Report is not routinely circulated it is available on request it can be run by the project team if they have access to Oracle Discoverer. It would be beneficial if the revised Guide was clear about the reports which are provided to project managers and what additional information can be provided on request to minimise the risk that financial information reported in capital monitoring reports is inaccurate.

Action Plan 1

31. The email issued by Financial Services with the capital monitoring spreadsheet asks project managers to check the current profile spend is up to date and amend this where necessary, providing explanations for any in year variances and for slippage or acceleration of spend to and from future years profiled spend.
32. Financial Services hold records of virements, slippage and acceleration and this information is included in the Capital Monitoring Report presented to SMT and the Policy and Resources Committee.
33. Virements to the capital budget can arise at the following levels:
 - between projects within a service
 - between services within a department
 - between departments.
34. Virements up to £200k can be approved by an Executive Director and anything over £200k must be approved by the Council. Our continuous monitoring programme confirmed that seven capital virements requests were raised in 2020/21 with all seven included in the capital monitoring report presented to and approved by the Business Continuity Committee in August 2020.
35. The capital programme is constantly changing throughout the year as new projects and funding streams are added and expenditure profiles are updated to reflect projected spend patterns. Consequently it can be difficult to accurately identify the total amount of capital slippage in any one year however over the past three years slippage levels have been approximately £20.5m in 2018/19, £17.5m in 2019/20 and £26.4m in 2020/21. Note that the 2020/21 slippage was partially due to the impact of COVID.
36. Whilst this will include 'true' slippage for example due to delays in supply of materials, weather disruptions or issues with contractors, it is also very likely that an element of it is due to inaccurate profiling of spend within capital projects. We are not able to distinguish between 'true' slippage and slippage due to inaccurate profiling.
37. Inaccurate profiling can have financial implications for the Council as forecasted capital expenditure influences treasury management decisions on required levels of borrowing. By way of illustration if the Council borrowed £20m over 32 years at a rate of 5.1% (these were the average amounts used in the Council's recent loans fund review) it would cost £1.28m per annum in interest payments.
38. In order to improve capital profiling it would be beneficial to include this as a topic to be considered in the training referenced in paragraph 22. There would also be benefit in including guidance on it when the Guide is updated after the Capital Strategy has been updated.

Action Plan 1 and 2

Capital expenditure is monitored in line with budget monitoring arrangements and reported regularly to relevant officers and elected members.

39. Capital monitoring is reported at a number of different levels including:

- Departmental Management Teams (Project Managers)
- Argyll and Bute Harbour Committee (Project Managers)
- Area committees (Project Managers)
- Strategic Management Team (Financial Services)
- Strategic Asset Management Board (extract only) (Financial Services)
- Policy and Resources Committee (Financial Services).

40. A review of reports against each of the bodies noted above confirmed all bodies receive reports which are consistent with the responsibilities/requirements of each body. The information provide by Project Managers is broadly consistent with that reported by Financial Services. The difference can be timing issues where a verbal update on figures would be provided, or can relate to the decisions that Members are required to make as is the case with the Argyll and Bute Harbour Committee who set the fees and charges.

Appendix 1 – Action Plan

	No.	Finding	Risk	Agreed Action	Responsibility / Due Date
Medium	1	<p>Capital Programme Planning & Management Guide</p> <p>The Council’s Capital Guide has not been revised since 2018 and requires a review to ensure it reflects current working practices and provides appropriate support to officers involved in the capital monitoring process. The Council is currently developing a new Capital Strategy which is to be presented to the Policy and Resources Committee in August 2021 and we recognise that a review of the Guide should be conducted after the Strategy has been finalised to ensure the two documents complement each other and. The Guide could also benefit from being linked to, or referencing, other relevant Council processes, in particular the Project Management section on the Hub.</p>	There may be an inconsistent approach to capital monitoring and a lack of available support for officers available in the process.	Capital Planning and Management Guide to be updated once the Capital Strategy has been approved to ensure the two are aligned and provide clarity.	Head of Commercial Services/Finance Manager 31 March 2022
Medium	2	<p>Capital Programme Training</p> <p>There is no training programme to support officers involved in the management of the Council’s capital programme. It would be beneficial to engage with project managers to identify training needs and address these through the development of a training programme to help ensure a consistent and robust approach to capital project management. In particular this should include training on capital project profiling.</p>	There may be an inconsistent approach to capital monitoring and inaccurate profiling may result in best value not being achieved in through treasury management activity.	Training documentation to be created that project managers can refer to. Refresher training to be provided for existing Project Managers and a plan put in place for training for any new staff that have capital budget monitoring responsibilities.	Finance Manager 30 June 2022

In order to assist management in using our reports a system of grading audit findings has been adopted to allow the significance of findings to be ascertained. The definitions of each classification are as follows:

Grading	Definition
High	A major observation on high level controls and other important internal controls or a significant matter relating to the critical success of the objectives of the system. The weakness may therefore give rise to loss or error.
Medium	Observations on less significant internal controls and/or improvements to the efficiency and effectiveness of controls which will assist in meeting the objectives of the system. The weakness is not necessarily substantial however the risk of error would be significantly reduced if corrective action was taken.
Low	Minor recommendations to improve the efficiency and effectiveness of controls or an isolated issue subsequently corrected. The weakness does not appear to significantly affect the ability of the system to meet its objectives.

Appendix 2 – Audit Opinion

Level of Assurance	Definition
High	Internal control, governance and the management of risk are at a high standard. Only marginal elements of residual risk have been identified with these either being accepted or dealt with. A sound system of control designed to achieve the system objectives is in place and being applied consistently.
Substantial	Internal control, governance and the management of risk is sound. However, there are minor areas of weakness which put some system objectives at risk and specific elements of residual risk that are slightly above an acceptable level and need to be addressed within a reasonable timescale.
Reasonable	Internal control, governance and the management of risk are broadly reliable. However, whilst not displaying a general trend, there are a number of areas of concern which have been identified where elements of residual risk or weakness may put some of the system objectives at risk.
Limited	Internal control, governance and the management of risk are displaying a general trend of unacceptable residual risk above an acceptable level and placing system objectives are at risk. Weakness must be addressed with a reasonable timescale with management allocating appropriate resources to the issues raised.
No Assurance	Internal control, governance and the management of risk is poor. Significant residual risk and/or significant non-compliance with basic controls exists leaving the system open to error, loss or abuse. Residual risk must be addressed immediately with management allocating appropriate resources to the issues.