Auditor: Amber Ahmed, Ext 3280

Final Internal Audit Report

to

- **Dr Grace Vickers, Chief Executive**
- **John Blair, Director, Resources**
- **Garry Sheret, Head of Property Facilities and Management**
- **William Jackson, Building Services Manager**
- **Greg Vettraino, Capital Contracts Manager Major Works**

on

Social Housing Programme – Phase 2

12 September 2018

1   Introduction

1.1   The purpose of the audit was to review the adequacy of the capital investment control framework established by Management to allow for the successful delivery of the Social Housing Programme.

2   Audit Scope

2.1   The scope of this audit was to focus on Phase 2 of the programme and reviewed the key capital investment processes and controls designed by Management to allow the social housing project to be delivered within cost, timeframe and to the required quality standards. This included a review of the management and control of the following areas:

- project cost, timeframes and quality of build;

- contractors, suppliers and consultants; and

- change, variations and post completion sheets.

3   Management Summary

3.1   The Council commenced a Social Housing Programme with the initial developments delivered from 2006. Phase 1 of the Social Housing Programme delivered 864 houses over a period of 7 years with a total budget of £108.7m and was completed in 2012. The Council is aiming to build a further 1,000 homes by 2022. Phase 2 of the Social Housing Programme is targeted to provide 428 homes with an original budget of £63.663m, funded from the Housing Revenue Capital Account.

3.2   The Council has approved a further 2 Social Housing programmes (Phase 3 and 4) which will follow on from Phase 2. Phase 3 was approved in December 2015 and is envisaged to deliver around 240 homes, to be constructed from a budget of £36m. In June 2017, additional funding from the Scottish Government was approved making the revised budget for Phase 2, £77.121m and Phase 3, £42.208m. Phase 4 was approved in February 2018 with a budget of £94.050m for social housing and £6m for Temporary Accommodation.

3.3   Whilst Phase 1 of the programme was implemented via frameworks for contractors and external design teams, in Phase 2 the Council adopted a design and build contract procurement route. The award of contracts for each separate build in Phase 2 was procured and awarded to two contractors through the housing construction framework. In order to attract more contractors to tender for Phase 3, each site is being tendered separately.

3.4   The following examples of good practice were found:

- Progress reports are reported to Cabinet/Council every 6-12 months and the Service now have regular meetings with Councillors to report on the progress made on housing projects;

- There is a monthly tracking on cost reports against the budget allocated to each site and the Head of Property Facilities Management receives monthly cost and progress reports;

- The design and build procurement approach provides certainty over costs and transfers many of the risks, such as the design, to the contractor who is best placed to manage them; and

- Issues were identified by Management with the inspection undertaken by the Clerk of Works on the complex care home. A Clerk of Works is now employed by the Council to check standards of workmanship and specifications are in accordance with the contract.

3.5   Improvements are required for: audit trails – ensuring that documentation is complete and easily accessible for each housing project; the controls for verifying variations; contract management documentation – ensuring all required documentation is completed appropriately; and the quality checking of progress reports to ensure they are accurate and complete.

3.6   Although the delivery of the Social Housing Programme is off target, in the main due to factors outwith the control of the Council, the controls in place to monitor and report on this are satisfactory. Internal Audit considers that the level of assurance we are able to give is Substantial Assurance.

3.7   The Internal Audit function conforms with the professional standards as set out in the Public Sector Internal Audit Standards (2017), including the production of this report to communicate the results of the review.

3.8   We would like to thank those officers who assisted us during our review.

4   Findings

Risk	Expected Control	Results	Effectiveness of Actual Control	Rec. Ref
4.1 Financial loss or reputational damage through the project not delivering affordable housing, not being delivered to original cost, to agreed timescales or to an acceptable quality	Project costs, timeframes and quality of build are adequately monitored by Management	**Timeframes** There is a risk of not achieving the target to provide a further 1,000 new builds by 2022 as the Phase 2 and 3 projects are off target. This risk was highlighted in the March 2018 progress report to Cabinet/Council. The target for Phase 2 was to complete 400-450 homes by the end of December 2017. The number of homes built at the end of December 2017 was 264 - 10 sites have been completed and 3 are still outstanding. Phase 2 is now expected to be completed by October 2019 which indicates a slippage from the original target of December 2017. In September 2016, it was reported that tendering for Phase 3 sites was to commence in October 2016 and the earliest potential construction start on site will be September 2017. However, this was delayed and the tendering for Phase 3 did not commence until March 2018 - 5 Sites have since been tendered. Management advised that there have been issues identifying sites for new builds and it will be necessary to acquire further land for development and/or develop Council owned surplus open space. In addition to this, it is proposed to purchase completed houses from external developers as an additional procurement route.	Satisfactory controls in place though programme timescales not being met due to lack of availability of sites/external factors	
		Progress Reports Six monthly progress reports are reported to Cabinet/Council detailing anticipated completion dates for each project. The progress reports do not highlight any changes from the original target or detail why sites have moved from one phase to the next (e.g. site 109 changing from phase 2 to 3 and site 23 moving from phase 3 to phase 2). Additional funding was received from the Scottish Government in June 2017, making the overall total budget for Phase 2, £77.121m. However, progress reports reported after this date did not include the revised budget. An error was identified in the March 2018 progress report. The progress report indicated that total builds from Phase 2 would be 419 but actual is 428 as one site had changed from 70 to 79 units. Management have advised that officers preparing the report altered the site numbers but forgot to change the total figures.	Satisfactory	5.1

Risk	Expected Control	Results	Effectiveness of Actual Control	Rec. Ref
		Cost reports Cost reports for each project are generated monthly by the Project Manager however the Integra report could not be reconciled to the cost reports. There was a lack of information to verify the figures in the cost reports and, in some cases, figures were just noted in the reports with no supporting documentation or calculations.	Satisfactory	5.2
		Audit trails Documentation required for audit testing was not always readily available and there was not always a complete audit trail for each housing project.	Satisfactory with a few exceptions	5.3
4.2 Financial loss or reputational damage through mismanagement of contractors, suppliers and consultants	Management regularly monitor the controls in place over the management of contractors, suppliers and consultants	**Contract Management Documentation** 13 sites from Phase 2 were competitively tendered; however for 2 of these sites additional construction work was undertaken and specialised art work was purchased but a Non-Competitive Action (NCA) form was not completed to explain why the main contractors were not used.	Satisfactory - subject to completion of NCA where applicable	5.4
		For 1 site, there was a change made on a tender document but this was not formally documented in a revised tender report.	Satisfactory – subject to update of tender document	5.5
		A final account is issued at the end of each project after costs have been agreed by all parties. For 1 site, the project was completed in 2013 yet the final accounts have not been completed due to a dispute with the contractor regarding solar panels. It is noted that accounts will not be finalised until issues regarding defects are resolved.	Satisfactory	N/A
		Collateral warranties are provided by the Contractor as part of agreeing costs for the construction work undertaken on a site. For 1 site, a practical completion was signed in 2015 but collateral warranties have not been obtained from the Contractor despite various reminders. This is an ongoing issue and a sum of £20k has been withheld from the Contractor until the collateral warranties are provided.	Satisfactory	N/A

Risk	Expected Control	Results	Effectiveness of Actual Control	Rec. Ref
4.3 Poor change control / variation procedures can result in financial loss and /or fraud	There are adequate controls in place over changes, variations and post completion sheets	**Variations** Pre-variations that occur during site investigations are listed in a tender reconciliation report and are presented to the Head of Property and Facilities Management before the contract sum is agreed to show the variations between the tender sum and contract sum. Testing revealed that there was a lack of change control / variations documents showing appropriate authorisation and 1 tender reconciliation report was missing. It was also noted that cost reports detailing variations were sometimes unclear.	Satisfactory	5.6
		Insurance of Buildings A new complex care home was opened in July 2017; however the insurer was not advised of its existence until December 2017 due to a miscommunication between departments. The insurance has been backdated to July 2017 after the insurer confirmed with the Council that no incidents had occurred during the uninsured period.	Satisfactory subject to checklist / prompt list being used to evidence	5.7
		Post Completions checks Practical Completion certificates are signed by the Project Manager at the time of handover who checks to ensure various professionals have complied with relevant building and health and safety requirements. However, it was noted that there is no checklist or prompt list to evidence this.	Satisfactory subject to checklist / prompt list being used to evidence	5.7

5　　Action Plan

Rec. Ref No	Recommendation	Rating	Management Response	Responsibility and Timescale
5.1	Quality Assurance checking of progress reports should be undertaken to ensure they are accurate and complete.	**Medium**	Initial indicative forecasts and budgets do change over time, especially with large and complex projects. Whilst there are risks, the Service continually work to overcome these and mitigate the risk. Budget figures will be updated in the progress reports. Quality checks are and have always been taken. Whilst some typos and a computational error were discovered, these can occur even with checking. Normally at least two senior staff members check reports and any official report or calculations/documentation should have a peer review from a construction colleague prior to issue. The reports are also issued to the Head of Property and Facilities Management and Head of Customer and Housing Services.	Capital Contracts Manager Major Works **Complete**
5.2	Costs incurred to date should reconcile with the expenditure on the Integra system and forecast figures should be supported with appropriate documentation.	**Low**	Cost reports can make allowances and may not always reflect exactly what is in Integra and in some instances Officers had not always updated cost figures from Integra. Predicted fees are updated to reflect the actual construction cost on the issue of the final certificate. Whilst there have been oversights, staff need to be more diligent and this has already been stressed. Variances from Integra that were picked up were generally included in the reports but were just not cross referencing exactly. Training has been provided to staff and guidance has been improved in report templates for future reports.	Capital Contracts Manager Major Works **Complete**

Rec. Ref No	Recommendation	Rating	Management Response	Responsibility and Timescale
5.3	Management should ensure documents are readily available and there is a clear audit trail for each housing project.	**Low**	For the most part, documentation was readily available but the filing is extensive and takes time to search through. Each housing project has a separate file, file reference number and a separate cost code which establishes a clear audit trail. Whilst specific project management software would potentially help, the IT difficulties and costs involved would be prohibitive. We are considering adopting the Council's Document Management System (CS10) as housing projects are large and complex with multiple projects. However our test project is proving there are a lot of difficulties to be overcome. Transferring to CS10 may be trialled on some more projects first.	Capital Contracts Manager Major Works, by **September 2019**
5.4	Ensure a Non Competitive Action form is completed for occasions where competitive tenders / quotes are not obtained.	**Medium**	The quote for the additional work was provided by the contractor but the Project Manager obtained a cheaper quote from another contractor and did not have time to obtain 3 quotes due to the risk of delaying the construction work. Significant savings were made to the Council; however extra actions could have been taken to document the process. For the specialised art work, the Officer had been in discussions with Land Services and Planning colleagues and felt this was sufficient, not thinking to submit a NCA form. Staff should be aware of the need for NCAs and this requirement has been reinforced and will be reinforced again in staff training following receipt of the final Internal Audit report.	Capital Contracts Manager Major Works **Complete**
5.5	Any changes made on a tender document should be formally documented and reported with an explanation.	**Low**	Senior staff were fully briefed and aware on tender changes but it would have been better to have it formally reported.	Capital Contracts Manager Major Works **Complete**

Rec. Ref No	Recommendation	Rating	Management Response	Responsibility and Timescale
5.6	Variations should be noted in a control change document with appropriate authorisation. Variations should be clearly demonstrated on the cost reports.	**Medium**	Monitoring variations through the monthly cost reports was seen as a more efficient process of scheduling changes which are monitored by the Capital Contracts Manager, issued to the Building Services Manager and onto the Head of Property and Facilities Management (acting as the Senior Responsible Officer) who personally monitors cost variations. Post contract variations change controls are now in place. Pre-construction change controls have also been put in place.	Capital Contracts Manager Major Works **Complete**
5.7	A checklist or prompt list should be in place to outline what needs to be checked before practical completion is signed off and this should include insurance requirements.	**Low**	Whilst a checklist has been implemented, officers should have the knowledge and wherewithal to investigate and carry out the appropriate checks according to the latest requirements. Construction are not responsible for implementing insurance once a building is handed over. This is a client/user requirement. Housing Services arrange for properties to be added to the insurance register; however the Complex Care unit was considered as social housing and that occupants were tenants. Property & Estates services are normally informed of non-domestic completions and arrange the insurance. Processes are being put in place to prevent such re-occurrence and the Property & Estates service will manage this going forward and will be informed of all completed construction projects.	Capital Contracts Manager Major Works **Complete**

Overall Audit Opinion level and definition

Comprehensive Assurance	Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. Some improvements in a few, relatively minor, areas might be required.
Substantial Assurance	Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives or leave them vulnerable to error or misuse.
Limited Assurance	Risk, control, and governance systems have some satisfactory aspects. There are, however, some significant weaknesses likely to undermine the achievement of objectives and leave them vulnerable to an unacceptable risk of error or misuse.
No Assurance	The systems for risk, control, and governance are ineffectively designed and operated. Objectives are not being achieved and the risk of serious error or misuse is unacceptable. Significant improvements are required.

Recommendation Ratings

Recommendations in Internal Audit Reports are suggested changes to existing procedures or processes, to improve the controls or to introduce controls where none exist. The rating of each recommendation reflects our risk assessment of non-implementation, being the product of the likelihood of the risk materialising and its impact. The ratings are:

High	Significant weaknesses in existing controls, leaving the Council or Service open to error, fraud, financial loss or reputational damage, where the risk is sufficiently high to require immediate action within one month of formally raising the issue. The risk should be added by Management to the relevant Risk Register for control and monitoring purposes and included in the relevant Head of Service Annual Assurance Statement.
Medium	Substantial weaknesses in existing controls, leaving the Council or Service open to medium risk of error, fraud, financial loss or reputational damage requiring reasonably urgent action within three months of formally raising the issue.
Low	Moderate weaknesses in existing controls, leaving the Council or Service open to low risk of error, fraud, financial loss or reputational damage requiring action within six months of formally raising the issue to improve efficiency, effectiveness and economy of operations or which otherwise require to be brought to the attention of Senior Management.
Other	Minor administrative weaknesses posing little risk of error, fraud, financial loss or reputational damage.

The Action Plans in Internal Audit Reports address only Recommendations rated High, Medium or Low. Outwith the Internal Audit Report, we inform Service Management about Other Minor matters to improve internal control and governance.

The recommendations will be input to Pentana performance system to assist with Management tracking of implementation. If responsible owners are unable to achieve the standard timescales for actions please notify the Chief Internal Auditor with the reason for the delay in implementation and the revised timescales to assist with the implementation and follow-up of these recommendations to improve internal control and governance.

Jill Stacey
Chief Internal Auditor