



**Chief Internal Auditor
Jill Stacey**

Audit Committee
Tuesday 11 December 2018
Item No: 5.5

Auditor: James Polanski, Ext 5646

Final Internal Audit Report

to

**Director, Education, Communities and Economy
LEADER Programme Coordinator**

on

Tyne Esk LEADER Programme

1 November 2018

1 Introduction and Audit Scope

- 1.1 The purpose of the audit was to follow-up on the recommendations made in the 2017/18 audit of the Tyne Esk LEADER (Liaison Entre Actions de Developpement de l'Economie Rurale) Programme to ensure that the recommendations have been implemented adequately. This follow-up review contributes to the governance arrangements of the programme, helps ensure compliance with the programme's various reporting and administrative requirements, and forms the basis of our annual internal audit coverage of the programme for the period 16 October 2017 to 15 October 2018 as required by the Service Level Agreement (SLA) with the Scottish Government.

2 Management Summary

- 2.1 The Tyne Esk LEADER Programme is part of the Scottish Rural Development Programme (SRDP) aimed at promoting economic and Community development within rural areas in Midlothian and East Lothian. The SRDP is part of the EU Common Agricultural Policy and is funded by the European Commission and the Scottish Government. There are a total of 21 LEADER programmes established throughout Scotland, and each of these is governed by a separate Local Action Group. LEADER is a bottom-up method of delivering support to communities for rural development. Grants are awarded by Local Action Groups (LAGs) to projects that support delivery of a Local Development Strategy. For each LAG there is an Accountable Body to support the administration of the programme.
- 2.2 Midlothian Council is the Accountable Body for the 2014-2020 Tyne Esk LEADER Programme. Midlothian Council, as the Accountable Body, has delegated responsibility for a range of processing, payment, and administration functions as set out in the SLA. This includes all aspects associated with the implementation of the approved Local Development Strategy, such as the presentation, assessment and clearance of applications through the LAGs, and the subsequent approval and post approval case management functions.
- 2.3 Midlothian Council has received a funding allocation from the Scottish Government of £3,490,769 to administer a LEADER Programme throughout the rural areas of Midlothian and East Lothian, and funding is reclaimed from the Scottish Government after it has been defrayed. This programme will deliver the priorities set out in the Tyne Esk LEADER Local Development Strategy (LDS).
- 2.4 As at September 2018, 89% of the funding has now been allocated, with 68% allocated to projects and 21% of the fund forecast for administration costs up to completion of the Programme. Therefore, the focus of the LEADER programme has changed from project development and approval of grants, to project monitoring and claims processing.
- 2.5 In June 2018, the Scottish Government conducted their second Monitoring Wash-Up visit for Midlothian's LEADER programme. The monitoring visit was positive, recognised examples of good practice, and the Programme's RAG (Red / Amber / Green) status with the Scottish Government was updated from Amber to Green.
- 2.6 The 2017/18 LEADER Internal Audit Report included 16 recommendations to Management covering various aspects of the programme. These recommendations were accepted by Management, and plans were put in place by the LEADER Programme Coordinator to implement these improvement actions.

- 2.7 This audit identified that of the 16 recommendations made in the 2017/18 Internal Audit Report, 13 (81%) were completed satisfactorily, and further improvements were required for 3 recommendations (19%).
- 2.8 During the course of this audit, 3 recently awarded projects as well as 3 projects that had progressed to claim stage and completion were tested to gain assurance that the Internal Audit recommendations had been fulfilled in practice.
- 2.9 The following examples of good practice were found, addressing the previous year's internal audit recommendations:
- From the sample of projects reviewed, adequate steps are being taken to ensure that sufficient quotes are obtained before the project is approved and, where relevant, procurement tendering evidence is obtained to gain assurance of value for money;
 - Applicants are now required to submit with their quotes confirmation that the quotes received are different suppliers that trade as standalone businesses and are not linked through shared ownership to the applicant;
 - The backlog of claims to the Scottish Government has been addressed;
 - LARCS (Local Actions in Rural Communities System) is used to store all relevant project details, and this was evidenced in the sample of 3 projects reviewed. Evidence was seen of the change management function of LARCS being regularly used;
 - In Situ monitoring forms are authorised by the Programme Coordinator, and further advice is sought from specialists (e.g. Quantity Surveyors) for complex projects;
 - The 'Technical Check' form has been further enhanced to evidence review of project risks;
 - A review of minutes confirmed that the enhancements identified during the last review have been implemented, and projects scores were available for the sample reviewed; and
 - The LAG is now at the maximum membership capacity (16 members) enhancing the perception of the group's independence.
- 2.10 The 3 remaining previous Internal Audit recommendations that need to be implemented in full to further improve internal controls and governance arrangements are detailed in the Findings section below.
- 2.11 The follow-up audit work on the implementation of improvement actions and the carrying out of audit testing of the sample projects against the enhanced practices has enabled Internal Audit to provide Substantial Assurance of the continued observance of the Council to the requirements of the Programme.
- 2.12 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.
- 2.13 We would like to thank those officers who assisted us during our review.

3 Findings

Original Rec No	Original Recommendation	Findings	Rec. Ref No
2	Reasonableness of Costs / Value for Money statements should be completed for all projects and the final signed version of this document should be uploaded to LARCS.	<p>A sample of 3 projects were reviewed. It was noted that a Reasonableness of Costs / Value For Money (RoC) statement was in place for each project and were saved in LARCS.</p> <p>It was identified that for 1 of the projects, the document was a Microsoft Word file (i.e. it was not signed by the applicant), and for 1 RoC the applicant's signature appeared to be copy / pasted into the document. Ideally, this form should be physically signed by the applicant or be signed via a secure digital signature, as the RoC form is verification from the applicant that they are not connected to the companies that will be used in the project.</p>	4.1
6	A process should be developed to evidence the comparison between the project application costs and the claims costs to support the prepayment checklist and ensure that the breaches and penalties rules do not need to be applied.	<p>Although it is clear that claims are monitored through the completion of the 'Claims Evidence List' form and the Prepayment Checklist, these forms do not specifically evidence the comparison of claim items directly with the items detailed in the RoC and the project application. The costs of different milestones are input in LARCS providing overall cost monitoring, but this does not evidence the comparison of supplier, item description, or sometimes the sub-cost components of the milestone (as detailed in the RoC and application).</p> <p>For complex capital projects additional monitoring is in place. This includes reports from the applicant's quantity surveyor, or further checks by a surveyor coordinated by the LEADER team if no quantity surveyor is employed by the applicant for the project.</p> <p>For the 3 projects reviewed, it was noted the audit trail could be further improved to evidence the check between the RoCs and the claims. This was particularly relevant for 1 project which was made up of a significant number of smaller purchases as some of the expenditure detailed in the RoC had not been claimed for at the project's completion, and this potentially exposes the project to a clawback of funds via the breaches and penalties rules.</p>	4.2
10	Management should clarify within the Technical Check whether what the applicant has supplied in terms of insurance is acceptable as it is understood that the evidence requirements will vary from project to project.	<p>Insurances had been obtained for 2 out of the 3 projects reviewed. The Technical Check form has been enhanced to detail the types of insurances submitted. However, it was noted that the check did not provide a specific explanation as to why insurances had or had not been obtained.</p> <p>The project that had not received confirmation of insurances was discussed with the LEADER Programme Coordinator and it was his view that as this was not a capital project, or a project where staff were immediately to be employed, it was not necessary to verify insurances. However, as some significant equipment purchases were being made for this project confirmation of contents insurance should have been obtained.</p>	4.3

4 Recommendations

Rec. Ref No	Recommendation	Rating	Management Response	Responsibility and Timescale
4.1	Reasonableness of Costs / Value for Money statements should be signed by the applicant for all future projects	Low	Agreed.	LEADER Programme Coordinator by 31 December 2018
4.2	The process should be further developed to evidence the comparison between the project application costs and the claims costs to support the prepayment checklist and ensure that the breaches and penalties rules do not need to be applied.	Medium	Agreed.	LEADER Programme Coordinator by 31 December 2018
4.3	Management should clarify within the Technical Check whether what the applicant has supplied in terms of insurance is acceptable as it is understood that the evidence requirements will vary from project to project. This includes an explanation if it is thought insurance submissions are not necessary for the project.	Low	Agreed.	LEADER Programme Coordinator by 31 December 2018

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:

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| 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