

MANCHESTER CITY COUNCIL

COMMITTEE: Audit Committee
DATE: 14th March 2008
SUBJECT: Statement of Internal Control – ERDF Grant
FROM: Deputy Chief Executive (Regeneration)

PURPOSE OF THE REPORT

The purpose of the report is to update the Committee on the further actions that were agreed to when the Committee last considered contingent liabilities related to ERDF grant in September 2007.

RECOMMENDATION

Members are recommended to:

- 1) Note and comment on the content of the report

FINANCIAL CONSEQUENCES FOR THE REVENUE AND CAPITAL BUDGETS

None directly.

BACKGROUND REPORTS

Annual review of Internal Control – Report of the City Treasurer to the Audit Committee, 1st June 2006

Statement of Internal Control – ERDF Grant – report of the Deputy Chief Executive (Regeneration) to the Audit Committee, 22nd March 2007

Statement of Internal Control – ERDF Grant – report of the Deputy Chief Executive (Regeneration) to the Audit Committee, 28th September 2007

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1.0 Introduction

- 1.1 In March 2007, a report was considered by Committee which set out proposals for the Deputy Chief Executive (Regeneration), in conjunction with Internal Audit, to review the arrangements for ensuring compliance with ERDF grant conditions to determine whether any additional measures were required. Audit Committee members will recall that, at the September 2007 meeting, the Committee noted the first phase of that on-going work in relation to the systematic review of ERDF project files. Committee requested a further report in March 2008 to provide an update on the second stage of the process. In addition, the Committee requested that officers include in this report an assessment of the resource implications involved in undertaking this exercise.

2.0 Statement of Internal Control – Agreed Actions

- 2.1 Audit Committee members will recall that, at the June 2006 meeting, in light of the draft EC 1997-99 ERDF audit findings, the Deputy Chief Executive (Regeneration) agreed to review the arrangements and procedures for ensuring compliance with ERDF grant conditions for current projects ie. all those projects in the 2000-2006 ERDF Programme. To this end, Internal Audit were commissioned to carry out sample testing of current ERDF projects to assess the levels of risk.
- 2.2 Within the 2000-06 ERDF Programme, Manchester City Council is the accountable body for 140 projects totalling £80.221m of ERDF grant across three action plans – North and South; Housing Market Renewal and New East Manchester.
- 2.3 All projects have been issued with a Blue File which provides clear guidance on the terms and conditions of grant funding and sets out a clear basis for the retention of key documents relating to project management, i.e. records of expenditure, records of procurement processes followed, evidence to demonstrate the achievement of target outputs and so on. If complied with, this Blue File project information management system will provide a robust framework for demonstrating compliance with ERDF grant terms and conditions. This view has been endorsed by Internal Audit.
- 2.4 Members will recall that the initial investigation of the control systems used to manage ERDF projects found that there were robust and appropriate policies in place and, if followed, should ensure proper management of project compliance. However, this investigation revealed a wide-ranging inconsistency in the application of these procedures and identified weaknesses in the records management relating to a number of projects. Arising from this work, a number of actions were agreed including a review of all 140 2000-06 ERDF Project Files, developing a more effective model of financial and programme management and addressing wider project management risks. Progress on all matters was reported in September 2007 and this report now outlines the second stage work of the review of ERDF Project files.

3.0 Review of Project Files and Other Work to Date

- 3.1 The review of ERDF project files started in February 2007 with the Regeneration Programmes Group (RPG) issuing clear instructions and timetables to all project officers clearly setting out the requirements and timescales for the submission of complete project files for review.
- 3.2 As previously agreed with this Committee, up to September 2007, the testing of project file completeness covered at the time all of the ERDF projects operating outside of the New East Manchester area (70 North and South and HMR Projects) plus a sample of 13 projects from within the New East Manchester (NEM) programme. A risk assessment was undertaken to select these 13 projects. As NEM is managing such a large number of ERDF projects (it was 69 at the time and is currently 67), it was agreed that this sample of 13 would initially be completed followed by full project file testing ahead of the March 2008 meeting of this Committee.
- 3.3 To date, a total of **138** projects in receipt of over **£79.521m** of ERDF grant have had their project records tested for completeness in accordance with grant funding and MCC record keeping requirements – **83** between March and September 2007 - which were the subject of the Committee Report on 28th September - and **55** (which comprises 52 NEM projects and 3 other) since October 2007. The remainder of this section concentrates on the remaining 55 projects.
- 3.4 These **55** projects represent **£19.907m** of the total ERDF checked. This exercise has demonstrated that managers across the Council and at NEM Ltd are committed to working through this process and demonstrating that their project records are being maintained to the required standards of completeness. Two NEM projects have not yet been checked as the records are held in locations away from Manchester and officers have not been able to validate the project files onsite yet.
- 3.5 Of the **55** projects tested since October, **41** have been found to contain all of the information required to provide a full auditable account of the delivery of the project. These **41** projects account for **£13,453m** of ERDF grant from a total of **£19,907m** tested since September 2007. With regard to the **14** projects found to have gaps within their files, work is ongoing to ensure that the responsible project officers trace relevant documentation to complete the files and that the completeness is subject to verification by officers from the Regeneration Programmes Group of the City Council.
- 3.6 Of these **14** projects, **9** (total ERDF value **£4.154m**) are delivered by external, non-MCC applicants. The City Council's risk is limited in these cases as any grant clawback claims made in respect of these projects against the City Council in its role as Accountable Body, would in turn be passed on to the project delivery body. These organisations will all receive a letter from the Council setting out what gaps have been found and the clawback implications for those organisations if those gaps are not filled.
- 3.7 The **5** MCC delivered projects (total ERDF value of **£2.299m**) which have been found to contain information gaps will now be subject to further

detailed testing and follow up checks to ensure that these gaps are filled and risks are lessened. Members should note that all **5** MCC projects identified as having some gaps in information are closed projects which have been through various audit and verification processes. This suggests that these gaps in information may be addressed through an administrative process to get the files back up to full completeness by accessing the required records (e.g. payroll) from elsewhere within the Council.

- 3.8 In order to provide the Committee with as accurate and complete picture as possible, staff will continue to work on the files over the coming weeks and a verbal update on further progress since this paper was written will be given to the Committee when it meets on the 14th March. In addition, Regeneration Programmes Group will continue to work with NEM Ltd to ensure that all files are fully populated and presented for verification over the coming months. A further report on this work, along with reports on the wider qualitative testing referred to in Section 4 can be made available should the Committee wish.
- 3.9 As a result of the processes outlined above, the view of Internal Audit is that senior managers within Regeneration recognise the improvements needed to reduce the exposure to risk and are actively addressing the improvements, particularly in respect of ownership, management controls, formal protocols, guidance and training. These actions should help to improve the control environment and provide an increased level of assurance.
- 3.10 The Committee meeting in September 2007 requested an assessment of the resource implications involved in undertaking this exercise. The work has been completed without the use of external consultancy or other services and has been entirely supported through the use of mainstream and grant funded staff resources. The Regeneration Programmes Group, a mainstream resourced team, has led the work at a time when the current ERDF programmes are moving to closure (due to complete in December 2008 – March 2009). This means that this type of assurance and closure work is consistent with the expected work programme for the Group at this time. Whilst the demands of the work have been considerable and have required that staff work together effectively across teams, departments and partnerships, to often conflicting deadlines, the work has been managed without detriment to other work programmes and without the need to incur any additional costs to the authority.

4.0 Other Actions

- 4.1 As part of the ongoing work agreed with Audit Committee, further testing of the quality and robustness of the information held on ERDF files is already underway and is being delivered with the support of the Head of Internal Audit, City Solicitor's and Head of Corporate Procurement who have all agreed to lend their support and respective expertise in helping to test project compliance with relevant EC Directives. Details of future planned actions are set out in the remainder of this section.

- 4.2 As previously reported, with Internal Audit, the Deputy Chief Executive (Regeneration) has put in place a process of self assessment and checks going forward to ensure that completed projects files re-tested now remain complete for the duration of the audit / clawback risk. This process is well underway and, consistent with the closure timetable for the current ERDF programme, will be complete by March 2009.
- 4.3 In addition to the completion of the project file review work, the Regeneration Programmes Group will continue to test the robustness of the project file records in terms of compliance with grant funding terms & conditions. This work is underway and assessing possible future audit risks and identifying any higher risk projects requiring further assessment. Given the size and complex nature of some of the ERDF funded projects that have been delivered in Manchester during this current programme, expertise from within the Council will be required to make risk assessments and test these projects for compliance with grant and EC rules, especially around procurement and input from both the Head of Corporate Procurement and Head of Regeneration (Legal) in City Solicitor's over the next 12 months has been agreed.
- 4.4 Members will recall from previous reports to this Committee that the audit of the 1997-1999 was the most rigorous audit yet undertaken by the EC in the region and that the auditors predominantly focused on project compliance with EC Public Procurement Directives. The emphasis on compliance with these Directives remains a high profile issue for the EC and it is expected that any closure audit of the current ERDF programme which is due to end with the submission of final claims to the EC in Spring 2009, will again focus on procurement and an allied competitiveness issue, that of State Aids.
- 4.5 As the current programme of ERDF funded projects in Manchester has seen a great deal of ERDF investment in large scale capital projects, predominantly in the New East Manchester area, there will be a need for more detailed testing of project compliance with these EC Directives and, given these complexity associated with these issues, additional support will be secured from within, and if necessary, brought in from outside of the Council.
- 4.6 Finally, as set out in the Internal Audit Plan submitted to Audit Committee on 29th June 2007 officers in Regeneration Programmes Group will continue working closely with Internal Audit during the remainder of 2007/08 and into 2008/09 in testing the quality of project information.

5.0 Conclusion

- 5.1 It is vital that project managers continue to adhere to the framework in place in relation to the Blue File system as future audits will focus on similar issues to those identified in the 1997-99 Programme. Thus, the ongoing risk is clearly identified in the Regeneration Business Plan. Good progress has been made in ensuring that project files are up to date and this work will continue over the next few months. Further work on the quality and robustness of the information in project files coupled with the completion of a

self-assessment process that provides some assurance on the continuing completeness of files will be essential in reducing the risk to the Council, as will ensuring clear lines of accountability which ultimately rest with project managers.

- 5.2 It should be noted that risk can never be completely eliminated whilst the Council and its partners are utilising external grant resources to deliver complex projects via a range of delivery routes. However, the measures set out in this report seek to provide assurance to the Council that steps are being taken to minimise this risk.

6.0 Recommendations

- 6.1 Members are requested to note and comment on the content of the report.