



## **Internal Audit Report**

### **Resources**

## **Ring Fenced Funding**

**Issued to:**

Steven Whyte, Director of Resources  
Jonathan Belford, Chief Officer – Finance  
Fraser Bell, Chief Officer – Governance  
External Audit

## **EXECUTIVE SUMMARY**

In 2019/20, the proportion of the overall block grant which was ring-fenced by the Scottish Government was £30.6 million - 8.1% of the total grant settlement for the year of £380.57 million. The objective of this audit was to provide assurance that the Council has appropriate arrangements in place to ensure that conditions relating to ring-fenced funding within the Scottish Government Grant are complied with.

Grants are generally administered in line with the Council's Scheme of Delegation including powers delegated to officers, Financial Regulations and Procurement Regulations. There are no separate written procedures, though individual grants are subject to specific terms and conditions set out in award letters. This has led to some variation in practice. Finance has agreed to develop procedures to increase assurance that grants are being administered in line with best practice – including nominated lead officers, development of a comprehensive grants register, and improved documentation to evidence that all and only appropriate spend has been attributed to relevant grants.

The timing of grant announcements and time limits on their use can cause difficulties in planning implementation and associated budgets. Finance has agreed to review procedures to ensure decision making can be adequately supported within appropriate timescales. Finance considers that the Council's Medium Term Financial Planning, including the annual Budget, is developed and updated based on the best information available. This includes the incorporation of assumptions about anticipated changes in funding, and any new information, including proposals for mainstreaming. If any recurring funding were to be discontinued a review would need to be undertaken of the future level of service being provided, and this would be factored into financial planning.

# 1. INTRODUCTION

- 1.1 The Scottish Government announces its funding package for local authorities each year in Local Government Finance Circulars. These typically detail funding which the Scottish Government indicates makes up approximately 85% of local authorities net revenue expenditure. It has three parts: General Revenue Grant, Non-Domestic Rates Income, and Specific Revenue Grants – commonly known as ‘Ring-Fenced Funding’. The Circular also details the values of Specific Capital Grants which have been allocated to local authorities for the coming financial year.
- 1.2 Both types of Specific Grant must be used in accordance with conditions stipulated in Grant Offer letters provided to each council. The letters are issued each year by Scottish Government Policy Teams and detail the extent of the offer, purpose of the grant, qualifying expenditure, payment arrangements, and reporting requirements. Specific Grants (referred to hereafter as ‘grant’ or ‘grants’) often enable the Scottish Government to use local authorities as a vehicle with which it can drive key policies forward.
- 1.3 In 2019/20, the proportion of the overall block grant which was ring-fenced by the Scottish Government rose from 4.5% to 8.1%, with total ring-fenced funding for 2019/20 amounting to £30.6 million. The type of grants received by Aberdeen City Council in 2019/20 and their value are detailed below with a comparison to the 2018/19 figures.

	2018/19	2019/20
<b>Revenue</b>	<b>£</b>	<b>£</b>
Gaelic Education	120,000	114,000
Pupil Equity Fund	2,791,000	2,784,000
Criminal Justice Services	4,057,000	4,123,000
Early Learning and Childcare Expansion	1,418,000	13,316,000
<b>Total Specific Revenue Grants</b>	<b>8,386,000</b>	<b>20,337,000</b>
<b>Total Revenue Grant</b>	<b>330,159,000</b>	<b>342,296,000</b>
	<b>2.5%</b>	<b>5.9%</b>
<b>Capital</b>		
Early Learning and Childcare Expansion	7,400,000	8,600,000
Cycling, Walking and Safer Streets	313,000	374,000
Town Centre Fund	-	1,351,000
<b>Total Specific Capital Grants</b>	<b>7,713,000</b>	<b>10,325,000</b>
<b>Total Capital Grant</b>	<b>31,390,000</b>	<b>38,274,000</b>
	<b>24.6%</b>	<b>27.0%</b>
<b>Total Specific Grants</b>	<b>16,099,000</b>	<b>30,662,000</b>
<b>Total Local Government Settlement</b>	<b>361,549,000</b>	<b>380,570,000</b>
	<b>4.5%</b>	<b>8.1%</b>

- 1.4 The objective of this audit was to provide assurance that the Council has appropriate arrangements in place to ensure that conditions relating to ring-fenced funding within the Scottish Government Grant are complied with. Because the Pupil Equity Fund was subject to review by Internal Audit in April 2019 (report AC1922), this component of specific grant income was excluded from the review.
- 1.5 The factual accuracy of this report and action to be taken with regard to the recommendations made have been agreed with Steven Whyte, Director of Resources, and Jonathan Belford, Chief Officer – Finance.

## 2. FINDINGS AND RECOMMENDATIONS

### 2.1 Governance

- 2.1.1 Comprehensive written procedures which are easily accessible by all members of staff can reduce the risk of errors and inconsistency. They are beneficial for the training of current and new employees and provide management with assurance that correct and consistent instructions are available to staff. This is important in the event of an experienced employee being absent or leaving, and they have increased importance where new systems or procedures are being introduced.
- 2.1.2 Ring-fenced funding is subject to Financial Regulations and Procurement Regulations as with any other Council funding. The Council has not developed specific guidance, with reliance placed on that contained in Grant Offer letters and any further guidance which may be issued from time to time by the Scottish Government in respect of specific grants. Council Officers can seek further guidance from Scottish Government Policy Teams to determine appropriate courses of action where they need more clarity.
- 2.1.3 Several documents are completed in the course of the grant funding period. These are: the Grant Application, Grant Acceptance, Grant Reports, Grant Claims, and a Statement of Compliance with Conditions of Grant.
- 2.1.4 The Council's Scheme of Delegation - Powers Delegated to Chief Officers includes: "To approve applications for grant funding. Thereafter, following consultation with the Convener of the City Growth and Resources Committee, to accept grand funding provided that the terms and conditions of such funding have been approved by the Chief Officer - Finance and the Head of Commercial and Procurement Services. Expenditure of such grant funding may then be approved by the relevant Chief Officer subject to any such terms and conditions and in compliance with the ACC Procurement Regulations and Financial Regulations."
- 2.1.5 Completion practice varied between grants in terms of the salary grade of the staff involved and whether they were Finance or Service based. Beyond the delegation to Chief Officers noted above, approved delegated authority in respect of the grants is not recorded. It is therefore not clear whether a Service Manager is authorised to sign off a Grant Acceptance Form or Statement of Compliance, or whether this responsibility is reserved for the Section 95 Officer (Chief Officer – Finance). Similarly, in one case a Trainee Accountant signed off a grant claim form, whilst in others it was a higher graded officer within Finance or the Service.
- 2.1.6 A brief description of the internal controls and authorisation required in the grant process would be beneficial to increase assurance that grants are being administered in accordance with both management's expectations and grant terms and conditions.

#### **Recommendation**

A brief procedural document should be developed for grant administration to ensure appropriate personnel follow approved practice.

#### **Service Response / Action**

Agreed. This will be linked to the current scheme of delegation in relation to grant acceptance.

#### **Implementation Date**

September 2020

#### **Responsible Officer**

Finance Operations  
Manager

#### **Grading**

Important within audited  
area

- 2.1.7 Scottish Government grant allocations are normally advised through Local Government Finance Circulars and the details are fed into the Council's budget setting process. Some specific grants, or the distribution values, are not known in advance and cannot be fed into the budget setting process. Letters can be received at later points in the year, and grants accepted under the Scheme of Governance – Powers Delegated to Officers.
- 2.1.8 The Grant Offers containing the value of each grant, the conditions which apply, and their value are received by the Council from Scottish Government Policy Teams. Grant Offer letters include a Grant Acceptance form which must be signed and returned within the financial year.
- 2.1.9 While most acceptance forms had been returned promptly, those involving Services delivered through Aberdeen City Health & Social Care Partnership were not returned until March 2019, though they had been sent to the Council in August and September 2018. There was an increased risk of deadlines being missed and grant not being recovered in this instance, as the grant conditions stated that 'Scottish Ministers shall not be bound to pay any instalment of the grant which has not been claimed by 31 March of the applicable financial year.' This type of grant condition is often included for ring fenced grants.

**Recommendation**

All grant documentation should be shared with appropriate officers in order that it can be completed and submitted to the Scottish Government timeously.

**Service Response / Action**

Agreed. This will be written into the procedure document in 2.1.6.

**Implementation Date**

September 2020

**Responsible Officer**

Finance Operations  
Manager

**Grading**

Significant within audited  
area

- 2.1.10 There is a risk of late claims being rejected, as stated in grant conditions. This risk is greater in the event that specific individuals have been assigned sole responsibility for applying, monitoring, reporting and claiming grants – particularly during a period of significant organisational change. There is currently no overall independent review to ensure adequate control is being exercised and all grant activities are being completed in accordance with Scottish Government requirements and timetables.
- 2.1.11 A register of grants which captures timelines, when income is expected, the value of this and any claims submitted would be beneficial. This could provide assurance for management that key documents and reports have been submitted to the Scottish Government and that the appropriate transactions have been completed and recorded timeously. A register could also capture where variances from Grant Offer values are expected, and any additional ring-fenced funding which has been announced such as additional awards of £78,721 and £35,000 to Criminal Justice in 2018 for the Problem-Solving Court in Aberdeen and Caledonian System Men's Programme respectively. Although bank reconciliation and budget monitoring measures should identify material variations, this may be some time after the event.

**Recommendation**

A register of specific grants should be developed and monitored regularly to enhance assurance over specific grant income.

**Service Response / Action**

Agreed. There are records of incoming grants and monitoring of grant expenditure in relation to the budget monitoring and grant conditions where applicable. However, these are not comprehensive. It has been recognised by the Service that there is a

requirement for a comprehensive grants register.

<u>Implementation Date</u>	<u>Responsible Officer</u>	<u>Grading</u>
September 2020	Finance Operations Manager	Important within audited area

## 2.2 Spending Plans

- 2.2.1 Specific grants represent an increasing proportion of Scottish Government funding. They allow the Scottish Government to use Local Authorities as a vehicle with which it drives certain policies and initiatives forward. There is therefore a requirement for them to be demonstrably applied to expenditure directly associated with achieving those aims. While some grants can be carried forward, many require expenditure or full legal commitment of funds within a set time period (typically the financial year in which they are provided).
- 2.2.2 It is therefore prudent for Services to have clear spending plans for each grant which demonstrate management's intentions and focus on meeting grant conditions in terms of the time period and nature of expenditure.
- 2.2.3 The extent of spending plans which Services have vary depending on the value and type of project or service being delivered through grant monies. For example, the Early Learning and Childcare Expansion Project has extensive planning documents for both capital and revenue expenditure. These are required to manage delivery of the obligation to meet increased childcare provision requirements by August 2020.
- 2.2.4 The works included in the Cycling, Walking and Safer Streets spending plan are used as 'fill in' jobs when Roads teams are less busy, generally outwith surface dressing and winter maintenance periods. While this represents the Service seeking to manage its workload efficiently and effectively, progress with the plan could be jeopardised where, for example, unexpected events divert staff resources away from planned works. If there is insufficient time to complete the works and use the funds available, under-recovery of grant monies could be reputationally damaging. Management needs to have assurance that adequate progress is being made and control maintained.
- 2.2.5 The Town Centre Capital Grant Fund (TCF) was announced by the Scottish Government on 1 March 2019, only 4 days before the Council set its 2019-20 budget. Aberdeen City Council was awarded £1.35 million with the caveat that *'If the grantee does not use the grant in the financial year 2019-20, unused grant is to be repaid to the Scottish Government unless otherwise agreed in writing by Scottish Ministers'*, meaning that a clear spending plan was essential to ensure prompt delivery of projects and commitment of funds within the due date.
- 2.2.6 The TCF grant was not anticipated and officers were required to identify desirable projects which met its criteria within a very short space of time. A list of potential projects for TCF was presented to the City Growth and Resources Committee in June 2019 by the External Funding and Policy Officer for consideration, but the value of projects approved fell short of the Grant Offer by over £137,000 and officers were asked to return with further projects in September 2019. The Committee has been advised that the Service was *'...unable to report on how the balance of the fund can be allocated due to not having the final costings from the approved projects...'* and that this is *'...due to the nature of the projects, in particular the capital aspects which have required seeking input from external sources, contractors etc.'*
- 2.2.7 The absence of a complete spending plan increases the risk of grant not being recovered – though in the case of this grant the requirement is *"If the Grantee does not use the grant in the financial year 2019-20, unused grant is to be repaid to the Scottish Government*

*unless otherwise agreed in writing by Scottish Ministers. It is expected that work will be completed; or, at least work or contracts signed or commenced within 2019-20.*" In this instance the risk may therefore be reduced as the timescale does not require full delivery of all projects. However, funds can only be legally committed once contracts are in place with suppliers, contractors and third party delivery partners – which require lead time to meet procurement and legal requirements and to evidence compliance with grant terms and conditions.

2.2.8 The Service planned to report to Committee in February 2020, though a progress report was required by the Scottish Government by November 2019. Return of the funds could disadvantage City development and prevent the Council from achieving the grant's objectives.

2.2.9 At the end of August 2019, 5 months into the 2019/20 financial year, no project expenditure had been processed. Although project leaders had been assigned, few had created individual project spending plans, and basic project timetables had only recently been developed (as at October 2019). Contracts and agreements are still in draft. The Council needs to determine ways in which it can change procedures and practice to reduce the risk of grant funding not being recovered.

<b><u>Recommendation</u></b>		
Procedures and practice should be reviewed to improve the efficiency of the project identification, approval, planning and delivery process.		
<b><u>Service Response / Action</u></b>		
Agreed. It is agreed that procedures and practice will be reviewed and linked in relation to the aforementioned processes. This will be incorporated into the procedures in recommendation 2.1.6. It is held that it is not viable to create reserve lists of projects and liaise with partners prior to grants being offered. This would mean committing resource inefficiently to speculative grants that may never materialise.		
<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
September 2020	Finance Operations Manager	Significant within audited area

2.2.10 Monitoring of the TCF was assigned to the Council's External Funding Team, which has previously overseen delivery of similar programmes. Although in this case having a single team over many ringfenced funded projects has not yet proven effective – as the projects (at the time audited) had not reached an advanced stage of delivery to utilise the available grant, consideration should be given as to whether a central team could be used to co-ordinate the use of and ensure compliance with the terms of grants included within the specific grant register recommended at 2.1.11 above.

<b><u>Recommendation</u></b>		
Consideration should be given to whether a central team could enhance control and assurance over specific grants.		
<b><u>Service Response / Action</u></b>		
This has been considered and it is felt that with the assurance provided by the new procedures and effective liaison between all relevant roles in the process, that this can bring about the required co-ordination and controls.		
<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
Implemented	Finance Operations Manager	Important within audited area

## 2.3 Income and Expenditure

- 2.3.1 Specific Grant income and expenditure is accounted for in the financial system through dedicated ledger codes. The coding structure allows budget holders and Finance Partners to monitor the budgets and produce management information in order to maintain control over the use of specific grant funding.
- 2.3.2 The majority of specific grants are received in regular periodic payments for which the Scottish Government requires statistical and financial returns. Most of the grants reviewed required initial returns to be submitted in November 2019 and therefore, as the draft audit report was issued in October 2019, Internal Audit was unable to review compliance for the current financial year, however there is evidence of these reports being submitted for relevant grants in the previous year.
- 2.3.3 A review of grant income received from the Scottish Government in 2018/19 and in the early part of 2019/20 showed grant income was generally being received as expected. However, for the 2019/20 Early Learning and Childcare revenue grant there is a variance between the Grant offer of £14.045 million, and project documentation provided by the Service which indicates it is working on the basis of £12.04 million being received. If plans are not in place to fully utilise available funds there is a risk of delays in implementing projects or in some cases of grants having to be repaid. The recommendation at 2.2.10 above applies.

### **Recommendation**

The level of grant funding available should be consistently recorded.

### **Service Response / Action**

Agreed. It is agreed that recording of grant funding available should be consistently recorded. This will be incorporated into the procedures in recommendation 2.1.6.

### **Implementation Date**

September 2020

### **Responsible Officer**

Finance Operations  
Manager

### **Grading**

Important within audited  
area

- 2.3.4 Payments associated with grants are subject to the Council's Financial and Procurement Regulations, and are processed through the Council's payroll, purchasing and payments systems. These systems are periodically reviewed by Internal Audit to provide assurance over the controls in place. Reliance is placed on the application of these controls to provide assurance over the legitimacy of expenditure.
- 2.3.5 However, transactions claimed as eligible grant expenditure against grants which must be used within a single financial year included accruals, adjustments and estimates, in addition to direct expenditure:
- 2.3.6 The majority of expenditure for Cycling, Walking and Safer Streets in 2018/19 included a spending plan category identifier (e.g. 051, 052, etc) within the transaction description, however over £113,000 of costs included in the 2018/19 claim did not include the identifier. Claims also included smaller works combined in one total. These gave the appearance in one instance of the Service making a £100,000 adjustment at year-end from work charged against other budgets, in addition to the items included in the spending plan and directly charged, reducing assurance that the expenditure met the conditions of the grant. In addition to these variations, whilst the overall grant claim matched the total recorded in the ledger (after adjustments), there was no record to support allocation of the costs between the expenditure categories included on the claim form – which did not clearly correspond to ledger coding, transaction descriptions or to the spending plan. It is



therefore difficult to demonstrate compliance with the terms of the grant, which included consideration of a minimum spend of 36% on cycling schemes.

2.3.7 The Criminal Justice grant claim includes an element for overheads (£231,000), which has not been calculated based on directly attributed costs. Whilst it is within the allowed percentage for overheads, which may have been incurred but not specifically charged against the Criminal Justice budget, supporting calculations indicate that it is a balancing figure added to claim the maximum available grant.

2.3.8 Improving the consistency of financial recording would aid in completion and verification of grant claims and demonstrating that approved spending plans have been delivered.

<b><u>Recommendation</u></b>		
The audit trail between spending plans, ledger transactions, grant claims and supporting documents should be improved.		
Estimates and adjustments should be reviewed to ensure they are compliant with grant terms and conditions.		
<b><u>Service Response / Action</u></b>		
Agreed. The service confirms that the Cycling, Walking and Safer Streets grant was compliant with grant criteria and the percentage spend on cycling schemes was considered at Strategic Commissioning Committee on 30 April 2018.		
It is agreed that procedures and practice will be reviewed in relation to the audit trail. This will be incorporated into the procedures in recommendation 2.1.6.		
<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
September 2020	Finance Operations Manager	Significant within audited area

2.3.9 Where grants are awarded for use in capital projects only, expenditure must meet the normal accounting rules for recognition of non-current assets. However, the Early Learning and Childcare Expansion capital grant has been used to fund feasibility studies to determine appropriate capacity building options. Such expenditure should not generally be included as capital expenditure unless it is directly associated with specific works.

2.3.10 Cycling, Walking and Safer Streets is also a capital grant, and expenditure in respect of the 'Safe Drive Stay Alive' campaign which did not result in a tangible asset being created or enhanced, has been charged against it. It may therefore be difficult to demonstrate that capital grants have been used wholly for appropriate purposes.

<b><u>Recommendation</u></b>		
The Service should ensure revenue and capital expenditure is appropriately recorded against relevant grants.		
<b><u>Service Response / Action</u></b>		
Agreed. A year end process exists that reviews appropriate treatment of revenue and capital expenditure, but it is noted that this requirement is of particular importance in respect of grant conditions. It is agreed that procedures and practice will be reviewed in relation to recording of revenue and capital expenditure. This will be incorporated into the procedures in recommendation 2.1.6.		
<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
September 2020	Finance Operations Manager	Significant within audited area

## 2.4 Medium Term Financial Planning

- 2.4.1 Financial planning sits alongside budget preparation, performance management and stakeholder reporting. The ability to look strategically beyond the current budget period is crucial for resilience and long-term financial sustainability. A longer and more strategic approach to planning helps determine future policy and development, and a medium-term financial strategy (MTFS) provides a framework for budget setting. Medium term financial planning should highlight the impact of known service and funding changes and include decisions that address any gaps in long-term financing. An effective MTFS makes clear the actions needed to ensure long-term financial sustainability.
- 2.4.2 The Council's anticipated medium term financial position and relevant assumptions were set out in the 2019/20 budget setting papers. These included anticipation of reductions in future funding and cost increases, though did not explicitly reference specific grant funding. The budget is prepared based on the best information available at the time, including initial indications from the Scottish Government (where available) in December of the preceding year. Planned funding is included in future years' budgets, along with recurring funding unless there is a defined end date.
- 2.4.3 While the Early Learning and Childcare Expansion project received a five-year funding agreement commencing 2017/18 for both Revenue and Capital, other grants such as Cycling, Walking and Safer Streets, and Criminal Justice Services receive only single year awards, though have been received on a recurring basis. The Town Centre Capital Grant Fund is in its first year and the Council does not anticipate it will recur. Guidance relating to the Gaelic Education project in 2019/20 reminds '*...authorities to plan for the mainstreaming of grant-aided project costs as early as possible, and certainly no later than five years from commencement of funding.*'
- 2.4.4 However, there remains a risk given that funding is regularly being confirmed by the Scottish Government for a single year, and the availability of detail regarding the amounts offered and associated conditions can be subject to delay. It may be appropriate to plan for such a contingency by developing outline exit strategies to be applied, subject to appropriate policy decisions, in the event that funding ceases at short notice.
- 2.4.5 'Mainstreaming' of funding involves moving grants provided for a specific purpose in previous years into the general revenue / capital grant. As there is then no direct link between the level of funding provided and delivery of any particular service or outcome, it is open for the Council to redetermine its priorities. This may provide an opportunity to review the level of service which is being delivered – though this may be difficult if e.g. expectations have been created and contracts entered into on the basis of previous funding allocations. It is however essential as there is no guarantee that equivalent levels of funding will be provided within the general grant.

### **Recommendation**

Strategies should be identified for situations where continuity of ring-fenced funding is not guaranteed.

### **Service Response / Action**

It has been considered by the Service that specific assumptions relating to cessation and mainstreaming of grants have been incorporated into budget assumptions based on the best available information. Medium Term Financial Planning, including the annual Budget, is developed and updated based on the best information available. This includes the incorporation of assumptions about anticipated changes in funding, and any new information, including proposals for mainstreaming. If any recurring funding were to be discontinued a review would need to be undertaken of the future level of service being provided, and this would be factored into financial planning. It is not

considered possible or best use of resources to pre-empt this except to the extent indicated.

**Internal Audit Comment**

Service position noted. There remains a risk if funding ceases at short notice.

**Grading**

Significant within audited area

**AUDITORS:** D Hughes  
C Harvey  
P Smith

## Appendix 1 – Grading of Recommendations

GRADE	DEFINITION
<b>Major at a Corporate Level</b>	The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss, or loss of reputation, to the Council.
<b>Major at a Service Level</b>	<p>The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss to the Service/area audited.</p> <p>Financial Regulations have been consistently breached.</p>
<b>Significant within audited area</b>	<p>Addressing this issue will enhance internal controls.</p> <p>An element of control is missing or only partial in nature.</p> <p>The existence of the weakness identified has an impact on a system's adequacy and effectiveness.</p> <p>Financial Regulations have been breached.</p>
<b>Important within audited area</b>	Although the element of internal control is satisfactory, a control weakness was identified, the existence of the weakness, taken independently or with other findings does not impair the overall system of internal control.