

# *Aberdeen City Council*

## Sport Aberdeen review of financial planning 2013/14 and governance arrangements - Internal Audit Review

Internal Audit Report  
2013/2014 for Aberdeen  
City Council

**January 2014**

Final Report



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This report has been prepared solely for Aberdeen City Council in accordance with the terms and conditions set out in our engagement letter 4<sup>th</sup> October 2010. We do not accept or assume any liability or duty of care for any other purpose or to any other party. This report should not be disclosed to any third party, quoted or referred to without our prior written consent.

Internal audit work will be performed in accordance with Public Sector Internal Audit Services. As a result, our work and deliverables are not designed or intended to comply with the International Auditing and Assurance Standards Board (IAASB), International Framework for Assurance Engagements (IFAE) and International Standard on Assurance Engagements (ISAE) 3000.

# 1. Executive Summary

	Trend	Critical	High	Medium	Low	Advisory	Total
<b>Risks as they relate to Sport Aberdeen</b>	This was a specific internal audit review focused on the 2013/14 budget setting and financial planning process within Sport Aberdeen.	2	2	1	-	-	<b>5</b>
<b>Risks as they relate to Aberdeen City Council as the core funder of Sport Aberdeen.</b>		-	5	-		-	<b>5</b>

## Summary of findings

- 1.01 Sport Aberdeen is core funded by the Council, and therefore needs to meet the conditions attached to the grant funding and the arrangement falls under the Council’s Following the Public Pound Guidance.
- 1.02 The internal audit review focused on the financial planning and budgeting arrangements for 2013/14 including the three year business plan and governance arrangements. It is recognised by both Sport Aberdeen and the Council that 2013/14 is a challenging year, and there were a number of factors within Sport Aberdeen which led to transitional arrangements, including finalising the new staffing restructures and a new management team in post from January 2013, and the development of the new vision alongside supporting values and aims. Overall our internal audit review was undertaken in August and September 2013 and reflects on a certain point in time and only the 2013/14 business planning process. Our review identified key areas of risk both for Sport Aberdeen as an organisation but also for Aberdeen City Council as “core” funder. Overall we have highlighted that:
- The scrutiny and approval of the 2013/14 budget did not reflect best practice. This budget was “tabled” at the Finance and Resources Sub Committee on 15 March 2013. In tabling the budget on the day it does not afford the members of the Finance and Resources Sub Committee with suitable time to review the budget and the accompanying assumptions in advance of the meeting. In addition, a proposition to increase income targets by 5% over the Sport Aberdeen Centres, Pools, Indoor Sport Centres, and a 10% increase in Income at the Golf Courses operated by Sport Aberdeen could not be supported by detailed plans outlining how this would be achieved.
  - During our work we performed a sample review on some of the key assumptions used in the 2013/14 budget and, where applicable, the 2014/15 and 2015/16 budgets. We identified a number of instances whereby the assumptions made by management and documented in the business plan were not subsequently incorporated into the detailed budget accurately or where the budget assumptions could not be supported by evidence.

- The business plan across the 3 years, recognising a forward looking plan contains less certainty, should still contain greater information on the future risks and challenges facing Sport Aberdeen, and in particular where scenarios can be considered and costed these should be reflected so a full financial position can be considered.
- The timetable in place within Sport Aberdeen to construct and approve the Business Plan should allow sufficient time for the Council as core funders to contribute and challenge as appropriate prior to the final business plan being approved.
- The Funding and Service Agreement needs updated to clearly articulate the information the Council requires and inclusion of key performance metrics to allow the Council to actively monitor the performance of Sport Aberdeen, as well as clearly set out what Sport Aberdeen responsibilities are, and how the relationship will be governed and managed by both parties.

## **Management comments**

### **Aberdeen City Council Management Comments**

The Council fully acknowledges and supports the auditors findings and recommendations and is committed to working with Sport Aberdeen in relation to the improvement and development of the governance framework that it has with Sport Aberdeen.

By way of background to this report, the working relationship between the Council and Sport Aberdeen has been controlled by reference to the Funding and Services Agreement, which sets out specific requirements and includes the requirement for Sport Aberdeen to provide acceptable Business Plans on an annual basis. The Funding and Services Agreement states in respect of the business plan that “On or before 31 October in each year during the period of this agreement, the Company will submit to the Council a draft Business Plan for the next Business Plan period.” The Agreement covers what will happen in the event that the Business Plan has not been approved by the Council by the last day in February of each year. For the financial year 2013/14 Sport Aberdeen was therefore expected to provide to the Council a draft Business Plan by 31 October 2012. This was not forthcoming and on 8 March 2013, the Council’s Culture and Sport Sub Committee agreed to provide an extension to Sport Aberdeen whereby a draft Business Plan was to be submitted by 31 March 2013, with a view to it being developed to an acceptable standard by 31 May 2013. This Committee also provided authorisation to officers to release the first quarterly grant payment to Sport Aberdeen.

While Sport Aberdeen did meet the revised deadline of 31 March for the initial draft, the revised deadline for submission of the Business Plan to be completed to a quality to be approved by council was not met. The Council recognises that Sport Aberdeen has now commenced the development of their 2014/15 Business Plan and that this was submitted to the Council in line with the requirements of the Funding and Services Agreement. Since receipt of the draft business plan, a robust process of review and challenge is progressing, including regular internal review sessions and meetings with senior officers in Sport Aberdeen to help to support the refinement of the business plan to an acceptable standard.

At the time of writing this report, it is anticipated that the Business Plan will be of a quality to be approved by the Council by the end of February, and officers would intend to take the acceptable Business Plan to an appropriate Council Committee at that time.

The development of the governance framework (referred to above) between Aberdeen City Council and arm's length external organisations includes a number of actions, including a clear separation between Service Committees and the Audit and Risk Committee to ensure the Council can direct and strategically influence the services that are undertaken by these organisations (including Sport Aberdeen), while at the same time objectively securing assurance in relation to their system of risk management.

Furthermore the Council is putting in place a Governance Hub featuring Service representation and specialist support staff, from Finance, Human Resources, Legal, Risk Management and Procurement, that will, in conjunction with the organisation gather information and reports and assess risk management and performance so as to provide assurance to the Council on a range of matters, including financial planning, organisational performance and risk management. The Governance Hub will provide reporting to the Service Committees and Audit and Risk Committee.

The Council expects to work with Sport Aberdeen in an open, transparent and objective way to secure the further improvements that can be achieved, which arise from this report.

### **Sport Aberdeen Management Comments**

The period in focus for the review [January – March 2013], was a particularly challenging and complex period for the Company. SA was going through fundamental change which was underpinned by an extensive process of organisational 'transformation' and modernisation being led by a new Senior Management Team.

It is fully acknowledged by the Board that things were in need of improvement at this time; and this report highlights the mitigating circumstances within each relevant recommendation which should be taken into consideration as part of the review.

The SA Board Directors are fully cognisant of their personal responsibilities as Directors and Charity Trustees. A highly relevant factor is the measures that SA has put in place during the on-going process of 'transformation' through 2013 which in the Boards opinion, goes a long way to addressing a significant number of 'findings' highlighted within the review report. These include, in no particular order;

- (i) Significantly improved reporting and recording process for the meetings of the Board and its Committees;
- (ii) Robust timetable for Business Plan development and Performance Reporting in place, linked to Board and Committees of the Board Meeting Cycle, and which fully accord to the requirements of the Funding and Services Agreement and the Council's Monitoring the Public Pound Guidance;
- (iii) Tighter budget and financial management process, with greater accountability across management teams;
- (iv) New financial Regulations and Procedures agreed by the Board and adopted throughout the company;
- (v) Production of a Risk Register, [also provided to ACC Corporate Governance and which had been provided to ECS as a follow up to the submission of the business plan April 2013]. The risk register itself remains a live document and reviewed and updated internally on a regular basis, with Risk as a standing item on both SMT Agendas, Finance and Resources Committee and Board Meetings;

- (vi) Performance & Scrutiny Committee meeting more frequently and in particular, providing a much more robust challenge to SMT in preparation of the 2014/2015 business plan and budget;
- (vii) More thorough and strategic approach to budget setting process for 2014/2015; and
- (viii) Monthly submission of KPI and financial performance information to the City Council, as per its request (since June 2013) and quarterly submission of progress of SA against its business plan objectives.

## 2. Background and scope

### Background

- 2.01 Sport Aberdeen was established as a company under charitable status with the aim of ensuring high quality, well-managed sports facilities in Aberdeen. For the 2013/14 financial year the Council has agreed to provide funding to Sports Aberdeen consisting of a service level payment (constituting core funding) of £5.423 million (£5.736 million in 2012/13). In addition to this, Sport Aberdeen receives from the Council £100,000 per year to cover Access to Leisure discounts, £15,000 per year for top up swimming and £349,200 per year as the Sport Scotland contribution to Active Schools. Payment of funding by the Council to Sport Aberdeen is contingent on them providing the services as described in the Funding and Service Provision Agreement, including the provision annually of a business plan and operational report.
- 2.02 Sport Aberdeen is core funded by the Council, therefore it is required to meet the conditions attached to the grant funding and the arrangement falls under the Council's Following the Public Pound Guidance. Essentially the Council are the core funders of Sport Aberdeen, as set out in the funding agreement, and Sport Aberdeen have a contractual obligation to meet the requirements set out by the Council.
- 2.03 The objective of this internal audit review was to independently consider (on a sample basis) certain of Sport Aberdeen's arrangements:
- The underlying financial assumptions that make up the Income and Expenditure statement and Balance Sheet; including a review of how the Aberdeen City Council grant funding is utilised;
  - The assumptions underpinning the projections in the current Sport Aberdeen business plan;
  - Sport Aberdeen's financial arrangements, particularly considering how they are ensuring accurate and complete recording of information and underlying records. This will include considering the quality of management information submitted to those who are Accountable for Sport Aberdeen (Management Team and the Board);
  - The overarching governance arrangements at Sport Aberdeen and the arrangements in place for any alternative arrangements for service delivery put in place by Sport Aberdeen in respect of management of Council facilities;
  - The knowledge and skill mix of Sport Aberdeen staff, in particular the senior management team.

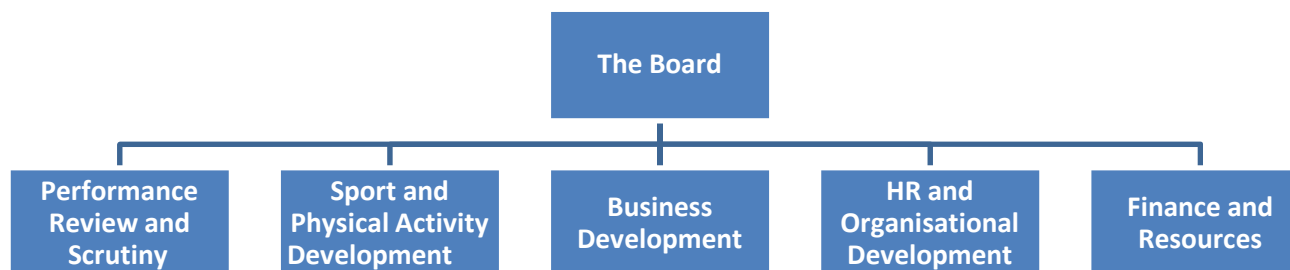
Our review was undertaken in August and September 2013, and focused on the 2013/14 budget setting process and business plan only. It is recognised that in this period Sport Aberdeen were facing specific challenges and transitional arrangements were in place over certain areas, for example:

- A new management team were only in post from January 2013 and this resulted in the finalisation of staffing restructures within the various Divisions;
- Developing a new vision for Sport Aberdeen, accompanied by supporting values and aims;

- Managing the ongoing consultation with the Trade Unions as part of the process of transformation and the move towards changed employee terms and conditions; and
- Continuing process of service re-design and modernisation.

## Sport Aberdeen

- 2.04 Sport Aberdeen commenced the operation of the majority of Aberdeen City Council’s sports facilities in July 2010 for a ten year period. The relationship between the Council and Sport Aberdeen is governed by a Funding and Service Provision Agreement and a Transfer Agreement. Former Council staff employed in the service were transferred to Sport Aberdeen under the Transfer of Undertakings (TUPE) Regulations.
- 2.05 The management team within Sport Aberdeen as at August 2013, consisted of a Chief Executive and senior management team: a Business Development Director; Operations Director; Sport and Physical Activity Development Director (vacant post from May 2013); and supported by a HR and Organisational Development Manager and a Finance and Resources Manager..
- 2.06 Sport Aberdeen is governed by a Board of Directors which is there to provide oversight and scrutiny of Sport Aberdeen’s operations and meets approximately eight times a year. The Board consists of nine Directors, including three Councillors which the Council nominates to sit on the Board. The Head of Communities, Culture and Sport also attends meetings of the Board in an observer role on behalf of the Council. There are five Sub Committees of the Board which meet on a monthly cycle:





## **Business and Financial Planning**

- 2.07 In March 2013 Sport Aberdeen submitted to the Council its draft Business Plan for the period 2013/14 to 2015/16. The business plan is designed to set out the direction of Sport Aberdeen and is intended to clarify to the Board of Directors, for staff and for its key funding partner, Aberdeen City Council over the future direction of Sport Aberdeen.
- 2.08 The business plan is a rolling 3-year plan and is required to be reviewed and updated on an annual basis in line with the requirements of its Funding Agreement with Aberdeen City Council.
- 2.09 The Business Plan sets out Sport Aberdeen’s vision “to be the best sport and leisure Charitable Trust in Scotland by 2020, through creating opportunities, inspiring people and changing lives.” It sets out to achieve this vision by being:
- The Brand of Choice
  - The Provider of Choice
  - The Employer of Choice
  - The Partner of Choice
- 2.10 Sport Aberdeen currently employs 314 staff, of which 138 are full time and 176 part time hours. . It has an annual gross budget of £10.740 million
- 2.11 Sport Aberdeen receives the following income:
- (i) Via Aberdeen City Council through the payment of a grant (“core funding”) for which SA delivers services in accordance with the Funding and Services Agreement.
  - (ii) through fees and charges levied for use of the facilities it manages by its customers; and
  - (iii) Through external grant funding for the delivery of discrete programmes, and also the ability to apply for additional sponsorship.

2.12 Within the Business Plan Sport Aberdeen has outlined the following financial forecasts:

<b>Income</b>	<b>2013/14</b>	<b>2014/15</b>	<b>2015/16</b>
Facility Receipts	4,508,578	4,764,593	4,950,804
External Grant Funding – SportScotland	349,200	349,200	349,200
External Grant Funding – Other	78,492	30,992	30,992
Sponsorship Development	52,000	50,000	50,000
Core ACC Funding	5,423,116	5,104,110	5,104,110
Access to leisure Funding	100,000	100,000	100,000
Transfer from Reserves	228,920	-	-
	<b>10,740,306</b>	<b>10,398,895</b>	<b>10,585,106</b>
<b>Expenditure</b>			
Payroll	5,797,997	5,443,627	5,609,047
T&C Implication of Delay	198,000	78,000	-
Utilities	1,186,748	1,275,755	1,371,435
Ground Maintenance	1,081,579	1,108,126	1,130,289
Business Support	1,071,177	1,053,462	998,412
Other	1,404,805	1,439,925	1,475,923
	<b>10,740,306</b>	<b>10,398,895</b>	<b>10,585,106</b>
<b>Surplus / (Deficit)</b>	<b>0</b>	<b>0</b>	<b>0</b>

2.13 As at July 2013 Sport Aberdeen reported a favourable budget variance of £28,000 as set out in the Board budget paper. This performance is a result of cost savings from staff costs £45,000 and other expenditure underspends of £48,000 to date. Overall Income is tracking £49,000 behind budget, with the £93,000 shortfall on major centre income being compensated by the outperformance of the golf budget by £52,500.

# 3. Detailed findings and recommendations

## 3.01 Lack of formal evidence to support the appropriate scrutiny of 2013/14 Sport Aberdeen Budget

### Finding

As part of the financial planning arrangements at Sport Aberdeen budgets were produced for each operational and functional activity in FY13/14. Budget holders were provided with “year to date” figures as at January 2013 and asked to use this information, alongside their wider knowledge and aspirations for the business to develop a FY13/14 budget for incorporation within the Sport Aberdeen Business Plan. This budget was “tabled” at the Finance and Resources Sub Committee on 15 March 2013. In tabling the budget on the day Members of the Finance and Resources Sub Committee do not have time to review the budget and the accompanying assumptions in detail.

The budget that was tabled outlined a one off draw on company reserves so that it was breakeven rather than in deficit for 2013/14 with certain options set out to balance the budget. The minutes of the meeting highlight that these options were agreed on the basis “*that there may be some further discussion with the SMT but, in principle, the options appeared realistic*”. The options were: to propose a 5% increase in Income over the Sport Aberdeen Centres, Pools, Indoor Sport Centres, and a 10% increase in Income at the Golf Courses operated by Sport Aberdeen. A range of reductions in Senior Management Team Expenditure budgets were also set out. At the meeting The Finance and Resources Manager was instructed to prepare a balanced budget on this basis for the Board on 20 March 2013 and to add to the Board report that is being drafted by the Chief Executive.

When we completed our fieldwork we were unable to review the budget tabled at the Finance and Resources Sub Committee on 15 March 2013 as the budget had been “overwritten” by the final budget presented by the Board on 20 March 2013. Although the minutes indicate that “*detailed discussion and challenge*” was provided by the Finance and Resources Sub Committee on the 2013/14 budget there was no detail outlining the nature of the discussion formally recorded. We were also unable to obtain any documentary evidence to support any of the options agreed at the Finance and Resources Sub Committee.

We also note that the time between the Finance and Resources Sub Committee on 15 March 2013 and the Board on 20 March 2013 is 3 working days. This does not provide sufficient time to finalise the budget paper and issue to Non-Executive Directors for consideration in advance of the Board meeting on 20 March 2013.

During our review of both the Board and the Finance and Resources Sub Committee minutes and reports we noted that the quality and the level of detail in the monthly finance paper was poor; for example lacked sufficient detail to outline the key variances in the budget; narrative on future challenges and risks ; and the forecast outcome for the end of the financial year.

## Risks

The performance and decision making of Sport Aberdeen governance committees will be compromised if Non-Executive Directors are not provided with the opportunity to review key reports for discussion and approval in advance of the meetings, particularly in respect of Sport Aberdeen financial position.

Sport Aberdeen will be unable to evidence key discussions and decisions if Committee papers are not retained (for example the original budget paper tabled on 15 March) and minutes do not provide sufficient detail of the discussions and decisions taken at each meeting.

Sport Aberdeen budget assumptions, needed in order to achieve a balanced budget, may be unsupported by evidence of the achievability and viability of the assumptions.

## Action plan

Finding rating	Recommended action	Responsible person / title
<p><b>Risk rating:</b> Sport Aberdeen – Critical</p>	<ul style="list-style-type: none"> <li>Sport Aberdeen will ensure that papers prepared for its key governance committees are prepared and issued to members at least one week in advance of the Committee meeting. These papers must be retained by Sport Aberdeen as evidence of information used in decision making.</li> </ul>	
<p>Aberdeen City Council – High</p>	<ul style="list-style-type: none"> <li>The minutes of the Finance and Resources Sub Committee should document the discussions had during the meeting and clearly outline the decisions taken by the Committee, including greater transparency over how the budget is produced.</li> <li>Any established budget / amendment to a budget (income or expenditure) should be clearly supported by key assumptions and evidence that supports the achievability of these budgets.</li> <li>The monthly Sport Aberdeen finance report needs further development so it provides sufficient detail to understand and challenge financial performance and make decisions that help Sport Aberdeen achieve its budget at year end.</li> </ul>	<p><b>Target date:</b></p>

### **Management Response**

Both Sport Aberdeen and Aberdeen City Council management agree the recommended actions. The “key governance committees” have been identified as the Sport Aberdeen Board; the Finance and Resources Committee; and the Performance and Scrutiny Committee.

### **Sport Aberdeen Management Response:**

It is indeed desirable that non-Executive Directors are provided with as much information in advance of meetings for them to consider and SA has endeavoured wherever possible to do so. It already has in place schedules for Board and Committees, including dates for agreeing agendas, preparation of reports for internal scrutiny and circulation.

SA is already substantially working towards the recommendations and has improved both the quality and content of reports presented to the Board and its Committees, supported by appropriate Board and Committee minute taking and record keeping arrangements. Presently, every effort is made to ensure that all reports and papers are circulated to the Board one week in advance of meetings. At the very least, these are circulated by e-mail, with hard copy to follow in the post. Clear time lines and deadlines exist for report authors, particularly when preparing reports for the main Board.

More comprehensive finance reports are already being provided to the Board and the Finance & Resources Committee, together with improved minute and record keeping.

The budget setting process for 2014/15 required budget holders to fully substantiate budgets for service areas. SA will continue to refine this and other budget monitoring processes. Improvements to the monthly SA finance and monitoring reports have already been further refined, with additional supporting comments from budget holders regarding under or over performance, future challenges and actions to be taken to bring service areas within budget at year end during 2013/2014.

The company is a "living organisation" and there can often be a need for papers to be submitted late. In the case highlighted within the report, decisions were not taken on the day but were deferred for 5 days to allow Board Trustees further time to read the paper in detail and respond with comments before final approval.

### **Aberdeen City Council Management Response:**

Compliance with the recommended actions will be monitored by the Council through the Council’s ALEO governance scrutiny process.

Sport Aberdeen has agreed to send copies of all papers and minutes for all board meetings and board committee meetings to the Council. Sport Aberdeen is preparing to put in place a system whereby appropriate board papers are made publically available.

### 3.02 Key budget Assumptions in 2013/14 Budget and lack of supporting evidence

#### Finding

During our work we performed, on a sample basis, a review of the key assumptions used in the 2013/14 budget and, where applicable, the 2014/15 and 2015/16 budgets. During our review we identified:

- The business plan budget assumes that there will be 50 new Sport Aberdeen Health and Fitness members a month. This is not the number reflected within the budget. What is assumed in the budget is that the monthly income received in January 2013 would be sustained throughout the year. When we reviewed the trial balance we noted that income in January 2013 was c£41k. However, the budget was calculated assuming £35k per month. As a result, membership in FY13/14 budget could be understated by c£72k, and this variation from budget to business plan is not clearly set out, including the assumptions made.
- For 2014/15 and 2015/16, Sport Aberdeen is assuming 50 new Sport Aberdeen members per month. However the 2015/16 budget does not assume the retention of the new members recruited during 2013/14 and 2014/15. Therefore, calculations suggest the membership income for 2015/16 is understated by c£160,000. We acknowledge that it is likely that there will be membership attrition over this period but the Sport Aberdeen aspiration is to recruit 50 new members net, each month and therefore this is another example where the business plan and budget do not correlate.
- The income budget for External Grant Funding and Sports Development was pulled together by the then Sport and Physical Activity Director who has subsequently left Sport Aberdeen. Sport Aberdeen was unable to locate any analysis that supports the income figures included within the Business Plan.
- Overall there is limited evidence which supports the key budget assumptions within the agreed 2013/14 budget. In particular, we were unable to evidence the rationale for a 5% increase in income, 10% increased income in Golf and whether the reductions in expenditure were achievable, the impact on service delivery and whether these were one off only savings or contributing to the longer term financial sustainability of Sport Aberdeen.
- During review and challenge of the Fy13/14 budget for Beach Leisure Centre we noted that the level of scrutiny by management was limited in certain areas. The following points were not sufficiently explained within the budget setting and business plan process:
  - Coaching fees have increased by 16% to £28.8k but there are no comments or assumptions.
  - Hair drier income has increased by 10% to £6.3k but assumption is that usage will decline so there is no correlation in this assumption.

#### Risks

If the budget does not reflect managements understanding of its business, the assumptions proposed by the management team or the management information retained by Sport Aberdeen then there is a significant risk that Sport Aberdeen will not achieve its budget at year end. Certain budget assumptions are not supported by sufficient detailed evidence which sets out clear rationale and therefore raises concern over whether the budget approved is achievable.

<b>Action plan</b>		
<b>Finding rating</b>	<b>Recommended action</b>	<b>Responsible person / title</b>
<p><b>Risk rating:</b> Sport Aberdeen – Critical</p> <p>Aberdeen City Council – High</p>	<p>All key budget assumptions must be supported by evidence for example clear trends in sports usage; whether the assumption has a 1 year impact or a longer term impact on Sport Aberdeen; what the various scenarios are and how likely these are to arise; and assumptions made in the budget must link to the business plan and business planning process. These budget assumptions need to robustly scrutinised and challenged by the Finance Sub Committee and also the Board.</p> <p>Based on our review Sport Aberdeen should consider whether the current financial management arrangements are fit for purpose.</p>	
<p><b>Target date:</b></p>		
<p><b><u>Management Response</u></b></p> <p>Both Sport Aberdeen and Aberdeen City Council management agree the recommended actions.</p> <p><b><u>Sport Aberdeen Management Response:</u></b></p> <p>SA accepts the need to make improvements in the transparency of working up budget assumptions and has been striving to do this - something that has been particularly evident in the 2014/2015 budget and the supporting 3 year Business Plan process.</p> <p>SA purchased a Leisure Management Information System [LMIS] in 2012, and live roll out commencing November 2012. Once the system has been operational across all areas for a full year [Dec 2014] this will provide much more robust data than has previously existed since [and prior to] transfer of SA., This will allow a detailed analysis of trends and an interrogation and ‘what ‘if’ scenario analysis to be performed on actual information.</p> <p>SA has worked within the budgetary and financial framework set by ACC. It has managed to meet all its responsibilities despite a budget reduction of circa £1.4m since formation. In addition, at the time of preparing this report, the trading position indicates approximately £100,000 ahead of budget target. This position has been achieved by robust budget management within a financial framework developed internally, closer scrutiny by budget holders, and proper and effective use of the company’s finances as an arm’s-length organisation, in full compliance of company and charitable regulations.</p> <p>SA is continually improving in this area and progress is being made and SA will continue to learn the lessons of the past and apply good practice to the process. Demonstrable improvements have been made in this regard via the Performance Monitoring reporting</p>		

including financial performance and the achievement of progress against key objectives as set out in its business plan. More is known about the financial position than at any time in SA history, reflecting the improvements made to financial processes by the Senior Management Team and the increased expertise available to it.

The new SA SMT now has a much greater understanding of the operational and financial performance of the company's areas of business activity. The approach adopted for 2014/2015 business planning and budget process was more comprehensive and robust and involved managers at various lower levels in the process. This has resulted in a greater sense of awareness and ownership for working too and achieving budgets.

**Aberdeen City Council Management Response**

Aberdeen City Council Management will monitor compliance with this recommendation through the Council's ALEO Governance Scrutiny Process.

Sport Aberdeen has now reviewed its financial management practices and has confirmed that it intends to consider future reviews of these practices as circumstances dictate.



### 3.03 Longer Term Financial planning – Limited evidence to support the achievement of future budgets as set out in the business plan including assessment of future known risks and challenges

#### Finding

There is significantly less evidence to support the achievability of the 14/15 and 15/16 budgets compared with the budget for financial period 2013/14, which is not unexpected given the forward look of the business plan. In each of these three years Sport Aberdeen is forecasting a breakeven budget. However it is anticipated that 2013/14 will require a £228,920 drawdown from reserves in order to achieve this breakeven target. During our review of the 3 year business plan it was noted that it was considered light in terms of outlining future known financial pressures, service challenges and risks which will have a potential impact on the financial position of Sport Aberdeen. For example:

- This proposed utilisation of reserves in 2013/14 is a result of the decision taken by Sport Aberdeen following the cessation of a historic arrangement which was an anomaly for both Sport Aberdeen and Aberdeen City Council. This loss of income will continue during 14/15 and 15/16, however it is unclear from the budget assumptions how Sport Aberdeen has planned to address the sustained reduction of £229,000 in future years as utilising reserves is not a sustainable option;
- Aberdeen Sports Village is currently developing its new Aquatics Centre which will offer flexibility for providing quality swimming participation for all ages and levels of ability including school swimming programmes learn to swim and keep fit for the residents of Aberdeen. It is anticipated that this new centre could have a significant impact on the swimming revenue at a number of the leisure facilities within Sport Aberdeen in addition to the loss of the elite swimming programme (COAST). Sport Aberdeen has performed some initial analysis on the potential impact the new Centre will have on its own “Learn to Swim” schemes but no financial analysis has been performed and incorporated into the budgets for 2013/14 or beyond;
- Highlighting the pension liability of £1.8 million and the potential impact this would have on Sport Aberdeen should it crystallise; and
- Outlining certain key assumptions within the budget setting process which are dependent on external factors out with the control of Sport Aberdeen for example, impact of weather on sport activities, risks with private company provision.

Although budgets generally become less accurate the further they look ahead it is the responsibility of management to ensure that appropriate processes are in place to develop suitable evidence based budgets for years two and three of the business plan. In addition, future financial challenges and opportunities should be identified and quantified and reflected appropriately within the budgets. The budget for years two and three of the budget plan should also be subject to suitable challenge and scrutiny by the Finance and Resources Sub Committee and the Board.

#### Risks

If longer terms budgets do not seek to quantify known future financial challenges and opportunities with a certain degree of accuracy it will become difficult for Sport Aberdeen to make meaningful longer term decisions that benefit both Sport Aberdeen and Aberdeen City Council.

## Action plan

Finding rating	Recommended action	Responsible person / title
<p><b>Risk rating:</b> Sport Aberdeen – High</p>	<p>All assumptions in the business plan, where known, should be costed and evaluated and included in the medium term budgets for 2014/15 and 2015/16. All known implications to date on the business plan need reflected and taken into account, taking into account any evidence and costing already completed, and in line with the Funding and Services Agreement. Where this results in a deficit position this should clearly be shown, alongside suitable plans to bring the budget back to breakeven. Where certain factors cannot be quantified they should still be set out to raise awareness of the key assumptions and challenges in place over the 3 year period and included in Sport Aberdeen’s Risk Register.</p>	<hr/> <p><b>Target date:</b></p> <hr/>
<p>Aberdeen City Council – High</p>	<p><b><u>Management Response</u></b></p> <p>Both Sport Aberdeen and Aberdeen City Council management agree the recommended actions.</p> <p><b><u>Sport Aberdeen Management response:</u></b></p> <p>It is recommended that the assumptions in the business plan need to be costed and evaluated and included in the budgets for 2014/15 and 2015/16. This is already in place as far as practicable in terms of the business planning / budget setting process for 2014/15.</p> <p>The timetable expected of SA required the 2014/15 business plan [covering 2014/15 – 2016/17] to be submitted to the City Council by 31<sup>st</sup> October 2013.</p> <p>Without ACC confirming its action in relation to its key projects having an impact on SA, it is not possible with any degree of accuracy, robustness or financial integrity to properly assess financial implications and risks to SA’s business.</p> <p>Notwithstanding this view, as an ALEO the Board and the SMT will continue in their best endeavours and within their responsibilities of managing the business on a daily basis, identifying necessary actions where it appears that the business is not performing according to budgetary expectations. These actions may not always accord with the actions or assumptions included within the business plan, which at best is a statement of intention at a given moment in time, in a particular set of circumstances and subject to regular review.</p> <p>While its forward planning budgetary process may not have been as rigorous as desired, SA has demonstrated an ability to manage reductions in its management fee since 2011/12, without having specific robust plans in place for so doing at the time of the first business plan and at transfer. This supports the capability of the Company to successfully manage its finances in a prudent manner, and provides further evidence that its management team has</p>	<hr/> <p><b>Target date:</b></p> <hr/>

the necessary mix of financial and management skills to manage a successful business at an acceptable level of risk both to the Board of Directors and the City Council.

**Aberdeen City Council Management Response**

Current ongoing processes in place to scrutinise and challenge the development of the 2014/15 Business Plan are already taking into cognisance this recommended action.

### 3.04 Business Planning – Recognising the relationship of the Council as “core funder”

Finding		
<p>During the 2013/14 period Sport Aberdeen undertook its own internal business planning process without consulting with Aberdeen City Council. As the core funder of Sport Aberdeen, it would be recognised practice for the Council to be consulted on the business plan prior to approval, and the right to scrutinise and challenge that plan. However, the plan was approved by the Sport Aberdeen Board in March 2013 without engagement with the Council. As a result, the Council legitimately challenged certain aspects of the plan and changes were made before final approval in May 2013. During a review of Board minutes we identified that there is a timetable in place within Sport Aberdeen for pulling together the 2014/15 business plan and budget for the agreed timescales of October 2013. However, there is not any time built into this timetable to consult with Aberdeen City Council during this process.</p>		
Risks		
<p>Sport Aberdeen may pull together a Business Plan that does not meet the needs and strategic priorities of Aberdeen City Council (the core funder). If there are not constructive discussions and sharing of information throughout the year there may be a risk that both organisations corporate objectives and outcomes will not be managed effectively.</p>		
Action plan		
Finding rating	Recommended action	Responsible person / title
<p><b>Risk rating:</b> Sport Aberdeen – High</p>	<p>A clear timetable should be agreed between Sport Aberdeen and the Council, which builds in appropriate time for Council scrutiny prior to final Board approval. This should be supported by a set of agreed principals and behaviours for both Council and Sport Aberdeen to follow (recommended to be built into the updated funding agreement).</p>	
<p>Aberdeen City Council – High</p>		<p style="text-decoration: underline;">Target date:</p>

**Management Response**

Both Sport Aberdeen and Aberdeen City Council management agree the recommended actions.

**Sport Aberdeen Management response:**

SA has and continues to recognise the role of the Council as its main funder, in providing challenge and scrutiny of its business plan, in particular through the approach identified in the Council's Following the Public Pound Guidance. SA will continue to be open and transparent with ACC and accepts the recommendation, but requests that the following additional comment be taken into consideration;

SA will involve ACC [the "funder"] in its business planning process and will do so prior to the plan going before the full Board for approval, but not before it goes through its own internal scrutiny via the Performance & Scrutiny and Finance & Resources Committees respectively. In addition, the Funding and Services Agreement requires variation to the current timetable for this to happen.

This approach will present the opportunity to improve face to face communication, improve relationships and speed up the latter stage of the business planning process. Meetings between SA and ACC will have to consider challenging and perhaps conflicting views but they will be essential if relationships are to improve. The responsibilities of the Company Directors to make decisions in the best interests of the company and their personal responsibilities cannot be ignored.

Sport Aberdeen welcomes the opportunity to jointly develop and agree a set of agreed principles and behaviours for both SA and ACC, including an appropriate independent appeals procedure.

**Aberdeen City Council Management Response**

It is noted that for the 2014/15 Business Plan, the draft Business Plan was submitted on 31/10/13 which complies with the requirements of the Funding and Services Agreement. A robust scrutiny and challenge process is currently ongoing to ensure that the final business plan is acceptable.

Sport Aberdeen and Aberdeen City Council have agreed to develop a clear timetable for future business planning processes by 31/3/14.

Work to review the Funding and Services Agreement is now scheduled.

### 3.05 Partnership Working – Funding Agreement needs reviewed and updated

Finding		
<p>It is acknowledged that the current Funding agreement between the Council and Sport Aberdeen is no longer fit for purpose. In particular:</p> <ul style="list-style-type: none"> <li>• It does not contain a suite of performance measures to allow the Council to measure the success of Sport Aberdeen and overall how Sport Aberdeen achieves best value and contributes to the Council’s overall strategic vision;</li> <li>• The funding relationship needs to be made clearer, including an explicit list of requirements on Sport Aberdeen and the Council, including a timetable for provision, with which achievement is monitored; How the relationship is to be managed and governed on a routine basis.</li> </ul>		
Risks		
<p>The absence of a clear specification of services may result in services being provided which might not be in the best interests of stakeholders. A lack of clarity in services specified may result in the Council being unable to determine whether value for money is being achieved</p>		
Action Plan		
Finding rating	Recommended action	Responsible person / title
<p><b>Risk rating:</b> Sport Aberdeen – Medium</p>	<p>Aberdeen City Council and Sport Aberdeen should work together to revise the specification of services, the deliverable outcomes required are stated in such a way that they are specific, measureable, attainable and time-bounded (SMART). This in turn will provide the basis for establishing meaningful performance indicators which are aligned with the service specification.</p>	
<p>Aberdeen City Council – High</p>	<p>Sport Aberdeen will need to establish performance management arrangements in place to ensure the criteria set out in the revised service specification can be collected and reported back to Aberdeen City Council and demonstrate appropriate utilisation of the grant funding provided by the Council. In addition, this data needs to be subjected to a data quality assurance check before provision to ensure that it is complete and accurate.</p>	<p style="text-decoration: underline;"><b>Target date:</b></p>
<p><b><u>Management Response</u></b> Both Sport Aberdeen and Aberdeen City Council management agree the recommended actions.</p> <p><b><u>Sport Aberdeen Management Comments:</u></b> SA is fully committed to work together with ACC [Departments of Education Culture &amp; Sport and Corporate Governance] to revise the funding agreement; however, it would need to reflect the way that SA was set up as an ALEO [Company Limited by Guarantee with Charitable Status]</p>		

and as such, be demonstrably independent from ACC to ensure the continued circa £1m saving per annum for the Council.

Any revisions to the key outcomes required of SA need to be considered within the current financial framework. If the outcomes are to change significantly, there may well be financial considerations which would have to be addressed by both partners, in advance of formal notification of any changes.

**Aberdeen City Council Management Response**

An agreed set of Performance Indicators has now been developed. Sport Aberdeen is now reporting against most of these Performance Indicators on a monthly basis, and are working towards being able to report against all of the indicators.

The review of the Funding and Services Agreement has been scheduled during February/March 2014.

Regular internal and external performance monitoring and scrutiny processes are now in place.

# Appendix 1 – Basis of our classifications

## Individual finding ratings

Finding rating	Assessment rationale
Critical	A finding that could have a: <ul style="list-style-type: none"><li>• <b>Critical</b> impact on operational performance; or</li><li>• <b>Critical</b> monetary or financial statement impact; or</li><li>• <b>Critical</b> breach in laws and regulations that could result in material fines or consequences; <i>or</i></li><li>• <b>Critical</b> impact on the reputation or brand of the organisation which could threaten its future viability.</li></ul>
High	A finding that could have a: <ul style="list-style-type: none"><li>• <b>Significant</b> impact on operational performance; or</li><li>• <b>Significant</b> monetary or financial statement impact ; or</li><li>• <b>Significant</b> breach in laws and regulations resulting in significant fines and consequences ; <i>or</i></li><li>• <b>Significant</b> impact on the reputation or brand of the organisation.</li></ul>
Medium	A finding that could have a: <ul style="list-style-type: none"><li>• <b>Moderate</b> impact on operational performance; or</li><li>• <b>Moderate</b> monetary or financial statement impact; or</li><li>• <b>Moderate</b> breach in laws and regulations resulting in fines and consequences; or</li><li>• <b>Moderate</b> impact on the reputation or brand of the organisation.</li></ul>



Low	A finding that could have a: <ul style="list-style-type: none"><li>• <b>Minor</b> impact on the organisation's operational performance; or</li><li>• <b>Minor</b> monetary or financial statement impact; or</li><li>• <b>Minor</b> breach in laws and regulations with limited consequences; or</li><li>• <b>Minor</b> impact on the reputation of the organisation.</li></ul>
Advisory	A finding that does not have a risk impact but has been raised to highlight areas of inefficiencies or good practice.

# Appendix 2 – Terms of reference

## **Background**

Sport Aberdeen came into operation in July 2010, managing sports and leisure facilities on behalf of Aberdeen City Council. Sport Aberdeen is set up as a charitable trust and as a non-profit organisation revenue generated is used to invest in the facilities and services in operation. Sport Aberdeen is fully funded through a regular annual grant from Aberdeen City Council, and is to support Aberdeen City Council in delivering the following objectives within the strategy “fit for the future”:

- Increase participation in sport to provide support for athletes and reward excellence
- Ensure high quality, well managed sport facilities in Aberdeen
- Recognise the contribution of sport, culture and arts in promoting the area as a tourist destination
- Recognise the role of sport and the arts in tackling anti-social behaviour.

As Sport Aberdeen is fully funded by the Council, it is required to meet the conditions attached to the grant funding and the arrangement falls under the Council’s Following the Public Pound Guidance. Recently Council Officers have raised concerns in respect of the arrangements in place with Sport Aberdeen, namely the late receipt of the business plan, differing financial figures being presented leading to queries over Sport Aberdeen’s financial viability and the overall governance and accountability arrangements in place. As a result, Council Officers have requested that internal audit independently review certain aspects of Sport Aberdeen’s arrangements.

## **Scope**

The objective of this review will be to independently review and challenge certain of Sport Aberdeen’s arrangements:

- Using the underlying financial records available at Sport Aberdeen we will assess the information and challenge the underlying assumptions (income and expenditure and balance sheet), including a review of how the Aberdeen City Council grant funding is utilised. This review will be linked to the requirements of the funding and service agreement.

- PwC will assess the assumptions underpinning the projections in the current Sport Aberdeen business plan, challenging the assumptions based on the data gathered above and based on review of other available Sport Aberdeen documentation made available to us. PwC will also conduct interviews with a number of relevant personnel at the Council and Sport Aberdeen.
- We will review and challenge Sport Aberdeen's financial arrangements, particularly considering how they are ensuring accurate and complete recording of information and underlying records. This will include considering the quality of management information submitted to those who are Accountable for Sport Aberdeen (Management Team and the Board)
- We will review the governance arrangements in place including considering: how the tone at the top is established, the key governance groups and reporting lines, quality of the information available; whether sufficient information is presented; and how effective the overall scrutiny role is discharged by the Board. In addition, we will also consider the governance arrangements for any alternative arrangements for service delivery put in place by Sport Aberdeen, including arrangements in respect of the management of Council facilities.
- We will consider the key management skills in place within the Sport Aberdeen Management Team, considering whether there are any gaps in skills both in terms of Management and also within those charged with Governance. In addition, we will consider the recent staff restructure and profiling of staff including staff management costs, linked to the business plan.

### **Limitations of Scope**

The scope of our review is outlined above. Our work will assume that the inputs to the accounting records of Sport Aberdeen have been properly extracted from relevant underlying documentation and we will not perform any procedures to check such extraction or accuracy. We will accept no responsibility for the achievement of any projections generated by our work, nor will we review any of the commercial risks associated with the viability of Sport Aberdeen, nor review any project contracts or other agreements.

Our work will not include any work in the nature of an audit and we will not verify any assets or liabilities of the business included in any of our deliverables.

# Appendix 3 - Limitations and responsibilities

## Limitations inherent to the internal auditor's work

We have undertaken a review of Sport Aberdeen, subject to the limitations outlined below.

### Internal control

Internal control, no matter how well designed and operated, can provide only reasonable and not absolute assurance regarding achievement of an organisation's objectives. The likelihood of achievement is affected by limitations inherent in all internal control systems. These include the possibility of poor judgment in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

### Future periods

Our assessment of controls relating to Sport Aberdeen is at August 2013. Historic evaluation of effectiveness is not relevant to future periods due to the risk that:

- the design of controls may become inadequate because of changes in operating environment, law, regulation or other; or
- the degree of compliance with policies and procedures may deteriorate.

## Responsibilities of management and internal auditors

It is management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.

We endeavour to plan our work so that we have a reasonable expectation of detecting significant control weaknesses and, if detected, we shall carry out additional work directed towards identification of consequent fraud or other irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected.

Accordingly, our examinations as internal auditors should not be relied upon solely to disclose fraud, defalcations or other irregularities which may exist.

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