

ABERDEEN CITY COUNCIL

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<b>COMMITTEE</b>	Audit, Risk and Scrutiny Committee
<b>DATE</b>	25 September 2018
<b>REPORT TITLE</b>	Internal Audit Report AC1829 – Stores Purchasing
<b>REPORT NUMBER</b>	IA/AC1829
<b>DIRECTOR</b>	N/A
<b>REPORT AUTHOR</b>	David Hughes
<b>TERMS OF REFERENCE</b>	2.2

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**1. PURPOSE OF REPORT**

- 1.1 The purpose of this report is to present the planned Internal Audit report on Stores Purchasing.

**2. RECOMMENDATION**

- 2.1 It is recommended that the Committee review, discuss and comment on the issues raised within this report and the attached appendix.

**3. BACKGROUND / MAIN ISSUES**

- 3.1 Internal Audit has completed the attached report which relates to an audit of Stores Purchasing.

**4. FINANCIAL IMPLICATIONS**

- 4.1 There are no direct financial implications arising from the recommendations of this report.

**5. LEGAL IMPLICATIONS**

- 5.1 There are no direct legal implications arising from the recommendations of this report.

**6. MANAGEMENT OF RISK**

- 6.1 The Internal Audit process considers risks involved in the areas subject to review. Any risk implications identified through the Internal Audit process are as detailed in the attached appendix.

## 7. OUTCOMES

- 7.1 There are no direct impacts, as a result of this report, in relation to the Local Outcome Improvement Plan Themes of Prosperous Economy, People or Place, or Enabling Technology, or on the Design Principles of the Target Operating Model.
- 7.2 However, Internal Audit plays a key role in providing assurance over, and helping to improve, the Council's framework of governance, risk management and control. These arrangements, put in place by the Council, help ensure that the Council achieves its strategic objectives in a well-managed and controlled environment.

## 8. IMPACT ASSESSMENTS

<b>Assessment</b>	<b>Outcome</b>
<b>Equality &amp; Human Rights Impact Assessment</b>	An assessment is not required because the reason for this report is for Committee to review, discuss and comment on the outcome of an internal audit. As a result, there will be no differential impact, as a result of the proposals in this report, on people with protected characteristics.
<b>Privacy Impact Assessment</b>	Not required
<b>Duty of Due Regard / Fairer Scotland Duty</b>	Not applicable

## 9. APPENDICES

- 9.1 Internal Audit report AC1829 – Stores Purchasing.

## 10. REPORT AUTHOR DETAILS

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# ABERDEEN CITY COUNCIL

## Internal Audit Report

### Operations

### Building Services Purchasing

**Issued to:**

Rob Polkinghorne, Chief Operating Officer  
Mark Reilly, Chief Officer – Operations & Protective Services  
Craig Innes, Chief Officer – Commercial and Procurement  
Sandra Buthlay, Interim Chief Officer – Finance  
Fraser Bell, Chief Officer – Governance  
Graham Williamson, Operations Manager  
Colin Maciver, Quantity Surveying Manager  
External Audit

## **EXECUTIVE SUMMARY**

Ordering and procurement of stock for repairs, maintenance and capital improvements on the Council's property portfolio is undertaken by Building Services supported by Commercial and Procurement Services. In 2017/18 total spend on materials, including direct issues to jobs was £5.256 million.

The objective of this audit was to consider whether adequate controls are in place regarding procurement and receipt of materials. This involved a review of procedures and analysis of procurement spend by Building Services for the financial year 2017/18.

Sixteen Suppliers were examined with which approximately 87% of Service expenditure is incurred. In five cases, covering over 15% of supplier expenditure in 2017/18, current contracts were not in place. In two cases contracts expired in February 2018 and Commercial and Procurement Services are in the process of adopting these Suppliers under a revised Framework Agreement. The remaining three contracts, from which the Service has procured items with a cumulative value in excess of European Procurement thresholds, expired between two and four years ago. The Service has stated that a transition period between one contract expiring and a replacement commencing is unavoidable and that it has been managing best value through ensuring that previous suppliers' costs are maintained. In addition, continuity of supply has been important to ensure that work can continue. The Service is currently working with Commercial and Procurement Services to ensure compliance with procurement rules and will have contracts in place or be able to otherwise demonstrate appropriate consideration and compliance by September 2018.

An issue was also raised during the audit regarding the fact that staff who were authorising orders were, occasionally, organisationally junior to the officer raising the order. Whilst segregation of duties was being evidenced, there is a risk that more senior staff could apply pressure on these staff to approve orders. The Service considered that the risk to service disruption, due to the low number of senior staff being available to approve orders, was greater but will introduce secondary controls.

# **1. INTRODUCTION**

- 1.1 Ordering and procurement of stock for repairs, maintenance and capital improvements on the Council's property portfolio is undertaken by Building Services supported by Commercial and Procurement Services. In 2017/18 total spend on materials, including direct issues to jobs was £5.256 million.
- 1.2 The objective of this audit was to consider whether adequate controls are in place regarding procurement and receipt of materials. This involved a review of procedures and analysis of procurement spend by Building Services for the financial year 2017/18.
- 1.3 The factual accuracy of this report and action to be taken with regard to the recommendations made have been agreed with Graham Williamson, Operations Manager, Colin Maciver, Quantity Surveying Manager, and Craig Innes, Chief Officer – Commercial and Procurement.

## 2. FINDINGS AND RECOMMENDATIONS

### 2.1 Written Procedures & Guidance

- 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 of correct and consistent practices being followed, especially in the event of an experienced employee being absent or leaving.
- 2.1.2 Current procedures are represented in clear flowcharts showing the various stages in order processing and authorisation. These largely mirror current Financial and Procurement regulations, and testing undertaken as described below (section 2.3: Purchasing) shows general compliance with the procedures.
- 2.1.3 It is indicated within the purchasing flowchart that when Purchase Orders are raised which are within the authorisation limits of the person raising them, they are either automatically approved, or may be approved by another user with the same authorisation limit. This was queried with the Service who confirmed that this is merely an error in wording and that an order does require secondary approval from an appropriate member of the Team.

#### **Recommendation**

The Service should amend the purchasing flowchart to reflect current practice

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

Agreed. This process will be reworded by the Service, to reflect the correct process which is being followed.

#### **Implementation Date**

August 2018

#### **Responsible Officer**

Quantity Surveying  
Manager

#### **Grading**

Important within audited  
area

- 2.1.4 It was noted during review of a sample of purchases (section 2.3: Purchasing) that in some instances officers with the same or lower authorisation limits to the officer preparing the purchase requisition were recorded as having authorised them. Although there is segregation of duties evidenced in these cases, the control is weaker as officers might approve orders because they have been instructed to do so by senior officers.

#### **Recommendation**

The Service should ensure orders are authorised by officers senior to the requisitioner.

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

During the previous audit on Stores Materials, carried out in August 2016, this same item was discussed. At the time, it was decided by the Service that the risk of disruption to service delivery was too great, based on the low numbers of senior staff in these teams, and the high number of orders raised. The Service does acknowledge that this risk exists, and will put in place separate controls to balance the risk against the costs of maintaining service delivery. Following a review, and risk assessment, the Service has identified other solutions to this risk. The Service proposes to discontinue the use of the 'Total View' I.T. system for authorising orders, as a weakness was identified where orders are only displayed in summary form, and do not give full details of the order to the authoriser, which does not give the authoriser the opportunity to scrutinise the order and spot any anomalies. The full 'Total' system gives much more detail, and only that system should be used for authorising orders. The second control will be a weekly

sample audit, to be run by the Stores Contract Manager, which will highlight any discrepancies. These controls are in addition to existing controls and alert reports.

<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
August 2018	Stores Contract Manager	Significant within audited area

- 2.1.5 It was additionally noted on the flowcharts that the stores delivery process had yet to be produced. However, the Service confirmed this process was present but the flowchart had not been updated to reflect this. The Service confirmed that documentation was reviewed periodically or following an audit, however given the documentation was dated March 2016, it may be preferable to schedule reviews to ensure all documentation remains current.

**Recommendation**

The Service should ensure that procedural guidance is reviewed regularly and updated promptly.

**Service Response / Action**

There are reviews scheduled as part of the Quality Management plan and ISO9001 accreditation. The Service will continue to review the processes periodically or following an audit.

<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
October 2018	Stores Contract Manager	Important within audited area

- 2.1.6 Staff order the majority of materials from a list of Suppliers contained within 'Supplier Dashboards'. These were examined and found to contain suppliers with whom valid agreements are not currently in place: contracts had either expired or framework agreements had not been formally adopted for use by the Council (see further discussion in section 2.2: Procurement below). In addition, whilst the Dashboards indicated other contracts had expired, some had been renewed and the Dashboards not updated.

- 2.1.7 Use of the Dashboards if they are not up to date could encourage the use of off-contract suppliers, with whom there is no valid agreement in place. This presents a risk to best value for the Council and an increased risk of breach of local and national procurement regulations. This risk could in part be mitigated by timely monitoring of spend with Suppliers with whom agreements have lapsed where there is a transition period from one Supplier to another to ensure that expenditure in excess of relevant procurement thresholds does not occur off contract. Where such expenditure is identified the Service should remove the Supplier from the dashboards to prevent off contract expenditure in contravention of Financial Regulations.

**Recommendation**

The Service should ensure that spend with off contract Suppliers (due to transitional arrangements) is monitored, in lieu of new contractual arrangements being put in place, with appropriate action being taken where expenditure is anticipated to be in excess of relevant procurement thresholds.

**Service Response / Action**

The Service and CPS are aware of these particular expired contracts, and have managed the risks during a transition to a new tender. A transition period is unavoidable once one tender expires, and the stores have a need to continue to supply the same materials to supply ongoing projects, without interruption or changes to the specification. The risks are mitigated due to these particular suppliers having held their previous

prices, providing the best value to the Council. There is concern that should a fully compliant route be insisted upon then there could be significant additional cost to the Council. Specifications are also tightly controlled by the Service, and orders are placed on ACC or framework terms and conditions. The Service and CPS are in the process of preparing fresh procurement routes for tendering these contracts, and they will continue working on these. This issue was raised within the previous audit in August 2016, and this transition period was agreed under action 2.3.4. The Service has been encouraged to seek savings and efficiencies wherever possible, rather than compliance at all costs, in collaboration with CPS colleagues. The Service will continue to use the best value supplier option to ACC, and will continue to liaise and work together with CPS to maintain compliance, while also providing the best value and cost savings to the council.

**Audit Position**

This had previously been signed off by Internal Audit based on the response that the expected transition period would be three months, which is reasonable. The contracts referred to below have been out of date for between two and four years, hence the reason that the recommendation has been made again. Whilst it is accepted that there will be a transition period and goods will be required to allow for continuation of projects and works, as stated, lengthy periods of off contract spend present compliance risks to the Council. Concerns over additional costs to the Council (by being fully compliant) have been raised by the Service. It is for the Service, in conjunction with Commercial and Procurement Services, to consider and determine the best procurement option and the balance of risk to be accepted. This consideration, including fulfilment of any requirements for authorisation, notification and publication, needs to be evidenced in advance of procurement routes being selected.

<b><u>Implementation Date</u></b>	<b><u>Responsible Officer</u></b>	<b><u>Grading</u></b>
September 2018	Quantity Surveying Manager Chief Officer – Commercial and Procurement	Significant within audited area

**2.2 Procurement**

- 2.2.1 Supplies of goods and services for which expenditure exceeds £50,000 over the lifetime of a contract or framework agreement require the approval of the relevant Committee. Where a contract has been established with a Supplier following Committee approval, it should be registered on the Aberdeen City Council Contracts Register.
- 2.2.2 Framework agreements cover a list of Suppliers arranged either locally or by a national body (such as Scotland Excel) for the provision of specific goods and services, within the terms of an overarching contract. Although these typically set terms and conditions and pricing structures, there is no commitment at that point to purchase any of the supplies. From these agreements individual Local Authorities must select suppliers and enter into contracts with them according to their own requirements and in accordance with procurement and financial rules.
- 2.2.3 The Council's Procurement Regulations require Head of Commercial and Procurement Services approval before contracts may be drawn down from framework agreements and, as noted above, Committee approval is required prior to entering into contracts in which over £50,000 will be spent. Services should not directly enter into contracts with, or obtain supplies from, suppliers on a national framework until these approvals have been obtained.



- 2.2.4 Following approval of Housing Revenue and Capital budgets by Committee on 3 December 2015, minutes from a meeting of the Communities, Housing and Infrastructure Committee on 25 August 2016 confirmed that approval had been given for relevant expenditure on repair, maintenance and upkeep of housing stock for a 4 year period by Building Services of £3.45million per annum for 2016/17 and 2017/18 and £2.95million per annum for 2019/20 and 2020/21. Minutes from the same meeting confirmed that approval had additionally been given for expenditure relating to heating and plumbing supplies and installation to the value of between £1.5 and £1.61 million per annum between 2016/17 and 2019/20. Examination of expenditure by the Service for 2017/18 confirmed that they had not exceeded these expenditure limits.
- 2.2.5 Sixteen suppliers were identified with whom expenditure had exceeded £50,000 between April 2017 and March 2018. Of these, valid contracts were in place for only eleven.
- 2.2.6 Framework agreements for two suppliers (paint and construction goods) had lapsed in February 2018. Commercial and Procurement Services have confirmed that work is underway for the adoption of these suppliers via a revised framework agreement.
- 2.2.7 Contracts with another two suppliers (windows and frames) expired in March 2014, with records showing expenditure of £422,629 and £254,138 between April 2015 and March 2018.
- 2.2.8 The contract with the final supplier (kitchens) ceased in March 2016, since which time the Service has incurred expenditure of £289,225 between April 2016 and March 2018.
- 2.2.9 The Service has stated that the majority of expenditure consisted of individual elements of spend of less than £10,000 and that 4 quotes were sought in the majority of cases. Examination of records confirmed this, except for two purchase orders for amounts of around £90,000 for goods commissioned from one of the suppliers in 2017, where there was no record of competitive quotations, tendering or separate approval on file.
- 2.2.10 However, as set out in the Council's Procurement Regulations, cumulative spend must be taken into account where there is regular expenditure on the same type of supply, and contracts must not be split to avoid the requirement for tendering and approvals. Expenditure on each of these supplies has exceeded EU public procurement threshold limits and should therefore have been subject to appropriate tendering procedures.
- 2.2.11 The Service stated it had continued to use the above suppliers due to them being able to supply materials which were considered to be of a high quality, lifespan and reasonable price and to meet architectural specifications. There was also suggestion that use of particular suppliers in the past necessitated continued purchasing from them in order to maintain assets, and replace parts, to the same specification.
- 2.2.12 The Service has stated that quotations for goods from other suppliers have been aggregated and compared to the original tender quotations from the aforementioned suppliers and their prices have remained competitive. Additionally, the types of materials currently being supplied are of a type which meet Architectural requirements and retain backward compatibility for ease of repairs or replacement. However, these arguments for single-sourcing supplies have not been tested through competitive tendering or other market testing exercises and this approach is in contravention not only of the Council's Procurement Regulations but also of Scottish Domestic Procurement law and the European Public Procurement Regime. There is additionally a potential risk of legitimate legal challenges from other suppliers, who may be able to supply similar items, claiming undue loss due to the Council's non-compliance with legislation. Regardless of the outcome of any legal action, this could expose the Council to legal costs, reputational damage and possible disruption of service delivery.

**Recommendation**

The Service, in conjunction with Commercial and Procurement Services, should ensure that valid contracts are in place or are established through competitive tendering for all supplies in excess of Council, National and EU thresholds.

The Service, in conjunction with Commercial and Procurement Services, should develop and implement a forward plan for procurement to ensure that future tendering exercises are completed prior to the expiry of existing contracts.

**Service Response / Action**

The Service will continue to work with CPS, and will maintain the forward plans, which have existed in various formats for several years. A new process for this has been proposed by CPS, which the Service will adopt. The Service has been fully transparent about these contracts, and has been working closely with CPS on all these issues, obtaining guidance throughout the process. With the windows example, a decision was made in the interest of best value to the council, to source windows that met the architect's requirements, and also provided the lowest long term maintenance costs to the council, providing savings over the material's life cycle. The competitive market testing was provided by reviewing the submitted price against the same supplier's previous winning tender bid. The total aggregated figure was also made up of several other purchases, which did include several competitive quotation exercises. This particular contract falls within the category of savings and efficiencies taking priority over compliance, and CPS have been liaised with in this regard. Compliance will be further considered under the action agreed at 2.1.7 above. Stores only purchase standard stock material, project material goes through a completely different process. The forward plan for 2018 has already been issued to CPS, and the Service will work with CPS to ensure savings and value for money in these contracts.

**Implementation Date**

September 2018

**Responsible Officer**

Quantity Surveying  
Manager  
Chief Officer –  
Commercial and  
Procurement

**Grading**

Major at a Service Level

**2.3 Purchasing**

- 2.3.1 Financial Regulations stipulate that all orders should be made on official purchase order forms appropriately authorised in advance of ordering goods or services from a Supplier. Review of a sample of 20 items of expenditure selected at random from April 2017 to March 2018 demonstrated that this was the case in practice.
- 2.3.2 It is important that all goods which are received are recorded in the stock system or those which have been bought in direct for jobs can be identified as having been allocated to a job. In all 20 instances reviewed records were complete.

**AUDITORS:** D Hughes  
C Harvey  
D Henderson

## 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.