MOORE STEPHENS

Park Transformation

Internal audit report for London Legacy Development Corporation

Status – Final

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Document history			Distribution	
Draft	V01	20/12/2013	[redacted]	Senior Programme Manager
Final			Colin Naish [redacted]	Executive Director of Infrastructure Senior Programme Manager

Contents

1 Introduction

1.1 This audit was completed in accordance with the approved annual Internal Audit plan for 2013/14.

1.2 The overall objective of this review was to provide assurance to the LLDC on the processes in place to support the effective financial management of the park transformation during a period of significant expenditure up to completion. This was achieved through a review of the processes and financial controls in place to meet the requirements of the Transformation Execution Plan. The full key risks addressed by this audit and scope of the audit are detailed in the extract from the assignment terms of reference at Appendix A.

1.3 The Infrastructure Directorate is responsible for the transformation of the Olympic Park, a key component for ensuring a legacy is secured. The Directorate was seconded to the London Legacy Development Corporation (LLDC) from the Olympic Delivery Authority (ODA) in 2011. A current base budget of £292 million is in place for the delivery of the project.

2 Conclusion

(Amber-Green)	Minor weaknesses have been identified in the control framework or non-compliance which may put achievement of system objectives at risk.

2.1 There is a satisfactory approach for the financial management of the transformation project in line with the processes set out in the LLDC Programme Execution Plan and LLDC key corporate processes. There remain appropriate governance arrangements in place since we reported on this area in our last review in June 2013. A focus of this review has been the level of assurance provided to LLDC, particularly in terms of costs and budgets. Overall, the reporting of assurance on project progress, costs and budgets adequately meets the requirements set out in the Programme Execution Plan. However, at this stage in the programme an enhanced level of cost assurance would be beneficial to LLDC in ensuring the level of certainty over costs – and in reducing the likelihood of cost surprises arising at late stages in the remaining projects. We have made a number of recommendations in the report intended to improve the level of cost assurance provided to LLDC by Mace. One example is the inclusion of an Anticipated Financial Cost (AFC) trend report that would provide immediate assurance to LLDC that the AFC is stable or moving in a positive direction over time. The most significant recommendation made in the report also addresses the area of cost assurance – in this case assurance over the controls in place by contractors to minimise the likelihood of fraud on projects. There are currently controls in place to counter fraud across the programme, but these tend to be of a detective nature. In our recommendation we advocate that a more proactive approach is taken.

2.2 The AFC report is a key tool for management in assessing the likely cost outturn for the programme. The AFC process is well-established and understood and was found to be operating effectively. During the review a number of minor discrepancies were identified – for example in tracing back the detailed composition of AFC to supporting documents. These discrepancies did not significantly affect the quality of the management information provided, but they may reflect the challenging monthly reporting cycle deadlines, where deliverable review concentrates on the accuracy of core management information. Our recommendations highlight a small number of areas where the quality of management information review should be strengthened to ensure that all aspects of status reports are checked prior to release.

2.3 .An important element of the AFC is the output from the risk management process. In particular the level of project risk as measured through quantitative risk analysis (QRA) reports. We reviewed the risk management process and tested a sample of QRA reports. As with the AFC process, we found that the process and controls were operating effectively and as intended. However, similarly we identified a small number of discrepancies in the risk reports which could indicate pressure on quality review for these deliverables. Again these discrepancies did not materially affect the overall quality of the management information provided, but it remains a control point that should be addressed. As part of our review we also assessed how cost risk is being dealt with through the risk management process. We found that cost risk is addressed appropriately at project, programme and corporate level. Cost risk is specifically included on the LLDC Corporate Risk Register for example.

2.4 LLDC's change control processes were also reviewed and tested – particularly in terms of reporting and reviewing the costs associated with any change request. The change control process was found to be operating effectively. No issues were identified.

2.5 This review covered as one of its core risk areas the processes and control in place to ensure efficient and cost-effective handover of projects upon completion. Our review was based upon review of documentation and discussion with both project management and client staff who have had experience of the handover process. The process was found to be comprehensive and fit for purpose.

2.6 The following table summarises the recommendations made across the key risks audited, grouped by priority ratings:

No.	Key risk	Priority rating		
		1	2	3
1	Costs exceed Budget	-	1	2
2	Forecasts are unreliable as a basis for financial planning to completion	-	1	2
3	Changes are not recognized or the related financial estimates are incorrect	-	-	-
4	Activities to be handed over are not identified sufficiently in advance which leads to inefficiencies and potential risks	-	-	-
	Total recommendations made	**-**	**2**	**5**

2.7 The recommendations and associated management actions arising from the above are detailed in section 5.

3 Key findings

3.1 **Key Risk 1: Costs exceed Budget**

3.2 A key mitigation activity for this risk is to ensure effective contract management. In the case of Transformation this will be in line with the requirement set out in the Programme Execution Plan. As Project Management Partner (PMP) Mace have been appointed to provide project and cost management services to support LLDC in meeting their programme objectives. MACE are responsible for ensuring that contractors deliver work on time and to budget.

3.3 MACE provides LLDC with a number of key assurance reports on a monthly and quarterly basis. Monthly Project Status Reports (PSRs) are produced by Mace to provide assurance to LLDC on project progress and to flag early warnings and potential risks and issues. We reviewed the PSRs for the individual projects from the October 2013 review schedule and found that they provide a clear overview of the progress of each individual project along with a full financial summary. One of the key success measures highlighted in the status reporting is the earned value (EV) analysis. EV analysis enables the comparison of the value of project work delivered against the planned value of that work and also the actual cost incurred. During the Transformation programme EV reporting has proven to be a useful management tool (particularly on the larger projects such as All Park) and one which has formed a driver in management decision making. We reviewed the process for EV report production and found that the controls applied by Mace provide reasonable assurance over the EV figures included in the PSRs.

3.4 The Deep Dive Report provides a level of assurance over and above the monthly review and reporting cycle. Based upon a review meeting attended by key LLDC and Mace staff, the review provides an in-depth snapshot of the project, including metrics and full commentary of issues and status. We reviewed the report for South Park from October 2013 The report included project status summary, programme and key milestones, performance to date broken down by WBS (work breakdown structure) and also key information on budget, cost pressures and risk and contingency.

3.5 The current assurance and project status reporting arrangements provide management with a range of useful data that provides a good snapshot of each project – and an aggregated summary for the Transformation Board. However, there are additional assurance reports that could be introduced that would further improve the effectiveness of the cost assurance review. These reports are: (i) A RAG (Red/Amber/Green) indicator, or similar measure, to reflect the quality of contractor cost processing and control and (ii) A breakdown of the degree of assurance obtained over the component parts of actual project cost. (**Recommendations 1 and 2**).

3.6 Fraud continues to represent a significant cost risk in all sectors of the economy. For example, in 2012 the National Fraud Authority estimated that fraud in the construction sector alone amounted to around £3 billion per year. It is therefore important that a proactive approach is taken to mitigate fraud and corruption risks. We reviewed the processes and controls in place to mitigate fraud and corruption risk within Transformation. We established that there are controls in place (for example including anti-fraud controls requirements in work instructions, the use of a construction reporting line for reporting suspicion of fraud and the monitoring of potential fraudulent activity through the cost verification programme). However, these controls are largely reactive and detective in nature. A more proactive approach should be taken by mace to verify that the Tier 1 contractors are adequately addressing fraud and corruption risk. **(Recommendation 3)**

3.7 To help convey the appropriate message within the organisation as to the importance of cost risk, control and assurance it is important that cost risk is appropriately prioritised and managed at all levels within the programme. A key element of this is treating cost risk effectively within the overall risk management process. We reviewed how cost risk is captured, managed and reporting in the risk management process and established that current arrangements ensure that it is correctly captured and prioritized. These arrangements include appropriate categorization and impact assessment, escalation and reporting. One good example of this prioritisation is the inclusion of a specific cost risk on the LLDC Corporate Risk Register.

3.8 The governance arrangements for the Transformation programme were reviewed in detail as part of our previous report on Park Transformation Assurance Processes (June 2013). These arrangements, based upon the framework set out in the Transformation Execution Plan, were found to be clear and effective. This review has concentrated on any governance changes implemented since our last review and has concluded that arrangements continue to be appropriate and effective. .

3.9 **Key Risk 2: Forecasts are unreliable as a basis for financial planning to completion**

3.10 The Anticipated Final Cost (AFC) is produced on a monthly basis to ensure that LLDC always has a current and realistic view of their projected transformation outturn costs. The AFC process is a key element in identifying potential cost pressures and opportunities and reporting them to the appropriate level of management both in PMP and LLDC. .

3.11 MACE provides a full and detailed budget forecast for all individual projects, combining these into a final summary for review at the Transformation Board. The AFC incorporates the Current Baseline Budget, current commitments, acknowledged trends, unsubstantiated trends and the Quantitative Risk Analysis outcome.

3.12 We reviewed the reporting process for AFC within the monthly status reporting cycle. Generally the content and presentation of AFC information was found to be clear and consistent. However, one element that is currently not incorporated in the reports is any trend analysis of AFC movement over time. Such a report would give a clear indication that AFC levels are stable or are moving in the required direction if reductions are targeted. The trends should show the AFC against the current baseline budget (CBB). **(Recommendation 4)**

3.13 We tested the calculation of the figures included within the AFC for the All Park South Park and Aquatics Projects for both October and November reporting periods and traced the figures through to source documentation to ensure that they were accurately presented**.** One discrepancy was identified in the November AFC Report for All Park where the Monthly Movement figure for Acknowledged Trends per the detailed Trends section of the Cost Report differed from the figures used in the Cost Report Summary and subsequent AFC Report by £49.5K. A re-performance of the calculated Acknowledged Trends total in the detailed Trends section indicated that this figure had been correctly calculated. There was therefore no apparent reason why this figure should not have been used in the subsequent reports. **(Recommendation 5)**

3.14 As part of our testing we also verified that items are not remaining as Acknowledged Trends for greater than the three month guideline. This control appears to be operating effectively as no items were identified as remaining in excess of the guideline period.

3.15 One of the key elements of the AFC is the output from the risk management process. MACE perform monthly Quantitative Risk Analyses (QRAs) for each project. Project Managers maintain their own project risk registers which are updated following a monthly risk review meeting led by an experienced risk manager from the Central Team. The Central Team then run a Monte Carlo analysis on the data from this meeting and the results are sent back to the project team for approval before inclusion in the final version of the QRA report. This information then forms a component part of the AFC for the period. As part of the monthly review cycle risks are then reviewed by the Project Implementation

Review groups. We reviewed a sample of QRA Reports to verify that data was complete, timely and subject to regular review. We found that the information in the QRA reports was consistent and accurate. However, some minor discrepancies were identified between data in the Executive Summary section of the October Risk Report and the Monthly Transformation Programme Report for the same period. There were also some inconsistencies in the presentation of numbers as positive or negative in the Risk Summary sections of the QRAs. The quality review arrangements for these reports should be strengthened and any the reasons for any valid inconsistencies between data should be clarified in the report. **(Recommendation 6)**

3.16 There is a monthly process in place for the reconciliation of the Mace to the LLDC financial records due to a timing difference in period end cut-off. We reviewed and tested this reconciliation process and found it to be operating effectively.

3.17 **Key Risk 3: Changes are not recognised or the related financial estimates are incorrect**

3.18 There is a formal and documented change control process in place which accommodates both programme and corporate change control. The process is managed by LLDC and coordinated between LLDC and the PMP. Potential change requests are gathered from the project teams every month and are reviewed at the PMP Internal Change Meeting. The list of approved changes resulting from this review, which cannot be added to (except in exceptional circumstances with Executive Director approval), is collated and passed to LLDC. These changes then pass through the LLDC change control process. This involves formal review at Pre-Meeting and Change Control Board meetings. Items passed to the Change Control Board will be approved, deferred or rejected. Approved items are passed to Finance staff for completion of appropriate virements and update to the CCB. The CCB can only be updated through changes approved by the Change Board.

3.19 Change requests are submitted on standard templates. Impacts of the change are detailed and any uncertainties (such as assumptions or dependencies) would be captured in the summary and description fields. This helps to ensure that all elements of the cost impact of the change – both known and uncertain – are properly captured for review by the Board.

3.20 We reviewed a sample of change control notices (CCNs) submitted to the October and November Change Control Boards for the ALL Park, South Park and Aquatics projects. In all cases notices had been properly completed and approved. The supporting documentation appended to the CCNs was appropriately detailed and comprehensive, with clear indication of challenge and discussion prior to approval.

3.21 **Key Risk 4: Activities to be handed over are not identified sufficiently in advance which leads to inefficiencies and potential risks**

3.22 The Transformation programme has reached the point in its maturity where projects are being handed over to operators for future use. There are a number of inherent risks in the handover phase of any project which must be addressed through effective project procedures and controls. Risks include handover of assets and deliverables that do not meet the required objectives or meet expected quality. There may be completeness or snagging issues. Also there may be a failure to hand over all of the supporting deliverables and documentation that will be necessary for future effective operation (including drawings, plans, warranties and maintenance procedures). All of these risks may have current or future cost implications. Controls to mitigate these risks include having an effective, agreed and documented handover process, ensuring that all stakeholders are involved in handover on a timely basis through effective stakeholder communications and maintaining up to date contractor schedules which incorporate key handover milestones. Our review revealed that the T-12 handover process that is currently used for programme handover incorporates both the stages of completion and take-over. T-12 relates to 12 weeks before the handover milestone, when the handover process formally commences. The process was found to be comprehensive and well documented. All of the potential risk areas noted above are addressed by the process, which provides a robust and effective framework for controlling the handover phase of a project. Stakeholder involvement is addressed in detail, as are the production of workstream acceptance certificates (WACs) which are cross-referenced to key deliverables. This last procedure provides a good control over the completeness of deliverable handover. We were able to verify the effectiveness of the process through discussion with one of the project sponsors who has been involved in two project handovers. He was able to confirm that the T-12 handover process was fit for purpose and accommodated the requirements of the client, PMP and nominated stakeholders. It also provides an element of flexibility where an even greater control level is required (for example in the case of the Aquatics project the handover period was started four weeks earlier than usual at T-16.

4 Audit approach

4.1 The audit was undertaken through discussions with key staff identified, documentation review and sample testing where appropriate.

4.2 A list of the LLDC staff consulted during the completion of this review is included at Appendix C.

5 Recommendations and management action plan

Finding and implication	Recommendation	Priority	Management response, responsible officer and implementation date
The current project status reporting does not include any assurance indicator over the cost capture, processing and reporting by the Tier 1 contractors. This could be based on a composite view of a contractor's level of disallowed costs, rejected NCEs (notified compensation events), level supporting evidence for applications and level of delays and errors in cost reports provided. **Implication**: A greater level of assurance could be provided on the cost risk by contractor than is currently in place. .	1. A RAG indicator or, similar measure, to reflect the quality of contractor cost processing and control.	3	Management Response: Recommendation accepted Action to be taken: Implement RAG indicator for contractor cost processing and control. Responsible officer: Colin Naish Date for implementation: 31 January 2014
The current project status reporting does not include an assurance report over the actual cost of each project. Such a report should include a breakdown of the total level of actual cost per project, broken down by category of cost. Categories should include total cost finalized, total cost for work completed, total cost verified. The balancing level of cost would then give an indication of the level of actual project cost that would still be subject to variation, thus representing an aspect of cost risk. . **Implication**: A greater level of assurance could be provided on the risk to actual cost than is currently in place	2. A breakdown of the degree of assurance obtained over the component parts of actual project cost.	3	Management Response: Recommendation accepted Action to be taken: Incorporate into project status reporting a breakdown of the total level of actual cost per project. Responsible officer: Colin Naish Date for implementation: 31 January 2014
Current controls to mitigate fraud and corruption tend to be reactive and detective rather than proactive such as ensuring appropriate policies and procedures are in place and that suitable fraud awareness programmes have been performed by Tier 1 contractors. **Implication**: The effectiveness of the mitigation of fraud and corruption risk could be improved across the programme.	3. A more proactive approach should be taken by Mace to verify that the Tier 1 contractors are adequately addressing fraud and corruption risk.	2	Management Response: Recommendation accepted Action to be taken: Design and initiate a programme of reviews of Tier One contractors' anti-fraud procedures and their implementation. Responsible officer: Colin Naish Date for implementation: 28 February 2014

Finding and implication	Recommendation	Priority	Management response, responsible officer and implementation date
There is currently no trend analysis of AFC movement over time included in the project status reporting process. **Implication**: Incremental AFC growth or insufficient and timely AFC reduction is not readily indicated by the current status reports.	4. An AFC trend analysis (for example a graphic presentation) should be included in the project status reports. The trends should show the AFC against the current baseline budget (CBB).	3	Management Response: Recommendation accepted Action to be taken: Incorporate AFC trend analysis into project status reports Responsible officer: Colin Naish Date for implementation: 31 January 2014
In reconciling AFC report data back to supporting documents (detailed Trend section of the Cost Report) a discrepancy of £49.5K was identified in the All Park Project in the total figure for the Monthly Movement of Acknowledged Trends. **Implication**: Inconsistencies and errors may be included in final reports.	5. AFC reports should be reconciled to supporting data and reports in all cases prior to be finalized.	2	Management Response: Recommendation accepted Action to be taken: ensure AFC reports are reconciled to supporting data as part of reporting cycle. Responsible officer: Colin Naish Date for implementation: 31 January 2014
Some minor discrepancies were identified between data in the Executive Summary section of the October Risk Report and the Monthly Transformation Programme Report for the same period. There were also some inconsistencies in the presentation of numbers as positive or negative in the Risk Summary sections of the QRAs. **Implication**: There may be further inconsistencies in these management reports.	6. The quality review arrangements for Risk Report and QRA reports should be strengthened and any the reasons for any valid inconsistencies between data should be clarified in the report.	3	Management Response: Recommendation accepted Action to be taken: hold an implementation review style meeting to review and challenge the output of each month's QRA analysis Responsible officer: Colin Naish Date for implementation: 31 January 2014

Appendices

A Audit objectives

The objective of this review was to provide assurance to the LLDC on the processes in place to support the effective financial management of the park transformation during a period of significant expenditure up to completion.

The review considered the following areas:

- The process of forecasting expenditure through to completion;
- Other sources of assurance in relation to the transformation of the park which LLDC can rely on;
- The process of identifying and monitoring changes and their financial consequences;
- The handover process post March 2014.

As part of the audit we will take into account any 'deep dives' which have been undertaken in relation to Park transformation.

The scope of the audit will also include expenditure on the stadium, however this will be restricted to financial management issues and will exclude wider project/ programme management processes.

The key risks centre around the probity and regularity of the financial management and control processes, specifically in relation to expenditure on park transformation. The key risks to be covered include:

- The costs exceed the budget;
- Forecasts are unreliable as a basis for financial planning to completion;
- Changes are not properly recognised or the related financial estimates are incorrect;
- Activities to be handed over are not identified sufficiently in advance which leads to inefficiencies and potential risks.

B Audit definitions

Opinion/conclusion	
(Green)	Overall, there is a sound control framework in place to achieve system objectives and the controls to manage the risks audited are being consistently applied. There may be some weaknesses but these are relatively small or relate to attaining higher or best practice standards.
(Amber-Green)	Minor weaknesses have been identified in the control framework or non-compliance which may put achievement of system objectives at risk.
(Amber)	Weaknesses have been identified in the control framework or non-compliance which put achievement of system objectives at risk. Some remedial action will be required.
(Amber-Red)	Significant weaknesses have been identified in the control framework or non-compliance with controls which put achievement of system objectives at risk. Remedial action should be taken promptly.
(Red)	Fundamental weaknesses have been identified in the control framework or non-compliance with controls leaving the systems open to error or abuse. Remedial action is required as a priority.

Risk and significance categories	
Priority ranking 1:	There is potential for financial loss, damage to the LLDC reputation or loss of information. This may have implications for the achievement of business objectives and the recommendation should be actioned immediately.
Priority ranking 2:	There is a need to strengthen internal control or enhance business efficiency.
Priority ranking 3:	Internal control should be strengthened, but there is little risk of material loss.

C Staff consulted during review

Name:	Job title
Jonathan Dutton	Executive Director of Finance and Corporate Services
Colin Naish	Executive Director of Infrastructure
[redacted]	Senior Programme Manager
[redacted]	Commercial Lead
[redacted]	Change Manager
[redacted]	Senior Manager - Assurance
[redacted]	Contract Administrator
[redacted]	Risk Lead
[redacted]	Project Controls Lead
[redacted]	Project Director
[redacted]	Project Sponsor - Venues

We would like to thank these staff for their assistance provided during the completion of this review.