

Final Internal Audit Report

Microsoft Office Enterprise Software Agreement

Procurement Compliance

April 2018

Distribution: Executive Director Resources (Final only)
 Interim Director of Commissioning, and Improvement
 Head of Commissioning and Improvement - Place
 ICT Category Manager
 ICT Contract Commercial Manager

Assurance Level	Recommendations Made	
Limited Assurance	Priority 1	1
	Priority 2	2
	Priority 3	0

Status of Our Reports

This report ("Report") was prepared by Mazars Public Sector Internal Audit Ltd at the request of London Borough of Croydon and terms for the preparation and scope of the Report have been agreed with them. The matters raised in this Report are only those which came to our attention during our internal audit work. Whilst every care has been taken to ensure that the information provided in this Report is as accurate as possible, Internal Audit have only been able to base findings on the information and documentation provided and consequently no complete guarantee can be given that this Report is necessarily a comprehensive statement of all the weaknesses that exist, or of all the improvements that may be required.

The Report was prepared solely for the use and benefit of London Borough of Croydon and to the fullest extent permitted by law Mazars Public Sector Internal Audit Ltd. accepts no responsibility and disclaims all liability to any third party who purports to use or rely for any reason whatsoever on the Report, its contents, conclusions, any extract, reinterpretation, amendment and/or modification. Accordingly, any reliance placed on the Report, its contents, conclusions, any extract, reinterpretation, amendment and/or modification by any third party is entirely at their own risk.

Please refer to the Statement of Responsibility in Appendix 3 of this report for further information about responsibilities, limitations and confidentiality

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1. Introduction

- 1.1 As part of its ICT Transformation, the Council has moved from a perpetual license arrangement to a cloud-based subscription arrangement with Microsoft.
- 1.2 A mini-competition was run using the Crown Commercial Services RM1054 Technology Products Framework Agreement in March 2016 to determine which Microsoft license re-seller represented best value-for-money.
- 1.3 The contract was awarded to Insight Direct (UK) Ltd, with a contract value based on tender documentation of £2,049,492 (£683,164 ex. VAT annual value over three years).
- 1.4 Following the tender process, two invoices were paid in August 2016 totalling £740,481.93 ex. VAT. This equates to a contract value of £2,221,446 over three years assuming the license requirement does not decrease.
- 1.5 A third invoice was paid in September 2016 totalling £82,992 ex VAT. An additional 800 licenses were required as it had not been identified during planning stage that transient and non-permanent workers would require access to applications via the Microsoft Office Enterprise Software Agreement. Two further purchase orders were raised for licenses totalling £40,904. If this is included in the contract value, the total over three years is £2,593,135.
- 1.6 This audit was undertaken as part of the agreed Internal Audit Plan for 2016/17.

2. Key Issues

Priority 1 Issues

A purchase order was raised in respect of the Insight Direct Ltd. appointment in place of a written contract as per the Tenders and Contracts Regulations. **(Rec. 2)**

Priority 2 Issues

The saving in the original strategy report was predicated on a lower and decreasing license requirement. However, the license requirement was understated due to the omission of transient workers and contractors. The saving originally envisaged may not be realised. This had not been identified at the point the CCB strategy report was approved. **(Rec. 1)**

The annual contract sum has risen by 26.5%. Although it is too early to tell whether the overall contract sum has risen by more than 25%, consideration should be given to making an early report to decision-makers. **(Rec. 3)**

3. Actions and Key Findings/Rationale

Control Area 2: Contract Strategy		Detailed Finding/Rationale		
Priority	Recommendation 1			
2	<p>Strategy and award reports should be reviewed prior to decision-making to ensure that contract and delivery strategies are consistent and that assumptions in regards to quantities are well-supported.</p> <p>Where it is identified that the future requirement for goods or services will be decreased with reference to the current requirement, the specific justifications as to why should be supported with underlying data where available.</p>	<p>The confidential Part B award report to the Cabinet Member for Finance and Treasury dated May 2016 stated that the estimated annual costs of the license agreement totalled £1.97million, based on a decreasing number of users initially set at 3,300.</p> <p>CCB strategy report 1103/15-16 stated that the estimates contained within it were based on 'starting with 3500 users (not the 4235 as currently [paid or] [sic]'. Furthermore, the saving in the report is predicated on a reduction in staff members, decreasing from 3500 in year one to 3000 in year five. It is unclear why this approach was taken, or, why it was expected that there would be a reduction of 735 users between March 2016 when the strategy report was approved, and April 2016 when the contract was due to be awarded.</p> <p>An additional 800 licenses had to be purchased following the award of the contract because the initial estimates did not take into account transient workers or contractors. However, the additional requirement should have presumably been known given that 800 added to 3500 is 4300, which was slightly more than the number of existing users at the point the strategy report was written.</p> <p>We were informed that an error had been made in that the '3500' quantity related to known individuals working for the Council. This was not an accurate assessment of how many licenses were required in practice as other licenses relating to servers or shared accounts had been omitted from this figure. This may have been due to insufficient challenge of underlying figures at the point the CCB strategy report was approved. As a result, the benefits specified in the business case may not be achieved.</p> <p>There is a risk that additional unexpected expenditure may be incurred. There is a risk that value-for-money may not be demonstrated where bidders are not provided with the opportunity to price on the basis of economies of scale. There is a risk that the robustness of information provided for decision making cannot be demonstrated.</p>		
Management Response		Agreed/Disagreed	Responsible Officer	Deadline
<p>We will ensure we adhere to process in relation to any contracts as per the recommendation above.</p> <p>Head of commissioning and Improvement - Place will refer this recommendation to the next CCB board for consideration.</p>		Agreed	Head of Commissioning and Improvement Place, ICT Category Manager	Completed

<u>Control Area 6: Formation of Contract, Compliance with the Contracting Authority's Legal Requirements, Retention and Security of Purchase Orders, Contracts and Deeds</u>			
Priority	Recommendation 2	Detailed Finding/Rationale	
1	<p>Staff should be reminded of the need to execute written contracts in accordance with the Tenders and Contracts Regulations.</p> <p>Consideration should be given to an application for a retrospective waiver.</p>	<p>Regulation 23 of the Tenders and Contracts Regulations states, 'The Council Solicitor and Monitoring Officer, the Heads of Legal Services or other person authorised by the Council Solicitor and Monitoring Officer must sign every written contract valued at £100,000 and above in accordance with the Council's Constitution and is responsible for settling the detailed terms thereof. However, the relevant Director may sign and settle the terms of Contracts valued at £100,000 and above if specifically authorised in writing to do so by the Council Solicitor and Monitoring Officer.'</p> <p>We were informed that only a purchase order was raised in respect of the contract with Insight Direct Ltd., initially valued at £2,049,492. A waiver was not obtained to relax the requirement to produce a signed written contract in respect of this contract.</p> <p>We were also provided with confirmation that an electronic agreement with Microsoft was executed. However, the Council's prime legal relationship in respect of the Crown Commercial Service's Framework is with Insight Direct Ltd.</p> <p>This represents non-compliance with the Tenders and Contracts Regulations.</p>	
Management Response		Agreed/Disagreed	Responsible Officer
<p>We accept that the Framework Call off contract should have been signed by both LBC & Insight at the time. However, both parties have implied terms & conditions in place and we have been adhering to these in our interactions.</p> <p>The framework call off contract has now been signed by LBC & Insight. A copy has been sent to the legal team and an electronic copy stored in the ICT contracts database.</p>		Agreed	ICT and SCC Category Managers
			Completed
		Agreed/Disagreed	Deadline

Control Area 6: Formation of Contract, Compliance with the Contracting Authority's Legal Requirements, Retention and Security of Purchase Orders, Contracts and Deeds

Priority	Recommendation 3	Detailed Finding/Rationale	Agreed/Disagreed	Responsible Officer	Deadline
2	<p>Consideration should be given to making a proactive report to the Cabinet Member for Finance and Treasury in respect of the increased contract sum, seeking approval for the variation to contract.</p>	<p>Regulation 29 of the Tenders and Contracts Regulations states, 'A report seeking authority for the change to the Contract must be made to the CCB, nominated Cabinet Member or Cabinet as appropriate... in any case, the original Contract value will be increased by more than 25%'.</p> <p>The initial annual value of the contract was £683,164. The annual value of the contract has risen to approximately £864,378 due to an increase in licenses. This equates to a 26.5% increase in the annual value, albeit not the contract value.</p> <p>We were informed that the Council may be reaching its limit on licenses, and that more may need to be purchased. In addition to this, a decrease in licenses is not guaranteed over a period of the next three years.</p> <p>There is a risk that the license agreement will become varied by more than twenty-five percent and this may not be identified to decision-makers in a timely manner.</p>	Agreed	ICT Contract Commercial Manager	7 th December 2017
Management Response		<p>We accept that a report should have been submitted to CCB/Cabinet Members as we cannot increase spend beyond 25% of original contract value without appropriate governance. The ICT Commercial Manager is currently putting a proactive report together and it will be submitted at the CCB meeting on 7th December 2017.</p> <p>It is worth mentioning that we have not yet breached any contract regulations at this time and we are still compliant with tender and contract regulation 29.</p>			

TERMS OF REFERENCE

Microsoft Enterprise Software License Agreement

Procurement Compliance

1. INTRODUCTION

- 1.1 As part of its ICT Transformation, the Council has moved from a perpetual license arrangement to cloud-based subscription arrangement with Microsoft.
- 1.2 A mini-competition was run using the Crown Commercial Services RM1054 Technology Products Framework Agreement in March 2016 to determine which Microsoft license re-seller represented best value-for-money.
- 1.3 The contract was awarded to Insight Direct (UK) Ltd. with an overall contract value of approximately £3.026million. The contract has an initial term of three years with the option to extend the contract to an overall term of five years.
- 1.4 This audit is being undertaken as part of the agreed Internal Audit Plan for 2016/17.

2. OBJECTIVES AND METHODOLOGY

- 2.1 The overall audit objective is to provide an objective independent opinion on the adequacy and effectiveness of controls / processes relating to the Microsoft Enterprise Software Agreement.
- 2.2 The audit will for each area included in the scope:
 - Walkthrough the processes to consider the key controls;
 - Conduct sample testing of the identified key controls, and
 - Report on these accordingly.

3. SCOPE

3.1 This audit will examine the Council's arrangements for the following areas relating to the Microsoft Software Enterprise Agreement (and number of recommendations made):

Control Areas/Risks	Recommendations		
	Priority 1 (High)	Priority 2 (Medium)	Priority 3 (Low)
Strategic Assessment and Business Justification (Strategic Outline Case)	0	0	0
Contract Strategy	0	1	0
Delivery/Procurement Strategy (Outline Business Case, VM & Options Appraisal and Authorisation to Proceed to Procurement)	0	0	0
Procurement (Advertising and/or Selection of Economic Operators)	0	0	0
Procurement (Assessing Value for Money) and Authorisation to Proceed to Award of Contract (Full Business Case)	0	0	0
Formation of Contract, Compliance with the Contracting Authority's Legal Requirements, Retention and Security of Purchase Orders, Contracts and Deeds	1	1	0
Total	1	2	0

3.2 The audit will, where appropriate, in the above areas incorporate compliance with relevant statutes.

DEFINITIONS FOR AUDIT OPINIONS AND RECOMMENDATIONS

In order to assist management in using our reports:

We categorise our **audit assurance opinion** according to our overall assessment of the risk management system, effectiveness of the controls in place and the level of compliance with these controls and the action being taken to remedy significant findings or weaknesses.

	Full Assurance	There is a sound system of control designed to achieve the system objectives and the controls are consistently applied.
	Substantial Assurance	While there is basically a sound system of control to achieve the system objectives, there are weaknesses in the design or level of non-compliance which may put this achievement at risk.
	Limited Assurance	There are significant weaknesses in key areas of system controls and/or non-compliance that puts achieving the system objectives at risk.
	No Assurance	Controls are non-existent or weak and/or there are high levels of non-compliance, leaving the system open to the high risk of error or abuse which could result in financial loss and/or reputational damage.

Priorities assigned to recommendations are based on the following criteria:

Priority 1 (High)	Fundamental control weaknesses that require the immediate attention of management to mitigate significant exposure to risk.
Priority 2 (Medium)	Control weakness that represent an exposure to risk and require timely action.
Priority 3 (Low)	Although control weaknesses are considered to be relatively minor and low risk, action to address still provides an opportunity for improvement. May also apply to areas considered to be of best practice.

STATEMENT OF RESPONSIBILITY

We take responsibility to the London Borough of Croydon for this report which is prepared on the basis of the limitations set out below.

The responsibility for designing and maintaining a sound system of internal control and the prevention and detection of fraud and other irregularities rests with management, with internal audit providing a service to management to enable them to achieve this objective. Specifically, we assess the adequacy and effectiveness of the system of internal control arrangements implemented by management and perform sample testing on those controls in the period under review with a view to providing an opinion on the extent to which risks in this area are managed.

We plan our work in order to ensure that we have a reasonable expectation of detecting significant control weaknesses. However, our procedures alone should not be relied upon to identify all strengths and weaknesses in internal controls, nor relied upon to identify any circumstances of fraud or irregularity. Even sound systems of internal control can only provide reasonable and not absolute assurance and may not be proof against collusive fraud. The matters raised in this report are only those which came to our attention during the course of our work and are not necessarily a comprehensive statement of all the weaknesses that exist or all improvements that might be made. Recommendations for improvements should be assessed by you for their full impact before they are implemented. The performance of our work is not and should not be taken as a substitute for management's responsibilities for the application of sound management practices.

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