

AUDIT COMMITTEE

20 DECEMBER 2012

OUTCOMES OF INTERNAL AUDIT ACTIVITY

Report from: Internal Audit

Author: Alison Russell, Audit Services Manager

Summary

To advise Members of the outcomes of Internal Audit activity completed since the last meeting of the Audit Committee.

1. Budget and Policy Framework

- 1.1 It is within the remit of the Audit Committee to take decisions regarding accounts and audit issues.

2. Background

- 2.1 This report contains the outcome of Internal Audit's work since the last report to this Committee.
- 2.2 Generally, Internal Audit reports identify areas where improvement in the control process should be made. However, there is no standard within the internal audit profession of grading the overall control environment. Furthermore, even where recommendations are prioritised, the recipient of the report has no indication of how well the overall control process is operating.
- 2.3 To address this, Medway Council's Internal Audit has introduced a grading system so that managers have a clear understanding of the operation of the control environment in their area. The audit opinion is set at one of four levels and is formed on completion of the audit testing and evaluation stage but **before** management implement any of the recommendations.
- 2.4 All audit reports containing recommendations designed to improve the control process are presented with an action plan, which has been agreed with management and specifies the action to be taken, by whom and when. This agreed management action plan is incorporated in the issued final audit report.
- 2.5 The definitions used by internal audit for the provision of an audit opinion and for determining the priority ranking for recommendations are shown at **Annex A**.

2.6 Internal Audit undertake follow up work, usually within six months, to determine the effectiveness of the control environment following implementation of the recommendations or other action taken by management to address the issues identified in the audit.

2.7 This report details work completed since the last report to Members. The format of the annexes is as follows: -

Annex A Definition of audit opinions and recommendation priorities

Annex B Schedule of completed audit work showing the audit opinion provided and Directorates covered

Annex C Summary information on completed audits.

3. Risk Management, Financial and Legal implications

3.1 There are no risk management, financial or legal implications arising from this report.

4. Recommendations

4.1 Members are asked to note the outcome of Internal Audit's work.

Lead officer contact

Name Alison Russell
Job Title Audit Services Manager
Telephone: 01634 332355
email: alison.russell@medway.uk

Background papers

None.

DEFINITIONS OF AUDIT OPINIONS

Opinion	Risk Based	Compliance	Value for Money
Good	Effective controls are in place to mitigate risks reviewed as part of the audit, maximising the likelihood of achieving service objectives and value for money and protecting the Authority against loss.	Key controls exist and compliance is consistent and effective.	Objectives are being achieved efficiently, effectively and economically.
Satisfactory	Key controls exist to mitigate the risks reviewed as part of the audit effectively. However, instances of failure to comply with the control process were identified and there are opportunities to strengthen the control system and/or improve value for money.	Key controls exist but there may be some inconsistency in compliance.	Objectives are largely being achieved efficiently, effectively and economically, but areas for further improvement.
Insufficient	Controls are in place to mitigate identified risks and they are complied with to varying degrees. However, there are one or more gaps in the control process that leave the system exposed to significant residual risk. Action is required to mitigate material risks.	Key controls exist but they are not applied, or significant evidence they are not applied consistently and effectively	Objectives are not being achieved through an appropriate balance of economy, efficiency and effectiveness. Value for Money could be significantly improved.
Uncontrolled	Controls are considered to be insufficient to effectively control at least one of the risks reviewed as part of the audit. Remedial mitigating action is required. There is also a need to improve compliance with existing controls and errors and omissions have been detected. Failure to improve controls could have a significant impact on service delivery, or lead to material financial loss or embarrassment to the Authority.	Failure to comply with large numbers of key controls across a high proportion of the risks reviewed.	Objectives are not being achieved economically, effectively and efficiently.

DEFINITIONS OF RECOMMENDATION PRIORITIES

High

The finding highlights a fundamental weakness in the system that puts the Council at risk. Management should prioritise action to address this issue.

Medium

The finding identified a weakness that leaves the system open to risk. Management should ensure action is taken to address this issue within a reasonable timeframe.

Low

The finding highlights an opportunity to enhance the system in order to increase the efficiency or effectiveness of the control environment. Management should address the issue as resources allow.

SCHEDULE OF COMPLETED WORK					ANNEX B	
	Opinion	Authority Wide	Children and Adults	Regeneration Community and Culture	Health	Business Support Department
Key Financial Systems						
Other Financial Systems						
School Financial Management	I		✓			✓
Risk Assessed and Additional Work						
External Assurances - IT	S	✓				
HR Data Security	S					✓
Public Health Transition	S				✓	
Project Management	•	✓				
Governance						
Follow Ups						
Civic Centre Fuel Pumps	S			✓		
General Ledger	S					✓
Probity Reviews						
The Howard	•					
The Howard Property Scheme	•					
Woodlands Primary	•					
Woodlands Building Works	•					
St Michael's RC Primary	•					
Temple Mill Primary (follow-up)	•					
Payroll at Satellite Sites	•					

Key:

G = Good, S = Satisfactory, I = Insufficient, U = Uncontrolled

• = Work carried out but no opinion provided in that area

SUMMARY INFORMATION ON COMPLETED AUDITS**SCHOOLS FINANCIAL MANAGEMENT *(final report issued 10.12.12)***

Under Section 151 of the Local Government Act 1972, Medway Council's Chief Finance Officer has a legal responsibility for ensuring the proper administration of the Council's financial affairs, including Medway Schools under Local Authority control. A programme of financial probity audits of Schools is being undertaken. The output of the review at each School has been provided to the individual School, Senior Management within the Council, and presented to the Council's Audit Committee.

The Guide to the Law, provided by the Department for Children, Schools and Families, defines the required School governance structure for ensuring financial probity. The Governing Body hold the Head Teacher to account for ensuring there are appropriate and effective financial management and governance arrangements in place. The School Business Manager (SBM) or equivalent is responsible for the delivery of sound financial administration.

Audit Committee approved an annual programme of work to review the financial management in Medway's Schools, through undertaking a series of probity reviews in Schools across Medway. It was agreed that an overarching report would be prepared providing an overall assurance on the financial management arrangements for Medway's Schools, and also providing a summary of issues and lessons learned, to be shared with all of Medway's Schools. To date we have undertaken nine probity audits resulting in thirteen reports.

A number of Medway Schools have moved to Academy status but Medway still has overall financial responsibility for 81 schools, providing schooling for 22,657 pupils. The total 2012/13 budget for these schools is £104.5m. Including the audit of School Bank Accounts and the probity audits Internal Audit have visited 14 Schools in 2012/13 so far, resulting in 19 reports. The Schools visited to date represent nearly 20% of the total number of pupils in Medway's Schools, and providing assurance over just above 23% of the total Medway's School budget

The accounts within Schools relating to voluntary funds and the PTA are not subject to Medway control, not included in the scope of probity reviews, and no assurance is being provided by Internal Audit in relation to these accounts. Schools have a responsibility to ensure that the voluntary fund accounts are audited and confirmation provided to the Council that this audit has been undertaken. An exercise is being undertaken by Education Finance and the Chief Finance Officer to chase those Schools which have failed to provide the required confirmation that their voluntary fund has been audited.

The Schools are supported by a number of services within Business Support Department and Children and Adults Directorate. We have liaised with relevant staff within the Council, both in terms of the probity audit programme risk assessment, and the individual School audits. We have also reviewed progress on actions that were previously agreed with Education Finance to strengthen their monitoring arrangements of School bank accounts, and enhance the guidance provided to Schools.

MANAGEMENT SUMMARY

This audit report provides an overall summary and opinion on the financial management with Schools based on the audits that have been undertaken in 2012/13, and with recognition of the enhancements being made to the monitoring and guidance provided by Education Finance. The level of financial risk varies between Schools, due to a number of factors including the size of the School, the level of income generating activity, and building work being undertaken.

The effectiveness of financial management within Schools varies significantly, and in the audits undertaken we have found Schools with relatively robust processes in place, and other Schools where there were significant issues. In the Appendices to this report management were provided with tables recording the main issues arising and actions that Schools can take to address these weaknesses. The report will be circulated to the Chairs of Governing Bodies for all Medway's Schools with the requirement that it is presented to the full Governing Body to help them consider the effectiveness of the financial management within their School. The Audit Commission's "Fraud Risk In Schools – Advice For School Governors" will be also be circulated for information.

The lack of effective control within Schools does not in general represent a lack of resources applied to the area, but rather a lack of awareness of the risks and the purpose of key control mechanisms, and a culture of trust and reliance on individual's integrity. This lack of awareness is leaving schools open to the loss of funds through fraud, theft or failure to pursue value for money, and also leaving individuals, and in particular School Business Managers and finance staff, in a vulnerable position. The six most significant weaknesses that we have found through the 2012/13 probity reviews are:

- Lack of effective supervision by headteachers of financial transactions and financial management processes.
- Lack of effective management or oversight of income streams
- Ineffective challenge relating to financial remuneration to staff, for instance overtime, expenses and timesheet-based payments.
- Conflicts of interest are not identified and appropriate action taken. Payments and other decisions are made or in some way influenced by staff members who are related or otherwise close to the payee or recipient.
- Poor procurement processes and lack of documentation held to support financial decisions and transactions
- Poor asset management including the management of stock.

We are pleased to note that Education Finance now receive full bank statements from Schools each quarter. Processes have been developed to request evidence of authorisation for transactions over a set figure and a check made of cheque sequence numbers. These arrangements have only recently been implemented and may be subject to further review and refinement.

The model School Finance Policy has been amended to reflect the need for Governing Bodies to ensure that they are responsible for authorising the opening, closing and amending of bank accounts, and also in specifying debit and purchasing cards used, the cardholder and arrangements for checking expenditure on the card. The Finance Manual for Schools is also due for review and update, and the findings of this first year of probity audits will be used to help inform the amendments made.

All outcomes of School probity audits are shared with Education Finance who have continued to raise awareness of the need for Schools to mitigate the risk of fraud and financial mismanagement through events attended by School Business Managers and Governing Body members.

CONCLUSION AND AUDIT OPINION

Our overall opinion on the effectiveness of the management of School finances is **“insufficient”**.

Medway Council will share this report with Governing Body Chairs, who will share this report with the Governing Body and use it as a basis for reviewing the arrangements within the School, and to support them in the completion of the School Financial Value Statement.

<h3>IT EXTERNAL ASSURANCES <i>(final report issued 22.10.12)</i></h3>
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The objective of this audit was to establish the extent, and legitimacy, of external assurance obtained on the Council's IT systems (not only those managed by ICT), including reviews of data protection. We also assessed whether management have addressed any issues arising from inspections effectively in order to minimise the risk of recurrence and, potentially, penalties being incurred.

From the 343 applications currently in use across the authority, we reviewed the arrangements of 14 of the more critical IT systems, as well as 2 secure networks and three main licensing bodies. We established from relevant officers whether they receive any form of assurance over the integrity of the system from outside parties.

The audit identified any external reviews performed and examined action plans arising, implementation of issues and reporting mechanisms, of which a summary is shown in the table below. Whilst reviewing the external assurance mechanisms in place we also obtained assurance around a number of internal control mechanisms in place. The key internal control arrangements are also recorded in a table provided to management as they contribute to the overall level of assurance around our IT applications.

FINDINGS

The audit established that there are two systems with the ISO9001 accreditation (Logotech (Terrarius) and The Partnership Suite) and another (Lagan) is working towards this standard of performance.

Three of the systems have an association with or are members of an external body, relating to the service they specialise in, these being The Electoral Commission (Eros), The Law Society (The Partnership Suite) and SELMS Consortium (Spydus).

Eight of the systems have been subject to external reviews within the last 12 months:

- In November 2011, Ofsted published an inspection of the Safeguarding and Looked After Children Services. The inspection highlighted room for improvement to ensure the Raise system should enable accurate case recording. Care Director and Raise are due to be replaced in the near future.

- In May 2012 External Auditors, under the International Standards on Auditing (ISA) reviewed Integra, Logotech Financials, ResourceLink and Spydus to gain an understanding of the systems in order to assist with the identification and assessment of the risk of material misstatement in the financial statements.
- Logotech Financials was subject to review also by External Auditors, regarding the statement of accounts.
- Logotech (Terrarius) was subject to review by External Auditors regarding Council properties. The system is due to be replaced in the near future.
- In August 2012, The Law Society undertook an audit within Legal Services, which included reference to The Partnership Suite and resulted in accreditation by Lexcel.

Three main licensing bodies, Adobe, Microsoft and Oracle (with which ICT must be compliant) carry out external checks on licensing. A minor non-compliance was identified with one licence provider, but the issues were addressed and, as a result, the licence was found to be appropriately managed and fully compliant.

The GCSX and N3 Connectivity Service sets minimum standards and processes Medway Council must comply with to connect to GCSX and NHS N3 network via the Government Connects programme. This programme is also associated with the Department of Health and The Department of Work and Pensions. An annual code of submission is completed to ensure data security and good practice. This may be inspected and provides an assurance that our system information is compliant. ICT meet the requirements and are compliant, enabling connection to the GCSX and N3 networks. The GCSX Connectivity is used by Benefits in particular to communicate with the DWP.

ICT use ITIL (IT Infrastructure Library) for incident management, a framework providing a defined process of logging, recording and resolving incidents, giving assurance that calls are recorded and dealt with in a consistent way. ICT are potentially looking to use it for change management and problem management in the future, although work has halted on this due to Better for Less priorities. This provides a framework of best practice in IT service management and a framework for the governance of IT.

Although not accredited to date, ICT has been working towards ISO27001 compliancy, but again, due to loss of key resources in this area, work stopped, although recent communication with the accrediting body suggests ICT have already achieved some parts and are not too far away from completing. Management is keen to progress with this in the future subject to resources.

Issues that were identified through external reviews have been monitored and addressed effectively by management, to minimise the risk of recurrence.

Through reviewing the external assurance we gained confirmation of a number of key internal controls that are in place which support the overall effective ICT governance arrangements:

- System administrators reside outside of ICT Services but are within their own service. These administrators are responsible for administrative functions and ICT provides support on technical issues that cannot be dealt with locally by these key people.

- All internal servers are managed by ICT, there are two servers externally managed; Covalent and Spydus.
- Third party access in terms of application providers, is provided ensuring a two-factor authentication using RSA tokens. RSA Secure ID is a mechanism developed by RSA, the security division of EMC, for performing two-factor authentication for a user to connect to a network.
- Change controls, patches and fixes are reviewed and applied in a controlled manner via ICT, using test systems before implementing to live versions, mitigating risk of damage to any systems and networks.
- Medway Council's Information Security Policy outlines its framework for ICT security.
- It was noted during the audit that internal training and procedures are in place throughout the services selected and these are reviewed on a continuous basis by management. Although not an external assurance it is key to ensuring users adhere to the best working practices.

The only control weakness that was identified during the audit is that the Council has not published a data protection policy, and there is no Council-wide process for ensuring compliance with the Data Protection Act.

AUDIT OPINION

This audit focused on 19 critical areas requiring external assurances. We found no issues arising in these areas and this, along with the internal ICT governance arrangements means that we have reached an overall opinion of 'Satisfactory'.

One High priority recommendation:

Finding:	The Council has not published a data protection policy, and there is no Council-wide process for ensuring compliance with the Data Protection Act.
Risk:	A potential breach of the data protection act could lead to damage in reputation and/or financial costs to the Council.
Recommendation:	Management should ensure there is a Data Protection Policy in place, which is communicated to all staff. The policy should include a mechanism whereby the Council ensures compliance with the Data Protection Act.
Response:	Accepted by Senior Information Risk Owner (SIRO). Target date – April 2013

HR DATA SECURITY (*final report issued 11.12.12*)

The audit reviewed the effectiveness of controls that are in place to protect HR data, in electronic and documented format, both within Medway Council's HR and Payroll functions and when provided to third parties. It did not, however, cover arrangements for the retention and disposal of documentation in other functions, schools and remote establishments or controls over access to Gun Wharf. Three risks relating to HR data security were reviewed to determine the effectiveness of controls and the opinions are shown below.

- **Risk 1: Employee data held within Medway's HR systems may be accessed by unauthorised and/or inappropriate persons**

Satisfactory: appropriate controls were found to be in place and operating effectively to ensure that only people with a genuine requirement are granted access to ResourceLink (the integrated HR/payroll system) and scanned documents within Swordfish (the intranet based document management system that can only be accessed via the Medway network).

However, we identified a number of issues regarding Swordfish which, when combined, presented an exposure to the risk that inappropriate persons may have been able to access confidential personal data. These issues were:

- Scanned documentation for current and former employees, including information such as bank account and emergency contact details, is retained indefinitely as it may be needed for subsequent pension queries;
- There was no process to ensure that access to Swordfish was disabled when users transfer to another role within the Council, e.g. outside HR/Payroll, and no longer had a legitimate need to access personnel records;
- Access to documentation relating to disciplinary action was not restricted to the smaller group of officers nominated by HR management.

Since being advised of this exposure, management have already taken action to address the issue of officers who no longer have a legitimate need to view personnel records still being able to access Swordfish.

Management have also taken action to tighten controls over access to Selfserve4You, by activating an automatic requirement for periodic password changes and ceasing to advise staff contacting the HR helpline requesting reset that the same answer can be used for all four security validation questions.

- **Risk 2: Employee data provided to third parties may not be protected sufficiently to prevent unauthorised disclosure**

Good: as there is a legal requirement to release data and/or make statutory payments to other government departments, e.g. HMRC, HR management place reliance on the integrity of their IT systems and protection of the data supplied and only provide the data requested. Other data released and/or payments made require consent by staff including union membership and voluntary contributions.

As part of the audit, the sickness monitoring/reporting service previously used by RCC, provided by an external company, was reviewed. Although a data breach led to the termination of the contract with the provider, controls put in place by the council, including a data processing agreement, were found to be good.

- **Risk 3: Confidential HR documentation may be accessed by unauthorised and/or inappropriate persons**

Satisfactory: there is a HR policy in place stipulating that documentation held in the office should be stored in lockable cupboards overnight, which we consider to be particularly important due to the open-plan nature of the Gun Wharf building, as all staff with a security fob are able to access the HR office.

However, we identified a number of issues which presented an exposure to the risk that inappropriate persons may be able to access confidential personal documentation:

- Insufficient lockable cupboards were available in the office area for storage of payroll documentation;
- Unrestricted access to incoming post, including envelopes and documents showing employee name and ERN and sickness forms not in secured envelopes;
- Unrestricted access to payroll documentation held in the archive storage area, including sickness forms and school pay runs showing employee number, name and bank account details;
- Lack of policy regarding the security of personnel documentation held elsewhere, for example by line managers, or when taken away from the office, including reporting the loss of information.

We understand that Payroll management had been unhappy with the archive storage area allocated to them on the move to Gun Wharf, and recognise that availability of an alternative, more secure, area was being negotiated when the audit commenced. Documentation has now been moved into this area and action has been taken to restrict access to the residue remaining in the 'general' archive area and secure documentation held in the office overnight.

CONCLUSION AND AUDIT OPINION

In recognition of the swift action taken by management when they were notified of the control weaknesses identified, our overall opinion on HR data security is '**satisfactory**'. These actions should reduce the risk of unauthorised and/or inappropriate access to personal data and, consequently, the risks of breaching the Data Protection Act and fraudulent activity such as identity theft. The audit follow-up in approximately six months time will enable us to confirm that these improvements have been sustained.

Two High priority findings:

Finding 1:	<ul style="list-style-type: none"> a) Payroll documentation, including sickness forms and authorised signatory lists, was stored in unlocked cupboards in the HR office. b) Unrestricted access to incoming post, including envelopes showing employee name and ERN and sickness forms not in secured envelopes. c) Payroll documents containing confidential information - including sickness forms and school pay runs that give details of employee number, name, bank account and branch - were not stored in locked cabinets in the archive storage area.
Risks:	<p>Inappropriate access to information.</p> <p>Data Protection Act could be breached.</p> <p>Information could be used fraudulently, e.g. for identity theft.</p>
Management action taken:	<ul style="list-style-type: none"> a) Replacement locks now obtained and fitted to cupboards in office, payroll documentation now retained securely outside

	<p>working hours. (Completed)</p> <p>b) A lockable mailbox (or similar) will be obtained and installed to improve the security of documents delivered to the HR/Payroll office. (Target date – by end of December 2012)</p> <p>c) Documents have now been transferred to the new, more secure, storage area, those remaining on shelving in the 'general' archive area have now been secured by fitting chains and padlocks. (Completed)</p>
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Finding 2:	<p>a) No formal notification process for amending access rights to Swordfish when users change job.</p> <p>b) Past employees are not removed from the Swordfish user list, although access is terminated when network account is closed.</p> <p>c) Users who do not have a legitimate need to have access can view disciplinary information held on Swordfish.</p>
Risks:	<p>Inappropriate access to information (information stored on Swordfish is retained indefinitely including data held on former employees).</p> <p>Data Protection Act could be breached.</p> <p>Information could be used for identity theft.</p>
Management action taken:	<p>a) ICT to be provided with a report of leavers and staff transferring to other positions monthly so that Swordfish access can be disabled. In the meantime, Swordfish access has been withdrawn for all current non-HR employees without a valid need to access HR/payroll documents.</p> <p>c) Identified that problem is due to categorisation of documents on scanning – liaising with ICT to address security issues.</p> <p>(Target date – by end of December 2012)</p>

Three additional medium priority findings also addressed by management, two already completed and the third to be implemented by the end of March 2013.

PUBLIC HEALTH TRANSITION *(final report issued 7.12.12)*

The Health and Social Care Act 2012 comes into force April 2013. The key areas of the bill are:

- Establishment of independent NHS Commissioning Board to allocate resources to the NHS
- Increases in General Practitioner powers to commission services on behalf of patients through Clinical Commissioning Groups (CCGs)
- Strengthening the role of the Care Quality Commission
- Giving new statutory duties for public health to local authorities
- Reinforcing the commitment to improve health and reduce health inequalities
- Abolishment of Primary Care Trusts (PCTs) and Strategic Health Authorities (SHAs)

The bill gives Local Authorities a ring fenced grant to fund its new public health responsibilities which will transfer from PCTs. This includes commissioning and providing health improvement services, health protection responsibilities and providing specialist public health advice to CCGs. The Director of Public Health and her team will be transferred to the Local Authority on 1 April 2013. A Health and Wellbeing Board will be established as a Committee of the Council to provide strategic leadership for health and wellbeing through the production of the Joint Strategic Needs assessment and the Joint Health and Wellbeing Strategy. It will also promote integration of commissioning and service provision to achieve the outcomes within the national outcomes frameworks and address local priorities.

The transfer of responsibility for public health from the NHS to Local Authorities, combined with the simultaneous abolition of the PCTs and the creation of the CCGs, represents a significant challenge to all Local Authorities to ensure that appropriate arrangements are in place for April 2013. The challenges have been made more onerous by the fact that a comprehensive and clear set of parameters regarding the nature of the changes was not provided up front by central government, and guidance has continued to be issued throughout 2012, necessitating regular reviews of project plans.

This audit is a high level review of the work being undertaken to mitigate the key risks relating to the transition. The audit seeks to provide assurance that the Authority has made adequate progress, and has reasonable plans in place, to ensure it is ready to meet its obligations

The project has been subject to external review by the SHA and found to be progressing well, and was commended for its good communication between the Public Health team and the Local Authority. From our review we were pleased to note that the project arrangements are robust, with a Project Transition Board, senior management involvement and sponsorship, workstreams in place to support the high level milestones provided by the SHA, effective risk management, and contingency inbuilt into the plan to maximize the chance of meeting the April deadline. We are therefore able to provide assurance that the project management arrangements in place are “**Good**”.

The key areas that we reviewed in order to provide assurance on the readiness of the Authority were:

Governance Arrangements

Good

The Authority has set up a shadow Health and Wellbeing board (HWB) consisting of appropriate representatives from Medway's Cabinet and senior management, the Health service and the Community. This will become a decision making Council Committee upon transition and will be subject to challenge by both the Health and Adult Social Care & Children and Young People's Overview and Scrutiny Committees.

Public Health will be a directorate within Medway Council with the Director of Public Health reporting directly to the Chief Executive. The directorate structure is currently subject to consultation. Medway's new responsibilities are defined by statute and working arrangements are currently being agreed with other new organisations in the Public Health arena.

Budget

Satisfactory

There is a budget that will transfer to Medway from April 2013, which will be ringfenced. The value of the grant from 2013 has not been finalised. Whilst the Authority is clear on its responsibilities the Director of Public Health is aware that there are differences between the detail of Medway's interpretation and that of other local authorities. This may result in differences between current expectations of the grant and the allocation.

The Chief Finance Officer is concerned the budget will not be sufficient to meet the demands of the transferred responsibilities. Work is ongoing to quantify issues as soon as information is available.

Administration –Facilities and ICT

Satisfactory

The key administrative tasks required for a successful Health Transition have been allocated to workstreams, each of which has a named owner. Preparations for the few remaining staff who have yet to transfer to Gun Wharf are in hand with desk space having been allocated and the basic IT requirements identified. There are some specific queries relating to IT governance and capacity which are currently being progressed.

Change Management

Satisfactory

Effective change management is critical to the smooth transfer of staff from the NHS to the Local Authority. Staff are being made aware of the impact of the Health transition via staff briefings and the Medway and Heath intranet sites. Induction for the Public Health staff is planned for the end of January 2013 and the main training requirements have been identified.

Better 4 Less is running in parallel with the Health Transition Project and Public Health is part of phase III b (due to start in January 2013). The impact of this was not originally considered as part of the Health Transition Project but we understand this has now been brought into the project risk register and mitigating action will be planned and monitored.

CONCLUSION AND AUDIT OPINION

The framework the Authority has in place for ensuring it will be ready for the Health Transition is “**Satisfactory**”. The project management methodology used is sound and appropriate structures are being readied for 1 April 2013. The project board will, however, need to ensure potential conflicts between the Health Transition and Better 4 Less projects are considered and that requirements for workstream sign off are documented.

This audit provides assurance on management action to date and provides reasonable but not absolute assurance over Medway's preparedness for the transition. There remain risks to the Authority arising from Finance, contractual responsibilities moving forward, Human Resources and future access to information.

3 medium priority recommendations have been made to address issues identified.

PROJECT MANAGEMENT REVIEW *(reported to CMT 31.10.12)*

An internal audit review of Project Management was requested by the Corporate Management Team (CMT) in light of the roll out of the new project management toolkit.

We reviewed the toolkit against industry standard and are of the opinion that it will provide a sound structure for the management of projects across the Council. The way that the toolkit is presented is clear and easily comprehensible and should therefore prove to be a useful tool in ensuring effective governance of projects.

The new project management toolkit is available on the intranet as part of the managers' toolkit section and a presentation on its use was made to a service managers' meeting in July 2012. Training sessions on project management have been, and continue to be, offered to staff. The publicising of the new toolkit and the need for managers to ensure effective governance of projects will need to be continually publicised in order to maximise awareness of this issue and ensure compliance with the toolkit.

As part of this review we also examined a small sample of projects, determined by CMT, in order to assess whether project management best practice had been followed, particularly the arrangements for governance and financial management. These projects were initiated prior to July 2012 when the toolkit was made available to managers (on the intranet). The purpose of the review was to determine whether the toolkit was likely to address any areas where the previous arrangements had been weak.

We reviewed a sample of five projects, four of which related to capital works, and were able to confirm that, in general, the principal requirements of good project management, as defined in methodologies such as Prince 2, had been met. For example, project plans setting out proposed timescales had been prepared for all the capital projects, and all projects had risk logs and financial budgets allocated, with budget monitoring returns produced periodically as required.

The key stage that we identified in the review where the toolkit will need to address previous weaknesses was in relation to the project initiation. Whilst all major projects require Cabinet approval and as such there are documents produced outlining the key elements of the proposed projects, the majority of the projects reviewed did not have a formal project initiation document combining governance arrangements, key controls, risk management and progress milestones. This can lead to a failure to monitor the project effectively through its lifecycle, and as such overspends and time overruns may not be identified and/or reported to senior management and members in a timely manner. The introduction of officer and Members advisory project boards should address this risk.

In conclusion, the review confirmed that the arrangements in place prior to the introduction of the toolkit were generally satisfactory, but with areas where the arrangements could be further strengthened in order to strengthen governance arrangements. We are satisfied that the toolkit will strengthen and formalise the previous arrangements, providing a robust governance framework for managing projects across the Council.

LOCAL MANAGEMENT OF PAYROLL PROCESSES

(final report issued 15.10.12)

Medway Council processed payments to staff totalling £157m through its payroll system in 2011/12. Payroll operations rely on information received from local management to ensure payments made are legitimate, accurate and timely. This 2011/12 audit focused on the manual controls in place at a number of sites across the Council, and every risk is mitigated by the robust level of control over the central management of payroll. In line with the approach agreed with Audit Committee for the program of probity reviews, this audit focussed on key controls at selected sites rather than the provision of an overall opinion on the control environment.

This audit reviewed local management processes in seven parts of the Authority in order to ensure payments are legitimate and correct. The sites visited were Deangate Ridge, Registrars, Drugs and Alcohol Action Team (DAAT), Events, Central Services, Outreach (Chattenden, White Road, Woodside and Hook Meadow Community Centres) and Youth Services (Strood and Gillingham areas).

FINDINGS

There is clear delegation of responsibilities for payroll processes at each establishment visited. Payroll documentation for permanent employees was generally handled appropriately although central payroll management identified two delays in processing leavers which led to overpayments of £1,100. This money has now been recovered.

Some services engage employees on zero-hours contracts and employ them when required to meet demand. These employees should be terminated on payroll when they are no longer employed. Four out of the seven establishments visited had casual employees on the payroll. 17 employees had not been paid at these sites for 12 months and 6 had not been paid for 6 months and all should have been processed as leavers. Further testing was carried out at these sites and we found no evidence of fraudulent payments being made.

In 2011-12 the total payroll amount processed for timesheet payments was £8m. This audit tested records held locally for accuracy and validity of overtime claims.

Registrars, Events, Deangate Ridge and Outreach (Chattenden and White Road) had procedures in place to ensure overtime claimed was correct and that management are able to verify this. It was not possible to confirm the accuracy of timesheets at Outreach (Woodside and Hook Meadow), Youth Services, Central Services and DAAT as rotas or other local records were not retained and management did not have personal knowledge of hours worked.

Budget monitoring reports provide management with an opportunity to identify material overpayments within a period and we found that these had been completed appropriately at six of the seven sites.

CONCLUSION

There are no of probity issues at any of the sites visited and we are satisfied that HR/Payroll management has adopted the action plan for strengthening control.

SUMMARY INFORMATION ON FOLLOW-UP AUDITS

CIVIC CENTRE FUEL PUMPS *(final report issued 22.10.12)*

The final report for the audit of Civic Centre Fuel Pumps, which focused on the fuel usage by services and external contractors, was issued in April 2011 – this was the first time the process had been subject to internal audit review. The audit process is not complete until an independent follow-up is performed in order to confirm progress in addressing the weaknesses identified in the original report, and on the basis of these findings reviewing the overall audit opinion. Medway Council has three fuel pumps at the Civic Centre site and financial records indicate that the total cost of fuel purchased for issue through the pumps in the last financial year was £157,657.

The original report recorded an overall audit opinion of 'Uncontrolled' and contained 8 high and 2 medium priority (mostly multi-part) recommendations. The proposed actions sought to address weaknesses in mitigating the following risks:

- All fuel purchased may not be accounted for;
- Fuel issued may not be used for bona-fide Council purposes;
- Cost of fuel used may not be charged to the correct service/contractor, or may not be charged accurately.

Management have provided and implemented many new procedures and processes since the previous audit in response to the recommendations made and the system software has been updated and is now included in the routine daily backup process. Interviews and fieldwork are now complete and we are able to provide the report outlining the findings of the follow-up and our overall opinion of the controls now in place.

FINDINGS

Our review confirmed that action has been taken to address the most significant concerns identified in the original audit and, as a result, significant improvements have been made in controlling all these risks. However, parts of some recommendations had not been fully implemented and some of the issues identified previously had recurred, as a consequence of which there is scope for further improvement.

The recommendations that had not been addressed fully related to the Operations Manager investigating the cause, and authorising the adjustment, of significant stock variances and the recording and checking of fuel keys available for issue. The recurring issues, which were largely outside the Operations Manager's control, were primarily fuel keys still being in circulation for vehicles no longer used by the Council or fuel keys that had been returned not being deactivated to prevent further use. Furthermore, although guidance on checking the management reports that are now provided to nominated 'fuel account managers' was issued to them, four of the seven account managers we contacted stated they were not aware of this guidance and did not know what they should be checking.

CONCLUSION

On the basis of the findings of this follow-up review of the controls in place to manage the purchase, issue and recharging of fuel our opinion is that the current arrangements are 'satisfactory'.

There were no significant issues outstanding but we made three medium priority recommendations to further strengthen the current arrangements, all of which were accepted by management for implementation by the end of December 2012.

GENERAL LEDGER <i>(final report issued 6.12.12)</i>
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In order to support External Audit in their annual statutory duty of examining the Council's key financial systems, an audit of the General Ledger system was carried out in January 2012 and a final report reference 11015 was issued on 20 April 2012 with the overall opinion on management controls over the system in 2011/12 of '**satisfactory**'.

From the testing performed we found that there were weaknesses in the controls over preparation and authorisation of journal transactions, but management advised us that they had taken appropriate action to improve journal processing and authorisation procedures from the beginning of the new financial year.

The processing and authorisation of journals was subject to review in the 2011-12 year-end External Audit. External Audit highlighted that the recommendation made in 2010-11 to improve controls over the authorisation of journals had not been fully implemented, so was repeated again in the 2011-12 accounts, confirming Internal Audit's findings.

The audit process is not complete until an independent follow-up is performed in order to confirm progress in addressing the weakness identified in the original report, and on the basis of those findings reviewing the overall audit opinion. This report summarises the results of further audit work carried out to confirm that the agreed action for controls over the preparation and authorisation of journals has been fully implemented.

FINDINGS

Management advised that controls for preparation and authorisation of journal transfers were implemented across the Finance Department from June 2012.

Audit testing confirmed that these are in place and are being adhered to across the department.

CONCLUSION AND AUDIT OPINION

On the basis of the controls now in place we can confirm that the overall audit opinion of **Satisfactory** remains.

SUMMARY INFORMATION ON SCHOOL PROBITY REVIEWS

Under Section 151 of the Local Government Act 1972, Medway Council's Chief Finance Officer has a legal responsibility for ensuring the proper administration of the Council's financial affairs, including Medway schools under Local Authority control. A programme of financial probity audits of schools is being undertaken. The output of the review at each school will be provided to the individual school, senior management within the Council and, once finalised, it will be presented to the Council's Audit Committee.

The Guide to the Law, provided by the Department for Children, Schools and Families, defines the required School governance structure for ensuring financial probity. The Governing Body hold the Head Teacher to account for ensuring there are appropriate and effective financial management and governance arrangements in place. The School Business Manager (SBM) or equivalent is responsible for the delivery of sound financial administration.

THE HOWARD SCHOOL – FINANCIAL PROBITY REVIEW

(final report issued 1.11.12)

The Howard School is an 11–18 bi-lateral grammar and high school for boys, with an annual budget of approximately £7m. The school became a Foundation School in 1998 and a Specialist Sports College with Information Communication Technology as its second strand in 2007. There are approximately 1500 pupils on roll.

The current Principal inherited a revenue deficit of approximately £200,000 and the school is close to the end of a 4 year budget recovery plan which has entailed £512,000 loan from the Council which the school should start paying back in 2013.

Our review covered income, payments and payroll expenditure, and began with an assessment of the control arrangements as set out in key documents and confirmed through interviews with the Headteacher and the Finance Staff. We obtained transaction data and where we identified areas of potential anomalies, we undertook targeted testing in order to provide assurance that there were no concerns arising.

A separate audit report has been completed on the Howard School Property Scheme (report 12021). This highlighted problems with procurement, contracting and purchasing arrangements. This audit, therefore, did not re-examine these issues.

Our review and testing of the financial control arrangements found control weaknesses across all income and payment processes.

CONCLUSION

The issues relating to the recruitment incentive scheme are reported separately. In relation to the other income and expenditure processes we found a number of control weaknesses but no evidence of any probity issues. We are also satisfied that the School has adopted the action plan for further strengthening the current financial arrangements.

Whilst no single high priority recommendation was made, financial controls were found to be weak in all areas e.g.:

- Payroll
 - A large number of payroll salary advances
 - Staff payments through petty cash
 - Conflict of interest in signing off overtime claims
 - Casual employee left on payroll when no longer required
 - One casual employee without current CRB clearance, although we were informed the school would not use them until a new CRB had been obtained
- Payments
 - Documentation to support payments not retained
 - Over-use of petty cash
 - Management oversight of the school credit card
- Income
 - Reconciling income banked to records of income due and received
 - Issue of receipts
- Premises security

An action plan records seventeen actions to further strengthen current arrangements.

THE HOWARD SCHOOL: SUBSIDISED ACCOMMODATION

(final report issued 6.9.12)

In 2002/03 the School introduced, with agreement from Medway Council, a recruitment incentive scheme due to difficulties they were having in recruiting good quality teaching staff. The incentive centred on the School offering subsidised accommodation to new teaching staff who moved into the area in order to take up a post at the School. The School also began to advertise teaching positions far afield and overseas. The scheme has focused on recruiting from Northern Ireland and a significant number of teaching positions have been filled from these recruitment exercises.

Initially the scheme involved providing subsidised accommodation for a period of three years as it was deemed that the ongoing incentive was required in order to retain staff. In 2007 when the present Principal joined the School the period of subsidy was reduced to one year.

This report focuses on the 2011/12 arrangements and the attendant costs, but costs have been incurred since the scheme began. The 2011/12 figures are provided in order to provide some context and to provide an indication of the amounts involved. In the 2011/12 academic year the School had six staff benefiting from this scheme, and six properties were involved in the scheme in 2011/12.

The rent payment process involves the School taking on the tenancy from the landlord, and paying the rent directly to the landlord on a monthly basis. One of these properties is owned by the School and therefore the School is the landlord for the tenants in this property, which is known as the School House. The School then arranges a tenancy agreement with the teacher. The teacher then pays a contribution to the School for the rent, which is taken direct from their monthly salary. This is currently set at 50% of the maximum rent paid per month except for the

School House where the contribution from the tenants has historically been set at a slightly lower rate.

The School also takes on responsibility for the payment of council tax and utility bills. The teachers make no contribution to these.

Where a deposit is required the School pays this up front. We have been informed that the School has only lost one deposit due to damage to the property.

A further property, in addition to the six noted above, is leased by the School to a teacher who was employed in 2005 and continues to live in the property. However the arrangement is that the teacher is wholly responsible for payment of the rent and pays the utilities bills and the Council Tax. The agreement for the School to continue the arrangement was made by the previous Principal.

The School has used a number of different properties since 2002/03 when the scheme began. The properties used have included properties obtained through Town and Country Housing, through other Agencies, and private arrangements with landlords. The properties have included one, two, three and four bed houses and flats.

Value for Money

The School is currently in deficit and working to a deficit recovery plan. The costs of the scheme are reported to the Governing Body as a reporting line under budget reports but on our review of Governing Body and Finance and Personnel committee papers going back to January 2007 we identified only one specific discussion of the rented accommodation. This was at the Finance and Personnel Committee on 24 January 2007. We have been unable to identify evidence of an evaluation of the value for money this scheme provides to the School.

The School House is owned by the School and the previous School Caretaker resided there. Since the School does not pay rent to a landlord for this property this is not really part of the subsidised accommodation scheme in the same way as the other properties. In 2011/12 the School made £2,218.84 in rent from this property. The School House is not generally popular with teachers as it is based within the School grounds and there are periods when this property is left vacant. There needs to be consideration given as to whether the School is making the most of this asset and consider other options as to how income from this asset might be maximised.

The overall expenditure by the School for rent and council tax for the other five properties in the scheme in the academic year 2011/12 (running 1/9/11 to 31/8/12) was:

SCHOOL EXPENDITURE 2011/12	
RENT	27,635
COUNCIL TAX	3,116.08
TOTAL	30,751.08

The identified expenditure on utility bills in the financial year 2011/12 for subsidised accommodation, including the School House, totalled £2,600. This figure is unlikely to be the full costs for utilities in year as there are a number of transactions relating to

energy bills which cannot be traced to any particular property and have therefore been omitted from this figure.

Furthermore there is an indirect cost to the School surrounding the administration of the scheme, which includes the need to find properties, arrange for teachers tenancy, furnish the properties, set up the appropriate financial processes and deal with any issues that arise at the property. It is difficult to quantify this indirect cost but we have been informed by the staff involved in the Scheme that time spent on managing the scheme is significant.

The continuation of the scheme has been subject to limited discussion by the School's full Leadership Group and there has been no full evaluation undertaken by management or the Governing Body of whether the scheme continues to be necessary. Over recent years there has been a significant improvement in both the academic achievement at the School and also the behaviour issues. The most recent OFSTED report in November 2008 rated the School as "Good" and the interim inspection in January 2012 confirmed that this performance had been sustained. As such potentially there is no need for the School to continue with such a costly incentive scheme.

There is a lack of documentation to evidence how the properties were selected in order to demonstrate that value for money was considered in the procurement exercises undertaken. Rents for current properties vary between £450 and £650 per month. The monthly cost to the School in terms of rent per property is between £125 and £325.

The council tax paid on these properties appears to be without any subsidy for single person occupancy that would provide a 25% discount. This may be due to the fact that the Howard takes on the liability of the Council Tax, whereas it is the individual tenant who would have to apply for the Single Person Discount as the School would not be eligible to do so. If the tenant were liable for the Council Tax and the Howard made an arrangement to reimburse the Council Tax payments at the discounted rate to the tenant, then the cost to the School would be reduced. We have calculated that the total amount that the School overpaid in relation to council tax for the 2011/12 academic year was nearly £900.00.

Contributions

There are no records to demonstrate how the level of contribution has been set. In 2011/12 the contribution for all tenants was set at 50% of the maximum rent. The total contribution paid in academic year 2011/12 in relation to the five properties is £17,225. Therefore the total cost to the School for running the scheme in 2011/12 was:

NET COST TO THE SCHOOL 2011/12	
RENT	27,635
COUNCIL TAX	3,116.08
TOTAL EXPENDITURE	30,751.08
Minus Contribution	(17,225)
Net Cost to School	13,526.08

Looking at current and also past arrangements it would appear that the contribution figure is set at a given amount irrespective of the level of rent or the number of tenants in the accommodation. This means that some of the properties have been more expensive for the School to let, whilst in other properties the School has in fact made a profit where there are two or more tenants.

In summary, the cost to the School in 2011/12 was something in excess of £16,100 (£13,500 plus £2,600) based on the net cost of the rent, council tax and utility bills. The arrangement is due to continue into 2012/13 and the School is already committed to offering subsidised accommodation to some newly appointed teachers. Extrapolation of the figures for 2011/12 to provide an estimate of potential total costs over the last five years, (i.e. since 2008/09 when the scheme was changed to a one year provision of subsidised accommodation, through to 2012/13) would give an overall direct cost to the School of just over £80,000. Additional costs incurred for furnishing properties, maintenance, and the costs of the management of the scheme have not been quantified.

Legal and H&S issues

With any employee benefit scheme there are potential tax issues that need to be considered. The School has not considered the possible taxation issues involved in the scheme for providing subsidised accommodation. There are also potential tax issues from the School paying the utilities and council tax for the properties. We understand that the School has now liaised with Medway Council's payroll team in order to get advice as to how to deal with taxation issues at year-end.

A landlord has a number of legal obligations arising from the decision to let a property such as:

- repairs to heating and hot water installations
- repairs to sinks, baths and other sanitary installations
- safety of gas and electrical appliances that you supply fire safety of furniture and furnishings that the landlord supplies

The School should ensure that these obligations have been met when the School signs the tenancy agreement with its landlord. When the School then lets the property to the teacher the School takes on these responsibilities as a landlord to the tenant.

We reviewed all the papers provided by the School relating to the tenancy arrangements dating back to 2006. We found no evidence of these health and safety checks being performed prior to the School signing the agreement with its landlords. We found evidence of gas certificates being sought for the privately rented properties, but there was no evidence of electrical certificates being requested. There was also no evidence of Portable Appliance Testing or evidence of fire safety checks for furniture and furnishings.

We have not found any evidence that the School has sought professional legal advice in relation to the drawing up of the tenancy contracts. Furthermore there could be an issue if the School has not ensured that the landlords of the properties have liability insurance in place. We have been informed that there was no landlord insurance in place for one of the currently rented properties.

Management

The management of the scheme rests with the School Business Manager and there is limited oversight by the Principal and the Governing Body including the Chair of Governors. The Principal signs the starting agreements between the School and the tenant, but management of the property and any roll-forward of the property from year to year is managed wholly by the School Business Manager with no effective oversight by the Principal. This means that the Principal does not obtain assurance that the Scheme is being managed appropriately, albeit the tenancy agreements between the landlord and the School are signed by the Principal.

During our review we identified a number of apparent errors:

- a) the members of staff sharing a two bed property are charged the same rent each as if they were occupying the property as a single tenant. In the case reviewed this has resulted in a total contribution that is higher than the property rent. As such these individuals are not in receipt of the subsidised property that the School has contractually agreed to supply. As such when the tax issues are reviewed there needs to be careful consideration as to which individuals have actually been in receipt of subsidised accommodation.
- b) one individual has been in the accommodation since 2005. We were informed that she is currently paying the full rent for the property, however our review of the School's records show that she is in fact paying £15 a month less than the rent that the School pays to the landlord.
- c) The council tax for one property has not been paid by the School although according to the tenancy agreement the School is liable from November 2011.
- d) The contribution for one individual in a rented property is noted on the agreement at one figure but is in fact contributing £15 less than this figure
- e) It would appear that the School is paying full council tax on some properties when in fact the School would be eligible to pay a reduced council tax based on the single person's discount.

Conclusion

The recruitment incentive scheme at the Howard School represents a significant cost to the School, but there has been no assessment of whether the benefit derived warrants this level of investment. We found some anomalies in how the scheme is currently running, and there are taxation, legal and health and safety issues which have not been considered.

Two High priority recommendations:

Finding 1:	The School has incurred £13.5k costs in 2011/12 in rent and council tax as part of the subsidised accommodation recruitment incentive. Additional costs are incurred in relation to the payment of utility bills and maintenance and furnishing properties
Risk:	Scheme not providing value for money
Recommendation:	The Governing Body should review whether the arrangement should continue, particularly given that the School is in deficit. An analysis should be undertaken of the cost of the

	scheme and the benefits that it provides. Consideration should be given as to which vacancies require a recruitment incentive, and whether other schemes might be more cost effective.
Response:	<p>A full value for money evaluation will be requested by the Chair of Governors from the Principal, on behalf of the Governing Body. All future vacancies will need to be subject to a risk assessment developed by the Leadership Group and agreed by the Governing Body before any incentive scheme is offered to new staff.</p> <p>The Chair of Governors will maintain responsibility for ensuring these actions are completed. The Principal and Leadership Group will be responsible for completing the actions</p> <p>Target date – December 2012</p>

Finding 2:	There has been no documented risk assessment or policy put in place regarding the legal issues relating to the scheme. Taxation issues relating to employee benefits have not been addressed, and health and safety issues not fully considered
Risk:	<p>Non-compliance with legal requirements</p> <p>Fines imposed</p> <p>Damage to reputation</p>
Recommendation:	<p>The School should liaise with Medway Council payroll in order to obtain guidance and advice regarding the taxation implications of the scheme on current and future tenants, and whether previous tenancy arrangements need to be reported.</p> <p>The School should review their responsibilities as a landlord to ensure that all health and safety issues are properly addressed.</p>
Response:	<p>The Principal will ensure that the finance team obtain the appropriate guidance on the taxation implications.</p> <p>The Policy committee will review the current Finance Policy and ensure that the incentive scheme is included and any recommendations for appropriate procedures are developed following expert advice.</p> <p>The Policy Committee will examine whether the Health and Safety aspects of being a landlord need to sit within the current Health and Safety policy or if a separate Recruitment and Retention policy with associated health and safety procedures would be more appropriate.</p> <p>The Principal will be responsible for ensuring taxation issues are addressed by the Finance Team.</p> <p>The Chair of Policy Committee will be responsible for ensuring the schools Finance and associated policies and procedures are fit for purpose.</p>

	<p>The Chair of Governors will remain ultimately responsible for ensuring changes are made.</p> <p>Target date – December 2012</p>
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WOODLANDS PRIMARY SCHOOL – FINANCIAL PROBITY REVIEW

(final report issued 16.11.12)

Woodlands Primary School embraced the extended schools agenda and, in addition to the breakfast and after school clubs found at a number of schools, Woodlands provides a range of facilities for the wider community (e.g. a sports centre and gym, an arts centre, children centre, holiday club and a nursery). The school has a current roll of approximately 380 pupils, aged between 4 and 11 years and approximately 115 children in the nursery. There are approximately 150 members of staff, of which 44 members of staff work in school's community facilities. In addition to the statutory DSG funding, the school received grants of £258k for the children centre and approximately £85k for the nursery through Early Years Intervention Funding and the school's income from activities, at approximately £0.5m is considerably greater than at any of any other school in Medway. The surplus has been used to fund building work and to subsidise the breakfast club and trips.

This report focuses on the operation of the payroll, procurement and income processes across the range of activities at the school. A second report is attached which reviewed the schools' building programme.

FINDINGS

This review covered payroll, procurement and income, and began with an assessment of the control arrangements as set out in key documents and confirmed through interviews with the Headteacher and the School Business Manager. We obtained transaction data and where we identified areas of potential anomalies, we undertook targeted testing in order to provide assurance that there were no concerns arising.

Our review and testing of the financial control arrangements confirmed that there were robust processes in place for the management of payroll, income and expenditure. An action plan records ten actions to further strengthen current arrangements.

During our review we identified a potentially significant issue relating to the treatment of VAT. Internal Audit have sought the advice from the Council's VAT advisers and the School is assessing its liability since 2008 by reviewing its income relating to the gym and catering associated with lettings. The Council will take action necessary to correct the matter with HMRC once the School has completed its review, with the commitment to resolve this matter before the School becomes an Academy, and to ensure there are sufficient funds held by the School to meet this obligation.

CONCLUSION

We are able to confirm that, with the exception of the VAT issue identified, the School has robust controls in place. We did not identify any probity issues.

One High priority recommendation:

Finding:	The school has various income streams, some of which are subject to standard VAT charges (ie gym sessions and catering). The school has not been charging VAT for catering and gym sessions.
Risk:	The school is breaching HMRC regulations and could be subject to fines.
Management Action:	<p>The school will calculate the outstanding VAT on income for gym sessions and catering income associated with lettings from September 2008 to September 2012 as per the requirement of HMRC. If the school has any queries, they will seek advice from the Principal Accountant in the Schools Finance Team. The School will need to get the outstanding VAT calculations signed off by the school's Governing Body and submit the calculations to the Education Finance Team.</p> <p>Implementation date –Immediate</p> <p>Education Finance will liaise with the school to ensure that appropriate provision has been made by the School to pay HMRC.</p> <p>Implementation date - November 2012.</p> <p>The school will charge VAT on catering associated with lettings.</p> <p>Implementation date - September 2012.</p> <p>The school governors will decide whether to increase the rate of gym sessions or pay the VAT out of current rate.</p> <p>Implementation date - December 2012</p>

WOODLANDS PRIMARY SCHOOL – BUILDING WORK

(final report issued 16.11.12)

In 2009/10, Woodlands Primary School had a highly publicised problem with a building project that was intended to convert the school to two forms of entry. Medway Council instigated remedial work that left the school short of two forms of entry. Since that date, the school has undertaken an extensive program of capital works funded from surpluses from the income and grants obtained from the School's community facilities.

During the probity audit of the Woodlands School (report 12013), the School's ongoing capital programme was identified. This report provides assurance over the Schools compliance with legal obligations and financial procedures related to its capital programme.

FINDINGS

The School carried out a number of building jobs in 2011 and 2012. In 2011 there were three building projects and three smaller building works with a total cost of approximately £99,000. In 2012 there were three different building projects with a total budget of £80,000. We are satisfied that all these building works were individual

projects and that each came below Medway Council's limit for tenders being required.

These projects were funded from the School's income streams and as such it was the responsibility of the School to monitor and manage them. We reviewed documentation supporting the 2011 and 2012 building programmes and are satisfied that the arrangements for the letting of the work and the management of the projects were satisfactory, in that:

- The school is taking appropriate steps to ensure it is not in breach of Building Regulations and consults with the Medway Council's Planning Officers when necessary.
- Plans for the works were included in the School Development Plan which is approved annually by Governing Body.
- The school is obtaining quotes where required although improvements are needed in documenting decisions to improve transparency.
- The school's current site manager is responsible for overseeing the building work at the school.
- The building work invoices are checked and initialled by the site manager prior to being paid to ensure that work has been completed satisfactorily to the proposed specifications and within the budget
- The school engaged an external project manager/consultant for the preliminary work for all of the building projects for summer 2012. The consultant produced a specification, and obtained quotes.
- Medway Council's Facilities Management monitors the School's compliance with Health and Safety legislation. The latest Compliance Monitoring report (dated 6 March 2012) shows that the school are largely compliant with relevant legislation although a number of remedial actions were identified. A re-inspection is due and will be arranged in the near future. The school's last asbestos survey was dated 1 January 2012. Weekly checks are performed and logged by the caretaker. Facilities Management have no concerns regarding asbestos at the school. The school ensures health and safety and asbestos issues are addressed with contractors prior to starting the commencement of work at the school.

A significant proportion of the monies used to fund these projects came from the income generated by the Sports Centre. The Sports Centre was built in 2007, costing £1.1m, with funding from a variety of sources, but the Football Foundation was the main funding provider. The school informed us that the grants used to build the sports centre placed no restrictions on use of income generated as long as the school maintained the facilities for the continued use of the community. In practice, the bulk of this commitment means replacing the pitch when it reaches the end of its life. Our enquires at the school and Medway Council have failed to obtain a copy of the grant terms and conditions, so we have been unable to confirm that the school's use of this income is appropriate.

The school's School Development Plan also includes a plan for the completion of two additional classrooms in order to create space for a separate IT suite and a library.

We have been informed by the Headteacher that the school is not planning to carry out this or any further building work until the school has become an academy, which is scheduled for April 2013.

Our review and testing of the school's capital programme confirmed that there were no probity issues. An action plan, records four actions to strengthen current arrangements.

CONCLUSION

We are able to confirm that the management of building projects is sufficiently controlled and we did not identify any probity issues in the capital programme. We have suggested enhancements to ensure the control framework is robust. We are also satisfied that the School has adopted the action plan for strengthening the current financial arrangements.

ST MICHAEL'S RC PRIMARY SCHOOL *(final report issued 7.12.12)*

St Michaels is a voluntary aided school in the Archdiocese of Southwark and has a current roll of approximately 370 pupils. The headteacher was appointed in September 2010. The School Business Manager oversees financial processes with support from two members of staff.

FINDINGS

Our review covered payroll, income and expenditure, and began with an assessment of the control arrangements as set out in key documents and confirmed through interviews with the headteacher and the School Business Manager (SBM). We obtained transaction data and where we identified areas of potential anomalies, we undertook targeted testing in order to provide assurance that there were no concerns arising.

Our review and testing of the financial control arrangements confirmed that there were robust processes in place for the management of payroll, income and expenditure. An action plan, records two actions to further strengthen current arrangements.

CONCLUSION

We are able to confirm that the School has robust controls in place and that we did not identify any probity issues. We are also satisfied that the School has adopted the action plan for further strengthening the current financial arrangements.

TEMPLE MILL PRIMARY SCHOOL *(final report issued 11.12.12)*

The financial probity audit for Temple Mill Primary School completed earlier this year (final report issued 27 June 2012) identified that further action was required to address control weaknesses arising from the previous investigation into misappropriation of funds (reported in November 2011) more effectively. Further improvements were recommended in respect of:

- Approval of purchases;
- Evidencing receipt of goods before payment is made;

- Banking income promptly;
- Recording all assets and protecting the asset register against loss or damage.

Six further recommendations were made, all being accepted by school management with an undertaking to implement them by September 2012.

The audit process is not complete until an independent follow-up is performed in order to confirm progress in addressing the weaknesses identified, to evaluate the extent to which financial controls have been improved. An initial meeting with the headteacher and Chair of Governors established that implementation of one of the recommendations – declarations of interest by all staff involved in the procurement process – had been delayed as a result of the former's absence following the summer break and we have been advised that this will now be in place by 21 December 2012.

We therefore carried out sample checks to confirm implementation of the remaining recommendations, and overall we can confirm that progress has been made in relation to most of the issues identified, and the current arrangements are a significant improvement over the controls in place at the time of the audit investigation in 2011.

However, weaknesses remain in the arrangements now in place and therefore further recommendations were made and accepted by the headteacher. These related to:

- Nominating a third authorised signatory for the bank account so the headteacher does not need to co-sign cheques reimbursing both herself and her spouse for mobile phone charges and purchases made for school use;
- Discouraging staff from purchasing items required for school use personally then claiming reimbursement, with proper purchasing procedures to be followed instead, i.e. requisition raised, approved by the headteacher then ordered officially by the school;
- Banking income received more frequently to ensure that cash holding does not exceed the maximum specified in the school's finance policy;
- Revising the format of the asset register to include additional information such as dates of purchase and cost, and ensuring that items purchased (such as 'desirable' electrical equipment) are recorded in the asset register promptly.

The level of issues is now such that we would not consider it necessary to undertake further follow up work - but do encourage the headteacher and chair of governors to implement the improvements noted, continue to monitor and review the financial arrangements in place, and to make use of the guidance and support provided by Medway Council.