AUDIT COMMITTEE

25 SEPTEMBER 2013

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 a list at **Annex A** of the individual outputs issued since the last report to this committee. The individual outputs are provided at **Annex B.** Each audit provides assurance over the appropriateness and effectiveness of the control arrangements in place. Controls are assessed in terms of whether they mitigate the identified risks, and maximise the likelihood of achieving stated objectives. Each output has been shared and agreed with management.

2.2 The definitions of the recommendation and audit opinion options, as endorsed by Audit Committee in July 2013, are shown at **Annex C.**

2.3 An overall audit opinion is provided for each full audit. Audit opinions are not provided in the outputs of individual site reviews, but these outputs form the basis of full audit reports which do contain an opinion on the council-wide procedures in place.

2.4 All audit recommendations are shared with management and agreed actions recorded, along with the implementation date and the officer responsible. The agreed management action plan relating to significant or material recommendations is incorporated in the issued final audit report, and summarised for Audit Committee.

2.5 Internal Audit obtains confirmation of progress on recommendations made, usually within six months. Where the audit resulted in an overall opinion that the control arrangements "Need Strengthening" or are "Weak", a follow up is undertaken of the revised arrangements. The original audit opinion is reviewed in light of these findings, and the outputs of these follow ups are presented to Audit Committee.

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

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

Annex B Summary information on completed audits

Annex C Definition of audit opinions and recommendation priorities

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.gov.uk

Background papers

None.

SCHEDULE OF COMPLETED WORK ANNEX A						
	Opinion	Authority Wide	Children and Adults	Regeneration Community and Culture	Health	Business Support Department
Risk Assessed and Additional Work						
Innovation Centre Medway				2		
Governance Audits						
National Fraud Initiative						2
Carbon Reduction Commitment						✓
Follow Ups						
Debtors Income						2
School Probity Reviews						
St Margaret’s Infants			✓			
Park Wood Infants			✓			
St Nicholas CEVC Infant			✓			
Hilltop Primary			✓			
Site Reviews						
Income - The Villager				✓		
Income - Trading Standards				✓		
Income - Duke of Edinburgh			✓			
Grant Payments - Rural Liaison						✓

Key: 1 = Strong 2 = Sufficient 3= Needs Strengthening 4 = Weak

✓ = work carried out but no opinion provided in that output

ANNEX B

SUMMARY INFORMATION ON COMPLETED AUDITS

INNOVATION CENTRE MEDWAY *(final report issued 11.9.13)*

In March 2013, as a result of an investigation into the management arrangements at the Innovation Centre Medway (ICM), a report was provided (as an exempt item) to the Audit Committee. That report contained an action plan for management containing 22 recommendations as there were significant failings identified, particularly in relation to financial management and ICT arrangements.

Although the ICM, in purely financial terms, does not represent a significant financial risk to the council, the ICM's risk profile is heightened by the following factors:

- It has a relatively volatile income stream
- the centre needs to be seen to be run like a commercial venture whilst being required to work to public sector arrangements and rules
- it is sited at a distance from the central council offices of Gun Wharf
- the council has not previously had involvement in a venture of this nature
- it has a high public profile which increases the reputational risk it poses to the council
- It provides a data centre which is run outside of the council's core ICT arrangements

We have now undertaken an audit review to confirm the progress that has been made in addressing the actions identified, and to provide an overall opinion on the financial management and ICT arrangements now in place at the ICM.

Office Licenses

We are pleased to report that responsibilities for office tenancies are separated appropriately, with key licensee decisions subject to authorisation. Each license is signed off by a senior officer within the Regeneration, Community and Culture Directorate (RCC), who is also responsible for approving decisions to end a license agreement. The office licenses are standardised and contain a "security of tenure exclusion". Incidental costs are not included in the license and are invoiced separately. Licensee debt is being effectively monitored and addressed and is now regularly reviewed, and there is regular liaison between the ICM Manager and the council's finance staff on this matter.

Financial Management

Financial management and procedures are robust with budgets subject to regular review by the ICM Manager, RCC management, and Finance. All expenditure is approved by RCC management. Finance currently reconcile office license income with integra records to ensure completeness and accuracy of records. Appropriate tendering arrangements are followed through liaison with category management. Maintenance arrangements which had previously been haphazard and with little demonstration of the pursuit of value for money have been addressed, largely through the roll out in June 2013 of NORSE as the council's provider of facilities management. An asset register is now in place.

Billing for electricity has begun, with all office spaces (bar one) being metered, and the licensees of the two largest office spaces have been billed and backdated to when they brought their business to the Centre.   The office space previously provided to an informal group, at nil cost, has now been re-allocated to an office licensee, providing rental income for this space.

The ICM is not budgeted to achieve break even this year, not least due to the remedial works required to address outstanding maintenance issues. A record is being kept of those items of expenditure that relate to remedial works so that at year end management can demonstrate the budget achieved beyond these costs accrued through previous poor management.

Reporting

The performance and management of the ICM is directed by RCC Senior Managers, with further oversight provided by the ICM Board. It is critical that the Board has a clear understanding of the purpose of the ICM, and a vision for its long term future. There is no overall documented strategy for the ICM, and as such there is a risk of incoherent decision making. There is little clarity over the extent to which the data centre should generate income from external clients. We also had a concern that investment in ICT might not meet or could exceed long term requirements for the ICM, however given the proposals anticipate reduced costs, and a significant increase in the level of capacity, it would appear that the implementation of the ICT enhancement is of benefit to the council. A further potential issue was identified, regarding the selection and vetting process for licensees, and whether there is a clear understanding by RCC managers and the ICM board as to which companies should be granted an office license, and methods for prioritizing applicants. It has been agreed that a report will be provided to the ICM Board over the strategy of the ICM, including the vetting and selection process.

Management of Information Technology

Previously the administrative systems at the ICM were held on a server at the ICM, with no oversight outside of the centre to ensure it met the council's governance requirements. It was found for instance that there were no formal back up arrangements. From August 2013 the ICM's administrative data is housed on the council's systems, the server is sited within Gun Wharf, and the system is subject to the standard security, resilience and capacity arrangements, including regular back up.

The Data Centre offers facilities such as air conditioning and secure racks, for housing computer hardware, either for licensees or external clients. The Data Centre is now subject to effective oversight by the ICM Manager to ensure appropriate authorization of all hardware stored at the centre.

The infrastructure to support the Data Centre was not providing value for money, as it was both costly and did not meet capacity or resilience requirements. The ICM Manager has arranged an increase in capacity which reduces some of the immediate service concerns. The password access to the system has been reviewed, with a full record maintained of access granted to the system. The single point of failure and the high costs of broadband provision are due to be addressed through the ICT revised arrangements being proposed.

The ICM Board approved a proposal by the ICM Manager, to go out to tender for the broadband management provision, with the expectation that a new arrangement would reduce costs whilst increasing the volume, quality, resilience and security of the ICT services available to the licensees. This would also facilitate generating more income from the Data Centre, should space for the hardware become available. The matter is currently with Category Management. The level of risk in continuing with the current arrangements in the interim has not been assessed, however we understand that management are investigating the possibility of seeking an exemption from the category management procedures in order to limit the period of time before the new arrangements are in place.

The management of the Data Centre is currently provided by one of the tenants within the ICM, and this arrangement has never been subject to a signed contract. The arrangement will need to be reviewed and either brought in house or appropriate procurement routes followed in order to ensure the council can demonstrate the pursuit of value for money.

CONCLUSION

Our overall opinion on the effectiveness of the arrangements for financial and ICT management at the Innovation Centre Medway is that, taking into account the proposed revised ICT provision, the arrangements are now **sufficient**. A definition of audit opinions is included in Appendix B to this report. The previous audit output resulted in 22 recommendations, and a further point arising at the time the output was reported to Audit Committee. This report contains 5 material level recommendations which have been made to address the outstanding issues identified, all of which have been agreed by management. These actions relate to:

1) The ICM Board formally agreeing the strategic direction of the ICM
2) The ICM Board formally agreeing the criteria for approving office licensees
3) Obtaining legal agreement regarding license queries
4) Ensuring office spaces only used by licensed companies
5) Procurement process to ensure value for money provided by provision of day to day management of the data centre

The income arrangements at the ICM will be subject to review later in the 2013/14 financial year.

CARBON REDUCTION COMMITMENT *(final report issued 9.9.13)*

The Carbon Reduction Commitment (CRC) Energy Efficiency Scheme applies to all organisations consuming at least 6,000 MWh (megawatt hours) of electricity in the 2008 calendar year. Organisations have been required to register and, from April 2010 onwards, produce an annual report of energy consumption and consequent carbon emissions. They are also required to purchase allowances for every tonne of carbon emitted, this currently priced at £12 tonne – the purchase cost of allowances for Medway's emissions reported for 2011/12 was almost £294,000.

An evidence pack must be produced and maintained to support the annual report and this should contain an 'audit certificate' signed by "a person who has management control of your activities". The pack may also be subject to periodic audit by the Environment

Agency. The majority of Medway's corporate properties and schools obtain their energy through the KCC Laser Energy Buying Group – this should obtain value for money through the economies of scale and market advantages available through procuring large volumes of energy. KCC Laser therefore have records of a very significant proportion of the energy provided to Medway's properties, and had developed the production of CRC annual reports and evidence packs for KCC and other authorities using their services – on that basis, an agreement was reached for Laser to produce the annual reports and evidence packs for Medway.

There is no stipulation that the requirement for an 'audit certificate' means that the evidence pack, or the annual reports, need to be subject to review by an organisation's internal audit function. However, as there is some synergy between checking evidence packs and the normal duties of internal auditors we have carried out a review of Medway's first two annual reports and the supporting evidence packs. Being aware that KCC's own internal audit function had reviewed Laser's processes for recording energy consumption and producing annual reports, and identified no significant issues, we placed reliance on their work and concentrated instead on the accuracy of properties and energy sources recorded for Medway. We reviewed the documentary evidence supporting the return for 2010/11, revisions for the 2011/12 return and the annual reports for 2010/11 and 2011/12.

<u>Property records</u>

We initially compared the properties recorded on the first annual report produced by Laser, for 2010/11, against an asset list provided by Medway's Corporate Asset & Property Management function. This exercise identified a number of mismatches and our check on a small sample of known properties also failed to identify the Market Hall MSCP on either report.

In summary, 65 properties shown on the Laser annual report were not identified on the Medway list (including Main Streetlighting and Underpass lighting - which appears reasonable - nine schools (eight being voluntary aided or controlled) and five housing-related properties; in addition, the annual report contained one duplicated entry (Feeder Pillar Jeffrey Street CP). Conversely, 43 properties shown on the Medway asset list were not identified on the Laser report, including 24 apparently housing-related properties. There were also a number of instances where the property name/description varied between the two reports, for example 'Woodlands ICS' and 'Lifelong Learning Centre' were identified to be the same building.

Whilst these mismatches possibly reflect the quality of the Medway asset records rather than any significant problem with the annual report produced by Laser, there is a risk that Medway's annual CRC report for 2010/11 may have included some ineligible consumption and omitted some that should have been included.

Comparison of properties shown on the annual reports for 2010/11 and 2011/12 indicated that a number that appeared in the initial report were omitted from that for 2011/12 and a number of new properties were identified for inclusion. The principal omissions were street/stairway/ underpass lighting, housing (HRA) properties, the gypsy caravan site, Lordswood Leisure Centre/Sports & Social Club (managed on behalf of the Council) and buildings that have been disposed of (e.g. Municipal Buildings). The principal additions were individual feeder pillars for lighting, landlord supplies for business start-up units (e.g.

Hopewell Drive) and new properties (e.g. Information Centre at Chatham Waterfront bus station), plus additional energy sources that had not been identified previously. The omission of residential dwellings and the changed approach to street lighting for the second year of the scheme is considered to be in line with guidance issued by the Environment Agency. The omission of certain properties and inclusion of additional energy sources indicates that both Medway property staff and Laser are being pro-active in identifying these and improving the accuracy of Medway's annual returns, but as some supplies that could be classed as residential (e.g. Landlords supply 56-63 Tintagel Manor) or care establishments (e.g. Platters Farm Lodge, Shalder House) continue to be included there is evidently scope for further improvement.

Energy usage

We compared the types of energy recorded on the CRC annual report and Medway's asset list for a sample of 27 properties, as well as identifying properties where no electricity supply had been identified – this would suggest an omission as the majority of properties need electricity for lighting or for gas-powered heating to operate. For example, in respect of the Market Hall MSCP it seems unlikely that electricity would not be needed for lifts, lighting and pay & display machines – but it appears possible that its omission may be due to energy bills being paid by Tesco.

In seven cases the CRC annual report indicated more energy sources than Medway's asset list, but it may be that some of the emissions relating to another three properties are not being included in the total calculated for the annual report. This exercise identified that no electricity meter was shown on the CRC annual report for twelve properties – though the Medway asset list indicated that three of these did have electricity meters. There is consequently a lack of assurance that all energy used in Medway buildings is being captured and, therefore, that the CRC emissions calculation is accurate.

To confirm that data used by Laser for calculating carbon emissions is accurate, we checked the 2010/11 records to determine whether energy usage recorded in the evidence pack for a sample of 19 properties could be tracked to invoices scanned into Integra. Potential anomalies were identified on two properties, the annual report indicating the following energy usage for the meters that were not matched to invoices:

- Corn Exchange Halls – second gas supply 50,555 KWh (9.282 tonnes CO_2);
- Lifelong Learning Centre – gas supply 37,666 KWh (6.915 tonnes CO_2).

Given that total carbon emissions were calculated to be 34,548 tonnes CO_2 these amounts represent a potential overstatement of less than 0.05%, so are not considered material.

This exercise also identified that electricity charges for the pumping station at Riverside, invoiced direct by EDF Energy, had not been captured on the annual report (though usage is relatively low at roughly 1000 kWh per month).

A review of annual reports to identify any properties that had been disposed of, either prior to or during the year, identified that the report for 2010/11 included 35,100 kWh (18.99 tonnes) used by the Municipal Buildings, a property that we believe was disposed of prior to April 2010, so it is unclear why this was included in the annual return. In addition, Shaws Wood OPH is recorded by Medway to have been sold on 5.5.10 so the usage of

83,856 kWh/45.37 tonnes in a period of just five weeks is considered unlikely to be accurate.

Annual reports

Comparison of the total energy consumption/carbon emissions for the two years indicates a significant reduction of 25.32% in Medway's emissions for 2011/12, contributory factors cited to include exclusion of street lighting, removal of 51 supplies and addition of 47 new supplies to the portfolio. Analysis of the energy consumption per meter identified a number of very significant differences between the two years, casting some doubt on the accuracy of data collection in one or both years, the most extreme being where no electricity usage whatsoever had been identified. Removal of street lighting and substitution of feeder pillars resulted in a net reduction of 10,514,770 kWh (5,688 tCO_2), omission of residential properties reduced consumption by 3,829,464 kWh (emissions by 817 tCO_2) and removal of non-Medway properties included in the 2010/11 return reduced consumption/emissions by a further 756,866 kWh (465 tCO_2).

Whilst this improvement is welcome, the size of reduction from the previous year has had the effect of improving Medway's position in the national Performance League Table disproportionately (from 1,098th of 1,301 organisations in the first year to 256th of 2,097 in the second) through significant scores being awarded for the percentage reduction in emissions and the proportion of organisational turnover they represent. This suggests that Medway's initial payment of £293,832 for CRC allowances for 2011/12 may rise significantly in future years, but as this was significantly lower than the provisional budget allowed, and Integra indicates that the budget for 2013/14 remains unchanged, this should not be a problem.

CONCLUSION

Our review of the initial CRC annual report reflected a lack of assurance over the accuracy of the data produced by Laser, due to queries surrounding the validity of both corporate properties and fuel types included in it. Extending the review to cover the second annual report indicated that both Medway property staff and Laser are being pro-active in improving the accuracy of the annual returns, but there is evidently scope for further improvement.

Whilst the resultant improvement in Medway's relative performance against other participants in the scheme appears impressive, it has had the effect of creating an artificially low initial cost for purchasing CRC allowances, but this is considered unlikely to lead to future overspends against budget.

No audit opinion was allocated, but three medium priority recommendations were made, relating to:

- further improving the accuracy of Medway's annual returns in respect of properties and energy sources to be included;
- checking the reasonableness of annual returns.

Recommendations were accepted by management and appropriate actions have already been taken to address the weaknesses identified.

NATIONAL FRAUD INITIATIVE *(final report issued 11.9.13)*

In March this year, the Audit Commission's National Fraud Initiative (NFI), which matches personal data held by various public bodies, confirmed that since its inception in 1996 it has helped to identify over £1 billion potentially lost to fraud, overpayment and error across the UK.

The NFI is one of a number of tools the council uses to maintain or improve its fraud resilience. The council has a statutory duty to submit data and failure to investigate the matches returned misses an opportunity to identify fraud and other overpayments. There are also reputational risks as the council's response to the matches is subject to oversight by the Audit Commission and External Audit.

In October 2012, Medway Council submitted the following data to the Audit Commission so that it could be matched to data provided by other local authorities and government departments:

- Concessionary Travel Passes
- Creditors History and Standing
- Housing Benefit Claimants
- Housing Tenants
- Insurance Claimants
- Payroll
- Private Residential Care Homes
- Resident Parking Permits
- Purchases under Right to Buy
- Licensed Taxi Drivers
- Blue Badge Parking Permits

The council was not able to provide the data required relating to personal alcohol allowances or market traders. The IT arrangement for holding the personal alcohol licenses does not retain the data in an appropriate format for submission to the NFI, and the market trader information is held hard copy. We understand that these arrangements are subject to review.

The data is matched in a series of reports which are published on an online reporting tool. It is the responsibility of each participating organisation to review the matches involving their data and determine which are legitimate, which are as a result of error, and which may require further investigation as potential fraud. Progress and outcomes have to be recorded on the online reporting tool and in June 2014 the Audit Commission will publish a report on the 2012/13 NFI exercise.

The Audit Commission has an advised timetable for all participating organisations, and recommends a preliminary evaluation of all matches by the end of May 2013. The Audit Commission has a stated expectation that the majority of matches will be closed before the March 2014 cut off, although it is accepted that there may be some ongoing investigations.

Medway Council has received 74 reports with a total of nearly 1000 matches, receiving the data in 12 releases, most of which were received in January and February 2013. The most significant level of matches relate to creditors and housing benefits.

Given the significant volume of matches to be reviewed, and the resource implications in undertaking this work, it has not been possible or deemed good use of resources to undertake an initial evaluation of 100% of the matches. Audit Services have worked with management to agree the reports that are likely to be most productive so that work can be prioritised.

Audit Services have provided training and ongoing support for staff undertaking the report checks, have taken responsibility for processing the reports related to Medway Council staff, and are responsible for handling any fraud investigations arising from the NFI and the outcome of all full investigations are reported to Audit Committee.

This report provides assurance on progress made to September 2013. Internal Audit will provide a formal report on Medway Council's delivery of the 2012/13 NFI early in the following financial year. The status of all matches at 3 September 2013 was analysed in order to assess progress.

Creditors

There are in total over 4,000 matches relating to creditors. The vast majority of these matches relate to potential duplicate payments of which a high proportion are matched because they are cyclical payments. In addition a number of the matches are quite imprecise. As such the checking of this report represents a high resource input with relatively low value outcome. We are pleased to note that the creditors team has now begun to focus on reviewing the duplicate supplier matches, of which there are just under 1000. Progress on these two reports is behind schedule but we acknowledge that the number of checks performed has increased over recent weeks.

Progress on the creditors matched with Medway Council payroll has been good, with nearly 75% of the matches reviewed and ensuing investigations completed.

The VAT report includes the remaining 700 creditor related matches. This report is relatively low risk and management are confident that the creditors system will ensure VAT is correct (to within 5p). A review of a sample of the matches has been undertaken and no anomalies have been identified. On this basis there is no intention to continue a review of this report.

Housing Benefit

There are nearly 3,500 Housing Benefit matches.

Audit Services arranged for the DWP to review the 1,800 Housing Benefit to Pension matches and identify any where there is a DWP interest. To date 13 % of the matches have been closed and a number of fraud referrals raised for investigation by the DWP's Fraud Investigation Service. No investigations have been completed but the council will be kept informed of actions taken. Where appropriate DWP are referring cases back to the council for further investigation or closure.

Audit Services have taken the lead on the housing benefit matches to Medway payroll and progress is on target to complete all these checks by the end of September. A number of investigations are underway and it has been arranged to include a reminder on the council's "self-serve4you" HR portal that it is the duty of all Medway residents, including any who are Medway Council employees, to inform the relevant department of a change in their circumstances.

Customer Contact have prioritised student loans and UK Border Agency matches and have then moved onto the other smaller datasets. The checking required to resolve these matches has proved to be onerous and has not yielded significant returns. It has been agreed that resources are going to be re-focused to the match between housing benefit and payroll reports relating to other councils, as checks of these matches are likely to prove more productive.

Blue Badges

There are just over 1,000 blue badge matches to deceased persons. Approximately 750 of these relate to badges due to expire by 2014, and the council's data in relation to these is poor. For this reason the matches have not been reviewed in full, but they have been used to identify where individuals with allocated disabled bays have since died. There may be up to 40 parking bays to be released as a result of this exercise.

The report relating to the remaining blue badge matches was released August 2013. The data submitted is of sufficient quality to warrant thorough investigation, and this work has now begun.

Other data sets

Progress on the smaller data sets has been good.

CONCLUSION

To date, Medway Council has identified approximately £56,000 in overpayments as a result of the 2012/13 NFI exercise, and a number of fraud investigations are underway. There have been limitations regarding some of the data sets submitted to the NFI, due to the way data has been collated and held by the council. We have been advised that these data arrangements are being reviewed. Reasonable progress has been made overall on the reports provided relating to Medway Council data, and an appropriate risk-based approach has been adopted.

Overall it is our opinion that the progress to date has been **sufficient.** There were no recommendations arising from this review.

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 is provided to the individual School, Senior Management within the Council, and once finalised it is presented to the Council's Audit Committee.

The Guide to the Law, provided by the then Department for Children, Schools and Families (now Department for Education), defines the required School governance structure for ensuring financial probity. The Governing Body hold the Headteacher 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.

ST MARGARET'S INFANT SCHOOL *(final report issued 2.7.13)*

St Margaret's Infants is a larger than average, three form infant school for children with ages ranging between 3-7 years. The Bursar oversees financial processes with support from one member of staff. Our review focussed on procurement, purchasing and payments processes within the school and commenced with an assessment of the control arrangements as set out in School's key documents and confirmed through interviews with the headteacher and the Bursar. 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. The audit did not examine payroll or income and cash handling processes.

Our review and testing of the financial control arrangements confirmed that there were robust processes in place for the management of procurement, purchasing and payments. An action plan, which management have agreed, records three actions to further strengthen current arrangements.

CONCLUSION

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

PARK WOOD INFANT SCHOOL *(final report issued 25.7.13)*

Park Wood Infant school is a larger than average, three form infant school for children with ages ranging between 3-7 years. The Bursar supports the Headteacher with the management of financial processes. Our review focussed on procurement, purchasing and payments processes within the school and commenced with an assessment of the control arrangements as set out in School's key documents and confirmed through interviews with the Headteacher and the Bursar. 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. The audit did not examine payroll or income and cash handling processes, but the audit does provide an opportunity to advise on best practice in these areas where incidental observations are made.

Our review and testing of the financial control arrangements confirmed that there were processes in place for the management of procurement, purchasing and payments but these were not complete or applied consistently. Action is required to strengthen arrangements over gifts and hospitality, credit card use and obtaining quotes / recording procurement decisions. Documentation to support purchase orders needs to be retained more consistently.

An action plan, which management have agreed, records six actions to further strengthen current arrangements.

CONCLUSION

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

ST NICHOLAS CEVC INFANT SCHOOL *(final report issued 2.8.13)*

St Nicholas CEVC Infants is an infant school for children with ages ranging between 4-6 years. On average there are 116 children in the school. Children are placed in 4 class groups according to their age.

Our review focussed on procurement, purchasing and payments processes within the school. We commenced with an assessment of the control arrangements as set out in School's key documents and then confirmed through interviews with the Headteacher and the Bursar. 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.

The audit did not examine payroll, or income and cash handling processes.

Our review and testing of the financial control arrangements confirmed that there were robust processes in place for the management of procurement, purchasing and payments. An action plan, which management have agreed, records three actions to further strengthen current arrangements.

CONCLUSION

We are able to confirm that the school has robust controls in place to manage procurement, purchasing and payments, and we did not identify any probity issues. We are also satisfied that the school has adopted the action plan to further strengthen the current financial arrangements.

HILLTOP PRIMARY SCHOOL *(final report issued 17.7.13)*

Hilltop is a large primary school with 425 pupils aged between 4 and 11 years. In 2012-13 £88,012 of income was generated locally, primarily through hire of facilities such as the hall and swimming pool but also through the breakfast club and contributions to school visits (the school does not have a separate voluntary fund).

Our review assessed the effectiveness of controls operating over the checking, handling and recording of income - we did not cover issues such as expenditure, procurement and payroll. We interviewed the staff responsible for the day-to-day arrangements for income, assessed the control arrangements in place, obtained local income records and undertook sample and observational testing in order to provide assurance on the application of the controls.

Our review and testing of the financial control arrangements confirmed that there are very robust processes in place for the management of income and we did not identify any probity issues.

CONCLUSION

We are able to confirm that the school has very robust controls in place over income and we did not identify any probity issues. As such, no recommendations to improve control were considered necessary.

Income Audit Site Reviews

The following audits form part of a series of income reviews to be undertaken within the Council during the current financial year. Issues arising from individual reviews will be reported to relevant management but no audit opinion will be allocated. Towards the end of the financial year the outcome of all the income reviews will be collated into an overview report, providing an overall audit opinion.

THE VILLAGER - Rural Bus Challenge *(final report issued 31.7.13)*

The Villager scheme (which originated from the Rural Bus Challenge) generated income of £36,712 in 2012/13, through individual and group membership fees, minibus hire for community groups and regular excursions.

Our review covered the checking and handling of income, income retention and budgetary control. We interviewed the staff responsible for the day-to-day arrangements for income and assessed the control arrangements in place. We obtained local income records and undertook sample and observational testing in order to provide assurance on the application of the controls.

Our review and testing of the financial control arrangements confirmed that, overall, there are processes in place for the management of income but arrangements need strengthening further.

There is no segregation between the duties of handling, recording, custody and transfer of income to cashiers, one member of staff is responsible for processing all income, which presents a risk of fraud and error and could place the member of staff concerned in a vulnerable position.

Local income records were not always updated or reconciled promptly and we identified inconsistencies in the calculation of charges for group hire. In addition, due to the absence of safe facilities, cash held exceeded the Medway Insurance limits for loss of a locked receptacle on several occasions.

The limited resources available expose the Council to a certain level of risk and further action is required to minimise this.

CONCLUSION

We are able to confirm that The Villager scheme has controls in place for income collection and recording, but work is needed to further strengthen arrangements.
Four recommendations were made and accepted by management, relating to:

- Involving two people in the process of handling, retaining and transferring income;
- Improving the accuracy of local income records;
- Formalising terms and conditions for group hire and applying these consistently;
- Transferring income to cashiers promptly;
- Raising invoices for hire charges promptly.

TRADING STANDARDS *(final report issued 2.9.13)*

Trading Standards generated income of £35,984 in 2012/13, through membership fees from the Fair Trader Scheme, fees from the issue of poisons, petroleum and explosive licences and verifications of weights and measures.

Our review covered the checking and handling of income, income retention and budgetary control. We interviewed the staff responsible for the day-to-day arrangements for income and assessed the control arrangements in place. We obtained local income records and undertook sample and observational testing in order to provide assurance on the application of the controls.

Our review and testing of the financial control arrangements confirmed that, overall, there are limited processes in place for the management of income and arrangements need strengthening considerably in recording and retaining local income records and reconciling income to ensure all income due is identified and income received can be accounted for.

These control weaknesses were illustrated by our testing identifying that an amount of £105 cash received by Trading Standards in October 2012 and apparently sent to Cashiers cannot be accounted for - as local income records are not held and reconciled to Integra this had not been noticed previously.

Similarly, our testing also identified that a payment relating to the membership of the Fair Trader Scheme, received in January 2013, had not been processed, the cheque being found in a desk drawer - this had been allocated to the member on the database, but this is not reconciled to income recorded on Integra.

In the longer term, Trading Standards are looking towards procuring a new IT solution for use across Regulatory Services, which will provide a more effective system for controlling licences and income due.

CONCLUSION

We consider that Trading Standards has limited controls in place for income collection, and work is needed to strengthen arrangements.

Three recommendations were made and accepted by management:

- Ensuring that the Council's schedule of fees and charges for Trading Standards includes the locally set fees for poisons registration from 2014/15;
- Updating licence spreadsheets to reflect actual income received, including additional fees and changes to existing licences, and following up expired licences promptly;
- Strengthening procedures to ensure all income received is sent to cashiers promptly, processed correctly and recorded on Integra.

All actions had been implemented by the conclusion of the audit.

DUKE OF EDINBURGH AWARDS *(final report issued 30.7.13)*

The Duke of Edinburgh Awards scheme generated income of £40,939 in 2012/13, through sales of publications, expedition fees and presentation evenings.

Our review covered the checking and handling of income, income retention and budgetary control and began with interviewing the staff responsible for the day-to-day arrangements for income. We then assessed the control arrangements in place, which we confirmed by obtaining local income records and undertaking sample and observational testing in order to provide assurance.

Our review and testing of the financial control arrangements confirmed that, overall, there are robust processes in place for the management of income. Controls are in place to ensure all income due is received, recorded, retained securely and transferred to Cashiers. Receipts from Cashiers are reconciled to local records and confirmed monthly against Integra crystal reports.

CONCLUSION

We are able to confirm that the Duke of Edinburgh Awards team has robust controls in place for income collection and recording and that we did not identify any significant issues.

However, two recommendations were made to further strengthen current arrangements, relating to involving a second person in checking/reviewing income and ensuring that income is transferred to cashiers on a weekly basis. Both were accepted by management.

Grant Payment Audit Site Reviews

The following audit forms part of a series of grant payment reviews to be undertaken within the Council during the current financial year. Issues arising from individual reviews will be reported to relevant management but no audit opinion will be allocated. Towards the end of the financial year the outcome of all the grant payment reviews will be collated into an overview report, providing an overall audit opinion

RURAL LIAISON GRANT *(final report issued 12.9.13)*

The Rural Liaison Grant (RLG) is provided from the council to the 11 parish councils within Medway. The RLG is £75,000 per annum allocated from the General Fund, and is overseen by the council's finance division. The initial allocation to the parishes, totalling £40,000, is allocated proportionately based on the population in the area. The parish councils can then make claims to the council for additional funding from the remaining £35,000.

Our audit found there to be robust processes in place to manage the RLG:

- The allocation from the £40,000 is retained by the council and only provided to the parish councils on receipt of evidence that expenditure has been incurred.
- Parish councils have been provided guidance as to allowable expenditure, and how to make claims from the grant fund.
- Whilst parish councils are permitted to carry over their allocation, large surpluses carried forward are challenged by the council.
- Parish councils can only claim funding from the additional £35,000 grant if they do not have surplus from their original allocation.
- The Chief Finance Officer considers claims for allocation from the additional £35,000 grant funding, and in 2012/13 only £5,000 was approved. The remaining funds were returned to the general fund at year-end.
- There is a rural liaison committee and the senior accountant responsible for oversight of the grant funding reports to this committee.

The RLG is a discretionary funding arrangement, and we were advised that it was set up to support the rural areas by providing additional funding for rural communities (over and above their parish precepts) as residents living in these areas find it harder to access services based in the towns. We were unable to find any documented set of objectives for the grant or any review of the arrangement. No specific recommendation has been made in relation to this point but the need to review all discretionary grant funding in light of the increasing pressures on the council's limited resources will be considered in the overarching audit report regarding grant payments to be prepared by year-end.

CONCLUSION

We are able to confirm that the authority's finance team has robust controls in place for grant payments for the Rural Liaison Grant and that we did not identify any significant issues. Management have agreed one action relating to grant payment administration.

FOLLOW UPS

DEBTORS INCOME *(final report issued 12.9.13)*

An audit of the Debtors Income system was carried out in March 2012 and a final report was issued in September 2012 with the overall opinion on management controls over the system being **insufficient.**

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 those findings reviewing the overall audit opinion.

Management were aware of deficiencies prior to the 2011/12 audit and were trialling new schemes and working on new policies at the time of the original audit. Management has since been working to address the two high and three medium priority recommendations reported in 2011/12.

This report summarises the results of further audit work carried out to confirm whether the agreed actions relating to the recovery of debt and lack of authorisation for writing-off unrecoverable debt (including review of write-backs) have been implemented.

CONCLUSION AND AUDIT OPINION

On the basis of the progress made in addressing the recommendations from 2011/12 we have reviewed the audit opinion and are satisfied that we can raise the overall opinion from **insufficient** to **satisfactory**.

Risk	Original opinion	Revised opinion	Progress
Details of debt held on the sales ledger may be inaccurate	Insufficient	Satisfactory	▲
Debt recovery processes may be ineffective	Insufficient	Satisfactory	▲
Ineffective processes in place for identifying and dealing with unrecoverable debt	Uncontrolled	Satisfactory	▲

Management have strengthened controls over setting up new debtors and raising invoices/ credit notes by ensuring requests have been authorised appropriately. We are aware that management are continuing to work on reducing aged debt, though total ‘non current’ debt (ie 31 days or more old) at the end of 2012/13 had increased by 12.3% over the corresponding figure for the previous year and outstanding balances over 365 days old had increased by 41.4%; however, significant reductions are evident in debts between 91-180 and 211-240 days old. Action has also been taken to ensure that write-off and write-back of debt up to £25,000 deemed irrecoverable is authorised by assistant directors and finance managers, though it should be noted that this arrangement, whilst considered reasonable and proportionate, fails to comply with the requirement in the Constitution for approval by director and, if over £5,000, the Chief Finance Officer.

Three additional recommendations were made and accepted by management:

- Producing reports of debtor records created/amended and credit notes input by staff with system administrator access, to be monitored by an independent officer;
- Formalising and documenting the delegation of authority permitting Finance Manager and Assistant Director/Chief Finance Officer approval for write off/write back of irrecoverable debts;
- Reporting the value of irrecoverable debt subject to write-off or write-back action to Members on an annual basis.

Annex C

DEFINITIONS OF AUDIT RECOMMENDATION AND OPINIONS

DEFINITION OF AUDIT RECOMMENDATION LEVELS	
Significant (High)	The finding highlights a weakness in the control arrangements that expose the Council to significant risk (determined taking into account both the likelihood and the impact of the risk).
Material (Medium)	The finding identifies a weakness in the control arrangements that expose the Council to a material, but not significant, risk (determined taking into account both the likelihood and the impact of the risk).
Point of Practice	Where the finding highlights an opportunity to enhance the control arrangements but the level of risk in not doing so is minimal, the matter will be shared with management, but the detail will not be reflected in the audit report.
DEFINITIONS OF AUDIT OPINIONS	
Strong (1)	Risk Based: Appropriate controls are in place and working effectively, maximising the likelihood of achieving service objectives and minimising the Council's risk exposure. Compliance: Fully compliant, with an appropriate system in place for ensuring ongoing compliance with all requirements.
Sufficient (2)	Risk Based: Control arrangements ensure that all critical risks are appropriately mitigated, but further action is required to minimise the Council's risk exposure. Compliance: Compliant with all significant requirements, with an appropriate system in place for monitoring compliance. Very minor areas of non-compliance.
Needs Strengthening (3)	Risk Based: There are one or more failings in the control process that leave the Council exposed to an unacceptable level of risk. Compliance: Individual cases of non-compliance with significant requirements and/or systematic failure to ensure compliance with all requirements.
Weak (4)	Risk Based: There are widespread or major failings in the control environment that leave the Council exposed to significant likelihood of critical risk. Urgent remedial action is required. Compliance: Non-compliant, poor arrangements in place to ensure compliance. Urgent remedial action is required.