

AUDIT COMMITTEE

26 NOVEMBER 2013

INTERNAL AUDIT PROGRAMME

Report from: Internal Audit

Author: Alison Russell, Audit Services Manager

Summary

To advise Members of progress in delivering the approved 2013/14 work programme, and present outcomes 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 Members approved the internal audit 2013/14 work programme on 21 March 2013 for year ending 31 March 2014. The programme is derived using a risk-based approach to ensure that the assurance provided by Internal Audit through this work is of added value to the council.

2.2 The programme includes audits of key financial systems and annual governance reviews, which are considered key activities and are given priority when resources are allocated. The aim is that all of the key assurance audits will be completed prior to the approval of the annual governance statement. The approved programme also includes audits of other financial systems, risk assessed audits, probity reviews, follow-ups, and the completion of any prior year audits outstanding as at May 2013.

2.3 Progress to date on the 2013/14 plan is set out at **Annex A**.

2.4 The Audit Programme is reviewed in year to reflect any changes of priority in year. Any proposed changes are presented to the Audit Committee for approval. Annex A provides details of three additional audits to the plan, and also includes the proposal to defer the audit of capital projects to 2014/15.

2.5 The intention is to utilise additional approved funding on delivering an escalated programme of school probity audits, beginning in January 2014.

2.6 This report also contains the outputs from each audit completed since the last update to the committee. These are set out in **Annex B**. Each audit and follow up 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.

- 2.7 The definitions of the recommendation and audit opinion options, as endorsed by Audit Committee in July 2013, are shown at **Annex C**.
- 2.8 An overall audit opinion is provided for each full audit. Audit opinions are not provided in the outputs of individual probity and site reviews, but these outputs form the basis of full audit reports that will contain an opinion on the council-wide procedures in place.
- 2.9 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.
- 2.10 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.

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 progress on the 2013/14 audit programme, including the three additional audits and the proposed deferment of one audit, and 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

Audit Plan 2013/14 – Progress Report

| | Opinion | All | C&A | RCC | Health | BSD |
|--|----------|--------------|--------------|--------------|--------|--------------|
| Activity ↓ | | | | | | |
| Key Financial Systems | | | | | | |
| Council Tax | | | | | | Q4 |
| Local Business Rates (1) (Review of introduction) | 2 | | | | | 11/13 |
| Local Business Rates (2) | | | | | | Q4 |
| Housing Benefit | | | | | | Q4 |
| Housing Rents | | | | | | Q4 |
| Other Financial Systems | | | | | | |
| Procurement (and category management c/f from 12/13) | | F | | | | |
| Social Care Payments | | | P | | | P |
| Payroll | | | | | | F |
| PCIS Compliance | | | | | | P |
| Local Income Management | | Q4 | | | | |
| <i>Visitor Information Centre</i> | ✓ | | | 07/13 | | |
| <i>The Villager (minibus hire)</i> | ✓ | | | 09/13 | | |
| <i>Trading Standards</i> | ✓ | | | 09/13 | | |
| <i>Duke of Edinburgh Awards</i> | ✓ | | 09/13 | | | |
| Handitills | ✓ | | | | | 11/13 |
| <i>Lifeline</i> | | | | | | F |
| Upnor Castle | ✓ | | | 11/13 | | 11/13 |
| AASSA | ✓ | | 11/13 | | | 11/13 |
| School Financial Management | | | Q4 | | | Q4 |
| Risk Assessed Audits | | | | | | |
| Local Welfare Provision | | | F | | | |
| Better for Less | | P | | | | |
| Health - Information Governance | | | | | F | |
| Foster Care (DBS and DP) | | | DR | | | |
| Innovation Centre Medway | 2 | 09/13 | | | | |
| Grant Payments | | Q4 | | | | |
| <i>Rural Liaison Grant</i> | ✓ | | | | | 09/13 |
| Adaptations | | | F | | | |
| Succes | ✓ | | | 11/13 | | |
| Data Quality – Equality and Diversity | | F | | | | |
| Asset Management – Divestments | | F | | | | |
| DBS – central processes | 2 | 11/13 | | | | |
| Maintenance Contracts highways | | | | F | | |

| Audit Plan 2013/14 – Progress Report | | | | | | | ANNEX A |
|---|----------|-----|--------------|--------------|--------|--------------|---------|
| Activity ↓ | Opinion | All | C&A | RCC | Health | BSD | |
| Medway Norse (Partnership audit c/f from 2012/13) | | P | | | | | |
| Governance Audits | | | | | | | |
| Risk Management | | Q4 | | | | | |
| Corporate Governance | | Q4 | | | | | |
| Carbon Reduction (c/f from 12/13) | ✓ | | | | | 09/13 | |
| School Probity Audits | | | | | | | |
| St Margaret's Infants | ✓ | | 09/13 | | | | |
| Park Wood Infants | ✓ | | 09/13 | | | | |
| St Nicholas CEVC Infant | ✓ | | 09/13 | | | | |
| Hilltop Primary | ✓ | | 09/13 | | | | |
| Balfour Junior | ✓ | | 11/13 | | | | |
| Bligh Federation | ✓ | | 11/13 | | | | |
| Byron Primary | | | F | | | | |
| Park Wood Junior | | | F | | | | |
| St Thomas Moore RC Primary | | | F | | | | |
| Luton Infant | | | F | | | | |
| Warren Wood Primary | | | P | | | | |
| Follow Ups | | | | | | | |
| Debtors | 2 | | | | | 09/13 | |
| IWorld Access | | | | | | F | |
| Waste Management | 2 | | | 11/13 | | | |
| HR data security | 2 | | | | | 11/13 | |
| Additional/Replacement Audits | | | | | | | |
| Trading Standards/Com Env Hlth | | | | F | | | |
| National Fraud Initiative | 2 | | | | | 09/13 | |
| Troubled Families | | | P | | | | |
| DEFERRED AUDITS | | | | | | | |
| Capital Projects | | | | | | | |

KEY

AC = month & year reported to Audit Committee

DR = draft report issued

F = fieldwork in progress

P = audit in planning stage

Bold = audits are reported to this Audit Committee

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

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

SUMMARY INFORMATION ON COMPLETED AUDITS**LOCAL BUSINESS RATES (*final report issued 1.11.13*)****MANAGEMENT SUMMARY**

Local Authorities are responsible for billing and collection of the Local Business Rates (LBR). The Valuation Office (VO) determines the rateable value (RV) for each non-domestic property and this is combined with a national multiplier (set by the government) to determine the annual bill. The multiplier for 2013/14 is £0.471. Organisations are entitled to relief on all or part of their rates if they meet certain criteria e.g. charity relief.

Prior to the 2013/14 financial year, Local Authority LBR receipts were transferred to Central Government, pooled centrally, and then redistributed according to formula assessed need. Under the terms of the Local Government Finance Act (2012), local authorities retain half their LBR receipts. The remaining half is still pooled centrally for redistribution.

Under the new arrangements, local authorities are incentivised to increase their local tax base and collection rates but bear risks associated with a reduction in receipts. Medway Council's retained LBR income is expected to be approximately £40m.

The objective of this audit is to provide assurance over the arrangements for identifying, mitigating and reporting the financial risks to the council as a result of the LBR arrangements. The review focused on:

- Appeals
- Significant in-year changes to RV or mandatory relief
- Reporting

The audit did not review the LBR income collection processes.

LBR has a significant role in balancing the council's budget in the current economic climate, and there is a significant level of potential volatility in the income Medway Council will receive. Appeals and in-year changes are the two most significant factors and as such management have sought to calculate potential impacts and report on these. It is for this reason that we are focusing on appeals and in-year changes.

Appeals:

The owner of a non-domestic property has the right to appeal to the VO against the RV in the hope that the LBR bill will be reduced. The VO rejects over half of the appeals and a small number of appeals result in the RV being increased. If there is a change in RV as a result of the appeal, the revised charge is backdated.

Local Authorities bear the cost of backdated LBR credits arising from successful appeals although the current advice (subject to regulatory confirmation) is that they are able to spread the effects over a five year period. Where the RV had been corrected by 31 March 2013, Medway Council is not responsible for the backdated

effects, but will have the 2013/14 effects. If the RV was adjusted on or after 1 April 2013, Medway Council will have backdated as well as ongoing effects.

When Medway Council's revenue budget for 2013/14 was calculated, there were 755 outstanding appeals with the VO (as at October 2012). These outstanding appeals mean a level of uncertainty in the council's potential income from LBR which then have to be subject to estimation. The Revenues and Benefits Manager (RBM):

- Estimated the likely change on RV for each appeal, based on his experience and the property type (applying the average across all properties to average out the effect of rejected appeals);
- Calculated the effect of this RV reduction to obtain a backdated cost of the appeal for the 2010/11, 2011/12, 2012/13 financial years and the ongoing cost for 2013/14, using the national multiplier for the appropriate year and the effective date for the appeal;
- Calculated the effect of this on the 2013/14 budget.

The RBM estimated that the total RV for Medway properties would be reduced by £4.5m. The backdated cost to the Authority for these appeals was estimated to be a total of £7.8m, and that this would have an impact of £3.1m in 2013/14. In making these estimates, the RBM acknowledged there were significant risks that changes in the appeals rejection rates, very large RV reductions, or a significant number of new appeals, could leave the Authority with a material shortfall against budgeted income.

By 30 June 2013, 356 of the original 755 appeals had been resolved by the VO. 286 of these were rejected and 70 resulted in an RV adjustment. In addition to the 399 unresolved appeals from the original list, 131 new appeals had been made, leaving 530 appeals outstanding at the time of the audit.

In order to provide assurance over the reasonableness of the estimates, Internal Audit reviewed the methodology used by the RBM and, having considered it reasonable, used it as the basis for testing the efficacy of the estimation process. We calculated the actual change in RV, and the actual reduced income, for the resolved appeals and found that the average reduction has been lower than the RBM's original estimates. The actual average RV adjustment per resolved appeal (-4%) was then used to estimate the effect on the RV for each unresolved appeal. We were also able to take account of appeals resolved prior to 31 March 2013, where the council was not liable for the backdated amount and the 131 confirmed new appeals lodged up to 30 June 2013. The potential effect of this on the Authority's income was calculated using the RBM's methodology.

The actual effects of the 356 resolved appeals was combined with the potential effects of the 530 unresolved appeals and compared to the RBM's original estimates. We estimate that

- the total RV for Medway properties would be reduced by £4.4m (cf £4.5m)
- this will cost the Authority a total of £6.4m in reduced income (cf £7.8m)
- this will have an impact of £2.9m (cf £3.1m) in 2013/14

We conclude that the assumptions the RBM used in estimating the impact of appeals on LBR income for 2013/14 were not unreasonable and given there is always an element of uncertainty over the outcome of the appeals (530 currently outstanding) we are satisfied that the budget figures provided by management are appropriately prudent.

Significant in-year changes to RV or mandatory relief:

As the council's budget is now directly affected, through the LBR, by the economic success of the area, there is an increased need for effective liaison between finance and other sections of the council. We are pleased to note that there is effective information sharing in place, but encourage continuing review of these arrangements to ensure a co-ordinated approach.

The Authority currently has 20 properties with an RV of £1m or more including the power stations on Grain, and loss of any of these businesses from Medway would have a very significant negative impact on the council's budgets.

The RBM receives a list of planning applications in order to gain early warning of new developments and he monitors changes to the larger non-domestic properties so that anything that might have a material impact on LBR income can be reported early.

When schools become academies, they become charitable trusts. As such, they become eligible for mandatory relief on their LBR. The RBM has estimated that the Authority could potentially lose approximately £0.5m in income should this happen. The RBM receives reports on future Academy conversions and is monitoring the effect of this. These have not been built into the budgets due to uncertainty of the timing of conversions, but are included in forecasts as and when conversion dates are set.

Reporting:

Members have received appropriate information on the budgetary implications of the changes to LBR funding through the Medium Term Financial Plan, capital and revenue budgets and a Cabinet report on Business Rate Reliefs. Material budgetary variances would be reported in quarterly monitoring reports, but there are currently no material variances. In addition, the Chief Finance Officer meets regularly with the Portfolio Holder for Finance and will ensure he is aware of all current issues.

CONCLUSION AND AUDIT OPINION

Our overall opinion is that the arrangements for identifying, mitigating and reporting the financial risks to the council as a result of the LBR arrangements are **Sufficient**. A definition of audit opinions is included in Appendix B to this report.

Management acknowledge the risks inherent in LBR, given the significant financial implications of the new LBR arrangements, the potential volatility in income, and the advice on the spread of costs over five years has yet to be documented in regulations. The situation is subject to monitoring by management and we are satisfied that mechanisms are in place to provide early warning of significant deviation from the current budgetary figures.

DISCLOSURE and BARRING SERVICE – CENTRAL PROCESSES *(final report issued 12.11.13)*

All local authorities are obliged to publish an annual governance statement covering their systems of risk management and internal control. To contribute towards this, Internal Audit carries out audits of various financial and operational systems to provide management with assurance that the controls being relied on to mitigate risks to achievement of the Council's objectives are in place and operating effectively.

The council has a responsibility to ensure that appropriate checks are made regarding relevant criminal history of applicants for specific posts, as part of a comprehensive vetting process.

Various departments within the council are involved in carrying out checks including HR, Children and Adults and Licensing.

BACKGROUND

The Criminal Records Bureau (CRB) and the Independent Safeguarding Authority (ISA) merged into the Disclosure and Barring Service (DBS) on 1 December 2012. DBS was established under the Protection of Freedoms Act 2012. CRB checks are now called DBS checks. Only those in sensitive posts or who have intensive contact with children or vulnerable people (regulated activity) need to be cleared and undergo criminal record checks. This has decreased the number of DBS checks the council needs to undertake in relation to employees whose roles do not qualify for a check under the new regulations (e.g. admin and audit staff who potentially handle information relating to children/vulnerable adults but are not in direct contact with them).

There are three types of check:

- the standard check (£26) is available for certain specified occupations, licences and entry into certain specified professions - it contains details of all spent and unspent convictions, cautions, reprimands and final warnings from the Police National Computer (PNC).
- the enhanced check (£44) is available for those carrying out certain activities or working in regulated activity with children or adults; applicants for gaming and lottery licences; and judicial appointments - it contains the same PNC information as the standard check but also includes a check of police records held locally.
- an enhanced check with barring lists (£44) is only available for those individuals who are in regulated activity and a small number of positions listed in Police Act regulations, for example, prospective adoptive parents - it contains the same PNC information and check of police records held locally as an enhanced check but in addition will check against the children's and/or adults barring lists.

In a related move, criminal record checks are no longer sent directly to employers but to the individual to allow them to challenge any concerns or suspected errors. This places the onus on the employer to ask to see the certificate once issued. Previously, a copy of the CRB certificate for staff was sent to the council's HR department, who then notified relevant managers should there be a positive

disclosure and followed-up that appropriate action involving the Assistant Director had been taken in relation to making a decision on whether the individual should be employed / continue in employment. Managers are now tasked with this role including identifying the various security features on certificates.

From 29 May 2013, the DBS began to filter off old and minor convictions and cautions, reprimands and warnings from certificates, following amendments to the *Exceptions Order 1975 (2013)* that certain spent convictions and cautions are 'protected' and are not subject to disclosure to employers, and cannot be taken into account. Job application forms need to reflect the filtering changes so that employers ask the right questions and employees give the right (legally accurate) answer.

From 17 June 2013, the Update Service came into effect. For an annual subscription fee of £13, applicants can have their DBS Certificate kept up-to-date and take it with them from role to role, within the same workforce, where the same type and level of check is required. This means that with their permission the employer can use their current DBS certificate to carry out a free, instant online check to see if any new information has come to light since its issue. However, it is the responsibility of the individual to remember to pay the annual subscription fee (DBS do not send out reminders), should they fail to do this, then a whole new check (costing £44) will need to be undertaken. The total cost for the first three years using the Update Service is £83 and £39 for every three years after that. There is no charge for volunteers using the Update Service. A decision will need to be made by the council on whether to recommend staff pay the annual subscription fee (with this refunded by the council) or stay with the three-yearly full renewal process.

As can be seen from the above, this is an audit of a system that has undergone much change in the past year and is still being developed with guidance from central government still subject to revisions.

The audit reviewed the council's policies, procedures, roles and responsibilities and training undertaken, to ensure that checking of eligible staff / non staff / contractors / volunteers is undertaken in accordance with DBS. It did not, however, include testing of compliance. A review of DBS compliance in relation to foster care is being undertaken this year, and general compliance across the council will be reviewed as a follow up to this audit, once the systems are finalised and have become embedded.

The council is also an umbrella organisation providing a DBS service to other local organisations. An admin charge of £14 is applied to each check. The council is not involved in the employment decision making process should there be positive disclosures.

This report provides an interim audit opinion of the progress to date and identifies emerging issues that should be addressed by management.

FINDINGS

Existing controls that remain relevant under the new arrangements include:

- individual in HR responsible for all DBS matters relating to staff;
- recruitment training for managers a requirement;
- previously Assistant Directors made decisions where any individual has a positive disclosure as to whether the individual is employed – now an additional control has been put in place and the Assistant Director,

Organisational Services has to approve all appointments where an individual has a criminal record;

- Ofsted have a responsibility for providing assurance that all checks have been completed for Medway school staff.

Steps taken to date regarding the new DBS arrangements:

- new DBS policy being drafted;
- guidance issued to relevant staff and procedures updated on Intranet;
- training provided to staff, managers and schools relating to new procedures.

Key findings and issues still to be addressed:

- there is lack of clarity as to whether the council DBS policy covers non-employees, leading to an inconsistent approach between DBS checks for employees and non-employees;
- management of DBS for non-employees does not follow council DBS policy - three service areas (Self Directed Support, Transport Procurement Unit and Licensing) do not follow council policy relating to AD approval of positive disclosures, accepting disclosures carried out by other councils (one department stated that any additional information supplied with the original check would not be seen) and also some inconsistency on periodic renewals;
- following the introduction of the update service in June 2013, no council-wide decision on using the service has been made, with some service areas e.g. foster care unaware of the pros and cons relating to this;
- the changes introduced in June mean that HR no longer receive a copy of disclosures issued, so are reliant on managers and recruiting officers advising them that individuals' disclosures have been seen and checked, however, as this was requested only recently there have been delays in receiving confirmation that renewal disclosures have been received by individuals and checked by managers – in addition, HR have not requested confirmation of who has checked the disclosure (this may not always be the manager) and when;
- guidance has not been issued on checking DBS certificate security features, this presents a risk that forgeries and the like to disclosures may not be recognised;
- following amendments to the Rehabilitation of Offenders Act 1974 (Exceptions) Order 1975 (as amended in 2013) that certain spent convictions and cautions are 'protected' and are not subject to disclosure to employers, questions asked verbally and on job application form relating to convictions, cautions, reprimands, warnings to reflect filtering changes have not been made / communicated to staff (the Employee Code of Conduct also needs to be updated to reflect the changes);
- there is no guidance to ensure that when staff (e.g. social workers) book taxi drivers and escorts to transport children/vulnerable adults to/from regulated activities they have the relevant (enhanced) DBS check, especially when using taxis/escorts from outside of Medway;
- the council does not ensure that companies/individuals where the council countersigns applications, in its capacity as an umbrella body, have their own policy relating to the handling of DBS certification information;
- cost analysis should be undertaken on the viability of providing the umbrella service, particularly in respect of ensuring that charges applied at least cover the costs incurred.

CONCLUSION AND AUDIT OPINION

The audit identified that the council's criminal records policy and procedures had not yet been updated to reflect the revised requirements of the Disclosure and Barring Service and various other recent developments. Although four significant risks have been identified, we are satisfied that all are currently being addressed. In particular a revised policy, incorporating improvements we recommended, is being presented to Employment Matters Committee for approval on 20 November 2013 (after which it will be published on the intranet) and revised procedures have now been produced and made available to managers. Our overall opinion on the effectiveness of the council's DBS process, based on the fact that this is a developing system and progress continues to be made, is that it is **Sufficient**.

Subsequent to the audit report being issued we were advised that the Employment Matters Committee agenda in November had been amended due to address Pay and Grading issues. As such the DBS policies will now be presented at the next Employment Matters Committee in January 2014. Management have confirmed that work around the DBS arrangements continues to be progressed.

We intend to carry out a follow-up to confirm the continued effectiveness of these measures early in 2014/15, along with testing of compliance with the council's revised procedures.

Four High priority finding:

| | |
|---------------------------------|--|
| Finding: | There is a lack of clarity as to whether the council DBS policy covers non-employees, leading to an inconsistent approach between DBS checks for employees and non-employees. |
| Risks: | Inconsistent approach |
| Management action taken: | The revised policy will be further amended to include links to directorate-specific procedures to be followed by service areas performing checks on non-employees prior to the policy's approval at the next Employee Matters Committee meeting on 20 November 2013. DBS leads for each directorate will be referred to in the policy and details added once they have been identified. |

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|---------------------------------|--|
| Finding: | Management of DBS for non-employees does not follow council DBS policy (e.g. positive returns on checks carried out on non-employees do not follow the same process as for employees). |
| Risks: | Inappropriate approval / refusal on positive disclosures Potential for adverse publicity should decision to engage someone with positive disclosure be challenged |
| Management action taken: | DBS lead to be identified in each directorate by end of December 2013 to enable a consistent approach to be taken over DBS applicability to non-employees. |

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|---------------------------------|--|
| Finding: | Unclear guidance on using the Update Service and security checking of DBS certificates provided to managers and recruiting officers. |
| Risks: | Inconsistent approach Forgeries may not be recognised Potential employment/ engagement of individuals presenting a risk to children or vulnerable adults |
| Management action taken: | The Employment Matters Committee will be consulted in November 2013 regarding the use of the update service, with the outcome to be included in the revised policy. Guidance on checking disclosure certificates has now been provided in the 'DBS Procedures' now available on the intranet. |

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|---------------------------------|--|
| Finding: | There is no guidance to ensure that when staff (e.g. social workers) book taxi drivers and escorts to transport children/vulnerable adults to/from regulated activities they have the relevant (enhanced) DBS check, especially when using taxis/escorts from outside of Medway. |
| Risks: | Children/vulnerable adults could be put at risk |
| Management action taken: | Issue to be discussed with the Children's Social Care Management Team by end of December 2013 and appropriate procedures put in place |

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.

BALFOUR JUNIOR SCHOOL (*final report issued 30.9.13*)

Balfour Junior is a community junior co-educational school catering for 480 pupils of 7-11 years of age. It has 16 open-plan teaching classrooms with attached activity areas, an ICT suite, a library, a music room, a sensory room and a hall with stage and gymnasium.

The current Headteacher joined the school in April 2011 and had identified concerns regarding the financial management arrangements in place at that time and began to introduce new control mechanisms. A new school business manager started in September 2012. The Headteacher and new School Business Manager have reviewed the procurement arrangements and their intention is to review the income and cash handling procedures next.

We reviewed the revised procurement processes and some historic procurement transactions. We also reviewed current income handling arrangements and governance issues. The audit did not include an examination of payroll processes.

FINDINGS

Governance

Our review confirmed that the school's current governance arrangements are appropriate and that all members and staff that may influence procurement decisions have declared their business interests. We were unable to locate declarations of interests for those involved in procurement pre 2011 and we did note from our transaction testing that two suppliers, relating to building maintenance and IT hardware, were associated with members of staff. Whilst we believe that the associations were generally known at the school, without declarations we are unable to provide assurance that these arrangements were appropriately considered and authorised.

Procurement

Current procurement arrangements and processes introduced by the Headteacher and School Business Manager are sound. We found that:

- Value for money is sought for major projects via a quote/tendering process and choice of options/contractor is approved at Governing Body Level.
- General procurement is managed by the school according to limits for quotes and tenders specified in the schools finance policy.
- Duties between ordering, receipting and payment are separated.
- Orders are authorised before being placed and are promptly entered on the schools financial management system.

Due to concerns raised by the Headteacher we agreed to extend the period covered by the review to cover 2 procurement arrangements in existence prior to 2011 where the suppliers were associated with staff members. One related to building maintenance and one to IT hardware purchases.

The lack of documentation regarding these arrangements meant it was impossible to investigate these fully, but we did identify potential value for money concerns as the school has incurred remedial and replacement costs since these arrangements ceased.

We are satisfied that these previous arrangements have ended, but given costs incurred to date there is a risk that further remedial maintenance work will be required in the future.

Income

We identified residential trips as the largest school-generated income source handled through the schools bank account. Income from 3 trips in 2012/13 generated income of £27,000.

We examined the income and expenditure for these 3 trips and were able to confirm that the trips were broadly self-financing and that income received was about that expected (based on pupil numbers and charges). However, there were significant gaps in the control process that leaves the school exposed to the risk of loss:

- There was no formal business case put forward for each trip;
- The Headteacher was not informed of pupil numbers or charges;
- No formal process for approving the use of hardship funds;
- Income was received and counted by one individual;
- Receipts were not issued;
- Records of income received per pupil was not retained beyond the end of each trip;
- Records of income due was not reconciled to income due or received;
- Income was not stored in a safe until it had been counted.

An action plan, which management have agreed, records 2 actions to strengthen current arrangements.

CONCLUSION

Following her appointment, the Headteacher was concerned about the financial arrangements at the school and has improved procurement and financial governance procedures. We are satisfied with these arrangements, in place since September 2012, and also pleased to note that further work is planned regarding income and cash handling.

The lack of appropriate procedures and documentation regarding historic procurement transactions makes it impossible for us to provide any assurance over these arrangements.

We have agreed with the Headteacher to continue to liaise regarding on-going improvements and possible further internal audit assurance.

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| BLIGH FEDERATION (<i>final report issued 12.11.13</i>) |
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The Bligh Federation was created on 2 April 2012 and consists of the infant school, with its linked children's centre, and junior school – up to the end of 2012/13 the schools operated with separate budgets and separate bank accounts. The Bligh Federation serves children aged between three months and 11 years, with 420 infant and junior pupils on the school roll and another 110 and 56 attending the nursery and day care respectively. The children's centre has approximately 1,360 children under five in its reach area and is open for 50 weeks a year, 11 hours a day from Monday to Friday, with some activities on Saturday.

Our review assessed the effectiveness of controls operating over the checking, handling and recording of income for both the infant school/children's centre and junior school and expenditure and budget management relating to the children's centre. The budgeted income for 2013/14 is £286,000, which is primarily from income generated through day and extended care. We did not review controls over expenditure (including payroll costs) and budget management for the schools section of the Federation.

We interviewed the staff responsible for the day-to-day arrangements for income in the Federation and expenditure relating to the children's centre, assessed the control arrangements in place, obtained local income, expenditure and budget monitoring records and undertook sample and observational testing in order to provide assurance on the application of the controls. The school has a separate voluntary fund and the children's centre has a Parents' Forum. We are not responsible for providing assurance over these funds and therefore these have been excluded from our review.

FINDINGS

Our review and testing of the financial control arrangements identified that appropriate systems were in place and generally operating effectively. However, a few aspects were considered to require improvement, primarily the recording/handling of income for both children's centre and extended school activities and procurement/ordering of goods for the children's centre. These included, for instance, some instances of miscoding of income between the children's centre and school, income received not being banked for 2-3 weeks, retention of money in the till exceeding limits in the insurance policy and purchase orders rarely being generated

on the financial management system when goods are purchased for the children's centre.

We noted that a timetable of children's centre activities, displayed in the reception area, included two activities with a charge shown (£10 for swimming lessons and £2 for 'toy box' sessions), but no associated income had been recorded in the Federation's financial records. We were assured that no actual charge is made and that the timetable should have clarified that these are voluntary contributions to the parents' forum.

CONCLUSION

We are able to confirm that the Federation has appropriate controls in place over income for children's centre and school/extended school activities and over expenditure and budget management relating to the children's centre, and that these are generally operating effectively. We did not identify any probity issues, and management has adopted the action plan to further strengthen the current control environment

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.

UPNOR CASTLE (*final report issued 18.9.13*)

Upnor Castle generated income of £52,134 in 2012/13, through general sales (gifts, souvenirs), admissions and wedding hire.

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. Income from wedding hire bookings is received at Gun Wharf via cheque and transferred to Cashiers. Income received at the castle is transferred weekly by secure collection.

We are able to confirm that Upnor Castle has robust controls in place for income collection and recording and that we did not identify any significant issues. We are also satisfied that management have adopted four actions relating to banking and stock for resale to further strengthen current arrangements.

ATTENDANCE ADVISORY SERVICE to SCHOOLS and ACADEMIES - AASSA (*final report issued 30.10.13*)

AASSA was selected for a review of local income handling arrangements, as total income received in 2012/13 was £145,966. AASSA works with schools/academies to improve/monitor attendance, including home visits, and generates income from these activities. Income is also generated through penalty notices issued on behalf of

schools to parents when attendance does not improve, and if penalty notices are not paid this can lead to prosecution where the council may be awarded costs.

The income total comprises of £24,632 from penalty notices, £3,521 from court costs and £117,813 academy income. In undertaking this audit we ascertained that very little income is handled locally. The largest proportion of income, relating to activities with schools and academies, is processed through sales ledger and was therefore not relevant to this audit. We also established that, apart from very isolated exceptions, income from penalty notices is sent directly to cashiers at Gun Wharf. Separately, Audit Services have been liaising with Legal Services regarding the mechanisms for disbursing court costs.

Our review therefore covered the penalty notices only and involved reviewing their records and income recorded on Integra.

Our review of the financial control arrangements confirmed that virtually all income goes directly to cashiers, so there is no cash handling involved, and we are satisfied that appropriate records of penalty notices issued and payments received are being maintained.

We are able to confirm that AASSA has robust controls in place for income collection and recording of penalty notices and that we did not identify any issues.

HANDITILLS (*final report issued 12.11.13*)

Handitills HT1 & HT2 located at Strood Contact Point and Riverside One collected income of £1.3m in 2012/13, for payments for Council Tax, Business Rates, Rents, Housing Benefits, Service Charges and Sundry Debtors. Additional income of £303,959 was collected from Parking Services using Handitill HT1 as an internal income transfer.

Our review covered the checking and handling of income, income retention and transportation of banking 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.

FINDINGS

Our review and testing of the financial control arrangements confirmed that, overall, there are appropriate processes in place for the management of income. Income for Handitills is received by cheque and cash and controls are in place to ensure all income due is received, recorded, retained and transported securely. We have however identified 8 proposed actions to strengthen the current arrangements.

During our fieldwork we found that the control arrangements at HT1 for dealing with the collection of the income by Contract Security Services (CSS) needed to be strengthened, as there was no record made of the CSS collection from the Handitill and no member of staff present at the time the Handitill was opened. We are pleased to note that management have since created a set of procedures around Handitill key security.

The use of HT1 for internal transfer of income from parking services weakens the controls in place and as such management have agreed to look into alternative means of transporting this income.

The arrangements for the cashiers to identify missing collections is not formalised, and therefore there is a risk of missed collections not being identified promptly. There is also an absence of control over unallocated income, arising from insufficiently marked envelopes or envelopes deposited with no details. The income is not banked until year-end and there is no centralised record of the cash held by the cashiers, or the reimbursements made.

Management are looking to undertake a broad review of the income management process, from payment to banking, and the Handitill procedures will be assessed as part of that broader review.

CONCLUSION

We are able to confirm that there are appropriate controls in place for Handitill income retention, transportation, collection and recording and that we identified some areas requiring improvement. We are also satisfied that management have adopted the action plan, containing 8 actions, for further strengthening the current financial arrangements.

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

SUCCES (*final report issued 6.11.13*)

FINDINGS

Medway Council is currently involved in approximately fifteen projects funded by the European Regional Development fund (ERDF). In 2012/13 this contributed approximately £1 million to Medway Council's revenue.

The Sustainable Uplifting Client Centred Employment Support (SUCCES) Project was one of these projects that ran from 1 February 2010 to 30 June 2013. Medway Council was the lead partner (LP) and there were four other EU project partners. The total partnership budget for this project is €2,699,182, and Medway Council's share was €1,096,735 over the project's lifetime. The project aimed to provide effective employment support and skills development for unemployed people living in deprived urban zones. As LP, Medway Council was responsible for disbursing funds to its EU partners and making contractual payments to local organisations within Medway.

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

- The project had clear objectives at the time the bid for funds was made, supporting the Authority's stated aim of "ensuring that people have the skills they need to take up job opportunities that are created";

- Partners were chosen carefully to ensure suitability for the project.
- Bids / agreements / contracts stipulated allowable expenditure and how performance would be monitored.
- Medway Council followed appropriate procurement rules in selecting contractors for delivery of the project locally.
- These local partners were issued Service Level/Partnership Agreements at each phase of the project defining the aims and objectives, specifications and requirements, including KPIs/targets that each partner was required to meet.
- Progress of the project is monitored through quarterly partnership meetings and remedial actions are taken to mitigate project delivery issues.
- Claims by EU partners and contractual payments to local partners are supported by evidence of both expenditure and outcomes. These reports are checked by the first level controller as well as by Medway Council prior to submission.
- Medway Council faces no currency risk from acting as LP as income is received in Euros and is then held in the Authority's Euro account until it is disbursed to EU partners (in euros). In the event of any claw back, this would be direct from the EU partners.

This project has received an award as an outstanding project from the European Commission and was in top five in the European Commission RegioStars award for good management delivery.

CONCLUSION

We are able to confirm that the Authority's SUCCES Project Team has robust controls in place for grant payments for the SUCCES Project Grant and that we did not identify any significant issues.

FOLLOW UPS

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| <h3>WASTE MANAGEMENT (<i>issued 17.10.13</i>)</h3> |
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The final report for the 2012/13 Internal Audit of the waste collection and disposal contracts was issued in March 2013. The audit opinion was that in all but one respect the contract management arrangements were satisfactory. However the key focus of the audit was risks relating to the monitoring of the contractor performance through agreed KPIs. The audit found that the KPIs did not provide the necessary mechanisms to monitor contractor performance effectively, and therefore the overall audit opinion was that the arrangements in place were **insufficient**.

The audit found that few of the stated KPIs specified in the contract related to on-going performance. A number of the KPIs for the collection contract related to "standing items" and a number of the disposal contract KPIs related to the contractor providing reports to the council. It was also found that the contract included KPIs that were no longer relevant, for instance those relating to wheelie bins, or were nullified when the same contractor was selected to provide both the collection and disposal service. We were pleased to note that management were using a suite of additional performance measures which were discussed at the regular performance meetings held with the contractor. However, given the value of the contracts (with a total approximate cost to the council of £264m based on current agreed periods) we

remained concerned that the council was at material risk of not achieving value for money. As part of the audit report we provided a list of KPIs used by other local authorities for consideration by management.

The contracts for waste collection and disposal contracts are in the process of being amended in order to reflect the new weekly recycling collection arrangements, and the opportunity has been taken by management to review the KPIs as part of this process.

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. It was agreed that internal audit would conduct a follow up review, and reconsider the overall audit opinion, in light of the revised KPIs.

FINDINGS

Internal audit attended an initial meeting between management and the contractor to discuss proposed amendments to the KPIs, and agreed that draft KPIs would be shared with internal audit prior to agreement. In September management provided a suite of proposed KPIs for inclusion in the amended contract, for internal audit review and input.

The suite of KPIs presented now provides a comprehensive mechanism for monitoring service delivery and the overall performance of the contractor. The KPIs are all measurable and specific.

For each KPI there is clarity over what level of performance will be deemed acceptable, and also a performance deduction regime for addressing under performance by the contractor.

As part of the review of the KPIs we provided feedback to management on the proposed KPIs, and a number of amendments were made to the KPIs to improve clarity. Unfortunately two issues raised have not resulted in amendments to the KPIs.

The first was that the performance deductions did not include arrangements for applying cumulative deductions if the contractor were to fail to meet KPIs over consecutive months. This matter was discussed with the Head of Waste Services who advised that whilst such arrangements would enhance the arrangements further, such arrangements were not in place in the original contract and it would be too significant a step change to include in the amended contract. Whilst we believe such arrangements would be appropriate we are content that there are other mitigations in place which limit the risk to the council of the contractor persistently failing to meet KPIs, such as the regular performance meetings held with the contractor, and the sanctions process built into the contract for rectification and default notices.

The second related to the fly tipping KPIs, and in particular the KPI for collection of syringes. The proposed KPI required collection in 90% of cases within one hour, and performance deductions based on percentage failure, applied on a monthly basis. We advised that the measures of compliance and performance deduction should also reflect the extent of collection delays given the significant risk this issue poses. We were advised that this could not be amended for inclusion in the contract as this was agreed through the KPI working group process. We find this response disappointing

given the agreed process for undertaking this review. We have advised management that whilst the measurement of length of delay will not form part of the contract it is something that the council should monitor, and any concerns regarding delays should be dealt with through their contract management meetings.

The KPIs have only just been agreed and are still awaiting formal inclusion within the contract, and therefore we have not been able to test the implementation of the KPIs. The overall assurance provided is therefore based on the appropriateness of the KPIs rather than their application.

CONCLUSION AND AUDIT OPINION

The revised KPIs and performance deduction regime provide an appropriate mechanism for monitoring performance of the contractor, and dealing with instances where the contractor fails to achieve the agreed targets. This suite of measures, alongside the regular performance meetings with the contractor and the sanctions built into the contract provide a robust structure for monitoring delivery of the contracts. On this basis we have revised the overall audit opinion to **satisfactory**.

HR DATA SECURITY (*issued 12.11.13*)

The 2012/13 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.

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 was '**satisfactory**'.

The audit process is not complete until a follow-up is performed in order to confirm that improvements made to weaknesses identified in the original report have been sustained and those not completed at the final report stage have now been implemented.

FINDINGS

This report summarises the results of further audit work carried out to confirm that high and medium priority actions have been completed and improvements have been sustained. The details of the actions taken and sustained by management were reported in an updated management action plan.

CONCLUSION AND AUDIT OPINION

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

DEFINITIONS OF AUDIT RECOMMENDATION AND OPINIONS

| DEFINITION OF AUDIT RECOMMENDATION LEVELS | |
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| 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) | <u>Risk Based:</u> Appropriate controls are in place and working effectively, maximising the likelihood of achieving service objectives and minimising the Council's risk exposure. <u>Compliance:</u> Fully compliant, with an appropriate system in place for ensuring ongoing compliance with all requirements. |
| Sufficient (2) | <u>Risk Based:</u> Control arrangements ensure that all critical risks are appropriately mitigated, but further action is required to minimise the Council's risk exposure. <u>Compliance:</u> Compliant with all significant requirements, with an appropriate system in place for monitoring compliance. Very minor areas of non-compliance. |
| Needs Strengthening (3) | <u>Risk Based:</u> There are one or more failings in the control process that leave the Council exposed to an unacceptable level of risk. <u>Compliance:</u> Individual cases of non-compliance with significant requirements and/or systematic failure to ensure compliance with all requirements. |
| Weak (4) | <u>Risk Based:</u> 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. <u>Compliance:</u> Non-compliant, poor arrangements in place to ensure compliance. Urgent remedial action is required. |