

Herefordshire Council

Audit Assurance Report 2006/07

1. Introduction

1.1 The CIPFA Code of Practice for Internal Audit In Local Government (2006) requires the Head of Internal Audit to formally submit an annual report to members. In line with good practice this Assurance Report:

- includes an opinion on the overall adequacy and effectiveness of the organisation's internal control environment.
- discloses any qualifications to that opinion, together with the reasons for the qualification.
- presents a summary of the audit work undertaken to formulate the opinion.
- draws attention to any issues the Audit Services Manager judges particularly relevant to the preparation of the Statement on Internal Control.
- summarises the performance of the Internal Audit function.
- comments on the compliance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice.

1.2 In compliance with the Code of Practice, the Council now has an Audit and Corporate Governance Committee with terms of reference:

"To provide:

- *Independent assurance of the adequacy of the Council's risk management framework and the associated control environment.*
- *Independent scrutiny of the Council's financial and non- financial performance to the extent it affects the Council's exposure to risk and weakens the control environment; and*
- *To oversee the financial reporting process".*

The Audit and Corporate Governance Committee also has a duty to review and approve the Statement on Internal Control.

1.3 Under the Accounts and Audit Regulations the Council has a duty to ensure that the its financial management is adequate and effective, there is a sound system of internal control and robust risk management arrangements are in place.

1.4 Herefordshire Council also has an obligation to include in its Statement of Accounts a statement on the system of internal control. The statement sets out the framework within which internal control is managed and reviewed and the main components of the system, including arrangements for internal audit. This assurance report is part of the framework. The Statement on Internal Control highlights significant areas for improvement and the actions undertaken to rectify them. A separate report on the Council's Statement on

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Internal Control will be made to the Audit and Corporate Governance Committee on 29th June 2007.

2. Audit Approach

- 2.1 Internal Audit is the independent appraisal function established by management to review the internal control system as a service to the Council. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources.
- 2.2 Audit Services acts as an aid to management and produces reports as a result of each of the reviews undertaken. It works in partnership with management to find solutions to any issues identified and seeks its agreement to any recommendations for improvement. Recommendations are developed with managers to produce action plans.
- 2.3 Audit Services is generally well received and helps management to achieve its objectives within a culture of strong stewardship.
- 2.4 The Audit Service has functional links with Members, Corporate Management Board, Schools, Heads of Service and colleagues across the Council. Audit Services would like to take this opportunity to thank all our clients for their help and co-operation during audit visits.

3. Background

- 3.1 The Annual Audit Plan is based upon risk assessments, utilising the Council's Risk Management Framework.
- 3.2 To ensure that the Council's priorities are considered, the Annual Audit is developed in consultation with Corporate Management Board. The Audit and Corporate Governance Committee approved the 2006-07 Audit Plan on 7th April 2006.
- 3.3 Audit Services' terms of reference has been formally agreed by the Audit and Corporate Governance Committee in the form of an Audit Charter, which outlines the independence of Audit Services and its reporting protocols.
- 3.4 The Audit Commission has completed its review of Audit Services, which involved comparing audit activity with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Internal Audit. The review has reaffirmed its ability to place reliance on the work of Audit Services.
- 3.5 The actual cost for Internal Audit Services amounted to £430,358 compared to a budget of £455,418.

4. Action Taken On 2005/06 Key Issues

- 4.1 The Audit and Corporate Governance Committee considered the Annual Assurance Report for the year ending 31st March 2006 on 30th June 2006. There were five issues identified, the status of these issues are:

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- The Council did not have a Code of Corporate Governance in line with good practice.

A Code has been developed and as part of the consultation process was considered by the Audit and Corporate Governance Committee, it is currently with the Standards Committee. In view of the pending publication of new guidance, the Council's Monitoring Officer has taken the view that it would be prudent to await its publication and use it to fine-tune the Council's Code.

- Although Risk Management is embedded at Corporate and Directorate levels and the Council has well defined procedures for recording and reporting financial and non-financial risks, there was a need to embed Risk Management at Key Manager level to ensure a consistent approach across the Council.

Significant improvements have been made and this has been confirmed in the Audit Commission's Annual Audit and Inspection Letter. The Director of Resources is the lead officer for risk management. Cabinet approved the revised and simplified Risk Management Framework on 12th October 2006. The first phase of training for key managers has been completed. An appointment has been made to the key risk management post of Corporate Risk Manager who will help to build on improvement already made.

- 'Staying Safe' improvements within the Children and Young People Directorate raised as part of the Joint Area Review.

The 2006 annual inspection showed that there were no inadequate assessments with regards to 'Staying Safe'. Although some areas for improvement were identified it is pleasing to note that the Inspectors felt the contribution the Council's services make to improving outcomes in this area were good overall.

- There is the need to ensure that the Council's Performance Management Framework is robustly and consistently followed across the Council.

The Audit Commission is of the view that the Council is making steady progress in strengthening its performance management arrangements and in embedding a performance culture. They also felt that the new network of Improvement Managers were beginning to result in a more consistent corporate approach to managing performance.

- Two fundamental systems were given marginal opinions. This related to the newly implemented software for Council Tax and Housing Benefit, as controls were not fully embedded at the time of the Audit.

Although improvements have been made at the 2006-07 review the Housing Benefit system was again given a marginal audit opinion, this was mainly due to issues arising from restructuring and the loss of key staff.

5. Use Of Resources

- 5.1 It is pleasing to report that the Council's Use of Resources score for 2006 has remained at 3, however it should be borne in mind that to support scores of 3 and above the Audit Commission has to consider whether relevant

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arrangements are embedded, that is, they have been operating consistently with clear outputs and are having an impact.

- 5.2 Comparison of the theme score for 2006 and 2005 has been summarised in the table below.

Theme	Score 2006	Score 2005
Financial Reporting	3	3
Financial Management	3	3
Financial Standing	2	2
Internal Control	2	2
Value for Money	3	3
Overall score	3	3

- 5.3 The standard scales used in the assessment are:

- 1 Below minimum requirements- inadequate performance
- 2 Only at minimum requirements – adequate performance
- 3 Consistently above minimum requirements- performing well
- 4 Well above minimum requirements – performing strongly.

6. Statement on Internal Control

- 6.1 A separate report will be presented to the Audit and Corporate Governance Committee. However Audit Services' review showed that the Council's procedures and protocols compared favourably with the Chartered Institute of Public Finance and Accountancy (CIPFA) checklist and overall was found to be satisfactory. However three areas were identified for improvement.

7. Summary Audit Work

- 7.1 The work of the Audit and Corporate Governance Committee continues to be developed and provides effective leadership on audit and governance issues. During 2006-07 it met five times (includes twice as the Audit Committee).
- 7.2 The Audit Plan was approved by the Audit Committee on 7th April, 2006 and was based upon the known risks at the time.
- 7.3 Delivery of the approved Audit Plan has been affected by three elements:
- additional time verifying performance indicators;
 - introduction of the DfES Toolkit for Secondary schools; and
 - time spent on fundamental systems

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7.4 To meet new obligations in respect of the latter, the following audit reviews have been added to the 2006-07 plan:

- Wigmore High School;
- Bishop of Hereford Bluecoat;
- Minster College;
- St Mary's R.C. School;
- Whitecross High School;
- Fairfield High School; and
- Lady Hawkins High School.

7.5 Lower risk work has been removed from 2006-07 Audit Plan and slipped into following years:

- Library Administration – Establishment;
- Barrs Court – School;
- Brookfield – School;
- Aconbury Centre – School;
- Bodenham St. Michael's C.E – School;
- Bridstow C. E. Primary – School;
- Brilley Parochial Primary – School;
- Brockhampton Primary – School;
- Bromyard St. Peter's Primary – School;
- Capital Grants – System;
- Leominster and Wigmore Youth Service – Establishment;
- Environmental Management Auditing – GEM;
- Charging and Trading Arrangements – Ad hoc Report;
- Grants and Donations – System;
- Hereford Registers – Establishment;
- Modern Records – Establishment;
- Recycling Income – System;
- Cemeteries & Crematorium – Establishment;

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7.6 Work removed from the 2006-07 Audit Plan will not impact adversely on the level of work required to give an end of year opinion on the Council's system of Internal control.

Fundamental Systems

7.7 Fundamental systems are systems whose failure could cause major disruption or loss of financial control to the Council. The outcome is summarised in table 1 below.

Table 1 Summary Fundamental Audit Opinions	2006/7	2005/6	2004/5
Audit Opinion	Number	Number	Number
Good	4	3	1
Satisfactory	10	10	10
Marginal	3	2	1
Unsatisfactory	1	0	0
Unsound	0	0	0
TOTAL	18	15	12

7.8 Although the number of marginal or worse opinions have increased, it is however pleasing to note that the number receiving good opinions has increased to four.

7.9 The marginal opinions related to:

- **Education Transport** – there were a number of key strengths within the service area, however there was a need for reconciliation of income to the Cedar System. Improvements were required in relation to its CRB procedures.
- **Housing Benefit** – although some good practices was evidenced, such as the reduction in the previous backlog of benefit claims and the minimal errors reported in claim processing tests, the reconciliation of Council Tax and Cedar systems were not up to date at the commencement of the audit, this improved by the completion of the audit. It should be noted that this system was given a marginal opinion in 2005-06, so it is disappointing to see that although some improvements have been made the overall opinion has not improved.
- **Salaries (Children & Young People)** – controls over the payment of salaries required improvement in particular the improvement in the input audit trail, with adequate authorisation and supporting documentation obtained for all payroll transactions. The findings from this audit do not differ greatly from those detailed at previous audit reviews and similar recommendations have been raised again.

7.10 The unsatisfactory opinion related to:

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- **ICT Financial Management System** – the ICT Finance Team was continually improving the process. Procedure documents were in place. However the audit review identified three key areas for improvement in relation to setting up budgets on to the Cedar System, improved controls over the payment of invoices, and the introduction of proper reconciliation protocols to the Cedar system. Following the review of the audit file by the Audit Commission, they are of the view that issues identified by Audit services could have an impact when carrying out their audit of the Council's final accounts. Under the circumstances they have requested that Audit Services carry out additional work on their behalf as part of the Audit Services follow-up work.

Non-Fundamental Systems

- 7.11 In this area there has been an improvement when compared to last year as there was one unsatisfactory system compared to three last year. As previously reported the Markets Fees and Charges system was given an unsatisfactory audit opinion due to fundamental system weakness, particularly over receipt books and supervisory checks to ensure that all income receivable is received.

Corporate Governance arrangements (including Anti Fraud arrangements)

- 7.12 The Council has key corporate governance documents and table 2 highlights their availability

Table 2 Schedule of Key Corporate Governance Arrangements Documents				
Policy/Document	Availability			
	Public	Partners	Staff	Members
Standing Orders	✓	✓	✓	✓
Financial Standing Orders and Regulations	✓	✓	✓	✓
Scheme Of Delegations	✓	✓	✓	✓
Whistle-Blowing Policy	✓	✓	✓	✓
Anti-fraud and Corruption Policy	✓	✓	✓	✓
Complaints Procedure	✓	✓	✓	✓
Code of Conduct for Employee	✓	✓	✓	✓
Standing Orders for the Regulation of Contracts	✓	✓	✓	✓
Corporate Plan	✓	✓	✓	✓
Operating Plan	✓	✓	✓	✓

- 7.13 The Council now has in place a partnership checklist, which includes risk identification. Heads of Service are obliged to complete this for major partnerships.

- 7.14 The Council has established a Standards Committee and has adopted a Code of Conduct for members incorporating the mandatory requirements of the model code. In addition, members have signed a formal declaration accepting the terms of the Code. The Head of Legal and Democratic Services has completed training for members.

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- 7.15 Directors and Heads of Service have given written assurance through a signed statement as to the operation of internal control and risk management within their Directorate/Service. In addition, all officers at Head of Service level and above have made individual declarations with regards to gifts and hospitality.
- 7.16 During the year, the Audit and Corporate Governance Committee (previously the Audit Committee) met five times. Good progress continues to be made with regards to the Committee's overall governance role, This is evidenced by the favourable words from the Audit Commission in their last Annual Audit and Inspection Letter.
- 7.17 A number of special investigations have been undertaken which were not related to any fundamental system. A report will be submitted to the Corporate Management Board on lessons learnt, which will be communicated to Heads of Service in due course. With regards to last years lessons learnt report feedback is still outstanding from a number of Heads of Service, this will be highlighted in this years report to Corporate Management Board. Where action has not been taken by Heads of Service this will be reported to the next Audit and Corporate Governance Committee.
- 7.18 The Council is taking part in the latest National Fraud Initiative (NFI) data matching exercise. At the present time, work is at the identification of cases for further investigation stage.

Performance Management

- 7.19 Audit Services completed its review of the Council's Performance Management Framework. It was found that the framework was better integrated within the Council, Individual Service Plans had improved in quality and action plans were more consistent since the last Audit. Nevertheless it was felt that that Service Plans were too long and required improved referencing. The Plans for 2007-08 have been made shorter and improved referencing was a key requirement.
- 7.20 Monitoring and reporting was much better than last year, with the regular Integrated Performance Reports to Cabinet being comprehensive.
- 7.21 Regarding Staff Reviews and Development (SRD) generally officers took their responsibility seriously and made an effort, however there seemed to be a misunderstanding as to its role. Although objectives were set the quality was the main issue. New guidance has been issued and it is hoped that this will help over come the issues identified.

Risk Management

- 7.22 Under the Accounts and Audit Regulations, the Council has an obligation to have sound risk management arrangements. This requirement is also a feature of the Use of Resources. Cabinet approved a revised Risk Management Framework in October 2006.
- 7.23 The Council's Performance Management is linked to risk management, as there is a requirement for all service plans to identify risk and the planned action to mitigate the risks identified.

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- 7.24 Cabinet and the Corporate Management Board review corporate risks as part of the regular Integrated Performance reports. The final report to Cabinet on 7th June, 2007 for 2006/07 highlighted the following high corporate risks after risk control measures have been taken into account.
- Corporate spending pressures outweigh the level of resources available to meet them. Particular pressures prevalent in Adult Social care;
 - Herefordshire Connects Programme does not go through robust investment appraisal and subsequent savings not being realised leading to service cuts;
 - Successful implementation of the Accommodation Strategy; and
 - Herefordshire Connects: Management capacity and capabilities not sufficiently developed to plan in advance, and deliver, the service changes required for realisation of efficiency savings.
- 7.25 Directorate Management Teams (DMTs) are required to review Risk Registers on a monthly basis. Not all DMT reviews were consistently documented.
- 7.26 The Council now has a Corporate Risk Manager who has the role of helping to embed risk management across the Council in a consistent way.
- 7.27 Risk management training has been completed for key managers with further training being planned as part of the embedding process.
- 7.28 The Audit Commission's latest Annual Audit and Inspection letter also confirms the progress being made with regards to risk management.

ICT Protocols and Controls

- 7.29 Although there were a number of marginal opinions in addition to an unsatisfactory opinion, the key reviews of Firewall Security, Back-Ups and Recovery were found to be satisfactory. The unsatisfactory opinion related to the CLIX system as it did not meet functional or security needs, nor did it fulfil central government requirements. This system will however, be replaced in the summer of 2008 as part of the Herefordshire Connects Programme.

Establishment Audits

- 7.30 Improvements continue to be made in this area, however, the main theme for improvements was around overall financial management. Work in relation to the new DfES toolkit will help improve this area.

Verification and Probity

- 7.31 Work within this area covered the verification and the successful signing off of two claim forms in relation to the Schools Sport Co-ordinator Programme. A review of the Waste Management Contract payment arrangements was completed and a recommendation made regarding variations. Reviews of contract monitoring within three directorates was undertaken and a cross

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Council review of delegation arrangements under Financial Regulations was completed.

- 7.32 Following verification work in relation to the Equality Standard for Local Government, it is pleasing to note that the Council has achieved Level 2 and is making progress towards Level 3 of the standard.

Audit Opinions

- 7.33 It is normal practice for all audits, except for recommendations follow-ups, to be given an audit opinion (Appendix 1 refers). All audits rated as unsatisfactory or worse and any fundamental or major systems found to be marginal or worse must be brought to the attention of the Audit and Corporate Governance Committee. Other than those previously mentioned there were no other audit reviews that met the above criteria.

Critical '1' Recommendations

- 7.34 Under current reporting protocols the Audit Services Manager has to bring to the attention of the Audit and Corporate Governance Committee 'Critical 1' recommendations. These are recommendations where non-compliance will be a high risk to the Council and where action is required urgently or within an agreed timescale.
- 7.35 Nine critical 1 recommendations were made during the year Three relate to CRB procedures and one to inventory records. The Audit Services Manager, the Legal Practice Manager and the Human Resources Manager will be developing guidance with regards to CRB procedures. In relation to inventory records, the Head of Financial Services has developed Accounting Guidelines, which are in the process of being finalised and sent out to Key Managers and Headteachers. Three related to the fundamental system ICT FMS and Procurement and cover the need for improved controls over payments, better reconciliation to Cedar, and budgets to be set.
- 7.36 The Audit Services Manager has met the Director of Corporate and Customer Services and the Head of ICT and Customer Services and agreed a way forward to meet the recommendations. The Head of ICT has developed an action plan in response to the audit recommendations. It should be noted that a much higher level of controls would have been required if this system was a corporate system. Audit follow up work is in progress.
- 7.37 Two related to improved cash control arrangements at a Council establishment where there was a need to ensure that a receipt was received when cash was banked and checks made to ensure that receipts for income banked were matched to the Cedar system.

Results of Recommendation Follow-Up

- 7.38 Recommendation follow up is featured in the Audit Plan for the year 2006/07. The outcome of follow-up work is summarised in Table 3 and detailed in Appendix 2.

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Table 3 Summary of Follow up Outcomes				
Status	2006/07		2005/06	
	Number	Percentage	Number	Percentage
Fully/Substantially Implemented	127	66	165	67
Partly Implemented	17	9	34	14
Not Implemented	49	25	47	19
Total	193	100	246	100

Other Corporate Issues

- 7.39 During the year the Council has under gone a number of external inspections, the findings have been summarised within the Statement on Internal Control. The outcomes have been favourable and not so favourable. Action is being taken by the Council to address areas identified for improvement.
- 7.40 The Herefordshire Connects Programme is progressing well and there is a Risk Register in place. The Project is being managed using Prince 2 Project Management Methodology, with the core members of the Project Board being the Chief Executive, the Director of Corporate and Customer Services, the Director of Resources and the Deloitte lead partner. Cabinet is kept informed of progress.
- 7.41 Arrangements in relation to the Public Service Trust are moving forward at a pace. There are good governance arrangements in place with the Council's Monitoring Officer and Audit Services Manager being members of the Integrated Governance Group, which meets regularly. Risk Registers are in place and the project is entered on the Council's Corporate Risk Register.

Compliance with the CIPFA Code/Audit Performance

- 7.42 The Audit Commission has completed its review of Audit Services against the new CIPFA Internal Audit Code of Practice. Some issues around quality control in relation to fundamental systems and statements of auditor independence have been identified. It has also been suggested that Audit Services informs the Audit and Corporate Governance Committee of the names of reports and the actions taken on the recommendations as part of follow up reporting.
- 7.41 Table 4 shows audit performance on local performance indicators

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Table 4 Local Performance Indicators	2005/06		2006/07	
	Target	Actual	Target	Actual
The half year assurance report is delivered to members*	October 0 5	February 06	November 06	December 06
The end of year assurance report is delivered to members	June 05	Sept 05	June 06	June 06
90% of service managers are satisfied with the Audit Service	90%	95%	90%	93.4%
100% of SRDs are completed by 31st May	100%	100%	100%	100%
Management accepts 95% of level 1 & 2 recommendations	95%	96%	96%	97%
The Audit Plan is agreed by the start of the new financial year	April 05	April 05	April 06	April 06
Ensure that the Council's Statement of Internal Control for previous financial year is published	July 05	July 05	June 06	June 06

8. Audit Benchmarking

- 8.1 Audit Services has taken part in the 2007 CIPFA Benchmarking Club exercise, the findings will not be known until later in the year.

9. Audit Opinion

- 9.1 I am of the opinion that the Council's overall level of internal control is satisfactory, however, action needs to be taken on the three areas identified in the Councils Statement on Internal Control.

**R. A. FORD
AUDIT SERVICES MANAGER
JUNE 2007**