

NORTH YORKSHIRE COUNTY COUNCIL

AUDIT COMMITTEE

8 MARCH 2012

INTERNAL AUDIT WORK ON CONTRACT ARRANGEMENTS

Report of the Head of Internal Audit

1.0 PURPOSE OF THE REPORT

- 1.1 To inform Members of the internal audit work performed during the year ended 31 January 2012 on contract arrangements and related matters and to give an opinion on the systems of internal control in respect of this area.

2.0 BACKGROUND

- 2.1 The Audit Committee is required to assess the quality and effectiveness of the corporate governance arrangements operating within the County Council. In relation to contract audit, the Committee receives assurance through the work of the Internal Audit Service (as provided by Veritau Ltd).
- 2.2 This report details the contract audit work undertaken by Veritau and provides a summary of the audit reports issued since the last report was presented to this Committee in March 2011. It should be noted that not all reports detailed in **Appendix 1** necessarily relate to a single directorate but may apply to a number of directorates depending on the area under review. Because this report addresses a functional theme rather than the activity of one directorate, there is no corresponding Statement of Assurance (SoA) or Directorate Risk Register (DRR). However, the majority of contract audit work falls under the responsibility of the Business and Environmental Services Directorate and the Finance and Central Services Directorate. The SoA and DRR for BES was presented to this Committee at its meeting in December 2011. The SoA and DRR for FCS are presented in a separate report on this agenda.

3.0 WORK DONE DURING THE YEAR ENDED 31 JANUARY 2012

- 3.1 A summary of the **internal audit reports** issued in the year since the last report on Contract Arrangements, to the Audit Committee in March 2011, is attached at **Appendix 1**. Specific attention is drawn to any Priority 1 agreed actions that management have chosen not to implement.
- 3.2 Veritau officers have also been involved in a number of other areas related to contract audit. These have included:

- providing advice and guidance to directorates and schools on ad hoc contract queries and on matters of compliance with the County Council's Contract and LMS Procedure Rules
- attending meetings of the Corporate Procurement Group (CPG) to report on relevant audit findings and to provide advice and input to the Group as required
- reviewing final accounts for capital projects. Using a risk based process, Veritau auditors identify projects to be reviewed and request the relevant documentation
- offering input and advice, where required, into the Highways Maintenance Contract 2012 project
- contributing to the annual review and update of the County Council's Contract Procedure Rules
- retaining copies of scoring mechanisms for pre qualification questionnaires (PQQs) and invitations to tender (ITTs). Details of scoring mechanisms must be logged with Veritau prior to the evaluation process taking place. This helps to ensure that the County Council can defend any challenge from unsuccessful tenderers (or others) that the evaluation model and any scoring mechanisms used may have been altered after the receipt or during the evaluation of PQQs and ITTs
- Veritau staff have presented a number of training courses throughout the county on the application of LMS Procedure Rules for the benefit of staff in schools
- carrying out a number of special investigations into contract related matters that have either been communicated via the Whistleblowers' hotline or have arisen from issues and concerns raised with Veritau by management

3.3 As with previous audit reports an overall opinion has been given for each of the specific systems or areas under review. The opinion given has been based on an assessment of the risks associated with any weaknesses in control identified.

3.4 The opinions used by Veritau are provided for the benefit of Members below:

High Assurance	Overall, very good management of risk. An effective control environment appears to be in operation.
Substantial	Overall, good management of risk with few weaknesses identified. An effective control environment is in operation but there is scope for further improvement in the areas identified.
Moderate	Overall, satisfactory management of risk with a number of weaknesses identified. An acceptable control environment is in operation but there are a number of improvements that could be made.
Limited	Overall, poor management of risk with significant control weaknesses in key areas and major improvements required before an effective control environment will be in operation.

No Assurance Overall, there is a fundamental failure in control and risks are not being effectively managed. A number of key areas require substantial improvement to protect the system from error and abuse.

3.5 The following categories of opinion are also applied to individual actions agreed with management:

Priority 1 (P1) – A fundamental system weakness, which presents unacceptable risk to the system objectives and requires urgent attention by management.

Priority 2 (P2) – A significant system weakness, whose impact or frequency presents risks to the system objectives, which needs to be addressed by management.

Priority 3 (P3) – The system objectives are not exposed to significant risk, but the issue merits attention by management.

3.6 It is important that agreed actions are formally followed up to ensure that they have been implemented. Veritau now formally follow up all agreed actions on a quarterly basis, taking account of the timescales previously agreed with management for implementation. **On the basis of the follow up work undertaken during the year, the Head of Internal Audit is satisfied with the progress that has been made by management to implement previously agreed actions necessary to address identified control weaknesses.**

3.7 All internal audit work undertaken by Veritau is based on an Audit Risk Assessment. Areas that are assessed as well controlled or low risk are reviewed less often and in our experience continue to be satisfactory between audits. Veritau's audit work is focussed on the higher risk areas. Veritau officers work closely with management to address any areas of concern. The scope of many audits means that a large number of processes are reviewed with many of these being found to be satisfactory or better. In most of the audits listed in **Appendix 1**, however, specific weaknesses of varying severity were identified which need to be addressed.

4.0 AUDIT OPINION

4.1 Veritau works to the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom. In connection with reporting to Audit Committees, that guidance states that:

The Head of Internal Audit's formal annual report to the organisation should:

- (a) include an opinion on the overall adequacy and effectiveness of the organisation's internal control environment
- (b) disclose any qualifications to that opinion
- (c) present a summary of the audit work undertaken to formulate the opinion, including reliance placed on work by other assurance bodies

- (d) draw attention to any issues the Head of Internal Audit judges particularly relevant to the preparation of the Annual Governance Statement.
- (e) compare work actually undertaken with the work that was planned and summarise the performance of the Internal Audit function against its performance measures and criteria
- (f) comment on compliance with these standards and communicate the results of the Internal Audit quality assurance programme”.

4.2 The overall opinion of the Head of Internal Audit on the controls operated in respect of contract matters is that they provide **Substantial Assurance**. There are no qualifications to that opinion and no reliance has been placed on the work of other assurance bodies in reaching that opinion.

5.0 RECOMMENDATION

5.1 That Members consider the information provided in this report to determine whether they are satisfied that the internal control environment operating in relation to contract arrangements is both adequate and effective.

MAX THOMAS
Head of Internal Audit
Veritau Ltd

BACKGROUND DOCUMENTS

Relevant Audit Reports kept by Veritau Ltd at 50 South Parade. Contact Roman Pronyszyn 2284.

Report prepared by Roman Pronyszyn, Audit & Information Assurance Manager and presented by Max Thomas, Head of Internal Audit

County Hall
Northallerton

29 February 2012

FINAL AUDIT REPORTS ISSUED IN THE YEAR ENDED 31 JANUARY 2012

	System/Area	Audit Opinion	Area Reviewed	Date Issued	Comments	Action Taken
A	Capital Contracts – Harrogate Library	High Assurance	Application of NYCC procedures and the effectiveness of contract monitoring in relation to the Harrogate Library contract.	19/01/12	<p>Arrangements for letting and monitoring of the contract were found to be in accordance with NYCC procedures.</p> <p>It was however found that the original copy of the contract had not been lodged with the County Archivist and the auditors had to obtain a copy of the original from the contractor.</p>	<p>One P2 finding was identified.</p> <p>Responsible Officer</p> <p>Assistant Director – Central Finance</p> <p>The AD-FCS was aware of the issue and has agreed to take action to ensure contracts are lodged with the Archivist where appropriate.</p>
B	Central Harrogate Highway Maintenance (<i>also BES report December 2011</i>)	Moderate Assurance	The contractor used by Harrogate Borough Council to undertake highway maintenance work under the previous agency agreement was Ringway Limited. The contract is now overseen by NYCC's Area 6 Highways Office. The audit reviewed the process followed to initiate highway maintenance and repairs and to monitor costs and contract performance.	27/06/11	<p>The main issues identified during the audit related to:</p> <ul style="list-style-type: none"> ▪ management being unable to confirm whether the amounts calculated to be paid to Ringway Limited were based upon agreed contract rates. ▪ a number of weaknesses in the procedures for authorising urgent work, budgetary control and the reconciliation of payments. 	<p>Two P2 actions were agreed with management and documented within the audit report.</p> <p>Responsible Officers</p> <p>Assistant Director – Highways and Transport</p> <p>Assistant Director – Highways and Operations</p> <p>The Symology system (previously operated by Harrogate BC) will be updated to reflect the current contract rates with Ringway Limited. This was expected to be completed by December 2011.</p>

APPENDIX 1

	System/Area	Audit Opinion	Area Reviewed	Date Issued	Comments	Action Taken
						A detailed action plan was put in place to address the various system and control weaknesses identified during the audit; to be implemented by December 2011.
C	HMC 2012 Project 2011/12 - Part 1 <i>(also BES report December 2011)</i>	High Assurance	The audit examined the procedures followed in the tendering process for the Highways Maintenance Contract 2012 and compliance with relevant legislation, policies and procedures (including the County Council's Contract Procedure Rules).	16/09/ 11	No weaknesses were identified during the audit of the tendering process for the 2012 HMC Project that needed to be brought to management's attention.	No actions raised in the audit report. Strong governance arrangements continue to be applied to this complex, high value project. A member of the audit team attends the fortnightly Mobilisation Team meetings to offer independent 'check and challenge'
D	HAS Contracting – Provider List	High Assurance	To ensure that the 2011/12 provider list has been procured in accordance with NYCC's procurement rules. The key controls within the procurement system are operating as envisaged.	05/01/12	Only one minor weakness concerning the recording of provider details in the Adult Integrated System.	One P2 issue identified and action agreed with management. Responsible Officer FSS Central

	System/Area	Audit Opinion	Area Reviewed	Date Issued	Comments	Action Taken
E	Budgetary Control – Highways Maintenance (<i>also in the BES report December 2011</i>)	Moderate Assurance	The audit examined whether the system for the calculation and monitoring of highways maintenance budgets was effective. The audit also reviewed the adequacy of processes in place for ensuring that overspends and variances are identified and dealt with appropriately.	20/06/11	<p>The main issues identified during the audit related to:</p> <ul style="list-style-type: none"> ▪ delays in agreeing final costs for some projects reviewed. ▪ in one case, poor initial budget and design planning and in another case, inadequate site investigation resulted in unforeseen overspends ▪ delays in the completion of cost variation forms. 	<p>Four P2 and two P3 actions were agreed with management.</p> <p>Responsible Officers Assistant Director – Highways and Transport Head of Highways Operations</p> <p>A reminder of the Scheme Procedure Sheet was issued highlighting all scheme elements and the importance of Early Partner involvement to identify all scheme costs.</p> <p>As part of the HMC contract governance arrangements, the Operational Management Group (OMG) meet on a monthly basis with Balfour Beatty and Jacobs UK where the number of completed schemes and scheme sign offs are reviewed.</p> <p>The level of site investigation appropriate to schemes is to be reviewed. Guidance will then be issued to all relevant staff as necessary.</p>

APPENDIX 1

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						OMG issued a key message following its October 2011 meeting requiring all outstanding schemes to receive higher priority in order to sign them off. A short timescale was put in place to achieve this. The message was reinforced at the Area / Network Strategy Managers meeting (AM/NSMT) and will continue to be re-iterated.
F	Budgetary Control – Engineering (<i>also in the BES report December 2011</i>)	Substantial Assurance	The audit examined whether the system for the calculation and monitoring of highways maintenance budgets was effective. The audit also reviewed the adequacy of processes in place for ensuring that overspends and variances are identified and dealt with appropriately.	20/06/11	<p>The issues identified during the audit related to:</p> <ul style="list-style-type: none"> ▪ the authorisation of a significant under-spend on a project ▪ the retention of evidence to support authorised overspends on highways schemes. 	<p>Two P3 actions were agreed with management.</p> <p>Responsible Officer</p> <p>Head of Commercial Services</p> <p>Corresponding Cost Variation Forms (CVFs) have been signed off and minuted at H&T MT with a ‘key lessons’ guidance note issued to AM/NSMT in September 2011. A revised CVF and protocols were issued in June 2011, with reminders in September 2011 (including the need to report reductions as well as increases).</p>

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G	Waste PFI Project <i>(also in the BES report December 2011)</i>	Substantial Assurance	The audit was limited to considering the future payment mechanisms associated with the contract.	11/06/11	<p>The following changes / improvements were identified during the audit:</p> <ul style="list-style-type: none"> ▪ the agreements needed to include a right for audit access to systems and/or documentation maintained by AmeyCespa. ▪ NYCC and CYC should investigate the benefits of establishing joint contract management arrangements to monitor performance and to record and report tonnages delivered to the new facility. 	<p>Two P2 and actions were agreed with management.</p> <p>Responsible Officers</p> <p>Assistant Director – Performance and Finance BES</p> <p>Assistant Director – Waste Management</p> <p>It was agreed that audit access would be incorporated into the contracts at commercial close.</p> <p>Joint contract monitoring was agreed in principle, and is being developed prior to financial close.</p>
H	Property Services – Project Cost Monitoring	Substantial Assurance	<p>To ensure that costs for works are thoroughly and regularly checked by NYCC Project Sponsors when information is provided by Jacobs UK, including the authorisation of change orders and additional budgets.</p> <p>There is a suitable monitoring mechanism in place to ensure that client officers regularly review the costs for works and fees against each project.</p>	16/06/11	The audit concluded that risks were well managed and that an effective control system now operated in the area. Two minor improvements were identified and agreed with management.	<p>One P2 and one P3 finding were implemented.</p> <p>Responsible Officer</p> <p>Finance Manager – CASU</p>

APPENDIX 1

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			There is a suitable system in place for identifying and enquiring into any substantial variances encountered.			