

## NORTH YORKSHIRE COUNTY COUNCIL

### AUDIT COMMITTEE

8 MARCH 2012

#### INTERNAL AUDIT WORK AND RELATED INTERNAL CONTROL MATTERS FOR FINANCE AND CENTRAL SERVICES AND MATERIAL FINANCIAL SYSTEMS

##### Joint Report of the Head of Internal Audit, Veritau Ltd and the Corporate Director – Finance and Central Services

#### 1.0 PURPOSE OF THE REPORT

- 1.1 To inform Members of the **internal audit work** performed during the year ended 31 January 2012 for the Finance and Central Services (F&CS) Directorate and on material financial systems and to give an opinion on the systems of internal control in respect of this area.
- 1.2 To consider the **Statement of Assurance** for 2011/12 signed by the Corporate Director – F&CS.
- 1.3 To consider the **Risk Register** for the Directorate.

#### 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 the F&CS Directorate the Committee receives assurance through the work of internal audit (as provided by Veritau Ltd), details of the Statement of Assurance provided by the Corporate Director, the Directorate Risk Register and the progress made to date by management to address the areas for improvement and the identified risks.
- 2.2 Accordingly there are three Appendices to this report:

##### Appendix 1

A summary of the **internal audit reports** issued in final in the year since the last report on the F&CS Directorate, to the Audit Committee in March 2011. Specific attention is drawn to any Priority 1 agreed actions that management have chosen not to implement.

## Appendix 2

The relevant extract from the **Statement of Assurance** provided at the 2010/11 year end by the Corporate Director detailing the issues identified and the proposed actions to be undertaken during 2011/12.

## Appendix 3

A copy of the current **Directorate Risk Register** and the proposed actions to manage these risks.

2.3 The Risk Prioritisation System used to derive all Risk Registers across the County Council categorises risks as follows:

- Category 1 and 2 are high risk (RED)
- Category 3 and 4 are medium risk (AMBER)
- Category 5 and 6 are low risk (GREEN)

These categories are of course relative not absolute assessments - equally the Risk Register at Directorate level is designed to identify the dozen or so principal risks that may impact on the achievement of performance targets etc for the Directorate as a whole in the year – it is not a full Register of all the risks that are managed in the Directorate.

## 3.0 WORK DONE DURING THE YEAR ENDED 31 JANUARY 2012

3.1 Detail of the work undertaken for the F&CS Directorate and the outcome of those audits is provided in **Appendix 1**.

3.2 Veritau has also been involved in a number of other areas of work in respect of F&CS. These have included:

- the provision of guidance and advice as part of the Corporate Procurement Group
- carrying out a number of special investigations that have either been communicated via the Whistleblowers' hotline or have arisen from issues and concerns raised with Veritau by F&CS 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 monthly 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 the F&CS senior managers 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 a number of the audits listed in **Appendix 1**, however, specific weaknesses 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 the F&CS Directorate and for Material Financial Systems is that they provide **Substantial Assurance**. There are no qualifications to this opinion and no reliance was placed on the work of other assurance bodies in reaching that opinion.

## 5.0 STATEMENT OF ASSURANCE AND DIRECTORATE RISK REGISTER

5.1 The Chief Executive and each Corporate Director produce a **Statement of Assurance** (SoA) at the end of each financial year. In this Statement the Corporate Director identifies those items that may give rise to internal control or performance risk issues for the Directorate in the forthcoming year. These issues feed into the process that enables the Annual Governance Statement (AGS) to be prepared for the County Council.

5.2 **Appendix 2** details the items identified by the Corporate Director in March 2011 (first two columns of the Appendix) – the *Progress to date* column has been added and records management action(s) to date in this financial year.

5.3 The **Directorate Risk Register** (DRR) is the end product of a systematic process that initially identifies risks at Service Unit level and then aggregates these via a sieving process to Directorate level. A similar process sieves Directorate level risks into the Corporate Risk Register.

5.4 **Appendix 3** summarises the risks identified when the DRR was last reviewed in December 2011. As with the SoA a *Progress to date* column has been added to record management action(s) to date.

- 5.5 There is bound to be a degree of overlap between SoA issues and the Directorate Risk Register. Cross referencing is therefore provided, where appropriate, between **Appendices 2 and 3** to assist Members consider the two documents in parallel.

**6.0 RECOMMENDATION**

- 6.1 That Members consider the information provided in this report and determine whether they are satisfied that the internal control environment operating in the Finance and Central Services Directorate is both adequate and effective.

MAX THOMAS  
Head of Internal Audit  
Veritau Ltd

JOHN MOORE  
Corporate Director – Finance and Central Services

County Hall  
Northallerton  
21 February 2012

**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.

**APPENDIX 1 - FINAL AUDIT REPORTS ISSUED IN THE YEAR ENDED 31 JANUARY 2012**

<b>System/Area</b>	<b>Audit Opinion</b>	<b>Areas Reviewed</b>	<b>Date Issued</b>	<b>Comments</b>	<b>Action Taken</b>
Waste Management (10/11)	Substantial Assurance	Management of Waste Disposal including accounting for income and expenditure, and exchange of information between NYCC and key partners.	01/06/11	It was concluded that arrangements for management of risks were good and that an effective control environment was in place. Some areas for further improvement were identified around recycling credits, management of invoices and follow up.	<p><b>Seven P2 and one P3 actions were agreed with management, and documented within the report.</b></p> <p><b>Responsible officers were:</b></p> <p><b>BES - Waste Service Manager</b></p> <p><b>F&amp;CS - Exchequer Services Manager</b></p>
Debtors (10/11)	Substantial Assurance	A review of procedures for processing income received from NYCC debtors, in line with the International Auditing Standards.	28/04/2011	A number of minor issues around low value invoices, county court costs and administration fees were identified. However, overall the conclusion was that the system was subject to an effective control environment.	<p><b>Four P2 and four P3 actions were identified.</b></p> <p><b>Responsible Officers were:</b></p> <p><b>Assistant Director, Central Finance</b></p> <p><b>Assistant Director, Finance and Management Support within Directorates</b></p>

System/Area	Audit Opinion	Areas Reviewed	Date Issued	Comments	Action Taken
Miscellaneous Income and Banking (10/11)	Substantial Assurance	A review of procedures for processing miscellaneous income and banking within NYCC, in line with the International Auditing Standards.	15/11/11	Arrangements were found to be effective with only minor reconciliation discrepancies.	<b>One P2 action was agreed and implemented.</b>  <b>The responsible officer</b> <b>F&amp;CS - Principle Accountant (CASU)</b>
Property Services – Payments to Jacobs UK	Moderate Assurance	To ensure that payments made to Jacobs in respect of technical officer services for NYCC's properties are adequately checked by the appropriate officers prior to payment being made.	15/06/11	Although the general control environment was found to be satisfactory, weaknesses were found in:  <ul style="list-style-type: none"> <li>- the checking of invoices submitted by Jacobs;</li> <li>- failure of the Prolog User Group to meet regularly; and</li> <li>- proper recording of fee challenges.</li> </ul> Revised arrangements are now in place to address each of the P2 weaknesses identified in the audit.	<b>Three P2 actions were agreed with management and documented in the reports.</b>  <b>Responsible Officer</b> <b>F&amp;CS - Finance Manager, (CASU)</b>

System/Area	Audit Opinion	Areas Reviewed	Date Issued	Comments	Action Taken
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> <p>There is a suitable system in place for identifying and enquiring into any substantial variances encountered.</p>	16/06/11	The audit concluded that risks were well managed and that an effective control system now operates in the area. Two minor improvements were identified and agreed with management.	<p><b>One P2 and one P3 finding were implemented.</b></p> <p><b>Responsible Officer</b> <b>F&amp;CS - Finance Manager, (CASU)</b></p>
Debtors HAS-PCT Reconciliation Check	Moderate Assurance	A review of the reconciliation and debt recovery process between the County Council (HAS) and the PCT. The audit concentrated on a number of disputed cases in the Selby area.	08/12/11	The audit found that ongoing problems with communications resulting in the HAS Finance team being unable to obtain copies of some of the information they required. The Finance team were also unable to agree the	<p><b>Three P2 findings were identified and appropriate action agreed.</b></p> <p><b>Responsible Officer</b> <b>HAS - Principal Finance Manager</b></p>



System/Area	Audit Opinion	Areas Reviewed	Date Issued	Comments	Action Taken
				<p>10/11 reconciliation with the PCT.</p> <p>In addition, the audit found weaknesses in the monitoring of CHC returns and some confusion in the use of "Determination Sheets" in relation to funding.</p> <p>The audit concluded with a moderate assurance.</p>	
Creditors	Substantial Assurance	<p>To identify any areas of duplicate data held within Accounts Payable.</p> <p>Payments made before the end of the 30 day period are only to companies that have submitted a form to NYCC or as part of an authorised process.</p>	29/11/11	<p>It was found that arrangements for managing risk were good and that an effective control environment operated. Potential improvements were identified in the identification and duplicate creditor names and addresses and in controls over relocation expenses.</p>	<p><b>Three P3 findings were identified.</b></p> <p><b>Responsible Officers:</b></p> <p><b>Exchequer Services Manager</b></p> <p><b>Assistant Director – Adult Social Care Operations</b></p> <p>In view of the overall high level of performance (duplicate payments representing less than 0.01% of payment) it was deemed not cost effective</p>

System/Area	Audit Opinion	Areas Reviewed	Date Issued	Comments	Action Taken
					to take substantial action regarding potential duplicate creditor names. Management also decided not to take action to recover the overpayment of relocation expenses.  The third issue concerned Financial Admin training is being addressed via the Learning Zone.
Treasury management	High Assurance	The effectiveness of controls over the investment of surplus cash on behalf of NYCC and other bodies as well as short and long term borrowing arrangements.	12/10/11	The audit found the control environment to be very effective and risk well managed. One minor issue concerning the documenting of bank reconciliations was raised.	<b>One P3 action was agreed</b>  <b>Responsible Officer</b>  <b>F&amp;CS - Principal Accountant</b>
Feeder Systems	High Assurance	Controls over a number of systems which feed the Oracle Financial system to ensure that the interface operates effectively and minimises the risk of erroneous payments.	04/01/12	Overall the audit found systems to be effective and well controlled. One issue regarding the interface with the SWIFT receivables feeder system was identified.	<b>One P3 finding was identified and agreed</b>  <b>Responsible Officer</b>  <b>F&amp;CS - System Manager</b>

**APPENDIX 2 - EXTRACT FROM STATEMENT OF ASSURANCE PROVIDED BY THE CORPORATE DIRECTOR – FINANCE AND CENTRAL SERVICES**

**AREAS FOR IMPROVEMENT IDENTIFIED**

**BY FINANCE AND CENTRAL SERVICES**

Areas for improvement		Action proposed	DRR Ref	Progress to date (Jan 2012)
A	<p><b>Pension Fund</b></p> <ul style="list-style-type: none"> <li>improve solvency</li> </ul>	<p>The need for the Pension Fund to recover solvency is well understood by the Pension Fund Committee. The Investment Strategy, and fund managers, continue to be monitored for their performance and appropriateness.</p> <p>The Investment Strategy has been reviewed to coincide with the outcome of the 31/3/10 Triennial Valuation. Changes will be made to both asset allocation and the fund manager roster to reduce volatility without (hopefully) impeding performance return.</p>	<b>B</b>	<p>The Pension Fund Committee continues to review its Investment Strategy, consequent asset allocation and the performance of individual fund managers on a regular basis.</p> <p>Changes to the Strategy are currently being made to reflect the changing conditions in financial markets.</p>
B	<p><b>Medium Term Financial Strategy</b></p> <ul style="list-style-type: none"> <li>need to validate funding assumptions and achieve targeted savings through the 4-year period 2011/15</li> </ul>	<p>The MTFS for the period 2011/15 reflects the need for substantial savings in order to “balance the books”.</p> <p>There is an approved and detailed savings matrix for 2011/12 and 2012/13. The projected shortfall in 2013/14 and 2014/15 is expected to be funded by savings generated from the One Council change programme. This prospect will need to be thoroughly assessed in the period to the start of 2013/14.</p>		<p>A detailed savings matrix for the 4 year period 2011/15 is in place – overall target saving is £69m and an updated MTFS for 2012/15 was approved by the County Council on 15/2/12.</p> <p>The Executive receive, via the Quarterly Performance and Budget Monitoring reports, details of progress made to date in the current year. Based on the report for Q3 considered by the Executive on 28/2/12 the savings target for 2011/12 is being delivered and plans are well advanced for 2012/13.</p> <p>The One Council programme is expected to contribute at least £7.6m towards the £69m. Work on developing ‘Action Plans’ for the various One</p>

## AREAS FOR IMPROVEMENT IDENTIFIED

### BY FINANCE AND CENTRAL SERVICES

Areas for improvement		Action proposed	DRR Ref	Progress to date (Jan 2012)
				Council workstreams is also well advanced and details will be reported to the Executive in April/May 2012.
C	<p><b>Service Continuity Planning</b></p> <ul style="list-style-type: none"> <li>a Corporate Policy/Strategy needs to be in place supported by the development, and testing, of a comprehensive suite of service based Continuity Plans</li> </ul>	<p>The Civil Contingency Act 2004 places a requirement on the County Council to have in place a set of internal SCP arrangements.</p> <p>Following a review of progress to date, a revised approach will be proposed based on “bottom-up” principles with greater attention paid to the need for corporate inputs (eg property, ICT) and streamlined “command” structures.</p>	<b>F/H/I</b>	<p>As reported to the December Committee meeting Management Board has signed off a revised draft SCP Policy/Strategy. BES has undertaken a pilot exercise which is about to be evaluated. Assuming the evaluation is positive Management Board will then be asked to roll-out the revised approach.</p> <p>Management Board has also undertaken a desk-top Gold command exercise – this identified a number of “response requirements” relating to ICT and property that can now be developed into a generic Response Plan for these aspects of the County Council’s overall SCP capability.</p>
D	<p><b>Information Governance</b></p> <ul style="list-style-type: none"> <li>need to maintain roll-out of Information Governance Framework Action Plan</li> </ul>	<p>The Corporate Information Governance Group (CIGG2) has developed a comprehensive set of policies within a single coherent Framework.</p> <p>The Action Plan focuses on roll-out issues (eg training of staff) that need to be progressed.</p> <p>There is also a need to develop a rigorous process for reporting and investigating breaches.</p>	<b>A</b>	<p>CIGG2 continues to progress the Action Plan. Regular reports on progress are submitted to this Committee.</p> <p>A standardised approach for reporting/investigating breaches has been devised that will be implemented in 2012/13.</p>

## AREAS FOR IMPROVEMENT IDENTIFIED

### BY FINANCE AND CENTRAL SERVICES

Areas for improvement		Action proposed	DRR Ref	Progress to date (Jan 2012)
E	<p><b>ICT Strategy</b></p> <ul style="list-style-type: none"> <li>a revised Corporate ICT Strategy needs to be in place that reflects the IT priorities of the County Council but is reconciled to the likely level of resources that will be available in the future</li> <li>within that Strategy the key item is the migration from Novell to Microsoft</li> </ul>	<p>A revised ICT Strategy (and resourced Action Plan) will be presented to the Management Board. The Strategy must address key issues such as the Microsoft transition, Disaster Recovery / IT resilience as well as be compatible with the requirements of the One Council change programme.</p>	<b>G</b>	<p>A revised Strategy is drafted but has been 'frozen' so that it can be made compatible with the needs / requirements of the One Council programme – several aspects of the Strategy are directly affected by One Council workstreams.</p> <p>However aspects of the draft Strategy, notably the migration from Novell to Microsoft and Disaster Recovery, are being progressed.</p>
F	<p><b>Connecting North Yorkshire</b></p> <ul style="list-style-type: none"> <li>need to progress BDUK procurement and secure commensurate grant funding</li> <li>also need to progress "not-spot" programme along with the BDUK project</li> </ul>	<p>A Connecting North Yorkshire Board has been established. Procurement has to be completed by June 2012 so that funding streams can be maximised.</p> <p>Need to develop key partner links to support delivery (eg LEP)</p> <p>A Project Team is in place (hosted by NYnet). In addition to the BDUK procurement, that Team needs to develop a sustainable not-spot methodology.</p>		<p>The Connecting North Yorkshire (CNY) Board meets on a regular basis.</p> <p>The BDUK/ERDF funded procurement is on schedule.</p> <p>Links are being developed with the LEP and the GO ON campaign has been launched.</p> <p>A Strategy for 'not-spots' is in place and a programme (using PRG grants) to establish c.15 community schemes is underway.</p> <p>A Members Seminar was held on the matter in November 2011 and a full progress report submitted to the Executive on 20/12/11.</p>

## AREAS FOR IMPROVEMENT IDENTIFIED

### BY FINANCE AND CENTRAL SERVICES

Areas for improvement		Action proposed	DRR Ref	Progress to date (Jan 2012)
G	<p><b>One Council</b></p> <ul style="list-style-type: none"> <li>• lead on 5 workstreams and contribute / respond, as necessary, to remaining workstreams</li> </ul>	<p>F&amp;CS is leading on the following workstreams</p> <ul style="list-style-type: none"> <li>• Property</li> <li>• IT</li> <li>• Procurement</li> <li>• Financial administration</li> <li>• Income</li> </ul> <p>Within these workstreams there will be proactive items (that can be progressed as soon as possible) and reactive items (ie created by other workstreams). Work on these workstreams will have to be resourced alongside "business as usual" tasks.</p>	<b>C</b>	<p>The Income workstream has been completed and the results fed into the recent Budget/MTFS process.</p> <p>Work on the other 4 workstreams is progressing on schedule with a detailed report concerning the proposed Actions to be taken on all workstreams due to be presented to the Executive in April/May 2012.</p>

### APPENDIX 3 – FINANCE AND CENTRAL SERVICES - RISK REGISTER

Risk Register					
Risk		Current Risk Rating	Post Risk Rating	SoA Ref	Progress to date (January 2012)
<b>A</b>	Information Governance breach leading to loss of reputation, fine, etc	5	2	<b>D</b>	Continued to implement roll out plan agreed by CIGG2. This includes staff training, development of information asset register and monitoring of bridges.
<b>B</b>	Solvency deteriorates due to liability growth exceeding expectations and / or underperforming investment returns, over optimistic actuarial assumptions, or adverse market conditions requiring a review of employer contributions, additional payments or extended recovery period	4	2	<b>A</b>	<b>See Appendix 2 item A.</b>
<b>C</b>	Unintended impact of One Council programme on ability of Directorate to maintain adequate service levels resulting in reduced financial / property / contract governance	3	4	<b>G</b>	The effect/impact of the One Council programme and its workstreams on F&CS is monitored on an ongoing basis. Internal audit work is commissioned to establish impact of savings on the control environment.
<b>D</b>	Major Corporate Health and Safety failure resulting in injuries, claims, reputational and service delivery impact and possible prosecution etc (including new Corporate Manslaughter Legislation)	5	3		This is a 'Standing' item in the Risk Register. The Health and Safety team has a range of rehearsed responses depending on nature of the incident.
<b>E</b>	Default of major lender/borrower over £1 million resulting in internal inquiry, loss of reputation, qualified final accounts. This includes the potential for not identifying and acting on the downgrading of credit ratings and other relevant factors and market sentiment towards particular organisations	2	3		Ongoing review/update of Treasury Management practices and criteria for lending to financial institutions are reported to Executive quarterly and discussed at monthly meetings with the Deputy Leader and Portfolio Holder.

## Risk Register

Risk		Current Risk Rating	Post Risk Rating	SoA Ref	Progress to date (January 2012)
<b>F</b>	Failure to deliver Service Continuity Planning across the County Council resulting in the potential for NYCC being unable to deliver its critical services and / or meet the statutory requirements	5	5	<b>C</b>	The revised Service Continuity Planning system and processes are under review. The pilot in BES has been carried out successfully. Next stage is for Management Board to sanction a full roll-out programme.
<b>G</b>	Failure to transfer from Novell to Microsoft Architecture	5	5	<b>E</b>	Business Case approved. First phase of project (ie migration to Microsoft Outlook) successfully completed. The next stage, which involves migrating/upgrading all pcs, will be much riskier (given its impact on users).
<b>H</b>	Failure to have an up to date and tested comprehensive disaster recovery and IT service continuity plan	6	5	<b>C</b>	DR plans implemented and tested successfully. Need to be further reviewed/tested when migration to Microsoft has been completed.
<b>I</b>	Unexpected loss/absence of key person(s) (e.g. Dir, AD / Service Head) for more than 3 months resulting in loss of service delivery and/or significant project delays, loss of management capability with consequent increase in stress, etc	2	4	<b>C</b>	Arrangements reviewed annually and/or if change in senior staff occurs. Review by FSMT just completed.
<b>J</b>	Failure to achieve Directorate savings as per the budget matrix resulting in the need to identify alternative savings	2	5		F&CS is on schedule to meet its matrix savings targets for all 4 years (total £2.1m).