

NORTH YORKSHIRE COUNTY COUNCIL

AUDIT COMMITTEE

28 JUNE 2012

ANNUAL REPORT OF THE HEAD OF INTERNAL AUDIT

1.0 PURPOSE OF THE REPORT

- 1.1 To provide a summary of the internal audit work performed during the year ended 31 March 2012 and to express an opinion on the overall internal control environment in place within the County Council.
- 1.2 To provide Members with details of breaches to Finance, Contract and Property Procedure Rules identified during 2011/12 audit work.
- 1.3 To consider the Internal Audit performance outturn for 2011/12 and targets for 2012/13.
- 1.4 To note the performance of Veritau as a Company in 2011/12.

2.0 BACKGROUND

- 2.1 The work of internal audit is governed by the Accounts and Audit Regulations 2011 and the CIPFA Code of Practice for Internal Audit in Local Government 2006. In accordance with the Code of Practice, the Head of Internal Audit is required to report to those charged with governance on the findings of audit work, provide an annual opinion on the Council's internal control environment and identify any issues relevant to the preparation of the Annual Governance Statement.
- 2.2 Since 1 April 2009, the County Council's internal audit, counter fraud and information governance services have been provided by Veritau Limited, a company jointly owned by North Yorkshire County Council and the City of York Council.
- 2.3 Audit work was undertaken across all of the County Council's services and activities in accordance with an Internal Audit Plan, which was approved by this Committee in April 2011.
- 2.4 Detailed internal audit findings have been reported to this Committee in accordance with the following cycle:-

June 2011	Corporate / thematic audits
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September 2011	Health and Adult Services IT Audit
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December 2011	Business and Environmental Services
March 2012	Finance and Central Services, which includes Material Financial Systems Corporate / thematic audits Chief Executive's Group Contract Audit Counter fraud matters
April 2012	Children & Young People's Services

2.5 In each of the above reports, with the exception of the report on counter fraud matters, the Head of Internal Audit provided an opinion on the system of internal control in operation within the particular functional area or directorate.

3.0 **OVERALL WORK DONE FOR 2011/12**

- 3.1 Veritau was responsible for promoting counter fraud arrangements within the County Council, and for providing advice and making recommendations to management to improve controls and/or to address the poor or inappropriate use of Council resources. In 2011/12, Veritau completed 95.2% of the Internal Audit Plan against an agreed performance target of 93%. The overall opinions provided to this Committee at meetings between April 2011 and June 2012 are summarised in **Appendix 1**.
- 3.2 The results of completed audit work have been reported to service managers, the Corporate Director – Finance and Central Services and the Audit Committee. Audit findings relating to 2011/12, which have not yet been reported to this Committee, will be presented in due course as part of the relevant directorate reports, submitted in accordance with the Audit Committee's Programme of Work.
- 3.3 Audit work was also performed for a number of external customers. The results of those audits were separately reported to the relevant organisations.
- 3.4 A new audit report format has been developed which incorporates a clearer assessment of the probability of identified risks occurring and their likely impact. In addition, greater use has been made of data interrogation software to support internal audit and fraud work.
- 3.5 Veritau was involved in a number of investigations during 2011/12. These investigations were carried out in response to whistleblowing communications or concerns raised with Veritau by management. Further proactive work was carried in to address a number of specific fraud risks, particularly within adult social services. The company also updated the County Council's Fraud and Loss Risk self assessment and the Counter Fraud Strategy. In addition, Veritau issued a number of alerts to schools to draw attention to potential threats and scams. Further detail on the counter fraud work carried out by Veritau during 2011/12 was reported to this Committee at its meeting in March 2012.

- 3.6 During 2011/12, the Information Governance Team (IGT) continued its work to assist the County Council's compliance with relevant legislation such as the Data Protection and Freedom of Information Acts and the Environmental Information Regulations. The IGT co-ordinates all requests for information (excluding Social Care Data Protection requests) and provides advice and guidance on the application of these Acts to officers across the County Council. A total of 1105 FOI requests were received during 2011/12 compared to 1096 in 2010/11. This suggests that the rate of increase in numbers received may finally be slowing down.
- 3.7 The IGT has also continued to help develop the County Council's information governance policy and strategy framework to incorporate the core measures identified in the Government's Data Handling review, the HMG Security Framework and ISO 27001. As the County Council's Senior Information Risk Owner (SIRO), the Corporate Director – Finance and Central Services, has continued to chair the Corporate Information Governance Group (CIGG2), which meets on a regular basis. CIGG 2 has addressed new and emerging issues as well as coordinating the development of the IG Framework. In addition, Veritau's auditors have undertaken a programme of work across the County Council designed to test the understanding and compliance of staff with the policy framework.
- 3.8 During the year, Veritau supported a number of officer groups within the County Council. Where appropriate, the Company will continue to be represented on these groups either in an advisory capacity or as a means of ensuring that Veritau staff are kept informed of current developments within the County Council. These groups include:
- Corporate Procurement Group
 - Corporate Governance Officer Group
 - Corporate Information Governance Officer Group
 - Corporate Risk Management Group
- 3.9 In June 2011, Veritau achieved Investors in People (IIP) accreditation. As Veritau's main asset is its people, it is important that the Company continues to train and develop its own staff so that it can provide the services required by its customers, both now and in the future. Management considered that achieving the IIP accreditation would act as a challenge by forcing the Company to critically examine its internal processes. This exercise has resulted in Veritau introducing a number of different procedures to make the best use of its training and development resources and to help the Company recognise the talents of its people.

4.0 INTERNAL AUDIT PERFORMANCE MANAGEMENT

- 4.1 The Accounts and Audit Regulations 2011 require each local authority to conduct an annual review of the effectiveness of its internal audit arrangements, and to report the findings of this review to an appropriate committee. The process is intended to form part of the wider review of the effectiveness of the system of internal control (required to prepare the Annual Governance Statement – AGS). Details of the 2011/12 review are included as a separate report (**see Item 4**) on this Agenda.

Veritau Performance

- 4.2 Despite the challenging climate, 2011/12 has been another successful year for Veritau. The Company has continued to deliver cost effective internal audit, counter fraud and information governance services to North Yorkshire County Council and the City of York Council together with a number of other public sector bodies in North Yorkshire. These services continue to be valued by the Company's clients particularly at a time of significant change.
- 4.3 One of the main priorities for 2011/12 was the establishment of a new company to deliver internal audit services to five of the North Yorkshire district councils. Following prolonged negotiations, agreement was finally reached to form the new company, Veritau North Yorkshire (VNY). The Company itself was established on 1 February 2012 and commenced trading on 1 April 2012. Work is now ongoing to train the staff who transferred to VNY and to ensure that working practices across both companies are fully integrated.
- 4.4 The Company achieved a trading profit before tax in 2011/12 of £17.5k. This compared favourably to the original budget which anticipated a breakeven position for the year. Investment in new systems and working practices has continued. A number of staff have been trained during the year to use the data interrogation software, IDEA. Five of the company's trainees completed their professional qualifications, representing the first group of employees to achieve this. In addition, the Company gained Investors in People (IIP) accreditation.
- 4.5 The Company Board meets on a regular basis and is currently chaired by the Corporate Director – Finance and Central Services. Cllr Watson is on the Board in his capacity as the Executive Member for Corporate Affairs whilst the Chairman of the Audit Committee attends as an observer.
- 4.6 **Appendix 2** details performance against the targets set for Veritau by the County Council's client officer for 2011/12. **Appendix 3** sets out the targets for Veritau for 2012/13.

5.0 BREACHES OF FINANCE, CONTRACT AND PROPERTY PROCEDURE RULES

- 5.1 It is recommended best practice for the Head of Internal Audit to report to the Audit Committee on any breaches of the County Council's Procedure Rules. As in previous years, the majority of breaches, which are identified, relate to the Contract Procedure Rules. Details of those breaches identified by internal audit work during 2011/12 are shown in **Appendix 4**.
- 5.2 It should be noted that some of the variations in the type and number of breaches identified between the years can be attributed to the fact that the scope of audit work will focus on different risk areas each year. In addition, the content of the CPRs does not remain the same and new rules are introduced whilst others are amended or deleted.

- 5.3 As a result, what constitutes a breach in 2011/12 may not, in all cases, have been a breach in earlier years. Moreover, an individual contract may 'score' as more than one breach if multiple issues were identified. All identified breaches are reported to the Corporate Procurement Group where Directorate Procurement Champions are requested to ensure that any key messages on compliance are communicated to staff as appropriate. In most cases it is sufficient to draw the attention of management to the relevant CPR requirement. If a wider training need is identified this is addressed accordingly. Finally in those cases where the breach identifies a fundamental weakness/deficiency in the CPR this will be addressed separately as part of the ongoing review process for all the Procedure Rules.
- 5.4 There were no significant breaches of the Finance Procedure Rules although a number of relatively minor breaches were noted. Examples of typical errors identified included:
- orders not being used correctly or not being annotated to record details of the corresponding delivery note
 - use of personal credit cards to purchase items for schools/establishments
 - lack of an appropriate scale of charges drawn up by the establishment to detail fees and charges
 - annual stock checks not being carried out on inventory records
 - VAT not accounted for correctly e.g. on adult meals at schools or appropriate VAT receipts not held
 - income records at establishments not always being fully completed on a timely basis
 - purchase invoices not always paid within 30 days of receipt
 - staff being reimbursed for expenses without supplying a valid receipt
 - failure to record assets taken off premises
 - lack of appropriate segregation of duties
 - failure to ensure that transactions (e.g. virements, credit notes, reconciliations etc) are correctly authorised
 - security and insurance issues with the storage of cash, credit cards or cheques
 - invoices/petty cash claims raised or submitted for minor amounts
- 5.5 Veritau auditors did not identify any significant breaches of Property Procedure Rules during 2011/12.

6.0 **AUDIT OPINION**

- 6.1 Veritau operates in accordance with the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom. In connection with reporting to an Audit Committee, the 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".

6.2 The overall opinion of the Head of Internal Audit on the controls operated in the County Council is that they provide **Substantial Assurance**. There are no qualifications to this opinion. The only reliance placed on the work of other assurance bodies in reaching this opinion relates to computer audit work, which was undertaken on behalf of Veritau by PricewaterhouseCoopers.

6.3 In giving this opinion attention is drawn to the following significant control issues, which are considered relevant to the preparation of the 2011/12 Annual Governance Statement:

- improvements in the County Council's information governance arrangements are still required. The key area where concerns remain is in relation to information security. A number of incidents were reported during the year which suggest that staff are still failing to adequately apply the appropriate safeguards to personal or sensitive information. Audit compliance testing also identified poor controls over potentially sensitive information
- control weaknesses were found in the system for processing travel and subsistence claims
- delays and errors were identified with charges for adult social care. Other control weaknesses were also identified in respect of the systems for calculating, monitoring and verifying these charges
- control weakness were found with a number of directorate / service based IT applications including poor access controls, the lack of systems or user documentation and inadequate change control procedures

7.0 **RECOMMENDATIONS**

7.1 Members are asked to:-

- (i) receive the overall “Substantial Assurance” opinion of the Head of Internal Audit regarding the internal control environment of the County Council
- (ii) note the findings on the breaches to Contract, Finance and Property Procedure Rules and the actions taken to address these matters.
- (iii) consider the Internal Audit performance outturn for 2011/12 and the performance targets for 2012/13.
- (iv) note the performance of Veritau as a Company in 2011/12.

MAX THOMAS
Head of Internal Audit

Report prepared and presented by Max Thomas, Head of Internal Audit

Veritau Ltd
Assurance Services for the Public Sector
County Hall
Northallerton

15 June 2012

OPINIONS ISSUED IN 2010/11

Report	Directorate/Audit Work Area	Opinion	Period Covered
June 2011	Corporate / thematic audits	Moderate	1 June 2010 to 31 May 2011
September 2011	Computer Audit	Moderate	1 September 2010 to 31 August 2011
	Health and Adult Services	Moderate	1 September 2010 to 31 August 2011
December 2011	Business and Environmental Services	Substantial	1 December 2010 to 30 November 2011
March 2012	Contract Audit	Substantial	1 February 2011 to 31 January 2012
	Finance and Material Systems	Substantial	1 February 2011 to 31 January 2012
	Chief Executive's Group	Substantial	1 February 2011 to 31 January 2012
	Corporate / thematic audits	Moderate	1 February 2011 to 31 January 2012
	Counter fraud matters	N/A	1 February 2011 to 31 January 2012
April 2012	Children and Young People's	Substantial	1 March 2011 to 29 February 2012

PERFORMANCE TARGETS 2011/12 OUT-TURN

Target		Actual		
Operational Issues				
1	To deliver 93% of the agreed Internal Audit Plan	30 Apr 2012	95.2% of the agreed Internal Audit plan completed	✓
2	To achieve a positive customer satisfaction rating of 95%	31 Mar 2012	100% customer satisfaction	✓
3	To ensure 95% of Priority 1 recommendations made are agreed	31 Mar 2012	100% of Priority 1 recommendations were agreed.	✓
4	To ensure 95% of FOI requests are answered within the Statutory deadline	31 Mar 2012	97.7% of FOI requests received during the year were responded to within the 20 day deadline.	✓
Performance Improvement Issues				
5	Continue to develop and roll-out the new information governance framework	31 Mar 2012	Good progress made but further work required before IG policy framework fully developed	✓
6	To undertake audit of compliance with IG policies	31 Mar 2012	Complete	✓
7	To further develop and implement effective counter fraud measures in line with the actions highlighted in the Veritau Business Plan, with particular reference to issues relating to Health and Adult Services, financial assessment and charging matters	31 Mar 2012	Good progress made but further work still required to fully embed new procedures	✓

PERFORMANCE TARGETS 2012/13

Target		
Operational Issues		
1	To deliver 93% of the agreed Internal Audit Plan.	30 April 2013
2	To achieve a positive customer satisfaction rating of 95%.	31 March 2013
3	To ensure 95% of Priority 1 recommendations made are agreed.	31 March 2013
4	To ensure 95% of FOI requests are answered within the statutory deadline of 20 working days.	31 March 2013

SIGNIFICANT BREACHES OF CONTRACT PROCEDURE RULES

The following table summarises the significant breaches of the Council's Contract Procedure Rules, identified by Veritau during 2011/12:

	Schools 2011/12	Schools 2010/11	Schools 2009/10	Other 2011/12	Other 2010/11	Other 2009/10
Quotations not sought or evidence not retained	7	16	12	0	1	0
Quotation/tender opening and recording procedures incorrect	18	15	14	0	0	0
LMS/CP rules waived but no documented or approved case to justify deviation	1	2	3	1	3	0
Failure to consult with Legal Services re contract conditions and signing and/or failure to obtain appropriate approval to proceed with procurement	5	0	3	0	0	1
Lease for equipment entered into without agreement of Finance	1	6	1	0	0	0
Contract not signed and dated by County Council and contractor	0	0	1	0	8	2
No contract in place or key clauses omitted	5	2	5	1	0	6
Correct procurement process not followed or lack of evidence to confirm	2	3	0	0	0	4
Contract expired but not re-tendered or contracts automatically rolled forward ¹	1	0	0	0	0	3

¹ 2009/10 - it was not possible to specify the exact number of rolling contracts that may have been automatically rolled forward by issuing a letter of agreement. The matter was raised with the directorates concerned.

	Schools 2011/12	Schools 2010/11	Schools 2009/10	Other 2011/12	Other 2010/11	Other 2009/10
Lowest quotation not selected and selection criteria not documented	1	0	0	0	0	0
Inadequate advertising	0	0	0	0	2	0
Scoring mechanism not indicated or not submitted to Veritau (for recording)	0	0	1	0	6	7
Contracts not stored in accordance with CPRs	0	0	0	2	11	17
No financial checks or other requisite checks	25	0	5	0	0	2
Failure to comply with all aspects of Rule 18	0	0	0	0	0	0
SCMS not utilised during procurement process	0	0	0	0	2	7
Inadequate contract monitoring	0	0	0	1	2	0
Cost variation forms not completed.	0	0	0	0	3	0
Issues identified with the Gateway process	0	0	0	0	2 ²	0
TOTALS	66	44	45	5	40	49

² An audit identified that, in general, directorates needed to develop a robust process for identifying those procurement exercises requiring a gateway 4 review and for identifying those that would be exempt.