

# Interim Audit Report

## **Copeland Borough Council**

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<b>Reference:</b>	Copeland Borough Council: Audit Commission Interim Report on Copeland Borough Council Appendix A. Ashley Wilson / Edwin Landles.
<b>Date:</b>	September 2005:

## Introduction

Our Audit Plan for the year 2004-2005 explained the work we would be carrying out to meet our Code of Audit Practice responsibilities. This report gives the results of our interim audit work on Financial Aspects of Corporate Governance and covers:-

- Main Accounting System
- Budgetary Control
- Closedown Plan
- Legality
- Financial Standing
- Systems of Internal Financial Control
- Standards of Financial Conduct

## Main conclusion

### **Main Accounting system**

The main accounting system (MAS) is adequate for producing financial information. There are however weaknesses in governance controls operating within the MAS. Such as: control account reconciliations not being completed on a timely basis, procedures notes for some key financial systems not being updated and controls over access to feeder systems.

### **Budgetary control**

The budgeting system is adequate in the sense that there is a reasonable probability that it would detect a material error. However there are problems with variance investigation, such as housing benefit payments having a £2.2m variance between actual and budget that was not clearly explained. This weakens the governance environment in which the council operates, particularly as the housing benefit system had not been reconciled at the time of our audit visit. We have been informed that as part of the restructure, responsibility for this reconciliation procedure has been passed from the benefits manager to a financial control section with a specific target of reconciling the benefits system. This will commence as from 1 July 2005.

### **Closedown plan**

The council has a detailed and specific plan for closure of its accounts. It needs to add a step to its plan for a senior officer to review the quality of working papers.

### **Legality**

Our work gained assurance that your monitoring officer is in a position to know of the major legal changes going on in the council.

The recent severance arrangements appear compliant with the powers of the council, but during their negotiation and agreement it is unclear that the section 151 officer was kept suitable informed.

### **Financial standing**

The council has set a balanced budget adequately monitors its revenue budgets and capital plans.

**Systems of internal financial control**

The council has made improvements in the uptake of references before taking on a new employee. There are still problems with criminal records bureau checks for casual employees. This could be of concern as one casual worker was taken on in a crèche without such a check.

**Standards of financial conduct**

The council have a fully staffed fraud department and the right policies in place. Our initial review of the council's approach to the Audit Commissions National Fraud Initiative indicates good progress is being made.

**The way forward**

Where we have found weaknesses, we have made recommendations that are summarised in the action plan at the end of this report.

**Status of our reports to the Council**

*Our reports are prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. Reports are prepared by appointed auditors and addressed to Members or officers. They are prepared for the sole use of the audited body, and no responsibility is taken by auditors to any Director/Member or officer in their individual capacity, or to any third party.*

## Financial aspects of Corporate Governance

It is the council's responsibility to put in place effective arrangements to ensure the proper conduct of its financial affairs, and to monitor their adequacy and effectiveness. It is our responsibility to review those arrangements.

### Main Accounting System

1. The council does not have up to date procedure notes for payroll or housing benefit systems. These are business critical systems and should have detailed procedure notes. Procedure notes are part of the governance controls that assist in giving assurance to management. Not only do they act as a source of reference for new staff members, but give clarity to expected procedures to be used and increase staff accountability. Last year we agreed a recommendation that procedure notes be brought up to date for all main systems. This has not been actioned due to pressure on resources available.
2. We agreed a low risk rating for 2003/04, on the assumption action would be taken in the year to date. As this has not been actioned, the risk is increased and procedure noted will need to be drafted. Procedure notes are part of the governance environment, without them it can be difficult to ensure staff comply with council requirements, and to hold them accountable when they do not. The new assessment criteria under the Use of Resources judgement that the audit commission will be implementing specifically considers procedure notes to be a basic requirement to achieve the minimum standards expected.
3. This has been recognised by the Head of Finance and Business Development, and it is felt that resources will available under the new structure.

#### The Council should:

R1 ensure procedure notes are produced for all business critical systems, including payroll and the housing benefit system.

4. Control accounts check that information held on feeder systems agrees with the main accounting system by reconciling the cumulative balance on the feeder system to the amount on the main accounting system. Our review noted that the sundry debtor reconciliation was not in balance. This control account was reported as having weaknesses in last years report.
5. The control accounts for Council Tax and NNDR do not include the cumulative year position for income and expenditure. This increases the risk that errors will not be picked up on a timely basis, and in appropriate entries made into business critical systems.

#### The Council should:

R2 ensure cumulative reconciliation controls are implemented for the Council Tax and NDR system

6. The bank and cash account is not always being reconciled on a timely basis. At the time of our audit visit in February 2005, the cash account had been reconciled up to November and did not have evidence of review by a senior member of staff. This increases the risk that errors or anomalies will not be picked up on a timely basis. We have been informed that this has now been rectified and reconciliations are on a timely basis, particularly as up to date reconciliations are required for final accounts purposes.

7. This is what we were informed of last year, when we pointed out bank reconciliations were not being completed or reviewed on a timely basis. Concerns over timely reconciliations were also reported in the 2002/3 Annual Audit and Inspection letter. It would appear that the reconciliations are in place for final accounts requirements, and then the system weakens during the year due to pressure on resources. Such reconciliations and their review are a basis element of good governance. Although other controls are in place, they do not offer the level of assurance that is given by timely bank reconciliations and their review.

**The Council should:**

R3 ensure the bank and cash reconciliation is reconciled monthly and reviewed by a senior member of staff

8. Unfortunately the Housing Benefit reconciliation for the year was not available at the time of our audit and had not been completed. The lack of reconciliation of the Housing Benefit payments account has been a problem at the council for a considerable time and could lead to a reduction in the councils Housing Benefit claim.
9. Last year we recommended that Housing Benefit should be added to the control accounts monitoring spreadsheet. This recommendation has not been implemented

**The Council should:**

R4 ensure that Housing Benefit should be added to the control accounts monitoring spreadsheet

R5 ensure the housing benefit control account reconciliation is completed and reconciled monthly during the year.

10. Segregation of duties is a key element of good governance control. Last year it was reported that journal transactions could be input by one person without review by a senior member of staff. We recommended that this situation be reviewed and a suitable control be introduced. If not possible to ensure all journals are reviewed, then a system of sample reviews done monthly could be implemented. All journals that involve the movement of income or expenditure should be reviewed. No action has been taken to introduce the agreed control at the time of our audit visit February 2005. We have been informed that this has been rectified as from March 2005. We will follow up the recommendation given below as part of our 2005/2006 audit.

**The Council should:**

R6 require journals to be subject to review by a separate member of staff to the preparer

Control of access to financial systems is important as unauthorised users may defraud the authority. The authority needs to improve its control of access in the following four systems Cash receipting, Debtors, Creditors and Payroll. The weaknesses the authority has include:

- out of date users left on those systems,
- staff who do not work with the system having access to initiate transactions, such as IT on the legacy system and Internal Audit on salaries, which should have been set up as view only, but was noted by IA to allow changes,

- IT having administration rights to the system that enables them to update master file details, such as bank account changes.

**The Council should:**

R7 review IT access levels to ensure access given is appropriate to the responsibilities of the individual involved and is only to individuals currently employed

**Budgetary control**

11. This refers to the council's ability to monitor its income and expenditure in the year against a plan.
12. We noted that budget reporting to executive has improved to give a summary of the overall position of the council before getting into detailed variances. Improvements can be continued by giving gross income and expenditure positions with explanation of variances in these elements as well. This may also help members when having to adopt the accounts, as they will have been reported to in a similar basis to the accounts during the year.
13. Whilst reviewing variances against budget allows the council to ensure there are no material errors in the main accounting system. We noted two variances where the explanations for variance are not valid.
14. One was the housing benefit payment variance. This showed a £2.2M variance as at the end of period seven on planned expenditure of £7.7M. A variance of this size is material, but there was no clear explanation for it at the time of the audit other than system difficulties. In the context of the failure to produce control account reconciliation, this variance gives cause for concern. A full reconciliation of housing benefit will be required before the audit opinion can be given.

**Closedown plan**

15. This refers to the council's method for producing a set of accounts from the main accounting system.
16. The council has a detailed plan that allocates specific tasks to specific officers on specific dates. There was no step in the plan for senior officer review of working papers. Accounts production and certification dates are being brought forward. If there is no quality control mechanism in the production of working papers. There is a risk that these deadlines will be missed.

**The Council should:**

R8 ensure a step is included in the closedown plan for a senior officer to review the working papers provided to support the financial statements.

**Legality**

17. The role of the monitoring officer is crucial in ensuring that the council's transactions remain within the law. We tested promptness of receipt of reports from other officers by the Monitoring Officer. We were satisfied that major projects and changes were notified to him promptly but that reports on more routine matters may not reach him.

18. During the recent severance negotiations due to the reorganisation of the council, it is unclear that the acting section 151 officer was kept reasonably informed of the basis and proposals being put forward to make the settlement. Although the packages appear to be within the powers of the council, this fact was not known to the section 151 officer until after the decision had been made and agreed with the departing staff member. Although the particular situation was sensitive due to the individual involved, it is important to good governance that proposals that involve costs to the council are clearly communicated to the section 151 officer so that she can ensure the interests of the council are protected.
19. The re-organisation of the council is continuing and the S151 officer needs to be kept clearly informed of cost implications to enable her to carry out this role effectively.

#### The Council should:

R9 consider reminding service heads that reports should be sent to the monitoring officer where there may be a legal implication

R10 consider reminding service heads that reports should be sent to the Section 151 officer where there may be a financial implication

### Financial Standing

20. The council sets a balanced budget and a capital programme within its resources. There are obviously changes in the course of the year to these budgets. These are shown in the budget and capital monitoring reports as appropriate. The budget is based on realistic assumptions.

### Standards of Internal Financial control

21. We have not completed our follow up of the governance report issued in January, but we have been informed that action has been taken to address the concerns reported. We will follow up and report on the issues covered in our governance report as part of the 2005/6 audit.
22. Following up our audit report from last year relating to the up take of reference and Criminal Record Bureau (CRB) Checks for employees we have undertaken further testing in this area. We are pleased to say that the uptake on references for new employees was satisfactory. However there were six casual workers who did not have a Criminal Records Bureau check received before they started work. One of these staff started work at a crèche, although they only stayed one day. The cause of the failure was that personnel had not been notified by managers of new starters. Although the risk is remote, the impact of a single incident occurring is high in terms of public profile.
23. We have been informed that procedures for employing casuals have been placed on the intranet as from February 2004, including CRB requirements. Managers have also been reminded of the need for CRB checks during training course in April 2004. Therefore it was surprising to find non-compliance with these requirements during our audit visit in February 2005. Since then a draft list of defined posts has been circulated by personnel to managers, which should be finalised and on the intranet by 30 July 2005. We recommend that as well as procedures and defined lists, personnel ensure such checks are completed before casual staff are taken.

**The Council should:**

R11 ensure CRB checks are always obtained where the council procedures require it before an employee either permanent or casual is taken on

24. Last year we noted that Operational risk is reviewed quarterly by a separate committee. This meets quarterly and draws in experience from all parts of the council and minutes are kept of decisions made. However, there was no risk register of operational risks faced. Without this document, it is not possible to easily assess the risks the council faces and the actions taken to address them, or the level of potential risk faced. The council should introduce an operational risk register.
25. We also noted that the council needs to ensure it learns from problems other councils have encountered, and that the
26. Council has no systematic way of capturing the problems afflicting other councils across the country and deciding whether it faces a similar risk.
27. In our report last year we made four recommendations concerning the preparation of the council's risk registers. The recommendations included the period of review, the need for an operational register, being specific about actions and the need to learn from risks at other authorities. Unfortunately none of these agreed recommendations have been implemented. The recommendation were that the council should:
  - review the risk register at least quarterly
  - include in the risk register details of actions taken and progress being made to address risks
  - have a risk register for operational risks
  - formalise the manner in which it considers external risks arising at other bodies that could be applicable to the council
28. We have been informed that these have formed part of the response to the Governance report finalised in December 2004, and will be action as part of the response to that report.
29. The council has recently had problems with purchasing officers not following standing orders when letting contracts. We reviewed Internal Audits work on the value of orders going to different suppliers, in order to assess whether orders were being disaggregated to avoid controls.
30. The authority's financial systems make this a difficult and time consuming review. However, the council is employing a procurement officer in its new structure.

**The Council should:**

R12 ensure the procurement officer has the means to monitor disaggregated orders placed with suppliers to enable identification of any potential non-compliance with standing orders

**Standards of financial conduct**

31. We reviewed the council's arrangements for detecting fraud and corruption. The council have an up to date policy and have a fully staffed fraud department with a clear programme of work. Having arrangements in place is not the same as saying that



procedures are followed in every case of alleged fraud. Issues noted above, in some instances indicate weaknesses that increase the risk faced by the council that the arrangements will not be implemented as expected.

32. However, our early review of progress on the National Fraud Initiative (NFI) indicates that Copeland BC has adopted a good practice approach, working with 'Job Centre Plus' and attracting funding from the DWP to assist in the process. We will follow up this initial review later in the year.

## **The way forward**

We recommend the attached action plan to the Audit Committee for consideration

## Action plan

Recommendation	Priority 1 = Low 2 = Med 3 = high	Responsibility	Agreed	Comments	Date
<b>Main Accounting system</b>					
<b>The Council should:</b>					
R1 ensure procedure notes are produced for all business critical systems, including payroll and the housing benefit system.	2	HFBD	Yes	HCS for benefits HPP for payroll	Oct 05 Dec05
R2 ensure cumulative reconciliation controls are implemented for the Council Tax and NDR system	3	HFBD	Yes		Sept 05
R3 ensure the bank and cash reconciliation is reconciled monthly and reviewed by a senior member of staff	3	HFBD	Yes	Following finance restructure	Sept 05
R4 ensure that Housing Benefit should be added to the control accounts monitoring spreadsheet	3	HFBD	Yes	Following finance restructure	Sept 05
R5 ensure the housing benefit control account reconciliation is completed and reconciled monthly during the year.	3	HFBD	Yes	Following finance restructure	Sept 05
<b>Budgetary control</b>					
R6 require journals to be subject to review by a separate member of staff to the preparer	2	HFBD	Yes	Implemented over £30k	Implemented
R7 review IT access levels to ensure access given is appropriate to the responsibilities of the individual involved and is only to individuals currently employed	2	HFBD	Yes		Sept 05

<b>Closedown plan</b>						
R8	ensure a step is included in the closedown plan for a senior officer to review the working papers provided to support the financial statements.	2	HFBD	Yes	Implemented in practice	For 05/06 closedown
<b>Legality</b>						
R9	consider reminding service heads that reports should be sent to the monitoring officer where there may be a legal implication	2	HFBD	Yes	Implemented	Implemented
R10	consider reminding service heads that reports should be sent to the S151 officer where there may be a financial implication	2	HFBD	Yes	Implemented	Implemented
<b>Systems of Internal Financial control</b>						
R11	ensure CRB checks are always obtained where the council procedures require it before an employee either permanent or casual is taken on	3	HFBD	Yes	Implemented	Implemented
R12	ensure the procurement officer has the means to monitor disaggregated orders placed with suppliers to enable identification of any potential non-compliance with standing orders	3	HFBD	Yes	Once in post	When in post

## Acknowledgments

Finally, I would like to take this opportunity to express my appreciation for the high level of assistance provided by Copeland Borough Council staff during the course of the interim audit visit of 2004/2005.