

**MANCHESTER CITY COUNCIL
REPORT FOR RESOLUTION**

COMMITTEE Audit Committee

DATE: 25 June 2009

SUBJECT: Internal Audit Annual Assurance Report 2008/09

REPORT OF: City Treasurer / Interim Head of Internal Audit

PURPOSE OF REPORT

To provide Members of the Audit Committee with the Internal Audit Annual Assurance report for 2008/09.

RECOMMENDATIONS

Members are requested to consider and comment on the Internal Audit Annual Assurance report for 2008/09.

FINANCIAL CONSEQUENCES FOR THE CAPITAL AND REVENUE BUDGETS:

None

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BACKGROUND DOCUMENTS

Interim Head of Internal Audit Annual Assurance Statement

WARDS AFFECTED N/A

IMPLICATIONS FOR KEY COUNCIL POLICIES

<u>Anti-poverty</u>	<u>Equal Opportunities</u>	<u>Environment</u>	<u>Employment</u>
None	None	None	None

2008/09 Internal Audit Annual Assurance Report

1. Background to report

- 1.1. The Chartered Institute for Public Finance and Accountancy Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 (The CIPFA Code) established the expected professional standards for internal audit in local government. The CIPFA Code is informed by standards from other professional institutes, including the Institute of Internal Auditors (IIA) and the Government Internal Audit Standards (GIAS) issued by HM Treasury, and is the standard against which the quality of internal audit in local government is assessed.
- 1.2. The CIPFA Code sets out the requirement for reporting to officers and Members of the Audit Committee to help inform their opinions on the effectiveness of the system of internal control as well as risk management and governance arrangements.
- 1.3. This responsibility was discharged through the presentation of the Interim Head of Internal Audit's Annual Assurance Statement to Audit Committee in May 2009. The statement reported that, except for a small number of significant issues that were raised in the report, **substantial** assurance could be provided that the Council's systems of governance, risk management and internal control were generally sound and operate reasonably consistently across departments in the year. This statement was supported by the work delivered in the 2008/09 Internal Audit Plan and this report summarises the audit opinions issued through this work. It is presented to Members of the Audit Committee for their consideration and comment.
- 1.4. This report does not focus on the performance of Internal Audit in the year. This has been considered by the City Treasurer as part of the Review of the Effectiveness of the System of Internal Audit. The annual review of the performance of Internal Audit will be presented to Audit Committee in September alongside benchmarking data that is currently being collated across Greater Manchester and the core cities groups.

2. Assurance Reports

- 2.1. Audit activity that has resulted in the issue of assurance opinions in the period and the key issues emerging from this work are set out below. This work has been categorised by Internal Audit teams, that broadly reflect the structure of the Council's directorates.

3. Corporate Services

Financial Systems

- 3.1. The focus of Internal Audit's work in relation to Corporate Services in the year related to audits of the core financial systems. A number of reviews identified the need to develop management monitoring and review processes to help support performance improvement. This was particularly the case for debt recovery in respect of sundry income and Council Tax.










- 3.2. Given the move to personnel / payroll and financial shared service centres and changes in the way financial systems and processes at the Council are being developed to improve efficiency a number of the systems we audited were in a process of transition. As a result of this we identified the need to ensure clarity of roles and responsibilities and develop improved segregation of duties and these should support improved systems of control in 2009/10.
- 3.3. The moderate assurance opinion on revenue budget monitoring was based on the fact that the Council's overall budget is monitored adequately and there are a range of effective strategies to ensure that services are delivered within the overall corporate and directorate budgets. Work is ongoing to develop and embed budget monitoring arrangements and we are aware of significant ongoing activity in this area that should deliver the improvements recommended in the report. Similarly on capital budget monitoring we concluded that the Council has overall robust arrangements to ensure that the budget is monitored and reported on a timely basis to support effective decision making.
- 3.4. The embedding of SAP in business processes continues to present challenges to the efficient and effective operation of a consistent approach to revenue and capital budget monitoring. The Business Support Team continues to support SAP development across the Council and it is increasingly recognised as the tool to support an integrated business management approach.
- 3.5. Overall our work supports the conclusion that controls over the core financial systems are generally sound and operating as intended.




















Non-Financial Systems






- 3.6. The focus of non-financial work in the Corporate Services team was on asset management and aspects of procurement. We noted the good progress made in the development of the corporate landlord role and based on a review of backlog maintenance can provide moderate assurance over this aspect of the Council's asset management arrangements.
- 3.7. We provided moderate assurance over the Council's overall arrangements in delivering the service delivery phase of PFI contracts with the primary focus for improvement being the development of clarity of responsibilities and a consistency of approach across the Council. This issue has been accepted by management and plans are being developed to positively address this risk. Moderate assurance was provided over the arrangements for corporate contract monitoring reflecting the need to develop controls to ensure the consistent monitoring of supply and service contracts across the Council. Our work on three capital framework contracts has been completed and an assurance opinion will be agreed and issued to management by the end of June.
- 3.8. We provided limited assurance over the arrangements in place to ensure the consistent application of the approved project management methodology on capital projects.





ICT Audit

- 3.9. Much of the planned work on the audit of the Council's ICT systems was deferred to 2009/10 as the timescale for completion coincided with the Conficker virus incident.
- 3.10. Work that was completed in previous years and in 2008/09 did identify concerns. Our most recent penetration testing review reconfirmed a number of significant areas for development in the arrangements for server patching and the resilience of ICT systems. This was demonstrated by the disruption caused by the virus. The Council is now aware of these issues but the resilience and integrity of the ICT infrastructure at the Council presents an ongoing risk to the achievement of objectives.
- 3.11. Moderate assurance can be provided from a review of e-mail usage. Areas for improvement include the management of e-mail accounts, monitoring of the use of web mail and encryption of e-mails sent from Blackberrys. Encryption and data security was an issue highlighted in October 2008 when the Council suffered the theft of an unencrypted laptop computer containing payroll data. This resulted in the public disclosure of the incident and communications are continuing with the Information Commissioner's Office in respect of the Council's response.
- 3.12. In summary there have been two significant governance, risk management and control issues relating to ICT that impact on our ability to give other than limited assurance. The issue of information governance is not an ICT responsibility but ICT solutions will need to support effective management of data across the Council. Positively the Council has appointed an Interim Strategic Head of ICT and has developed and approved both an Information and ICT strategy. The successful implementation of these strategies should mitigate the risks that have emerged this year and offer the opportunity for sustained service improvement.

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
Financial Systems			
Benefits	Final	Substantial 	
National Non Domestic Rates	Final	Substantial 	
Council Tax	Final	Moderate 	
Income Systems	Final	Moderate 	
Treasury Management	Final	Substantial	

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
			
Creditor payments	Final	Moderate 	
SAP Payroll	Final	Substantial 	
Cash / Income Collection and Receipting	Final	Substantial 	
Systems Reconciliation	Final	Substantial 	
Asset Management	Final	Substantial 	
Capital Budget Monitoring	Final	Substantial 	
Revenue Budget Monitoring	Final	Moderate 	
Access to Academy	Final	Substantial 	
Purchase Card (Review of Expenditure Approval)	Final	Limited 	










Non-Financial Systems			
Corporate Contract Monitoring	Draft	Moderate 	tbc
Partnership Service Delivery in PFI	Draft	Moderate 	tbc
Project Management Methodology	Final	Limited 	
ERDF	Final	Management 	N/A

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
		letter	
Use of Framework Contracts	Draft	tbc	tbc
ICT			
ICT: SAP Basis	Final	Limited 	
ICT: E-Mail Policy	Draft	Moderate 	tbc
ICT : External Penetration Testing	Draft	No 	tbc

4. Regeneration

- 4.1. Substantial assurance can be provided over the programme and project appraisal and approval processes that ensure the Housing Market Renewal programme was being delivered in accordance with grant terms and conditions.
- 4.2. Following on from issues raised in 2007/08, Internal Audit support was requested in respect to review specific aspects of two ERDF funded projects. This identified concerns over the Council's Accountable Body arrangements and the risk of financial clawback. Senior Officers within Regeneration recognise the need to establish a robust assurance framework to ensure compliance with terms and conditions of funding.
- 4.3. We were unable to provide any assurance that the Council's Urban Traffic Control Section had effective financial management arrangements. Of particular concern was the lack of procurement processes for the delivery of works. Action is being taken and we consider this should address the concerns raised.
- 4.4. We can provide moderate assurance over the operation of Section 106 arrangements, ensuring developments are aligned to the Council's strategic and corporate aims and objectives. However, it is recognised that improved monitoring processes need to be developed to ensure obligations are in fact delivered. A full report to Scrutiny Committee that will include actions to address these risks is being presented in July.
- 4.5. The review of heritage assets (art works and rare books) identified a need for the development of an overall Council strategy for the management of these assets and the establishment of specific asset management plans within libraries and galleries to minimise the risks of loss, damage and potential for theft.

4.6. Within the homelessness audit we focused on partnership working, use of management information and management of risks. In these areas there were a number of areas for improvement. We are aware that steps are being taken to improve the governance arrangements with strategic partners and should help develop the arrangements in place to achieve strategic objectives and government targets in respect of reducing the use of temporary accommodation

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
Urban Traffic Control	Final	No 	
Housing Market Renewal	Final	Substantial 	
Heritage Security	Draft	Limited 	tbc
Manchester Adult Education Service	Draft	Moderate 	tbc
District Strategic Regeneration Frameworks	Draft	Substantial 	tbc
Planning Service – Section 106 Agreements	Draft	Moderate 	tbc
Homelessness	Draft	Moderate 	tbc

5. Children's Services







5.1. Internal Audit reports in respect of Children's Services relate to the Children's Services Directorate as well as to schools. It is important to note that for schools the assurance opinions and assessment of risks are within the context of the school and whilst areas for development may be important at a school level they do not necessarily reflect significant risks to the Council as a whole.



Children's Services

5.2. We gave moderate assurance over the operation of the district model, concluding that there were robust arrangements for co-ordinating work and decision-making, including delegated decisions. However, a clearer framework of accountabilities and roles and responsibilities was needed for District and Deputy District Managers. The Education Services redesign audit concluded that a clear strategic direction had been set but that action was needed to

monitor and evaluate the activity of School Effectiveness Officers and to ensure that resources were targeted on the highest priorities.

- 5.3. We provided limited assurance that external funding was managed effectively. A strategic approach was being developed and some good practice was demonstrated, although we were concerned that non-compliance with grant conditions could have left the Council liable to funding clawback. Youth Services controls were partially effective in facilitating delivery of key outcomes, and areas for development included management of performance against key objectives and planning. Initial findings on Council activity over children missing from education indicated the need for formal, up-to-date policies and procedures, better case management and effective data monitoring.
- 5.4. The audits of school budgets and procurement identified a number of areas for improvement. These emphasised the need to develop further develop policies and procedures to help support schools' financial management arrangements and the need for schools to implement mechanisms to ensure compliance with expected standards for procurement and budgetary control. In each of these audits we issued a report to Children's Services and also wrote to each the schools visited to emphasise the areas for development.
- 5.5. The 'Building Schools for the Future' programme was being effectively managed, but with room for improvement in benefits realisation. Similarly, the Sure Start programme operated effectively but we made recommendations in respect of risk and performance management and data quality. Procurement controls over out-of-city placement of children with special educational needs needed improvement but we acknowledged the progress made.
- 5.6. The work on the Annual Pupil Census and City Learning Centres was issued in the previous reporting format but the assurance opinions for these are considered to be moderate and limited respectively.

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
Annual Pupil Census	Final	Moderate 	N/A
City Learning Centres	Final	Limited 	N/A
School Budgets	Final	Moderate 	
Procurement in Schools	Draft	Limited 	tbc
Building Schools for the Future	Draft	Substantial 	tbc

District Model – Delegations	Draft	Moderate 	tbc
Education Service Redesign	Draft	Substantial 	tbc
Children Missing from Education	Draft	tbc	tbc









Schools

- 5.7. We completed external assessments of 39 primary schools against the Financial Management Standard in Schools (FMSiS). Of these, 24 met the Standard, 11 did not and we are awaiting further evidence for four more. Schools that did meet the Standard were more aware of, and better prepared to meet, the requirements. Reasons for schools not meeting the Standard included the need for:
- the submission of higher quality information to school governors, for example budget monitoring reports;
 - evidence of compliance with regulations and procedures, for example in the procurement process; and
 - governing bodies to demonstrate active scrutiny and challenge.
- 5.8. The 37 primary schools on the audit plan to March 2009 were audited and we can give assurance that most schools understand and operate governance and financial management controls satisfactorily. While there is a need in many for some improvement, several required more fundamental development. Audit findings largely mirrored findings from FMSiS and included the need for more effective:
- cashflow forecasting and budget monitoring;
 - procurement, including compliance with Schools Financial Regulations;
 - segregation of duties and authorisations over income and procurement; and
 - governing body approval, scrutiny and challenge of decision making.
- 5.9. For all FMSiS assessment and school audits we have made recommendations for improvement and will prepare a summary findings report for Education to help address common themes and concerns.
- 5.10. Audits of secondary schools have identified some issues of concern around procurement and financial management. Particular concerns have been noted around the transition of secondary schools to academies and we are currently working with Education to address these risks.
- 5.11. We reported the need for the Council's governor, school support and finance functions to work with schools to address these issues. We also acknowledged that improvement actions were being progressed through Governor and Head Teacher support and School Effectiveness Officers. Our audit of procurement





















activity in schools provided limited assurance and we were particularly concerned at the lack of compliance with financial regulations, which we also considered to need updating.















































- 5.12. As noted above reviews of budget monitoring and procurement identified a number of areas of concern, particular around non compliance with schools financial regulations. Concerns included a lack of governor engagement in financial management and procurement decisions, non compliance with tendering requirements and ineffective segregation of duties in purchasing processes. One of the difficulties the Council faces is ensuring consistency of approach across schools and we recognise that the Education Service is working to help schools address these risks.
- 5.13. We take some assurance from the completed School Governance Project, which introduced more effective tools for communicating with governors and a clerking service for schools. Internal Audit will continue to work with Education on their Manchester Challenge funded governance project, which aims to introduce more fundamental change to whole-school governance during 2009.

Secondary Schools

School	Assurance Opinion	Capacity to Improve	School	Assurance Opinion	Capacity to Improve
St Paul's Catholic High School	Moderate 		Whalley Range High School	Substantial 	
North Ridge High School	Moderate 		The Barlow RC High School	Moderate 	









Primary Schools

School	Assurance Opinion	Capacity to Improve	School	Assurance Opinion	Capacity to Improve
Barlow Hall Primary School	Substantial 		St Joseph's	Moderate 	
St Anthony's Primary School	Moderate 		St Clement's	Moderate 	
The Grange School	Moderate 		Old Hall	Substantial 	
Higher Openshaw Primary School	Moderate 		Green End	Moderate 	
Ashgate Specialist School	Moderate 		Ladybarn	Substantial 	







School	Assurance Opinion	Capacity to Improve	School	Assurance Opinion	Capacity to Improve
Crosslee	Moderate 		St Ambrose	Moderate 	
St Cuthbert's	Substantial 		Ashgate	Moderate 	
Crab Lane	Moderate 		Rolls Crescent	Limited 	
St Wilfird's, Northenden	Moderate 		Charlestown	Moderate 	
Plymouth Grove	Moderate 		Moston Lane	Moderate 	
All Saints	Moderate 		Broad oak	Moderate 	
St Mary's RC Levenshulme	Moderate 		St Chrysostom's	Moderate 	
The Birches	Moderate 		The Manchester Federation	Limited 	
Heald Place	Moderate 		Bowker Vale	Moderate 	
St Mary's CofE	Limited 		Armitage	Limited 	
Benchill	Limited 		Brookburn	Moderate 	
Holy Name	Moderate 		St John's RC	Limited 	
St Peters Catholic Primary	Moderate 		Manchester Hospital Schools and Home Teaching Service	Substantial 	
St Bernard's	Moderate 				

6. Neighbourhood Services

- 6.1. An audit of the Council's Business Continuity arrangements delivered moderate overall assurance but reported major concerns over the nature and extent of testing activity. On Individual Budgets we gave moderate assurance that budget allocation operated effectively and over the effectiveness of the audit process, although we had concerns over completion and evidencing and recommended improvements to guidance, audit risk assessment and recovery action. The care provider monitoring audit gave substantial assurance over monitoring of contracts and management information but recommended improvements in the quality of, and compliance with, procedures. We provided moderate assurance over the system for safeguarding adults concluding that Safeguarding Board governance, staff training and compliance with policies and procedures needed attention.
- 6.2. The audit of the Drug and Alcohol Strategy Team (DAST) has identified a need to establish formal contractual arrangements with a number of service providers and implement controls to ensure the effective and efficient monitoring of these contracts.
- 6.3. Initial findings from work on MiCare indicated the need for improved risk management but also identified an active, business-led approach to resolving some of the user and functional issues which were impacting adversely on implementation. Further work is planned in 2009/10 to review the effectiveness of this activity.

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
Older People Care Provider Monitoring	Final	Substantial 	N/A
Individual Budgets (Update – Audit Arrangements)	Final	Moderate 	
Adult Protection (Adult Social Care)	Final	Moderate 	
Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
Business Continuity Planning	Final	Moderate 	
Drug and Alcohol Strategy Team (DAST)	Draft	Moderate 	tbc
Antisocial Behaviour and Respect Agenda	Final	Management letter	N/A

7. Performance and Governance

Audit Area	Audit Status	Assurance Opinion	Capacity to Improve
LPSA2 Certification	Final	Certification issued	N/A
Comprehensive Area Assessment	Advice, guidance and support		
Corporate Performance Management – Business Planning	Advice, guidance and support		
Annual Governance Statement	Advice, guidance and support		
Annual Governance Statement	Final	Substantial 	
Manchester Partnership	Draft	Substantial 	
Thematic Partnerships	Draft	Substantial 	tbc
National Indicator Set	Draft	Moderate 	tbc
Value for Money (Strategy)	Draft	tbc	tbc

Performance

- 7.1. Our audit of performance indicators provided substantial assurance that performance was managed effectively, delivering accurate, consistent and complete results. Moderate assurance was given on delivery against the National Indicator Set with recommendations for more consistent application of remedial action planning and pro-active work to influence annual and survey based indicators. Discussions are ongoing with management as to how Internal Audit can provide effective support to the developments in this area in 2009/10.
- 7.2. We certified a number of LPSA2 targets following work to demonstrate that reported results fairly represented performance and supported Performance Reward Grant claims.
- 7.3. We have been involved in the review of business planning arrangements during the year and progress contributes to be made in the development of business plans. The challenge and support processes in 2008/09 were comprehensive and added value to the final business plans. The Council has begun to develop a self assessment processes that links to business planning and proposes a further review of arrangements in 2009/10 as recognition that effective business planning is critical in the effective management of performance and the achievement of objectives.
- 7.4. Our emergent findings on the review of value for money arrangements suggest that the Council has a wide range of mechanisms for the identification and

achievement of value for money. The review will likely recommend the establishment of a value for money framework including identification of a corporate lead for value for money at SMT level to ensure the effective and efficient coordination of the Council's approach.

Governance

- 7.5. Responsibility for the Council's governance arrangements was assigned to an SMT sub-group. Improvements include the publication of a Handbook for Leaders, adoption of a Council Code of Corporate Governance and the partnership governance framework.
- 7.6. Internal Audit worked closely with Financial Management to give assurance over the process for producing an Annual Governance Statement. This included a comprehensive assessment of compliance with the principles of the Council's Code of Corporate Governance. Further work is imminent which will give an opinion on the accuracy and completeness of Head of Service supporting statements.
- 7.7. The Manchester Partnership audit gave substantial assurance over the effectiveness of partnership governance, though risk and performance management needed development. The audit also reported that the partnership governance framework was developing well, giving assurance that external evaluations of self-assessments were consistent, reliable and accurate and noting plans to introduce monitoring and reporting arrangements. The framework consolidated the Council's knowledge of its partnerships but further work was needed to inform a view of the impact on governance in individual partnerships. This work was followed by a Thematic Partnership audit which, while identifying good practice in some, reported the need for more consistency of approach, clearer links between partnership activity and LAA deliverables and improved performance management and reporting.

8. Investigations

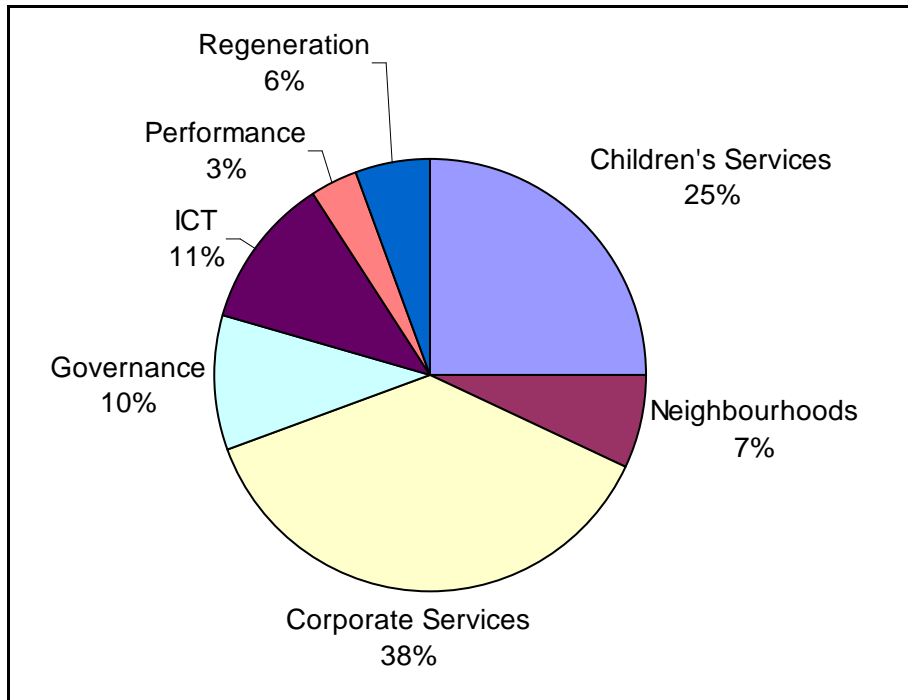
- 8.1. No organisation can guarantee that it will be free from fraud or financial irregularity, the extent of which can be a measure of the effectiveness of internal controls. Internal Audit has carried out a number of investigations referred during the year, either independently or by offering advice and support to managers and investigating officers. The work included examination of potential fraud and corruption, theft of money and poor management practice. Reports have been provided to relevant managers and recommendations for action and system improvements made as necessary.
- 8.2. Work has included facilitation of the National Fraud Initiative exercise and whilst a number of matches have been identified for review the review is at an early stage and there are no matters of significant concern.
- 8.3. Support has been provided in the investigation of staff in cases of alleged financial misconduct. These investigations have identified control and compliance issues that expose the Council to potential financial, regulatory and reputational risks. Steps have been taken to improve the systems of control but further audit work will be required in this area in 2009/10.

- 8.4. As in 2007/08, a number of investigations have been conducted at schools supporting Education, concerning issues such as theft, adequacy of financial management arrangements and probity.

9. Recommendation Monitoring and Implementation

- 9.1. A revised approach to the monitoring of implementation of audit recommendations was introduced in 2008/09. This clarified the responsibility of managers and of Internal Audit as well as the timescales for reporting. This process and the positive engagement on this matter by the Strategic Management Team and the Audit Committee has helped reinforce the importance of recommendation implementation. A number of particular examples have emerged in the year that demonstrate a heightened level of management engagement in this process.
- 9.2. The pace of change across all services at the Council is a challenge as specific recommendations can be superseded by changes in structures, systems and processes. In some areas there has been a lack of resource capacity to deliver planned solutions and the need to secure additional resources for implementation is now formally recognised in audit reports.
- 9.3. At 30 May 2009, 111 recommendations from 2007/08 and 2008/09 had been implemented. 20 recommendations had been mitigated by other means and four had been reported as implemented by management and are awaiting Internal Audit validation. Seven recommendations have been referred back to management as they were more than 12 months past their due date. These seven related to recruitment. Internal Audit are satisfied that the outstanding risks and recommendations should be addressed within the recruitment service improvement project in 2009/10. All are classed as medium risk and have been referred back to management.
- 9.4. There are 88 recommendations past their due date but not yet implemented. This compares to 124 recommendations that were past their due date at 31 December 2008.
- 9.5. 15 of the 88 outstanding recommendations, including recommendations on ICT, related to audits from 2007/08 and were classed as high risk. There were no outstanding critical or major recommendations from 2008/09 and just nine significant issues, of which six relate to the recent reviews of payroll and council tax.

Diagram 1 - Outstanding Recommendations by Directorate / Area



9.6. Overall, a high number of outstanding recommendations remain but the majority have not been overdue for long. The progress in implementation has improved and whilst follow-up on progress of implementation will continue, Internal Audit considers that appropriate actions are being taken to address recommendations in most business areas.

10. Conclusion

10.1. Members are asked to consider and comment on the Internal Audit Annual Assurance Report.