

Committee: Performance Select Committee

Agenda Item

Date: 05 February 2008

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Title: Revised Working Arrangements between
Internal Audit and Audit Commission

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Item for
information

Summary

This report presents the revised working arrangements between the Finance Section, Internal Audit and the Audit Commission to provide assurance on future Budget Setting and Budgetary Control, Monitoring and Management. It also includes a Joint Working Protocol with the Audit Commission which summarises the key actions that the Authority, Internal Audit and external audit agree to undertake.

Recommendations

That members note the report and the UDC Joint Working Protocol.

Background Papers

UDC Joint Working Protocol (attached)

Impact

Communication/Consultation	The report has previously been circulated amongst relevant officers and the Audit Commission
Community Safety	None identified
Equalities	None identified
Finance	This document outlines the future Budget Setting and Budgetary Controls auditing processes
Human Rights	None identified
Legal implications	There are no specific legal implications

Sustainability	None identified
Ward-specific impacts	None identified
Workforce/Workplace	None identified

Situation

Events over the past few months at the Council have led to serious shortcomings in the Council's budget-setting, budgetary control and financial management arrangements becoming apparent. The Council overspent its 2006/07 budget by some £770k, and subsequent detailed review of the 2007/08 budget initially estimated a budget shortfall of £1.2m, which has subsequently been revised to a shortfall of £938k (even after additional savings of some £550k have been taken into account). A forecast for 2008/09 showed a budget gap of some £1.8m, and the Council has taken emergency steps to reduce staff costs by £1m by 31 March 2008, as part of a package of measures to bridge the gap for 2008/09.

The reasons for the problems that the Council has experienced have been explored in a number of previous reports prepared and presented to the Council and committees of the Council at various times over the last six months, and are not repeated in detail here, but they include the omission of items that should have been included in the budget; double-counting of some items; erroneous assumptions underpinning key estimates; and projected savings that have not been achieved.

Against this backdrop, Internal Audit and External Audit have met the Council Chief Executive and acting Chief Finance Officer to discuss the roles that each can play in seeking to put in place more robust systems and processes of budgetary control and financial management at the Council, with the objective of providing assurance to the Council and seeking to mitigate the risks of problems arising in the future.

Internal Audit

Budgetary control work proposals

The responsibility for Budget Setting and Budgetary Control, Monitoring and Management rests with the Finance Section, Management, Budget holders and Members and historically this area has been assessed as being of low to insignificant risk to the ability of the Council to achieve its objectives.

Previous Internal Audit plans have not included separate budget or budgetary controls audits, at either corporate or operational level, instead concentrating on

service budget control and management as a generic part of all internal audits of specific service areas.

Budget Setting and Budgetary Control, Monitoring and Management is now considered a high risk area as a result of the errors identified in the 2007-08 budget setting process.

The Council is now operating under tight financial constraints making it critical that its budgetary needs are predicted with the greatest accuracy possible and that effective controls are in place to ensure that expenditure is managed within approved totals and that income due is pursued.

For Internal Audit to be able to provide assurance that robust controls are now in place, it is proposed that the following three levels of audit are undertaken by Internal Audit as part of its 2008-09 Audit Plan:

1. Corporate Budget
2. Budget Monitoring and Reporting
3. Service Budget Control and Management

Audit Objective

The objective for audit of these three areas is to gain adequate assurance that the key risks for the Council in terms of setting, monitoring and managing budgets have been identified and that proper controls are in place and are effective.

Audit Scope

1. Corporate Budget

20 audit days to be allocated in October / November 2008 to focus on the budget setting process and provisional decisions being taken for the 2009-10 budget. Depending of the level of assurance assessed for the 2009-10 budget setting process, the number of audit days allocated to this area will be reviewed and adjusted for accordingly in the 2009-10 and subsequent audit plans.

Potential Risk Areas to be considered during the audit:

- Budgets setting process does not provide clarity as to accountability of budget holders, service managers and others authorised to commit expenditure or tasked with income collection;
- Budgetary structures and procedures fail to promote the delivery of corporate priorities;

- Budgets calculations do not take into consideration all relevant financial and operational information available to the Council;
- Risks associated with budgeting assumptions are not formally identified or considered at an appropriate level;
- Budgets are inaccurately calculated;
- Lack of adequate working papers to support the make-up of the budget;
- Budgets are not subject to any formal review or approval at the appropriate level;
- Lack of documentary evidence to support the approval of the budget at the appropriate level.

2. Budget Monitoring and Reporting

In view of the new cyclical system of budget management reporting to be introduced in June 2008, Internal Audit will allocate 15 audit days from September 2008 to March 2009 for reviewing the new procedures and provide assurance on their effectiveness. The number of audit days allocated to this area will be reviewed and adjusted for accordingly in the 2009-10 and subsequent audit plans.

Potential Risk Areas to be considered during the audit:

- Any adjustments to approved budgets are not properly authorised or recorded;
- Budget information is not made available to budget holders in good time or not in a format that allows for effective monitoring;
- Budget monitoring processes do not provide for the timely identification, investigation and reporting of significant budget variances;
- Budget reports are not regularly received by strategic management together with relevant contextual information to allow for informed performance appraisal;
- The appropriate member committees do not receive budget monitoring information that is accurate, relevant, understandable and consistent with underlying records, and data is not as up to date as possible when reported;

- Inappropriate or ineffective IT controls are in place.

3. Service Budget Control and Management

In addition to the above, Internal Audit will continue to undertake budget control and management testing for all service areas audited from the 2008-09 Internal Audit plan.

Audit Commission

Budgetary control work proposals

In considering the role that External Audit can play in the overall assurance that the Council can receive in respect of the budgeting and financial management processes, regard has been taken of the initiatives that the Council are taking to strengthen and improve the quality and robustness of their own systems and procedures, as well as the work that Internal Audit propose to carry out as set out above. This is to ensure that audit resources are directed to the areas of highest risk and where the greatest additional value can be derived, and that duplication and overlap are kept to a minimum.

In the context of the Internal Audit proposals set out above, the Audit Commission would propose to carry out the following pieces of work:

1. Undertake a review of the Council's revised Medium Term Financial Strategy (MTFS) when it is produced in March 2008. This will include compliance against the 'Use of Resources' key lines of enquiry, best practice identified from other councils, and learning from key publications such as 'World Class Financial Management'.
2. Carry out a review of the adequacy of the Council's new budgetary control arrangements being introduced in June 2008. This will include an analysis of the Council's current financial management arrangements using the Commission's 'Better Budget Management Toolkit' to identify specific areas for improvement.
3. Review the work to be carried out by the Internal Audit team on the Council's budgetary control as set out above, with a view to placing reliance on that work and also forming a conclusion on the adequacy of the Internal Audit review.

The detailed scope and timing of these pieces of work will be discussed and agreed with relevant officers of the Council.

In addition, the financial diagnostic review being undertaken by Bill Roots for the Council may identify further issues that external audit may want to follow up on, or undertake further work – for example, if there are specific areas of weakness identified. Once the outcomes of this review are known, any proposals for further work will be agreed with officers.

Risk Analysis

Risk	Likelihood	Impact	Mitigating actions
The key risks for the Council in terms of setting, monitoring and managing budgets have not been identified and that proper controls are in place and are effective	1 - Little or no likelihood	4 - Catastrophic effect – immediate action required	Internal Audit plan provision for Budget Setting and Budgetary Control Audits Audit Commission external audit plan Performance Select Committee