

## **AUDIT COMMITTEE**

### **Minutes of a meeting of the Audit Committee held on Monday, 27th June 2011 at 6.00 pm in the Reception Suite, Civic Offices, Telford**

**PRESENT:** R.K.Austin (Vice-Chairman acting as Chairman for the meeting), I.T.W.Fletcher, R.J.Sloan, W.L.Tomlinson and C.R.Turley.

**Officers:** P.Clifford (Corporate Director), J.Eatough (Head of Governance), P.Harris (Corporate Finance Manager), J.Marriott (Audit & Assurance Service Delivery Manager) and A.Roberts (Democratic Services Officer).

**Also Present:** A.Cardoza and A.Bunting – KPMG External Auditors.

#### **AUC-1      MINUTES**

**RESOLVED** – that the minutes of the meeting of the Audit Committee held on 22nd March 2011 be confirmed and signed by the Chairman.

#### **AUC-2      APOLOGIES FOR ABSENCE**

D.G.Davies (Chairman)

#### **AUC-3      DECLARATIONS OF INTEREST**

Councillor I.T.W.Fletcher declared a personal interest in relation to minute reference AUC-9 in that he was a member of the Management Committee of the Priorslee Community Centre. He also declared a personal interest in connection with minute reference AUC-11 as he was a governor of Adams Grammar School.

Councillor W.L.Tomlinson declared a personal interest in relation to minute reference AUC-9 in relation to the Shawbirch Community Centre.

#### **AUC-4      REVIEW OF THE TERMS OF REFERENCE FOR THE AUDIT COMMITTEE**

The Audit & Assurance Service Delivery Manager reminded members verbally that it had been agreed through the Constitution that every Committee would at its first meeting following the Annual Council Meeting review the committee's terms of reference. Members were advised that no amendments to the terms of reference were proposed currently but once the revised arrangement in respect to local public were confirmed they would be further reviewed. Accordingly, it was;

**RESOLVED** – that following the review that had been conducted by the Audit & Assurance Service Delivery Manager and the consideration by the Committee it was formally agreed that no amendments to the Terms of Reference of the Audit Committee were required.

## **AUC-5      KPMG INTERIM AUDIT REPORT – 2010/11**

The report from KPMG was received which summarised their key findings that had arisen from the interim audit work in relation to the 2010/11 financial statements.

The Committee was informed that during February – March 2011 KPMG had completed their planning and control evaluation work. This work included a review of the Council's general control environment including the IT systems; testing of certain controls over the Council's key financial; an assessment of the Internal Audit function and its work; review of the Council's accounts production process and a review of the Council's work to restate the 2009/10 financial statements under IFRS.

The report outlined a summary of the headline messages within Section 2 of the report and Section 3 outlined KPMG's key findings from their interim work in relation to the 2010/11 financial statements. Members were further referred to their recommendations within Appendix 1 of the report. The Committee were also informed of KPMG's review of the Council's implementation of their prior recommendations.

Members were informed that KPMG had assessed the controls over the key financial systems were generally sound. However, it was reported that there were some weaknesses in relation to non-pay expenditure and financial reporting (in relation to journals).

The Committee were also advised of their key findings in connection with their review of Internal Audit, where it was assessed that Internal Audit fully complied with the Code of Practice for Internal Audit in Local Government. It was reported that no significant issues had been identified and that they were able to place full reliance on Internal Audit's work on the Council's key financial systems.

Councillor Tomlinson commented that he was pleased to see that there were no major issues outlined within the report. He did enquire in relation to the implementation of the new Financial System as to whether KPMG had undertaken any work in respect to the system's implementation. By way of response the meeting was informed that they were not directly involved with the implementation of Agresso which was due to "go live" on 4th July. Councillor Fletcher enquired as to whether the implementation of the new financial system had been placed on the Strategic Risk Register, particularly in his view that this would be considered as containing elements of high risk. The Corporate Director advised that it was not considered as such a strategic item but was included in the key strategic risk in respect to resources (including financial resources). Members were informed that there was a Project Risk Register.

**RESOLVED** – that the contents of the KPMG Interim report for 2010/11 be noted.

## **AUC-6      KPMG AUDIT PLAN AND FEE LETTER – 2011/12**

The Committee received the Annual Audit Fee Letter – 2011/2012 that had been received from KPMG. Members were referred to the letter that outlined the audit

work that would be undertaken by KPMG for the 2011/12 financial year together with the fee that was proposed to be charged to the Council. The proposals for the anticipated work were based on the risk based approach to audit planning as set out in the Code of Audit Practice and work mandated by the Audit Commission. Members were further informed that as KPMG had not completed the audit for 2010/11 the audit planning process for 2011/12 including the risk assessment would be continued as the year progressed with the fees being reviewed and updated as necessary.

The Committee was informed that the Audit Commission had published its work programme and scale of fees for 2011/12. The letter stated that the Audit Fee was based on a fee that was charged by reference to a scale of fees dependent on the size and complexity of the Council, and that based on this the indicative fee for 2011/12 was £258,480 (plus VAT). Members were informed that this proposed fee was a significant reduction of 10% when compared to the previous fee of £287,200 that had originally been planned for 2010/11.

The letter further indicated that the 2011/12 scale fee reflected significant reductions from the new approach to the Value for Money audit which had resulted in a reduction of the volume of work had reduced compared to the previous use of resources scored judgements regime. Fees had also been reduced because a number of the additional audit costs associated with the introduction of the IFRS were not present in the ensuing year.

Members were referred to Appendix 1 of the letter which outlined a number of assumptions upon which the indicative fee had been based. KPMG also advised the Committee that the setting of the proposed figure was also based on a similar level of risk that had been identified for 2010/11, except for the IFRS system implementation. KPMG indicated that a separate audit plan for the 2011/12 financial statements would be issued later in the year, which would identify the planned audit processes and, if required any changes to the fee. Any further changes would be reported to the Audit Committee in due course.

The Committee was informed that the proposed fee would exclude any additional work which it may be agreed that KPMG would undertake, which would be subject to further discussions. In connection with certification of the 2011/12 grants and returns the estimated fee was an additional £35,000. The final fee in this respect would depend on a number of factors that could not be predicted with any certainty at this stage but would include the number and nature of the schemes which would require certification.

**RESOLVED – that the Audit Plan and Fee Letter – 2011/12 as prepared by KPMG – External Auditors be noted.**

#### **AUC-7      KPMG VALUE FOR MONEY AUDIT PLAN – 2010/11**

The report of KPMG was received which sought to describe how the new Value for Money (VFM) Audit approach would operate. The report also set out KPMG's revised risk assessment for their VFM conclusion. The Committee were informed on the Audit Commission's Code of Audit Practice (the Code). This Code summarised

the responsibilities into two objectives on which they were required to review and report on the Council's use of resources and the financial statements.

Members were advised as to the VFM audit approach and how it was structured around two criteria as outlined within the report. This criteria replaced the previous ten criteria/key lines of enquiry under the previous UoR audit regime.

In connection with the assessment of identified risks it was outlined as how these risks would impact on their VFM assessment. The risks that had been identified were Managing with less; Restructuring and Service Review Programme; Capital Programme; Single Status and the Railfreight Terminal.

The report indicated that due to the current economic climate the financial environment in which the public sector operated had changed significantly with the state of the public finances and the scale of funding cuts had led to increased pressure on public spending. In response to this the Audit Commission had introduced a new approach to local VFM work at these bodies which had previously been subject to a UoR assessment. It was now required to focus the audit on planning work based on consideration of the significant risks of giving a wrong conclusion (audit risk) and undertake only as much work that was appropriate to enable them to provide a safe VFM conclusion.

KPMG advised the Committee that the VFM audit would draw heavily on other audit work that was undertaken which was relevant to their VFM responsibilities together with the results from last year's VFM audit. From this initial work they would then form an assessment of the residual audit risk to identify the areas where more detailed VFM work was required. The report also contrasted the differing sections of the VFM audit.

**RESOLVED – that the Value for Money Audit Plan for 2010/11 as prepared by KPMG – External Auditors be noted.**

**AUC-8      TREASURY MANAGEMENT – 2010/11 ANNUAL REPORT AND 2011/12 TO DATE**

The report of the Head of Finance was received which sought to update members on the 2010/11 Treasury Management outturn and details of the current position for 2011/12 to date.

The Committee were advised that the Annual report was outlined within paragraphs 7-16 of the report that had been submitted. The Committee were also referred to the outline of the portfolio outturn position as at 31st March 2011, which had resulted in the total debt outstanding at £130.905m and total investments at a level of £75.678m which had resulted in a the level of indebtedness being £55.227m.

The report outlined that the Council had a Treasury Management Strategy which set out how to monitor borrowing opportunities determined by the prevailing markets; reduce the volatility of investment returns while maintaining flexible arrangements and achieving an optimum return on investments commensurate with proper levels of security and liquidity.

Members were advised as to the Council's response to the current economic climate in that 2010/11 had seen continued problems with both sovereign and individual bank credit ratings. It was noted that the Base rate remained at 0.5% throughout the whole of 2010/11, and whilst the UK economy had come out of recession the recovery to date had been sluggish. As a result the Council had withdrawn money from the external fund managers and the Council had no funds with any external fund managers. These funds were invested internally thus reducing the need for extra borrowing, reduce investment risk and volatility.

In relation to borrowing the Committee was advised of the Council strategy which had been based on taking a pragmatic approach to the use of PWLB (prior to the Government's decision to increase rates) thereby spreading interest rate risk and thus taking advantage of rate movements when deemed appropriate. Members were referred to the table within the report that detailed the breakdown of the varying debt maturity as at 31st March 2011.

During the year it was confirmed that the Council had operated within the Treasury Limits and Prudential Indicators as set out in the Council's Treasury Policy Statement and the Annual Treasury Statement at all times. Appendix 1 of the report indicated that there had been no breaches of the limits during the year.

In relation to investments it was noted that the Council had previously made investments both internally and externally. In connection with the externally managed investments the Council had previously employed 3 fund managers at the beginning of 2009/10. It was reported that this had subsequently been reduced to one fund manager and that during 2010/11 it had been decided to withdraw funds held by the final fund manager with the result that all of the Council's investments were managed internally. Members noted that the rate of return that had been achieved with the internal investments of 3.63% far exceeded the rate of return of the external fund manager of 1.12% (gross of fees).

In relation to the Shropshire Council Debt Members were advised that an annual contribution was made with £2.14m being paid in 2010/11 towards the former County Council costs on pre disaggregation debt. The Committee noted that the interest paid averaged 5.19%, which was significantly higher than the rate payable by Telford & Wrekin on its own borrowings. A number of Members commented on the Shropshire Council debt and that the debt repayments were high and questioned as to how long the debt would remain. The Committee was informed that the length remaining was approx 20 years. Councillor Tomlinson enquired as to whether the Council could borrow elsewhere at a more competitive rate. The meeting was advised that the Council could however a premium charge would be applied and that any cost benefit would be minimal, accordingly it had been decided to leave the current loan in place.

The Committee was referred to the table that indicated the net overall position for 2010/11, with the sound overall position resulting from a mix of cash flow benefits plus pro-active treasury management activities. The budget reflected the position when the budget was set, with the underspend being achieved through active management of debt principal and the low interest rates prevailing for the year. Overall a net saving of just over £1.2m was made against budget for the year.

The remainder of the report dealt with the current financial year based largely on information to 31 May 2011. Members were informed that in the current economic climate, the strategy for the next few months was to review investment opportunities as they arose. The Council would also review borrowing opportunities throughout the year and seek to take advantage of the advantageous interest rates if possible.

Members received an update on interest rates. The Committee were reminded that the Base rate began the year at 0.5% and had remained there. The expectation was that either in late 2011 or early 2012 interest rates would begin to rise again, but this was dependent on how the economy would progress. Any increase was unlikely in the short term and most city forecasters did not expect an increase until September 2011 at the earliest.

The Committee was reminded that the Council had agreed the required indicators at Council on 3 March 2011. It was noted that there had been no breaches of the indicators and none had been amended. The Council set itself an Operational limit for external debt of £310m for 2011/12 and an Authorised limit of £330m, the current total borrowing outstanding of £118m was well within both limits.

In relation to the investment strategy for the year was to gain maximum benefit at minimum risk whilst achieving as a minimum, the 7 day deposit rate. For the period to 31 May 2010 some £328m worth of investments had been made from overnight deposits up to 21 days, with the Rates achieved ranging from 0.25% to 0.75%.

Finally the Committee was referred to Appendix 2 of the report that outlined the investments that had been made with individual Counterparties. At the end of May the greatest exposure with a single counterparty was £20.0m with Barclays, Royal Bank of Scotland and Lloyds TSB (just over 25.9% of the portfolio). The highest sovereign exposure to non UK sovereigns was 6.5% with Belgium.

**RESOLVED** – that the content of the report, the Council's response to the Economic Climate and the performance against Prudential Indicators be noted.

#### **AUC-9      INTERNAL AUDIT REPORT ON PROPERTY LEASES**

The report of the Audit & Assurance Service Delivery Manager was received which sought to inform members of the results of the recently completed audit report in relation to the leasing of Community Centres within the Borough.

The Committee was advised that following the presentation of the Dawley Town Hall audit report it had already been concluded that an audit should be undertaken in relation to the leasing arrangements for other community centres owned by the Council.

Members were referred to the contents of this report which highlighted the good practice areas that had been identified and the summary of the conclusions and the overall opinion of Internal Audit following completion of the audit.

Councillor Tomlinson welcomed the report but took the opportunity of providing by way of background to the situation that had occurred at Shawbirch Community

Centre. Councillor Fletcher provided background information in connection with the similar situation that had arisen at Priorslee Community Centre.

**RESOLVED** – that the Final Audit Report in connection with the Leasing of Community Centres be noted.

#### **AUC-10      THE ANNUAL GOVERNANCE STATEMENT – 2010/11**

The report of the Head of Governance was which sought the Committee's review and approval of the Annual Governance Statement 2010/11 which would accompany the 2010/11 annual accounts. Members were informed that the statement was agreed at the Cabinet meeting held on 21st June and then signed by the Leader and the Chief Executive.

The Committee was informed that under the Accounts and Audit (England) Regulations 2011 the Council was required to produce an Annual Governance Statement and it was best practice that the Statement should be signed by the Leader and Chief Executive of the Council. Members were referred to the Annual Governance Statement for 2010/11 as attached at Appendix A to the report and which had been developed based on the requirements of the regulations and CIPFA/Solace guidance. The statement further included an action plan at Annex 1 which ensured that the Council would continue to improve the existing governance arrangements.

It was further reported that the action plan attached to the 2009/10 statement (implemented during 2010/11) had been reviewed, updated and was presented to the Audit Committee in November 2010 and the position as at 31st March 2011 was attached as Appendix B to this report. The Annual Governance Statement outlined that the Council had adhered to its Local Code of Corporate Governance, continually reviewing procedures to maintain and demonstrate good corporate governance and that it had in place robust systems of internal control. The Council can be assured that during 2010/11, including since the commencement of organisational changes in January 2010 the existing governance framework had continued to support proper governance.

The Committee was advised that the required assurance for the annual governance statement was provided by all areas of the Council and externally by the following: Leader and Chief Executive – who sign the statement; Senior management – Corporate Directors, Assistant Chief Executive and Heads of Service; the Chief Financial Officer; the Monitoring Officer; Elected Members – Scrutiny arrangements, Standards Committee, Audit Committee and other Regulatory Committees; Internal Audit; Partners; External Audit; and other external inspection agencies. There was further information to support this report and provide assurance attached in Appendix C to the report.

The 2010/11 Annual Governance Statement set out the Council's governance arrangements that operated during the period and measured the effectiveness of them. Unitary elections took place on 5th May 2011 and new councillors were elected. A new administration was elected at the Annual Council meeting on 26th May 2011. It was expected that the new administration would make changes to the

Council's governance arrangements during 2011/12 which would be included in the 2011/12 statement. It was noted that the new administration had already proposed a review of the statutory Director of Children's Services role.

**RESOLVED** – that the **Annual Governance Statement 2010/11 as attached at Appendix A to the report be approved and the information contained within the report be noted**

**AUC-11**      **INTERNAL AUDIT 2010/11 QUARTER 4 UPDATE REPORT AND ANNUAL REPORT**

Members considered the report of the Audit & Assurance Service Delivery Manager which sought to update members on the work of Internal Audit during quarter four – January – March 2011 and to present the 2010/11 Annual Report.

The Committee was reminded that it received a quarterly update of the work of Internal Audit and this report included the update report for quarter four – January to March 2011. Members were informed that this report included the Annual Report on the Internal Audit activity for 2010/11 to continue to demonstrate good governance and support the Annual Governance Statement.

The report provided information on the work of Internal Audit during January to the end of March 2011 and also provided an update on the progress of previous audit reports issued (April 2009 to December 2010). It was reported that Internal Audit activity during this period had focussed on completion of the audits set out in the Internal Audit Plan including the final areas of work for the external auditor. There had also been unplanned work during the period including the co-ordination of the requirements for the publication of information in respect to expenditure over £500 and requests for specific reviews from senior officers.

Members were referred to the various appendices attached to the report which included a List of final reports issued in quarter four graded – red, amber, yellow or green. This report also included details of budgeted time, actual time and percentage variance at Appendix A; a list of all work undertaken for quarter four of 1 day or more at Appendix B; details of the previous graded reports from April 2009 to December 2010 with their current status, at appendix C; and a summary of the Amber reports issued quarter 4 at Appendix D.

Further details of the report areas listed within the report were provided by the Audit & Assurance Manager.

The Committee was also referred to the section of the report which comprised the Annual Internal Audit report for 2010/11. Members were advised that the Council's Section 151 officer's statutory obligation under the Accounts and Audit (England) Regulations 2011 was to provide assurance on the systems of internal control as provided by the work of internal audit. The purpose of this Annual Report was to provide this assurance in accordance with the current Council's assurance framework.

The system of internal control helped the Council to manage and control the risks which could affect the achievement of its priorities and objectives rather than eliminate them completely. Internal Audit and the other assurance processes therefore provided reasonable and not absolute assurance of the adequacy and effectiveness of the systems of internal control within the Annual Governance Statement.

The planned Internal Audit resources for 2010/11 were 1309 days plus 70 days specialist ICT audit provided under contract (from an external provider). The actual resources available were 1188 due to restructuring and maternity leave. However an external contractor had been used to provide 95 days to cover the majority of the resource shortfall (total days therefore 1283 – 26 days less than planned).

Based on the work undertaken during the year the main areas of which were outlined within the report and the implementation by management of the agreed recommendations it could be reported again that Internal Audit could provide reasonable assurance that the systems of internal control within these areas of the Council were operating adequately and effectively when reviewed during the year.

It was noted by the Committee that 68 reports were issued during 2010/11, which was a lower total than in the previous two years as a result of the complexity of the areas reviewed and reduction in resources. Members were informed that out the 68 (79) reports 78% (85%) were green (good) or yellow (reasonable). There was a corresponding increase of amber (limited) reports but no red (poor) reports. Summary amber reports and explanations had been reported to the Committee with detailed reports being circulated to members of the Committee prior to the meeting. The majority of areas had already implemented many of the recommendations but it was noted that ICT were in the process of implementation due to staffing resources and reorganisation.

There had been a 49% increase in Financial Regulation/DCSF recommendations which indicated an increase in none adherence to key controls. This was reflected in the increase in the number of Amber reports. Where Financial Regulation/DCSF or legal recommendations were made management agreed short implementation timescales or had already implemented the action by the time the final report was agreed. There had been a reduction in policy and procedure recommendations of 9% and a 59% decrease in the number of best practice recommendations.

A revised requirement of the Accounts and Audit (England) Regulations 2011 was for an annual review of internal audit rather than as previously an annual review of “the system of internal Audit”. The Council had taken the criteria from the existing assessment and used them to review internal audit for 2010/11. Members were referred to Appendix G which outlined how the review had been undertaken, the results and the resulting action plan.

The Committee were also referred to the part within the report that dealt with external review. Members noted that KPMG had been the Council’s External Auditors since 1st April 2007. It was reported that there was continuous liaison between Internal and External Audit to ensure that Internal Audit was undertaking appropriate work upon which the External Auditor could rely and reduce the external

audit fee. Internal Audit had delivered all the work for 2010/11 upon which External Audit placed reliance. In order to place reliance on the work of Internal Audit the External Auditor assessed the performance of Internal Audit each year against the CIPFA Code. KPMG had undertaken the 2010/11 review and the report was due by the end of June 2011. Although there had been no indication from KPMG of any adverse findings and the Council had implemented the minor actions from the previous review. In addition KPMG had also reviewed the Council against the CIPFA Statement on the Role of the Chief Internal Auditor in Public Sector (2010) and provided positive feedback.

The Committee also received information as to how Internal Audit had achieved local performance targets. Members were advised that Internal Audit had completed all the work for the External Auditor and therefore achieved the target of 100%. The Committee was further informed that if this work had not been completed on time and to an acceptable standard it was possible that the External Auditor would have undertaken some or all of the work at a considerably higher cost to the Council. The unit had also completed 92% of the other planned work and achieved the target set. It was noted that this achievement was an improvement on the last 2 years and was commended given that the team went through a restructure which was implemented in October 2010.

During the year to improve the team's efficiency, effectiveness and productivity team development and training sessions had been held. At these sessions and continually during the year the audit team had investigated and implemented new/alternative ways of service delivery (practices, use of technology, procedures and standard documentation) based on customer feedback, sharing best practice with other local authorities and service providers.

The team had also in addition to efficiency and productivity improvements, achieved 23.3% staff savings (target 20%) and 20% non-staff savings to assist the Council in meeting the budget gap. Internal Audit is a member of the CIPFA benchmarking club (membership of 147 local authorities). Members were informed that a report had been presented to the Audit Committee in November 2010 providing the results which showed that Internal Audit compared positively against other unitary authorities. Using this and qualitative data from the benchmarking club additional areas for improvement had been identified and included in the 2011/12 Service Action Plan.

The details of received customer feedback received via post audit questionnaire feedback was detailed in Appendix F of the report.

In conclusion the Committee was advised of the various impending changes as outlined within the report that would be faced by Internal Audit in 2011/12 that might have an effect on internal audit activity.

**RESOLVED – that the information contained within the Internal Audit Quarter 4 Update Report and the contents of the 2010/11 Internal Audit Annual Report be noted**

**AUC-12      OUTLINE OF AUDIT COMMITTEE BUSINESS FOR 2011/12**

Members received a programme of proposed business items for consideration by the Committee for the 2011/12 Civic Year. Members were referred to the revised timetable that had been produced since the dispatch of the agenda, which outlined the proposed training sessions that would be provided throughout the current Civic Year.

**RESOLVED – that the outline of business for the forthcoming meetings of the Audit Committee for the 2011/12 Civic Year be noted**

The meeting ended at 7.10 p.m.

**Chairman:**

**Date:**