



Audit Committee

Date **Thursday 28 June 2012**
Time **10.00 am**
Venue **Committee Room 1A - County Hall, Durham**

Business

Part A

**Items during which the Press and Public are welcome to attend.
Members of the Public can ask questions with the Chairman's
agreement.**

1. Minutes of the meeting held on 31 May 2012 (Pages 1 - 6)
2. Declarations of interest
3. Disposal of Council Land and Property - Report of Corporate Director, Regeneration and Economic Development (Pages 7 - 12)
4. Annual Internal Audit Report 2011/12 - Report of Manager of Internal Audit and Risk (Pages 13 - 36)
5. Internal Audit Plan 2012-13 (July 2012 - June 2013) - Report of Corporate Director, Resources (Pages 37 - 50)
6. Review of the Effectiveness of Internal Audit - Report of Corporate Director, Resources (Pages 51 - 82)
7. Agreement of Accounting Policies for Application in the 2011/12 Financial Statements - Report of Corporate Director, Resources (Pages 83 - 110)
8. Consideration of 'Going Concern Status' for the Statement of Accounts for the Year Ended 31 March 2012 - Report of Corporate Director, Resources (Pages 111 - 122)
9. Draft Annual Governance Statement for the year April 2011 - March 2012 - Report of Corporate Director, Resources (Pages 123 - 140)
10. 2011/12 Annual Report of the Audit Committee to County Council - Report of Chair of the Audit Committee (Pages 141 - 154)
11. Such other business as, in the opinion of the Chairman of the meeting, is of sufficient urgency to warrant consideration
12. Any resolution relating to the exclusion of the public during the discussion of items containing exempt information

Part B

Items during which it is considered the meeting will not be open to the public (consideration of exempt or confidential information)

13. Annual Fraud Report 2011/12 - Report of Manager of Internal Audit and Risk (Pages 155 - 188)
14. Such other business as, in the opinion of the Chairman of the meeting, is of sufficient urgency to warrant consideration

Colette Longbottom
Head of Legal and Democratic Services

County Hall
Durham
20 June 2012

To: **The Members of the Audit Committee**

Councillor E Bell (Chairman)
Councillor O Temple (Vice-Chairman)

Councillors C Carr, B Harrison, M Hodgson, L Marshall, B Myers,
R Ord and D J Southwell

Co-opted Members:

T Hoban and K Larkin-Bramley

Contact: Ros Layfield

Tel: 0191 383 4205

DURHAM COUNTY COUNCIL

At a Meeting of **Audit Committee** held in Committee Room 1A - County Hall, Durham on **Thursday 31 May 2012 at 10.00 am**

Present:

Councillor E Bell (Chairman)

Members of the Committee:

Councillors O Temple (Vice-Chairman), R Ord and D J Southwell

Co-opted Members:

Mr T Hoban and Ms K Larkin-Bramley

External Auditors:

C Banks, S Kenny

Apologies:

Apologies for absence were received from Councillors C Carr, B Harrison, M Hodgson, L Marshall and B Myers and Mr D McLure

1 Minutes

The minutes of the meeting held on 31 May 2012 were agreed as a correct record and signed by the Chairman.

Consideration was given to all current items on the Committee's Action Plan (for copy of action plan see file of Minutes), with several items on the Plan to be considered later in the meeting. In reply to a question from Ms Larkin-Bramley the Manager of Internal Risk and Audit informed the Committee that an update on the dates of reports shown as TBA would be brought to the next meeting.

2 Declarations of Interest

Declarations of interest were provided by Members of the Committee. A generic declaration of interest would be recorded given that Members were school governors, members of various Committees of the Council, former District Councillor's and bodies such as the Probation Board, Fire Authority and Police Authority. Together with other declarations from Ms Larkin-Bramley, a declaration be provided that she is a lecturer at New College Durham.

3 Strategic Risk Management Progress Report for the Quarter period January to March 2012

The Committee considered a report of the Corporate Director, Resources that highlighted the strategic risks facing the Authority and gave an insight into the work carried out by the Corporate Risk Management Group during the period January to March 2012 (for copy see file of Minutes).

The Risk and Governance Manager informed the Committee that two new risks had been identified during the quarter and provided an update on the risk relating to Seaham North Pier.

Resolved:

That the Committee confirm the report provided assurance that strategic risks were being effectively managed within the risk management framework across the Council.

4 The Work of Corporate Risk Management April 2011 - March 2012

The Committee considered a report of the Corporate Director, Resources which demonstrated the effectiveness of risk management across the Council during the year April 2011 to March 2012 and the effectiveness of the Corporate Risk Management Group in supporting Services in their management of risk, and also provided evidence to support the Annual Governance Statement (for copy see file of Minutes).

Councillor Southwell raised concerns regarding attendance by Members at risk management seminars. The Head of Legal and Democratic Services informed the Committee that an induction pack for Members following the elections in 2013 was currently being considered and agreed to include risk management as part of the pack.

Resolved:

That the Committee note the report and confirm it provided assurance that strategic risks were being effectively managed within the risk management framework.

5 Internal Audit Progress Report Quarter Ended 31 March 2012

The Committee considered a report of the Manager of Internal Risk and Audit that provided information on the work carried out by Internal Audit during the period April 2011 to March 2012 (for copy see file of Minutes).

Councillor Temple referred to the target of 90% around planned assurance and expressed some concern that this target was not being met. He asked whether 90% was an achievable target, and if so, whether resource or other factors were causing the target not being met. The Manager of Internal Risk and Audit replied that an update on the resource position would be provided to the next meeting when the 2012/13 Audit Plan was to be presented for approval.

Resolved:

That the progress made on delivering the internal audit plan for 2011/12 to gain assurance on the adequacy and effectiveness of the Council's internal control environment be noted.

6 External Audit - Durham County Council Audit Plan 2011/12

The Committee considered a report of the External Auditor that set out the work for the 2011/12 audit, based on a risk-based approach to audit planning (for copy see file of Minutes).

Resolved:

That the 2011/12 Audit Plan be approved.

7 Update on Duplicate Payments

The Committee considered a report of the Corporate Director, Resources that provided an update of the actions being taken and further plans to reduce the Authority's risk of making duplicate payments and received an update on the situation regarding duplicate payments up to 31 March 2012 and the amounts of money recovered (for copy see file of Minutes).

The Committee noted that good progress had been made on the amounts recovered but raised concern that in some cases, the resource required to recover small amounts may not be cost effective. Priority needed to be given to preventing duplicate payments occurring.

Resolved:

- (i) That the level of duplicate payments made in 2011/12 and the progress made to date with regards to recovering these sums be noted
- (ii) That the work being undertaken by the Procure to Pay review team to address compliance issues with regards to the corporate policy and system control weaknesses be noted.

8 External Audit - Interim Governance Report Pension Fund

The Committee considered an Interim Governance Report of the External Auditor on the Durham County Council Pension Fund (for copy see file of Minutes).

The Committee referred to those recommendations within the report where action was not taken or planned and requested that full management explanations be provided to the next meeting.

Resolved:

That the Interim Governance Report be noted.

9 External Audit - Interim Governance Report Durham County Council

The Committee considered an Interim Governance Report of the External Auditor County Council's annual financial statements (for copy see file of Minutes).

The Committee referred to those recommendations within the report where action was not taken or planned and requested that full management explanations and updates be provided to the next meeting.

Resolved:

That the Interim Governance Report be noted.

10 Compliance with International Auditing Standards

The Committee considered a report of the Corporate Director, Resources that sought approval to a draft response from the Chair of the Committee relating to a letter sent from the Audit Commission regarding compliance with International Auditing Standards (for copy see file of Minutes).

The Committee informed the Corporate Director, Resources that the draft response was in the name of Edward Bell and this should be shown as Councillor Edward Bell.

Resolved:

That the response provided by the Corporate Director, resources be noted and the response to be provided by the Audit Committee be approved, subject to the inclusion of the designation of Councillor, as discussed.

11 Any resolution relating to the exclusion of the public during the discussion of items containing exempt information.

Resolved:

That under Section 100A(4) of the Local Government Act 1972, the public be excluded from the meeting for the following item of business on the grounds that it involves the likely disclosure of exempt information as defined in Paragraph 3 of Schedule 12A to the said Act.

12 Internal Audit Progress Report Quarter Ended 31 March 2012

The Committee considered a report of the Manager of Internal Risk and Audit that provided information on the work carried out by Internal Audit during the period April 2011 to March 2012 (for copy see file of Minutes).

Resolved:

That the progress made on delivering the internal audit plan for 2011/12 together with that made by service managers in responding to the work of internal audit to gain assurance on the adequacy and effectiveness of the Council's internal control environment be noted.

Action Plan- Work of Audit Committee- Part A- 31 May 2012

Ref No.	Date of Meeting	Item No.	Title of Report	Action Required	By Whom	Report to Committee (date)/ implemented
1.	6.1.11 28.7.11 5.1.12	8	Bank Account Rationalisation/ Reconciliation	Six monthly update reports be provided	Corporate Director, Resources	30.7.12
2.	29.9.11 10.11.11 5.1.12 16.2.12 22.3.12	4	Single Asset Register	Progress report on phase 2 to be brought to a future meeting, and a report to provide assurance on the policies and procedures on the valuation and disposal of land, be brought to the next meeting	Gerald Darby Valuation and disposal of land Phase 2 Single Asset register	28.6.12 27.9.12
4.	29.9.11 31.10.11 22.3.12	10	Icelandic banks	Update - as and when necessary	Corporate Director, Resources	TBA
6.	5.1.12	9	Annual Audit Letter	Report to be brought to Committee outlining changes and implications of changes to HRA Funding	Jeff Garfoot	TBA Update to 28.6.12
7.	16.2.12	6	F M Standards	Once Section 151 Officer had completed the process, further details be brought back to Committee	Corporate Director, Resources	TBA Update to 28.6.12
8.	22.3.12	3	Budget and MTFP setting process	Timetable for next financial year be provided to members, once set.	Jeff Garfoot	TBA Update to 28.6.12
	31.5.12		Interim Governance Reports	Updated management response to be brought to next Committee	Jeff Garfoot	28.6.12

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Audit Committee

28th June 2012



Disposal of Council Land and Property

**Report of Stuart Timmiss Head of
Planning**

**Ian Thompson Corporate Director of Regeneration and Economic
Development**

**Neil Foster Cabinet Portfolio Member for Regeneration and
Economic Development**

Purpose of the Report

1. The purpose of the report is to outline current policies and procedures relating to the identification, valuation and disposal of land.

Background

2. Following discussions at a previous Audit Committee about the Single Asset Register in March, a request was made to bring forward a report to this Committee outlining current policies and procedures relating to the identification, valuation and disposal of land. The report outlines how the strategy links to targets for capital receipts to enable the Committee to have assurance that arrangements are in place to optimise the best use of assets and maximise returns.
3. The County Council owns a range of land and property which in light of the increasing focus on the way public sector assets are managed, these assets need to be actively managed in order to ensure that value for money is achieved from their use. The Corporate Asset Management Plan together with the Capital Strategy details the County Council's approach to property and land assets. Sitting beneath this overarching strategy are a number of policies and procedures relating to the valuation and disposal of land and these are set out below:-

Disposal and Acquisition Strategy

4. Prior to Local Government Reorganisation (LGR) the seven District Councils and County Council each operated their own policies and systems regarding the disposal and acquisition of land. In order to ensure a uniformity of approach it was considered appropriate that a strategy for all land and property disposals and acquisitions be adopted and a Disposal and Acquisition Strategy was developed and implemented to form part of its overall Asset Management Planning process.

The document is attached hereto and was approved by Cabinet in December 2010.

5. In terms of ensuring that the Council is seen to be getting Value for Money, the Strategy requires that all valuations for disposal should be undertaken at the earliest opportunity in the process by a suitably qualified member of the Royal Institution of Chartered Surveyors, and continually reviewed through the disposal process. Where it is decided to negotiate a disposal to a single party, rather than offer on the open market, all negotiations for disposals should be conducted or advised by a suitably qualified property professional, preferably a member of the Royal Institution of Chartered Surveyors.
6. Ombudsman guidance recommends that all negotiations should be conducted at the offices of the Council and with two people negotiating. This is not feasible in every case however this is the starting point to ensure and demonstrate that best practice is being adhered to.
7. All terms agreed for disposals require delegated approval from a senior manager and internal processes within Planning and Assets require at least two officers have the opportunity to consider disposal prices agreed by individual officers.

Disposal Programme

8. Following Local Government Review, work was undertaken to develop a Four Year Disposal Programme to underpin the Councils Medium Term Financial Plan.
9. In developing this Programme the work undertaken by the County Durham (Strategic Housing Land Availability Assessment) SHLAA Partnership was utilised. By way of explanation, under national planning policy, Local Planning Authorities are required to carry out a Strategic Housing Land Availability Assessment (SHLAA) annually. This is to ensure a flexible and responsive supply of housing land is maintained and identifies the amount of land which has the potential to accommodate new housing development over the next 15 years.
10. The Programme therefore included those County Council owned sites identified as suitable for development within the first five years of the SHLAA. It also included surplus property identified from Property and Service Reviews such as the Office Accommodation Project Strategy and sites identified from the Disposal Programmes of the former County and District Councils.
11. Please note that the programme is a Living Document and continues to be updated monthly to reflect market conditions and other surplus land and property identified from exercises such as Property/Service reviews and Service Asset Management processes.
12. The 2011/12 – 2014/15 Capital Budget agreed at County Council on 23 February 2011 had the following targets for Capital Receipts.

Income Type	2011/12	2012/13	2013/14	2014/15
	£m	£m	£m	£m
Land/Building Disposal	12.9	9.9	8.0	8.9
VAT Shelter	1.5	2.7	2.5	1.6
TOTAL	14.4	12.6	10.5	10.5

13. The achievement of land sales against target is monitored throughout the year through monthly officer meetings, a quarterly update report to the MOWG (Member/ Officer Working Group and through the RED Service Plan.
14. The new MTFP Capital Receipts targets reported to County Council on 22 February 2012 revised the annual income targets to take into account the slippage of income from 2011/12 to 2012/13. On that basis the current Capital Receipts targets are as follows (the Land Sale targets below excludes BSF/Schools Receipts).

Income Type	2011/12	2012/13	2013/14	2014/15	2015/16
	£m	£m	£m	£m	£m
Land/Building Disposal	4.482	15.934	7.500	8.400	8.400
VAT Shelter	1.500	2.700	2.500	1.600	1.600
TOTAL	5.982	18.634	10.000	10.000	10.000

Minor Disposals

15. The Council receives a large volume of requests to purchase land. Dealing with minor land sales is equally as time consuming as dealing with larger value and at the present moment in time we have received 540 requests and continue to receive around 25-30 new requests each month.
16. Following LGR applications of this nature were logged but not processed due to lack of resources as a consequence a backlog built up. To address this the Council have employed an Assistant Estates Surveyor and we now have a robust process in place which has resulted in addressing the backlog. To date 89 offer letters have been sent out after initial consultations and terms agreed on a number of requests with expected capital receipts of £105,250 with further sales of £140,500 in negotiation.
17. 50 requests are currently being processed and we have received combined processing fees amounting to £8,400.

Reactive Disposals

18. There are occasions where the Authority may wish to dispose of property that is not formally classified as surplus or considered to be under-performing. Examples include disposals to developers for community regeneration schemes by way of asset backed vehicles or nominated registered housing associations for the development of affordable housing.

Disposals at an Undervalue

19. Finally, there may be circumstances where a Local Authority considers it appropriate to dispose of land at an undervalue and, to allow Authorities more flexibility in such instances, the General Disposal Consent (England) 2003 came into effect on 4th April 2003.
20. The main provision of the consent is that there is a general consent for Local Authorities to dispose of land or grant a lease in excess of 7 years for less than the best consideration reasonably obtainable, where:-
 - I. The Authority considers that the purpose for which the land and property is to be disposed is likely to contribute to the promotion or improvement of the economic, social or environmental well being of the whole or any part of its area or any persons resident or present in its area; and
 - II. The difference between the full market value and the actual consideration payable does not exceed £2m
21. A Policy for the “Disposals of Land at an Undervalue” has been developed and was approved by Cabinet on 11th November 2009. This sets out the process to be followed and the Disposal and Acquisition strategy requires that in order to protect the authority’s interest in the event of subsequent sales, disposals should include, where, appropriate an asset lock, claw back or uplift clause, restrictive covenants, ransom strip retention, user rights or right of preemption.
22. It also requires that a valuation should be undertaken to identify the undervalue (unrestricted less restricted value) and an attempt should be made to financially value the economic, social or environmental benefits to the authority and community which justify a disposal at less than best price.
23. The overriding factor to be considered when disposing at below the best price is to ensure that it is within the authority’s power to so, and the reasons are well documented, transparent and justifiable.
24. A restructure within Assets will also ensure improved coordination of disposals and give priority to the realisation of capital receipts.

Recommendations and reasons

21. Members note the report to gain assurance that there are appropriate arrangements in place for the disposal of land.

Contact: Gerard Darby Tel: 0191 3834528

Appendix 1: Implications

Finance

No direct financial implications

Risk

None

Staffing

None

Equality and Diversity / Public Sector Equality Duty

None

Accommodation

None

Crime and disorder

None

Human Rights

None

Consultation

None

Procurement

None

Disability Discrimination

None

Legal Implications

None

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Audit Committee

28 June 2012

Annual Internal Audit Report 2011/12



Report of Manager of Internal Audit and Risk

Don McLure, Corporate Director Resources

Purpose of the Report

1. The purpose of this report is to present the Annual Internal Audit Report for 2011/12. (Copy attached at Appendix 2).

Background

2. The Council has a responsibility for maintaining sound systems of internal control that support the achieving of its objectives and for reviewing their effectiveness.
3. This report fulfils the requirement of the CIPFA Code of Practice for the Head of Internal Audit to provide, "a written report to those charged with governance timed to support the Statement of Internal Control", which is now incorporated as part of the Council's Annual Governance Statement.
4. The Annual Internal Audit Report should therefore be considered in the context of fulfilling the requirement to provide an opinion on the overall adequacy and effectiveness of the Council's control environment during the year, and how this opinion has been derived.
5. The opinion on the control environment and any significant issues arising will be reflected in the Council's Annual Government Statement which will be published as part of the Council's Annual Governance Statement of Accounts for 2011/12.
6. Based on the work undertaken, Internal Audit is able to provide a **Moderate** overall assurance opinion on the adequacy and effectiveness of internal control operating across the Council in 2011/12. This moderate opinion ranking is the same as 2010/11 and provides assurance that there is basically a sound system of control in place, but there are some weaknesses and evidence of non-compliance with controls or ineffective controls. Control objectives are however often achieved in all service groupings across the Council.

Recommendation

7. Members note the content of the Annual Internal Audit Report and the overall 'moderate' opinion provided on the adequacy and effectiveness of the Council's control environment for 2011/12.

Contact: Avril Wallage Tel: 0191 383 3537

Appendix 1: Implications

Finance

There are no direct financial implications arising for the Council as a result of this report, although we aim through our audit planning arrangements to review core systems in operation and ensure through our broad programme of work that the Council has made safe and efficient arrangements for the proper administration of its financial affairs.

Staffing

None

Risk

This report requires no decision and so a risk assessment has not been carried out

Equality and Diversity / Public Sector Equality Duty

None

Accommodation

None

Crime and disorder

None

Human rights

None

Consultation

None

Procurement

None

Disability issues

None

Legal Implications

None

DURHAM COUNTY COUNCIL

Internal Audit

**Annual Report
2011-2012**

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Introduction

1. This report summarises work carried out by internal Audit during the financial year ended 31/3/2012 and provides assurance on the effectiveness of the Council's control environment, risk management and corporate governance arrangements in place during the year.

Background

2. The requirement for an internal audit function is implied by Section 151 of the Local Government Act 1972 which requires that Local Authorities to, "make arrangements for the proper administration of their financial affairs and ensure that one of its officers has responsibility for the administration of those affairs".
3. The Accounts and Audit (England) Regulation 2011 requires the Council to, "undertake an adequate and effective system of internal audit of its accounting records and its system of internal control in accordance with the proper practices in relation to internal control". The Council has delegated this responsibility to the Corporate Director Resources and the Internal Audit and Risk service carry out the Internal Audit Role.
4. The guidance accompanying the legislation states that proper internal control practice for internal audit is that contained within the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom
5. This report fulfils the requirement of the CIPFA Code of Practice for the Head of Internal Audit to provide, "a written report to those charges with governance timed to support the Statement of Internal Control", which is now incorporated as part of the Council's Annual Governance statement.

Service Provided and Audit Methodology

6. Internal Auditing is an independent, objective assurance and consultancy activity designed to add value and improve an organisation's operations.
7. The primary objective of Internal Audit is to provide an independent and objective opinion on the Council's control environment.
8. The Internal Audit Charter, agreed by the Audit Committee, establishes and defines the terms of reference and audit strategy for how the service is to be delivered.
9. Audit services are also provided to a number of external clients including the Durham Police Authority, Durham and Darlington Fire & Rescue Authority and the Durham and Mountsett Crematoria Joint Committees.
10. The service is also responsible for the audit of the Durham County Pension Fund.
11. The agreed audit strategy to provide independent assurance, as detailed in the Internal Audit Charter, is summarised as follows:
 - To work in consultation with senior management teams and other providers of assurance to prepare strategic and annual audit plans

- To carry out planned assurance reviews of the effectiveness of the management of operational risks in all key service activities/systems over a rolling 5 year programme (Strategic Plan)
- To carry out assurance reviews of the management of strategic risks where the effective management of the risk is heavily dependent on identified controls,
- To carry out annual reviews of key risks where a high level of assurance is required to demonstrate the continuous effectiveness of internal controls, for example those associated with key financial systems
- To use a Control Risk Assessment (CRA) methodology to focus audit resources on providing assurance on key controls where there is little or no other assurance on their adequacy or effectiveness.

Types of Audit Work Carried Out in 2011/12

Assurance Reviews

12. Assurance reviews are those incorporated into annual audit plans from strategic plans where the CRA methodology is to be applied. They also include service requests to provide assurance on more specific risks within a particular service activity.
13. On completion of each assurance review an opinion on the adequacy and / or the effectiveness of the control framework in place is provided to inform the annual audit opinion.

Advice and Consultancy Work

14. In addition to planned assurance reviews, provision is also made in annual audit plans to support service managers by undertaken advice and consultancy type work. The outcomes from this work can also provide assurance on the control framework.

Counter Fraud Work

15. Provision is made in annual audit plans to support service managers at an operational level to mitigate the strategic risk of fraud and corruption. Control weaknesses identified when fraud is suspected or proven also impacts on the overall opinion on the adequacy and effectiveness of the Council's internal control system.

Grant Certification

16. Some provision is also made in internal audit plans for the certification of external grant claims where required. Again, the outcomes of this work can help inform the annual opinion on the control environment.

Audit Quality Assurance framework

17. The Internal Audit Charter sets out the performance and quality framework for the service.
18. Key contacts, determined by the appropriate head of service, agree the terms of reference for each audit review and are able to challenge the findings and content of draft reports prior to them being finalised.
19. A summary of our performance against agreed indicators is provided in **Appendix A.**
20. It should be noted that the audit planning year was revised during the year and approved annual plans for 2011/12 covered work to be carried in the period July 2011 to June 2012. An interim plan was approved for the period April to June 2011 and the performance figures quoted relate to work carried out in the period April 2011 to March 2012. The actual performance in delivering planned assurance reviews from the approved 2011/12 plan up to the 31st March 2012 is also shown for information.
21. As can be seen the % of planned assurance work completed is below target. The main reasons for this are summarised below:
 - Reduction in audit days available due to retirement, secondment and temporary vacancies
 - Inadequate provisions for unplanned work, particularly that carried over as work in progress from the previous year
 - Inadequate provision for fraud and irregularly investigations
 - Planned work (including some advice and consultancy work) taking longer than estimated
22. Slippage on the approved plan is being addressed through the acquisition of additional resources through the Internal Audit Partnership with an external provider and the temporary engagement of an agency worker, funded from budget savings from temporary vacant posts.
23. The Accounts and Audit (England) Regulation 2011 requires the Council to carry out an annual review of the effectiveness of Internal Audit. The outcome is reported to Audit Committee and is subject to independent review by the external auditor.
24. The outcomes of the last review carried out by the Corporate Director Resources, and considered by the Audit Committee in June 2011 consisted of an assessment of compliance with the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 and an assessment of compliance with CIPFA's Statement on the role of the Head of Internal Audit (HIA) in public section organisations. The review concluded that the service is substantially compliant with the requirements of the Code and the Statement and noted actions being taken to achieve full compliance. A similar exercise will be carried out this year to be considered at the same meeting of the Audit Committee as this report.
25. Independent quality reviews are undertaken by audit managers as a matter of routine and periodically by the head of internal audit to ensure consistent

application of agreed processes and procedures and to ensure expected quality standards are maintained.

26. Internal Audit continues to be a member of the CIPFA Audit Benchmarking Club. The outcomes from this annual exercise are subject to challenge by the Audit Committee.

Improvements made during the year to improve the quality and effectiveness of the service

27. The main areas where improvements were identified through the last annual review of the effectiveness of the service related to:
- Embedding a risk based audit approach
 - Improving relationships with other regulatory and inspection agencies
 - Improving assurance on programme and project risks
28. The implementation of the revised audit strategy and the CRA methodology outlined above reflected a risk based approach to internal auditing. This has allowed a much more focused and consistent approach to the development of the scope of audit assurance reviews informed by an assessment of key risks and other sources of assurance agreed with the key contact as part of the planning and preparation process of each assignment.
29. Audit processes have also been revised during the year to reflect this risk based approach. These include:
- Revised Terms of Reference Format informed by the agreed CRA
 - A revised audit report format to help focus executive summaries on key findings i.e those that will increase the impact or the likelihood of key risk occurring if not addressed. The CRA is updated at the end of the process and issued with final reports to reflect actual controls in place and provides a mechanism for on-going self-assessment.
 - Revised methodology for categorising the importance of audit findings, resultant recommendations and audit assurance opinions. A copy of this revised methodology is attached at Appendix D.
 - The introduction of a Post Audit Evaluation (PAE). This is carried out by the lead auditor in conjunction with the relevant audit manager on the completion of each audit. In addition to providing a mechanism for reflecting on what went well during the audit and identifying any areas for improvement, the PAE also consists of an audit need risk assessment which is used to inform the strategic audit plan and future audit coverage.
30. Work was begun during the year to develop a corporate assurance framework to help identify key assurance providers and the assurance they provide on the management of risks. As a result, a corporate assurance framework was approved by full Council in December 2011. This provides a high level illustration of the Council's assurance framework but further work is needed in the current year to develop a more co-ordinated and coherent approach to assurance provision.

31. More resources were allocated in the 2011/12 audit plans to improve assurance on programme and projects. However, some work scheduled in this area has not progressed, at the request of the management, due to concerns about duplication with other assurance providers and the demands placed on the service. Whilst the CRA approach seeks to ensure that reliance would be placed on the work of other assurance providers, these concerns have emphasised the need for clarity over roles and responsibility of the various internal providers of assurance and on which risks they provide assurance. Work has therefore begun to clarify the roles and responsibilities of other assurance providers, whether internal or external, and the nature and limitation of what assurance they provide as part of development of the corporate assurance framework. This will however take time to develop and require the investment of not only internal audit resources but also that of senior management.
32. In recognition that the in house risk and audit service may not have all the necessary skills and experience to provide reliable independent assurance in the specialist area of the Pension Fund, an internal audit partner was appointed to develop a strategic risk register and assurance map in consultation with management and the Pension Fund Committee. The partner also delivered the pension fund audit in 2011/12. This partnership arrangement has allowed the opportunity of skills transfer and the sharing of best practice with the in house team which has contributed to further improvements to audit processes and procedures introduced during the year.
33. The head of internal audit now reports direct to the Corporate Director Resources rather than the head of corporate finance. This change has helped raised the profile of the audit service and improved its independence. It has also provided a better strategic platform for the work of the service to influence senior management.

Summary of audit work carried out

Assurance Work

34. Our work programme for the financial year 2011-12 was determined by an approved interim plan covering the period April to June 2011 and the approved Annual Audit Plan for year ending June 2012.
35. A summary of assurance work complete during the year is attached at **Appendix E**. Details of work carried out in the previous 2 financial years together with work in progress at the 31st March which has subsequently been completed is also included to provide a more informed opinion on the control environment.

Added Value Work

36. All planned reviews are designed to add value as they provide independent assurance, through evaluation and challenge, on the adequacy and effectiveness of arrangements in place to manage risks. This evaluation and challenge supports the effective and efficient use of resources and and value for money (VFM).

37. Through our advice and consultancy work we are able to add value pro-actively and reactively.
38. Reactive work involves positively responding to ad-hoc requests for advice and reviews added to the plan to address new or emerging risks. It also includes responding to potential fraud or irregularities and we ensure that all such incidents are properly investigated and that appropriate action is taken by managers, whether or not fraud or malpractice is proven. This work is delivered from the contingency provision within the plan.
39. A summary of added value work undertaken is attached at **Appendix B**.

Key Areas for Opinion

40. The key areas of the control environment where assurance is required to inform our overall opinion are:
 - Financial Management
 - Risk Management
 - Corporate Governance
41. Assurance has been provided on some aspects of all key financial systems during the year. It is acknowledged that good progress has been made during the year in improving the operational efficiency and performance of both of Oracle, following the closure of the former council district systems, and the Revenue and Benefits systems, following the implementation, on schedule, of a the new single system and a new cash management system. However, testing of the control environment in operation during the year still highlighted a number of weaknesses in key controls. Key issues arising from audit work where controls have improved or further improvements have been identified are summarised in **Appendix C**.
42. Independent assurance on the effectiveness of the Council's risk management arrangements has been provided by consideration of the adequacy and effectiveness of operational risk management through the risk based audit approach and the CRA methodology applied to individual audit assignments. In addition specific work has been carried out to provide independent assurance on the management of some strategic risks.
43. A number of audits have been carried out during the year to provide independent assurance on the effectiveness of specific key corporate governance arrangements. In addition, compliance with relevant key council policies and procedures has also been considered as part of the risk based approach to the audit of service related planned assurance reviews.
44. Recommendations made to improve the control environment helps to embed effective risk management and strengthen the effectiveness of the Council's corporate governance arrangements.
45. Significant control issues where audit findings concluded that controls in place provided only limited assurance that risks were managed effectively and where actions are still to be implemented to address these are summarised in Appendix C.

Audit Opinion Statement

46. The Council has responsibility for maintaining a sound system of internal control that supports the achieving of its objectives.
47. Internal Audit is required to provide an opinion on the Council's risk management, control and governance process.
48. In giving this opinion it should be noted that assurance can never be absolute and therefore only reasonable assurance can be provided that there are no major weaknesses in these processes.
49. In assessing the level of assurance to be given, we based our opinion on:
 - All audits undertaken during the year
 - Follow up action on audit recommendations
 - Any significant recommendations not accepted by management and the consequent risk
 - The effects of any significant changes in the Council's systems
 - Matters arising from previous reports to the Audit Committee
 - Any limitations which may have been placed on the scope of the internal audit
 - The extent to which resource constraints may impinge on internal audit's ability to meet the full audit needs of the Council
 - The outcomes of the audit quality assurance process
 - The reliability of other sources of assurance considering when determining the scope of internal audit reviews
50. Consideration of the direction of travel on the adequacy and effectiveness of the control environment since unitary status as illustrated in Appendix E. We are satisfied that sufficient internal audit work has been undertaken to allow us to draw a reasonable conclusion as to the adequacy and effectiveness of the Councils system of internal control. Based on the work undertaken, we are able to provide a **Moderate** overall assurance opinion on the adequacy and effectiveness of internal control operating across the Council in 2011/12. This moderate opinion ranking provides assurance that there is basically a sound system of control in place, but there are some weaknesses and evidence of non-compliance with controls or ineffective controls. Control objectives are often achieved however in all service groupings across the Council.
51. This overall 'moderate' opinion reflects the same overall opinion as the last 2 years.
52. The adequacy and effectiveness of key financial controls is a major consideration in our opinion. Whilst good progress has been made during the year to improve a number of key financial systems that will provide a much better operational platform for effective financial risk management going

forward, some key controls were still absent or not operating effectively in 2011/12 hence the same “moderate” opinion on the financial control environment as the last 2 years. The full benefit of new systems together with those arising from the recent utilisation of the finance service should ensure an improvement in the financial control environment in 2012/13.

53. As can be seen from Appendix E, the majority of work undertaken on core governance risks has resulted in a “moderate” assurance opinion. Likewise the opinion on the effectiveness of operational risk management across service groupings, with the exception of CYPs and AWH, was considered to be “moderate”. These outcomes reflect the extent of change across the Council since Local Government Reorganisation, with those services subject to less change being in a position to maintain a higher level of control.
54. Where Internal Audit has identified areas for improvement, recommendations were made to minimise the level of risk, and action plans for their implementation were drawn up and agreed by management.
55. All audits with a limited assurance opinion have disclosed at least one high risk finding and these are subject to more rigorous follow up and are reported to Audit Committee on an exception basis.
56. Progress made by management on the implementation of audit recommendation is monitored, reported and subject to challenge by the Audit Committee. Whilst good progress has been made by management in implementing agreed actions a number of high risk actions were overdue at the end of the year, even where revised target implementation dates have been agreed, and consequently this has impacted on the overall opinion.

PERFORMANCE INDICATORS

Efficiency			
Objective: To provide maximum assurance to inform the annual audit opinion			
KPI	Measure of Assessment	Target and (Frequency of Measurement)	Actual as at 31/3/12
Planned audits completed	% of assurance work planned to be completed in the financial year to draft report stage as at 31 March % of planned assurance work from the annual plan July 2011– June 2012 as at 31 March	90% (Quarterly)	66% - adjusted to 85% when work in progress considered (80%) 60%
Timeliness of Draft Reports	% of draft reports issued within 30 Calendar days of end of fieldwork/closure interview Average time taken is also reported for information	90% (Quarterly)	87% (91%) 18 days on average (12)
Timeliness of Final Reports	% of final reports issued within 14 calendar days of receipt of management response Average time taken is also reported for information	95% (Quarterly)	92% (91%) 5 days on average (5)
Quarterly Progress Reports	Quarterly progress reports issued to Corporate Directors within one month of end of period	100% (Quarterly)	100% (96%)
Terms of Reference	% of TOR's agreed with key contact in advance of fieldwork commencing	95% (Quarterly)	88% (97%)
Quality			
Objective: To ensure that the service is effective and adding value			
KPI	Measure of Assessment	Target and (Frequency of Measurement)	
Recommendations agreed	% of Recommendations made compared with recommendations accepted	95% (Quarterly)	98% (99%)
Post Audit Customer Satisfaction Survey Feedback	% of customers scoring audit service good or above (4 out of 5) where 1 is poor and 5 is very good	100% (Quarterly)	96% (87%) Overall average score 4.49 (4.47)
Customers providing feedback Response	% of Customer returning satisfaction returns	70% (Quarterly)	47% (56%)
Cost			
Objective: To ensure that the service is cost effective			
KPI	Measure of Assessment	Target and (Frequency of Measurement)	
Cost per chargeable audit day	CIPFA Benchmarking Club – Comparator Group (Unitary)	Lower than average (Annually)	Yes (No)

* figures in brackets are 2010/11 actual shown for comparison purposes

VALUE ADDED WORK

Information Governance

The service is represented on the corporate Information Governance Group to provide advice and guidance and to carry out independent assurance work on the Council's information governance arrangements.

Grant Work

As the Council strives to maximise external funding to help it deliver its objectives, we have been increasingly required to provide independent assurance that funding is correctly spent by certifying grant claims. Such work adds value by ensuring no grant is lost through claw back or reputation damage that may impact on future external funding opportunities.

Personalisation of Care Services

We have continued to work closely with social care staff implementing the new personalisation process for care services. Further work is planned in this area in this area to ensure controls established continue to be effective.

Procure to Pay (P2P) Workstreams

We have continued to work closely with our colleagues in Finance to provide advice and guidance to in support of the P2P project team set up to improve the effectiveness of the procure to pay process within Oracle E Business Suite.

New Revenues and Benefits System and Icon Cash Management System

We have provided substantial support to the implementation on these major financial systems, advising on the control framework design and carrying out testing on the integrity of data conversions and reconciliations.

Membership of the Strategic Procurement Network (SPN)

The SPN is a corporate group and Internal Audit provides independent advice and challenge on internal control and VFM issues as they arise as well as acting as the Resources Service Grouping representative.

Membership of the Information Security Forum (ISF)

The ISF is a corporate group and Internal Audit provides advice and guidance on information security issues. We also carry out assurance work on the information security arrangements which assist in the Council's ability to retain its compliance with the information security standard (ISO27001).

Partnership Governance Framework

We have continued to work with officers in Partnerships and Community Engagement, ACE, and service link officers to review partnership governance arrangements leading to the development of an annual online self assessment process.

Counter Fraud

Work has continued during the year to promote the Council's Counter fraud and Corruption Strategy to help embed a zero tolerance culture across the Council. Other work carried out includes:

- Helping service managers identify fraud risks and to design controls to prevent and /or detect fraud occurring.
- Conducting counter fraud reviews to help detect fraud and error in known high risk areas
- Supporting managers to investigate suspected fraud and irregularities
- Helping service managers prevent reoccurrences
- Monitoring and reporting upon fraud & irregularity activity to the Corporate Management Team and the Audit Committee

Miscellaneous Service Requests

Examples of ad hoc advice and consultancy work carried out during the year in include:

- Production of performance management data for the Housing/Council Tax Benefits Service
- Free School Meals eligibility
- Precepting arrangements
- Support in the development of Single Asset Register
- School clerking recharges
- Relocation of the Library at Barnard Castle
- Due Diligence Analysis relating to the transfer of Public Health
- Shared Lives Procedures
- Bishop Auckland Town Hall (BATH) Catering Contract Arrangements
- Systems relating to Direct Payment (DP) Bank Accounts and associated monies with AWH
- Library Service - Recovery of unpaid monies / suspended memberships
- Review of Registrars Service
- Support to head teachers and governing bodies on the new School Financial Value Standard

KEY CONTROL ISSUES

Key Financial Systems

As can be seen from Appendix D, the overall assurance opinion on the financial control environment operating during 2011/12 is considered to be **Moderate**. In some specific areas, only limited assurance could be provided. Weaknesses identified in relation to these areas are considered significant and may put the system objectives at high risk. Consequently controls in these areas are not considered adequate to manage potential risks effectively.

The full benefits of ICON cash management are yet to be realised as it has not yet been rolled out across the whole Council. Consequently there are still a number of piecemeal arrangements in place for the collection and receipting of income. An income management strategy is not yet in place and policies and procedures are not yet standardised.

The planned implementation of Financial Management Standards, supporting by robust operational accounting policy and procedures will help address this.

It is acknowledged that good progress has been made during the year to improve the overall financial management framework, including the recent unitisation of the finance service. Improvements made to Oracle during the year and the demise of the former district council feeder systems, together with the implementation of the ICON cash management system, have reduced the number of reconciliations required and therefore provide a much sounder basis for effective controls as the potential for error is greatly reduced. However, some key reconciliations between ICON and Oracle, including bank reconciliation and clearing of suspense accounts, were not always timely during the year resulting in a temporary suspension of debt recovery procedures.

Improved performance management arrangements have been implemented during the year to monitor the extent of creditor payments being processed manually outside of the authorisation control built into the P2P Module of Oracle. Whilst performance has improved, controls relating to the manual payment of invoices remain poor due to absence of approved lists of authorised signatories. In addition the electronic authorisation limits set within Oracle have on occasions been disabled during the year to allow the speedier processing of payments.

The absence of up to date lists of approved authorised officers, linked to an approved detailed scheme of delegation, increases the likelihood that inappropriate payments could be submitted for payment. Roles and responsibilities are not clearly documented and little assurance can be provided that an adequate division of duties is maintained and/ or that there is clear accountability for payments authorised. Interrogation of creditor payments have identified duplicated payments amounting to £110K during the year. The majority of this has already been recovered and action is being taken to ensure full recover of all overpayments.

Procedures in place for creating and monitoring direct debit payments made from the Council's bank account were found to be weak and have exposed the Council to the risk of loss through fraud.

Control weaknesses identified at audit are being addressed through the P2P project improvement plan.

Authorised signatories are not maintained by the payroll section to act as a deterrent against inappropriate adjustments to payroll being submitted. Subject to the system development plan being accepted, this is to be addressed by introducing a workflow facility within ResourceLink which will allow for the electronic review and authorisation of claims.

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ICT Charges

The database of external ICT customers was not up to date consequently there was a risk of loss income through the failure to raise invoices for services provided. Management are in the process of ensuring appropriate SLA's are established and raising invoices accordingly.

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Pension Fund

There is a lack of clarify over the roles and responsibilities of the Pension Fund Committee. This together with a number of other control weakness relating to the governance arrangements for the fund are to be addressed through revised terms of reference.

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Findings

Individual findings are assessed on their impact and likelihood based on the assessment rationale in the tables below:

Impact Rating	Assessment Rationale
Critical	A finding that could have a:
	Critical impact on operational performance (Significant disruption to service delivery)
	Critical monetary or financial statement impact (In excess of 5% of service income or expenditure budget)
	Critical breach in laws and regulations that could result in significant fine and consequences (Intervention by regulatory body or failure to maintain existing status under inspection regime)
	Critical impact on the reputation of the Council (Significant reputational damage with partners/central government and/or significant number of complaints from service users)
	Critical impact on the wellbeing of employees or the public (Loss of life/serious injury to employees or the public)
Major	A finding that could have a:
	Major impact on operational performance (Disruption to service delivery)
	Major monetary or financial statement impact (1-5% of service income or expenditure budget)
	Major breach in laws, regulations or internal policies and procedures (non compliance will have major impact on operational performance, monetary or financial statement impact or reputation of the service)
	Major impact on the reputation of the service within the Council and/or complaints from service users
Minor	A finding that could have a:
	Minor impact on operational performance (Very little or no disruption to service delivery)
	Minor monetary or financial statement impact (less than 1% of service income or expenditure budget)
	Minor breach in internal policies and procedures (non compliance will have very little or no impact on operational performance, monetary or financial statement impact or reputation of the service)

Likelihood	Assessment criteria
Probable	Highly likely that the event will occur (>50% chance of occurring)
Possible	Reasonable likelihood that the event will occur (10% - 50% chance of occurring)
Unlikely	The event is not expected to occur (<10% chance of occurring)

Overall Finding Rating

This grid is used to determine the overall finding rating.

LIKELIHOOD			
Probable	M	H	H
Possible	L	M	H
Unlikely	L	L	L
	Minor	Major	Critical
	IMPACT		

Priority of our recommendations

We define the priority of our recommendations arising from each overall finding as follows;

High	Action that is considered imperative to ensure that the service/system/process objectives are not exposed to significant risk from weaknesses in critical or key controls
Medium	Action required to ensure that the service/system/process objectives are not exposed to major risk from weaknesses in controls
Low	Action required to ensure that the service/system/process objectives is not exposed to minor risk from weaknesses in controls
Advisory	Action that is considered desirable to address minor weaknesses in control that if implemented may not reduce the impact or likelihood or a risk occurring but should result in enhanced control or better value for money.

Overall Assurance Opinion

Based upon the ratings of findings and recommendations arising during the audit as summarised in risk matrix above we define the overall conclusion of the audit through the following assurance opinions:

Full Assurance	There is a sound system of control designed to achieve the process/system/service objectives and manage the risks to achieving those objectives. (No H, M or L findings/recommendations)
Substantial Assurance	Whilst there is a sound system of control, there are some weaknesses, which may put some of the system objectives at minor risk. (No H or M findings/recommendations)
Moderate Assurance	Whilst there is basically a sound system of control, there are some weaknesses, which may put some of the system objectives at major risk. (No H findings/recommendations)
Limited Assurance	There are weaknesses in key areas in the system of control, which put the system objectives at significant risk.(H findings/recommendations)
No Assurance	Control is weak as controls in numerous key areas are ineffective leaving the system open to significant risk of error or abuse

SUMMARY OF WORK CARRIED OUT

Audit Area	Sub Area	2009/10 Opinion	2010/11 Opinion	2011/12 Opinion	Opinion Conclusion
CORPORATE FINANCIAL MANAGEMENT RISKS					
P2P	Compliance with key controls		Limited		
	Petty Cash Usage		Moderate		
	Data Quality	Substantial	Moderate		
	Internal use of Credit Cards		Limited		Limited
	Procurement Cards		Limited		
	Supplier/Contractors bank account amendments			Moderate	
	Direct Debit Payments			Limited	
Customer to Cash	Income from DCC Assets		Limited		
	Income Reconciliation: Revenues & Benefits	Substantial			
	Income from Online Sales	Moderate			Moderate
	Cash Management		Limited	*Limited	
	Cashier Security			Moderate	
	Income collection (Debtors)		Limited	** Moderate	
NNDR	Key Controls	Substantial	Limited		Moderate
	Governance review			*Moderate	
Payroll	Central System Key Controls		Moderate		
	Governance review			Moderate	
	Teachers Pension Fund: Annual Auditor Certification (TR17)		Moderate	Moderate	
	Review of controls				
	Service based key controls	Moderate			Moderate
	HR arrangements across Directorates			Limited	
	Electronic Data Interchange	Limited			
	Tupe allowances	Limited			
	Member expenses		Moderate		
Council Tax	Compliance with key controls	Substantial	*Limited		Moderate
	Governance review			*Moderate	
Housing and Council Tax Benefits	Compliance with key controls	Moderate	Moderate		
	Governance review			Moderate	
	Housing and Council Tax Grant	Limited	Moderate		Moderate
	Housing and Council Tax Grant - Control Framework			Full	
	Fraud and Error Unit			*Moderate	
Treasury Management	Short Term Investments	Moderate	Substantial	Substantial	
	Banking Contract		Substantial		Moderate
	Bank reconciliations	Substantial	Moderate	Limited	
General Ledger:	Review of Opening Balances		Moderate		
	Feeder systems and reconciliation processes	Substantial		Substantial	
	VAT	Limited			
	PAYE	Moderate			Moderate
	SIMS/Oracle Reconciliation			Moderate	
	SSID Oracle reconciliation			Moderate	
	Journals			*Moderate	
	Key controls and reconciliations			*Limited	
Financial Planning	MFTP - Control Design			Full	Substantial
	Budgetary Control & Financial Reporting	Moderate		**Substantial	
Housing Rents	Compliance with key controls	Moderate			Moderate
Insurance	Governance review			Moderate	Moderate

CORE GOVERNANCE RISKS

Information Governance	Data Quality	Moderate	Substantial		
	Sickness Absence			Moderate	
	Freedom of Information		Substantial		
	Information Security	Moderate	Moderate	Moderate	
	Payment Card Industry Data Security Standard		Limited	Limited	
	Caldicott arrangements (A&CS)	Moderate	Moderate		
	Home working		Moderate		
	Internet Security	Moderate	Moderate		
	Standards Compliance			Moderate	
	Mobile computing		Substantial		
	SQL Server		Moderate		
	Code of Connection (CoCo)	Moderate	Moderate		
	Business Continuity for IT		Limited		
	IS-IT Strategy		Substantial		Moderate
	Software Licenses		Limited		
	Information Security:	Limited			
	3rd Party Acceptable Use		No Assurance		
	Business Continuity Planning		No Assurance		
	Personal Information		Limited		
	Organisational Arrangements		Moderate		
	ICT Asset Management			*Moderate	
	Applications Review			*Moderate	
	ITSS	Substantial			
	Change Controls	Moderate			
	Unix Security	Moderate			
	Network Management	Moderate		Moderate	
	Windows Security	Substantial			
	E-Tendering	Substantial			
Compliance with HR Policies and Procedures	Flexi System			Moderate	Moderate
	Recruitment and selection			*Moderate	
Procurement	Exemptions and Variations			*Moderate	
	Tenders			Substantial	Substantial
	EU Regulations			Substantial	
Capital Programme Management	Key Controls			Moderate	Moderate
Equality, Diversity and Community Cohesion	Equality Impact Assessments			Full	Full
Business Continuity Planning		Substantial			Substantial
Delegated Powers		Moderate			Moderate
Key Decisions		Moderate			Moderate

SERVICE BASED OPERATIONAL RISK						
Establishment Audits	AWH		Moderate	Substantial		
	Schools FMSIS Inspections		Substantial	Substantial	Moderate	
	Schools Other			Substantial		
	Other CYPS		Limited	Substantial		
	Leisure Centres		Moderate	Moderate		
ACE	Community Associations Funding			Moderate		
	AAP Neighbourhood Fund				Moderate	
	AAP Members Initiative Fund			Moderate	Moderate	
AWH	Welfare Rights			Substantial		
	Traveller Arrangements - Illegal Encampments			Moderate		
	DECHA (Durham Employers Care & Health Alliance)		Substantial			
	DAC (Durham Assessment Centre)		Substantial			
	Shared Lives Placement Scheme			Substantial		
	Personalisation - Direct Payments		Moderate			
	Contract Monitoring				Substantial	
	Regalment Services				Substantial	
	Extra Care Housing				Moderate	
	Continuing Health Care				Limited	
	Emergency Duty Team Sectional and Overtime Costs				Substantial	
	Share lives financial inspections				Substantial	
	Gala Hospitality and Catering				Limited	
	Fees and charges - Key controls				Moderate	
	Various service based financial systems		Substantial	Substantial		
	CYPS	Education Psychology Service			Moderate	
		Children missing from education			Substantial	
Review of Free School Meals Eligibility in Primary Schools				Moderate		
External & High Cost Child Placements				Substantial		
ITSS			Substantial			
Community of Learning - Extended Services Cluster				Moderate		
School Transport			Limited			
School Transport Charging Arrangements					Full	
Voluntary Funding Arrangements in Schools					Moderate	
Safe recruitment and selection arrangements within schools					*Limited	
School Academy Transfer Arrangements					Moderate	
BSF Programme					Substantial	
Schools SLA's					Moderate	
School Budget Preparation and Monitoring					Substantial	
School Governor Support Service					Moderate	
Summary of service based financial systems		Limited	Substantial			
Education Development Service				Substantial		

PENSION FUND	Deferred Benefits		Substantial		
	Contributions (Internal and External)		Substantial	Moderate	
	Bank Reconciliation		Limited		
	Transfer Values and Interfund Transfers	Moderate			Moderate
	Benefits and Allowances	Substantial			
	Governance			Limited	
	Investments			Substantial	
	Benefits and other payments			Moderate	
*Draft Report					
** Indicative					

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Audit Committee

28 June 2012



Internal Audit Plan 2012-13 (JULY 2012 TO JUNE 2013)

Report of Don McLure, Corporate Director Resources

Purpose of the Report

1. To submit the proposed Annual Internal Audit Plan for 2012-13. Due to the revised audit planning year agreed last year, this covers the period July 2012 to June 2013.

Background

2. The agreed audit strategy and terms of reference for the internal audit service are detailed in the Internal Audit Charter, last reviewed by the Audit Committee in October 2011.
3. The types of audit work included in Annual Internal Audit Plans are as follows:

Planned Assurance Reviews

4. The key responsibility of internal audit is to provide an independent annual assurance opinion on the adequacy and effectiveness of the Council's control framework and environment - including risk management, control and governance arrangements. This is a statutory requirement.
5. The Council's Control Framework is the key controls in place to manage key risks. Independent assurance is required to:
 - ensure that risks have been properly identified and assessed (strategic and inherent/operational)
 - control design is adequate to manage identified risks
 - controls are effective in practice
6. Responsibilities for ensuring an effective control framework are defined as follows:
 - **1st Line** – front line/day to day management - responsible for establishing controls to mitigate risks
 - **2nd Line** – oversight function e.g corporate risk management, corporate performance management, service based quality assurance and compliance teams
 - **3rd line** – internal audit, external audit, external inspection/review agencies and the Audit Committee - provide independent review of 1st and 2nd line of defence.
7. Independent assurance is provided by Internal Audit to fulfil the requirements of a number of customers/stakeholders, namely:

- Service Managers
 - Corporate Management Team
 - S151 Officer
 - Monitoring Officer
 - External Audit
 - External bodies
 - Audit Committee/Council
 - The Public
8. The audit strategy reflects the implementation of a revised risk based approach to internal auditing to help embed operational risk management through the use of a Control Risk Assessment (CRA) methodology. Operational risks are those that arise directly from the core activities of delivering services that may not always be documented.
9. Operational risk types include:
- Financial Management Risks
 - Project Risks
 - Performance Management Risks
 - Partnership Risks
 - Human Resources Risks
 - IT Risks
 - Procurement and Contract Risks
 - Legal Risks
 - Service Specific Risks
10. To enable a systematic review of key risks and key controls across the whole Council, which is necessary to inform the annual audit opinion, an exercise was begun last year in consultation with service managers to identify all key service activities on which assurance is required by, “those charged with governance,” which in this Authority is the Audit Committee.
11. This led to the development of a draft strategic audit plan that was endorsed by Corporate Management Team (CMT) and approved by the Audit Committee on 8th June and 30th June 2011 respectively.
12. The agreed audit strategy to provide independent assurance, as detailed in the Internal Audit Charter, can be summarised as follows:
- To work in consultation with senior management teams and other providers of assurance to prepare strategic and annual audit plans
 - To carry out planned assurance reviews of all key service activities/systems over a rolling 5 year programme
 - To focus on key risks and key controls where there is little or no assurance
 - To take assurance from the work of 1st and 2nd line of defence to reduce or tailor audit reviews of the 1st Line.
13. In accordance with the agreed audit strategy, we will, in consultation with the nominated service manager or key contact, prepare a Control Risk Assessment (CRA) prior to the start of each planned assurance review included in annual audit plans to:

- Identify and agree key service/system operational objectives
- Assess and agree key risks
- Identify and agree expected/existing key controls
- Identify other key sources of assurance and what assurance they provide that risks are effectively managed
- Inform the scope and terms of reference for audit
- Identify key stakeholders/contacts and circulation list for report
- Provide a mechanism for on going **self**-assessment post audit (CRSA)

14. Wherever possible Internal Audit will seek to place reliance on the work of other assurance providers to avoid any unnecessary duplication.

15. In the longer term, it is intended that all key risks and key controls and the level of assurance provided by all key assurance providers are captured in assurance maps, categorised by risk type. These assurance maps will underpin the Council's assurance framework and provide clarity to CMT and the Audit Committee on how and when assurance is provided that key controls are both adequate and effective in managing identified risks. Any duplication or gaps in assurance identified through the mapping process should then provide a basis for a more co-ordinated and coherent approach to future assurance provision.

Counter Fraud Work

16. Provision is also made in annual audit plans to support service managers at an operational level to mitigate the strategic risk of fraud and corruption. Given the current economic climate and the extent of change across the Council this risk has increased.

17. Work carried out under this category includes:

- Preparing and promoting the Council's Counter Fraud and Corruption Strategy
- Helping service managers identify fraud risks and design controls to prevent and/or detect fraud occurring
- Conducting counter fraud reviews to help detect fraud and error in known high risk areas
- Supporting managers to investigate fraud
- Helping service managers prevent reoccurrences
- Monitoring and reporting upon fraud & irregularity activity

Grant Certification Work

18. Some provision is made in internal audit plans for the certification of grant claims where grant conditions of external funding providers require it.

Follow Up

19. Provision is made in annual plans to provide assurance that management responds appropriately to address agreed weaknesses in controls, identified through the audit process, which may increase the impact or the likelihood of risk occurring above an acceptable level.

Monitoring and Reporting

20. Provision is made in the plan for monitoring the delivery of the agreed plans to the required professional standards and for reporting progress to Corporate Directors and the Audit Committee on a quarterly basis. This reporting mechanism will also allow a regular forum for consideration of new or emerging risks.

Advice and consultancy role and contingency provision

21. Given the extent of the transformation and change agenda with which the Council is faced at this time, it is important that audit plans are flexible and allow for the service to be pro active in supporting management in the consideration of control issues relating to new or emerging risks. Consequently it is proposed that only approximately 70% of estimated audit resources available to allocate to service based reviews are allocated each year. The remaining 30% will be set aside as a contingency provision to respond to:

- New and emerging risks including fraud and irregularity investigations
- Support in the development and implementation of projects, processes or new initiatives
- Ad hoc requests for advice and guidance
- Known weaknesses in the control environment identified through fraud and irregularity investigations or planned assurance work where additional or follow up work is required.

22. Service requests are encouraged at any time and will be considered in relation to the risk and the type of audit work required e.g. control design and/or compliance assurance, grant certification work, advice and consultancy etc, and whether or not the service has the necessary skills and resources to undertaken the work requested.

23. Any proposals to amend approved plans will be discussed with Corporate Directors and any significant changes will be reported to the Audit Committee for approval.

Preparation of 2012-13 Audit Plan

24. Year 1 of the strategic audit plan agreed last year formed the basis of the 2011-12 annual audit plan. Yrs 2-5 were only provisional and subject to consultation and agreement as part of the annual planning process.

25. In consultation with Service Groupings Senior Management Teams, the provisional strategic plan has been reviewed and revised to reflect changes in structures and service activities and preference for the timing of reviews initially scheduled for Yr 2 of the strategic plan.

26. The draft proposed annual audit plan for 2012-13 is attached as Appendix 2. This incorporates:

- Corporate Provisions
- Work started in 2011-12 where provision will be needed beyond 30th June
- Work deferred from the approved 2011-12 plan carried forward into 2012-13 as previously agreed.

- Work scheduled for Yr 2 from the draft strategic plan - revised following consultation
 - Service Requests
27. Given the audit strategy outlined above it is particularly important that we engage with the most appropriate officer(s) at the planning and preparation stage to discuss and develop the CRA. This stage of the audit process is therefore key to the effectiveness of the audit and inevitably requires access to the right people and information at the right time to allow us to complete planned reviews effectively and within agreed timescales. The nominated key contact(s) should therefore be the officer best placed to identify and agree service objectives, key risks, key controls, other assurance sources and the resultant draft audit report.
28. We will endeavour to schedule agreed work within the timing preference expressed by services, but inevitably this may not always be possible due to the practicalities of scheduling work across all service groupings to match estimated audit resources available. It should also be noted that given the importance of the planning and preparation stage of the audit process, planning meetings will normally be scheduled with identified key contacts well in advance of the proposed timescale for completing the audit fieldwork. It is not until the CRA is complete and the scope and TOR is agreed that we have a better understanding of what reliance can be placed on the work of other assurance providers and the audit resources required to complete the fieldwork. Consequently, planning meetings for an audit review scheduled to be undertaken at an agreed time may commence several weeks or months in advance. The wider the scope, eg a cross cutting corporate review the longer the lead in time is expected to be as it may be necessary to consult with a number of people.
29. The estimated gross audit days available to deliver the Council's Internal Audit Plan for 2012/13 have been determined as follows:

Estimated Gross Days Available (20.5 FTE)	5333	100%
Less overheads:		
<i>Uncontrollable</i> , e.g. annual leave, bank holidays, sickness, maternity		18
<i>Controllable</i> , e.g. training, divisional/ departmental duties		14
Productive Days Available	3626	68%
Less days to external organisations:		
Durham Police Authority	180	
Durham and Darlington Fire & Rescue Authority	75	
Pension Fund	20	
Durham Joint Crematorium	22	
Mounsett Joint Crematorium	20	
Durham City Charter	6	
	323	
Productive Days Available to Durham County Council	3303	62%

30. Monitoring of the plan will continue during the year through quarterly progress reporting to provide feedback on delivery and to discuss any new or emerging risks.

Recommendations

31. It is recommended that Members :

- Note the audit strategy previously agreed.
- Approve the proposed audit plan, as detailed in the attached Appendix 2.

Contact: Avril Wallage Tel: 0191 3833537

Appendix 1: Implications

Finance

No direct financial implications

Risk

None

Staffing

None

Equality and Diversity / Public Sector Equality Duty

None

Accommodation

None

Crime and disorder

None

Human Rights

None

Consultation

None

Procurement

None

Disability Discrimination

None

Legal Implications

Compliance with the Accounts and Audit Regulations 2011

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CORPORATE PROVISIONS		DAYS	SUB T	TOTAL
PLANNING, REPORTING AND SERVICE DEVELOPMENT				
Planning and reporting		250		
Follow Up		200		
Quality Assurance and Performance Monitoring (Including development of Audit Manual)		70		
Development of Audit and Risk Management Software (Including improving development of library key of inherence/operation risks)		30		
Further Development of Corporate Assurance Mapping		20		
Audit Committee Reporting and Support		40		610
COUNTER FRAUD				
Counter Fraud Awareness	Maintaining awareness of new initiatives, promoting fraud awareness, monitoring and	50		
NFI	Co-ordination of NFI submissions and outcomes. Included service request to amend I	50		
Grants Receivable	To identify all main external grant funding sources and development and implement a risk assessed programme of compliance assurance testing in this high risk fraud	20		
Grants Payable	To identify all grant payments made by the Council and develop and implement risk based programme of compliance assuring testing in this high risk fraud area.	20		
Cash Security	Review of cash collect points and cash security guidance & unannounced spot checks	10		
Payroll	IDEA Data interrogation/Analysis	20		
	Timesheets Authorisation	10		
	Overtime - duplicate/inflated claims	10		
	Starters and leavers	20		
Expenses & Allowances	Data Analysis to test for duplicate/inflated claims	20		
Creditor Payments	IDEA Data Interrogation	40		
Housing Tenancy	Testing to detect sub letting. Dependent on outcomes from review of planned assurance work in this area.	5		
Contingency for Fraud & Irregularity Investigations	Provision to complete investigations in progress at the year end and new cases arise	300		575
CORPORATE GOVERNANCE				
Strategic Risk Management	Review of effectiveness of Corporate Risk Management Arrangements - Test sample of effectiveness of controls in place identified in strategic risk registers to mitigate identified risks	10		
Corporate Governance	Review of the effectiveness of self assessed governance arrangements in place to inform the annual review of the effectiveness of the Council's Corporate Governance Arrangements - Test sample of arrangements in place where no other source of	10		
Scheme of Delegation	Corporate review of arrangements in place for services to establish operational schemes of delegation to ensure adequate segregation of duties and clarify over roles, responsibilities and accountability for day to day management decisions	10		
Corporate Assurance Framework	Further work to support development of a Corporate Assurance Framework	10		40
GRANT CERTIFICATION	Provision to respond to service requests to certify grant claims from external funding	40		40
ADVICE AND CONSULTANCY CONTINGENCY	Provision to address new and emerging risks and to complete work in progress at the 30-6-12	555		555
				1820

SERVICE ACTIVITY/RISK AREA	SERVICE	PROPOSED AUDIT SCOPE	TYPE OF AUDIT WORK	TIMING PREFERENCE	DAYS	SUB T	TOTAL
ACE							
AUDITS DEFERRED FROM 2011-12							
Business Continuity							
Policy & Communications		Review of overall control framework	Assurance		20		
SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN							
Corporate Communications	Policy & Communications	Support to Development of New Internet Review of effectiveness of Control Framework relating to New Internet	Advice & Consultancy Assurance	July/August 2012 Oct/Nov 2012	5		
Data Quality	Planning & Performance	Rolling programme of risk assessed performance indicators	Assurance		10		
Data Protection	Planning & Performance	Rolling programme of reviews:			40		
		Training Review	Assurance	Sept/Oct 2012	10		
		Review of Access to Personal Data on System	Assurance	Jan/Feb 2013	10		
Information Governance General	Planning & Performance	On going representation on Information Governance Group	Advice & Consultancy		3		
Partnerships Governance	Partnerships & Community Engagement	Risk Assessed Rolling Programme of Review of Partnerships Governance Arrangements	Assurance		30		
Community Engagement	Partnerships & Community Engagement	Community Building Funding	Advice & Consultancy	Sept/Oct 2012	5		
Overview & Scrutiny	Overview & Scrutiny	None. No independent assurance considered necessary by Management. Reliance placed on management assurance processes in place given the nature of service i.e. It is itself a provider of assurance on the activities of other service areas.					133
AWH							
WORK IN PROGRESS @ 30-6-12							
Public Health Transition	PPP	Support to Receiver Group on due diligence	Assurance		20		
SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN							
County Durham Care (In house service provider)	Adult Care	Review of overall control framework	Assurance		30		
Assessment and Review of Care Needs	Adult Care	Review of overall control framework	Assurance		20		
Management of service users finances and Property	Finance Services	Review of overall control framework	Assurance		15		
Information Governance	PPP	Caldcott Compliance	Assurance		5		
Adult Learning Service	Social Inclusion	Review of overall control framework. To incorporate request from service to review effectiveness of financial recovery arrangements	Assurance	April 2013	20		
SERVICE REQUESTS							
Personalisation/Direct Payment	Adult Care /Commissioning	Review of effectiveness of overall management of the scheme.	Assurance		30		140
CYPS							
AUDITS DEFERRED FROM 2011-12							
Planning & Quality Assurance within CYPS and the Children's and Families Trust							
Early Intervention & Partnership Service		Review of overall control framework	Assurance		20		
SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN							
Looked After Children	Safeguarding and Specialist Services	Review of overall control framework. Service request to follow up VFM study to be incorporated.	Assurance		15		

SERVICE ACTIVITY/RISK AREA	SERVICE	PROPOSED AUDIT SCOPE	TYPE OF AUDIT WORK	TIMING PREFERENCE	DAYS	SUB T	TOTAL
Specialist Services	Safeguarding and Specialist Services	Review of overall control framework To incorporate service request to focus upon Prevention and Early Intervention	Assurance		15		
School Admissions	County Wide Services	To further develop work undertaken previously in this area by writing a program that staff would run to interrogate Admissions data rather than having to manually input the parameters themselves	Advice and Consultancy		2		
Learning Support Services	County Wide Services	Review of overall control framework	Assurance		15		
Durham Schools Continuing Professional Development Partnership	Achievement Services	Review of overall control framework	Assurance		15		
Safeguarding of Children in Schools	Achievement Services	Review of overall control framework	Assurance		10		
Schools	Achievement Services	Financial Management. Visits to the 9 schools who had not achieved FMSIS.	Assurance		50		
Information Governance	Early Intervention & Partnership Service	Risk Assessment of Key Schools Risks to inform future assurance needs of both the LA and the Schools Governing Bodies	Advice and Consultancy		10		
	Early Intervention & Partnership Service	Caldicott Compliance	Assurance		5		
SERVICE REQUESTS							
School Attendance Enforcement	County Wide Services	Fixed Penalty Notice Arrangements	Advice & Consultancy		2		
Award of additional pay in Schools	Achievement Services	Review to consider effectiveness of performance management / award arrangements.	Assurance		15		
MTPF Savings - Home to School and College Transport		VFM from corporate contracts - robustness of estimated budget savings	Assurance		5		
One Point - Integrated Services with NHS	Early Intervention & Partnership Service	Review of overall governance arrangements, financial and operational management	Assurance		15		
Troubled Families Programme	Safeguarding and Specialist Services	Review of grant governance arrangements	Assurance		10		
School Benevolent Fund		Verification of annual accounts	Third Party Assurance		5		209

NEIGHBOURHOOD SERVICES

AUDITS DEFERRED FROM 2011-12

Pollution Control	EHCP - Environmental Protection	Review of overall control framework	Assurance	Oct-12	15		
Refuse & Recycling	Direct Services - Streetscene	Review of overall control framework	Assurance	2013-14	0		
Strategic Waste Management	Direct Services - Strategic Waste	Review of overall control framework	Assurance	2013-14	0		

SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN

Bereavement Services	Direct Services - Streetscene	Review of overall control framework	Assurance		15		
Non Council Services	Direct Services - Fleet	Review of policies and procedures relating to employee service/purchase schemes e.g. MOT's / Car Servicing / Taxi MOTs	Advices and Consultancy		5		
Enforcement & Education	Direct Services - Streetscene	Follow up to work commenced in 11/12 but deferred pending review of service	Assurance		10		
Construction Services and Planned Maintenance Programme	Direct Services - Building and Facilities Maintenance	Review of overall control framework	Assurance		20		
Housing Maintenance	Direct Services - Building and Facilities Maintenance	Review of overall control framework	Assurance		20		
Public Health Enforcement - Mandatory Licences	EHCP - Environmental Protection	Review of overall control framework	Assurance		10		
Events Management	Sport & Leisure - Events Management	Review of effectiveness of control framework - Compliance testing follow up of 11/12 review control framework	Assurance		10		
Stores Management	Financial Management	Review of overall control framework	Assurance		15		

SERVICE ACTIVITY/RISK AREA	SERVICE	PROPOSED AUDIT SCOPE	TYPE OF AUDIT WORK	TIMING PREFERENCE	DAYS	SUB T	TOTAL
SERVICE REQUESTS							
Gala Theatre	Sport & Leisure - Indoor Facilities	Review of contracting arrangements relating to productions, show settlements and merchandising	Assurance		15		
Stalls Management	Technical Services	On site processes for stores management disposal of scrap .	Advice and Consultancy - Counter Fraud Risk	Jul-12	15		
Budgetary Control	Technical Services	Duplicate receipting of invoices on Oracle and allocation of costs to budget heads.	Advice and Consultancy		5		
Cash and Income Management	Sport & Leisure - Indoor Facilities EHCP	Review of cash reconciliation and cash receipting arrangements (including analysis of alternative methods) and recovery	Assurance		15		
Energy Management	Sport & Leisure - Indoor Facilities	Review of bill payment arrangements and effectiveness of budgetary control	Assurance		10		
County Durham Sport Markets	Sport & Leisure - Indoor Facilities EHCP - Consumer Protection	Certification of Accounts	Grant Certification		10		
MTFP Savings	Direct Services - County Fleet	Review of Market Strategy	Advice & Consultancy		5		
Stanley Bowls Club	Direct Services - County Fleet	Use of Council vehicles for home to work journey	Advice & Consultancy		10		
	Sports & Leisure	Annual Audit of Accounts	Third Party Body		5		210

RESOURCES

AUDITS DEFERRED FROM 2011-12

Oracle EBS	Corporate Finance	Application review - access and privileges set up	Assurance		20		
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SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN

Committee Services	Legal & Democratic Services	Review of overall control environment	Assurance		10		
Compliance with laws and regulations	Legal & Democratic Services	Representation of RIPA Working Group	Advice & Consultancy		3		
Overall Financial Management	Finance	S151 Compliance	Assurance		15		
Compliance with HR Policies and procedures	HR&OD	Compliance with flexible working policy and that contract variations correctly reflected in HR/Payroll Records	Assurance		20		
Payroll	HR&OD	Key Controls	Assurance		20		
General Ledger	Corporate Finance	Taxation/Payee	Assurance		10		
	Corporate Finance	EBS Workstream support	Advice & Consultancy		5		
	Financial Services	VAT	Assurance		10		
	Corporate Finance	Bank Reconciliation (excluding income)	Assurance		15		
	Financial Services	Revenues & Benefits reconciliations (Note: To exclude reconciliations from the scope of the reviews of HB, CT, NNDR and debtors)	Assurance	July/August 2012	20		
Treasury Management	Corporate Finance	Short term investments	Assurance		10		
Provision of services to third parties	Corporate Finance	Banking arrangements	Assurance		15		
	Corporate Finance	Review of SLA's for external bodies - excluding ICT which has been already subject to separate review	Assurance		15		
Procurement	Corporate Finance	Representation on SPN	Advice & Consultancy		3		
	Financial Services / Corporate Finance	Procurement Cards	Assurance		10		
Financial Planning	Financial Services	Budgetary Control and Financial Reporting	Assurance	Sept/Oct 2012	30		
P2P	Financial Services / Corporate Finance	Key Controls	Assurance		30		
Housing and Council Tax Benefits	Financial Services	Housing Benefit Grant Claim (Subsidy)	Assurance		10		
NNDR	Financial Services	Key Controls excluding reconciliations	Assurance		30		
Council Tax	Financial Services	Key Controls(excluding reconciliations)	Assurance		25		
	Financial Services	Key Controls(excluding reconciliations)	Assurance		30		
	Financial Services	Support on implementation of Local Council Tax Scheme	Advice & Consultancy		5		
Cash and Income Management	Financial Services	ICON Cash Management (including income bank reconciliation)	Assurance	Jan/Feb 2013	30		

SERVICE ACTIVITY/RISK AREA	SERVICE	PROPOSED AUDIT SCOPE	TYPE OF AUDIT WORK	TIMING PREFERENCE	DAYS	SUB T	TOTAL
Information Security		Use of Credit/Debit card terminals	Assurance	Jan/Feb 2013	5		
		Income and Debt Recovery	Assurance		25		
	ICT	Information Security Policy Compliance Reviews;	Assurance	Each quarter	20		
		- Forensic Readiness - Security Incident Management - Systems Development & Maintenance - Warranty					
Business Support	ICT	Information Security Forum	Advice & Consultancy		3		
Technical Services	ICT	Income and expenditure arrangement Project	Assurance		10		
	ICT	Unix Security	Assurance		10		
	ICT	Windows Security	Assurance	July/August 2012	10		
	ICT	Internet Security	Assurance		10		
SERVICE REQUESTS							
Corporate Credit Cards	Corporate Finance	Risk of inappropriate usage	Assurance	April/May 2013	5		
Collection Fund	Corporate Finance	TBA	Advice & Consultancy		5		
Leases	Corporate Finance	TBA	Advice & Consultancy		15		
Oracle EPM Project	Corporate Finance	TBA	Advice & Consultancy		5		
Oracle BI Project	Corporate Finance	TBA	Advice & Consultancy		5		
Oracle R12 Project	Corporate Finance	TBA	Advice & Consultancy		5		
Petty Cash	Financial Services / Corporate Finance	Risk of inappropriate usage	Assurance	After Sept 2012	20		
Invoice scanning and indexing arrangements	Financial Services	TBA	Advice & Consultancy	July/August 2012	5		
Information Security	ICT	Access / Password Controls	Assurance		10		
Public Services Network	ICT	TBA	Assurance		10		569
RED							
AUDITS IN PROGRESS @ 30-6-12							
Taxi Contracts	Transport & Contract Services	Continuation of review of taxi contracts.	Advice and Consultancy		15		
AUDITS DEFERRED FROM 2011-12							
Implementation of new planning system	Planning & Assets	Project assurance support	Advice & Consultancy		10		
Grants	Strategy, Policy and Partnerships	Review of grants bidding protocol and control of grants claimable	Advice & Consultancy/Counter Fraud		30		
Business Durham	Economic Development & Housing	Review of overall control framework following merger of CDDC and Business Services	Assurance	Nov/Dec 2012	20		
ALMOs Contract Monitoring	Economic Development & Housing	Review of overall control framework	Assurance	Sept 2012	20		
SERVICE ACTIVITIES SCHEDULED IN STRATEGIC PLAN							
Visit County Durham	Economic Development & Housing	Review of overall control framework	Assurance	Sept/Oct 2012	10		
Private Sector Housing	Economic Development & Housing	Review of overall control framework	Assurance	Jan/Feb 2013	15		
Housing Tenancies	Economic Development & Housing	Review of overall control framework	Assurance		30		
Supported Housing	Transport & Contract Services	Review of overall control framework	Assurance	July/August 2012	15		
SERVICE REQUESTS							
Development Control - Mystery Shopping	Planning & Assets		Advice & Consultancy	After July 2012	10		
Project Genesis	Strategy, Policy and Partnerships		Project Assurance		30		
Projects outside of scope of corporate programme	Transport & Contract Services		Advice & Consultancy		3		
Utility Bills - Contract management system review	Planning & Assets		Advice & Consultancy		15		1484
TOTAL AUDIT RESOURCES REQUIRED							3304

Contingency 855
Contingency as a % of total available days 26%
Contingency as a % of total days available less planning provision 32%

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AUDIT COMMITTEE

28th June 2012



Review of the Effectiveness of Internal Audit

Report of Don McLure, Corporate Director of Resources

Purpose of the Report

1. The purpose of this report is to advise Members of the outcome of the annual review of the effectiveness of Internal Audit.

Background

2. The Authority has a requirement under the Accounts and Audit (England) Regulations 2011 to review the effectiveness of Internal Audit each year. Internal Audit is an important element of the system of internal control and consideration of its effectiveness contributes to the annual review of the Authority's corporate governance arrangements, and is required to inform the Annual Governance Statement (AGS). If Internal Audit is not considered effective, the reliability of the annual internal audit opinion is in question.
3. The outcomes of the last review carried out by the Corporate Director Resources, and considered by the Audit Committee in June 2011, were informed by work undertaken during the year, an assessment of compliance with the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 and an assessment of compliance with CIPFA's Statement on the role of the Head of Internal Audit (HIA) in public sector organisations. The review concluded that the service is effective but noted that some improvements had been identified for the service to be fully compliant with the requirements of the Code and the Statement.

Improvements made during the year

4. The main areas where improvements were identified from the last exercise related to:
 - Embedding a risk based audit approach
 - Improving relationships with other regulatory and inspection agencies
 - Improving assurance on programme and project risks

5. In response, the Internal Audit Charter, which defines the detailed terms of reference and audit strategy, was reviewed during the year to reflect an improved risk based auditing approach. This revised approach is summarised as follows:
- To work in consultation with senior management teams and other providers of assurance to prepare strategic and annual audit plans
 - To carry out planned assurance reviews of the effectiveness of the management of operational risks in all key service activities/systems over a rolling 5 year programme (Strategic Plan)
 - To carry out assurance reviews of the management of strategic risks where the effective management of the risk is heavily dependent on identified controls
 - To carry out annual reviews of key risks where a high level of assurance is required to demonstrate the continued effectiveness of internal controls, for example those associated with key financial systems
 - To use a Control Risk Assessment (CRA) methodology to focus audit resources on providing assurance on key controls where there is little or no other assurance on their adequacy or effectiveness
6. The use of a CRA methodology provides a much more focused and consistent approach to the development of the scope of audit assurance reviews. Reviews are informed by an assessment of key risks and other sources of assurance agreed with the key contact as part of the planning and preparation process of each assignment.
7. Audit processes have also been revised during the year to reflect this risk based approach. These include:
- A revised Terms of Reference format informed by the agreed CRA.
 - A revised audit report format to help focus executive summaries on key findings i.e. those that will increase the impact or the likelihood of key risks occurring if not addressed. The CRA is updated at the end of the process and issued with final reports to reflect actual controls in place and provides a mechanism for on-going self-assessment.
 - A revised methodology for categorising the importance of audit findings, resultant recommendations and audit assurance opinions.
 - The introduction of a Post Audit Evaluation (PAE). This is carried out by the lead auditor in conjunction with the relevant audit manager on

the completion of each audit. In addition to providing a mechanism for reflecting on what went well during the audit and identifying any areas for improvement, the PAE also consists of an audit need risk assessment which is used to inform the strategic audit plan and future audit coverage.

8. Work was begun during the year to develop a corporate assurance framework to help identify key assurance providers and the assurance they provide on the management of risks and / or the effectiveness of internal controls. As a result, a corporate assurance framework was approved by full Council in December. This provides a high level illustration of the Council's assurance framework but further work is needed in the current year to understand the nature of assurance provided and to develop a more co-ordinated and coherent approach to assurance provision.
9. More resources were allocated in 2011/12 to improve assurance on programme and projects. However, some work scheduled in this area has not progressed, at the request of management, due to concerns about duplication with other assurance providers and the demands placed on service managers. Whilst the CRA approach seeks to ensure that reliance would be placed on the work of other assurance providers wherever possible, these concerns have emphasised the need for clarity over roles and responsibilities of the various internal providers of assurance and on which risks they provide assurance. Work has therefore begun to clarify the roles and responsibilities of other assurance providers, whether internal or external, and the nature and limitation of what assurance they provide as part of development of the corporate assurance framework. This will however take time to develop and require the investment of not only internal audit resources but also that of senior management.
10. Briefing sessions have been provided to the Improvement Planning Group (IPG) and Tier 4 managers to improve understanding of the role and work of internal audit and how the service can help support managers through the added value of independent and objective assurance.
11. In recognition that the in house risk and audit service may not have all the necessary skills and experience to provide reliable assurance in the specialist area of the Pension Fund, an internal audit partner was appointed to develop a strategic risk register and assurance map in consultation with management and the Pension Fund Committee. The partner was also commissioned to deliver pension fund audit in 2011/12. This partnership arrangement has allowed the opportunity of skills transfer and the sharing of best practice with the in house team which has contributed to further improvements to audit processes and procedures introduced during the year. The appointment of an external partner has also enabled the "call off" of additional audit resources when required and the contract has therefore been extended on this basis for another year. Audit coverage of the pension fund for 2012/13 is to be considered in consultation with management and the Pension Fund Committee following review of performance in 2011/12.

12. The Head of Internal Audit now reports direct to the Corporate Director Resources rather than the Head of Finance. This change has helped raised the profile of the audit service and improved its independence. It has also provided a better platform for the work of the service to influence senior management.

. Approach to this years annual review of effectiveness

13. This years review of effectiveness has been informed following consideration of an approach suggested by the external auditor and consists of a series of questions considered independently by:

- The Chair of the Audit Committee
- The Corporate Director Resources
- External Audit
- The Head of Internal Audit

14. Copies of the completed questionnaires are attached as Appendices 2, 3, 4 and 5.

15. It should be noted that responses provided by the Corporate Director Resources and the Head of Internal Audit also incorporate feedback from other Corporate Directors following 1-2-1 discussions reflecting on effectiveness in 2011/12 as well as consideration of priorities for audit coverage in 2012/13.

Conclusions

16. The service has made good progress in implementing a risk based approach to auditing. This is particularly important given the reduction in audit resources as a result of budget efficiencies.

17. Audit Plans to develop assurance maps, linked to identified and agreed key risks, as the CRA approach is rolled out across all services, will provide an improved understanding of the risk profile of the Council and lead to a more co-ordinated and coherent approach to assurance. This in turn will improve the risk based approach to strategic audit planning.

18. It has been recognised that the skills mix of the in house team needs improving in the specialist areas of IT audit and fraud investigation and plans are already in place to address this.

19. Plans to increase IT audit resources will enhance the skills and knowledge in this specialist area, improve succession planning, enable independent forensic investigations and provide greater flexibility to respond to changing demands on the service.

20. Plans to increase fraud investigative skills will enhance the investigation of irregularities and allow planned counter fraud work to progress on a more

timely basis. This will help improve the management of fraud risk within the Council and help it to respond to the requirements of “Fighting Fraud Locally” which is the National Fraud Authority’s strategy to help reduce fraud in the public sector.

21. The planned investment in IIA qualifications will not only help develop those individual members of staff undertaking the training but will also help embed the risk based approach across the whole service through the sharing of best professional practice and additional support available through the IIA. The profile of the service will also be raised by having a number of IIA qualified staff and should make the service more marketable to potential new external clients.
22. The engagement of an external partner has increased the flexibility of the service to respond to changing demands and has provided access to additional, skills, knowledge and experience to supplement the in house team when required.
23. Overall the effectiveness and performance of the service is considered adequate and continues to improve. It is particularly pleasing to note that since the introduction of the CRA methodology the percentage of customers scoring the audit service good or above (4 out of 5) has increased from 87% to 96%.
24. It is also pleasing to note that the external auditor has observed that, “the standard of audit reports has improved in recent years, including progress reports which are now much clearer.”
25. The comments made by the Chair and Vice Chair in their assessment of the service are acknowledged and a training session for the Committee will be arranged for the Head of Internal Audit to go through the risk based approach and the whole audit process in a practical session.
26. The need to improve the monitoring of managers progress in the implementation of agreed audit recommendations as highlighted in the Chair and Vice Chair’s assessment is also acknowledged. Whilst there has been good progress in implementation, performance does vary across service groupings. In future, the Head of Internal Audit will provide more detail of key findings from audit work completed each quarter, together with overdue recommendations, in progress reports, (not just the statistics) so that the Committee will be in a better position to evaluate the added value from audit work undertaken and where necessary challenge management on the lack of progress made in addressing issues raised.
27. It is recognised by the Head of Internal Audit that further improvements can be made to enhance effectiveness and improve performance in delivering agreed targets and the efficiency of some audit processes. To help achieve this, performance management processes are being reviewed and all aspects of audit work, processes and procedures will be documented in a comprehensive updated audit manual to improve the

existing quality assurance framework. There is an action in the Resources Service Plan to achieve this by 31/3/13.

Recommendations

28. Members are asked to consider the responses provided in appendices 2, 3, 4 and 5 to gain assurance on the effectiveness of internal audit and to place reliance on its work.

**Contact: Don McLure, Corporate Director Resources Tel 0191
383 33675**

Appendix 1: Implications

Finance

There are no direct financial implications arising for the Council as a result of this report.

Staffing

None

Risk

None

Equality and Diversity

None

Accommodation

None

Crime and disorder

None

Human rights

None

Consultation

None

Procurement

None

Disability

None

Legal Implications

Compliance with Accounts and Audit Regulations 2011

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EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

Completed by the Chair and Vice Chair on behalf of the Audit Committee

Understanding

How well does internal audit demonstrate that it:	Strong	Adequate	Needs improving
Recognises its accountability to the audit committee;	√		
Has a strong understanding of the responsibilities and operation of the audit committee.	√		
Understands the expectations of the audit committee and the chairman	√		
Understands the organisation's business and risk environment?		√	
Comments			
Internal Audit is still developing its risk based approach to audit and needs clear communication to the Audit Committee by way of training.			

Terms of Reference and Audit Strategy

Do the terms of reference for internal audit define?	Yes	No
Roles and responsibilities, including those in relation to other internal functions	√	
Expectations of management	√	
Scope of internal audit	√	

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

work		
Access to information	√	
Has internal audit's terms of reference been reviewed within the last two years?	√	
Does internal audit terms of reference reflect the organisations needs?	√	
Are internal audit's terms of reference visible to everyone in the organisation?	√	
Does internal audit terms of reference and audit strategy facilitate:		
<ul style="list-style-type: none"> Consistency in the quality of service to the organisation 	√	
<ul style="list-style-type: none"> Understanding of the organisation's business issues; 	√	
<ul style="list-style-type: none"> The delivery of value to the organisation 	√	
<ul style="list-style-type: none"> Adequate independence over the activities its audits 	√	
Comments		

Audit Resources

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

	Strong	Adequate	Needs improvement
How well does internal audit's staffing reflect its roles and responsibilities			√

	Yes	No
On the basis of the work performed by internal audit over the past 12 months, does internal audit appear to have the right mix of skills, experience in competencies in specialist areas such as IT, counter fraud, pension fund?		√
Does internal audit have a programme of staff development and skills enhancement?	√	
Does the internal audit function offer adequate career progression opportunities for its employees?	?	

Comments

There is a strong desire to develop the skills set/directory of the staff particularly in ICT and fraud but also to ensure there are enough resources to adequately staff the service.

We are not clear if there is a pathway for the promotion and development of staff

Communications

	Yes	No
Has internal audit attended all the audit committee meetings it was scheduled to attend?	√	
Has internal audit made itself available for consultation outside of	√	

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

audit committee meetings?		
Does internal audit determine that the chairman of the audit committee is fully briefed on significant findings or developments prior to audit committee meetings?	√	
Have reports been received from internal audit on a sufficiently timely basis?	√	
Does internal audit promptly advise the audit committee about significant issues and significant developments, including on special projects such as fraud investigations?	√ ??	
Does internal audit promptly advise the committee about significant changes to the internal audit plan?	√	
Does internal audit contribute to the committee's understanding of the overall assurance framework within the organisation and the role internal audit plays in this framework?	√	
Does the internal audit function proactively share its knowledge widely with the business i.e. outside the strict reporting channels?	√	√

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

	Strong	Adequate	Needs improving
Evaluate internal audit's responsiveness to requests from the audit committee	√		
Evaluate internal audit's frankness and candour with the committee	√		
Evaluate internal audit's handling of difficult or contentious issues		√	
Evaluate the usual level of preparation for audit committee meetings demonstrated by internal audit.	√		
Evaluate the quality of internal audit reports and papers tabled with the audit committee. Consider their relevance and clarity.	√		
Evaluate the strength of internal audit's process to monitor the status of open matters/ recommendation		√	

Comments

The Committee needs to develop a strategy for more effective monitoring of the implementation of audit recommendations and be able to demonstrate the success and/added value of internal audit as a result.

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

Performance

Assess the quality of the internal audit plan in terms of:	Strong	Adequate	Needs improvement
Comprehensiveness, clarity and timeliness;		√	
Coverage of priority and high risk areas;		√	
Focus on testing of the control framework.	√		
What was your assessment of the scope of the internal audit as outlined in the plan?		√	
	Yes	No	
Was it clear from its reporting to the committee that internal audit:			
<ul style="list-style-type: none"> Delivered the services outlined in the plan; 			√
<ul style="list-style-type: none"> Were in accordance with the agreed timetable? 			√
Is there evidence of effective coordination of internal audit work and other assurance providers?	√		
Are success measures used for evaluation the performance of the internal audit function?			√
Does the internal audit function offer adequate career progression opportunities for its employees?	?		

EVALUATION OF INTERNAL AUDIT – AUDIT COMMITTEE

Are there sufficient performance based reward mechanisms to motivate internal audit employees?	?	
Do you consider that internal audit has added value to the organisation?	√	

	Strong	Adequate	Needs improvement
How would you assess the committee's confidence in internal audit?		√	
How would you assess internal audit's overall performance?		√	

Overall Comments
We think the plan should be S.M.A.R.T.E.R - if it was we suspect that PI's would reflect the success or areas for development

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EVALUATION OF INTERNAL AUDIT - MANAGEMENT

To be completed by Don McLure, Corporate Director Resources, on behalf of Management

Planning

	Yes	NO
Are internal audit's terms of reference sufficiently visible to everyone in your business?	<input checked="" type="checkbox"/>	
Is there sufficient pre-planning and coordination by the internal auditors with the management before each phase of the internal audit?	<input checked="" type="checkbox"/>	
Does internal audit discuss its approach and major areas of audit focus with senior management?	<input checked="" type="checkbox"/>	
Did senior management raise any major areas of concern that were not reviewed by the internal audit team?		<input checked="" type="checkbox"/>
Comments		
<p>One to ones with the Chief Internal Auditor and the Corporate Director Resources with each chief officer has helped the audit planning process significantly</p>		

EVALUATION OF INTERNAL AUDIT - MANAGEMENT

Skills and Experience

	Yes	No
Do you consider the internal audit team to have sufficient professional experience, project management, inter-personal skills and seniority to effectively carry out the work required?		<input checked="" type="checkbox"/>
Do you consider the internal audit team have sufficient experience in the functional specialisations, e.g. risk assessment, IT, fraud investigations to effectively carry out the work that was required?		<input checked="" type="checkbox"/>
Do you believe the internal audit team have sufficient understanding of the business and the risks it faces?	<input checked="" type="checkbox"/>	
Do you believe the members of the internal audit team are independent of the activities they audit?	<input checked="" type="checkbox"/>	
Do you believe the structure of internal audit allows for adequate supervision of the audit process?	<input checked="" type="checkbox"/>	

Performance

	Yes	No
Is there a formal process in place to ensure that internal audit keep senior management up	<input checked="" type="checkbox"/>	

EVALUATION OF INTERNAL AUDIT - MANAGEMENT

to date with audit progress in delivering annual plans?		
Does internal audit provide senior management with early identification and advice of contentious issues, problem areas and delays?	<input checked="" type="checkbox"/>	
Does internal audit suggest how such issues could be resolved?	<input checked="" type="checkbox"/>	
Are audit suggestions realistic, robust and presented clearly and on a timely basis?	<input checked="" type="checkbox"/>	
Are internal audit reports:		
<ul style="list-style-type: none"> • Relevant, clear and constructive 	<input checked="" type="checkbox"/>	
<ul style="list-style-type: none"> • Sufficiently detailed to enable effective management action 	<input checked="" type="checkbox"/>	
<ul style="list-style-type: none"> • issued on a timely basis? 	<input checked="" type="checkbox"/>	
Are internal audit findings discussed with senior management prior to being tabled with the audit committee?	<input checked="" type="checkbox"/>	
Does internal audit follow up recommendations to see whether they have been implemented	<input checked="" type="checkbox"/>	
Does management have any major unresolved disagreements with internal audit?		<input checked="" type="checkbox"/>
Does internal audit add value to your business?	<input checked="" type="checkbox"/>	

EVALUATION OF INTERNAL AUDIT - MANAGEMENT

In what ways does internal audit add value to your business?	By providing the assurance or otherwise of robust internal controls processes and strong, effective management of these processes		
	Strong	Adequate	Needs improvement
Assess the strength of internal audit's understanding of the organisation and the risk it faces.		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
How strongly do senior members of the internal audit team demonstrate an appreciation of the issues key to management's role and responsibilities		<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>
Do members of the internal audit team consistently demonstrate independence in all their deliberations?	<input checked="" type="checkbox"/>		
In your view, does the way in which internal audit is funded impair its independence?	No		

Comments

Good progress is being made with the Internal Audit service offer but more needs to be done.

The right strategy for the Service is now in place but the Team needs strengthening with a better skills match in order to be able to deliver the strategy.

Although there is evidence of improvement, there is still more cultural change

EVALUATION OF INTERNAL AUDIT - MANAGEMENT

required within some team members.

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EVALUATION OF INTERNAL AUDIT – EXTERNAL AUDITOR

Terms of Reference and Audit Strategy

	Strong	Adequate	Needs improvement
Evaluate internal audit's current terms of reference given your understanding of the organisation's business, complexity, risk environment and the current developments in internal audit		✓	

	Yes	No
From your knowledge of internal audit and industry best practice, do you consider internal audit's current terms of reference of appropriate quality?	✓	

Comments

The requirement to carry out a detailed review of Internal Audit every three years no longer exists and it is some time since our previous review. Therefore, it is difficult to provide a fair assessment in the more detailed areas included within this checklist.

Skills and experience

	Strong	Adequate	Needs improvement
What is your evaluation of the senior members of the internal audit		✓	

EVALUATION OF INTERNAL AUDIT – EXTERNAL AUDITOR

team's understanding of the organisation, its business and its risk environment			
What is your assessment of the internal audit team's experience in key functional specialisations, in the context of what is needed for the proper discharge of their roles and responsibilities:		✓ IT Risk management	

Comments

The requirement to carry out a detailed review of Internal Audit every three years no longer exists and it is some time since our previous review.

Our review of Internal Audit is therefore now limited to:

- reviewing Internal Audit plans to identify work we may seek to place reliance on;
- reviewing individual pieces of Internal Audit work to identify any issues that may be relevant to our understanding of the control environment; and
- reviewing individual pieces of Internal Audit work where we are seeking to place reliance for the audit of the financial statements.

It is therefore difficult for us to provide a fair assessment in the more detailed areas included in the checklist above.

	Yes	No
Do you consider the internal audit team have the professional experience, technical skills, inter-personal skills and seniority to effectively carry out the internal audit work required?	✓	
Do you consider internal audit have sufficient resources to satisfy their terms of reference?	✓	
Does the structure of	✓	

EVALUATION OF INTERNAL AUDIT – EXTERNAL AUDITOR

internal audit appear to facilitate a proper understanding of the organisation's business issues?		
Does internal audit's staffing appear to adequately reflect its roles and responsibilities?	✓	
In your assessment, is the internal audit strategy and methodology robust and does it reflect the latest thinking in internal audit	Not known without detailed review of methodology	
Comments		
see comments above		

Work Programme

	Yes	No
Are there regular discussions between internal and external audit on internal and external audit strategies, assessment of risks and the implications of audit findings and audit work?	✓	
Is progress against plan monitored jointly by internal and external audit regularly throughout the year?	✓	
Do you receive copies of all relevant internal audit reports issued by internal audit?	✓	
Are copies of internal audit reports received on a timely basis?	✓	not always on Galileo on a timely basis but sent as soon as requested after reported to audit

EVALUATION OF INTERNAL AUDIT – EXTERNAL AUDITOR

		committee
Are internal audit reports of a standard comparable to best practice in other organisations?	✓	
To the best of your knowledge, are there any major areas of risk or concern that internal audit did not cover in the last financial year?		✓

Overall Comments

The standard of Internal Audit reports has improved in recent years, including progress reports, which are now much clearer.

EVALUATION OF INTERNAL AUDIT – SELF ASSESSMENT

Understanding

	Strong	Adequate	Needs improvement
Evaluate internal audit's understanding of:			
<ul style="list-style-type: none"> The responsibilities and operation of the audit committee 	√		
<ul style="list-style-type: none"> The organisations business 		√	
<ul style="list-style-type: none"> The organisation's risk environment 			√
<ul style="list-style-type: none"> The organisation's control framework 			√
Comments			
<p>Due to the extent of change impacting on the County Council, largely as a result of external factors, its objectives and in particular its risk and control environment is constantly changing. Consequently, internal audits understanding of the Council's risk environment and control framework will always include an element that needs improving.</p> <p>Whilst there is an embedded approach to assess, monitor and report upon high level corporate strategic risks, operational or inherent risk management is not so visible.</p> <p>The audit strategy and risk based approach adopted to develop Control Risk Assessments (CRA) in consultation with management, as part of the planning and preparation of each planned assurance review, is designed to improve internal audits understanding of the business, key risks and key controls as they are at the time of each audit review. This approach ensures that audit resources are focused upon providing assurance on high risk areas where there is little or no other assurance and helps embed operational risk management</p> <p>The audit strategy to review all key service activities over a five year rolling programme will enable, in the longer term, internal audit to have a better understanding of the Council's overall risk and control environment and the work of other assurance providers. It is intended to use knowledge gained on the risk, control and assurance framework over this period to develop assurance maps of key risk areas which will help provide clarity over the Council's assurance framework and improve internal audit's risk based strategic planning.</p>			

EVALUATION OF INTERNAL AUDIT – SELF ASSESSMENT

Charter and Structure

	Yes	No
Do the terms of reference for internal audit define in sufficient detail, for the purposes of directing internal audit:		
<ul style="list-style-type: none"> Roles and responsibilities, including those in relation to other internal functions; 	√	
<ul style="list-style-type: none"> Expectations of management: 	√	
<ul style="list-style-type: none"> Scope of internal audit work 	√	
<ul style="list-style-type: none"> Access to information? 	√	

Skills and experience

	Strong	Adequate	Needs improvement
How well does internal audit's staffing reflect its roles and responsibilities?		√	
Assess the staff mix and competencies of the internal audit team.			√
Evaluate internal audit's independence from the activities it audits.	√		

EVALUATION OF INTERNAL AUDIT – SELF ASSESSMENT

Comments

The establishment and qualifications of the in house team are as follows:

Post	Number of FTE
Head of Internal Audit	1
Audit Managers	2
Principal Auditors	6 (Includes Counter Fraud Officer)
Senior Auditor	9.1
Auditor	4
Audit Assistant	0.4
Total	22.5

Qualifications	Number
CCAB	7
Part CCAB	4
Accounting Technician	7
IIA Qualification in Computer Auditing	1
CIPFA Certificate in investigative practice	1

At present there are a number of vacancies at senior auditor level:

- One post is temporarily vacant due to the secondment (promotion) of a member of staff to strategic finance to assist with final accounts closure. This temporary vacancy is being covered through the acting up by one of the Auditor post holders.
- One post is temporarily vacant due to a 2 year secondment (promotion) of a member of staff to strategic finance wef 16/4/2012.
- One post is a permanent vacancy due to the promotion of a member staff to ACE last year. Audit days lost through this post are currently being addressed temporarily through a part time officer in a job share post working full time and the use of agency staff/internal audit partnership.
- 0.8 FTE post is a permanent vacancy due to the recent resignation of a part time member of staff.

It is intended to address these vacancies in the current year by:

- The permanent filling of 1 post
- The temporary filling of 1 post on a 2 year secondment basis
- The continuation of the 1 part time member of staff working full time

The increasing volume of fraud and irregularity work has diverted resources set aside for counter fraud work and highlighted the need to increase and develop investigatory skills. Therefore to enhance the current dedicated counter fraud resource, it is proposed that the 2 year secondment be targeted to the appointment of a qualified fraud investigation officer.

In addition, it has been recognised, from slippage in the internal audit plan during 2011/12, that the service is under resourced in the specialist area of IT Audit, with reliance now being placed on one member of staff to provide IT audit to all our existing customers. At present, the service does not have the skills or capacity to undertake forensic investigations. This work is currently undertaken by the IT service. To strengthen the IT audit capacity and to

EVALUATION OF INTERNAL AUDIT – SELF ASSESSMENT

allow forensic investigations to be undertaken independently, an additional post of Computer Auditor is to be created at Principal Auditor level.

In acknowledgement that the Institute of Internal Auditors is now recognised as the most relevant professional body for the training and development of audit staff, 3 audit staff are to undertake distance learning training for the IIA's Diploma qualification. Modules studied for this qualification include:

- The Internal Audit Environment
- Financial Risks and Controls
- Internal Audit Practice
- Information Systems Auditing
- Corporate Governance and Risk Management

This investment in training will help embed and enhance the risk based approach to auditing recently introduced and will widen information systems auditing skills to non Computer Audit specialists.

In recognition that the in house team may not have all the necessary skills and experience to provide reliable assurance in the specialist area of the pension fund, an internal audit partner was appointed to develop and deliver pension fund audit in 2011/12. This partnership allowed the call off of additional audit resources during the year to address slippage as a result of unforeseen vacancies, skills transfers and the sharing of best audit practice . The partnership agreement has been extended for a further 12 months.

Communications

	Strong	Adequate	Needs improvement
Evaluate internal audit's responsiveness to requests from the audit committee,	√		
Evaluate internal audit's frankness and candour with the committee.	√		
Evaluate internal audit's handling of difficult or contentious issues.		√	
Evaluate internal audit's process to monitor the status of open matters/recommendations		√	

EVALUATION OF INTERNAL AUDIT – SELF ASSESSMENT

	Yes	No
Over the last 12 months, has the chairman of the audit committee been fully briefed on significant findings or developments prior to audit committee meetings?	√	

Performance

	Strong	Adequate	Needs improvement
How would you assess internal audit's overall performance?		√	

In what way has internal audit added value to the organisation?

Through its independent assurance work, Internal audit has continued to add value to the organisation by helping service managers to assess risks and evaluate the effectiveness of controls in place to manage them. The implementation of audit recommendations to address control weaknesses has improved risk management.

The implementation of the CRA methodology has provided the added value of on-going Control Risk Self-Assessment (CRSA) which will help embed effective risk management. In helping to embed effective risk management the service has improved the effectiveness of the Council's corporate governance arrangements.

It is particularly pleasing to note that since the introduction of the CRA methodology the percentage of customers scoring the audit service good or above (4 out of 5) has increased from 87% to 96%.

Through its advice and consultancy work, Internal Audit has worked pro-actively with management to develop adequate controls during the implementation of new systems, projects and initiatives and has championed good governance.

Through its pro-active counter fraud work and reactive support to managers in the investigation of fraud and irregularity, the service continues to add value by helping to manage the strategic risk of financial and reputational loss through fraud and corruption.

In this way, the service has continued to support management in the achievement of the Council's objectives.

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Audit Committee

28 June 2012



Agreement of Accounting Policies for Application in the 2011/12 Financial Statements

Don McLure, Corporate Director Resources

Purpose of the Report

1. The purpose of this report is to update the Audit Committee on the County Council's accounting policies to be applied in the preparation of the 2011/12 Statement of Accounts and to seek confirmation from the Audit Committee that appropriate policies are being applied.
2. Appendix 2 provides a summary of all changes to be applied in preparing the 2011/12 Statement of Accounts.
3. Objective 2 of the Audit Committee's Terms of Reference requires it to provide *'Independent assurance over the financial reporting of the Council's Statement of Accounts ensuring that any issues arising from the process of drawing up, auditing and certifying the Council's annual accounts are dealt with properly.to maintain an understanding of accounting policies and internal and external reporting requirements'*.

Background

4. It is a requirement of the Local Government Act 2003 and the Accounts and Audit Regulations 2003 for the Statement of Accounts to be produced in accordance with proper accounting practices.
5. This report concentrates on the main accounting changes introduced in the Code of Practice on Local Authority Accounting (the Code) in 2011/12.
6. The full list of accounting policies the Council proposes to disclose in its Statement of Accounts notes are detailed in Appendix 2.

New Accounting Policies

7. New accounting policies are required and have been prepared to cover the following two areas in accordance with Code guidance and subsequent LAAP Bulletins:

- **Heritage Assets:** The Code introduces a new accounting policy in relation to the treatment of heritage assets which will impact on the treatment of those heritage assets managed and held by the Council. The new standard will require that a new class of asset, heritage assets, is disclosed separately in the Council's balance sheet in the 2011/12 financial statements together with comparative data for 2010/11. Heritage assets are assets that are held and managed by the Council 'principally for their contribution to knowledge or culture'. The Code requires that heritage assets are measured at valuation in the 2011/12 financial statements (including the 2010/11 comparative information). In addition to recognising the assets on the balance sheet a significant number of narrative disclosure notes are required, e.g. the nature and extent of the collections held by the Council.
- **Carbon Reduction Commitment Allowances:** LAAP Bulletin 91 introduces a new accounting policy in relation to the obligation to purchase and surrender Carbon Reduction Commitment (CRC) Allowances in relation to carbon dioxide emissions. Following the end of 2011/12, participating authorities will submit the annual report on their emissions for the 2011/12 financial year. The retrospective purchase of allowances is anticipated to take place from 1 June 2012. Participating authorities are then required to surrender allowances to the scheme by the last working day in July 2012 in proportion to their reported emissions for the preceding scheme year and in accordance with the scheme requirements.

Amended Accounting Policies

8. The wording of existing accounting policies in several areas has been improved to more accurately reflect the County Council's approach and improve compliance with Code disclosure requirements:
 - **Government Grants and Contributions:** This policy has been amended to more accurately reflect the County Council's approach and remains in line with Code requirements.
 - **Interests in Companies and Other Entities:** This policy has been amended to reflect the County Council's decision not to produce group accounts on the grounds of materiality in 2011/12.
 - **Private Finance Initiative (PFI) and Similar Contracts:** This policy has been amended to provide more information on the County Council's PFI schemes in line with Code guidance.

Deleted Accounting Policies

9. The following accounting policy in relation to Area Based Grant has been deleted as it is no longer relevant following changes in the way grant is allocated to councils:

- *“Area Based Grant (ABG) is a general grant allocated by central government directly to local authorities as additional revenue funding. ABG is non-ringfenced and is credited to Taxation and Non-Specific Grant Income in the Comprehensive Income and Expenditure Statement.”*

Other issues

10. Whilst not a change in accounting policy, the 2011/12 Code has also introduced a new requirement to disclose the number and cost of exit packages agreed. This disclosure will form part of the officers’ remuneration note. The requirement is to disclose exit packages agreed in rising bands of £20,000 up to £100,000 and bands of £50,000 thereafter. The packages included in the bands are those agreed by the Council, i.e. those packages for which the Council is demonstrably committed. The costs include all relevant redundancy costs, pension contributions in respect of added years and other departure costs if applicable.

Recommendations and reasons

11. The Committee is recommended to:
 - review the accounting policies; and
 - approve their use in the preparation of the 2011/12 financial statements.

Appendix 1: Implications

Finance -

The report considers the Accounting Policies for the County Council's Statement of Accounts for 2011/12.

Staffing -

None

Risk -

None

Equality and Diversity / Public Sector Equality Duty -

None

Accommodation -

None

Crime and Disorder -

None

Human Rights -

None

Consultation -

None

Procurement -

None

Disability Issues -

None

Legal Implications -

None

Accounting Policy	New policy	Amended policy	No change	In line with Code
1. General Principles			✓	✓
2. Accruals of Income & Expenditure			✓	✓
3. Cash and Cash Equivalents			✓	✓
4. Exceptional Items			✓	✓
5. Prior Period Adjustments, Changes in Accounting Policies and Estimates and Errors			✓	✓
6. Charges to Revenue for Non-Current Assets			✓	✓
7. Employee Benefits			✓	✓
8. Events After the Reporting Period			✓	✓
9. Financial Instruments			✓	✓
10. Foreign Currency Translation			✓	✓
11. Government Grants and Contributions		✓ ¹		✓
12. Heritage Assets (NEW)	✓			✓
13. Intangible Assets			✓	
14. Interests in Companies and Other Entities		✓ ²		✓
15. Inventories & Long Term Contracts			✓	✓
16. Investment Property			✓	✓

¹ Amended to improve the clarity of the accounting policy, in line with the Code.

² Amended to reflect the decision not produce group accounts on the grounds of materiality

Accounting Policy	New policy	Amended policy	No change	In line with Code
17. Jointly Controlled Operations and Jointly Controlled Assets			✓	✓
18. Leases			✓	✓
19. Overheads & Support Services			✓	✓
20. Property, Plant and Equipment			✓	✓
21. Disposals and Non-current Assets Held for Sale			✓	✓
22. Private Finance Initiative (PFI) and Similar Contracts		✓ ³		✓
23. Provisions			✓	✓
24. Landfill Allowance Schemes			✓	✓
25. Contingent Liabilities			✓	✓
26. Contingent Assets			✓	✓
27. Reserves			✓	✓
28. Revenue Expenditure Funded from Capital under Statute			✓	✓
29. Value Added Tax (VAT)			✓	✓
30. Carbon Reduction Commitment Allowances (NEW)	✓			✓

³ Amended to provide further information on the County Council's PFI schemes in line with Code guidance.

Accounting Policies

1. General Principles

The Statement of Accounts summarises the County Council's transactions for the 2011/12 financial year and its position at the year-end of 31 March 2012. The County Council is required to prepare an annual Statement of Accounts by the Accounts and Audit Regulations 2011, which those Regulations require to be prepared in accordance with proper accounting practices.

Those practices primarily comprise the Code of Practice on Local Authority Accounting in the United Kingdom 2011/12 (the Code) and the Service Reporting Code of Practice 2011/12 (SeRCOP), supported by International Financial Reporting Standards (IFRS).

The accounting convention adopted in the Statement of Accounts is principally historical cost, modified by the revaluation of certain categories of non-current assets and financial instruments.

The Code requires that a Local Authority's Statement of Accounts is prepared on a 'going concern' basis, that is, the accounts are based on the assumption that the County Council will continue in operational existence for the foreseeable future.

2. Accruals of Income and Expenditure

Activity is accounted for in the year that it takes place, not simply when cash payments are made or received. In particular:

- Revenue from the sale of goods is recognised when the County Council transfers the significant risks and rewards of ownership to the purchaser and it is probable that economic benefits or service potential associated with the transaction will flow to the County Council.
- Revenue from the provision of services is recognised when the County Council can measure reliably the percentage of completion of the transaction and it is probable that economic benefits or service potential associated with the transaction will flow to the County Council.
- Supplies are recorded as expenditure when they are consumed - where there is a gap between the date supplies are received and their consumption, they are carried as inventories on the Balance Sheet.
- Expenses in relation to services received (including services provided by employees) are recorded as expenditure when the services are received rather than when payments are made.
- Interest receivable on investments and payable on borrowings is accounted for respectively as income and expenditure on the basis of the effective interest rate for the relevant financial instrument rather than the cash flows fixed or determined by the contract.
- Where revenue and expenditure have been recognised but cash has not been received or paid, a debtor or creditor for the relevant amount is recorded in the Balance Sheet. Where debts may not be settled, the balance of debtors is written down and a charge made to revenue for the income that might not be collected. The County Council has a policy of

not accruing for manual sundry creditor or sundry debtor provisions for less than £1,000 other than in exceptional circumstances.

3. Cash and Cash Equivalents

Cash is represented by cash in hand and deposits with financial institutions repayable without penalty on notice of not more than 24 hours. Cash equivalents are investments that mature in no more than three months or less from the date of acquisition and that are readily convertible to known amounts of cash with insignificant risk of change in value. In the Cash Flow Statement, cash and cash equivalents are shown net of bank overdrafts that are repayable on demand and form an integral part of the County Council's cash management.

4. Exceptional Items

When items of income and expense are material, their nature and amount is disclosed separately, either on the face of the Comprehensive Income and Expenditure Statement or in the notes to the accounts, depending on how significant the items are to an understanding of the County Council's financial performance.

5. Prior Period Adjustments, Changes in Accounting Policies and Estimates and Errors

Prior period adjustments may arise as a result of a change in accounting policies or to correct a material error. Changes in accounting estimates are accounted for prospectively, i.e. in the current and future years affected by the change and do not give rise to a prior period adjustment.

Changes in accounting policies are only made when required by proper accounting practices or the change provides more reliable or relevant information about the effect of transactions, other events and conditions on the County Council's financial position or financial performance. Where a change is made, it is applied retrospectively (unless stated otherwise) by adjusting opening balances and comparative amounts for the prior period as if the new policy had always been applied.

Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period.

6. Charges to Revenue for Non-Current Assets

Services, support services and trading accounts are debited with the following amounts to record the cost of holding fixed assets during the year:

- Depreciation attributable to the assets used by the relevant service.
- Revaluation and impairment losses on assets used by the service where there are no accumulated gains in the Revaluation Reserve against which the losses can be written off.
- Amortisation of intangible fixed assets attributable to the service.

The County Council is not required to raise Council Tax to fund depreciation, revaluation and impairment losses or amortisations. However, it is required to make an annual contribution from revenue towards the reduction in its overall

borrowing requirement equal to an amount calculated on a prudent basis determined by the council in accordance with statutory guidance.

Depreciation, revaluation and impairment losses and amortisations are therefore replaced by the contribution in the General Fund Balance (Minimum Revenue Provision), by way of an adjusting transaction with the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

7. Employee Benefits

Benefits Payable During Employment

Short-term employee benefits are those due to be settled within 12 months of the year-end.

They include such benefits as wages and salaries, paid annual leave and paid sick leave, bonuses and nonmonetary benefits (e.g. cars) for current employees and are recognised as an expense for services in the year in which employees render service to the County Council. An accrual is made for the cost of holiday entitlements (or any form of leave, e.g. time off in lieu) earned by employees but not taken before the year end which employees can carry forward into the next financial year. The accrual is made at the wage and salary rates applicable in the following accounting year, being the period in which the employee takes the benefit. The accrual is charged to Surplus or Deficit on the Provision of Services, but then reversed out through the Movement in Reserves Statement so that holiday benefits are charged to revenue in the financial year in which the holiday absence occurs.

Termination Benefits

Termination benefits are amounts payable as a result of a decision by the County Council to terminate an officer's employment before the normal retirement date or an officer's decision to accept voluntary redundancy and are charged on an accruals basis to the Non Distributed Costs line in the Comprehensive Income and Expenditure Statement when the County Council is demonstrably committed to the termination of the employment of an officer or group of officers or making an offer to encourage voluntary redundancy. Where termination benefits involve the enhancement of pensions, statutory provisions require the General Fund balance to be charged with the amount payable by the County Council to the pension fund or pensioner in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, appropriations are required to and from the Pensions Reserve to remove the notional debits and credits for pension enhancement termination benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year end.

Post Employment Benefits

Employees of the County Council are members of two separate pension schemes:

- The Local Government Pensions Scheme, administered by Durham County Council.

- The Teachers' Pension Scheme, administered by Capita Teachers' Pensions on behalf of the Department for Education (DfE).

Both schemes provided defined benefits to members (retirement lump sums and pensions), earned as employees worked for the County Council.

However, the arrangements for the teachers' scheme mean that liabilities for these benefits cannot ordinarily be identified specifically to the County Council. The scheme is therefore accounted for as if it were a defined contribution scheme and no liability for future payments of benefits is recognised in the Balance Sheet. The Children's and Education Services line in the Comprehensive Income and Expenditure Statement is charged with the employer's contributions payable to Teachers' Pensions in the year.

The Local Government Pension Scheme

The Local Government Scheme is accounted for as a defined benefits scheme:

- The liabilities of the Durham County Council pension fund attributable to the County Council are included in the Balance Sheet on an actuarial basis using the projected unit method – i.e. an assessment of the future payments that will be made in relation to retirement benefits earned to date by employees, based on assumptions about mortality rates, employee turnover rates, etc, and projections of projected earnings for current employees.
- Liabilities are discounted to their value at current prices, using a discount rate of 5.50% (based on the indicative rate of return on high quality corporate bond Aon Hewitt UK Corporate AA Curve – Swaps Extrapolation).
- The assets of Durham County Council pension fund attributable to the County Council are included in the Balance Sheet at their fair value:
 1. quoted securities – current bid price.
 2. unquoted securities – professional estimate.
 3. unitised securities – current bid price.
 4. property – market value.

The change in the net pensions liability is analysed into seven components:

1. Current service cost – the increase in liabilities as a result of years of service earned this year – allocated in the Comprehensive Income and Expenditure Statement to the services for which the employees worked.
2. Past service cost – the increase in liabilities arising from current year decisions whose effect relates to years of service earned in earlier years – debited to the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement as part of Non Distributed Costs.
3. Interest cost – the expected increase in the present value of liabilities during the year as they move one year closer to being paid – debited to

the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.

4. Expected return on assets – the annual investment return on the fund assets attributable to the County Council, based on an average of the expected long-term return – credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.
5. Gains or losses on settlements and curtailments – the result of actions to relieve the County Council of liabilities or events that reduce the expected future service or accrual of benefits of employees – debited or credited to the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement as part of Non Distributed Costs.
6. Actuarial gains and losses – changes in the net pensions liability that arise because events have not coincided with assumptions made at the last actuarial valuation or because the actuaries have updated their assumptions – debited to the Pensions Reserve.
7. Contributions paid to the Durham County Council pension fund – cash paid as employer’s contributions to the pension fund in settlement of liabilities; not accounted for as an expense.

In relation to retirement benefits, statutory provisions require the General Fund balance to be charged with the amount payable by the County Council to the pension fund or directly to pensioners in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, this means that there are appropriations to and from the Pensions Reserve to remove the notional debits and credits for retirement benefits and replace them with debits for the cash paid to the pension fund and pensioners and any such amounts payable but unpaid at the year-end. The negative balance that arises on the Pensions Reserve thereby measures the beneficial impact to the General Fund of being required to account for retirement benefits on the basis of cash flows rather than as benefits are earned by employees.

Discretionary Benefits

The County Council also has restricted powers to make discretionary awards of retirement benefits in the event of early retirements. Any liabilities estimated to arise as a result of an award to any member of staff (including teachers) are accrued in the year of the decision to make the award and accounted for using the same policies as are applied to the Local Government Pension Scheme.

8. Events After the Reporting Period

Events after the Balance Sheet date are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- Those that provide evidence of conditions that existed at the end of the reporting period - the Statement of Accounts is adjusted to reflect such events.

- Those that are indicative of conditions that arose after the reporting period - the Statement of Accounts is not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect.

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

9. Financial Instruments

Financial Liabilities

Financial liabilities are recognised on the Balance Sheet when the County Council becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value and are carried at their amortised cost. Annual charges to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest payable are based on the carrying amount of the liability, multiplied by the effective rate of interest for the instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments over the life of the instrument to the amount at which it was originally recognised.

For most of the borrowings that the County Council has, this means that the amount presented in the Balance Sheet is the outstanding principal repayable (plus accrued interest); and interest charged to the Comprehensive Income and Expenditure Statement is the amount payable for the year according to the loan agreement.

Gains and losses on the repurchase or early settlement of borrowing are credited and debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement in the year of repurchase/settlement. However, where repurchase has taken place as part of a restructuring of the loan portfolio that involves the modification or exchange of existing instruments, the premium or discount is respectively deducted from or added to the amortised cost of the new or modified loan and the write-down to the Comprehensive Income and Expenditure Statement is spread over the life of the loan by an adjustment to the effective interest rate.

Where premiums and discounts have been charged to the Comprehensive Income and Expenditure Statement, regulations allow the impact on the General Fund Balance to be spread over future years. The County Council has a policy of spreading the gain or loss over the term that was remaining on the loan against which the premium was payable or discount receivable when it was repaid. The reconciliation of amounts charged to the Comprehensive Income and Expenditure Statement to the net charge required against the General Fund Balance is managed by a transfer to or from the Financial Instruments Adjustment Account in the Movement in Reserves Statement.

Financial Assets

Financial assets are classified into two types:

- Loans and receivables – assets that have fixed or determinable payments but are not quoted in an active market.

- Available-for-sale assets – assets that have a quoted market price and/or do not have fixed or determinable payments.

Loans and Receivables

Loans and receivables are recognised on the Balance Sheet when the County Council becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value. They are subsequently measured at their amortised cost. Annual credits to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest receivable are based on the carrying amount of the asset multiplied by the effective rate of interest for the instrument. For most of the loans that the County Council has made, this means that the amount presented in the Balance Sheet is the outstanding principal receivable (plus accrued interest) and interest credited to the Comprehensive Income and Expenditure Statement is the amount receivable for the year in the loan agreement.

However, the County Council has made a number of loans to voluntary organisations at less than market rates (soft loans). When soft loans are made, and amounts are material, a loss is recorded in the Comprehensive Income and Expenditure Statement (debited to the appropriate service) for the present value of the interest that will be foregone over the life of the instrument, resulting in a lower amortised cost than the outstanding principal. Interest is credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement at a marginally higher effective rate of interest than the rate receivable from the voluntary organisations, with the difference serving to increase the amortised cost of the loan in the Balance Sheet. Statutory provisions require that the impact of soft loans on the General Fund Balance is the interest receivable for the financial year – the reconciliation of amounts debited and credited to the Comprehensive Income and Expenditure Statement to the net gain required against the General Fund Balance is managed by a transfer to or from the Financial Instruments Adjustment Account in the Movement in Reserves Statement.

Where assets are identified as impaired because of a likelihood arising from a past event that payments due under the contract will not be made, the asset is written down and a charge made to the relevant service (for receivables specific to that service) or the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. The impairment loss is measured as the difference between the carrying amount and the present value of the revised future cash flows discounted at the asset's original effective interest rate.

Any gains and losses that arise on the derecognition of an asset are credited or debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.

Available-for-Sale Assets

Available-for-sale assets are recognised on the Balance Sheet when the County Council becomes a party to the contractual provisions of a financial instrument and are initially measured and carried at fair value. Where the

asset has fixed or determinable payments, annual credits to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest receivable are based on the amortised cost of the asset multiplied by the effective rate of interest for the instrument. Where there are no fixed or determinable payments, income (e.g. dividends) is credited to the Comprehensive Income and Expenditure Statement when it becomes receivable by the County Council.

Assets are maintained in the Balance Sheet at fair value. Values are based on the following principles:

- Instruments with quoted market prices – the market price.
- Other instruments with fixed and determinable payments – discounted cash flow analysis.
- Equity shares with no quoted market prices – independent appraisal of company valuations.

Changes in fair value are balanced by an entry in the Available-for-Sale Reserve and the gain/loss is recognised in the Surplus or Deficit on Revaluation of Available-for-Sale Financial Assets. The exception is where impairment losses have been incurred – these are debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement, along with any net gain or loss for the asset accumulated in the Available-for-Sale Reserve.

Where assets are identified as impaired because of a likelihood arising from a past event that payments due under the contract will not be made (fixed or determinable payments) or fair value falls below cost, the asset is written down and a charge made to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. If the asset has fixed or determinable payments, the impairment loss is measured as the difference between the carrying amount and the present value of the revised future cash flows discounted at the asset's original effective interest rate. Otherwise, the impairment loss is measured as any shortfall of fair value against the acquisition cost of the instrument (net of any principal repayment and amortisation).

Any gains and losses that arise on the derecognition of the asset are credited or debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement, along with any accumulated gains or losses previously recognised in the Available-for-Sale Reserve.

Where fair value cannot be measured reliably, the instrument is carried at cost (less any impairment losses).

10. Foreign Currency Translation

Where the County Council has entered into a transaction denominated in a foreign currency, the transaction is converted into sterling at the exchange rate applicable on the date the transaction was effective. Where amounts in foreign currency are outstanding at the year-end, they are reconverted at the spot exchange rate at 31 March. Resulting gains or losses are recognised in

the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.

11. Government Grants and Contributions

Whether paid on account, by instalments or in arrears, government grants and third party contributions and donations are recognised as due to the County Council when there is reasonable assurance that:

- the County Council will comply with the conditions attached to the payments, and
- the grants or contributions will be received.

Amounts recognised as due to the County Council are not credited to the Comprehensive Income and Expenditure Statement until conditions attached to the grant or contribution have been satisfied. Conditions are stipulations that specify that the future economic benefits or service potential embodied in the asset acquired using the grant or contribution are required to be consumed by the recipient as specified, or future economic benefits or service potential must be returned to the transferor.

Monies advanced as grants and contributions for which conditions have not been satisfied are carried in the Balance Sheet as creditors. When conditions are satisfied, the grant or contribution is credited to the relevant service line (attributable revenue grants and contributions) or Taxation and Non-Specific Grant Income (non-ringfenced revenue grants and all capital grants) in the Comprehensive Income and Expenditure Statement.

Where capital grants are credited to the Comprehensive Income and Expenditure Statement, they are reversed out of the General Fund Balance in the Movement in Reserves Statement. Where the grant has yet to be used to finance capital expenditure, it is posted to the Capital Grants Unapplied reserve. Where it has been applied, it is posted to the Capital Adjustment Account. Amounts in the Capital Grants Unapplied reserve are transferred to the Capital Adjustment Account once they have been applied to fund capital expenditure.

12. Heritage Assets

Tangible and Intangible Heritage Assets

A tangible heritage asset is defined as a tangible asset with historical, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture.

An intangible heritage asset is defined as an intangible asset with cultural, environmental, or historical significance. Examples of intangible heritage assets include recordings of significant historical events.

Recognition and measurement

A key feature of heritage assets is that they have cultural, environmental or historical associations that make their preservation for future generations important. Heritage assets are maintained principally for their contribution to knowledge and culture. Where an asset meets the definition of a heritage asset but is used for operational purposes, it is not classified as a heritage

asset. For example, a historic building used as a museum is classified within land and buildings, as this is its primary purpose, but the exhibits within it may be classified as heritage.

Heritage assets are recognised and measured (including the treatment of revaluation gains and losses) in accordance with the County Council's accounting policies on property, plant and equipment. However, some of the measurement rules are relaxed in relation to heritage assets and the County Council's approach is as follows:

- Heritage assets valuations are based on insurance values, where available, as this is the most appropriate and relevant basis. In some cases, these values are supported by professional valuations, for example by auction houses.
- Insurance values are reviewed regularly and assets will be revalued where a change is deemed to be significant.
- In the absence of insurance values, for example where an asset is either not insured or is self-insured, the asset's most recent valuation before reclassification is used. This is usually historic cost but some buildings and monuments were measured on an existing use value (EUV) basis prior to reclassification.
- Where no appropriate valuation is available, heritage assets are not disclosed on the balance sheet, however they are disclosed in the narrative notes to the financial statements.

Items are recognised on the balance sheet where they are held by the County Council on long-term loan or where the County Council has the risks and rewards of ownership, as evidenced by the need to insure them. Similarly, items that the County Council has lent out long-term are not recognised. Items held on short-term loan, for example for temporary exhibitions, are not recognised.

The County Council is custodian or guardian of a number of monuments or sites. These are recognised as heritage assets; however they do not usually have any appropriate valuation so they are not recognised on the balance sheet.

The County Council's collections of heritage assets are accounted for as follows:

Museum Collections and Artefacts

This includes museum exhibits and items such as books of remembrance and miners banners. They are reported in the balance sheet at insurance value.

Artwork, including Public Art and Sculptures

This includes paintings, sculptures and outdoor public art installations around the county. Some items in this collection are reported at insurance value, others at cost and there are a number for which no value is available so they are not reported on the balance sheet.

The distinction between sculptures, monuments and statues can be subjective, however for the purposes of classification the County Council has

determined that sculptures are generally modern, commissioned pieces of art, monuments can be modern or historic and are usually dedicated to people or events and statues are usually historical structures. Monuments and statues are included under the heading “Monuments, Statues and Historic Buildings” below.

Monuments, Statues and Historic Buildings

This includes war and colliery memorials, statues and non-operational historic buildings around the county. Some items in this collection are reported at insurance value, some at existing use value and some at cost. There are a number for which no value is available and are not reported on the balance sheet.

Civic Regalia and Silverware

This includes civic chains, badges of office and silverware used for civic purposes, and are recorded at insurance value.

Geophysical / Archaeological

This includes pit wheel sites and roman archaeological sites. No appropriate or relevant valuations are available for these assets so they are not recognised on the balance sheet.

Depreciation

Depreciation is not charged on heritage assets which have indefinite lives.

Impairment

The carrying amounts of heritage assets are reviewed where there is evidence of impairment for heritage assets, e.g. where an item has suffered physical deterioration or breakage or where doubts arise as to its authenticity. Any impairment is recognised and measured in accordance with the County Council’s general policies on impairment.

Disposal

Heritage assets are rarely disposed of. However, in such cases, disposal proceeds are accounted for in accordance with the County Council’s general provisions relating to the disposal of property, plant and equipment. Proceeds are disclosed separately in the notes to the financial statements and are accounted for in accordance with statutory accounting requirements relating to capital expenditure and capital receipts.

13. Intangible Assets

Expenditure on non-monetary assets that do not have physical substance but are controlled by the County Council as a result of past events (e.g. software licences) is capitalised when it is expected that future economic benefits or service potential will flow from the intangible asset to the County Council.

Internally generated assets are capitalised where it is demonstrable that the project is technically feasible and is intended to be completed (with adequate resources being available) and the County Council will be able to generate future economic benefits or deliver service potential by being able to sell or

use the asset. Expenditure is capitalised where it can be measured reliably as attributable to the asset and is restricted to that incurred during the development phase (research expenditure cannot be capitalised). Expenditure on the development of websites is not capitalised if the website is solely or primarily intended to promote or advertise the County Council's goods or services.

Intangible assets are measured initially at cost. Amounts are only revalued where the fair value of the assets held by the County Council can be determined by reference to an active market. In practice, no intangible asset held by the County Council meets this criterion, and they are therefore carried at amortised cost. The depreciable amount of an intangible asset is amortised over its useful life to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. An asset is tested for impairment whenever there is an indication that the asset might be impaired – any losses recognised are posted to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. Any gain or loss arising on the disposal or abandonment of an intangible asset is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement.

Where expenditure on intangible assets qualifies as capital expenditure for statutory purposes, amortisation, impairment losses and disposal gains and losses are not permitted to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and the Capital Receipts Reserve.

14. Interests in Companies and Other Entities

The Code requires local authorities to produce group accounts to reflect significant activities provided to Council taxpayers by other organisations in which an authority has an interest. The County Council has reviewed its interests in companies and other entities that have the nature of subsidiaries, associates and jointly controlled entities against the criteria for group accounts as set out in the Code and has concluded that there are no such material interests that require the preparation of group accounts. In the County Council's own single-entity accounts, the interests in companies and other entities are recorded as financial assets at cost, less any provision for losses.

15. Inventories and Long Term Contracts

Inventories are included in the Balance Sheet at the lower of cost and net realisable value. The cost of inventories is assigned using the weighted average costing formula.

Long term contracts are accounted for on the basis of charging the Surplus or Deficit on the Provision of Services with the value of works and services received under the contract during the financial year.

16. Investment Property

Investment properties are those that are used solely to earn rentals and/or for capital appreciation. The definition is not met if the property is used in any way to facilitate the delivery of services or production of goods or is held for sale.

Investment properties are measured initially at cost and subsequently at fair value, based on the amount at which the asset could be exchanged between knowledgeable parties at arm's-length. Properties are not depreciated but are revalued annually according to market conditions at the year-end.

Gains and losses on revaluation are posted to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. The same treatment is applied to gains and losses on disposal.

Rentals received in relation to investment properties are credited to the Financing and Investment Income line and result in a gain for the General Fund Balance. However, revaluation and disposal gains and losses are not permitted by statutory arrangements to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and the Capital Receipts Reserve.

17. Jointly Controlled Operations and Jointly Controlled Assets

Jointly controlled operations are activities undertaken by the County Council in conjunction with other venturers that involve the use of the assets and resources of the venturers rather than the establishment of a separate entity. The County Council recognises on its Balance Sheet the assets that it controls and the liabilities that it incurs and debits and credits the Comprehensive Income and Expenditure Statement with the expenditure it incurs and the share of income it earns from the activity of the operation.

Jointly controlled assets are items of property, plant or equipment that are jointly controlled by the County Council and other venturers, with the assets being used to obtain benefits for the venturers. The joint venture does not involve the establishment of a separate entity. The County Council accounts for only its share of the jointly controlled assets, the liabilities and expenses that it incurs on its own behalf or jointly with others in respect of its interest in the joint venture and income that it earns from the venture.

18. Leases

Leases are classified as finance leases where the terms of the lease transfer substantially all the risks and rewards incidental to ownership of the property, plant or equipment from the lessor to the lessee. All other leases are classified as operating leases.

Where a lease covers both land and buildings, the land and buildings elements are considered separately for classification.

Arrangements that do not have the legal status of a lease but convey a right to use an asset in return for payment are accounted for under this policy where fulfilment of the arrangement is dependent on the use of specific assets.

The County Council as Lessee

Finance Leases

Property, plant and equipment held under finance leases is recognised on the Balance Sheet at the commencement of the lease at its fair value measured at the lease's inception (or the present value of the minimum lease payments, if lower). The asset recognised is matched by a liability for the obligation to

pay the lessor. Initial direct costs of the County Council are added to the carrying amount of the asset. Premiums paid on entry into a lease are applied to writing down the lease liability. Contingent rents are charged as expenses in the periods in which they are incurred.

Lease payments are apportioned between:

- a charge for the acquisition of the interest in the property, plant or equipment - applied to write down the lease liability, and
- a finance charge (debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement).

Property, Plant and Equipment recognised under finance leases is accounted for using the policies applied generally to such assets, subject to depreciation being charged over the lease term if this is shorter than the asset's estimated useful life (where ownership of the asset does not transfer to the County Council at the end of the lease period).

The County Council is not required to raise Council Tax to cover depreciation or revaluation and impairment losses arising on leased assets. Instead, a prudent annual contribution is made from revenue funds towards the deemed capital investment in accordance with statutory requirements. Depreciation and revaluation and impairment losses are therefore substituted by a revenue contribution in the General Fund Balance, by way of an adjusting transaction with the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

Operating Leases

Rentals paid under operating leases are charged to the Comprehensive Income and Expenditure Statement as an expense of the services benefitting from use of the leased property, plant or equipment. Charges are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a rent-free period at the commencement of the lease).

The County Council as Lessor

Finance Leases

Where the County Council grants a finance lease over a property or an item of plant or equipment, the relevant asset is written out of the Balance Sheet as a disposal. At the commencement of the lease, the carrying amount of the asset in the Balance Sheet (whether Property, Plant and Equipment or Assets Held for Sale) is written off to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement as part of the gain or loss on disposal. A gain, representing the County Council's net investment in the lease, is credited to the same line in the Comprehensive Income and Expenditure Statement also as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal), matched by a lease (long-term debtor) asset in the Balance Sheet.

Lease rentals receivable are apportioned between:

- a charge for the acquisition of the interest in the property - applied to write down the lease debtor (together with any premiums received), and
- finance income (credited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement).

The gain credited to the Comprehensive Income and Expenditure Statement on disposal is not permitted by statute to increase the General Fund Balance and is required to be treated as a capital receipt. Where a premium has been received, this is posted out of the General Fund Balance to the Capital Receipts Reserve in the Movement in Reserves Statement. Where the amount due in relation to the lease asset is to be settled by the payment of rentals in future financial years, this is posted out of the General Fund Balance to the Deferred Capital Receipts Reserve in the Movement in Reserves Statement. When the future rentals are received, the element for the capital receipt for the disposal of the asset is used to write down the lease debtor. At this point, the deferred capital receipts are transferred to the Capital Receipts Reserve.

The written-off value of disposals is not a charge against Council Tax, as the cost of non-current assets is fully provided for under separate arrangements for capital financing. Amounts are therefore appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

Operating Leases

Where the County Council grants an operating lease over a property or an item of plant or equipment, the asset is retained in the Balance Sheet. Rental income is credited to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Credits are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a premium paid at the commencement of the lease). Initial direct costs incurred in negotiating and arranging the lease are added to the carrying amount of the relevant asset and charged as an expense over the lease term on the same basis as rental income.

19. Overheads and Support Services

The costs of overheads and support services are charged to those that benefit from the supply or service in accordance with the costing principles of the CIPFA Service Reporting Code of Practice 2011/12 (SeRCOP). The total absorption costing principle is used - the full cost of overheads and support services are shared between users in proportion to the benefits received, with the exception of:

- Corporate and Democratic Core - costs relating to the Council's status as a multifunctional, democratic organisation.
- Non Distributed Costs - the cost of discretionary benefits awarded to employees retiring early and impairment losses chargeable on Assets Held for Sale.

These two cost categories are defined in SeRCOP and accounted for as separate headings in the Comprehensive Income and Expenditure Statement, as part of Net Expenditure on Continuing Services.

20. Property, Plant and Equipment

Assets that have physical substance and are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and that are expected to be used during more than one financial year are classified as Property, Plant and Equipment.

Recognition

Expenditure on the acquisition, creation or enhancement of Property, Plant and Equipment is capitalised on an accruals basis, provided that it is probable that the future economic benefits or service potential associated with the item will flow to the County Council and the cost of the item can be measured reliably. Expenditure that maintains but does not add to an asset's potential to deliver future economic benefits or service potential (i.e. repairs and maintenance) is charged as an expense when it is incurred.

Measurement

Assets are initially measured at cost, comprising:

- the purchase price;
- any costs attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management;
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

The County Council does not capitalise borrowing costs incurred whilst assets are under construction.

The cost of assets acquired other than by purchase is deemed to be its fair value, unless the acquisition does not have commercial substance (i.e. it will not lead to a variation in the cash flows of the County Council). In the latter case, where an asset is acquired via an exchange, the cost of the acquisition is the carrying amount of the asset given up by the County Council.

Donated assets are measured initially at fair value. The difference between fair value and any consideration paid is credited to the Taxation and Non-Specific Grant Income line of the Comprehensive Income and Expenditure Statement, unless the donation has been made conditionally. Until conditions are satisfied, the gain is held in the Donated Assets Account. Where gains are credited to the Comprehensive Income and Expenditure Statement, they are reversed out of the General Fund Balance to the Capital Adjustment Account in the Movement in Reserves Statement.

Assets are then carried in the Balance Sheet using the following measurement bases:

- Infrastructure, community assets and assets under construction – depreciated historical cost.

- Dwellings – fair value, determined using the basis of existing use value for social housing (EUV-SH); and
- All other assets – fair value, determined as the amount that would be paid for the asset in its existing use (existing use value – EUV).

Where there is no market-based evidence of fair value because of the specialist nature of an asset, depreciated replacement cost (DRC) is used as an estimate of fair value.

Where non-property assets that have short useful lives or low values (or both), depreciated historical cost basis is used as a proxy for fair value.

Assets included in the Balance Sheet at fair value are revalued sufficiently regularly to ensure that their carrying amount is not materially different from their fair value at the year-end, but as a minimum every five years. Increases in valuations are matched by credits to the Revaluation Reserve to recognise unrealised gains. Exceptionally, gains might be credited to the Comprehensive Income and Expenditure Statement where they arise from the reversal of a loss previously charged to a service.

Where decreases in value are identified, they are accounted for by:

- Where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains).
- Where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

The Revaluation Reserve contains revaluation gains recognised since 1 April 2007 only, the date of its formal implementation. Gains arising before that date have been consolidated into the Capital Adjustment Account.

Impairment

Assets are assessed at each year-end as to whether there is any indication that an asset may be impaired. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall.

Where impairment losses are identified, they are accounted for by:

- Where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains).
- Where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

Where an impairment loss is reversed subsequently, the reversal is credited to the relevant service line(s) in the Comprehensive Income and Expenditure

Statement, up to the amount of the original loss, adjusted for depreciation that would have been charged if the loss had not been recognised.

Depreciation

Depreciation is provided for on all Property, Plant and Equipment assets by the systematic allocation of their depreciable amounts over their useful lives. An exception is made for assets without a determinable finite useful life (i.e. freehold land and certain Community Assets) and assets that are not yet available for use (i.e. assets under construction).

Depreciation is calculated on the following bases:

- Dwellings and other buildings – straight-line allocation over the useful life of the property as estimated by the valuer up to a maximum of 50 years.
- Vehicles, plant, furniture and equipment – a percentage of the value of each class of assets in the Balance Sheet, as advised by a suitably qualified officer.
- Infrastructure – straight-line allocation over 40 years.

Where an item of Property, Plant and Equipment has a value greater than £5m and major components greater than 20% of the value of the asset, the components are depreciated separately at rates representative of their useful life.

Revaluation gains are also depreciated, with an amount equal to the difference between current value depreciation charged on assets and the depreciation that would have been chargeable based on their historical cost being transferred each year from the Revaluation Reserve to the Capital Adjustment Account.

21. Disposals and Non-current Assets Held for Sale

When it becomes probable that the carrying amount of an asset will be recovered principally through a sale transaction rather than through its continuing use, it is reclassified as an Asset Held for Sale. The asset is revalued immediately before reclassification and then carried at the lower of this amount and fair value less costs to sell. Where there is a subsequent decrease to fair value less costs to sell, the loss is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Gains in fair value are recognised only up to the amount of any losses previously recognised in the Surplus or Deficit on Provision of Services. Depreciation is not charged on Assets Held for Sale.

If assets no longer meet the criteria to be classified as Assets Held for Sale, they are reclassified back to non-current assets and valued at the lower of their carrying amount before they were classified as held for sale; adjusted for depreciation, amortisation or revaluations that would have been recognised had they not been classified as Held for Sale, and their recoverable amount at the date of the decision not to sell.

Assets that are to be abandoned or scrapped are not reclassified as Assets Held for Sale.

When an asset is disposed of or decommissioned, the carrying amount of the asset in the Balance Sheet (whether Property, Plant and Equipment or Assets Held for Sale) is written off to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement as part of the gain or loss on disposal. Receipts from disposals (if any) are credited to the same line in the Comprehensive Income and Expenditure Statement also as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal). Any revaluation gains accumulated for the asset in the Revaluation Reserve are transferred to the Capital Adjustment Account.

Amounts received for a disposal are categorised as capital receipts. A proportion of receipts relating to housing disposals (75% for dwellings, 50% for land and other assets, net of statutory deductions and allowances) is payable to the Government. The balance of receipts is required to be credited to the Capital Receipts Reserve, and can then only be used for new capital investment or set aside to reduce the County Council's underlying need to borrow (the capital financing requirement). Receipts are appropriated to the Reserve from the General Fund Balance in the Movement in Reserves Statement.

The written-off value of disposals is not a charge against Council Tax, as the cost of non-current assets is fully provided for under separate arrangements for capital financing. Amounts are appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

22. Private Finance Initiative (PFI) and Similar Contracts

PFI and similar contracts are agreements to receive services, where the responsibility for making available the property, plant and equipment needed to provide the services passes to the PFI contractor. As the County Council is deemed to control the services that are provided under its PFI schemes, and as ownership of the property, plant and equipment will pass to the Council at the end of the contracts for no additional charge, the County Council carries the assets used under the contracts on its Balance Sheet as part of Property, Plant and Equipment.

The original recognition of these assets at fair value (based on the cost to purchase the property, plant and equipment) was balanced by the recognition of a liability for amounts due to the scheme operator to pay for the capital investment.

For the BSF Schools PFI Project, the liability was written down by an initial capital contribution of £0.270m.

Non-current assets recognised on the Balance Sheet are revalued and depreciated in the same way as property, plant and equipment owned by the County Council. The amounts payable to the PFI operators each year are analysed into five elements:

- Fair value of the services received during the year – debited to the relevant service in the Comprehensive Income and Expenditure Statement.

- Finance cost – an interest charge of 10.15% on the outstanding Balance Sheet liability, debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.
- Contingent rent – increases in the amount to be paid for the property arising during the contract, debited to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.
- Payment towards liability – applied to write down the Balance Sheet liability towards the PFI operator (the profile of write-downs is calculated using the same principles as for a finance lease).
- Lifecycle replacement costs – proportion of the amounts payable is posted to the Balance Sheet as a prepayment and then recognised as additions to Property, Plant and Equipment when the relevant works are eventually carried out.

23. Provisions

Provisions are made where an event has taken place that gives the County Council a legal or constructive obligation that probably requires settlement by a transfer of economic benefits or service potential and a reliable estimate can be made of the amount of the obligation. For example, the County Council may be involved in a court case that could eventually result in the making of a settlement or the payment of compensation.

Provisions are charged as an expense to the appropriate service line in the Comprehensive Income and Expenditure Statement in the year that the County Council becomes aware of the obligation, and are measured at the best estimate at the balance sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.

When payments are eventually made, they are charged to the provision carried in the Balance Sheet. Estimated settlements are reviewed at the end of each financial year - where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service.

Where some or all of the payment required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received if the County Council settles the obligation.

24. Landfill Allowance Schemes

Landfill allowances, whether allocated by DEFRA or purchased from another Waste Disposal Authority (WDA) are recognised as current assets and are initially measured at fair value. Landfill allowances allocated by DEFRA are accounted for as a government grant.

After initial recognition, allowances are measured at the lower of cost and net realisable value.

As landfill is used, a liability and an expense are recognised. The liability is discharged either by surrendering allowances or by payment of a cash penalty

to DEFRA (or by a combination). The liability is measured at the best estimate of the expenditure required to meet the obligation, normally the market price of the number of allowances required to meet the liability at the reporting date. However, where some of the obligation will be met by paying a cash penalty to DEFRA, that part of its liability is measured at the cost of the penalty.

25. Contingent Liabilities

A contingent liability arises where an event has taken place that gives the County Council a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the County Council. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required or the amount of the obligation cannot be measured reliably.

Contingent liabilities are not recognised in the Balance Sheet but disclosed in a note to the accounts.

26. Contingent Assets

A contingent asset arises where an event has taken place that gives the County Council a possible asset whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the County Council.

Contingent assets are not recognised in the Balance Sheet but disclosed in a note to the accounts where it is probable that there will be an inflow of economic benefits or service potential.

27. Reserves

The County Council sets aside specific amounts as reserves for future policy purposes or to cover contingencies. Reserves are created by appropriating amounts out of the General Fund Balance in the Movement in Reserves Statement. When expenditure to be financed from a reserve is incurred, it is charged to the appropriate service in that year to score against the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement. The reserve is then appropriated back into the General Fund Balance in the Movement in Reserves Statement so that there is no net charge against council tax for the expenditure.

Certain reserves are kept to manage the accounting processes for non-current assets, financial instruments, retirement and employee benefits and do not represent usable resources for the County Council - these reserves are explained in the relevant policies.

28. Revenue Expenditure Funded from Capital under Statute

Expenditure incurred during the year that may be capitalised under statutory provisions but that does not result in the creation of a non-current asset has been charged as expenditure to the relevant service in the Comprehensive Income and Expenditure Statement in the year. Where the County Council has determined to meet the cost of this expenditure from existing capital resources or by borrowing, a transfer in the Movement in Reserves Statement

from the General Fund Balance to the Capital Adjustment Account then reverses out the amounts charged so that there is no impact on the level of Council Tax.

29. Value Added Tax (VAT)

VAT payable is included as an expense only to the extent that it is not recoverable from HM Revenue and Customs. VAT receivable is excluded from income.

30. Carbon Reduction Commitment Allowances

The County Council is required to participate in the Carbon Reduction Commitment (CRC) Energy Efficiency Scheme. This scheme is currently in its introductory phase which will last until 31 March 2014. The County Council is required to purchase and surrender allowances, currently retrospectively, on the basis of emissions i.e. carbon dioxide produced as energy is used. As carbon dioxide is emitted (i.e. as energy is used), a liability and an expense are recognised. The liability will be discharged by surrendering allowances. The liability is measured at the best estimate of the expenditure required to meet the obligation, normally at the current market price of the number of allowances required to meet the liability at the reporting date. The cost to the County Council is recognised and reported in the costs of the County Council's services and is apportioned to services on the basis of energy consumption.

Audit Committee

28 June 2012



**Consideration of 'Going Concern Status'
for the Statement of Accounts for the year
ended 31 March 2012**

Don McLure, Corporate Director Resources

Purpose of the Report

1. The Audit Commission has asked that Durham County Council assess whether it should be considered a 'going concern', and whether the accounts should be prepared on that basis. This report considers the County Council's status as a going concern.

Background

2. The general principles adopted in compiling the Statement of Accounts are in accordance with the 'Code of Practice on Local Authority Accounting 2011/12' (the Code) as published by the Chartered Institute of Public Finance and Accountancy (CIPFA). The Code defines proper accounting practices for local authorities in England, Wales, Scotland and Northern Ireland.
3. The Code requires that a local authority's Statement of Accounts is prepared on a going concern basis; that is, the accounts should be prepared on the assumption that the authority will continue in operational existence for the foreseeable future. This means that the Comprehensive Income and Expenditure Statement and Balance Sheet assume no intention to curtail significantly the scale of the operation.
4. An inability to apply the going concern concept can have a fundamental impact on the financial statements

Key Issues

5. The assumption that a local authority's services will continue to operate for the foreseeable future is made because local authorities carry out functions essential to the local community and are themselves revenue-raising bodies (with limits on their revenue-raising powers arising only at the discretion of central government). If an authority were in financial difficulty, the prospects are therefore that alternative arrangements might be made by central government either for the

continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year.

6. Local Authorities derive their powers from statute and their financing and accounting framework is closely monitored by primary and secondary legislation. It is a fundamental concept of local authority accounting that wherever accounting principles and legislative requirements are in conflict the legislative requirements apply.
7. An organisation must consider its financial performance to assess its ability to continue as a going concern. This assessment should cover historical, current and future performance.

Historical Position

8. Durham County Council became a Unitary Authority on 1 April 2009, bringing together the seven former District Councils in County Durham with the County Council.
9. The assets and liabilities of the former District Councils were transferred to the County Council on 1 April 2009. At that date, the Net Assets of the County Council was £1,240.742m, reducing to £900.094m at 31 March 2010. At 31 March 2011 there was a further decrease to £856.994m.
10. Net assets as at 31 March 2012 are £571.791m.

Current Position

11. The County Council holds general reserves of £21.874m at 31 March 2012 and reserves earmarked for specific future purposes of £100.425m.
12. The Net Assets of the County Council at 31 March 2012 amount to £571.791m, a decrease of £285.203m.

Future Plans

13. The County Council approved its budget for 2012/13 and Medium Term Financial Plan to 2015/16 in February 2012.

Medium Term Financial Plan – 2012/13 to 2015/16

14. The following assumptions have been utilised in developing the MTFP model for 2012/13 – 2015/16:
 - (i) Government Grant reductions for the MTFP period have been developed utilising information from both the 2012/13 Finance Settlement, the CSR and the Autumn Statement. The forecast reductions in Government Grant are shown in the following table:

Forecast Government Grant Reductions

Year	Grant Reduction £m
2012/13	17.177
2013/14	4.930
2014/15	14.840
2015/16	11.560

- (ii) Forecast Pay and Price Inflation levels have taken into account the 1% pay increase cap for 2013/14 and 2014/15 as detailed below:

Pay and Price Inflation Assumption

Year	Pay Inflation	Price Inflation
2012/13	0.0%	2.0%
2013/14	1.0%	2.0%
2014/15	1.0%	1.5%
2015/16	1.5%	1.5%

- (iii) Continuing budget pressures in relation to Landfill Tax, Carbon Tax, Employer Pension Contributions, Concessionary Fares, energy price inflation and Adults Social Care demographic pressures.
- (iv) All staffing budgets currently have a 3% turnover allowance deducted. In the coming years, staff turnover is expected to reduce with a 2.5% turnover rate felt to be more prudent which the report is recommending be built into the MTFP from 2013/14.
- (v) Continuing need to support both the current and additional capital programmes, whilst accounting for variations in estimated investment income.
- (vi) Council Tax increases for 2013/14 to 2015/16 are assumed to be 2.5% per annum.
- (vii) There is a need for additional savings to be identified in 2013/14, 2014/15 and 2015/16 totalling £23.3m to achieve a balanced budget across the whole MTFP.

15. The Local Government Finance Bill, if enacted will introduce two key policies which will have a significant impact upon the MTFP from 2013/14 as detailed below:
- (ii) **Localisation of Business Rates** – the Government’s Local Government Resource Review (LGRR) recommends that councils should be able to retain all business rate income generated locally. This would provide a constant income stream and could incentivise councils to grow their local economies on the basis that they will be able to retain the additional business rates generated from any new businesses and growth in existing businesses. The business rate income would replace Formula Grant received from Government. To ensure no Council is favoured or penalised, a system of ‘top ups’ and ‘tariffs’ will be introduced as a starting point. Beyond this time however, a significant proportion of the Council’s ongoing income, will in effect depend upon the health and vitality of the local economy. This will be a significant risk for the Council as there is little, if any link, between the local economy and the demand for major services such as for example; care provision for the elderly and safeguarding services for children. The MTFP model makes no assumptions at this stage of the likely financial impact of this policy.
 - (iii) **Localisation of Council Tax Benefit Support** – the Government intends to implement this policy also from 1 April 2013. Before implementation, the Government intends to top slice 10% of council tax benefit funding, which equates to circa £5.6m for County Durham. The Council will become responsible for developing a policy to distribute council tax benefit although the Government will stipulate that key vulnerable groups, such as pensioners, must be protected. This is likely to result in people of working age facing a disproportionate impact. The MTFP model assumes the funding reduction from withheld council tax benefit funding will be fully passported via a revised Council Tax Benefit Scheme. The Council will also be financially responsible for any increased costs due to residents claiming additional benefit, especially during a period of recession.
16. A balanced MTFP model has been developed after taking into account the assumptions detailed above. The MTFP model is summarised in the following table:

MTFP Summary Position

	2012/13	2013/14	2014/15	2015/16	TOTAL
	£m	£m	£m	£m	£m
Reduction in Resource Base	5.440	5.030	12.873	7.315	30.658
Budget Pressures	21.180	15.876	11.584	13.467	62.107
Savings Required	26.620	20.906	24.457	20.782	92.765

2012/13 Proposals

17. The Council continues to face unprecedented levels of reductions in Government grants over the current Comprehensive Spending Review (CSR) period to 31 March 2015.
18. In total, the County Council is forecasting that Government Support for the five year period 2011/12 to 2015/16 will reduce by £108.7m and by £115.8m when including the forecast grant reduction for 2016/17. This equates to a 30% reduction in Government Support over this period.
19. After also taking into account estimated base budget pressures and growth in some priority service areas, the County Council is forecasting the need to deliver £159.2m of cash savings for the five year period 2011/12 to 2015/16 and savings of £171.8m when including forecasts for 2016/17. This equates to a 40% net revenue budget reduction over this period.
20. Despite having to make the above unprecedented level of savings, the County Council agreed a net revenue budget of £432.58m for 2012/13. Although the budget requires the delivery of £26.6m in 2012/13 in order to deliver a balanced budget, it is also able to protect and increase some service budgets for the benefit of council tax payers.
21. The 2012/13 budget also absorbs several significant cost pressures including:
 - Landfill tax of £1.07m due to the Government increasing the costs of landfill by £8 per tonne from April 2012;
 - Additional employer pension contributions of £1.2m due to a 5.3% increase on the sum required to recover the forecast deficit for County Council employees on the Pension Fund;
 - Concessionary fares - due to the increasing numbers of pensioners qualifying for bus passes, the increasing patronage on bus services

and the withdrawal of Government Grants to bus companies, the concessionary fares budget is forecasted to increase by £0.85m;

- Excessive inflation experienced during 2011/12 on energy and fuel costs has required £1.35m and £1.0m to be added to base budgets in 2012/13.

22. After taking into account base budget pressures and savings, the Council's 2012/13 Net Budget Requirement is £432.58m. How the Budget is financed is detailed below:

Financing of 2012/13 Budget

Financing Method	Amount
	£m
NNDR	219.007
Revenue Support Grant	4.245
Council Tax	201.788
Council Tax Freeze Grant	4.989
New Homes Bonus	2.551
TOTAL	432.580

Capital Funding

23. The Council continues to strive to attract grant funding from external sources and was recently successful in receiving a grant of £6.9m for improving Superfast Broadband access in remote areas across the County.
24. Funding of £3.8m has also been confirmed from the Housing and Communities Agency to improve four Gypsy and Travellers' sites across the County. These much needed improvements will start in 2012/13.
25. Government support for Capital investment in schools has significantly reduced below expectation for 2012/13 with a £3.6m reduction from the 2011/12 levels.
26. After taking into account external grants, forecasted income from capital receipts and unsupported prudential borrowing, there will be enough funding for the Council to be able to make new investments of £60.2m in 2012/13 and £43.3m in 2013/14 in addition to the current earmarked schemes in the Capital Programme. This would result in the Council having a Capital Programme of £359.4m across the 2012/13 to 2015/16 three year MTFP period as shown in the following table.

Service Grouping	2012/13	2013/14	2014/15	2015/16	Total
	£m	£m	£m	£m	£m
ACE	3.703	2.619	-	-	6.322
AWH	2.059	1.862	4.584	-	8.505
CYPS	96.580	42.055	0.533	-	139.168
Neighbourhoods	29.867	15.949	1.054	-	46.870
RED	43.079	17.038	0.250	-	60.367
Resources	22.148	5.650	0.491	-	28.289
Other	-	9.924	30.000	30.000	69.924
Total	197.436	95.097	36.912	30.000	359.445
Financed by					
Grants & Contributions	85.490	44.172	-	-	129.662
Revenue and Reserves	5.426	1.607	0.807	-	7.840
Capital Receipts	18.634	10.000	10.000	10.000	48.634
Capital Receipts – BSF/Schools	2.974	8.000	3.000	-	13.974
Borrowing	84.912	31.318	23.105	20.000	159.335
Total	197.436	95.097	36.912	30.000	359.445

27. The County Council has been able to set a balanced budget for 2012/13 and has a plan in place to continue to deliver local services up to 2016. Based on this, it is clear that the County Council is a going concern.

Financial Reserves

28. The County Council holds reserves as
- A working balance to help cushion the impact of uneven cashflow and avoid unnecessary temporary borrowing – this forms part of the general reserve
 - A contingency to cushion the impact of unexpected events or emergencies – this also forms part of General Reserves.
 - A means of building up funds, earmarked reserves, to meet known or predicted liabilities.
29. Bearing in mind the current levels of general reserves and the risks facing the Council, the Council has adopted the following policy for reserves, in summary,
- To set aside sufficient sums in earmarked reserves as it considers prudent to do so.
 - Aim to maintain, broadly, general reserves of between 3% and 4% of the budget requirement which equates to £13m to £17m.

30. Earmarked Reserves will be established to provide resources for specific purposes. Protocols will be established for each new reserve and the Corporate Director Resources will review the appropriateness of reserves on an annual basis.
31. Each Earmarked Reserve, with the exception of the schools reserve, is reviewed on an annual basis. The Schools' reserve is the responsibility of individual schools with balances at the year end which make up the total reserve.
32. The actual General Reserve balance of £21.874m as at 31 March 2012 is higher than the County Council's current General Reserve policy of maintaining the reserve between 3% - 4% (£13m - £17m) of net Revenue Expenditure. The policy will be reviewed as part of the 2013/14 budget setting process due to the potential significant risks associated with the upcoming introduction of new arrangements for Business Rates and Council Tax Benefit from 1 April 2013.
33. Based on the level of reserves held, the County Council has demonstrated robust financial management that underpins its status as a going concern.

Risk

34. A number of risks will need to be managed and mitigated during the MTFP process. These risks will be assessed continually throughout the MTFP four year period. Some of the key risks already identified include:
 - (i) Ensure the achievement of a balanced budget and financial position across the MTFP period.
 - (ii) Ensure all savings are risk assessed across a range of factors e.g. impact upon customers, stakeholders, partners and staff.
 - (iii) The Finance Settlements for 2013/14 and 2014/15 are estimated based upon the original CSR 2010. The Government has confirmed that the next Finance Settlement will be for the two year period 2013/14 to 2014/15 but will not be announced until December 2012. This leaves Councils little time to plan effectively, especially if the settlement should be significantly worse than forecast.
 - (iv) The localisation of the Business Rates from April 2013 will result in the Council being subject to a wide range of risks relating to the state of the local economy over which the Council will have very little control. The MTFP Model assumes the outcome for the County Council will be cost neutral after receiving a 'top-up' payment.

- (v) Pay Award – the current 2012/13 budget model assumes there will be no pay award.
 - (vi) Localisation of Council Tax Support from April 2013 – the Government is to top slice the Council Tax Benefit Transfer by 10% which equates to circa £5.6m. The Model assumes this impact will be passported fully via a revised Council Tax Benefit Scheme.
 - (vii) The MTFP model builds in assumptions in relation to Concessionary Fares. There are still inherent risks however in relation to bus services due to inflationary pressures linked to fuel, further pressures due to withdrawn Government grants, and increases in demand.
 - (viii) AWH relies heavily on the independent sector to provide adequate volumes of appropriate services for service users. Market pressures and increases in minimum wage levels will mean that the rates the Council pays will require careful consideration in the later years of the MTFP period.
35. Based on the above there are no risks which would indicate that the County Council is not a going concern.

Conclusion

36. When approving the accounts, the Audit Committee members being those charged with governance for the County Council will need to consider which of the following three basic scenarios is the most appropriate:
- the body is clearly a going concern and it is appropriate for the accounts to be prepared on the going concern basis;
 - the body is a going concern but there are uncertainties regarding future issues which should be disclosed in the accounts to ensure the true and fair view;
 - the body is not a going concern and the accounts will need to be prepared on an appropriate alternative basis.
37. Based on the assessment undertaken, in my view:
- the County Council has a history of stable finance and ready access to financial resources in the future,
 - there are no significant financial, operating or other risks that would jeopardise the County Council's continuing operation.
38. Therefore the County Council is clearly a going concern and it is appropriate for the Statement of Accounts to be prepared on that basis.

Recommendaton

39. It is recommended that the County Council should be considered as a going concern and that the Statement of Accounts should be prepared on that basis.

Contact: Hilary Appleton Tel: (0191) 383 3544

Appendix 1: Implications

Finance -

The report considers the County Council as a 'going concern'.

Staffing -

None

Risk -

None

Equality and Diversity / Public Sector Equality Duty -

None

Accommodation -

None

Crime and Disorder -

None

Human Rights -

None

Consultation -

None

Procurement -

None

Disability Issues -

None

Legal Implications -

None

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Audit Committee

28 June 2012

**Draft Annual Governance Statement for
the year April 2011 – March 2012**



Report of Don McLure, Corporate Director, Resources

Purpose of the Report

1. This report seeks approval of the draft Annual Governance Statement (AGS), attached in Appendix 2, and the list of significant governance improvements attached in Appendix 3.

Background

2. The Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively. The Council also has a duty under the Local Government Act 1999 to make arrangements to secure continuous improvement in the way which functions are exercised, having regard to a combination of economy, efficiency and effectiveness.
3. The Council has approved and adopted a code of corporate governance which is consistent with the principles of the CIPFA/SOLACE Framework – 'Delivering Good Governance in Local Government'. The AGS explains how the Council complies with this code and also meets the requirements of Regulation 4 (3) of the Accounts and Audit (England) Regulations 2011 in relation to the publication of a Statement on Internal Control.

Presentation of the AGS

4. In order to prepare the AGS each year, the Council has a responsibility for conducting, at least annually, a review of the effectiveness of its governance framework, including the system of internal control.
5. In preparing the AGS, those charged with governance must seek adequate assurance that its corporate governance arrangements are effective and identify any significant areas of improvement. The Corporate Director, Resources co-ordinates and oversees the Council's corporate assurance arrangements, and prepares the AGS to demonstrate how far the Council complies with the principles of good governance and recommending improvements, to be published in the Council's Annual Statement of Accounts. Progress is monitored and corrective action taken where needed each quarter against the action plan of governance improvements.

6. In gathering the evidence to prepare the AGS, the following approach has been adopted:

6.1 Consideration of corporate sources of assurance

- Progress made on improvements identified as part of the previous years AGS;
- The identification of key documents, processes and procedures that support the governance framework, many of which may have been revised during the year. This information has been gathered from across the Council, and is recorded in detail;
- The work of those officers who have specific responsibility for the development and maintenance of the governance framework. Key officers confirmed any changes in the governance arrangements since the last review;
- External Audit Annual Report;
- The work of Internal Audit, including the annual opinion on the adequacy of internal control by the Manager of Internal Audit & Risk as set out in the Annual Internal Audit report;
- Current strategic risk registers;
- The review of the effectiveness of the system of Internal Audit;
- Partnership governance arrangements;
- Other work undertaken by the External Auditor, the Audit Commission and other review agencies.

6.2 Service assurance on the effectiveness of the governance framework

Corporate Directors and the Assistant Chief Executive completed an assurance statement, which noted any changes implemented during the 2011/ 12 year, and to identify any improvements required/ planned.

Recommendations and reasons

7. Audit Committee to:

- approve the draft AGS for 2011/ 12 attached in Appendix 2;
- approve the list of significant governance improvements in Appendix 3;
- confirm that this report can proceed for information to full Council.

Contact: David Marshall Tel: 0191 3834311

Appendix 1: Implications

Finance - Financial planning and management is a key component of effective corporate governance.

Staffing - Ensuring the adequate capability of staff meets a core principle of the Chartered Institute of Public Finance and Accountancy (CIPFA)/Society of Local Authority Chief Executives (SOLACE) guidance.

Risk – Delivery of the corporate governance action plan will strengthen the decision making and strategic and operational management of the Council’s business.

Equality and Diversity/ Public Sector Equality Duty - Engaging local communities including hard to reach groups meets a core principle of the CIPFA/ SOLACE guidance.

Accommodation – None directly, although asset management is a key component of effective corporate governance.

Crime and Disorder – None.

Human Rights - None.

Consultation - Engaging local communities meets a core principle of the CIPFA/ SOLACE guidance.

Procurement – None.

Disability issues – Ensuring access to services meets a core principle of the CIPFA/ SOLACE guidance.

Legal Implications – Ensuring compliance with relevant laws and regulations, and ensuring that expenditure is lawful, is a key component of effective corporate governance.

1. SCOPE OF RESPONSIBILITY

Durham County Council (the Council) is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

The Council also has a duty under the Local Government Act 1999 to make arrangements to secure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness.

In discharging this overall responsibility, the Council is responsible for putting in place proper arrangements for the governance of its affairs, facilitating the effective exercise of its functions, which includes arrangements for the management of risk.

The Council has approved, adopted and published on its website, a code of corporate governance, which is consistent with the principles of the CIPFA/SOLACE Framework – “Delivering Good Governance in Local Government”. This statement explains how the Council has complied with the code and also meets the requirements of Regulation 4 (3) of the Accounts and Audit (England) Regulations 2011 in relation to the publication of an Annual Governance Statement.

2. THE PURPOSE OF THE GOVERNANCE FRAMEWORK

The governance framework comprises of the systems and processes, and culture and values, by which the Council is directed and controlled and its activities through which it accounts to, engages with and leads the community. It enables the Council to monitor the achievement of its strategic objectives and to consider whether those objectives have led to the delivery of appropriate, cost effective services for the people of County Durham.

The system of internal control is a significant part of that framework and is designed to manage risk to a reasonable level. It cannot eliminate all risk of failure to achieve policies, aims and objectives and can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of the Council's policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The governance framework has been in place at the Council for the year ended 31 March 2012 and up to the date of approval of the statement of accounts.

3. THE GOVERNANCE FRAMEWORK

The key elements of the systems and processes that comprise the Council's governance arrangements are detailed in the Council's local Code of Corporate Governance, which is documented in the Council's [Constitution](#). This sets out the key documents and processes that determine the way the Council is directed and controlled to meet the six core principles of the CIPFA/ SOLACE Framework. The following sections demonstrate assurance that the Council has complied with each of these principles in practice, and also highlights where we have further improved our corporate governance arrangements during 2011/12.

Principle 1: Focusing on the purpose of the authority and on outcomes for the community and creating and implementing a vision for the local area

The [Sustainable Community Strategy 2010-30](#) (SCS) which has been produced by the Council in conjunction with its partners on the County Durham Partnership (CDP), demonstrates its shared long-term vision for the future of County Durham. This vision for County Durham, namely 'Altogether Better Durham' outlines two areas of focus – **Altogether Better Place** and **Altogether Better for People** and five priority themes, which represent the major issues identified by residents:

- Altogether wealthier;
- Altogether better for children and young people;
- Altogether healthier;
- Altogether greener;
- Altogether safer.

The SCS is renewed every three years and this work provides input into the Council Plan and various strategic planning work such as the Joint Strategic Needs Assessment.

The CDP, which is the strategic partnership for the County, is made up of key public, private and voluntary sector partners, and is underpinned by thematic partnerships set around the five priority themes. Operationally, it is supported by the Delivery Implementation Group (DIG), whose role is to monitor performance towards implementing the SCS, and consider strategically how plans align and where efficiencies and value can be maximised through integration, shared services and joint commissioning.

The [Council Plan](#) contains the Council's corporate priorities and the key actions to take in support of delivering the longer term goals in the SCS and the Council's own improvement agenda. The Council Plan is supported by a series of Service Plans at a Service Grouping level which details the planned actions to deliver the Council's vision. Plans developed in partnership are also in place to deliver the goals of the SCS. For example, during the year, the thematic partnership for 'Altogether Better for Children and Young People' revised the Children, Young People's and Families Plan for 2012-2016.

The Council Plan and the [Medium Term Financial Plan 2012 - 16](#) (MTFP2) enable the Council to make best use of resources, and enable the continued provision of value for money (VFM) services that meet the needs of residents, businesses and other stakeholders. To provide assurance on its VFM in 2011/12, the Council used profiles based on the Audit Commission's VFM profiles. Independent assurance of

our VFM was also gained from the Audit Commission, who issued an unqualified VFM conclusion in October 2011. To enable better use of resources, we have further strengthened our governance arrangements by:

- Implementing a single asset register;
- Developing Asset Management plans;
- Reviewing the Capital Prioritisation process through Corporate Management Team and the Member Officer Working Group;
- Unitising both the Finance function and Human Resources function across the Council.

To measure the quality of services, the Council has a locally led performance management framework. In 2011, Cabinet agreed a new approach, the 'Future of performance management, efficiency and improvement in Durham', following abolition of the national local government performance framework. Detailed [reports](#) on the Council's performance have been provided to Cabinet on a quarterly basis, and assurance is also gained through performance clinics between the Chief Executive and individual Directors during the year. Through good governance, the Council continues to improve the quality of services, and this has been confirmed by external independent sources of assurance. For example, during 2011/12, in Children and Young People's Services, the conclusions of a number of independent external assessments were that:

- Ofsted rated County Durham's Children's Services as 'outstanding' following inspection of safeguarding and services for Looked After Children;
- A positive result of the unannounced inspection of contact, referral and assessment was achieved with no areas identified for priority action;
- All Children's Homes are judged good or better;
- The outcome of the last four fostering inspections and the last two adoption service inspections received an 'outstanding' grading;
- Aycliffe Centre for children was rated outstanding;
- Overall 4 star rating for the Adoption Service.

A comprehensive schedule of Savings targets have been programmed which are designed to achieve the necessary savings to enable us to deliver a balanced budget and MTFP. To ensure the effective delivery of its objectives and efficiency savings, the Council has also undertaken a series of Extended Management Team meetings consisting of the Chief Executive, Directors and Heads of Service with a programme of activity linked to the strategic management of the Council. Assurance over the delivery of this programme is gained by detailed and frequent monitoring undertaken by CMT and Cabinet and the target savings of £66m for 2011/12 have been delivered.

Members have robustly scrutinised the performance of the Council, demonstrated by a number of key scrutiny reviews of Council services during 2011-12, which are outlined in the [Overview and Scrutiny Annual Report](#).

The Council considers the governance implications of its actions, and revised its Code of Corporate Governance in March 2012 to ensure that it remains consistent with the principles of the CIPFA/SOLACE Framework – "Delivering Good Governance in Local Government".

Principle 2: Members and officers working together to achieve a common purpose with clearly defined functions and roles

The key document describing the roles and responsibilities of Member and Senior Officer posts and functions is the Council [Constitution](#).

Members and Officers work together on the workload of the Cabinet which is managed through a system of Cabinet pre-agenda meetings. To support this, Corporate Directors have held regular briefing sessions with Cabinet Portfolio Members and their support Members. For example, a number of informal sessions took place throughout the MTFP planning process to ensure CMT and Cabinet have a shared understanding of the complexities in the MTFP process, and all Opposition parties were briefed during the development of the MTFP.

The Council has appointed the Corporate Director, Resources as Chief Financial Officer (CFO) and Section 151 Officer to fulfil the governance requirements of the CIPFA Statement on the Role of the Chief Financial Officer in Local Government (2010). The CFO, who is a member of the Corporate Management Team and reports directly to the Chief Executive, has been involved in all Corporate Management Team discussions, and has reviewed all reports to Cabinet which have financial implications. The CFO has also provided an opinion under section 25 of the Local Government Act 2003 on the reserves for the County Council, which Members considered when setting the budget.

Member remuneration is overseen by an independent panel, and their report was approved by Council on in February 2012.

Principle 3: Promoting values for the authority and demonstrating the values of good governance through upholding high standards of conduct and behaviour

The key elements of the Council's approach to communicating and embedding the expected standards of behaviour for Members and staff are detailed in the Council [Constitution](#). The Council's Codes of Conduct included in the Constitution also apply to its partnership working.

The Standards Committee has the key governance role of promoting and monitoring high standards of conduct by elected members, independent members and co-opted members. The [Standards Committee Annual Report](#) was presented to the Full Council in October 2011, outlining its business which includes details of Member conduct complaints and Local Government Ombudsman investigations.

The ethical framework will be reviewed during 2012/13 to confirm that it meets the requirements of the Localism Bill, due to be enacted on 31 July 2012, and as part of this work, the Council will demonstrate that the ethical agenda is being developed with the public and other stakeholders, rather than being inward-facing. Where appropriate, however, we have still reviewed key governance documents to ensure our values are followed in practice, such as the Council's Policy Framework Procedure Rules which were updated in May 2011. In terms of disclosure of gifts, hospitality and interests, assurance is gained over Member declarations and registrations by the Monitoring Officer maintaining and monitoring the Register of Gifts, Interests and Hospitality for Members, which is available online. Staff declarations are maintained and monitored by their Head of Service.

A climate of openness has been encouraged by the Council Leader who holds regular Cabinet meetings at various locations throughout County Durham. The values of the Council are further promoted in the Single Equality Scheme which includes 'protected characteristics' covered by the Equality Act. Supporting this scheme is an impact assessments process, which ensures that the impact on equality is considered in the Council's decision making. For example, in 2011/12, the MTFP was fully equality impact assessed. Our commitment is further demonstrated by equality impact assessment training, attended by 174 people during the year.

Principle 4: Taking informed and transparent decisions which are subject to effective scrutiny and managing risk

The Council's [Constitution](#) sets out how the Council operates, how decisions are made and the procedures which are followed to ensure that these are effective, transparent and accountable to local people. This includes the Officer Scheme of Delegation, which is reviewed annually in line with the review of the Constitution. A revised Constitution was approved by the full Council in May 2011, having been reviewed by an all-party group, namely the Constitution Working Group. Key changes to the Constitution in 2011/ 12 were:

- Amending the Scheme of Delegation to align it with changes in responsibilities;
- A Civic Protocol and Order of Precedence guidance document for event organisers where civic dignitaries would be invited to attend;
- Inclusion of the revised Code of Practice for Members and Officers in dealing with planning matters;
- Incorporation of the revised Local Code of Corporate Governance, following completion of the Annual Governance Statement for 2010/11;
- Extending the remit of the Corporate Issues Overview and Scrutiny Committee to include the oversight role of RIPA.

Overview and Scrutiny, which consists of an Overview and Scrutiny Management Board and six committees, has the key role to make decision-making processes transparent, accountable and inclusive and to improve services for people by being responsive to their needs. To maintain independent assurance, the Council refreshed co-opted members to the Council's Overview and Scrutiny Committees in March 2012. Where appropriate, Members have scrutinised the decisions of the Council, demonstrated by a number of key scrutiny reviews which are outlined in the [Overview and Scrutiny Annual Report](#)

To maintain the accountability and integrity of the Council's decision-making, a number of further improvements to governance in this area have been implemented in 2011/ 12, notably:

- The Data Protection Policy, which includes a Data Breach procedure;
- The development of Records Retention schedules for all service areas;
- Assurance provided by an independent third party that the Council has complied with the Code of Connection under the Government Connect programme;
- The revised Contract Procedure Rules, which are the Council's rules on how a contract must be let. The involvement of the corporate procurement team on all procurements provides assurance that the Rules are being complied with;
- The Corporate Strategy for Commissioning and Procurement, which includes the supplier engagement strategy reviewed by local enterprise agencies;
- The Civica Fraud Management Software.

The Council has ensured that it complies with legal requirements in its decision making by ensuring that all reports requiring a decision include the legal implications, report authors confirming that they have obtained legal advice on proposals contained in reports, and the source of that legal advice.

The Council operates a risk management approach that supports its decision making processes. This is underpinned by a risk management strategy and policy, which was reviewed in January 2012, and is overseen by the Corporate Risk Management Group, which met four times during the year. Each key decision made by the Council has been supported by a risk assessment, and in addition, each efficiency proposal underpinning the MTFP was risk assessed. Strategic risks were reviewed throughout the year.

The Council has an Audit Committee with responsibility for monitoring and reviewing the risk, control and governance processes and associated assurance processes. The committee met eight times in 2011/ 12.

The key mechanisms provided for the public to raise concerns about potential breaches of conduct are:

- the Confidential Reporting Code (Whistle blowing policy), which is part of the Council's Constitution, and is monitored by the Audit Committee;
- the Council's complaints procedures, which are monitored by the Standards Committee, whose remit includes Member conduct complaints, Local Government Ombudsman investigations and complaints handling by Services. [Reports](#) on complaints have been provided quarterly to the Committee.

The arrangements for counter-fraud of benefits will change during 2012/13 as a result of the central government proposal to bring benefits and tax credit fraud investigations under a Single Fraud Investigation Service, administered by the Department for Works and Pensions.

Principle 5: Developing the capacity and capability of Members and Officers to be effective

The Council is committed to continually meeting the development needs of Members and Officers.

Our approach to Member development is outlined in the Member Learning and Development Strategy, which was reviewed in 2011 to reflect the extension of responsibilities of the Member Development and Support Group, who oversee the implementation of the strategy. Assurance on the effectiveness of our approach to Member development is demonstrated by the Council being awarded the North East Charter on Member Development in May 2011.

To support employees through the major restructuring process associated with the MTFP outcomes, an Employee Support Programme is in place. A number of key governance improvements around officer capability have also been delivered during the year, namely:

- Implementing the Homeworking policy;
- Reviewing the Disciplinary policy in consultation with the Trade Unions;
- Undertaking an interim review of the Officer appraisal process;
- Reviewing the Recruitment and Selection Policy.

Assurance on the effectiveness of our approach to Officer development is demonstrated by the Council maintaining the Investor in People Standard.

Additional independent assurance over the Council's recruitment and selection procedures was provided by the post-registration visit in May 2011 of the UK Border Agency, who reported 'full compliance' for our systems and procedures for monitoring the employment of foreign nationals who require the right to work in the UK, and this is reflected in the CRB Disclosure Policy.

Principle 6: Engaging with local people and other stakeholders to ensure robust public accountability

As the strategic partnership for the County, the CDP is the lead umbrella partnership for most other partnerships in County Durham, and the Leader of the Council is the chair of the CDP. The Council's relationships with partners are managed through the Partnership Governance Framework, which was updated in 2011.

The Council's approach to engaging stakeholders is outlined in the Consultation and Engagement Strategy. This is complemented by the County Durham Partnership Community Engagement and Empowerment framework, which has shaped and supported a common vision and approach for community engagement by partners in County Durham, and the County Durham Compact, which provides a framework for partnership and engagement with the voluntary and community sector. Key examples of, and improvements in, our engagement with stakeholders during the year include:

- Stakeholders being involved in the development of the MTFP, demonstrated by undertaking a detailed consultation process which can be found in the County Council's MTFP and Budget Report. The 2012/13 budget decisions have taken the results of this consultation into account especially in relation to the areas of the budget to protect and those areas where a greater level of saving is expected;
- Extensive consultation with service users and families/parents around planning activity, such as the CYPFP annual review workshops;
- The new Staff Recognition scheme launched in 2011;
- Raising awareness of Members, Officers and key Partners in respect of the Councillor Call for Action process;
- The development of an appeals mechanism to ensure that the Council has a robust mechanism in place for Petitions, and that petitioners have an opportunity to challenge Council inaction regarding a particular petition issue;
- Further improving the Council's website to achieve a SOCITIM 3 star rating, and expanding the use of social media;
- Corporate Directors holding regular briefing sessions with Members, and holding regular staff roadshows to keep staff up to date with priorities and plans for change;
- Commencing a programme of Community Governance reviews.

The Council has a strong commitment to working with partners to meet the needs of its communities. There are 14 Area Action Partnerships (AAP) in place across the County, who are each governed by a board comprising members of the public, partner organisations and elected Councillors. These are multi-agency partnerships who are fully engaged with the community in identifying and resolving local priorities, and utilise locality budgets to drive improvements to service quality. 105 people attended the inaugural Countywide AAP meeting in 2011.

Assurance over the effectiveness of the AAPs was provided by an Overview and Scrutiny report, presented to Cabinet in September 2011, which concluded that AAPs were fit for purpose, as the governance arrangements were shown to be an extremely robust mechanism for ensuring the Council works with local communities and key partners to make sure local services meet local needs. Furthermore, AAPs were also commended in a national award scheme, and a high quality pilot approach

used as part of the participatory budgeting process was highlighted nationally to be one of the best in the country.

4 REVIEW OF EFFECTIVENESS

The Council has responsibility for conducting, at least annually, a review of the effectiveness of its governance framework including the system of internal control. The review of effectiveness is informed by the work of the senior managers within the Council who have responsibility for the development and maintenance of the governance environment, the annual report of the Manager of Internal Audit and Risk, and also by comments made by the external auditors and other review agencies and inspectorates.

The process for maintaining and reviewing the effectiveness of the corporate governance framework involves the key Member and Officer functions outlined below, namely:

- The Executive;
- Chief Financial Officer;
- Monitoring Officer;
- Overview and Scrutiny Committee;
- Standards Committee;
- Audit Committee.

The Council's [Constitution](#) sets out the governance roles and responsibilities of these functions. In addition:

- The Corporate Director, Resources co-ordinates and oversees the Council's corporate assurance arrangements by:
 - Preparing and maintaining the Council's Code of Corporate Governance as a formal framework for the Council's governance arrangements;
 - Reviewing the systems, processes and documentation to determine whether they meet the requirements of this Code, reporting any breaches and recommending improvements;
 - Preparing an Annual Governance Statement to demonstrate how far the Council complies with the principles of good governance and recommending improvements.
- Internal and External Audit provide independent assurance on the effectiveness of the corporate governance framework.

The review was also informed by a statement provided by each Corporate Director and the Assistant Chief Executive commenting on the effectiveness of the Council's governance arrangements generally and how they impacted on their service areas. These included consideration of the effectiveness of internal controls.

Based on internal audit work undertaken during 2011/12, the Manager of Internal Audit and Risk has issued a moderate overall assurance opinion on the adequacy and effectiveness of internal control operating across the Council in 2011/12. This moderate opinion ranking provides assurance that there is basically a sound system of control in place across the Council, but there are some weak areas and some evidence of non-compliance that are being corrected and improvements put in

place. Control objectives are often achieved but improvements need to be made in our strive for excellence.

Significant issues arising from the review of the effectiveness, where improvements are needed, are outlined in section 5 below. These will be included in an action plan and will be regularly reviewed and monitored.

5 SIGNIFICANT GOVERNANCE ISSUES

We have been advised on the implications of the result of the review of the effectiveness of the governance framework by the Audit Committee. The Council is fully committed to the principles of corporate governance, and has made further progress during the past twelve months in developing its arrangements.

Following the production of the Annual Governance Statement (AGS) for 2010/11, an action plan, containing the following recommendations was produced. Progress made in implementing each recommendation, as outlined below, was confirmed by the Corporate Director, Resources and formed the starting point of the work to produce the 2011/12 AGS.

1. Continue the positive direction of travel by implementing the planned control improvements to financial systems.

A number of key actions to address the financial systems weaknesses have been incorporated into the Resources Service Improvement Plan. Operational processes are much more effective. Bank reconciliation work is up to date and the Oracle system is much more reliable such that user confidence in the system is much improved.

2. Pay Harmonisation and Single Status.

A project is in place to develop and implement a pay structure for the Council and resolve outstanding pay harmonisation and single status issues, which have been complex given the implications of TUPE following Local Government Reorganisation. During 2011/12, the target date was revised to December 2012, and we are on target to implement this action by that date.

3. Implement an Information Management and Governance Strategy

A staged approach is being taken to developing the Council's information management and governance arrangements focusing on 3 main areas: records management, data protection, and access to information. A new Data Protection Policy and Data Breach procedures were agreed by Cabinet in May 2011 and awareness raising has taken place with all Heads of Service and Tier 4 managers, and has been rolled out to all staff. Key elements still to be developed are a formal procedure for dealing with access to information requests, including freedom of information and environmental information, and a long term records management strategy for the Council. This is no longer considered a significant area for governance improvement.

4. Implement revised Financial Management Standards.

The Council is developing Financial Management Standards to supplement the very high level roles and responsibilities defined in the financial procedures rules contained in the Constitution. Financial management standards set out in more detail how the procedure rules will be implemented to help embed sound financial management across the Council. Most of the work to implement these standards is complete, but finalisation requires the input of a number of finance staff who are currently focused on producing the annual accounts.

5. Business Continuity.

To develop a robust ICT architecture with as few single points of failure as possible and replication of key systems, a business continuity specification and options for delivery are being developed by the Head of ICT.

6. Changing Government Policy on the Ethical Framework.

Following the abolition of the current Standards regime, the Council will review the ethical framework and implement a new compliant, fit for purpose and workable ethical structure for the Council. Supporting this, advice and guidance will be provided to Members and Officers on the new ethical structure. Progress has been delayed due to the late changes to the Localism Bill, such as clarification on the production of a recommended code from LGA and the regulations on interests. An initial report agreeing the establishment of a new Standards Committee was presented to full Council on the 21st March 2012.

7. Improve accessibility to key policies.

A single searchable database of all current strategies, policies and procedures has been developed as part of the Council's new intranet which was launched in April 2012. To complement traditional briefings and communications on strategies and policies, online e-learning packages have been developed and introduced for key policies such as data protection. This action is now complete.

8. Performance Management of Integrated Teams.

The Children's Trust intends to transform services for children and young people by developing services in local communities, for local communities. To support this, a Performance Management Framework for Integrated teams has been implemented, and this action is now complete.

9. Succession Planning.

Effective succession planning for the future is a long-term goal, but the Redeployment Policy is the key policy in place to match the "at risk" employee skills with the changing demands of the Council during this period of significant change. This action is now complete.

The Corporate Director, Resources also sought assurance on the effectiveness of the Council's governance arrangements from each of the Council's Corporate Directors and the Assistant Chief Executive. As a result of this exercise, and the work of both Internal and External Audit, a number of issues have been identified where improvement in the Council's governance arrangements are required. The most significant issues, agreed by the Corporate Management Team (CMT) at its

meeting on 20 June 2012, and as reported to the Audit Committee on 28 June 2012, together with a summary of action taken or being taken to address each issue, are detailed below. These issues have all been carried forward from the Annual Governance Statement for 2010/ 11, as target dates were revised either due to external pressures, or where, although progress has been made, it was always envisaged that the actions would not be fully completed by March 2012. No new significant issues were identified as a result of our annual effectiveness review.

1. Continue the positive direction of travel by implementing the planned control improvements to financial systems.

The actions to address the financial systems weaknesses will be incorporated into the Resources Service Improvement Plan. Progress on these improvement plans will be monitored by CMT throughout the year.

2. Pay Harmonisation and Single Status.

Work is underway to fully implement the project, and resolve outstanding pay harmonisation and single status issues, with planned implementation from October 2012 subject to the outcome of trade union employee ballots.

3. Implement revised Financial Management Standards

The revised Financial Management Standards should be finalised and implemented as soon as possible on the basis that the original implementation date has been missed.

4. Business Continuity.

Develop a robust ICT architecture with as few potential single points of failure as possible and replication of key systems.

5. Changing Government Policy on the Ethical Framework.

When central government have clarified the late changes to the Localism Bill, we will review the ethical framework and implement a new compliant, fit for purpose and workable ethical structure for the Council, and provide advice and guidance to Members, Officers and other key stakeholders on the new ethical structure.

We propose over the coming year to take steps to further enhance our governance arrangements. We are satisfied that these steps will address the need for improvements that were identified in our review of effectiveness and will monitor their implementation and operation as part of our next annual review.

.....

Signed:

Simon Henig
Leader of Durham County Council

George Garlick
Chief Executive

Don McLure
Corporate Director, Resources

Appendix 3: Governance Action Plan – 2011-12 Annual Governance Statement

The Lead Officer is the officer who will oversee and monitor the implementation of the action. However, for a number of actions, it is the responsibility of the Services, not the Lead Officer, to implement the actions.

No.	Significant governance issue	Further Action Required	Lead Officer	Target Implementation Date
1	A number of significant weaknesses in the system of financial control.	The actions to address the financial systems weaknesses will be incorporated into the Resources Service Improvement Plan. Progress on these improvement plans will be monitored by CMT throughout the year.	Don McLure	Throughout 2012/ 13
2	Pay Harmonisation and Single Status.	Work is underway to fully implement the project, and resolve outstanding pay harmonisation and single status issues	Kim Jobson	December 2012
4	Implement revised Financial Management Standards.	The revised Financial Management Standards should be finalised and implemented.	Jeff Garfoot	December 2012
5	Business Continuity	Develop a robust ICT architecture with as few potential single points of failure as possible and replication of key systems.	Phil Jackman	March 2013
6	Changing Government Policy on the Ethical Framework resulting from the enactment of the Localism Bill on 31 July 2012.	When central government have clarified the late changes to the Localism Bill, we will review the ethical framework and implement a new compliant, fit for purpose and workable ethical structure for the Council, and provide advice and guidance to Members and Officers on the new ethical structure.	Colette Longbottom	October 2012
		Provide appropriate training and guidance for key partners, suppliers, service providers and other stakeholders to build awareness of the Council's ethical ethos and practice.	Colette Longbottom	October 2012

AUDIT COMMITTEE

28th June 2012



**2011/12 Annual Report of the Audit
Committee to County Council**

Councillor Edward Bell, Chair of the Audit Committee

Purpose of the Report

- 1 To present a draft report of the work of the Audit Committee for the period April 2011 to March 2012, for agreement prior to reporting to full Council at its meeting on 25th July 2012

Background

- 2 In accordance with best practice, the Audit Committee has agreed to report a summary of its work to Full Council.

Recommendations and Reasons

- 11 Members agree the draft report as attached for onward reporting to County Council on 25th July 2012

Contact: Avril Wallage, Manager of Internal Audit & Risk Tel 0191 383 3537

Appendix 1: Implications

Finance

None

Staffing

None

Risk

None

Equality and Diversity/Public Sector Equality Duty

None

Accommodation

None

Crime and disorder

None

Human rights

None

Consultation

None

Procurement

None

Disability Issues

None

Legal Implications

None

County Council

25th July 2012

Report of the Audit Committee for the Period April 2011 to March 2012



Councillor Edward Bell, Chair of Audit Committee

Purpose of the Report

1. To inform the Council of the work of the Audit Committee during 2011/12 that shows how this committee has been successful in improving governance across the Council.
2. The Committee has requested that bi-annual reports be made to Full Council and a previous report covering the work of the Audit Committee to 31 October 2011 was presented to the Council on 7th December 2011.
3. This report incorporates details previously reported relating to 2011/12 to provide a full record of work carried out during the year.

Background

4. The Audit Committee of the County Council has been in place since 2007.
5. The role of the committee is set out in its terms of reference within the Constitution approved by Council.
6. Good corporate governance requires independent and effective assurance processes to be in place to ensure effective financial management and reporting in order to achieve the Council's corporate and service objectives. It is the responsibility of the Audit Committee to undertake these aspects of governance on behalf of the Council.
7. The specific objectives of the Audit Committee set out in the Council's Constitution are to provide independent assurance to Cabinet and Full Council over the:
 - Adequacy and effectiveness of the Council's governance arrangements, including the effectiveness of the risk management framework and the associated control environment.

- Financial Reporting of the Council's Statement of Accounts ensuring that any issues arising from the process of compiling, auditing and certifying the Council accounts are dealt with properly.
8. The membership and terms of reference of the Committee are set out in the Council's Constitution. This had been amended in March 2010 following the decision of Full Council to delegate its responsibility for the approval of the Annual Statement of Accounts and the Annual Governance Statement to the Committee.
 9. The membership during the period April 2011 to March 2012 was as follows:

Chair: Cllr Edward Bell

Vice Chair: Cllr Owen Temple

Members: Cllr Reg Ord
Cllr Colin Carr
Cllr Brian Myers
Cllr Dennis Southwell
Cllr Barbara Harrison
Cllr Michele Hodgson
Cllr Linda Marshall

Co-optees: Ms Katherine Larkin Bramley
Mr Thomas Hoban

Summary of Meetings

26th May 2011

10. The Committee considered 3 reports from the Corporate Director Resources relating to the work of Corporate Risk Management to gain assurance that the Council is managing its risks effectively:
 - (i) highlighted changes to the key corporate and service strategic risks arising during the period January to March 2011;
 - (ii) summarised the work of Corporate Risk Management during the whole of 2010/11;
 - (iii) detailed the findings from an external review carried out by Zurich Municipal, the Council's Insurers, providing independent assurance to the Committee on the effectiveness of the operation of the Council's risk management framework.
11. The Committee considered a report from the Manager of Internal Audit and Risk, which outlined the work and performance of Internal Audit during the period January to March 2011 to gain assurance on the effectiveness of the Council's control environment.

12. The Committee received an update from the Corporate Director Resources on the performance of the payment of invoices to gain assurance that risks associated with late payments were being effectively managed.
13. The Committee considered an update report of the Corporate Director, Resources on the progress made on the implementation of recommendations made by the external auditor in the Annual Governance Report to gain assurance that improvements identified were being addressed. Further assurance was requested on progress being made on the development of a single asset register and asset revaluation.
14. The Committee considered 2 reports from the Corporate Director, Resources relating to Housing Benefit that provided assurance that identified improvements in the governance arrangements relating to the service were being effectively addressed:
 - (i) an update on the implementation of recommendations from the Audit Commission's Housing Benefits Inspection;
 - (ii) progress on the implementation of the integrated Revenues and Benefits System that would address many of the improvements identified in the Inspection report. The Committee asked that the Revenue and Benefits Manager attend the September meeting to provide further assurance.
15. The Committee noted the response provided by the Chair on behalf of the Committee, required by the external auditor to fulfil International Auditing Standards (IAS), relating to the Council's arrangement for the management of fraud and compliance with relevant laws and regulations.
16. The Committee considered and approved a report of the External Auditor outlining the Pension Fund Audit Plan for 2010/11.

30th June 2011

17. The Committee considered the Annual Internal Audit Report for 2010/11, and the overall opinion provided, to gain assurance on the adequacy and effectiveness of the Council's control environment to inform the Annual Governance Statement.
18. The Committee considered a report of the Corporate Director Resources, on the outcome of the annual review of the effectiveness of Internal Audit to gain assurance that the opinion provided in the Annual Audit Report could be relied upon.
19. The Committee considered a report from the Manager of Internal Audit and Risk outlining the risk based internal audit strategy. A proposed Strategic Audit Plan 2011-2016 was noted and the 2011/12 Audit Plan was approved. In reviewing this strategy the Committee considered how and where it gets the assurance it needs to be able to fulfil its role. This is

illustrated by the Council's overall assurance framework which is attached at Appendix 2 for approval.

20. The Committee agreed an action plan to improve its effectiveness following a self assessment workshop held in May 2011. A copy of the Action Plan is attached at Appendix 3 for information.
21. The Committee noted the Department of Communities and Local Government consultation exercise in relation to proposals on the future of public audit, following the decision to disband the Audit Commission, and the response provided to the consultation by the Corporate Director, Resources.
22. The Committee noted the Risk Management Improvement Plan to gain assurance that actions required, following the review of the Strategic Risk Management Framework by Zurich Municipal, had been incorporated and were being addressed.
23. The Committee approved the revised Risk Management Strategy and Policy following the annual review. An example risk assessment was demonstrated to ensure the Committee understood how this would work in practice.
24. The Committee considered and noted a report of the Corporate Director Resources, on the implications for the Council of the Bribery Act 2010 which came into effect from 1 July 2011.
25. The Committee considered the External Auditor's Interim Governance Reports relating to the 2010/11 audit of the Pension Fund and Durham County Council. The response to recommendations made to improve the control environment, provided by the Corporate Director Resources, was noted.
26. The Committee approved the draft 2010/11 Annual Governance Statement and noted the significant improvements made to the Council's governance arrangements during the year.
27. The Committee noted a letter from the External Auditor relating to a risk identified to the Group Accounts Opinion Audit.
28. The Committee considered the Annual Fraud Report 2010/11 provided by the Manager of Internal Audit and Risk, to gain assurance on the effectiveness of the Council's Counter Fraud and Corruption Strategy.

28th July 2011

29. The Committee considered the draft 2010/11 Statement of Accounts that had been certified on the 30th June in accordance with statutory requirements.

30. The Committee reviewed the Final Outturn Report for the General Fund and Housing Revenue Account and considered the implications for the Statements of Accounts.
31. The Committee agreed the Annual Report of the Chair of the Audit Committee summarising the work of the Committee in 2010/11 that was reported to full Council at its September meeting.
32. The Committee noted progress on the consolidation of the Council's bank accounts to gain assurance that risks associated with operating several banks accounts were being addressed.
33. The Committee considered a progress report of the External Auditor that outlined progress on the delivery of their responsibilities. The report also provided an update on key emerging national issues and developments of interest to the Committee.

29th September 2011

34. The Committee received an update from the Corporate Director Resources on the status of the final accounts. It was noted that the Council's combined Statement of Accounts were not yet complete. A set of accounts, including the pension fund, which was complete, was tabled at the meeting together with the Pension Fund Annual Governance Report, but were not considered by the Committee. The difficulties in finalising the accounts were noted and assurance provided by both the External Auditor and the Corporate Director that the accounts would be submitted for approval at a special meeting to be convened for this purpose on the 31st October 2011.
35. The Committee considered a report of the Corporate Director, Regeneration and Economic Development, that provided an update on the development of a Single Asset Register. Given the importance of this to the preparation of the 2011/12 Accounts, the Committee asked for a further update to be provided at the next scheduled meeting.
36. The Committee received an update report from the Civil Contingencies Unit Manager on the management of risks identified in the Durham and Darlington Local Resilience Forum's Community Risk Register.
37. The Committee considered an update report from the Assistant Chief Executive on the Council's Partnership Governance Framework and approved those partnerships on which assurance will be provided as part of the 2011/12 Internal Audit Plan.
38. The Committee considered a report of the Corporate Director Resources, which provided assurance on improvements being made to reduce the risk of duplicate payments.

39. The Committee approved the Council's Annual Governance Statement which will be published as part of the Statement of Accounts.
40. The Committee considered a progress report on the work and performance of Internal Audit, and the assurance provided on the control environment, for period the April to June 2011.
41. The Committee noted the verbal update provided by the Corporate Director Resources on the latest position regarding actions being taken to recover funds lost through the collapse of Icelandic Banks.

31st October 2011 Special Audit Committee

42. The Committee approved the Council's 2010/11 Statements of Accounts. In giving this approval the Committee considered a report from the Corporate Director Resources explaining the process for signing off the accounts and problems encountered in their preparation. The Committee also considered the Annual Governance Reports made by the External Auditor in relation to both the Pension Fund and Durham County Council. It was noted that the External Auditor will issue an unqualified opinion on the accounts of the County Council, the Group Accounting Statements, the Pension Fund Accounting Statements and the Value for Money Conclusion. This was a much improved position from last year where a qualified VFM opinion was provided in relation to the County Council's Statements.
43. In considering the Annual Governance Reports, the Committee noted adjustments made to the financial statements to correct errors disclosed during the audit and adjustments due to errors that management had declined to amend due to immateriality, which were approved in a letter of representation.
44. It was noted that the main errors in the draft County Council accounts primarily related to capital accounting entries for property, plant and equipment. The Corporate Director Resources provided assurance that work in progress to develop a single asset register and to strengthen capital accounting practices, as part of the unitisation of the finance function, would deliver the improvements required for the current year accounts. Progress on this together with recommendations made in the Annual Governance Reports will be monitored by the Committee.

10th November 2011

45. The Committee approved revised operational terms of reference which required amendment following the increase in membership resulting from the delegated authority to approve the financial statement of accounts. An updated forward plan of business was agreed in accordance with paragraph 6.1 of the terms of reference.

46. The Committee agreed a report of the Corporate Director, Resources which highlighted the strategic risks facing the Council and gave an insight into the work carried out by the Corporate Risk Management Group during the period July to September 2011.
47. The Committee noted a report of the Manager of Internal Audit & Risk which advised of the work carried out by Internal Audit during the period April to September 2011.
48. The Committee agreed a draft report of the Chair of the Audit Committee of the work of the Audit Committee for the period April to October 2011, to be reported to Council on the 7th December 2011.
49. The Committee approved a revision to the Internal Audit Charter which sets out the terms of reference and strategy for the Internal Audit Service.
50. The Committee agreed a joint report of the Head of Planning and Assets, and Head of Finance which provided an update on the development of a Single Asset Register to gain assurance that improvements required to the control environment relating to council assets were on track.
51. The Committee considered a report of the Corporate Director, Resources that provided an update on the status of the Benefits Inspection Action Plan (BIAP) and which set out how the performance of the Benefits Service is being monitored and managed, now and going forward. The Head of Finance (Financial Services) emphasised the importance that this was being given by the Authority, and members were given an update on the processes and timescales involved in moving to one new system. The Committee noted assurance being provided by CMT and Scrutiny on performance and resolved to rely on this assurance to avoid any duplication.
52. The Committee noted a report of the External Auditor advising of the procurement processes in place for local authorities, fire authorities, and police authorities in securing external auditors for the future.

5th January 2012

53. The Committee received assurance from a report of the Head of Environmental Health and Consumer Protection which provided an update on the strategic risks associated with contaminated land and the potential 'failure to identify and effectively regulate contaminated land'. Funding had not been made available for the current financial year which meant that the strategic risk remained high. A further bid had been submitted for 2012 which received strong support from the Committee.
54. The Committee considered a revision to the Local Code of Corporate Governance following the completion of an annual review of effectiveness of the County Council's Corporate Governance arrangements and recommended its adoption to the Constitution Working Group.

55. The Committee approved the timetable and preparation strategy for the 2011/12 Annual Governance Statement.
56. The Committee noted progress being made on the implementation of the governance action plan which highlighted areas of improvement arising from the annual review of the effectiveness of corporate governance arrangements in 2010/11.
57. The Committee noted a report of the Corporate Director, Resources, which detailed all recommendations for improving control weaknesses incorporated in the External Auditors 2010/11 interim and final governance reports. Management's response to recommendations made was noted. To monitor progress made on implementation, the Committee requested an update on progress to be considered as a standard item at each future Committee meeting until such time as assurance could be provided that all recommendations had been addressed.
58. The Committee noted a report of the Corporate Director, Resources, which provided the latest position on the rationalisation of the number of bank accounts in use across the Council to gain assurance that the risks of having numerous bank accounts was being addressed. On internal audit report on bank reconciliation was considered concurrently to gain further assurance that controls in place were adequate, and where not, that progress on agreed corrective action was being made on a timely basis.
59. The Committee considered a report of the External Auditor which presented the Annual Audit Letter for 2010/11. The External Auditor informed the Committee that an unqualified opinion had been provided on 31 October and that reasonable progress to address control weaknesses continued to be made.
60. The Committee was provided with a verbal update regarding work around the single asset register, a key piece of work which was one of the main factors in the delay of approving last year's accounts by the required statutory deadline.

16th February 2012

61. The Committee received assurance in a report of the Corporate Director, Resources that highlighted the strategic risks facing the Council and the work carried out by the Corporate Risk Management Group during the period October to December 2011. Additional briefing papers were circulated to the Committee which provided further information on two of the significant risks highlighted in the report, requested by the Chair and Vice Chair at pre-agenda.
62. The Committee approved minor revisions to the Councils' Risk Management Strategy and Policy.

63. The Committee received an update for the Corporate Director, Resources on the Annual Governance Statement action plan and sought additional assurance that planned target implementation dates would be achieved.
64. The Committee considered an update on the implementation of actions for improving control weaknesses incorporated in the External Auditor's 2010/11 Interim and Final Governance Reports and noted progress to date. To enable more effective monitoring the Committee requested key action priorities to be highlighted in future reports.
65. The Committee received an update on the work around the single asset register, and noted, although slightly behind schedule, no key issues had arisen. It was noted that assurance on the reliability and completeness of the asset register would be provided through periodic testing.
66. The Committee noted a report of the External Auditors that provided an update on progress in delivering their responsibilities.
67. The Committee noted a report of the Manager of Internal Audit and Risk that informed members of the work carried out by Internal Audit during the period October to December 2011 and challenged the reasons provided by management for the deferment of some planned work. Further information was requested to be provided from the relevant service manager.

22nd March 2012

68. The Head of Corporate Finance provided a briefing to members on the Council's budget setting procedures to gain assurance that adequate processes were in place to manage risk effectively.
69. The Committee received a further update on progress being made on the on the implementing of the agreed governance action plan.
70. The Committee noted a further update report of the Corporate Director, an progress made regarding the implementation of agreed recommendations for improving control weaknesses incorporated in the External Auditor's 2010/11 Interim and Final Governance Reports.
71. The Committee considered the annual report of the External Auditor on the outcomes of the Council's 2010/11 claims and returns and noted the improved position from the same exercise in 2009/10.
72. The Committee considered a report of the External Auditor on the audit plan for 2011/12 Accounts for the DCC Pension Fund and noted the key risk areas to be reviewed.
73. The Committee noted a report of the Corporate Director, Resources that provided members with a summary of the key accounting changes in the latest edition of the Code of Practice for Local Authority Accounting in the UK, which will apply to 2011/12 accounts. It was noted out that this would

bring about changes to the recording of the heritage assets owned by the Authority.

74. The Committee received an update of the Corporate Director, Resources, on the work around the single asset register and noted that Phase 1 was now complete. A progress report on phase 2, which was underway, was requested. The Committee noted that arrangements in place for the value and sale of land appeared fragmented and requested that a report be brought to committee to provide assurance that policies and procedures in place are effective and that expected targets for capital receipts are achievable.
75. The Manager of Internal Audit and Risk updated members on work which had been deferred and reported at the last meeting. It was noted that the Chair and Vice Chair had met with the Head of Housing and had gained assurance on the reasons for the deferment of the planned audit review of ALMO contract monitoring arrangements and that it had been agreed that the work would commence in six months time.
76. The Committee received an update from the Corporate Director, Resources on the position with the recovery of funds following the collapse of the Icelandic banks. It was noted that £4.775m had been recovered to date and that it was expected that most of the £7m owed would be received.
77. The External Auditor updated the Committee on future changes for the Authority's external auditor. It was noted that the Council's proposed external Auditors from 2012/13, following the decision to abolish the Audit Commission, was DA Mazars Partnership. A five year contract, effective from the 1st September 2012, is expected to be awarded. Thereafter, the Council would be required to appoint its own external auditor.

How the Audit Committee has made a difference during 2011/12

78. The Committee made a significant difference to the Council's governance, control and risk framework during the period April to October by :
 - Striving to help support the Council deliver its objectives and priorities by being a proactive and reactive body encouraging the early reporting of any risk and control issues to ensure that appropriate and timely action is taken to address them
 - Continuing to raise the profile of the Internal Audit and Risk Management Service through its reports to Audit Committee
 - Independent questioning and contributing to the development and control of internal audit plans
 - Seeking assurance on the effectiveness of corporate risk management arrangements
 - Seeking assurance on the effectiveness of the Council's corporate governance arrangements from a number of different assurance sources

- Improving the accountability of service managers to respond to outstanding internal audit reports and the implementation of agreed internal audit recommendations thereby helping to drive improvement in controls to manage risks effectively
- Continuing to provide regular challenge and demanding accountability on the effectiveness of the implementation and operation of key financial systems
- Challenging the level of internal audit resources and their work to ensure that the service is effective and a reliable assurance opinion on the Council's controls framework is provided
- Challenging how the Annual Governance Statement has been determined and reviewing the assurance framework in place to ensure that the Council's corporate governance arrangements are effective
- Challenging progress being made to overcome the control issues and difficulties encountered in preparing the Council's Statements of Accounts

Future Work

79. In accordance with best practice, the Committee has undertaken an annual review of its effectiveness. This year's review took the form of an on line anonymous survey developed by the Audit Commission.

80. The results of the survey, capturing feedback from 13 respondents, were reported and discussed in a workshop facilitated by the external auditor, drawing on his experience of the operation of audit committees elsewhere, on 13 May 2011.

81. The majority of actions identified for improvement in the workshop have now been implemented but further work is still need in some areas. In particular work planned to improve induction and training for new members will be progressed to response to any changes to Committee membership arising from next year's Council elections.

Recommendations and reasons

82. Members note the report and the work undertaken by the Audit Committee during the 2011/12.

Contact: Avril Wallage, Manager of Internal Audit & Risk, Tel 0191 383 3537

Appendix 1: Implications

Finance - There are no direct financial implications arising for the Council as a result of this report.

Staffing - None.

Risk – Not a key decision

Equality and Diversity/ Public Sector Equality Duty - None

Accommodation - None

Crime and disorder - The Audit Committee provide independent assurance that the Council's arrangements to combat the risk of loss through fraud are effective and all reported potential fraudulent acts are appropriately investigated and reported to the police where it is appropriate to do so.

Human rights - None

Consultation - None

Procurement – None.

Disability issues – None.

Legal Implications – None.

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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