Kent County Council

# AGENDA

## GOVERNANCE AND AUDIT COMMITTEE

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| **Wednesday, 19th September, 2007, at 10.30 am** | Ask for: | **Andrew Tait** |
| **Medway Room, Sessions House, County Hall, Maidstone** | Telephone | **01622 694342** |

*Tea/Coffee will be available 15 minutes before the start of the meeting*

**UNRESTRICTED ITEMS**

*(During these items the meeting is likely to be open to the public)*

1. Substitutes
2. Minutes - 29 June 2007 (Pages 1 - 4)
3. Declarations of Interest in items on the agenda for this meeting
4. Dates of future meetings:

| **Already agreed dates** | **To be agreed** |
|---|---|
| Tuesday, 4 December 2007 | Wednesday, 17 September 2008 |
| Wednesday, 5 March 2008 | Tuesday, 2 December 2008 |
| Monday, 30 June 2008 | Wednesday, 4 March 2009 |
| | Tuesday, 30 June 2009 |

5. Appointment of Head of Audit and Risk (Pages 5 - 10)
6. Future agenda planning - Focussing on the big issues (Pages 11 - 12)
7. Value for Money in Libraries (Pages 13 - 22)
8. Statement of Accounts 2006/07 (Pages 23 - 64)
9. Debt Recovery (Pages 65 - 68)
10. Arrangements for Audit and Risk from August 2007 (Pages 69 - 72)
11. Internal Audit Reporting (Pages 73 - 86)
12. Internal Audit Reporting - Irregularities (Pages 87 - 88)

13. Other items which the Chairman decides are urgent

## EXEMPT ITEMS

*(At the time of preparing the agenda there were no exempt items. During any such items which may arise the meeting is likely NOT to be open to the public)*

Peter Sass
Head of Democratic Services and Local Leadership
(01622) 694002

**Tuesday, 11 September 2007**

*Please note that any background documents referred to in the accompanying papers maybe inspected by arrangement with the officer responsible for preparing the relevant report.*

# KENT COUNTY COUNCIL

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## GOVERNANCE AND AUDIT COMMITTEE

MINUTES of a meeting of the Governance and Audit Committee held at County Hall, Maidstone on Wednesday, 29 June 2007.

PRESENT: Mr C G Findlay (Chairman), Mr R L H Long, TD (Vice-Chairman), Mr D L Brazier, Mr A R Chell, Mr C J Law, Mr J F London, Mrs M E Newell, Mr W V Newman, Mr R J Parry, Mr D Smyth, Mr M V Snelling and Mr R Tolputt.

OFFICERS: The Director of Finance, Mrs L McMullan, the Head of Audit and Risk, Mr A Wood; the Head of Corporate Performance, Mrs S Garton; the Head of Financial Services, Mr N Vickers; the Chief Accountant, Mrs C Head; and the Democratic Services Officer, Mr A Tait.

ALSO IN ATTENDANCE: Mrs J Eilbeck and Mr M Stevenson of PricewaterhouseCoopers; Mr D Wells, Mr S Mead and Ms K Shergill from the Audit Commission.

## UNRESTRICTED ITEMS

**14. Minutes – 7 March 2006**
*(Item 2)*

(1) With reference to Minute 2 (2) (b), the Head of Democratic Services informed the Committee that there would be no report on CRB Checks for Members as the County Council's Code was voluntary and was in the remit of the Standards Committee.

(2) RESOLVED that subject to the presence of Mr M Stevenson from PricewaterhouseCoopers being recorded instead of Mr Brown the Minutes of the meeting held on 7 March 2007 are correctly recorded and that they be signed by the Chairman.

**15. Annual Audit and Inspection Letter**
*(Item 3 – Report by Director of Business Solutions and Policy)*

RESOLVED that the report be noted.

**16. External Audit Plan and Fee**
*(Item 4 – Report by Head of Audit and Risk)*

RESOLVED that the Audit and Inspection Plan and Fee for 2007/08 be approved.

**17. Ombudsman Complaints**
*(Item 5 – Report by Chief Executive)*

RESOLVED that the report be noted.

**18. Ombudsman Report – Implications for the Authority**
*(Item 6 – Report by Director of Business Solutions and Policy)*

RESOLVED that the findings of the Local Government Ombudsman be noted together with the County Council's response.

**19. Draft Statement of Accounts 2006/07**
*(Item 7 – Report by Director of Finance)*

(1) The ISA (UK&I) 260 Letter was tabled.

(2) The Committee delayed approval of the Statement of Accounts until it had considered the Internal Audit Annual Report and the review of the effectiveness of the Internal Audit function (Minute 24).

(3) RESOLVED that the Statement of Accounts for 2006/07 be approved subject to the Chairman, Vice-Chairman, Labour and Liberal Democrat Group Spokesmen being consulted on any changes which may be made to the Accounts following completion of the external audit.

**20. Treasury Management Annual Review**
*(Item 8 – Report by Director of Finance)*

RESOLVED that the report be noted.

**21. Spending the Council's Money**
*(Item 9 – Report by Director of Finance)*

(1) The proposed amendments to the Constitution were tabled as Appendix 3.

(2) RESOLVED that:-

(a) the replacement of the "Code of Practice on Tenders and Contracts" by "Spending the Council's Money" be agreed; and

(b) the proposed changes to the relevant Appendix in the Constitution be recommended to the meeting of the County Council in September 2007.

**22. Strategic Risk Register and a Review of Risk Strategy**
*(Item 10 – Report by Head of Audit and Risk)*

RESOLVED that:-

(a) the current Strategic Risk Register be noted together with the impact that the risks would have and the controls that are in place to mitigate the likelihood of the risks occurring; and

(b) the proposed amendments to the Risk Strategy set out in paragraph 9 of the report be agreed and the consequent revised Risk Strategy set out in Appendix 3 of the report be approved.

**23. Governance of Partnerships**
*(Item 11 – Report by Head of Audit and Risk)*

RESOLVED that the report be noted.

**24. Internal Audit Annual Report**
*(Item 12 – Report by Head of Audit and Risk)*

RESOLVED that the outcome of Internal Audit's work be noted, including the outcome of the self-assessment of the effectiveness of the internal audit function.

**25. Internal Audit Reporting**
*(Item 13 – Report by Head of Audit and Risk)*

RESOLVED that the report be noted.

**26. Internal Audit Reporting - Irregularities**
*(Item 14 – Report by Head of Audit and Risk)*

RESOLVED that the report be noted.

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**Item 5**

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| By: | The Head of Audit & Risk |
| To: | Governance and Audit Committee<br>19 September 2007 |
| Subject: | **APPOINTMENT OF HEAD OF AUDIT AND RISK** |
| Accountable Officer: | The Head of Audit & Risk |
| Classification: | Unrestricted |

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**Summary**: To provide an update to the Governance and Audit Committee on the Head of Audit and Risk role, key contacts, other aspects of the audit services contract and the next steps planned.

**FOR INFORMATION**

## 1. HEAD OF AUDIT AND RISK ROLE - BACKGROUND

The culture of Kent County Council is one of excellence, innovation and development. Against that backdrop it is important to ensure that Members and officers have assurance that business objectives are being achieved and that associated risks are being managed or mitigated. Internal audit has a significant role to play in providing that assurance in relation both to the risks themselves and to the management controls in place.

A key role in the provision of audit is the Head of Audit and Risk. Over the past four years, there have been five changes in appointment to the post of Head of Audit and Risk. To help achieve some stability in this role and assist in the continuous improvement of the finance function, KCC has developed an innovative solution by bringing in PwC resources to perform the Head of Audit and Risk role for the next 2 years. During this time PwC will work with the Council in true partnership to provide the best audit service possible.

These arrangements will allow KCC and PwC jointly providing a responsive, risk-based service that not only provides assurance on existing arrangements but also continually strives to keep the Council at the forefront of local authority provision, delivering the best possible services to residents, in the most efficient and effective manner, making the best use of the Council's available resources.

## 2. KEY CONTACTS

Formally, **Janet Dawson** will be Head of Audit and Risk. Janet is a partner in PwC with experience in internal and external audit in the public sector. She will lead, on behalf of the Director of Finance, on issues relating to internal audit, risk, insurance and VFM.

She will be supported by her colleague **Sean Rooney**, as well as by KCC staff. Sean is a PwC senior manager who specialises in risk management and public sector internal audit.

Both Janet and Sean are currently contactable through the Internal Audit team. Full contact details including KCC extensions and email addresses will be established and circulated shortly.

## 3. KEY RESPONSIBILITIES

The purpose of the role is to lead on the strategic approach to the management of risk and internal audit and the promotion and maintenance of the highest standards of internal control and governance. The Head of Audit and Risk will also lead on the setting and delivery of the Value for Money programme on behalf of the Value for Money Board. Key responsibilities will include;

- Advising and reporting to the Governance & Audit Committee and the Director of Finance on key governance and internal audit issues facing the Council
- Developing innovative approaches to the provision of an internal audit service to the Council
- Providing the strategic direction to the achievement of objectives related to strategic risk management and lead the Corporate Risk Management Group
- Ensuring that proper arrangements are in place to provide an effective best practice internal audit service to the Council
- Presenting the strategic audit plan and providing an annual assurance to Governance & Audit Committee
- Ensuring effective communication with the Council's external auditors to secure co-ordination in the deployment of audit resource

- Managing the overall relationship with senior management in service directorates on strategic issues related to risk management, internal audit and internal control issues
- Ensuring that appropriate arrangements are in place to protect the assets and liabilities of the Council through external insurance or internal self-funded arrangements
- Leading on the setting and delivery of the Value for Money programme on behalf of the Value for Money Board
- Contributing to the overall management of Corporate Finance as a member of Corporate Finance Management Team and the finance function as a member of Finance Strategy Board.

Janet will be responsible for the elements set out above. Much of this role comprises setting the strategic direction of the service, and will enable Janet to bring in her experience, that of PwC and examples of best practice to the service. However, the more operational elements of the role such as leading the planning, delivery and resource management, reporting and relationship management at a senior levels across the organisation will be undertaken by Sean.

## 4. OTHER ASPECTS OF THE CONTRACT

In addition to the Head of Audit and Risk role, we will also be supporting KCC in the following audit and assurance activity;

- **IT Audits** - Provide up to 150 days of IT audit resource for the delivery of a range of audits (including IT audit planning) that will provide the Council with assurance that the IT environment is well controlled and effective.
- **General audit assurance work** - Provide up to 50 days of general audit resource for the delivery of a wide range of audit assurance work which the Council may require from time to time to assist in the delivery of the annual audit plan.
- **Specialist audit work** - The provision of and/or training in specialist audit work including the areas of Fraud Investigation, Forensic Accounting, Value for Money and any other assurance services etc. These services will be requested, scoped and costed as required.

Discussions about work to support the full audit of the Kent Pension Fund accounts are taking place with the Audit Commission and will be included in the internal audit plan as appropriate.

## 5. BENEFITS OF THE CONTRACT

The contract for audit services and the Head of Audit and Risk role is structured in an innovative way so as to bring a number of benefits to KCC, including continuous improvement to the audit and risk function.

Our objective is to take forward the improvements already in train, thereby providing some consistency of approach and some stability for the staff, whilst looking for opportunities to develop them and the section quickly towards best practice over the contract period.

Our initial meetings with the internal audit staff have already identified areas where we are all keen to make improvements in working practices, for example:

- Aligning risk and audit planning and reporting cycles better with a view to greater integration in future;
- Supporting the development of the Governance and Audit Committee; and
- Opportunities for staff training and development.

Other key benefits include;

- Our delivery team is structured to ensure full integration with your finance function, to facilitate access to the right resources at the right time. We will work together to identify the key risks and plan the most appropriate audit approach.
- Innovation – PwC have a track record of innovation in the internal audit market place. We were the first of the firms to introduce automated working papers and remote site working and we regularly use web based questionnaires and computer interrogation techniques to broaden the assurance that we can give. We are working with a number of our clients on the next generation of reporting that uses broadcast technology rather than paper to communicate effectively and quickly with the key users of audit reports.

## 6. NEXT STEPS

We are currently planning a round of meetings across the Council with key members, officers and officer groups to introduce ourselves, to develop our understand the needs of the organisation from the risk management and audit functions and to confirm the risk related audit areas of the audit plan for the six months to 31 March 2008. Work will start in the coming months to plan the work programmes for 2008/09 for risk management, audit and value for money and ensure that those are reported before the start of the financial year.

In conjunction with planning our approach over the next 24 months, we will be giving consideration to the forward agenda for the Governance and Audit Committee, appropriate issues and reporting timescales.

More immediately, we will be reviewing the requirements of the CIPFA Code of Governance for 2007/08, mapping those against the current arrangements, and identifying any actions required by the Council and by Internal Audit to ensure compliance and appropriate reporting by 31 March 2008.

In conclusion, we are excited by the opportunity to develop this innovative approach with you and we look forward to working with all of you in the future.

Janet Dawson
Head of Audit and Risk
Extension 4614
3 September 2007

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| By: | The Head of Audit & Risk | **Item 6** |
| To: | Governance and Audit Committee<br>19 September 2007 | |
| Subject: | **Future agenda planning – focusing on the big issues** | |
| Accountable Officer: | The Head of Audit & Risk | |
| Classification: | Unrestricted | |

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**Summary**: This report considers future agenda planning for the Governance and Audit Committee, involvement of members in identifying issues to be included and a means for doing so.

**FOR INFORMATION**

The agendas for the Governance and Audit Committee over the past 12 months have focused on the development of the reporting processes and protocols for audit and risk management, certain aspects of governance arrangements and plans and outcomes from the audit of the financial statements. This has been important work to ensure that arrangements are in place for managing risks and that appropriate information on those risks, their associated controls and levels of assurance within the Council is being recorded and can be reported.

There is now scope to move the agendas to focus more heavily on strategic risks, the levels of assurance required and the provision of supportive challenge to officers to promote continuous improvements in the governance and internal control environment. There is also an opportunity to review the current reporting formats, attendance at meetings and effective use of time.

Issues to consider include:

- Which strategic objectives do members consider to be most significant?
- How confident are members that risks associated with those objectives are being managed effectively?
- Which other areas of risk interest or concern Committee members most?
- What assurances do members require and in what format, e.g. assurance mapping, officer presentation, audit reporting, business unit self certification?
- What other sources of information (e.g. other Councils, other government bodies, service specialists, private sector bodies) would be of interest?
- How effective do members consider the Committee to be in providing review and challenge to the governance arrangements of the Council?

**Next steps**

In order to make the agendas of greater interest, to promote engagement and challenge, we are proposing to structure future agendas to include consideration of the issues above. Members are asked to provide their views on the issues raised to the Director of Finance or Head of Audit and Risk by the end of October.

The outcome of the consultation process, proposed agenda topics and any changes to reporting format will be discussed at the December meeting. Any updates to the Committee Charter required as a result of this process will also be reported to the December meeting.

Janet Dawson
Head of Audit and Risk
Extension 4614
3 September 2007

Item 7

By: The Head of Audit & Risk

To: Governance & Audit Committee – 19th September 2007

Subject: Value for Money in Libraries

Classification: Unrestricted

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**Summary**: This report provides Members with the outcomes of the Value for Money Review of the Library Service

**For Information**

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**INTRODUCTION**

1 An on-going programme of Value for Money (VfM) reviews has been planned and was shared with this Committee on the 7th March 2007 as part of the Council's approach to managing VfM across the Authority.

2 The second is of those reviews is now complete and the outcomes of the review are presented in this report.

**APPROACH TO VALUE FOR MONEY REVIEWS**

3 For each review, it is important that there is a degree of external challenge. To date, this has been provided by PriceWaterhouseCoopers (PwC). PwC are able to bring challenge not only to the costs and outcomes, but also comparison of the particular service strategy to other Authorities and emerging best practice.

4 Having completed the first two VfM reviews, it is important to reflect on the lessons learnt from the process, in order to improve the process for future reviews. This will be carried out in the autumn and reported to this Committee in December.

**LIBRARIES VALUE FOR MONEY REVIEW**

5 The overall objective of this review is to consider whether value for money is being provided through the Libraries Service (excluding Archives) and to make recommendations (if appropriate) where value for money can be improved. The review is being conducted in three phases:

- Phase 1: High-level service context including library strategy review; overall budget analysis; and comparisons to other local authorities;
- Phase 2: Review of premises costs. Transport cost and arrangements, route planning for van deliveries for the circulation of new and existing stock reservations and withdrawn items; and

- Phase 3: Front of house process review to assess the opportunity to reduce staff down time and increase stock issues.

Phase 1 is now complete, the outcome of which is detailed below.

6 The review, which was carried out by PriceWaterhouseCoopers (PwC), states that "*The Libraries Service is clearly demonstrating high performance in a number of key areas.*" Page 3 of the executive summary which is attached gives nine examples to support this statement.

7 PwC acknowledges that "*the service continues to identify and develop new opportunities to improve value for money.*"

8 In contrast to this, the key finding of the review is that "*The Council has 104 static library branches (as at July 2007) dispersed throughout the County which is the result of Elected Member policy and this policy has consequences in terms of value for money: If providing a high quality service is not just about meeting the PLSS targets, but about providing the right number of libraries in the right locations, then it is suggested that this decision be reconsidered in the context of value for money and to consider options that might enable a further enhancement of the service through a revised portfolio of libraries.*"

9 The review also identified six findings which draw on the examples of national best practice, which could lead to actions to help achieve better value for money outcomes for the Libraries Service, library users and the residents of Kent. Many of these national examples are being replicated in Kent already, others are under consideration. In the main the phase 1 report has identified very little that the service was not already aware of or has considered for changes.

10 The six findings are shown on page 6 of the attached executive summary and the Library service response to the recommendations is contained in Appendix 2.

11 A copy of the full report is available on request.

**SUMMARY AND RECOMMENDATIONS**

12. Members are asked to note the key findings of Phase 1 of the VfM review of Libraries.

Andy Wood
Head of Financial Management
01622 694**622**
andy.wood@kent.gov.uk

## Appendix 2 - Management Response to PWCs Recommendations

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|---|---|
| Recommendation 1 | IT expenditure is not offering value for money. This is an historic issue related to the nature of the contract. The service should continue to exploit technology developments at the Council and through the South East Library Management Systems (SELMS) particularly in light of the opportunities from Better Stock Better Libraries; |
| Management Response | The Service recognises this as an issue and is already actively considering a range of options for the next ICT contract (due to start April 2009) including the SELMS model. |
| Recommendation 2 | The overall utilisation of workstations within libraries is approximately 50%. This average utilisation is a reflection of high utilisation in some libraries and low utilisation in others. value for money could be better delivered by moving some of the workstations from libraries with lower utilisation rates to those with higher utilisation rates; |
| Management Response | The service is unable to implement this at the moment, because it would mean failing on one of the public service standards (no.3). However, the standards are expected to change in the near future and once there is certainty in this area, the Service will be able to review current allocation of work stations. |
| Recommendation 3 | Despite Kent increasing overall issues, AV issues and therefore income for AV material is likely to reduce in the future as part of a national trend and the service should build on the income generation initiatives put into practice and consider the implementation of innovative solutions |
| Management Response | The service recently completed a study of income generation which reviewed best practice in this area across the country and across different sectors. This study was undertaken on behalf of South East Region library authorities and was part funded by MLA SE. The service is currently starting the process of implementation of the recommendations from this report. Findings from the study found that if we extend the loan period and reduce hire charges for AV materials we can substantially increase issues and income. As part of annual fees and charges report to the Cabinet Member we will be looking to extend the existing pilot schemes in Dartford, Dover and Tonbridge to the rest of the county |
| Recommendation 4 | The Library Service has introduced an instant library card and one-off guest membership to promote social inclusion and negate the immediate need for proof of identification in certain circumstances. This will make it easier for people to join and should be widely promoted to attract a wide range of new members; |

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| Management Response | This approach was welcomed and management feel that they would like to explore taking this further in line with some of the case studies offered by PWC to broaden access opportunities. |
| Recommendation 5 | The Library Service should implement more efficient procurement as is identified in the Stock services Review. It is noted that the timescales will vary but implementation of many substantial recommendations is not possible until 2009 due to IT constraints prior to letting of a new contract; |
| Management Response | The service is currently working hard to achieve this along with other initiative such as online payments. |
| Recommendation 6 | There is some information that indicates a backlog in building maintenance. We have not been able to compare maintenance spend with other library authorities or other local authority services to determine if this is a result of deficiencies in the overall budget or whether the service is not getting value for money from the maintenance contracts that are procured. Further research on maintenance spending and value for money is needed as part of developing the asset management strategy. |
| Management Response | The service is already developing and working on an asset management strategy. |

**Number of Libraries issue**

The current network of libraries in Kent is largely the one inherited by KCC at Local Government re-organisation in 1974. This was a combination of the County Library Service (which served largely rural communities) and a number of Borough Councils, which had provided urban library facilities in their own areas. The resulting network is inconsistent in its provision across the County and therefore not the one we would have created had we developed a Countywide Library Service from scratch. While welcoming the affection people in Kent have for their local libraries, we recognise that short-term radical change of the library network would be very unpopular and therefore politically unwise. Managers have put forward a series of proposals for incremental change over the years since 1974, the latest of which has resulted in member decision to close three very small and poorly used libraries during 2007. Changing use of libraries, and changing habits of our customers, combined with the development of much improved remote access to our services, have enabled us to develop proposals for further reductions over the coming years. We have also been piloting some different models of local service access by working in partnership with other KCC Units, Parish Councils and schools. We will be putting forward proposals for further phases of network rationalisation in the medium-term which, if adopted by members, would move us nearer to the kind of library network which would enable us to consistently provide the highest quality service within available resources.

# Executive summary

**Scope and approach**

The overall objective is to consider whether value for money is being provided through the Libraries Service (excluding Archives) and to make recommendations (if appropriate) where value for money can be improved.

The review is being conducted in three phases. The first phase is the context, overall budget analysis and comparisons and library strategy. There is a need to understand the context of the service provision and the way in which Kent provides its Libraries Services. The areas for wider consideration in phase 1 were:

The key changes in patterns of libraries usage;
The key value for money indicators e.g. cost per book issued, IT costs by usage;
The existing projects and programmes of work which look to provide value for money and how they will achieve these objectives.

**Where the service is now**

The Libraries Service is clearly demonstrating high performance in a number of key areas, for example:

The strategy is regularly reviewed by the service to ensure it reflects current priorities and customer needs. Outcomes from new initiatives such as the MLA ‘A Blueprint for Excellence – Public Libraries 2008–2011’ are considered as part of the development of the strategy;
Kent were one of only two councils to improve their score by two to achieve top ratings for culture (service assessment is primarily made up of library indicators) in 2006;
Achieving high performance against the Public Library Service Standards amongst their family group in the majority of categories;
Overall issues for 2006/07 were up by 1.48% against the 2005/06 figure (this includes AV which is estimated to be falling nationally by a significant percentage due to external factors such as the increase in the availability of alternative sources);
Book issues were up 3.4% for the same period. Trend analysis indicates that issues for the authority have been consistently rising for the past 18 months;
Opening hours review recently implemented an 11% increase in opening hours (with no additional costs) increasing customer satisfaction with the potential to increase visits and issues;
Consistent theme of investigation and consideration into new options which would deliver efficiency savings, increase value for money and improve response to customer needs, examples include the Access Services and Stock Services review;
Maintaining low comparative premises costs despite the number of libraries; and
Spend on books and materials per head of population in 2005/06 was just below average at 22nd out of 34 counties, a significant improvement on 2000/01 when spend was the lowest of all counties. Page 3

# Executive summary

It has been clear throughout the review that the service continues to identify and develop new opportunities to improve value for money. There are a number of ongoing initiatives, projects and programmes underway all of which either have improved or will improve value for money

Our findings from the review indicate a number of areas where the Libraries Service faces challenges in continuing to achieve value for money. The key issues are:

Number of Libraries;
Employee costs (figures to be re-assessed once savings embedded from restructure);
Building maintenance;
Book issues;
Acquisition levels;

IT expenditure; and
Customer satisfaction

**Key findings and issues**

Kent has a reasonably dispersed population across several main towns. The dispersed nature of the population is very different to many other County Councils. The distance from a library does not accurately reflect accessibility for the individual as there are a number of other factors to be taken into consideration such as the location of the library and the public transport network. The Council has 104 static library branches dispersed (as at July 2007) throughout the County which is the result of elected member policy and this policy has consequences in terms of value for money, although an accurate comparison of value for money against services with lower libraries per head or per hectare is very difficult. If providing a high quality service is not just about meeting the PLSS targets, but about providing the right number of libraries in the right locations, then it is suggested that this decision be reconsidered in the context of value for money and to consider options that might enable a further enhancement of the service through a revised portfolio of libraries.

Employee costs are driven by the number of libraries, staff and average salary. In Kent, the average salary is in line with comparator authorities but number of employees per ’000 population is above average. This is, in part due to the high number of libraries. In fact, the number of employees per library is below average but due to the above average number of libraries overall staff levels are higher than the average.

These figures are based on the old structure as we do not have comparator costs for the new structure. It is noted that these will reduce once the structure is embedded and the savings have been achieved through the restructuring. The proposed staff restructure may impact on performance; for example issues and customer satisfaction levels as a result of the reduced staff capacity following implementation of the new structure. The new structure will also deliver savings and it is early to say if the overall result will be greater or lower value for money.

# Executive summary

The Library Service has acknowledged that whilst these figures and recent increase in total issues are encouraging and evidence of a change in the direction of travel there is still some way to go to achieve the desired increase in service levels and even greater value for money for library users and the residents of Kent. The historical levels of investment have meant that the service was starting from a position of under investment in the service but is now beginning to increase performance and close the gap with other authorities.

IT expenditure is significantly above average in Kent and has grown at more than twice the average rate since 2000/01. The increase in expenditure is in part due to the cost of extending the number of computerised libraries in 2004/05 and 2005/06 from 41 libraries to a total 87 libraries. These costs were built in to the existing IT contract some years ago and will not be reduced until the next contract is implemented in 2009.

**How the service can improve value for money – conclusions and recommendations**

As part of the review of the service a number of recommendations have been identified, which have been developed from the key findings and issues and also draw on the examples of national best practice to achieve better value for money outcomes for the Libraries Service, library users and the residents of Kent:

IT expenditure is not offering value for money. This is an historic issue related to the nature of the contract. The service should consider exploiting technology developments at the Council and through the South East Library Management Systems (SELMS) particularly in light of the opportunities from Better Stock Better Libraries;

The overall utilisation of workstations within libraries is approximately 50%. This average utilisation is a reflection of high utilisation in some libraries and low utilisation in others. value for money could be better delivered by moving some of the workstations from libraries with lower utilisation rates to those with higher utilisation rates;

Despite Kent increasing overall issues, AV issues and therefore income for AV material is likely to reduce in the future as part of a national trend and the service should build on the income generation initiatives put into practice and consider the implementation of innovative solutions;

The Library Service has introduced an instant library card and one-off guest membership to promote social inclusion and negate the immediate need for proof of identification in certain circumstances. This will make it easier for people to join and should be widely promoted to attract a wide range of new members;

Implement more efficient procurement as identified in the Stock Services review e.g. online payments and electronic stock ordering. It is noted that the timescales will vary but implementation of many substantial recommendations is not possible until 2009 due to IT constraints prior to letting of a new contract; and

There is some information that indicates a backlog in building maintenance. We have not been able to compare maintenance spend with other library authorities or other local authority services to determine if this is a result of deficiencies in the overall budget or whether the available budget is not delivering value for money from maintenance contracts that are procured. Further research on maintenance spending and value for money is needed as part of developing an asset management strategy.

# Executive summary

The County Council has the statutory requirement to provide a comprehensive and efficient library service and the DCMS has powers to intervene if this is not happening. DCMS has written to local authorities to express concern about library closures and to seek information on proposals for the current financial year. It is recommended that Members review the policy decision to operate a high number of libraries per ‘000 and also a high number per ‘000 hectares, in the context of the need to improve value for money for library users and the residents of Kent. The number of libraries is the result of elected Member policy and this policy has consequences in terms of value for money. An accurate comparison of value for money against services with lower libraries per head or per hectare is very difficult. The Library Service has demonstrated evidence of improved performance from the CPA assessment, reducing costs through the staff restructure and is demonstrating value for money through a number of new initiatives. Maintaining a large portfolio of static libraries does not necessarily mean that costs and therefore value for money cannot be achieved, as indicated by the example of Devon who have a relatively high number of libraries delivered at relatively low cost. Our experience does indicate that there is likely to be inherent inefficiencies within the service from maintaining such a large portfolio of libraries, 104 static libraries in Kent. These inefficiencies are likely to relate to employee and premises costs, although any reduction in these costs whilst maintaining the same number of libraries is likely to have a significant impact on performance.

**Next steps**

As identified in the terms of reference there is the potential for two reviews to address further elements of value for money, subject to agreement of scope and timeline of these phases, particularly noting that the service is currently being restructured:

The high number of libraries per ‘000 population and also a high number per ‘000 hectares will have a direct impact on transport arrangements and route planning for van deliveries for the circulation of new and existing stock, reservations and withdrawn items, and it’s possible costs could be reduced in this area through improved route planning and circulation of stock; and

There is an opportunity to conduct a front of house process review to assess the opportunity to reduce staff down time and increase stock issues and reduce staff handling of the stock. This would need to take into account the differences in roles between librarians and customer service staff.

*Our work has been undertaken in accordance with the terms and conditions agreed between ourselves and Kent County Council on February 2007. We do not accept any duty of care or responsibility to any party other than Kent County Council. Any oral comments made in discussions relating to this report are not intended to have any greater significance than* *explanations of matters contained in the report. Any oral comments that we make do not constitute oral advice unless we confirm any such advice formally in writing.*

*In the event that, pursuant to a request which the Kent County Council has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PwC promptly and consult with PwC prior to disclosing such report. Kent County Council agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Kent County Council shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC, Kent County Council discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.*

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Item No 8

By: The Director of Finance

To: Governance and Audit Committee – 19 September 2007

Subject: 2006/07 Report to those charged with governance (ISA 260)

Classification: Unrestricted

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Summary: This report asks Members to note the final ISA 260 for the 2006-07 accounts.

**FOR DECISION**

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## 1. INTRODUCTION

1.1 The draft ISA 260 was discussed at the Governance and Audit Committee in June. A final ISA 260 was issued and discussed with the Chairman of Governance and Audit prior to the Statement of Accounts being signed. The accounts were signed on the 24th July.

## 2. ISA 260 - CONTENTS

2.1 The final ISA 260 contains a number of accounting matters that were not previously identified in the report that went to the June meeting.

2.2 It also contains a summary of recommendations and management responses in Appendix D. The management responses will be taken forward and implemented by the target dates where stated.

## 3. RECOMMENDATION

3.1 Members are asked to:
Note the final ISA 260.

**Cath Head**
**Chief Accountant**
**Ext: 1135**

**Lynda McMullan**
**Director of Finance**
**Ext: 4550**

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Government and Public Sector

July 2007

# Kent County Council

## 2006/07 Report to those charged with governance

PRICEWATERHOUSECOOPERS

PRICEWATERHOUSECOOPERS

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July 2007

Ladies and Gentlemen

**2006/07 Report to those charged with governance**

We are pleased to present our final report in connection with the audit of the 2006/07 Financial Statements. This replaces the report presented to you at the Governance and Audit Committee on 29 June 2007.

The key changes to this report include:

- Inclusion of the accounting matters identified during the audit of the Pension Fund; and
- New accounting matters identified following the draft ISA 260 Report, including:
  - The difference between the Authority's Credit Ceiling and Capital Financing Requirement (Adjustment A);
  - Accounting for debtors and creditors;
  - Sports England Debtor;
  - Asylum seekers bad debt provision; and
  - Value of landfill allowances.

We would like to express our thanks to the management and staff at Kent County Council for the assistance given to us during the course of our work.

Yours faithfully

PricewaterhouseCoopers LLP
Encs

# Contents



***Code of Audit Practice and Statement of Responsibilities of Auditors and of Audited Bodies***

*In March 2005 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and of audited bodies'. It is available from the Chief Executive of each audited body. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas. Our reports and management letters are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.*

# Executive summary



### The purpose of this report

This report summarises the results of our 2006/07 audit of accounts.

It includes the issues arising from our audit of the financial statements and those issues which we are formally required to report to you under the Audit Commission's Code of Audit Practice and International Standard of Auditing (UK & Ireland) (ISA(UK&I)) 260 - "Communication of audit matters with those charged with governance".

It also includes the results of the work we have undertaken on 'Use of Resources' under the Code of Audit Practice, to support our formal conclusion in this area.

Our work during the year was performed in line with the plan that we presented to you on 30 June 2006. We have issued or plan to issue a number of reports during the audit year, detailing the findings from our work and making recommendations for improvement, where appropriate. A list of these reports is included at Appendix A to this letter.

We have set out below the most important issues and recommendations that we have discussed with you in the course of our work.

### Financial Statements

We have now completed our audit of the Authority's 2006/07 Financial Statements. We have noted several matters that we wish to bring to your attention including:

- Contract Services (DSO) pension provision;
- Prior period adjustment for the Kent Pension Fund Liability;
- Provision for the costs and recognition of income for the Kent Police HQ roof;
- Accounting for PFI Schemes;
- The difference between the Authority's Credit Ceiling and Capital Financing Requirement (Adjustment A);
- Restructuring of debt;
- Accounting for prepayments;
- Accounting for debtors and creditors;
- Sports England debtor;
- Asylum seekers bad debt provision;
- Bad and doubtful debt provisions;
- Value of landfill allowances;
- Accounting for archives and libraries IT services;

- Shepway collaboration;
- Pension SORP;
- Statement of Investment Principles;
- Review of fund manager/custodian internal control reports;
- Late payment of pension contributions;
- Annual Returns; and
- Other best practice issues.

These matters have been set out in more detail within the financial statements section of this report.

We anticipate, at the time of writing this report, that we will issue an unqualified audit opinion on the financial statements.



## Use of Resources

Under the Audit Code of Practice we are required to give an opinion on the Authority's use of resources. This opinion has been arrived at following an assessment of the Authority against a set of criteria issued by the Audit Commission. We are pleased to confirm that at the time of writing this report we propose to issue an unqualified opinion on Use of Resources..

During 2006/07 we have also completed our Use of Resources Assessment. This differs from the opinion and feeds into the Authority's wider Comprehensive Performance Assessment (CPA) score. The Authority achieved an excellent Level 4 score for the CPA Use of Resources assessment.

We have been working with the Authority on a number of targeted reviews. The one completed review, on School Clusters, has been reported to the Governance & Audit Committee. The remaining reviews are work-in-progress and will be reported to the same Committee as they are completed.

# Financial statements



## Accounts

We have completed the audit of the Authority's accounts in line with the Code of Audit Practice and Auditing Standards. At the time of writing this report we anticipate issuing an unqualified audit opinion on the financial statements.

### Accounting matters for consideration

ISA 260 requires us to report to you any material weaknesses in the accounting and internal control systems identified during the audit. We have detailed below those matters that we have identified as part of our audit that fall to be reported to those charged with governance.

### Direct Service Organisation (DSO) Pension Provision

As identified in our 2005/06 ISA 260 Report the Contract Services Division was externalised in 1999. At this point, the Authority recognised that they would be liable for the additional unfunded pension liability for the 102 people who worked in this area and who took early retirement just before or shortly after the transfer. The cost of this pension 'top up' is met directly by the directorates, and is paid through the payroll system, rather than being met through the pension fund.

At the time of the transfer an actuarial valuation was performed and a liability set up within Strategic Planning for the future cost of these pensions. This provision, which currently stands at £455k, is not sufficient to meet the expected total liability as valued by the actuaries Hymans Robertson. However, the actuarial valuation is now included as a 'liability related to defined benefit pension schemes' alongside the main pension liability on the balance sheet, and amounts to £2,487k as at 31 March 2007. The provision of £455k has been moved to reserves in the final version of the 2006/07 financial statements. As with the pensions prior period adjustment (see below) we have noted that the actuary does not appear to have been in receipt of all relevant information needed to calculate the FRS 17 entries, for example, the value of any assets (provision) and the ongoing contributions being paid to meet the costs of the additional pensions. Therefore the full set of FRS 17 figures required to meet the FRS 17 disclosure requirements has not been provided by the actuary.

Whilst the funds set aside (as a provision/reserve) to meet the pension costs are currently significantly less than the liability, funding has been formally built into the Medium Term Financial Plan from 2009/10, when the existing provision set aside to meet the ongoing contributions is expected to run out.

### Prior period adjustment for the Kent Pension Fund liability

During 2006/07 the Authority identified a £4.2 million 'unfunded liability' that arose when officers took early retirement and the Authority agreed to top up their full pension. These unfunded liabilities were incurred between the restructurings of 1974 and 1998. Although officers were aware of these liabilities it had not been possible to forward the relevant information to the actuaries because they could not be separately identified until the pensions administration and pensions payroll were integrated in 2005/06. As a result the related actuarial liabilities have been previously omitted from the total FRS 17 pension liabilities. However, the figures were included within the pension fund notes in the accounts.

The actuaries have now been informed of this additional amount and have included the unfunded liability in their calculations of the FRS 17 figures for 2006/07. This has resulted in a prior period adjustment being required to restate the 2005/06 figures. The prior period adjustment has resulted in a £62m increase in the pension liability for 2005/06.

**Pension liabilities**

New arrangements should be put in place so that the Pensions and the Accounting Teams work with the actuaries to ensure that complete and accurate information is provided them to enable them to calculate the Council's FRS 17 figures.

In addition a quality assurance exercise should be undertaken on the figures received from the actuaries to ensure that they are reasonable and can be traced back to the source information, where possible.

## Provision for the costs and recognition of income for the Kent Police HQ roof

The Authority provided the design plans for the Kent Police HQ roof. During 2005/06 the Authority contributed to the costs of emergency repairs to the Police HQ building's roof and identified a potential liability for costs of a replacement roof. No provision was made at this stage for the potential cost of replacing the roof as no actual claim had been made against the Authority, liability had yet to be determined and it was not possible to estimate the potential liability at that stage.

There continues to be no provision for the costs to replace the roof in the 2006/07 accounts and there has been no correspondence between the two organisations to progress this issue during the year. However, there has been liaison with the Authority's insurers.

A long term debtor of £417k has been recognised in the 2006/07 accounts to recognise anticipated income against the costs of repairs from an insurance claim. However, although officers are confident that the insurance claim will be paid the insurers have not confirmed this in writing. The legal team responsible for the claim considers that there is still an element of risk that the Authority may not receive the proceeds of this claim. We would advise that the debtor should not be recognised in the accounts as there is still an element of uncertainty that the claim will be settled. Once the letter confirming that the insurers will settle claim has been received then it would be appropriate to recognise the debtor and associated income. This item appears on our unadjusted differences in Appendix B.

**Kent Police HQ roof**

Due to the element of uncertainty still surrounding the insurance claim for £417k, the income and associated debtor should be removed from the 2006/07 financial statements.

When discussions with the insurer are concluded, the authority should enter into discussions with Kent Police Authority to resolve the issue of the repairs required to the police HQ roof. Any costs which are likely to be incurred should be provided for within the budget and medium term financial plan and in turn the financial statements.

## Accounting for PFI Schemes

In the 2005/06 ISA 260 report we noted the complexity of accounting for PFI schemes. We have worked with the Authority over the course of 2006/07 to ensure that the correct accounting treatment has been applied to these schemes in the 2006/07 accounts.

One of the required accounting entries is to build up the estimated residual value of the asset at the end of contract's life, at which point the asset is transferred to the Authority for nil cost. A second is to recognise the value of the assets transferred to the PFI contractor as a prepayment for services to be received over the life of the contract. The estimated values have been arrived at through discussions with the Authority's valuer. However, the values used to calculate the accounting entries differ slightly from those provided by the valuer. The differences have not led to a material error in the accounts and have been included in our Statement of Unadjusted Differences in Appendix B.

### The difference between the Authority's Credit Ceiling and Capital Financing Requirement (Adjustment A)

Upon the implementation of the Prudential Framework in 2003/04, authorities were required to calculate a new measure of their underlying need to borrow, the Capital Financing Requirement (CFR). This replaced the Credit Ceiling (CC) as the key measure of capital indebtedness. However, in order to avoid undue shifts in council tax, authorities are required to calculate their Minimum Revenue Provision (MRP) using the CFR, adjusted for the difference (called Adjustment A) between the CC at 31 March 2004 and the CFR at 1 April 2004.

Because of the importance of the inter-relationship between these two figures, auditors have been asking authorities to review any differences between the two measures and to attempt to reconcile them. There is no necessity that the two figures should be the same (although they should be broadly comparable), and most authorities have found a substantial difference between the two. For the Authority, the difference is £27.8m: £736.1m for the CC and £763.9m for the CFR. We consider that reconciliation of the £27.8m difference is important for two main reasons:

- The difference could indicate errors in the calculation of either or both of the CFR and CC - our work to date has not found any evidence that this is the case.
- The higher CFR could show a need to set aside more resources to cover the underlying borrowing requirement than would be accomplished by an MRP based on the CC - work in this area has been difficult, as some of the effects of the difference appear to date back a considerable number of years for which reliable records are no longer available or require a detailed knowledge of the background to historical accounting entries which has been lost.

The Authority has carried out a substantial amount of work to understand the reasons for the difference, including engaging Butler's, the Authority's Treasury Management Specialists, to review the previous work undertaken to reconcile the CFR to CC to ensure that it is reasonable.

The impact on the accounts would be seen in the MRP. This is calculated based on 4% of the capital financing requirement (less Adjustment A) and results in an adjustment to the Statement of Movement on the General Fund Balance based on the difference between MRP and depreciation. Therefore the difference caused by Adjustment A is a reduction in the MRP of £1.1m.

We are, therefore, satisfied that any adverse impact of the remaining unreconciled difference of £27.8m would not be material for the 2006/07 statement of accounts and that the Authority has met the minimum requirements for making a revenue provision. However, work on reconciling the difference should continue, particularly if new guidance becomes available as a result of national research into the issue, to ensure that the Authority is assured that a material cumulative under-provision will not accrue over future financial years.

### Restructuring of debt

During 2004/05 the Authority restructured its debt financing, and incurred a cost of £2.1 million for the early redemption of the existing loans (a 'premium'). This cost was being spread over the lives of the replacement loans, which average 30 years.

In 2006/07 the replacement loans were themselves replaced with loans of a similar nature and duration. As a result, the premia incurred in 2004/05 continues to be spread over the life of the replacement loans. Whilst this approach can be justified under the current regulations, it now appears likely that the ability to do this in future will cease. It is possible that the cost of any future premia that are incurred on the restructuring of debt will have to be met in full in the year that they are incurred. There could be a requirement for prior period adjustment.

Monitoring the developments and entering into the debate (where possible) will be important to help to ensure that any future decisions on the restructuring of debt also consider the accounting impact (not just the cash position) that may result from the changes in the regulations within this area.

### Accounting for prepayments

Prepayments are calculated monthly so that any element of an invoice for services (eg rentals) relating to March 2007 may have been excluded for accounting purposes and allowed to remain within the prepayment, rather than being separated out as expenditure in the year. This could lead to an understatement of expenditure and overstatement of prepayments, although it is noted that any expenditure misstatement due to incorrect accounting treatment in 2006/07 will be largely off-set by the application of the same policy in 2005/06, leaving only the balance sheet impact.

Through testing of prepayments in the Chief Executive's and the Environment and Regeneration directorates we identified £77,388 of 'prepayment' that was actually 2006/07 expenditure.

As a result of the consistent application year on year and given the relatively small scale of the errors identified to date, we believe that the risk of material misstatement to the accounts as a result of this accounting treatment is likely to be low.

**Prepayments**

The Authority should review its accounting treatment for prepayments and consider whether it would be more appropriate to separate out expenditure relating to the year of account on a daily, rather than a monthly, basis.

## Accounting for debtors and creditors

Internal audit's work on expenditure cut-off identified cut off errors in the internet based procurement system (i-Proc). This system automatically raises creditors based on the date the goods were received. However, in some cases, goods received in 2006/07 were incorrectly shown to be receipted in 2007/08 on the system. This resulted in expenditure relating to 2006/07 being recognised in 2007/08.

For these payments processed on i-Proc creditors amounting to £16,808 were not raised in Adult Services and Childrens, Families and Education. Of this, £11,654 has been taken to the Summary of Unadjusted Differences in Appendix B. The remaining £5,154 is made up of individual debtors that total less than £500. The Authority's policy is that debtors and creditors should only be raised for invoices received post year end amounting to over £500.

This policy is adopted for all elements of spend across the Authority and there is a risk that this method of accounting for debtors and creditors could lead to a more significant understatement of income and expenditure in the accounts.

Officers have estimated that the total unrecognised liability could be anywhere between £20k and £50k. This estimated difference has been taken to the Summary of Unadjusted Differences in Appendix B.

Given the effect on both income and expenditure, and that any misstatement will be off-set to some extent by the same accounting treatment being adopted in 2005/06, and the management estimate above, we have concluded that the risk of material misstatement to the accounts is very low.

**Accounting for debtors and creditors**

The authority should review its accounting policy for raising debtors and creditors and consider whether it would be more appropriate to raise debtors and creditors to recognise all identified items relating to the year of account.

## Sports England debtor

In 2004/05 a debtor of £112k was raised in relation to grant funding owed by Sports England for the sports facility at Tunbridge Wells High School. In the same year, over £1 million income was received from Sport England towards the cost of the new sports facility.

As identified in our 2004/05 Audit Report one of the conditions of the grant funding was that the sports facility should be opened up to public use. Due to delays in meeting this condition of the grant, the outstanding funding has not been received to date and there was also a risk that the funding already received could have to be repaid.

Whilst we note that the school has now been opened for public use following the transfer to a private company, Scencio, the outstanding funding has still not been paid by Sports England.

The Authority should continue to work with the school, Scencio and Sports England to resolve any outstanding issues and secure the outstanding funding for the project.

### Asylum seekers bad debt provision

A debtor totalling £9.7m for claims to the Home Office and the Department for Education and Skills in respect of services provided to Asylum Seekers has been included within the accounts. Of this, £3.2m relates to services provided in 2005/06 and the remainder to services provided in 2006/07. The debtor has been raised by the Children's, Families and Education directorate for the first time in 2006/07, due to responsibilities being transferred from the old Social Services directorate on the restructuring of the Authority.

Bad and doubtful debt provisions of £369k and £700k are included within the Adult and Social Services and Corporate directorates respectively. The provision has not moved since 2005/06. In addition, a 'miscellaneous provision' amounting to £227k remains within the Adult and Social Services directorate.

It is not clear whether the current provisions agree directly to the asylum debtor as at 31 March 2007. There is a risk that the net debtor is over or understated as a result.

**Asylum seekers bad debt provision**

The Authority should review its method for calculating the bad debt provision for the asylum seeker debtor and ensure that any provision is appropriate based on the assessment of recoverability of the outstanding debt.

### Bad and doubtful debt provisions

The Communities directorate has provided £27k for bad and doubtful debts, on a total debtor balance of £4.1 million. This provision was inherited from the Social Services and Strategic Planning directorates when the Authority was restructured on 1st April 2006 and has not moved since the prior year. The debts to which it relates have now been received or written off during 2006/07. This has resulted in a provision remaining for debts that no longer exist.

This has been included within our Statement of Unadjusted Differences in Appendix B.

The directorate has not made any other provision for bad and doubtful debts at year end.

**Bad and doubtful debt provisions**

In the light of the restructuring that took place in 2006/07 the Authority should review its policies for providing for bad and doubtful debts to determine whether these are adequate. Following any revisions the policy should be re-communicated to all directorates to ensure that it is consistently applied. Where directorates feel that they require their own policy for providing bad and doubtful debts this should be fully documented, applied consistently and communicated to the relevant officers.

### Value of landfill allowances

The government allocates each Waste Disposal Authority a quota of landfill allowance permits. Where these are not used, they can be traded with other authorities. This is known as the Landfill Allowance Trading Scheme (LATS).

For the purposes of the accounts, the Authority recognises income and a debtor for the allowances received from DEFRA, and expenditure and a creditor for the allowances it needs to hold in order to cover its landfill usage. The SORP and LAAP Bulletin 64 require landfill allowance permits to be valued at the lower of cost and net realisable value.

The value used in the accounts for allowances was £17.98, being the weighted average value calculated by the Chartered Institute of Public Finance Accountants based on average trading values during the year.

We understand that trades for future allowances i.e. from 2009/10 onwards are occurring at much higher values (£25 to £30 per allowance). However, there is currently a proposed cut off at the end of September 2009 at which point all existing unutilised LATS become unusable and it is therefore doubtful whether there is currently a significant demand for LATS before this cut off date.

Actual sales of allowances at the 2 April 2007 suggest that £5 is a more realistic market value for KCC allowances. Therefore by using the weighted average value for the allowances, rather than the more realistic market value, the net worth of the Authority is potentially overstated by £1.4m. This is held in an earmarked reserve which is not realised until cash is actually received for the proceeds from the sale of these allowances.

The effect of using the different values for allowances has been included in our Summary of Unadjusted Differences in Appendix B.

**LATS Values**

Landfill allowances should be included in the financial statements based on the lower of cost and net realisable value as set out in the SORP and LAAP Bulletin 64.

### Accounting for archives and libraries IT services

Archives and libraries have a contract with BT which provides a managed service for provision and management of IT services to libraries. Contractual change requests are charged in addition to the core services. These cover new items of equipment, such as additional computers and printers, along with maintenance of the existing network. Under the terms of the contract, the cost of change requests can be paid immediately or spread over the life of the contract, in which case it will be subject to inflation. As a result, it was decided within Archives and Libraries that, wherever it is possible to meet these expenses within budget, they would be paid immediately and expensed in the year.

However, the appropriate accounting treatment would be to expense only the elements of change requests relating to maintenance work in the year (£283k in 2006/07). Costs relating to provision of additional equipment (£233k in 2006/07) should be set up as a prepayment and expensed over the life of the remaining contract in recognition of the fact that the equipment is being leased over this period.

Whilst expenditure in any one year will be overstated, through expensing change requests related to IT equipment added in year, this is offset by the understatement of the leasing expense for equipment added through change requests in prior years. Therefore, we have deemed the risk of material misstatement as a result of this incorrect accounting treatment to be low.

**Accounting for archives and libraries IT service**

The directorate finance teams should review any new contractual arrangements, or changes to existing arrangements, to ensure that the accounting treatment adopted is in line with financial reporting standards.

### Shepway collaboration

As noted in our 2005/06 ISA 260 Report, the Landscape Services Division of Commercial Services has been providing services to Shepway District Council since August 2004. Whilst a 'heads of agreement' setting out the broad areas covered by the arrangement was drawn up at the start of the arrangement, no formal service level agreement setting out the detailed service requirement has ever been in place.

In 2006/07, the Authority agreed to the provision of services to the value of £457k in addition to provision of core services of £3,388k. The costs for the additional services were met by the Authority.

We understand that provision of services to Shepway District Council is to be discontinued during 2007/08.

## Pension Fund

### Pension SORP

The current ‘Financial Reports of Pension Schemes Statement of Recommended Practice (Revised 2002)’ (the ‘Pension SORP’) specifies that investments should be shown within the financial statements at mid price (the mid point between bid and offer pricing).

The new SORP 'Financial Reports of Pension Schemes (Revised May 2007)’ is effective for accounting periods commencing on or after 6 April 2007. It will therefore apply to the Kent County Council Superannuation Fund for the year end 31 March 2009 (as the first accounting period commencing after 6 April 2007, is the accounting period commencing 1 April 2008). This SORP changes the investment valuation basis from mid price to bid price, so as to be consistent with the new International Financial Reporting Standards (IFRS).

With the adoption of IFRS, Goldman Sachs have already adopted bid pricing and consequently have been supplying valuations of Investments at bid prices rather than mid prices.

The financial statements of the Kent County Council Superannuation Fund for the financial year ended 31 March 2007 include these investments at bid price, which is not compliant with the SORP that is in operation for that period, although the effect is not material.

**Pension SORP**

The Authority should ensure that their Custodians and investment managers are notified of the need for mid price for financial reporting purposes for the year ended 31 March 2008 and at bid price thereafter.



### Statement of Investment Principles

We reviewed the year end investment holdings in order to consider whether they were in line with the Kent County Council Superannuation Fund Statement of Investment Principles (SIP).

The SIP specifies that the fund should have 15% invested in Fixed Interest Securities. As at 31 March 2007 the actual investment was only 12%. Furthermore, the percentage of asset invested in UK equities stands at 38% where it should be 34.5%.

In June's Superannuation Fund Committee minutes it was noted that the Director of Finance wished to maintain the flexibility of not following the SIP rigidly as it allows pragmatic decisions to be taken rather than locking into a fixed formula. The minutes specify that the allocation decisions will in future be reported to Committee.

**Statement of Investment Principles**

The Statement of Investment Principles should be updated to reflect this change. We would recommend that a tolerance level of flexibility is included to ensure that the investment recommendations which are made by Hymans Robertson are in general still followed.

### Review of Fund Manager/Custodian Internal Control Reports

There are currently no procedures or process in place for KCC to review the Fund Manager's/Custodian's Internal control reports, which are be known as FRAG21, SAS70 or AAF 10/06 reports.

These audit reports are produced annually for Fund Managers and custodians and conclude on the effectiveness of the organisation's controls over third party assets and transactions.

We raised this issue during our interim audit and at the time of our final audit the group accountant had completed the review of the reports and had only noted minor exceptions.

**Review of Fund Manager/Custodian Internal Control Reports**

Going forward Fund Manager's/Custodian's internal control reports should be reviewed by the Authority to identify any exceptions that could place the KCC Superannuation Fund's assets at risk. In the event that exceptions have been identified, management should seek to identify additional assurances or implement additional internal controls within KCC to satisfy itself that the assets of the fund are not at risk.

These reports should also be considered by Officers when preparing the information for Members to support the decision making process when deciding whether or not to appoint Fund Mangers.

### Late payment of contributions

We reported to you in 2004/05 and 2005/06 an issue with respect to the late payment by employers of pension contributions and discussed the ambiguity as to whether this needed to be reported to The Pensions Regulator.

Following our report last year KCC took measures to try and improve the value and occurrences of late payments. The value of late payment of contributions from admitted and scheduled bodies to KCC fell from £8.2m to £3.6m. Whilst the amount still remains high, it is a marked improvement.

These late payments continue to be spread across a number of months and across a number of scheduled and admitted bodies. We noted that there were 30 (down from 42 in 2005/06) bodies who paid their contributions 3 or more times after the due date, with St Simon Stock the worst offender again paying their contributions late on 8 occasions.

As discussed in our ISA 260 "Report to those charged with governance" in 2005/06, KCC would not appear to have an obligation to ensure that these contributions are calculated correctly and paid on time (other than for contributions in respect of its own staff). However, the Authority *may* have a duty to report these breaches of the law under section 70 of the Pensions Act 2004, to the Pension Regulator.

Briefing note No. 2 produced by the Pensions Regulator in May 2005 states that "the Pension Regulator does not expect managers to report every instance where the employer has failed to pay contributions by the due date". It clarifies this by further adding that they would "not normally expect to receive a report of: isolated late payments of contribution where the matter has been put right; or short periods of lateness…"

It goes on to say, however, that "… in some cases, the manager may be concerned that a late payment is symptomatic of more serious or widespread problems relating to the employer which may require the attention of the regulator. Where a late payment raised concerns about the conduct of the employer, we would like to receive a report".

Therefore, the Authority may therefore wish to consider, for those bodies that have persistently paid late, whether this is symptomatic of a more serious problem and whether it can do more to encourage timely payment.

## Annual Returns

In our ISA 260 "Report to those charged with governance" in 2005/06, we noted that, at the time of our audit, KCC had not received all the annual return forms from the admitted and scheduled bodies despite the deadline for the return of these forms being the 30 April. This continues to be a problem.

The annual returns are used, amongst other things, to check that all contributions have been received.

At the time of our audit the final figure had not been calculated and we were unable to agree the total contributions received figure (as per the annual returns) to the financial statements.

However, we were able to agree the figure for contributions within financial statements to the general ledger. As the general ledger has been reconciled to the bank statement, we are confident that all contributions received into the bank account of the Authority have been accounted for. The area of risk lies with contributions that are receivable but that have not been received into the Authority's bank account.

Given that these contributions were due by the 19th April, we consider this risk to be low.

## Other Best Practice Issues

In addition to the Pension Fund accounts as included in the Authority's Statement of Accounts, we also produce a separate opinion for the Pension Fund accounts as contained within the Kent County Council Superannuation Fund Annual Report. For that reason, we also produce an ISA260 report for the Superannuation Fund Committee.

In addition to the items relating to the Pension Fund that are set out above, our ISA260 report for the Superannuation Fund Committee will also discuss in detail the following items which relate to best practice:

- Banking arrangements for the Pension Fund; and
- The timing of special contributions for early retirements

## Unadjusted differences

We are required to report to you all unadjusted differences which we have identified during the course of our audit, other than those of a trivial nature. These misstatements are set out in Appendix B to this report.

## Elector's questions

We have received several Electors' Questions since the presentation of our 2005/06 ISA 260 Report. The areas on which we have received questions are:

- The Chief Executive's pay;
- Manston Airport;
- The Authority's investment in the Manston to Virginia flight service; and
- The cancellation of the recycling service in Cherry Lane.

Several of the issues raised have been included in our audit programme and are reported elsewhere in this letter, where appropriate.

We received a specific question on the value for money of the Chief Executive's pay. Both the Chief Executive's contract award and that of another Chief Officer had been approved by the Personnel Committee, which had considered the contracts, remuneration and allowances awarded. The Director of HR had also been closely involved and had taken legal and other advice.

Nonetheless we have two points to raise. Firstly, absolute commitments were given to the payments of allowances at the end of the contracts. As the commitments were contractual and not contingent, they should have been accrued for at the point of award. An adjustment to the accounts was made so that these costs are now provided for.

As the trigger for the payments is departure, it is not in our view appropriate to record these as remuneration of the current year in the banding table within the accounts and therefore the current disclosures are correct. The allowances will need to be reported in this table in the year in which they become payable, i.e. the year of departure. We also considered whether the new contractual terms should be reported as Related Party transactions, but concluded that this was not required as the transactions are wholly between the Authority and its employees.

Secondly, we considered the nature of the allowances agreed, which were classed in both cases as recruitment and retention payments and a value for money assessment was performed and documented in one case. Typically such an allowance would be pensionable and therefore it is important that the exception (because it had been agreed in these cases that the nature of the payments meant that this would not be appropriate) was properly documented to prevent subsequent confusion or error. The documentation has not made this clear and we recommend that this point is clarified with the beneficiaries at the earliest opportunity. The Director of HR has undertaken to do this immediately and does not anticipate any difficulty in receiving confirmation.

## Financial standing

During 2006/07 the Authority under-spent by £7,740k (excluding the delegated schools budget and the unallocated dedicated schools grant) at portfolio level, most of which was due to the re-phasing of revenue funded projects. The main areas of this under-spend were:

- Education and School Improvement – £2,342k
- Environment Highways and Waste - £2,386k
- Finance - £6,535k

This is the second year that the Authority has reported a significant underspend at portfolio level (2005/06: £8,957k).

The reserves balances as at 31 March 2007 were:

- General Fund - £25,835k (£25,835k in 2005/06)
- Earmarked Capital Reserve - £26,698k (£24,884k in 2005/06)

- Earmarked Revenue Reserves - £81,181k (£74,094k in 2005/06)

Schools' reserves were £67,639k as at 31 March 2007, an increase of £2,013k (3%) on 2005/06.

The Authority therefore scores well for financial standing in our CPA assessment.

## Capital budget outturn

Capital outturn for 2006/07 was £237,059k, £39,092k of which was delegated to schools and £5,834k to the Property Enterprise Fund. The total capital budget for the year was £251,896k, although final approval to spend is only given when the project is approved. There was therefore re-phasing of £14,837k into future years.

The Property Enterprise Fund was established in 2006/07 with the aim of maximising the value of the Authority's land and property portfolio. To achieve this, capital receipts from the disposal of non operational property will be reinvested into assets with higher growth potential and also via the strategic acquisition of land and property to add value to the Authority's portfolio. The Fund received an approval to operate a £10m temporary borrowing facility. In 2006/07, £2.714m of temporary borrowing was utilised to finance the activities of the Fund.

Capital outturn can be split across portfolios as shown below.

| Portfolio | £000's |
|---|---|
| Education and Schools Improvement | 97,771 |
| Children and Family Services | 3,354 |
| Adult Social Services | 10,719 |
| Environment, Highways and Waste | 37,747 |
| Regeneration and Supporting Independence | 24,490 |
| Communities | 8,941 |
| Corporate Support and Health | 2,332 |
| Policy and Performance | 470 |
| Finance | 6,309 |
| **Total (excluding schools)** | **192,133** |
| Capital devolved to Schools | 39,092 |
| **Total** | **231,225** |
| Property Enterprise Fund | 5,834 |
| **Total including PEF** | **237,059** |

## Trading operations

Trading operations have, for the most part, performed well during the year. A total operational surplus of £4,693k was achieved, a 29% increase on 2005/06. Surpluses were achieved by all but 2 of the 11 trading operations, with County Print and Passenger Services reporting small deficits of £48k and £29k respectively.

The directorate's turnover has expanded by 15% during the year to 2006/07, with the majority of this increase being attributable to the LASER business unit. The profit achieved on the LASER turnover in 2006/07 was £1.4m, The working capital position for the Commercial Services directorate has worsened during the course of 2006/07. Debtors in the Sales Ledger Control Account have increased by 32% to £29.7m, compared with only an 11% increase in creditors in the Purchase Ledger Control Account to £11m. The directorate's overdraft has increased by 83% to £7.8m.

This worsening of the working capital position is mainly attributed to delays in the receipt of invoices from energy suppliers within the LASER trading operation, which means that billing of customers by KCC is in turn delayed. This situation has been exacerbated in 2006/07 as a result of mergers of suppliers which led to further delays in the Authority receiving invoices. There has been no significant increase in the provision for bad and doubtful debts within LASER, as the majority of the debtors are less than 6 months old (£21.2 million of the total LASER debtor of £21.6m), attracting a 0% provision in line with the directorate's bad debt policy.

Although as a division of the Authority there is not a going concern risk regarding Commercial Services, there is a risk that the Division may require additional working capital from central Finance.

We have also noted that the dividend which the directorate is expected to achieve and contribute to the Authority in future years continues to rise and the directorate remains under pressure to exceed these dividends to generate excess profit to invest in capital projects or to enable it to make investments in new or existing operations.

The amount of income received by the Authority from Commercial Services is small compared to the total income receivable by the Authority. However, there is a risk that the Authority is relying upon these trading dividends to fund future activities and that, if Commercial Services are unable to meet the dividend, a funding gap, albeit potentially small, may appear in the Authority's budget.

**Working capital position and dividend payment**

We understand that the directorate has been reviewing the situation to identify possible solutions to ease the problems with cash flow. This review should be continued, and extended to identify whether all business units are sustainable in the long term, that the risk profile of the business units continue to be acceptable to the authority and whether the financial structure of the division is appropriate to support future plans.

In addition the Authority should continue to closely monitor the financial position of Commercial Services to ensure that dividends are achievable.

The Authority currently only discloses activities undertaken by its Commercial Services directorate as trading operations within the financial statements. However, the Authority also undertakes a number of other activities that meet the CIPFA definition of a trading activity. These include:

- Oakwood House;
- Personnel and Development services;
- Legal Services; and
- Schools Support Services.

The SORP gives the Authority discretion on what it discloses as a trading operation in the financial statements. However, as suggested in our 2005/06 ISA 260 Report, consideration should be given to disclosing some or all of the above in the financial statements as trading operations.

## Financial outlook for 2007/08

Gross expenditure of £2,115m has been budgeted in 2007/08 (£1,987m in 2006/07). The main causes of this rise are:

- Pay and price increases - £27.7m
- Government/legislative pressures - £4.6m

- Demand-led pressures & delivering “Towards 2010” targets - £17.4m
- Delegated schools budget - £33.8m
- Service strategies and improvements - £24.4m

Within the 2007/08 budget there are proposed savings and additional income of £41.8m along with an increase in the dedicated schools budget of £38.8m.The above increases in costs have required a council tax increase of 4.95%.

## Internal audit

We have maintained a good working relationship with Kent Audit (the Authority's internal audit service) during 2006/07.

As part of our wider assessment of the Authority's control environment we are required to review the internal audit arrangements. We have reviewed the 2006/07 Internal Audit plan and, where applicable to our audit approach, individual audit reports.

We have been able to place reliance on the work performed by Kent Audit in areas of our financial statements audit. This enables us to perform a more focused audit in higher risk areas and to minimise any risk of duplication of work.

## Systems of internal control

We are required to report to you any material weaknesses in the accounting and internal control systems identified during the audit. At the time of writing this report the most significant weaknesses in the internal control systems that we wish to bring the attention of members are set out below.

### Communities budget monitoring

Communities was a new directorate created during the restructuring. Communities has had a number of new staff appointed to senior positions and the new systems and processes have taken time to bed in. Of the 20 units within the Communities directorate, 5 have not supplied budget monitoring returns since the restructuring on 1 April 2006. As a result, under or over spends on budget may not be identified and appropriate action may not be taken to address adverse variances.

### Monitoring of IT network activity

There is limited evidence of proactive and formal monitoring of IT network activity, powerful access to, and changes to, the IT environment. There is, therefore, a risk that unauthorised or unusual activity will not be detected promptly.

### Review of IT segregation of duties

There has been no periodic review of the segregation of duties for users of the IT network to ensure that access to sensitive or conflicting functions has been prevented. This may provide an opportunity for fraud or misuse that could be prevented.

## Standards of Financial Conduct and the Prevention and Detection of Fraud and Corruption

At the time of writing this report we have reviewed the reports produced by Internal Audit for the Governance and Audit Committee on cases of fraud and irregularity that they have investigated. There have been no other matters raised in this area in the period.

## The Legality of Financial Transactions

At the time of writing this report and with the exception of matters raised with us by electors, and those which we have discussed with officers, there have been no matters raised in this area in the period.

# Use of Resources

## Work performed

In accordance with the Code of Audit Practice, we have performed work to conclude on the Authority's arrangements for achieving economy, efficiency and effectiveness in its use of resources. Our work to support our conclusion comprised the following elements:

- Use of Resources assessment for CPA:
  - Financial Reporting
  - Financial Management
  - Financial Standing
  - Internal Control
  - Value for Money
- Mandatory Data Quality Review work
- Review of the Statement on Internal control
- Audit of the Best Value Performance Plan (the Authority's Annual Plan).



### Use of Resources Opinion

Under the Code of Audit Practice we are required to provide a conclusion on the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources. This conclusion is reached by assessing the Authority's arrangements against a set of criteria issued by the Audit Commission. Our conclusion is based on the use of resources assessment undertaken in October 2007 as part of the CPA process and updated as necessary, our Local Government data quality work, and other information that came to our attention during the course of our audit work.

At the time of writing this report, we intend to issue an unqualified use of resources conclusion.

### Use of Resources Assessment

During 2006/07 we have completed the annual Use of Resources assessment for the Authority. This assessment was submitted to the Audit Commission and formed part of the overall CPA assessment. This assessment covers five key areas:

- Financial reporting;
- Financial management;
- Financial standing;
- Internal control; and

- Value for money.

Overall the Authority achieved a level 4 score. This was an excellent result and officers should be congratulated for their efforts in achieving this score.

The score is broken down into the following scores for each Use of Resources area as follows:

- Financial reporting - 4
- Financial management - 4
- Financial standing - 4
- Internal control - 3
- Value for money – 4

### Targeted work

During 2006/07 we have also undertaken or have commenced several pieces of targeted performance work. These include:

- A review of Highways Management;
- A Value for Money (VfM) review of the Schools Clusters Arrangement;
- A VfM review of Libraries;
- A VfM review of Waste Management;
- A VfM review of Learning Disabilities Day Care;
- Review of Carbon Management Policies; and
- The provision of risk management training.

The results of the VfM review of Schools Clusters Arrangements have been reported to Members at a previous Governance and Audit Committee meeting. The remaining reviews are still in progress and the findings from these reviews will be reported to Members or Management, as appropriate.

### Data Quality work

At the time of writing we have completed Stage 1 of the Data Quality work. We have not identified any issues from the completion of this work and the Authority has met the minimum requirements as set out by the Audit Commission's criteria.

The outcomes of this work will be used in Stages 2 and 3 of the Data Quality work to take place over the summer of 2007.

### Statement on Internal Control

Local Authorities are required to produce a Statement on Internal Control (SIC) which is consistent with guidance issued by CIPFA / SOLACE. The SIC was included in the financial statements.

We reviewed the SIC to consider whether it complied with the CIPFA / SOLACE guidance and whether it is misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

### Best Value Performance Plan

Our work on the 2006/07 Best Value Performance Plan (BVPP), issued by the Authority in June 2006. Our audit report on the BVPP was issued in December 2006 and concluded that the Best Value Plan was prepared in accordance with section 7 of the Local Government Act 1999 and the Audit Commission's statutory Code of Audit Practice. The work on the 2007/08 BVPP forms part of the 2007/08 audit to be undertaken by the Audit Commission as part of their 2007/08 Audit Plan.

# Audit plans and fee update



### Audit Plan 2006/07

We issued our Audit Plan for 2006/07 and presented it to Members on 30 June 2006.

We have performed appropriate reporting procedures for each of the risks identified in our Audit Plan of 2006/07. In this report we comment only on those areas where we believe we need to communicate with those charged with governance.

### Audit fees update for 2006/07

We reported our fee proposals as part of the Audit Plan for 2006/07.

Our actual fees are expected to be in line with our proposals.

Our fees charged were:

| | 2006/07 Outturn | 2006/07 Fee proposal |
|---|---:|---:|
| Accounts | £253,511 | £253,098 |
| Use of Resources | £125,440 | £125,440 |
| Targeted Audit Work | £194,340 | £0 |
| **Total** | **£573,291** | **£378,538** |

The increase shown in the 2006/07 outturn column was caused by the following:

- An additional £413 was incurred as a result of undertaking the audit of the Authority's FRS 17 figures as part of the Audit Commission's FRS 17 protocol; and
- An additional £194,340 of targeted performance work was agreed following the finalisation of the original 2006/07 Joint Audit and Inspection Plan.

The fees set out above do not include an amount of approximately £12,000 charged by the Audit Commission's Relationship Manager.

In addition, we performed work which fell outside of the Code of Audit Practice relating to a review of Passenger Services. Our fee for this work was £24,134.

# Appendix A: 2006/07 targeted audit work

Below we set out the status of the targeted audit work that we have completed or are currently completing as part of 2006/07 audit plan:

- Value for Money (VfM) review of the Schools Clusters Arrangement – Report has been issued as final and presented to members.
- The provision of risk management training – No report is to be issued as part of this work.
- Review of Highways Management – Report has been issued as final to management.
- VfM review of Libraries – Report is in draft format and is with management for their responses.
- A VfM review of Waste Management - Report is in draft format and is with management for their responses.
- A VfM review of Learning Disabilities Day Care – Fieldwork is well advanced.
- Review of Carbon Management Policies – Fieldwork is in progress.

# Appendix B: Summary of unadjusted differences

We have identified the following errors during our audit of the financial statements that have not been adjusted by management.  The Audit Committee are requested formally to consider the listed unadjusted errors and determine whether the accounts should be amended. If the errors are not adjusted we will require a written representation from you explaining your reasons for not making the adjustments.

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **CORPORATE SERVICES** | | | | |
| **Prepayments** – Charges for the final week in March and quarter 1 for various properties rented by the Chief Executive's directorate have all been accounted for as a prepayment.<br><br>The rent for the last week of March should actually be accounted for as 2006/07 expenditure. | Rent Expenditure<br>£76,572 | | | Prepayments<br>£76,572 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **Debtors** - A debtor has been set up for re-claiming of damages paid by KCC on a property at Foster Street. Whilst evidence from the external lawyer has suggested the money will be reclaimed, the time elapsed since the damages were initially paid (in 04/05) does create an element of doubt. However, no bad debt provision has been set up against this debt. The adjustment assumes a 100% specific provision against this debt. | Bad and Doubtful debt expense<br>£71,230 | | | Bad and doubtful debt provision<br>£71,230 |
| **Long term debtor for the police HQ roof** - In 2005/06 KCC included expenditure in their accounts for the costs of emergency repairs to the Kent Police HQ roof. As the building originally belonged to KCC and was designed with KCC input, it was argued they were liable for repairs.<br>The insurance claim in respect of this expenditure is included as a debtor in the 2006/07 accounts. However, as no confirmation has been received from the insurers that this will be paid, the reimbursement is not 'virtually certain' and should not be | Corporate Services Income<br>£ 417,379 | | | Long term debtors<br>£ 417,379 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| recognised as a debtor. | | | | |
| **Prepayment recognised for the '6 Schools' PFI -** A prepayment is recognised in the accounts in respect of buildings which are transferred to PFI contractors. This is to recognise the fact that the Authority continues to receive benefit from these buildings and is written down over the life of the contract.<br><br>Prepayments have been set up for the North School and Holmesdale school in 2006/07. As elements of the buildings transferred have been demolished, prepayments have only been recognised for those elements which continue to be in use. The initial prepayment calculated was based on the best information available at the time. However, subsequent information on which buildings have been retained shows that the £6.4m prepayment recognised was overstated by £49,771.<br><br>The write down of the | Statement of movement on the General Fund £32,003 | Expenditure £32,003 | I & E – Gain on disposal £49,771<br><br>Prepayment £32,003 | Prepayment £49,771<br><br>CFA £32,003 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| prepayment has also been overstated, by £32,003. | | | | |
| **Build up of the residual value of Westview and Westbrook PFI** - The residual value of PFI projects which will transfer to the Authority for nil consideration at the end of the contract is built up annually as a prepayment in the accounts, based on the valuation of the buildings at the balance sheet date.<br><br>The build up for only one of the two projects was initially recognised in the accounts, understating the prepayment. However, the prepayment recognised for this project was overstated as it initially included the valuation of the land. This should be excluded as land remains the property of the Authority. The net understatement of the asset was £20,370. | Statement of Movement in the General Fund balance £20,370 | Income £20,370 | Prepayment £20,370 | CFA £20,370 |
| **Assets under construction -** Capital expenditure during 2006/07 on an asset which is already operational has been incorrectly classified as assets under construction. | | | Fixed Assets - Land and Buildings £15,563 | Fixed assets - AUC £15,563 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **CHIEF EXECUTIVE'S** | | | | |
| **Debtors -** The Chief Executive's directorate are recognising a debtor for £102k in respect of overpayments to employees when the payroll was outsourced to Capita. £60k of the debtor relates to overpayments incurred prior to May 2005. As a result, the Authority does not believe that it will be able to recover the overpayments from the individuals involved.<br><br>The debtor was included as the Authority initially hoped to recover the debt from Capita. It is now thought to be increasingly unlikely that this debt will be recovered. Therefore, it is considered prudent to provide for this at 100%, until the issue is resolved | Bad and doubtful debt expense<br>£72,000 | | | Bad and doubtful debt provision<br>£72,000 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **COMMERCIAL SERVICES** | | | | |
| **Adequacy of Doubtful Debts provision -** A specific provision of £6k has been made 'in full' for 3 debts totalling £7,166. The provision should, therefore be increased by the difference. | Bad and doubtful debt expense £1,166 | | | Bad and Doubtful Debts provision £1,166 |
| **Miscellaneous provision for excess mileage** - This provision relates to excess mileage on vehicles transferred from Corporate Services in 2004/05. Given that the charge is not expected to be levied until the vehicles are returned, the entire provision is being held for 6 years following the date of transfer.<br><br>The total estimated cost of the excess mileage at the time of the transfer was £153,360. However, a provision for £175k is included in the accounts. The difference between the estimated cost and the actual provision should be written back. | | Commercial services income<br><br>£21,640 | Miscellaneous provisions<br><br>£21,640 | |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **ENVIRONMENT AND REGENERATION** | | | | |
| **Creditors** - A capital creditor for Ringway infrastructure services was set up at year end. It was subsequently realised that this creditor should not have been set up. | | Expenditure £20,237 | Creditors £20,237 | |
| **Creditors -** A prepayment for the lease of land was wholly attributed to 2007/08. 6 of the 91 days included in this rental period are in 2006/07 and should be expensed in year. | Expenditure £817 | | | Prepayment £817 |
| **Accounting for Landfill Allowance Trading Scheme –** Landfill allowances are valued at £17.98, being the weighted average value as at 31 March 2007, as advised by CIPFA. Post year end sales of the landfill allowances suggest that £5 is a more realistic market value for the allowances. | Income £5,293,789 | Expenditure £3,897,634 | Creditors £3,897,634 | Debtors £5,293,789 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **COMMUNITIES** | | | | |
| **Income** - Two post year end income receipts (amounting to £7,156 & £960) relating to 2006/07 have not been included as year end debtors. | | Income £8,116 | Debtors £8,116 | |
| **Reversal of bad debt provision** – A bad debt provision relating to 2005/06 has still been included in the financial statements even though the debt has been collected or written off. | Debtors £27,000 | | | Communities Income £27,000 |
| **Creditors** - A £35,000 creditor was raised in respect of a new joint post of Website Officer to be shared with Kent Police. The officer has yet to be appointed, so the associated expenditure represents a roll forward of budget rather than a true year end creditor. | | Expenditure £35,000 | Creditor £35,000 | |
| **CHILDREN'S, FAMILIES AND EDUCATION** | | | | |
| **Creditors -** During the year, KCC undertook a project in partnership with the Vulnerable Young Person Support Group (VYPSG). It was thought that a grant | | Expenditure £35,000 | Creditors £35,000 | |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| received by the two bodies had funded 2 members of staff in the year, with only one actually being paid for in year (at a cost of £35k). Therefore, an accrual was set up for the second member of staff. On further investigation, it was found that only one member of staff was grant funded. | | | | |
| **Creditors -** A creditor has been set up for Swalcliffe Park School Trust's Spring term fees. These were actually paid on 16/03/07. | | Expenditure<br>£10,495 | Creditors<br>£10,495 | |
| **Expenditure cut-off -** Internal audit's work around expenditure cut-off identified cut off errors in the i-Proc system due to human error, with 2006/07 expenditure being expensed in 2007/08. The errors identified within the CFE directorate have not been corrected. | Expenditure<br>£3,414 | | | Creditors<br>£3,414 |
| **Accounting treatment for the School Loans Scheme -** Loans are made to schools by the Authority to assist them with capital projects or with cash flow difficulties. In school accounts the loan is recognised as a creditor. However, the loan is not | | | **2006/07**<br>Debtors<br>£1,706,000<br><br>**2005/06**<br>£2,906,000 | **2006/07**<br>Reserves<br>£1,706,000<br><br>**2005/06**<br>£2,906,000 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| recognised as a debtor for the Authority so that the two entries do not cancel on consolidation of the accounts. Rather, it is taken straight to the school's reserve.<br><br>This incorrectly reduces the net worth of the Authority in the accounts and, as such, is shown as a movement in the Statement of Total Recognised Gains and Losses. | | | | |
| **ADULT AND SOCIAL SERVICES** | | | | |
| **Expenditure cut-off -** Internal audit's work around expenditure cut-off identified cut off errors in the i-Proc system due to human error, with 2006/07 expenditure being expensed in 2007/08. The errors identified within the Adult and Social Services directorate have not been corrected. | Expenditure £8,240 | | | Creditors £8,240 |

| Unadjusted Misstatement | Income and Expenditure Account | | Balance Sheet | |
|---|---|---|---|---|
| | Dr | Cr | Dr | Cr |
| **Income cut-off -** A post year end income receipt (amounting to £9,900) relating to 2006/07 has not been included as a year end debtor. | | Income<br>£9,900 | Debtor<br>£9,900 | |
| **Net effect** | **£6,023,980** | **£4,090,395** | **£8,767,729** | **£10,701,314** |

# Appendix C: Use of Resources conclusion

The Audit Commission has published 12 Code of Practice criteria on which auditors will be required to reach a conclusion on the adequacy of an audited body's arrangements for economy, efficiency and effectiveness in its Use of Resources.

These code criteria are linked to the CPA and Data Quality Review Key Lines of Enquiry (KLoEs). A score of Level 2 or higher under the KLoEs will result in an assessment of adequate for the purposes of the Code criteria. The Code criteria and the linked KLoEs are shown in the table below:

| Code Criteria | Description | Associated KLoE | CPA Score | Use of Resources Conclusion |
|---|---|---|---|---|
| 1 | The body has put in place arrangements for setting, reviewing and implementing its strategic and operational objectives. | N/A | N/A | Adequate |
| 2 | The body has put in place channels of communication with service users and other stakeholders including partners, and there are monitoring arrangements to ensure that key messages about services are taken into account. | N/A | N/A | Adequate |
| 3 | The body has put in place arrangements for monitoring and scrutiny of performance, to identify potential variances against strategic objectives, standards and targets, for taking action where necessary, and reporting to members. | N/A | N/A | Adequate |
| 4 | The body has put in place arrangements to monitor the quality of its published performance information, and to report the results to members. | LG DQ Stage 1 | Level 3 | Adequate |
| 5 | The body has put in place arrangements to maintain a sound system of internal control | 4.2 | 3 | Adequate |

| Code Criteria | Description | Associated KLoE | CPA Score | Use of Resources Conclusion |
|---|---|---|---|---|
| 6 | The body has put in place arrangements to manage its significant business risks. | 4.1 | 3 | Adequate |
| 7 | The body has put in place arrangements to manage and improve value for money. | 5.2 | 3 | Adequate |
| 8 | The body has put in place a medium-term financial strategy, budgets and a capital programme that are soundly based and designed to deliver its strategic priorities. | 2.1 | 4 | Adequate |
| 9 | The body has put in place arrangements to ensure that its spending matches its available resources. | 3.1 | 4 | Adequate |
| 10 | The body has put in place arrangements for managing performance against budgets. | 2.2 | 4 | Adequate |
| 11 | The body has put in place arrangements for the management of its asset base. | 2.3 | 3 | Adequate |
| 12 | The body has put in place arrangements that are designed to promote and ensure probity and propriety in the conduct of its business. | 4.3 | 4 | Adequate |

# Appendix D: Summary of recommendations contained in this letter

| Page | Recommendation | Management Response | Target Implementation Date |
|---|---|---|---|
| 8 | **Pension liabilities**<br><br>We recommend that the Authority carries out a thorough investigation of pension fund information supplied to the actuaries to ensure that it is meeting its obligation to supply its actuaries with full details of its pension obligations. | The accounting team will obtain assurance from the pensions section on the completeness of the data provided to the actuary and will then check the value of unfunded liabilities on the actuary's report to actual payments made in addition to the checks that are already made. | December 2007 |
| 8 | **Kent Police HQ roof**<br><br>Due to the uncertainty surrounding the insurance claim for £417k, the income and associated debtor should be removed from the 2006/07 financial statements.<br><br>When discussions with the insurer are concluded, the Authority should enter into discussions with Kent Police Authority to resolve the issue. Any costs which are likely to be incurred should be provided for within the budget and medium term financial plan and in turn the financial statements. | The discussions with the insurer have been very positive and we are confident that the claim will be paid. | To resolve by 30 November 2007 |
| 10 | **Prepayments**<br><br>The Authority should review its accounting treatment for prepayments and consider whether it would be more appropriate to separate out expenditure relating to the year of account on a daily, rather than a monthly, basis. | We will consider this, but in doing so will also consider value for money in additional work required and also the materiality. | Review by end November 2007 |

| Page | Recommendation | Management Response | Target Implementation Date |
|---|---|---|---|
| 10 | **Accounting for debtors and creditors**<br>The Authority should review its accounting policy for raising debtors and creditors and consider whether it would be more appropriate to raise debtors and creditors to recognise all identified items relating to the year of account. | Unlikely that this will change as the de minimus is a guideline only. From investigations relating to 06/07 assuming 50% of invoices under £500 paid in the new year with an old year invoice date didn't have a creditor raised, the impact was approximately £24k. | N/a |
| 11 | **Asylum Seeker bad debt provision**<br>The Authority should review its method for calculating the bad debt provision for the asylum debtor and ensure that any provision is appropriate based on the assessment of recoverability of the outstanding debt. | It is difficult to judge an appropriate level of provision when govt. are lax in publishing grant rules, their audits lag so far behind the year in question (only just done 2005-06) and trying to secure the funding requires a vigorous and lengthy process of lobbying. However, we will review the method taking into account the issues identified above. | March 2008 |
| 11 | **Bad and doubtful debt provisions**<br>The Authority should review its policies for providing for bad and doubtful debts to determine whether these are adequate. The policy should be communicated to all directorates to ensure that it is consistently applied. Where directorates feel that they require their own policy for providing bad and doubtful debts this should be fully documented, applied consistently and communicated to the relevant officers. | This will be reviewed in light of the restructure where new directorates may need to have more than one policy. | End November 2007 |
| 12 | **LATS Values**<br>Landfill allowances should be included in the financial statements based on the lower of cost or net realisable value as set out in the SORP and LAAP Bulletin 64. | We will consider for 07/08 accounts. Our reasoning around including at DEFRA prices in 06/07 was the comparatives across different authorities and we have evidence that others have used the same figures. | March 2008 |
| 12 | **Accounting for archives and libraries IT service**<br>The directorate finance teams should review any new contractual arrangements, or changes to existing arrangements, to ensure | Agreed | December 2007 |

| Page | Recommendation | Management Response | Target Implementation Date |
|---|---|---|---|
| | that the accounting treatment adopted is in line with financial reporting standards. | | |
| 12 | **Pension SORP**<br><br>The Authority should ensure that their Custodians and investment managers are notified of the need for mid price for financial reporting purposes for the year ended 31 March 2008 and at bid price thereafter. | The change required to bid price for the 2008-09 accounts is acknowledged. We will request that Goldman Sachs Asset management return to mid pricing. | August 2007 |
| 12 | **Statement of Investment Principals**<br><br>The Statement of Investment Principals should be updated to reflect this change. We would recommend that a tolerance level of flexibility is included to ensure that the investment recommendations which are made by Hymans Robertson are in general still followed. | The SIP will be updated and submitted to the Superannuation Fund Committee to specify tolerance levels around the allocations to specific asset classes. | September 2007 |
| 13 | **Review of Fund Manager/Custodian Internal Control Reports**<br><br>Going forward Fund Manager's/Custodian's internal control reports should be reviewed by the Authority to identify any exceptions that could place the KCC Superannuation Fund's assets at risk. In the event that exceptions have been identified, management should seek to identify additional assurances or internal controls within KCC to satisfy itself that the assets of the fund are not at risk.<br><br>These reports should also form part of the decision making process by Members when deciding whether or not to appoint Fund Mangers. | The reports for existing managers are reviewed. Officers will ensure that when we are tendering for new managers their internal control processes are included in the Officers evaluation. | August 2007 |

| Page | Recommendation | Management Response | Target Implementation Date |
|---|---|---|---|
| 17 | **Working capital position and dividend payment**<br><br>We understand that the directorate has been reviewing the situation to identify possible solutions to ease the problems with cash flow. This review should be continued, and extended to identify whether all business units are sustainable in the long term, that the risk profile of the business units continue to be acceptable to the Authority and whether the financial structure of the division is appropriate to support future plans.<br><br>In addition the Authority should continue to closely monitor the financial position of Commercial Services to ensure that dividends are achievable. | Cash flow pressures were largely caused by exceptional energy billing circumstances within LASER towards the end of the financial year. These have now been remedied and are un-likely to re-occur. Other possible improvements have been identified from the review already undertaken.<br><br>Recognition of the risks, potential and viability for all units has been incorporated into their 2007/08 budgets and longer-term financial projections.<br><br>Rigorous monthly monitoring of the performance of each unit has always and continues to be undertaken to ensure that the year on year increased levels of dividend can be achieved. | Ongoing |

| | | |
|---|---|---|
| By: | Director of Finance | **Item 9** |
| To: | Governance & Audit Committee – 19 September 2007 | |
| Subject: | DEBT RECOVERY | |
| File Ref: | | |

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Summary: To report on the Council's debt recovery position.

FOR INFORMATION

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**INTRODUCTION**

1. The purpose of this report is to provide Audit and Governance Committee with a summary of the Council's outstanding debt position i.e. amounts owed to the Council related to the provision of our services.

2. The report will be issued on a 6 monthly basis and will provide a comparison of the current outstanding debtor levels with that of the previous year.

**DEBT MANAGEMENT POLICY**

3. A council wide debt management policy was introduced in April 2004 and was agreed by the Chief Officers Group (COG). The policy was revised in November 2006. The objective of the policy is to set best practice with consistent and effective processes for the maximisation of income and the management of the Council's debtors.

4. Given the nature of their debt, Adult Services have their own debt management policy for care related debt, which is currently under review.

**MANAGEMENT SUMMARY**

5. The overall outstanding debtor position as at 31 July 2007 is £28,176,650.

   Throughout this report Chief Executive (CED) will include the old Corporate debt, CFE will include the old Education debt, Adult Services (AS) will include the old Social Services debt and E&R will include the old Strategic Planning debt. We are unable to retrospectively amend our financial system to reflect the new directorate structure. Please also note that the debt reporting is calculated from the invoice due date and not the invoice date.

The following table is an analysis of the summary position for 31 July 2007 in comparison to 31 July 2006. The figures are inclusive of secured debt.

| Directorate | Total Debt 31/07/07 | Total Debt 31/07/06 | % Change | Under 60 Days 31/07/07 | Under 60 Days 31/07/06 | % Change | Over 6 Months 31/07/07 | Over 6 Months 31/07/06 | % Change |
|---|---|---|---|---|---|---|---|---|---|
| CED | 5,891,398 | 3,902,164 | +51 | 5,779,102 | 3,761,664 | +53 | 24,437 | 101,438 | -75 |
| CFE | 2,309,578 | 4,544,659 | -49 | 1,660,350 | 3,107,563 | -46 | 386,219 | 389,171 | -1 |
| AS | 16,215,729 | 18,091,045 | -10 | 7,418,074 | 7,188,434 | +3 | 6,384,573 | 7,011,432 | -9 |
| E&R | 2,805,775 | 5,905,571 | -52 | 1,679,543 | 3,584,004 | -53 | 584,721 | 1,215,018 | -52 |
| Communities | 954,170 | 513,282 | +86 | 855,711 | 508,934 | +68 | 7,734 | 0 | - |
| **Total** | **28,176,650** | **32,956,721** | **-15** | **17,392,780** | **18,150,599** | **-4** | **7,387,684** | **8,717,059** | **-15** |

Note – In the last year the total debt and the debt levels over 6 months of age have both reduced by 15%

## SECURED DEBT

6. Legislation permits the Council to secure debts by obtaining a legal charge against an individual's property, having a legal charge in place does protect the Council's position. However, in the majority of cases it is some considerable time before the legal charge is redeemed and the outstanding debt is repaid. This usually occurs after a service user is deceased.

7. The table below details our secured debt position as at 31 July 2007 in comparison to 31 July 2006.

| Period | Secured Amount | Period | Secured Amount |
|---|---|---|---|
| 31/07/07 | 3,322,727 | 31/07/06 | 3,171,239 |

This means that 11.79% of the Council's overall debt at 31 July 2007, is secured.

## DEBT RECOVERY PERFORMANCE INDICATORS

8. There are two corporate performance indicators that the Debt Recovery team aims to achieve. The performance indicators are based on a percentage of the total outstanding debt rather than on the value of the outstanding debt. This provides a more meaningful indication of how effective debt recovery action, by the team, is.

   - Total outstanding debt less than 60 days old – target 60% or more.
   - Total outstanding debt over 6 months old – target 20% or less.

   The percentage excludes secured debt.

9. The performance outcomes for 31 July 2007 in comparison to 31 July 2006 are as follows.

| Period | Under 60 Days Old | Over 6 Months Old |
|---|---|---|
| 31/07/06 | 70% | 20% |
| 31/07/07 | 61% | 21% |

This means that on 31 July 2007 both targets were achieved.

**IMPROVEMENTS**

10. The Debt Recovery team strives for continuous improvement and seeks best practice. Listed below are some of the areas in which improvements have been made throughout the County during the last 18 months.

(1) On-line access to Land Registry direct – this facility provides a valuable resource to enable title deeds of properties to be verified. This has speeded up the process where debts can be secured by a legal charge.

(2) Recovery of debts through the County Court – since November 2006 the Debt Recovery team have pursued debtors through the small claims court. This facility reduces costs, by not having to engage the services of our in-house legal department, and speeds up the recovery process.

(3) Automatic write-back – forms part of the Council's revised debt management policy and allows the Debt Recovery team to automatically write-back a debt to its originating budget code, where the directorate has failed to resolve. CIPFA benchmarking indicates that other counties are adopting this approach.

(4) Instalment plans – a more realistic approach to instalments has been adopted. Entering into an instalment arrangement for small sums and long periods is not cost effective.

(5) Regular debt meetings – Debt Recovery undertakes regular six-weekly meetings with directorate colleagues. The meetings have had a positive outcome on progressing old, high value debt issues.

(6) External agency – the Debt Recovery team uses a debt collection agency for the issue of a set of predefined letters. The Debt Recovery team carefully selects cases for referral, using experience to judge cases that are likely to produce good results. The Debt Recovery team also instigates, on-line person searches and tracing agents to locate the whereabouts of debtors who have absconded.

(7) Exchequer newsletter – quarterly newsletters are issued to Finance and some directorate colleagues. The purpose of the newsletter is to communicate information about the services of Exchequer. Debt Recovery has used this newsletter to address the slow resolution of

disputes and queries raised by debtors and has communicated the importance of accurate debtor information.

**RECOMMENDATION**

11. Members are asked to note this report.

Terri-anne McPherson
Principal Debt Recovery Officer

| | |
|---|---|
| By: | The Head of Audit & Risk |
| To: | Governance and Audit Committee<br>19 September 2007 |
| Subject: | **ARRANGEMENTS FOR AUDIT AND RISK FROM 1 AUGUST 2007** |
| Accountable Officer: | The Head of Audit & Risk |
| Classification: | Unrestricted |

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**Summary**: This report provides information on the progress of developing the second half of the 2007/08 audit plan and a proposed audit plan for the second half of the 2007/08 year.

**FOR INFORMATION**

In December 2006 the Head of Audit and Risk reported on a revised approach to audit planning and risk management in KCC. A new approach was necessary because:-

- An analysis of the assurance levels given to audits over the past 3 years shows that there are a higher percentage of minimal or limited assurances being given now compared to previous years. In 2003/04, the percentage was 29%. In 2005/06, the figure rose to 46%.
- There is a collective desire both within Internal Audit and service directorates to further improve the 'added value' that Internal Audit provides in the service directorates.
- There is a need to further integrate the risk management process into our business planning process.

**Progress to date**

The new approach focuses on the risk to the Council of not meeting its business objectives and requires Internal Audit to 'map' all of the business objectives, risks and controls of every business plan. 10 Risk Management workshops were held which were attended by over 150 officers who have an interest in the subject. Further workshops are being held during September and October, including one for Members. Following these workshops Internal Audit staff have met with service managers and staff to help to facilitate the mapping of their objectives, risks and controls. This has been done by using a template and a risk matrix in order to score the risks. In a lot of cases business managers had undertaken this task themselves. At the time of writing there were outstanding completed templates expected from managers. However, it is a time consuming task and these are expected in the next few weeks.

To give Members an idea of the scale of this task and the valuable input of service managers and staff we have listed below details of the progress to date:-

- Internal Audit staff have met with over 100 service managers and staff
- Over 200 business objectives have been mapped
- Over 450 risks have been mapped
- Over 800 controls mapped

We estimate that the above number (excluding meetings with staff) will double when all of the completed templates have been received. Once we have received the information, the next task will be to carry out a moderation process on the data which will involve some further discussions with the directorates.

We are therefore, still in the process of developing the second half of the 2007/08 plan. However, all of the objectives, risks and controls that have been captured with also form the basis for the 2008/09 audit plan and future plans.

**Next Stage**

Internal Audit's next task has been to input all of the objectives, risks and controls into 'Team Risk' which is an audit software tool designed to facilitate the development of an audit plan. Once all of the above have been input we will be able to categorise the auditable areas based on the inherent risks identified from the mapping process.

We will also be identifying the means by which we can capture other key information, for example new projects/developments, integrating information from risk registers, as well as ensuring that the information is kept current and up to date.

**Benefits**

One of the objectives of developing a new risk based approach to the audit plan was to get risk management embedded within the Authority. The risk management workshops and the meetings Internal Audit staff have had with service managers have considerably raised awareness amongst staff. The majority of the managers that we have met with have stated that both processes have been very useful and have helped them to understand risks and controls and their contribution to ensuring that their objectives are met.

Another benefit of our meetings with managers has been the number of requests that Internal Audit staff have received to liaise with service. This will help Internal Audit to gain greater understanding of the directorates and to be aware of any new systems, procedures and projects that are being proposed where we can advise on controls.

**Conclusions**

A lot of progress has been made in identifying and mapping all of the Authority's business objectives, risks and controls. This process will continue to enable the second half of the 2007/08 plan to be developed and all future plans.

Directorates have been very supportive of the process and have also benefited from the risk management workshops and the 'mapping' exercises.

Internal Audit will have a database of all of the Authority's objectives, risks and controls from which we can build our audit plans and provide assurance on how risks are being managed. This will be the starting point for the audit plan for 2008/09.

Finally, we'd like to thank all of the staff who took the time to meet with us, who mapped their objectives, risks and controls and contributed to this process. We appreciate that this took a lot of time and commitment on their part. Without their input we would not have been able to achieve this exercise.

**Internal Audit Half Year Plan October 2007 to March 2008**

The Internal Audit half year plan from April to September, together with the planned chargeable days of 2,775 for 2007/08 was reported to the March 2007 Governance and Audit Committee. To date approximately 750 days of the 2007/08 plan has been delivered.

Part of the proposed six month plan from October 2007 to March 2008 will comprise audits to provide assurance on key financial systems, corporate governance and where there have been specific requests from directorates. We will be covering the following areas which will take approximately 430 days.

- Schools' Payroll
- Overtime Payments
- Asylum Seekers' Cash Handling
- Revenue Budget Monitoring (E&R)
- Purchase Cards
- Compliance with the Standing Orders and Scheme of Delegation

- Contract Audit
- Pensions/Investments
- Governance of Partnerships
- ICT audits.

The remainder of the plan (approximately 700 days) will be developed from mapping the objectives, risks and controls from directorates' business objectives and identifying where reliance is being placed on controls to manage high scoring risks. We expect to have completed this exercise by the end of September, with a view to confirming audit areas with directorates and agreeing terms of reference in October.

The remainder of the budget includes:-

| | |
|---|---|
| Advice & Information | 450 days |
| Fraud & Irregularity work | 120 days |
| Contingency | 300 days |

The audit plan for the 6 months to 31 March 2008 will be drafted and ready for approval by the end of October.

**Recommendation**

To avoid delaying the delivery of the audits planned until after the next Committee meeting in December, members are asked to delegate approval of the six month audit plan to 31 March 2008 to the Director of Finance, in consultation with the Chair of the Committee and opposition members.  The plan will then be reported retrospectively to the December meeting.

Janet Dawson
Head of Audit and Risk
Extension 4614
3 September 2007

Item No: 11

By: The Head of Audit & Risk

To: Governance and Audit Committee
19 September 2007

Subject: **INTERNAL AUDIT REPORTING**

Accountable Officer: The Head of Audit & Risk

Classification: Unrestricted

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**Summary**: This report summarises the outcomes of Internal Audit activity, providing assurance as to the operation of control within the Council.

**FOR INFORMATION**

## Introduction

1. This report contains the outcome of Internal Audit's work completed during June, and July 2007. Assurances are provided in accordance with the definitions of Internal Audit assurance levels shown in Annex A.

2. The format of this report, which was agreed at a previous meeting, is as follows:

   **Annex B** Audits completed to date. Audits appearing for the first time are shown in bold. Nine audits were completed in this period, which are listed in the table below:

| Directorate | Audit Title | Assurance |
|---|---|---|
| AW | Follow up to the Procurement of Consumables | Limited |
| AW | Medium Term Planning | High |
| AW | Risk Management | High |
| AW | Virus Protection | Substantial |
| AW | Corporate Governance | Substantial |
| CED | Year end Accounting Processes | Substantial |
| CF&E | Sharing of Information on Children | Substantial |
| CF&E | Reimbursement of Schools Maternity Pay | Substantial |
| CSD | Community Safety Revenue Budget Management | Substantial |

**Annex C** Summary information, with the directorates' response for all follow up audits where control was previously assessed as 'unsatisfactory/minimal'

**Annex D** Brief details of audit work completed in the period.

**Annex E** Summary of directorates' progress with the implementation of internal audit recommendations.

Members can see from Annex E that of the 36 recommendations due to be in place, 31 have been actioned and five remain outstanding. Three of the outstanding recommendations are due to be completed by the end of September 2007.

3. Members should note that the audit assurance expressed is at the time of issue of the audit report but before full implementation of the agreed management action plan. Directorates' progress with the implementation of recommendations is followed up and reported at Annex D, after the date by which it has been agreed that action will be undertaken. Where a 'minimal' assurance has been given, there will be further re-evaluation in a six-monthly review.

4. Furthermore, each audit does not carry equal weight when forming the overall assurance on the operation of control within the Authority. Whilst the key systems will have a major impact, other systems, for example establishment audits, become more significant when the outcomes of a number of similar audits have been obtained. In this instance, the key indicator is the trend in audit assurances within a directorate and across the Authority.

**Irregularities**

**5.** Since the end of May seven cases of suspected irregularity have been reported, each involving either KCC finances or business processes. Details of completed irregularity investigations are given in my separate report at agenda item x.

## Performance of Internal Audit

6. At the Audit Committee meeting on 3 March 2004, Members agreed to receive regular reports on Internal Audit's performance against a range of indicators. For those measures where information is available, performance is shown below:

| Performance Indicator | Target | Actual (Apr – July) |
|---|---|---|
| ***Productivity and Efficiency*** | | |
| • % of available time spent on direct audit work | 80% | 75% |
| • % of draft reports completed within 10 days of finishing fieldwork | 89% | 80% |
| • Preparation of annual plan | By March | Reported 7.3.07 |
| • Periodic reports on progress | G&A Cttee meetings | Reported: 30.06.06 20 09.06 05.12.06 |
| • Preparation of annual report | Prior to annual assurance statement | Reported 29.06.07 |
| ***Quality of Service*** | | |
| • Average Client satisfaction score | 70% | 93% |
| ***Staff Management*** | | |
| • Staff with professional qualifications (including trainees) | 60% | 74% |

## Recommendation

7. Members are asked to **note** the outcome of Internal Audit's work.

**Janet Dawson**
**Head of Audit & Risk**
Ext: 4614
3 September 2007

## Definitions of Internal Audit Assurance Levels

| Assurance Level | Summary description | Detailed definition |
|---|---|---|
| **High** | Strong controls in place and complied with. | The system/area under review is not exposed to foreseeable risk, as key controls exist and are applied consistently and effectively. |
| **Substantial** | Controls in place but improvements beneficial. | There is some limited exposure to risk of error, loss, fraud, impropriety or damage to reputation, which can be mitigated by achievable measures. Key or compensating controls exist but there may be some inconsistency in application. |
| **Limited** | Improvements in controls or the application of controls required. | The area/system is exposed to risks that could lead to failure to achieve the objectives of the area/system under review e.g., error, loss, fraud/impropriety or damage to reputation.<br><br>This is because, key controls exist but they are not applied, **or** there is significant evidence that they are not applied consistently and effectively. |
| **Minimal** | Urgent improvements in controls or the application of controls required. | The authority and/or service is exposed to a significant risk that could lead to failure to achieve key authority/service objectives, major loss/error, fraud/impropriety or damage to reputation.<br><br>This is because key controls do not exist with the absence of at least one critical control, **or** there is evidence that there is significant non-compliance with key controls. |

## Audit Programme and Coverage by Directorate June and July 2007

| Report | Directorate | Audit Plan | Overall Opinion | Budget Mngment | Payroll | Payment | Income | Banking & Cash Handling | Accounting Systems & Processes | Resource Mngment | General Financial Control | Procurement | Governance | Business Process | Info System |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | **Authority-wide** | | | | | | | | | | | | | | |
| | ***Brought forward from 2006/7 Plan*** | | | | | | | | | | | | | | |
| June 07 | Trading Companies | ✓ | L | | | | | | | | | | | | |
| June 07 | BS57799 | ✓ | H | | | | | | | | | | | | |
| June 07 | Telephone PBX | ✓ | S | | | | | | | | | | | | |
| June 07 | *Follow up ICT Disaster Recovery* | ✓ | L | | | | | | | | | | | L | |
| **Sep 07** | **Follow up to the Procurement of Consumables** | ✓ | **L** | | | | | | | | | **L** | | | |
| **Sep 07** | **Medium Term Planning** | ✓ | **H** | | | | | | | **H** | | | | | |
| **Sep 07** | **Risk Management** | ✓ | **H** | | | | | | | | | | **H** | | |
| **Sep 07** | **2007/08 Plan**<br>**Virus Protection** | ✓ | **S** | | | | | | | | | | | | **S** |
| **Sep 07** | **Corporate Governance** | ✓ | **S** | | | | | | | | | | **S** | | |
| | **Chief Executive's Department** | | | | | | | | | | | | | | |
| | ***Brought forward from 2006/07 Plan*** | | | | | | | | | | | | | | |

**Annex B**

## Audit Programme and Coverage by Directorate June and July 2007

| Report | Directorate | Audit Plan | Overall Opinion | Budget Mngment | Payroll | Payment | Income | Banking & Cash Handling | Accounting Systems & Processes | Resource Mngment | General Financial Control | Procurement | Governance | Business Process | Info System |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| June 07 | *VAT provision of asylum seekers services* | ✓ | S | | | | S | | | | | | | | |
| June 07 | Physical Security & Environmental Controls | ✓ | S | | | | | | | | | | | | |
| June 07 | *VAT payments to providers of Care (Adult Social Services)* | ✓ | S | | | | S | | | | | | | | |
| June 07 | *Technical Administration of the Oracle Financial, HR & Payroll System* | ✓ | S | | | | | | | | | | | | S |
| June 07 | *Commercial Services CODA* | ✓ | S | | | | | | | | | | | | S |
| June 07 | Commercial Services Insurance Funds | ✓ | L | | | | | | L | | | | | | |
| **Sep 07** | **2007/08 Plan**<br><br>**Year end Accounting Processes** | ✓ | **S** | | | | | | **S** | | | | | | |
| | <u>**Children, Families & Education**</u> | | | | | | | | | | | | | | |
| | ***Brought forward from 2006/07 Plan*** | | | | | | | | | | | | | | |
| June 07 | *Foster & Adoption Payments* | ✓ | S | | | S | | | | | | | | | |
| June 07 | *Schools Advisory Service* | ✓ | H | | | | | | | | | | | | |
| June 07 | *Student Awards* | ✓ | H | | | | | | | | | | | | |

**Annex B**

## Audit Programme and Coverage by Directorate June and July 2007

| Report | Directorate | Audit Plan | Overall Opinion | Budget Mngment | Payroll | Payment | Income | Banking & Cash Handling | Accounting Systems & Processes | Resource Mngment | General Financial Control | Procurement | Governance | Business Process | Info System |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| June 07 | *Attendance & Behaviour Safer Schools* | ✓ | S | | | | | | | | | | | S | |
| June 07 | *Schools Managed Capital Projects* | ✓ | S | | | | | | | S | | | | | |
| **Sep 07** | ***Sharing of Information on Children*** | ✓ | **S** | | | | | | | | | | | | **S** |
| **Sep 07** | ***2007/08 Plan*** <br> ***Reimbursement of Schools' Maternity pay*** | ✓ | **S** | | | **S** | | | | | | | | | |
| | **Adult Services** | | | | | | | | | | | | | | |
| | ***Brought forward from 2006/07 Plan*** | | | | | | | | | | | | | | |
| June 07 | Swift pre Implementation Review | ✓ | S | | | | | | | | | | | | S |
| June 07 | Domiciliary Care TDM | ✓ | L | | | L | | | | | | | | | |
| June 07 | Former Self Funders | ✓ | L | | | | | | | | | | | | |
| June 07 | Residential Care Mental Health Payments | ✓ | S | | | S | | | | | | | | | |
| June 07 | Voluntary Organisations | ✓ | S | | | S | | | | | | | | | |
| | **Environment & Regeneration** | | | | | | | | | | | | | | |

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**Annex B**

## Audit Programme and Coverage by Directorate June and July 2007

| Report | Directorate | Audit Plan | Overall Opinion | Budget Mngment | Payroll | Payment | Income | Banking & Cash Handling | Accounting Systems & Processes | Resource Mngment | General Financial Control | Procurement | Governance | Business Process | Info System |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| June 07 | ***Brought forward from 2006/07 Plan*** Transport \|Network Management | ✓ | S | S | | | | | | | | | | | |
| June 07 | KHS Coastal Protection | ✓ | L | | | | | | L | | | | | | |
| | **<u>Communities Directorate</u>** | | | | | | | | | | | | | | |
| June 07 | *Brought forward from 2006/07 Plan* Youth & Community | ✓ | H | | | | | H | | | | | | | |
| June 07 | Libraries | ✓ | S | | | | | | | | | | | S | |
| **Sep 07** | **Community Safety Revenue Budget Management** | ✓ | **S** | **S** | | | | | | | | | | | |

**Annex C**

**Audit Work Completed in the Period**
**June 2007 – July 2007**

**Matters Arising from Previous Reports**

**Authority Wide**

**Follow up to The Procurement of Consumables**

**Audit Assurance - Limited**

An audit of the procurement of consumables was carried out during 2003/04 and report 22/04 was issued on 30 June 2004, the audit opinion was unsatisfactory. Internal Audit requires a follow up of all unsatisfactory (now minimal) audits to evaluate the effectiveness of agreed actions taken to improve controls.

The follow up audit was delayed because of the anticipated changes to the Council's procurement arrangements arising from the implementation of a new Procurement Strategy and 'Spending the Council's Money' which will replace the Contracts and Tenders Code of Practice. The Procurement Strategy was endorsed by the Chief Officer's Group and presented to the Cabinet on 11 July 2005, however, the Code had not yet been implemented.

A key risk identified in the last audit was that excessive procurement of consumables may be diverted to external suppliers and benefits to the Authority may be lost. The new Procurement Strategy and new Code aim to clarify the Council's buying policy for all spending on goods, services and works and the procurement structure should ensure their implementation.

During the course of the follow up audit our review of five payment codes comparing expenditure over a similar eight month period in 2005/06 and 2006/07 showed that officers with purchasing responsibilities continued to spend a greater proportion of their consumables budget, approximately 72%, with external suppliers compared ho internal purchases.

Subsequent to the issue of this report, the Procurement Unit undertook a review of the expenditure data used as the basis of our 2006/07 analysis. Their findings supported our report of miscodings and they have suggested adjusting for additional errors. Nevertheless, using their base figures, the overall adjusted leakage to external suppliers would still remain high at over £2.1m.

We noted that some improvements had been made in shifting the directorates buying preferences for printing, stationery and office expenses to Commercial Services but general leakage of business to external suppliers could be further reduced if the strategy is strictly implemented. We appreciate that since the audit, and in line with our recommendations, further strong guidance has been given to staff with responsibility for purchasing consumable items which should, if actioned improve matters further.

*Management Response*

*The figures included in the audit considerably overstated the external spend on the headings covered and Internal Audit were made aware of this. All the findings relate* *to the period before the issue of the spend mandate in March 2007. for the first time this explicitly stated that for the following headings spend had to be via Commercial Services of county wide contracts ,which have been put in place.*

- *Stationery*
- *Computer Consumables*
- *IT*
- *Mobile phones*
- *Recruitment advertising*
- *Office equipment*
- *Vehicles*
- *Furniture*
- *Cleaning supplies*
- *Energy*
- *Sports equipment*
- *Fire extinguishers*

*We are putting arrangements in place through Exchequer Services to monitor compliance and PwC will be undertaking an exercise to ensure that we are getting best value through those contracts.*

*Nick Vickers*
*Head of Financial Services*

## Audit Work Completed in the Period
## June 2007 – July 2007

### Completed audits

| Directorate | Audit | Description | Audit Assurance |
|---|---|---|---|
| AW | Medium term Planning | A review of the medium term planning process. | High |
| AW | Risk Management | An audit of the Authority's risk management arrangements | High |
| AW | Virus Protection | A review of the arrangements in place to protect KCCs systems and data from viruses and malware. | Substantial |
| AW | Corporate Governance | A review of corporate governance in relation to the promotion and demonstration of ethical standards and values. | Substantial |
| CED | Year end accounting processes | An audit to ensure all payments and income are accounted for in the correct financial year. | Substantial |
| CF&E | Sharing of Information on children | An examination of controls over electronically held data on children within Impulse, CAPITA-EMS and Swift. | Substantial |
| CF&E | Reimbursement of schools' maternity pay | A review of the processes in place for reimbursing schools' maternity pay | Substantial |
| CSD | Community Safety revenue budget management | An audit of revenue budget monitoring | Substantial |

# Audit Work Completed in the Period
# June 2007 – July 2007

## Advisory and other work

| Directorate | Audit work | Description |
|---|---|---|
| Chief Executive's Department | JP Morgan | An interim review of control processes operating to provide assurance as to the custody of assets on behalf of the Kent Pension Fund. |
| Community Services Directorate & CED (Commercial Services) | Health & Safety | Advice and information provided to both these areas at a time when Commercial Services were without an overall Health and Safety Adviser and Community Services were a newly formed directorate. Both areas have put together an Action Plan to ensure full coverage of Health and Safety issues in their respective areas. A full audit of compliance with the Health and Safety Policy in Commercial Services and the Communities Directorate is planned for March 2008. |

Annex C

## Directorates Progress with Implementation of Audit Recommendations (covers period June to July 2007)

| Directorate | Total actions due to be in place by end of July 2007 | Actions in place | Outstanding actions (priority) | | | Progress with outstanding actions | |
|---|---|---|---|---|---|---|---|
| | | | VH | H | M | Audit | Comments |
| Authority Wide | 5 | 5 | | | | | |
| Chief Executive | 9 | 8 | | | 1 | Network Management Review | Partial Progress: Funding is being requested for suitable network management tools. Tender specification is being produced. And the unit is still in the process of seeking funding |
| Children and Families | 5 | 4 | | 1 | | VAT on Asylum Seekers Accomodation | This recommendation will be completed by the end of September 2007 |
| Adult Social Services | 11 | 9 | 2 | | | VAT on Care Payments | These recommendations will be completed by the end September 2007 |
| Environment & Regeneration | 4 | 4 | | | | | |
| Communities | 2 | 1 | | 1 | | KDAAT - Partnership Arrangements | This recommendation has been deffered and will be implemented during November 2007 |
| | **36** | **31** | **2** | **2** | **1** | | |

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Item No :12

| | |
|---|---|
| By: | The Head of Audit & Risk |
| To: | Governance & Audit Committee<br>19 September 2007 |
| Subject: | **INTERNAL AUDIT REPORTING – IRREGULARITIES** |
| Accountable Officer: | The Head of Audit & Risk |
| Classification: | Unrestricted |

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**Summary:** This report provides brief details of all irregularity cases completed during the period May 2007 to July 2007.

**FOR INFORMATION**

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## Introduction

1. In line with best practice and as agreed by Members of the Audit Committee at their meeting on the 1 March 2005, this report summarises the outcome of irregularity investigations that have been concluded within the period from May to July 2007.

2. During the period, seven new cases of potential irregularity were reported, for which investigations are continuing. Where significant, details of these irregularities are reported separately to the Chairman of the Governance and Audit Committee during informal meetings, to ensure that he is made aware of possible problems as they arise.

3. Appendix 1 summarises the investigations that have been completed within the period.

## Recommendation

4. Members are asked to note this report.

**Janet Dawson**
**Head of Audit & Risk**
Ext: 4614
3 September 2007

**Summary of Irregularity Cases Concluded in the Period May to July 2007**

| Ref | Directorate | Nature of Irregularity | Value | Outcome |
|---|---|---|---|---|
| 715 | CED | Theft/loss of Member's Community Grant | £2,000 | • In 2006 an application for a community grant was received from a member of the public to replace a boiler in a leased building where she was providing dance classes to the local community.<br>• As part of the process to evaluate how the grant had been used, the Community Liaison Manager visited the dancing school, but found that it had closed down and the dancing teacher had 'disappeared' shortly after the grant had been awarded.<br>• Enquiries were made but the dancing teacher could not be traced and the matter was referred to the police, however, they have been unable to trace her. |
| 726 | CED Commercial Services | Overcharging by taxi company | £5,456 recovered | • As part of the ongoing monitoring of contracts with transport providers, a taxi company engaged to transport two children to school was found to be charging for two taxis and two escorts but only using one.<br>• The company was contacted and admitted that it had not always provided two taxis and escorts. The company has repaid the overcharged amount and the contract with the company has since been revised. |