



Exeter City Council

Interim Audit Report 2009-10

20 May 2010

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1 Executive summary

Introduction

- 1.1 In carrying out our audit, we comply with statutory requirements governing our duties, in particular, the Audit Commission Act 1998 and the Code of Audit Practice (the Code).
- 1.2 The Code of Audit Practice emphasises the respective responsibilities between audited bodies and their auditors. The Council is responsible for putting in place proper arrangements for the governance of its affairs and the stewardship of its resources. We are required to form an opinion on the Council's annual financial statements and a conclusion on whether the Council has proper arrangements in place for securing economy, efficiency and effectiveness in the use of resources.

Scope

- 1.3 We have completed our interim audit at the Council in accordance with our agreed audit strategy as set out in the Financial Statements Audit Plan presented to Scrutiny Committee - Resources on 27 January 2010. Our interim audit also covered use of resources work to reach our draft conclusion.

Overall conclusions

Accounts

- 1.4 Our initial assessment of risks facing the Council which could impact our audit, as set out in our 2009-10 Financial Statements Plan, remains appropriate and provides a sound basis upon which to set our audit strategy.
- 1.5 The internal audit service continues to provide an independent and satisfactory service to the Council and we are able to take assurance from their work in contributing to an effective internal control environment.
- 1.6 Our information systems specialist performed a high level review of the general IT control environment, as part of the overall review of the internal controls system, and concluded that, from the work undertaken to date, there are no material weaknesses which are likely to adversely impact on the Council's financial statements.
- 1.7 The Council has an appropriate accounts closedown timetable in place to prepare and submit its accounts by the 30 June 2010 deadline.
- 1.8 Our follow up of the action taken by the Council to implement recommendations made in our 2008-09 interim report has identified only one recommendation that the Council has yet to implement, relating to the authorisation of journal entries. The Council has either fully implemented, or is making satisfactory progress in the implementation of, the other 11 recommendations made.

Use of resources

- 1.9 Our assessment to date has highlighted that the Council has strengthened its arrangements across a number of areas, and we are proposing to increase our assessment of its understanding of costs and delivery of efficiencies, financial reporting, and governance arrangements from a level two to level three. It is important to note that the proposed scores are indicative at this stage and may change once we have reviewed additional evidence that has been requested to support assertions made and as a result of both internal and external quality assurance. The finalised scores will be published by the Audit Commission in October 2010.

Emerging issues: Local Government Reorganisation

- 1.10 Since preparing our audit fee letter, the appropriate statutory provisions have come into force relating to the Council's unitary status. We have started to hold detailed discussions with officers on the impact of this change on our audit programme and any specific risk-based work that we may need to undertake as well as the impact upon our review of other areas, such as use of resources.
- 1.11 Such a significant development and the preparations involved within a very short timescale present a range of additional risks to the Council's ongoing arrangements as well as their preparations for taking on new services and activities. We also recognise that the Council is also undertaking its preparations at a time of further uncertainty due to the judicial review initiated by Devon County Council and manifesto commitments out forward by the Conservative party.
- 1.12 We will ensure that we continue to work closely with management, during these preparations, to ensure that we maintain a proportionate audit approach whilst addressing any specific risk areas. At this time, we envisage undertaking any work required within the existing fee but will report to management and Scrutiny Committee - Resources, should this not remain possible.

Use of this report

- 1.13 This report has been prepared to advise you of the matters arising from our interim audit and should not be used for any other purpose or be given to third parties without our prior written consent.
- 1.14 Our report is part of a continuing dialogue between the Council and ourselves and should not be relied upon to detect all errors, systems or control weaknesses or opportunities for improvements in management arrangements that might exist. The Council should assess the wider implications of our conclusions and recommendations before deciding whether to accept or implement them, seeking your own specialist advice as appropriate.
- 1.15 We accept no responsibility in the event that any third party incurs claims, or liabilities, or sustains loss, or damage, as a result of their having relied on anything contained within this report.

The way forward

- 1.16 We have set out our findings and recommendations in the appendices to this report. We have agreed action to implement the recommendations made with the Head of Treasury.

Acknowledgements

- 1.17 We would like to record our appreciation for the assistance and co-operation provided to us during our interim audit by the Council's staff.

Grant Thornton UK LLP

20 May 2010

2 Interim accounts audit

Introduction

2.1 As part of the interim audit, and in advance of our final accounts audit visit, we considered:

- the key risks facing the Council;
- the effectiveness of the internal audit service;
- our review of financial reporting controls, including information technology controls, journal entry controls, financial accounting systems and closedown procedures; and
- emerging accounting issues.

Key risks

2.2 Our 2009-10 Financial Statements Plan was issued in November 2009 and set out the key risks facing the Council which could impact on the 2009-10 financial statements audit. The risks consider both national accounting issues and the risks facing the Council specifically.

2.3 As part of our interim audit, we reviewed these risks and have set out, below, the outcome of work completed and any further work planned. We can confirm that our initial risk assessment remains appropriate and provides a sound basis upon which to set our audit strategy. It is also important that the Council addresses the emerging accounting issues stated in the following paragraphs and later within this report.

2.4 We set out below an update on our risk assessment.

- **Accounting for National Non-Domestic Rates and Council Tax under the Statement of Recommended Practice (SORP) 2009** - We have discussed the changes to the SORP as part of our ongoing dialogue with officers of the Council and are satisfied that adequate arrangements are in place for the financial statements to be prepared in accordance with the SORP. We will continue to provide feedback at the request of officers, as necessary, throughout the closedown process.
- **International Financial Reporting Standards (IFRS)** - The Council continues to make good progress towards the implementation of IFRS and has assigned adequate staff resource to ensure that this is achieved in accordance with the required deadlines. We will continue to monitor progress against the Council's IFRS transition plan and provide an early review of its restated IFRS balance sheet to ensure that it has fulfilled the accounting requirements. We are pleased to report that we assessed the Council's preparations as 'Green', the equivalent of 'good', in a recent submission to the Audit Commission, which was one of only a minority of Council's assessed as such.
- **Group accounts** - We have discussed the Council's arrangements for ensuring that it receives, in a timely way, the audit opinion for its subsidiary accounts and will continue to monitor these arrangements to ensure that subsidiary accounts are audited and approved in accordance with a timetable that allows the group accounts

to be finalised in accordance with statutory deadlines.

- **Icelandic banks** - We have discussed the current situation with the Council and are satisfied that officers are aware of the guidance currently available on recoverable amounts. We will review the entries made in the final accounts as part of our audit to ensure they reflect the most recent information available.

The internal audit service

- 2.5 We review internal audit's overall arrangements against the CIPFA Standards for Internal Audit including its terms of reference, the independence of internal audit, relationships with management and the Scrutiny Committee, staffing, training and development, management of audit assignments, and quality assurance, to ensure that these are adequate to provide robust and reliable work. Where the arrangements are deemed to be adequate, we can gain assurance from the overall work undertaken by internal audit and can conclude that the service itself is contributing positively to the internal control environment and overall governance arrangements within the Council.
- 2.6 We undertake a detailed review of the internal audit service every three years, with an interim review in intervening years. The last detailed review of the Council's internal audit service was completed in 2007-08 and this work has been reviewed and updated as part of our planned programme of work for 2009-10.
- 2.7 Overall, we have concluded that the internal audit service continues to provide an independent and satisfactory service to the Council and that we can take assurance from their work in contributing to an effective internal control environment at the Council.
- 2.8 In assessing the effectiveness of internal audit work, we performed a detailed review of two internal audit files. This review considered whether:
- systems were adequately documented;
 - key controls had been identified and evaluated;
 - key controls had been tested; and
 - weaknesses had been reported to management.
- 2.9 Our review of these files highlighted one area where the existing arrangements could be strengthened further.
- 2.10 Our review of the detailed testing undertaken by Internal Audit for the two audits we selected identified that, for a number of tests, a sampling approach was adopted. Whilst we do not disagree that this was an appropriate approach, or that the number of items selected or the period covered was inappropriate, there was no explanation provided on file for the sample sizes selected. To further strengthen the documentation of internal audit files, the rationale for the audit approach taken for each test, together with an explanation of the sampling technique applied, should be clearly set out. This enables someone who independently reviews the file, or for the auditors that completes the audit work in following years, to gain a sound understanding of the approach adopted and the reason for this.

Recommendation 1

Each test carried out by Internal Audit which utilises a sampling approach should include an explanation of the reason why that approach is the most appropriate and a justification for the number of items selected for further testing.

Review of information technology controls

- 2.11 The Council makes use of Cedar Open Accounts (COA) eFinancials, a finance package purchased from a third party, to administer its accounts. COA eFinancials is administered within the Finance department and sits within the Council's main IT network, which is managed by the IT department. Our information systems specialist performed a high level review of the general IT control environment, as part of the overall review of the internal controls system, and concluded that from the work undertaken to date, there are no material weaknesses which are likely to adversely impact on the Council's financial statements.
- 2.12 However, during the course of our audit work in this area, we have identified a number of areas where arrangements could be enhanced in order to improve the overall control environment. We do not consider these to pose a significant risk to the accounts and have reported them to management through our interim audit feedback meeting.

User administrative access

- 2.13 Administrative access to the COA eFinancials application is restricted to the Accountant and two Assistant Accountants within the Finance department. However, these individuals also perform operational functions in the eFinancials application.
- 2.14 Administrative access should be restricted to only those individuals who require the privileged access to perform their job. Without appropriate segregation of duties, there is an increased risk of erroneous or inappropriate actions when one or more individuals have incompatible duties.
- 2.15 If appropriate segregation of duties cannot be achieved, (usually due to the small size of the Finance or ICT department), monitoring controls can be implemented to mitigate the risk of incompatible functions being performed by one or more individuals. Without monitoring controls, there is an increased risk of unauthorised actions performed, for example, initiation and approval of a transaction by the same individual, which may go undetected by management.

Recommendation 2

Management should consider the feasibility of removing powerful administrative access from operational users of COA eFinancials to ensure appropriate segregation of duties is maintained in the system.

If this is not feasible, then management should consider monitoring the actions performed by the administrator accounts to ensure actions performed are appropriate and authorised.

User access reviews

- 2.16 A user access review for COA eFinancials was performed by Council management when the system was implemented; however, there is no formal process in place to ensure user access is reviewed on a regular basis going forward.
- 2.17 If user access is not reviewed by management on a regular basis, there is a risk access will become disproportionate over time with user job responsibilities. There is also a higher risk of segregation of duties issues as individuals transfer or move on to different positions within the Council.

Recommendation 3

Management should consider implementing a process to review user access to the COA eFinancials application on a regular basis to ensure access is appropriate based on job functions.

Regular leaver listings

- 2.18 A process is in place that notifies all system administrators across the Council of leavers, long-term absences and transfers between jobs/services. It is each systems administrator's responsibility to remove applicable users from the system accordingly. However, the Council needs to ensure that a process is put in place to ensure that user access is disabled by the systems administrators on a timely basis.

Recommendation 4

Management should implement a review process to ensure that access has been appropriately removed by each system administrator in a timely manner.

Network intrusion detection and prevention

- 2.19 There is some limited intrusion prevention as part of the Council's firewalls, but there is no separate and dedicated system for intrusion detection or prevention (IDS/IPS). We understand management is waiting on the results from the recent Code of Connection audit to determine the priority of implementing dedicated IDS/IPS.

Journal entry controls

- 2.20 Journals are used to process manual changes to data within the financial ledger. Journals processed by officers are not currently authorised, although the Council has acknowledged, following our recommendation in 2008-09, that an authorisation process for journals above a pre-determined threshold should be implemented.
- 2.21 Without an authorisation process in place, there remains a risk to the Council that inappropriate or erroneous journals are processed that impact on the financial statements, although the extent of this risk is mitigated through the small number of people who have access to process journals on the financial system.

Recommendation 5

As recommended in 2008-09, the Council should introduce a requirement for independent approval of journals above pre-determined thresholds.

Closedown procedures

- 2.22 Our review considered the Council's timetable for closing down the financial systems in order to prepare the draft accounts. We have also discussed our requirements for the level and quality of working papers to be made available at the start of our final accounts audit visit.
- 2.23 The Council has an overall timetable in place, which outlines the key dates and responsible officers for each task. This timetable shows that the Council expects to meet the statutory deadline of 30 June 2010 for the approval of draft accounts.

Emerging accounting issues

- 2.24 We have discussed a number of emerging issues with the Council's finance team. Those that have not been raised elsewhere in this report are briefly summarised below.

Unitary status

- 2.25 A programme of regular meetings are now in place with senior officers at the Council to discuss its ongoing preparations for the transition to unitary status on 1 April 2011. We will continue to monitor the progress made, provide ongoing advice and recommend opportunities to support the Council's transition where these are identified.

Progress in implementing prior year recommendations

- 2.26 As part of our planned programme of work, we followed up the recommendations made in our interim report issued last year. Our work shows that the Council has made progress in the implementation of these recommendation as detailed below.
- 2.27 Two recommendations were made relating to the Council's internal audit service, both of which have been implemented. Eight recommendations were made relating to the finance function of which only one, relating to the authorisation of journal entries, is included again in this report at paragraph 2.21.
- 2.28 Two recommendations were made relating to the Council's IT arrangements. The Council is continuing to implement our recommendation on change management documentation as part of the new service desk, and will consider the implementation of dedicated intrusion detection and prevention systems following the findings from the recent Code of Connection audit.

3 Use of resources

Introduction

- 3.1 Our use of resources work involves us reaching formal conclusions on the Council's arrangements across a broad range of areas, as shown in exhibit two. The Council is responsible for reporting on these arrangements as part of its Annual Governance Statement (AGS).

Exhibit One: use of resources - areas of work

Key areas set out in the code of audit practice
Establishing strategic and operational objectives
Determining policy and making decisions
Ensuring that services meet the needs of residents and taxpayers and arrangements for engaging with the wider community
Ensuring compliance with established policies, procedures, laws and regulations
Identifying, evaluating and managing operational and financial risks and opportunities, including those arising from involvement in partnerships and joint working
Managing financial and other resources, including arrangements to safeguard the financial standing of the audited body
Monitoring and reviewing performance, including arrangements to ensure data quality
Ensuring that the audited body's affairs are managed in accordance with proper standards of conduct, and to prevent and detect fraud and corruption

- 3.2 In order to conclude on the use of resources areas, we perform an assessment against a number of Key Line of Enquiry (KLoE) in line with the procedures for Comprehensive Area Assessment (CAA), using the underlying principles of performance, attached at Appendix B.
- 3.3 The use of resources assessment is structured into three themes that focus on:
- sound and strategic financial management - Managing Finances;
 - strategic commissioning and good governance - Governing the Business; and
 - the management of natural resources, assets and people - Managing Resources.

- 3.4 Our provisional assessment from our use of resources work is summarised in exhibit two below, together with the prior year assessment. It is important to emphasise that the scores for 2010 are provisional at this stage. As well as being dependent on further evidence that we have requested to support our discussions with officers, the scores will be internally and externally quality assessed which may result in a change. The finalised scores will be published by the Audit Commission in October 2010.

Exhibit Two: Use of resources scores 2010 compared to 2009

Theme	KLoE	KLoE description	2010 provisional audited score	2009 final score
Managing finances	1.1	Does the organisation plan its finances effectively to deliver its strategic priorities and secure sound financial health?	2	2
	1.2	Does the organisation have a sound understanding of its costs and performance and achieves efficiencies in its activities?	3	2
	1.3	Is the organisation's financial reporting timely, reliable and does it meet the needs of internal users, stakeholders and local people?	3	2
Governing the business	2.1	Does the organisation commission and procure quality services and supplies, tailored to local needs, to deliver sustainable outcomes and value for money?	3	3
	2.2	Does the organisation produce relevant and reliable data and information to support decision making and manage performance?	3	3
	2.3	Does the organisation promote and demonstrate the principles and values of good governance?	3	2
	2.4	Does the organisation manage its risks and maintain a sound system of internal control?	2	2
Managing resources	3.1	Is the organisation making effective use of natural resources?	2	Not assessed in 2009

Theme	KLoE	KLoE description	2010 provisional audited score	2009 final score
	3.2	Does the organisation manage its assets effectively to help deliver its strategic priorities and service needs?	Not assessed in 2010	Not assessed in 2009
	3.3	Does the organisation plan, organise and develop its workforce effectively to support the achievement of its strategic priorities?	2	2

- 3.5 The main area which will be subject to further review for the current assessment is reviewing the outcomes achieved by the Council as a result of its understanding of costs and an update of our assessment of the Council's year end financial and operational performance to determine how value for money improvements have been achieved.

Theme 1: Sound and strategic financial management

- 3.6 The Council is managing well within a challenging financial position and has taken informed decisions to cut back on non essential services to help manage costs. The Council has suffered increase pressures from funding changes in the Concessionary Fares Scheme, as well as reductions in rents, car parking income and planning fees as a result of the economic downturn. Despite this, the Council continues to perform well and in some services, performance has improved.
- 3.7 Key services such as street cleansing and waste collection are delivered to a high standard at a low cost. The Council has further improved arrangements for financial reporting and has invested significant resource in preparing for the implementation of IFRS. Whilst we have assessed KLoE 1.1 at a level 2, we recognise that the Council has made good progress in redesigning its service plans to better link service objectives with corporate priorities and performance information and these have been implemented for 2010-11. As such, the outcomes which are required to demonstrate performance at a level 3 are likely to be able to be more clearly demonstrated over the forthcoming year.

Theme 2: Strategic commissioning and good governance.

- 3.8 The Council has consulted widely on its sustainable procurement and commissioning strategy and progress has been made against the implementation plan. The Council works closely with the PCT and other stakeholders in the design of services and works with small businesses in Exeter and the region to increase involvement in bidding for Council work. The Green Accord scheme gives suppliers a mechanism for demonstrating their green credentials by tackling issues such as fuel usage, travel and waste reduction/recycling and in doing so helps each service achieve compliance with the Council's Sustainable Purchasing Policy.
- 3.9 The Council prepares performance benchmarking reports for scrutiny committees, senior managers and other members of its benchmarking family. This includes information on diversity and equality issues. Our spot checks of performance indicators have not identified

any misstated performance information and no significant data quality issues were identified through our housing and council tax benefit certification work for 2008-09. The Council has a data sharing protocol in place and works with partners to ensure data quality is strong in the preparation of shared national indicators.

- 3.10 A member development committee actively oversees development opportunities for members. A comprehensive range of training sessions have been delivered during the year, to improve members skill sets. Courses are promoted to Councillors via email and the member newsletter, or targeted at individuals where a need has been identified through their development plan. The Council's complaints procedure and whistle-blowing policy, along with details of the Local Government Ombudsman scheme, are on the Council's external website, which also contains details of the work of the standards committee and specific details of each Councillor's interests and expenses.
- 3.11 At the time of our assessment we were unable to assess KLOE 2.4 as a level 3 as further work is required by the Council to develop its operational risk management arrangements within service areas. The Council is working with individual services to ensure that operational risks are managed in a consistent manner. This resulted in the roll-out of a standard operational risk register template and training is being delivered to services to ensure it is implemented effectively. All National Fraud Initiative matches, including lower priority matches, have been investigated and resolved, resulting in no proven cases of fraud. As a result of the internal audit programme delivered in 2008-09, the overall Head of Internal Audit opinion confirmed that "key systems are operating soundly and that there are no fundamental breakdown of controls resulting in material discrepancy".

Theme 3: The management of natural resources, assets and people

- 3.12 The Council has adequate arrangements in place to make effective use of its natural resources, with well established policies and procedures, and targets set to reduce resource use. However, the Council has focussed its targets and measuring its use of natural resources principally on its main civic centre offices and has not considered, in sufficient detail, other buildings where energy use is also high, such as leisure centres, due to a lack of information. In order to develop its arrangements further to move towards a level 3, the Council needs to take a wider view of its resource use and demonstrate outcomes across all of its buildings.
- 3.13 The Council has appropriate arrangements in place to manage its workforce, with good examples of initiatives in place to develop its workforce, manage its staff effectively and establish robust working practices. The Council is active in reviewing workforce requirements and annually prepares information to members on the workforce profile to the Council and future implications, including comparisons with other bodies. Our assessment of the Council's workforce arrangements has not been updated in 2009-10, and the 2008-09 score at level 2 brought forward, in accordance with the approach mandated by the Audit Commission.

Reporting

- 3.14 We will provide a more detailed report, setting out the findings and recommendations arising from our review, once our work has been completed and the quality assurance process has concluded, in late summer 2010.

A Action plan - interim accounts audit

Rec. No.	Para. Ref.	Recommendation	Priority	Management response	Implementation date & responsibility
1	2.10	<p>Internal audit</p> <p>Each test carried out by Internal Audit which utilises a sampling approach should include an explanation of the reason why that approach is the most appropriate and a justification for the number of items selected for further testing.</p>	M	Agree	<p>Head of Audit</p> <p>With immediate effect</p>
2	2.15	<p>User administrative access</p> <p>Management should consider the feasibility of removing powerful administrative access from operational users of COA eFinancials to ensure appropriate segregation of duties is maintained in the system.</p> <p>If this is not feasible, then management should consider monitoring the actions performed by the administrator accounts to ensure actions performed are appropriate and authorised.</p>	H	<p>Although in a District Council, it is not feasible to separate the Administration role from Operational Roles, we have already set up two access names for those users who require greater access. We will remind staff of the importance of using the correct access and explore ways of spot-checking the use of the administrator access to ensure that it is not used for operational purposes.</p>	<p>Corporate Finance Manager</p> <p>September 2010</p>

Rec. No.	Para. Ref.	Recommendation	Priority	Management response	Implementation date & responsibility
3	2.17	<p>User access reviews</p> <p>Management should consider implementing a process to review user access to the COA eFinancials application on a regular basis to ensure access is appropriate based on job functions.</p>	M	Agreed	<p>Corporate Finance Manager</p> <p>June 2010</p>
4	2.18	<p>Regular leaver listings</p> <p>Management should implement a review process to ensure that access has been appropriately removed by each system administrator in a timely manner.</p>	L	<p>Agreed. The systems administrator will undertake regular monitoring to ensure leavers are removed promptly.</p> <p>Please note that as part of their auditing testing, Internal Audit check that current listed users are still valid.</p>	<p>Corporate Finance Manager</p> <p>With immediate effect</p>
5	2.21	<p>Journal entry controls</p> <p>As recommended in 2008-09, the Council should introduce a requirement for independent approval of journals above pre-determined thresholds.</p>	M	We have attempted to achieve this, however, currently it appears that the system will only allow all authorised or none. We will seek to explore the possibility of a system development to achieve this.	<p>Service Finance Manager</p> <p>October 2010</p>

B Use of resources - underlying principles

Level 2 - performance adequately	Level 3 - performs well	Level 4 - performs excellently
Arrangements consistent with established professional practice and guidance, meet statutory requirements and operate effectively.	Implemented effective arrangements that are: <ul style="list-style-type: none"> • forward looking and proactive in identifying and developing opportunities for improvement; and • include more sophisticated measuring and assessment techniques. 	Demonstrating innovation or best practice .
Arrangements sufficient to address the KLoE.	Outputs and outcomes demonstrate arrangements which are effective and have the intended impact , and show evidence of effective partnership working .	Demonstrating strong outcomes for the community including through partnership working .
Arrangements achieve minimum acceptable levels of performance .	Evidence of performing consistently above minimum acceptable levels and achieving VFM .	Evidence of performing well above minimum acceptable levels and achieving excellent VFM .



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