

HERTFORDSHIRE COUNTY COUNCIL

**INTERNAL AUDIT
ANNUAL REPORT**

2003/04

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Internal Audit
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INVESTOR IN PEOPLE

Hertfordshire County Council

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INTRODUCTION

This Annual Report brings together, service by service, the main issues we have raised in the course of our 2003/4 audit work. Wherever possible, it also outlines management's responses and actions taken to address our recommendations. We now follow up all audits to check on the implementation of agreed actions.

It is intended particularly for senior management and the Audit Committee, and to provide the Audit Commission with summaries of the work on which they may wish to place reliance.

All of the audits summarised here have been formally reported to the relevant managers, and I would like to thank all of them for being receptive to our comments and recommendations.

The following paragraphs set out the key messages emerging from our 2003/4 work.

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KEY MESSAGES

System of internal control

Under the Accounts and Audit Regulations 2003, the Council is required, for the first time, to undertake an annual review of the effectiveness of its system of internal control. The authority must also include a statement on internal control with its financial statements at the year-end, starting with the 2003/4 accounts. The Regulations define the system of internal control as one which “facilitates the effective exercise of [the Council’s] functions and which includes arrangements for the management of risk”.

We have undertaken this review, with the involvement of the Monitoring Officer, Finance Director and other key staff. We are reporting on it separately to the June 2004 Audit Committee. We found that, in all key respects, the Council’s system of internal control was sound, with no major issues requiring formal identification for corrective action.

This Internal Audit Annual Report also provides an independent opinion on the adequacy and effectiveness of the Council’s system of financial control, including in particular:

- the key controls operating within and around the core financial systems
- high level financial management in each Department and corporately
- arrangements for the letting and monitoring of contracts
- controls over information management and security.

In the Chief Internal Auditor’s opinion, the above arrangements were adequate and effective in 2003/04, with sound controls in all key areas.

This opinion is based on a programme of audit work which was delivered:

- in accordance with the approved Audit Plan, (of which well over 90% was delivered), which in turn resulted from the systematic risk assessment of all auditable areas
- by suitably experienced and qualified auditors
- in accordance with the CIPFA Code of Practice for Internal Audit in Local Government
- to standards that have been reviewed and approved by the Audit Commission acting as external auditors.

Risk management

Through 2003/04, Internal Audit worked closely with the Head of Risk Management on the continued refinement of risk management arrangements. This included:

- operation of a process, approved by the Cabinet, for the involvement of members in the annual identification and ongoing management of risk
- identification and assessment, through the Finance Board, of the key risks currently faced by services and the measures being taken to mitigate them.
- sharing of Internal Audit's own assessment of key risks
- attendance at the Safety and Risk Management Board.

SHARP and SAP

SHARP, the major project for Simplifying Hertfordshire's Accounting and Resource Processes, involved significant internal audit work, briefly summarised under Corporate Services below. The project's key output was the successful implementation, on 5 April 2004, of the SAP resource management system for both Finance and for Human Resources/Payroll.

The new system was accompanied by considerable changes in procurement, accounting and HR processes, and we both monitored and participated in the system development, policy agreement, training and documentation that these entailed. There was huge commitment from the dedicated SHARP team and from many other staff, and the project was managed in a highly professional and effective way.

Inevitably, some issues remain to be resolved – indeed SAP will provide the means whereby a number of control issues will be addressed or improved. Nevertheless, the opportunity was taken to resolve some long-standing anomalies in the “legacy” systems, and to improve the Council's financial position. The Council also succeeded in keeping the key existing financial systems operational, and well controlled in all key respects, despite the heavy demands on staff resources in the period leading up to the implementation of SAP.

Financial management in Departments

For each Department, we once again undertook an audit of the overall financial management arrangements. These were sound in all key respects. We found:

- strengthened budget monitoring, particularly in Children, Schools and Families, and active management of volatile and demand-led budgets
- effective measures leading to the reduction of older outstanding debts
- good responsiveness to the demands of legislative change
- some work understandably awaiting SAP implementation, such as revised schemes of delegation, and the agreeing of authorised signatories
- the bedding-in of previous major change, although with, in some cases, more work to do.

Our opinion was also informed by the findings of our many other service-based audits, which showed financial management to be generally of high quality, with no major weaknesses.

Procurement

With the development of a strategic approach to the procurement of goods and services, the Council continued to implement a programme of significant change in an effective manner. We contributed through our audits, and through processes such as development workshops, to considerable improvements in the ways that key supplier relationships were managed.

The procurement module of the SHARP project introduced new and efficient mechanisms – such as purchasing cards, supplier web sites, and electronic catalogues – in a well-controlled way. The development of a “purchasing gateway” for all procurement other than through “authorised systems” (mainly for specialised services commissioned by Departments) should significantly improve the economies of scale and efficiencies of processing for the Council.

Partnerships

The introduction of innovative partnering and collaboration with major contractors and other bodies continued to demand significant changes in working practices. In the Property alliance, in Hertfordshire Highways, and in the Health Partnerships, we often identified the need for:

- improved communication processes between the parties
- better data and more fully developed information technology
- clear definitions of roles and responsibilities
- fully documented processes.

Nevertheless, there were many cases of successful partnership working, including the framework agreements with strategic contractors, and challenges were being effectively met and problems overcome.

Information and Communications Technology

We continued to both input to and monitor Project Sharp and the implementation of SAP. We concentrated on both the progress made within the project itself, and the impact on internal control arising from the transfer of procedures from the superseded systems. To this end, our final work on the legacy mainframe services highlighted areas to be considered in respect of services HCC expect in the future.

Computer Audit reviewed the controls in and around a large number of departmental systems, and found no issues of major concern. The introduction of arrangements

for the corporate control of the acquisition and support of software had also been well managed.

Security around the data communications links between Health Partnership Trusts and HCC was sound. We observed that the processes of information sharing with external parties required a formalised approach, and acknowledged that this had already been recognised as needing particular attention, with a protocol being developed.

Anti-fraud and corruption work

As in previous years, we undertook a wide range of work designed to detect or minimise the risk of fraud or corruption. In many cases, this work was integrated into our systems audits, and involved a range of computer-aided audit techniques. Such work included:

- conclusion of the Audit Commission's 2002 national data-matching exercise, through which we identified some £8,000 in overpaid pensions
- analytical review of the payroll and creditors systems to test for irregular payments
- targeted testing of expenses claims
- an audit of the use of business cards
- testing of debt write-offs and other adjustments
- checks at establishments on the handling of clients' cash and property
- analytical review and investigation of apparent school meals income shortfalls.

The principal cases requiring detailed investigations were:

- three suspected creditor cheque frauds, each of just below £10,000
- the suspected fraudulent claiming of a residence order allowance totalling over £10,000.

In all appropriate cases, we referred our findings to the police. Wherever possible, we ensured that losses were recovered.

The broader Internal Audit role

In addition to the work outlined above, we contributed to a range of corporate activities, including:

- co-ordination and validation of performance indicators
- contributing to the second national Comprehensive Performance Assessment, which again resulted in the Council being evaluated as "excellent", with Internal Audit achieving the maximum score
- acting as lead officer for, and reporting to, the Audit Committee

- chairing the Finance Board
- regular liaison with the Audit Commission's local external audit team.

We delivered audits for a number of external clients, including in particular Hertfordshire Police Authority and Connexions.

GLOSSARY

The following definitions cover some of the audit terms and abbreviations used most frequently in this Annual Report.

BCP	<i>Business Continuity Plan: a plan for the continuation of a service following a disaster or other major interruption</i>
Best Value	<i>A framework required by legislation, designed to secure continuous improvement through an annual BV Performance Plan, and a review programme focussing on national and local priorities</i>
BVPI	<i>Best Value performance indicator</i>
CPA	<i>Comprehensive Performance Assessment: an in-depth assessment by government of Councils' performance and governance arrangements</i>
Core financial system	<i>A computerised or other process fundamental to the operation of the authority's financial affairs</i>
Corporate governance	<i>The arrangements by which organisations direct and control their functions, and (in local government) relate to their communities</i>
Corruption	<i>The offering, giving, soliciting or acceptance of an inducement or reward which may influence the actions of the Council, its members or its officers</i>
Data matching	<i>Comparison using computer techniques of different sets of information, from within the Council or from other bodies, designed to detect possible fraud</i>
Fraud	<i>The intentional distortion of financial records, carried out to conceal the misappropriation of assets or otherwise for gain</i>
ICT	<i>Information and Communications Technology</i>

Internal control	<i>A procedure which ensures that an organisation's objectives are properly and efficiently carried out</i>
Irregularity	<i>An improper or erroneous use of the Council's resources</i>
Key controls	<i>Those processes most likely to prevent or detect material errors or other irregularities</i>
Legacy system	<i>A system which has been superseded, but which holds data which continues to need to be accessible</i>
Pre-implementation review	<i>An audit of a computerised or other system shortly before its live operation</i>
Risk assessment	<i>A systematic process for assessing the probability of material error, loss or irregularity in an activity</i>
SHARP	<i>A project aimed at Simplifying Hertfordshire's Accounting and Resource Processes</i>
SAP	<i>A comprehensive computer system, known as an enterprise resource planning package, for managing finance and other key resources</i>
Substantive test	<i>An audit check of sufficient numbers of transactions or records to give a good level of confidence in their completeness, accuracy and validity</i>
Systems audit	<i>An audit approach involving the documentation, evaluation and testing of controls within a financial process</i>

WORK IN DEPARTMENTS

ADULT CARE SERVICES

Our review of **financial management** within the Department confirmed that the main financial controls were operating well. As in previous years, a comprehensive budget pack, which includes departmental schemes of delegation, was produced and made available to budget holders early in the year. The large volatile budgets have action plans in place and continue to be closely monitored in order that, as far as is possible, overspending is contained. In particular, budget provision of over £2million relating to the estimated impact of the loss on residential allowances has been clarified and will be compensated by way of specific grant. There has also been resolution of some old outstanding debts - in particular, £114,000 attributed to one home care client. The Department is currently reviewing outstanding debt, which as at 04/04/04 stood at £12.5million, £668,000 of which was over 9 months old. The department has not yet rolled out performance management agreements to all staff, but intends to implement a programme from April 2004.

Central systems

We are satisfied with the controls operating within the department with regard to the submission of the **Asylum Seekers grant claim** to the Home Office. We were pleased to see that the ACS Policy for Working with Asylum Seekers has recently been reviewed and updated and that, for adult asylum seekers, the payment recording and verification processes in place are improved and that authorisations are in accordance with the scheme of delegation.

Our review of **Direct Payments** to ACS clients found that the controls within the financial systems were adequate. We made a few minor recommendations relating to the checking of Financial Assessment Forms and monitoring of the accuracy and prompt return of clients' quarterly financial statements, all of which were accepted.

We are satisfied that appropriate provision is being made to ensure that the **SSIS** (Social Services Information Systems) technical infrastructure can be sustained until the system is replaced fully by **IRIS** (Integrated Recording and Information System) and the Health Partnership Trust systems.

Our computer audit group continued its watching brief involvement in the following IT systems:

- **IRIS**
- **FiLIS (Financial and Local Information system)**
- **Supporting People**

Commissioning

ACS procedures to ensure delivery of **Repairs and Maintenance** and **Disability Discrimination Act (DDA) requirements** were broadly satisfactory. Management information will be improved as will communication with the project sponsor.

Following our audit of **Delayed Discharge** arrangements, we are very satisfied with the systems in place to monitor clients and manage funding and welcome the innovative use of funds to find new solutions to provide suitable placements for clients who no longer need acute hospital beds.

We continued to monitor the **Partnership arrangements with the Heath Sector**.

We are also satisfied with the provision that has been made for secure **data communications links** between Health Partnership Trusts and HCC. Information sharing is recognised as needing particular attention and a protocol is under development.

We followed up earlier work on **Leonard Cheshire Homecare** and are pleased to note that this contract is working well.

After a pilot trial, **Electronic Monitoring** for homecare clients has proved very successful and has led to a great improvement in accuracy of billing.

Work done on the **Homeability Service** (now Integrated Equipment Service) is reported under the HBS section of Corporate Services.

The following table summarises our visits to **in-house Provider Units** and **Area Teams** in 2003/04:

Type of unit or area	Number of units/areas	
	Audited	Planned
Day Centres (Physically Disabled) Adults	1	1
Hostels (Physically Disabled) Adults	1	1
Hostels (Learning Disability) Adults	15	15
Staffed Group Homes and Housing Support Teams (Learning Disability) Adults	2	2
Day Centres (Learning Disability) Adults	4	4
Multi-Purpose Day Centres Adults	2	2
Area Elderly Physical Disability Teams	7	7
Area Community Learning Disability Teams	7	7
Total	39	39

In addition to carrying out audits of the in-house residential units and the Area Teams, we continued to deal with a number of general queries, particularly regarding the security of HCC and clients' cash and the recording of staff hours. All managers provided a full response to the concerns that we raised.

Consultancy

A number of the following ACS audits became consultancy work as the projects were in their infancy:

- **Berkhamstead Day Centre and Offices**
- **Community Hospitals projects**
- **Learning Disability Hostels**
- **Beds and Luton Trust**
- **Runwood Homes and Quantum Care, property projects**

We also continued our involvement in the **Western House** project, and during the year investigated the cause of the delay in starting the building work.

CHILDREN SCHOOLS AND FAMILIES

Our previous 2002/3 audit of departmental **financial management arrangements** had found that, while budget monitoring at the level of budget managers and the finance managers was good, there had been marked shortcomings in the reporting of the budget position to the CSF Board, Finance Director and Cabinet. Recommendations made in our 2002/3 report to address these issues were clearly implemented in 2003/4, when we found that reporting of the budget position was much improved. The CSF Board regularly received reports showing significant variances expected at the year-end, including those that were less certain (reported as 'areas of concern'). This information was shared with the Finance Director, and formed the basis of the reports to Cabinet.

The department has not, however, completed the revision of its Scheme of Delegation from the Chief Officer, nor reconciled its records of authorised signatories to those actually used by ITnet. In both areas, the impending change anticipated by the introduction of SAP, and the increase in workload that this created, were the reasons for postponing this work.

We found that the financial commitments represented by **Out County Placements** were very closely monitored, in an effort to achieve the most accurate budget outturn forecasts that can be produced for this major CSF budget. Our report contained only one recommendation – that better contract documentation be kept for placements. To date we still await a commitment from management to act on this.

Our follow up of our first audits of the **Quadrants** (in 2003/4) found their financial procedures to be much improved.

The audit of the bedding in of the **new property arrangements** with the consultants MACE and Mouchel Parkman demonstrated that the time needed for this process had been underestimated. There was a lack of clarity, particularly from the end user viewpoint, around the fixed fee arrangements and the use of framework contractors, which has subsequently been addressed. However, the implementation of Repairs and Maintenance within CSF, both planned and responsive, was well maintained and under control.

Schools

The following table summarises our coverage in the year:

School sector	Number of schools	
	Audited	Planned
Nursery	5	5
Primary	115	130
Middle	2	2
Secondary	40	42
Special	10	12
Total	172	191

Among the totals listed above we carried out audits at four schools that closed. These figures also include some twenty two schools that we judged presented higher than average risk for their type, and two that we had assessed as being in our highest risk category (and were therefore revisited sooner than the 'average' interval in all cases).

We continued to find that, apart from a small minority of cases, the standard of financial administration within schools was very good. We did, however, make recommendations to introduce controls or to improve these as necessary. Recommendations we most frequently made included:

- the need to highlight budget variances and to record the causes of these and actions taken in response, and sometimes for governors to more fully document their scrutiny of the budget position and decisions arising from this
- the need to review and update the schedule of financial delegation, governors' committee terms of reference, the register of pecuniary interests and financial policies (notably charging)

- reminding schools of the regulations for the signing of cheques (usually larger amounts or those payable to the Head)
- to address delays in banking receipts and the corresponding breach of insurance limits (although we acknowledge that there have been problems with the cash collection contract set-up for schools, that we have recently helped to resolve)
- the update of and checks on asset inventories
- better accounting for school trips, journeys and similar activities
- better checks between the cost of providing music tuition, the recharges from the Music Service, and the charges made to pupils
- the avoidance of occasional local payments to individuals who should properly have been treated as employees.

We try to ensure that our recommendations are not burdensome, and to remind schools that our focus is on 'ends rather than means', i.e. that we are prepared to consider alternative means of achieving financial control. We make verbal recommendations where we feel that the issue is not significant enough to warrant inclusion in our report. We are also prepared to reconsider any recommendations that schools find impractical or unnecessary, but such issues are normally resolved at the end of audit discussion of the audit findings.

In addition to carrying out scheduled school audits, we responded to many **enquiries for advice and guidance** in respect of issues affecting schools' financial administration.

One of the issues that occupied us during the year was interpretation of the requirements around the **Community Facilities powers** that legislation in 2002 gave governing bodies. We encountered a number of cases where schools were operating such **extended school activities**, and where we found that the school had not appreciated that any supplies or services made by the school to the activity attract VAT. Some schools may have to recover significant unpaid VAT for the activity.

Our colleagues in the School Funding Unit referred only one case where they identified significant issues with a secondary school's **Annual Accounting Return**. We addressed these issues, and later reviewed the school's procedures, which we found to be good.

We once again examined the procedures to ensure that **school budget share allocations** reach schools safely.

We reviewed the process for the **Transfer of Pupil, Financial and Payroll data** and recommended minor improvements relating to training and password control. We also recommended improvements in the documentation and training in relation to the **Schools' Online Admissions Service** and the administrative procedures relating to the **Special Educational Needs System**.

We were satisfied with the controls surrounding the proposed method for **Recharging Schools within SAP**, but recommended that greater awareness of security issues surrounding the **Schools' Local Finance Packages** be promoted.

We examined the **financial planning** practices in a few schools, and also their mechanisms for capturing and reporting **pupil number data**. We intend to extend the scope of our audits in 2003/4 to routinely cover these areas. To free time within audits for this, we shall develop control self-assessment guidance for schools, to allow us to reduce coverage in 'traditional' aspects of the audit where we judge this possible.

We have continued to receive reports from Hertfordshire Business Services (HBS) regarding schools where there is an **unexplained shortfall** between the income expected **for meals taken** and the corresponding amount actually banked. Wherever possible we look into these cases when we next carry out a scheduled audit of the school. They can often be explained often by data errors, or amounts of unreported debts that schools have still to recover from parents. We are reconsidering our approach to this problem for 2004/05 in order to find the most efficient and effective way of tackling it.

We carried out audits of the arrangements for the provision of **school meals** both under the corporate arrangements and where schools had opted for their own contract. The corporate CSF Service Level Agreement with HBS for the provision of school meals is out of date and will be updated.

The audit of **School Contracts** covered **cleaning, catering** and **grounds maintenance** contracts where the school had let its own contract rather than use the corporate arrangements. Although the number of schools in this category is currently very small, we identified a lack of awareness of the proper control of the procurement process. Training in procurement is available and, with reinforcement of documented procedures, future compliance should improve.

We became aware that a few schools, in the opinion of HBS, had fallen victim to 'sharp practice' on the part of salesmen dealing in **photocopier leases**. A handful of schools entered contracts that HBS regard as offering very poor value for money. These cases emphasise the need for some schools to be aware of proper contracting arrangements, and to heed the advice from the Authority on good purchasing practice.

Other provider units and teams

The following table summarises our routine visits to in-house Provider Units in the year:

Type of unit	Number of units	
	Audited	Planned
Education Support Centres	3	3
Community Homes, Children (incl. Family Assessment Unit)	8	8
Hostels for Children with learning disabilities	2	2
Total	13	13

Our audits of the community homes and hostels continued to focus on the high- risk areas of cash handling and security. In particular, we noted the following:

- cash payments, particularly pocket money payments to children at two units were poorly recorded
- security weaknesses – specifically inadequate maintenance of inventory records and safe registers, and poor back up of computer records at a number of Homes.

All managers provided a full response to the concerns that we raised.

Other CSF audits

Although we were generally satisfied with the controls around the contract with NTL under the **National Grid for Learning**, we had concerns about tender evaluation records and the use of the contractors' own unverified statistics as a basis for payment, which will be addressed.

The audit of **Education Workshops** (EWS) has led to steps being taken to ensure the regularisation of sub-contractors in use who were not on the HCC approved list. The operating basis of EWS and its sister body **Herts Media** will be clarified and properly documented.

Our finding that the **Homestart Scheme** required wider advertising to reach all families in need has been taken up.

The report on our audit of the **Asylum Seekers Grant claim** is being finalised.

About two years ago we received information that a child placed in the care of relatives under a Residence Order (which had begun in February 1998) had moved out in December 1999, but that her uncle had continued to claim the **Residence Order Allowance**. After gathering further information we referred this matter to the police. We allege that the uncle has wrongly received in excess of £10,000 over a 26 month period. The police have recently arrested and charged the uncle. We understand that they are now investigating an allegation that a second person was complicit in this.

During the year we also completed audits of:

- the financial systems and procedures within the **Schools Standards & Curriculum Division** based at Wheathampstead
- the **funding of providers of nursery places** to 3 and 4 year olds in the private, voluntary, and independent sectors
- the **Hospital and Home Education Service**
- budgets within the **Development and Directorate Divisions** (in the case of the former we have not yet received a response to our report, and in the case of the latter we hope to issue this by the end of May)
- the administration by the County Council of **endowments** made to Hertfordshire schools (we hope to issue this report by the end of May).

We will complete the audit of both mainstream and SEN **home-to-school transport** as soon as possible.

COMMUNITY INFORMATION

We carried out our annual review of the department's **Financial Management Arrangements** and made only minor recommendations regarding improvements to project control, the testing of business continuity planning and the control of financial monitoring information.

We agreed to a request from the Head of Finance for the Department not to carry out our planned audit of **Departmental Payroll Procedures**, in the light of the latest assessment of the impact of the introduction of SAP upon these.

Library services

We carried audits of the **Dacorum** and **Hertsmere Library Districts** (i.e. visits to the major units within each). Generally we found their financial administration to be

sound, notably control of their delegated budgets. No management response has been received to our report on the Hertsmere District (first issued in June 2003), despite repeated reminders. This follows the absence of any response to our report on the Stevenage District, first issued in November 2002. Management has said that the workload created by the introduction of SAP has not yet allowed time to deal with these outstanding reports.

Information and Communications Technology (ICT) Infrastructure

Our computer audit of the **ICT Infrastructure and Organisation** found well-structured procedures that allow for the maintenance of a **Central Application Portfolio** of authorised and supported applications & software. Departments are able to use this information to consider currently utilised solutions for new initiatives.

Our work on the **Legacy Mainframe Systems** highlighted areas to be considered in respect of services we expect in the future. This included 'software currency' being a standard contract review agenda item, and that consideration be given to providing advice and guidance for any reporting which spans SAP and 'old mainframe' data. Further recommendations concerned the reporting of system security exposures by users, and a formal control over requests for access to archived and 'dumped' data.

ICT Infrastructure has implemented a formal corporate process for managing **Change Control** to the technical infrastructure. However, controls on Information Systems are more disparate, and we have recommended that a unified approach to this be developed.

Our review of HCC's **Intranet Service - Connect** - found appropriate business continuity planning (BCP), support and change control measures in place. Our recommendations centred on improvements to the performance of the 'search' software used and the promotion of general feedback on the design.

The **IT Hardware Inventory management** review found that the accuracy of data is improving due to the introduction of the appropriate support procedures with ITnet and interaction with LANDesk. Our main recommendation was that BCP issues should be addressed.

We also reviewed the following areas:

- ◆ **External web hosting**
- ◆ **LANDesk**
- ◆ **Local Government On-line.**

Our work on the **SHARP** project and the implementation of **SAP** is covered under Corporate Services below.

CORPORATE SERVICES

We are generally satisfied with the **Financial Management** controls operating within the Corporate Services Department, and found that all of the key controls were operating well. Our review of the financial procedures in operation identified a few control weaknesses, most of which were expected to be addressed as part of the implementation of SAP (covered below). These included:

- schemes of delegation and sub-delegations
- the need for a departmental register of assets owned by the department
- authorised signatories listings – discrepancies in these were resolved, and arrangements were put in place to ensure that they do not recur.

Project SHARP and the SAP system

E.U. and U.K. legislation as well as local financial and contract regulations were observed throughout the **Project SHARP** (Simplifying Hertfordshire's Accounting and Resource Processes) programme, leading to the tendering and letting of a contract for the supply and running of an **SAP system**. We reviewed the evaluation criteria, attended the tender evaluation meeting, and were happy with the process which led to the selection of Logica CMG as the preferred supplier, using SAP technology.

We participated in the workshops during the Blueprint stage of the SAP development and contributed to the evaluation of draft procedures. A comprehensive training schedule was developed for SAP and is currently under way for staff, prioritised on a needs basis.

We provided audit input into many aspects of the project, and issued an interim report on the project prior to the go live date (5 April 2004). We found Project SHARP generally well managed, and the project team showed great commitment and drive in delivering the project on time. We did highlight some concerns that did not require immediate action, but which we will address in the early phases of our post-implementation work on SAP in 2004/5. These included:

- ◆ the completeness and adequacy of the data migration from the legacy systems
- ◆ the controls around the setting up of new vendors
- ◆ the effects of the changes in purchasing authorisation levels
- ◆ the adequacy of the user support arrangements
- ◆ the mechanism for adding, deleting and amending the access of system users

- ◆ the arrangements for monitoring the managed financial services contract.

HCC further negotiated with ITnet and Logica CMG for provision of the HR / Payroll service. This required re-negotiation of the existing contract with ITnet for **Managed Financial Services** to accommodate their use of SAP for the payroll service previously supplied using UNI2000. These variations were permissible under the original contract and we were provided with a copy of the signed variation.

Performance Indicators

We have continued to provide advice on the correct definitions of the statutory **Best Value Performance Indicators** (PI's). We corrected a number of PI's prior to submission to external audit. The external auditors have reported that the authority omitted the financial PI's initially from the Best Value Performance Plan as published on 30 June 2003. A few contextual PI's were also omitted; these and the financial BVPI's were all added as an addendum to the BVPP on the website. The external auditor has recommended that the Council review its quality assurance process again, in order to provide accurate PI outturn data earlier.

CORPORATE FINANCE

Much of our work was undertaken with a view to securing any required improvements as part of the implementation of SAP. The main issues that we identified are referred to below.

Budgetary Control and Financial Ledger

We considered **Budgetary Control** procedures in our Financial Management reviews of all Departments and were generally satisfied. Monthly reporting to Members was ongoing. Issues that we had raised in 2002/3 concerning CSF were largely resolved, and are referred to under CSF above.

We were generally satisfied with the controls operating within the **General Ledger**. Our review of the procedures in operation identified some minor control weaknesses relating to the prompt clearance of error suspense items, adherence to 2002/03 closedown timetable deadlines, and the adequacy of supporting documentation for a few paper journals.

We noted a general improvement in the priority given to **Balance Sheet Monitoring**. However, there were still a number of codes with balances over £10,000 which have shown no variation since March 2002. 70 cost centres had either inappropriate or no responsible officer allocated.

Discrepancies were still being found between HCC departments and ITnet's database of **Authorised Signatories**. This area is still being examined, as there is a need for a fundamental review to ensure that adequate authorisation and separation of duties are put in place for the revised processes, including SAP access and roles.

There was ineffective authority-wide co-ordination to guarantee that all available **Government Grants** were applied for and claimed within the time deadlines specified in the grant conditions. However, Economic and Community Development Unit were developing a website and purchasing new software to aid monitoring.

We were generally satisfied with the controls operating within the **Capital** section of Corporate Finance, in particular that the final output from the main accounting system was correctly presented in the Authority's Annual Statement of Accounts. We were also generally satisfied with the controls operating around **Specific Reserves**.

Bank and Cash

The recommendation on the clearing of the BACS rejects subledgers (from the 2002/03 **Bank Reconciliation** audit review) had not been dealt with, and was therefore repeated.

We were generally satisfied with the controls operating within the **Cashier** department relating to the Imprest account. Our review of the financial procedures in operation identified that the majority of the payments processed were sound and adequately approved, although the signature could often not be deciphered.

We dealt with 3 attempted **Cheques Frauds**, each for approximately £9k which were referred to the Police; in all instances the money was reimbursed to HCC by the Bank and they took responsibility for further action.

Prior to the migration of the **Imprest account** balances into SAP, the SHARP team checked all balances and bank accounts. We established that there were 22 unidentified accounts; these are being dealt with appropriately. ITnet's end of year process should include checking the reconciliation to the advance and the bank statement sent.

The review of the use of **Business Cards** to make purchases on behalf of HCC raised a number of significant concerns, including the fact that the majority of users had not signed the guidelines agreeing to abide by the rules for usage. We found a small number of Instances of inappropriate usage and authorisation. These have been referred to Service Departments for appropriate action and the tightening of controls.

Creditors

We were generally satisfied with the controls operating within the **Creditor payments** system. All payments for a full year were analysed during our Fraud detection matching, and this revealed a number of duplicate payments with a total overpayment value of £29,000. These were mainly due to fax and copy invoices being processed on another of the multiple vendor references for the supplier. Finance Managers in the relevant departments were asked to investigate the duplicate payments and seek repayment. We had hoped that the introduction of the SAP system would have been accompanied by a radical clean up of vendor data, but this has not been as fully completed as had originally been planned (around 30,000 vendor records have been reduced to around 18,000). There is scope for further improvement in the quality of the vendor database.

Debtors

We were generally satisfied with the controls and monitoring procedures for **Debtors**. The total value of debts has grown but the value of debt aged over 6 months has shown a decrease. At 31 March 2003, debts over nine months old amounted to £3.2m, but this had been reduced to £2.5m by 31 March 2004. Some of this reduction can be directly attributable to the clearance of old and small debts in preparation for the implementation of the SAP system, and to management action by the Finance Board. We were satisfied that managers were regularly reviewing the debt position, and no significant control issues were highlighted during our testing of the **Education Billing** and Homecare **Debtors**.

Payroll, Employee Benefits and Pensions

We were satisfied with the operation of the key **Payroll** controls within ITnet under the Unipay system. We undertook matching of Payroll records as part of our fraud detection work, and have notified ITnet of inconsistencies particularly in respect of National Insurance contributions codes. Staff who appeared to be working on two or more jobs with more than 48 aggregate working hours were being investigated by County Personnel.

We continue to be concerned at the delay in the reconciliation of the **Payroll Control Accounts** relating to the adjustments of pay. The net balance of the four codes exceeded £80,000. Until these are reconciled, we cannot give an absolutely assurance that all pay advances and deductions have been properly accounted for. The Assistant Finance Director is currently reviewing the actions to be taken by HCC and ITnet.

Our **Analytical Review** monitoring throughout the year did not identify any significant areas of concern, although it did clearly illustrate the decline in numbers

of weekly and fortnightly paid staff as expected, following single status and preparation for data migration to SAP.

We were generally satisfied that **Income Tax and National Insurance Contributions** were correctly collected on HCC's behalf by ITnet and paid to the Inland Revenue. However, we were concerned that the controls operating within ITnet did not prevent two legislative deadlines from being missed and that, following the annual input of employee tax codes as provided by the Inland Revenue, an error report listing over 200 unmatched records was not investigated.

We had concerns that the **Relocation** allowances scheme has been devolved to local personnel units without sufficient knowledge or detailed guidance. A separate scheme was required for overseas appointments. The eligibility to the applicable scheme also needed to be determined, and where appropriate justified, before a post was advertised.

We continued to provide management information on **Travel and Subsistence** payments made through payroll. This information will be available directly from the SAP system in future.

We have concluded the investigations following the Audit Commission **National Fraud Initiative** 2002; this identified the continued payment of pensions relating to five dead pensioners. The largest overpayment was £4.6k, out of a total of £8.2k. Recovery procedures had been put in place to reclaim the overpayments, but these have now been written-off.

We were generally satisfied that **Pensions** were being paid correctly. Our audit review was undertaken with due consideration to the impending changes within the section regarding the implementation of AXIS system which will generate the payments to Pensioners after April 2004. Computer Audit's review of the new **AXISe** Pensions system concentrated on the transition of pensions payroll data, and processes from UNIPAY to payment through AXISe.

We issued our report on the controls operated by **Capital International**, one of our Pension Fund Managers, to the other Counties who also have Pension Funds invested with them. Computer Audit undertook a brief review of the **Shareholder II** system. No system weaknesses were found; as only a few transactions are now recorded on this system, which has largely been superseded by the appointment of the Global Custodian ABN AMRO Mellon, it is no longer considered to be a significant computer system but it continues to provide limited management information.

COUNTY SECRETARY'S

We were generally satisfied with the controls within the **Coroners** financial systems, and were pleased to note the work that had been carried out to improve and document the systems. We were also satisfied with the management of the **Members' Allowance budgets and the Chairman's Fund**. We made a few minor recommendations, all of which have been accepted.

We also provided some advice on the re-letting of the **Legal Services Property Disposals** contract.

HERTFORDSHIRE BUSINESS SERVICES

We found the **overall financial management** arrangements at Hertfordshire Business Services (HBS) to be generally satisfactory, with only minor weaknesses. A review of business planning and budgetary monitoring is planned and should assist in improving the control environment.

The audit of the implementation of the **VISION** project (recommendations for the future of HBS, formerly County Supplies and Contract Services) found that all processes were continuously subject to measurement and review. The processes used by HBS to develop, communicate and implement the VISION project provide an excellent model for other parts of the council that are undergoing cultural changes and demands.

Computer Audit reviewed the methods in use to control the **Development of ICT Projects** and found good controls within HBS, but recommended improvement required in departments communications with Corporate ICT.

We carried out audits of both **Energy Management** (the responsibility of HBS) and of energy strategy (the province of Hertfordshire Property). The outgoing contractor had handed over the energy management information database in a very poor state of repair - this had led to a number of problems, which will be addressed.

In general, the arrangements, systems, processes and controls for implementing the **Vehicle Replacement Programme** are well structured and maintained. Our audit found, however, that the infrastructure surrounding the activities and subsequent implementation of the vehicle replacement programme remained largely informal and undocumented.

Computer Audit recommended minor improvements to access security around both the **Hertfordshire Reprographics Local Finance System** and the **Fleet Management System** and for the latter, the compilation of a business continuity plan.

The **Home Ability** function became the Integrated Equipment Service on 1st April 2004. We found that a proper project management approach had been taken, and recommended the introduction of realistic performance indicators and methods of measurement. A full audit of the new service is scheduled for 2004/5.

Our audit of the **Schools Catering** Service Level Agreements with the Contract Support Unit identified a number of weaknesses and learning points which will be addressed in the re-organisation of the schools catering arrangements.

The audits of both the **County Hall Post Room** and of **Facilities Management** at Mount Pleasant found only minor weaknesses, which have been addressed.

We audited the purchasing of suspended files under the **Central Buying Consortium** as an example of low value/high volume purchasing. The management of the purchasing, contract development and contract management systems and procedures was well controlled.

We were satisfied with the controls over the production and business development of the **HBS Catalogue**. HBS had made good use of sponsorships and other sources of income to support the printing and distribution of the catalogue.

The audit of the **Mobile Phone Contract** arrangements, which are tendered by the Office of Government Commerce, found that contract management was effective.

The monitoring of the **Wheathampstead Catering Contract** at the Development Centre, currently held by Catering Alliance, was well managed, helping to provide an efficient and cost effective service.

We are completing our work on **Impressions** and **Network Printing**.

PEOPLE AND PROPERTY

Corporate Personnel

There have been improvements both in the service provided by Manpower under the **Recruitment Centre contract** and in proper use of the contract being made by HCC departments.

The **Frizzelle Financial Advice** arrangement was found to be operating satisfactorily. We recommended minor improvements, which will be applied.

Our computer audit of the **Criminal Records Bureau** document tracking system (Checkpoint), indicated minor improvements required in the areas of technical documentation, change control, business continuity, and requirements concerning record retention.

Property

We were satisfied with the key controls operating in the Corporate Estates section of Herts Property to manage and monitor the contract with Lambert Smith Hampton as consultants for **Estates and Valuation**.

We undertook the following interim audits:

- **MACE for Design and Projects**
- **Property Care Mouchel**
- **Minor Works Mouchel**
- **Measured Term Contractors**
- **Property Trading Systems.**

The systems had not been in place long enough for a full evaluation, and the development of the performance measurement system and the project manual was still at draft stage. At the time of the audit, investment had not yet been made in developing or installing new software systems.

We also carried out reviews of the **IT-related aspects** of the new Property Services Contracts, namely:

- **MACE**
- **Mouchel**
- **Lambert Smith Hampton**

We carried out an interim audit of **Strategic Contractors and the Framework Agreements**. These were satisfactorily controlled.

We were satisfied with the controls in operation over **Facilities Management**, and also over the operation of the **Select List** and the **Contract Register**, although there were minor weaknesses in the subsidiary register.

The audit of the **Corporate Property Database** revealed a number of weaknesses, which are to be addressed.

Safety, Emergency and Risk Management Unit

Our audit risk analysis again included the results of corporate risk management. We contributed to the **SERM Board** and provided the results of our **Security** audit, which will be progressed.

ENVIRONMENT

Resources

The Department's **Overall Financial Management** arrangements were found to be generally satisfactory, subject to a few minor findings which will be addressed.

We are satisfied with the key controls operating within both the **Confirm System** and **HERMIS**, and made only minor recommendations regarding system access and back up.

Transport Management

We kept a watching brief on the tendering, evaluation and award of the Design and Build contract for the **Baldock By-Pass**. We were happy with the allocation of roles and responsibilities, the determination of project objectives and targets, and with the selection of contractors, tendering and award of the contract.

Our audit of the **Safety Camera Partnership** found that HCC procedures and financial controls were properly managed and maintained.

We continued our watching brief on the **Detrunking** process.

Hertfordshire Highways

In 2003/4, the Highways Agency and Highways Partnership arrangements with the district councils were ended and an Integrated Works Programme was introduced. At the same time cutting edge partnership arrangements were set up, with **Mouchel** (MTSC) consultants and **Amey Lafarge** (ALF) contractors co-locating with the council **client contract management** side in four new **Area Offices** and one **Strategic Office** under the designation **Hertfordshire Highways**. This new arrangement required both the introduction of new systems and the inculcation of a new culture. Initially there was a lack of clarity about the newly established system and many controls were not operating. As is typical during periods of substantial change, there was a dip in contract performance and operational difficulties.

We met with management to assist in developing strategies to improve communication and feedback, develop understanding of the contract, integrate systems between the partners in the Alliance, progress training, particularly in the use of HERMIS and to advance teamwork.

Our work on **Street Lighting** found improved performance, but problems remained with performance monitoring, long-term outages and stump removal. These are being addressed.

Strategy

At the request of the Director of Environment, two special audits of **Section 106 Agreements** were carried out in 2003/04. This provision of the Town and Country Planning Act 1990 governs contributions from developers towards the cost of additional improvements. The first audit was to determine whether the enforcement and implementation of such agreements was both effective and efficient. The second was a detailed study of the controls, authorisation, spending and monitoring processes for the agreements covering the **51 Clarendon Road** (Watford) and **Leavesden Park** developments (Three Rivers).

The Section 106 Report was reviewed by the Environment Scrutiny Committee on 21st October 2003, and highlighted some significant findings. The further unscheduled audit covering the two specific projects confirmed our earlier findings. As a result of these audits, the Environment Department instigated a formal project plan to address all the issues we raised. The results of an **update review** by Internal Audit were reported to the Audit Committee on 11th December 2003. We have subsequently carried out a further **follow-up** on the progress of the project plan.

The agreed actions resulting from the 2003/4 audit were carried forward into a works programme, and were completed according to schedule. Some have not yet been fully implemented and these comprise:

- implementing improvements to the financial monitoring system
- agreeing and issuing draft process documents
- exploring functionality of AMOS database after full population has been completed.

Nevertheless, there are clear and marked improvements to the S106 process that, once fully implemented, will improve the effectiveness and efficiency of the system.

EXTERNAL CLIENTS

Connexions

We provided an audit of **Connexions**, the consortium, of which HCC is a member, for the provision to young Hertfordshire people of access to information, advice, guidance and support.

We were generally satisfied with the accuracy and completeness of the processes for completing the monthly grant claim. Budgetary control during 2002/03 was satisfactory, although budgets for the current year had not been entered to Walker (the County's ledger system) at the time of the review (mid May 2003). The Service Level Agreements that have been created do not allow for the performance of the services to be effectively monitored, therefore we were not able to confirm that the grant monies have been spent in accordance with the Terms of Memorandum and the Grant Conditions. The Finance Manager was aware of this significant issue: performance indicators, monitoring and contract management are high priority areas for development over the next twelve months.

Herts Careers Service is the main sub-contracted delivery agent for Connexions Hertfordshire. We obtained satisfactory assurances from their external auditors that the company's financial accounting systems are adequate and can be relied upon.

Other Audits

We will report the internal audit service provided to our largest external client, the **Hertfordshire Police Authority**, to that body's Audit Panel. We will also report separately to the **Magistrates Courts Service** on our audit of that service.

The **not-for-profit organisations** whose final accounts we audited this year without charge were the Dimsdale Charity, Herts Charity for Deprived Children, Bowley Charity, Hertfordshire Association of Local Councils, and the HCC Staff Social Club.

FIRE & RESCUE

This year's audit of the Service's **financial management arrangements** found that previous recommendations had been implemented, namely:

- an annual review of charges
- a review of Balance Sheet codes
- the drawing-up of IT back-up procedures.

The Schedule of Delegation from the Chief Officer still requires some update, and the Service's Administration Manual has not been updated for several years (any review was postponed pending the introduction of SAP). Training on the Performance Management scheme has been undertaken, but no reviews have occurred. Business Continuity plans still do not cover support functions. Additional recommendations are made this year:

- to introduce a register of gifts and hospitality
- to create an inventory for (non-operational) service assets.

The audit of **Phase 2 of the Personal Protective Equipment Contract**, deferred from last year, found that stock records were insufficient and there was no independent monitoring of contract delivery. Stock control was such that we had to rely upon Ballycare records in order to monitor the contract.

Our audit of the management of the **St. Albans Fire Station** project found that there had been delays arising from pre-funding issues, and that communication between Hertfordshire Property, the consultant (MACE) and Hertfordshire Fire and Rescue had been poor or non-existent. These factors have led to further work in developing the use of the project management gateway system, and further training. Improved communication between Hertfordshire Property (HPS), the initial project sponsor, and the Fire and Rescue Service should improve project management.

All systems, **Repair and Maintenance** procedures and controls within Hertfordshire Fire and Rescue Service are satisfactory. There were, however, problems arising from procedures within and the management information supplied by the consultant, Mouchel Parkman. A performance measurement system is being instituted which should improve control over these areas. These are reported upon elsewhere in this report.

Our audit found that **Capital projects** would be better controlled by the use of a system to monitor and track the status and position of the project. Our audit recommendations should help in driving projects forward where slippage is incurred and make the stage of the gateway system reached clearer.

Control over the contract for **Fire Engines** was found to be good with monitoring being carried out by the Fire Service Procurement Association (FSPA). Minor improvements in cross-referencing documents within Herts Fire and Rescue Service were recommended.

We found the contract for the use of Hertfordshire Fire and Rescue Service facilities by **BSI** for testing fire extinguishers to be well controlled. Minor improvements in invoice administration have been recommended and are in-hand.

We were satisfied that the tendering, letting and implementation of the **Integrated Command and Control** system upgrade were properly controlled.

The Management Board of the **Commercial Training Unit** monitors its budget well and the Unit appears very successful. This audit also covered the **Training Unit**, and here too we found regular budget monitoring in evidence. We noted that training is provided to fire-fighters from other Counties, etc. but that the charges are not based on a costing of the courses in question. However, we recognise that it is arguable whether the calculation of costs (and therefore the charge) should be done on a marginal cost or full absorption basis.

Our audit of **charges and income** raised by the Service found that a comprehensive policy exists for charging for 'special services' (e.g. pumping out of premises, etc), and the decision whether to charge for such services is reviewed in each case up to the level of Divisional Officer. Generally we found the controls applied over the sources of income we covered in the audit to be sound. We made recommendations to tighten controls over the only significant source of cash income – the canteen facility in Hertford.