



INTERNAL AUDIT REPORT



FINANCIAL RESILIENCE 2015/16

Issue Date:	First draft: 09/11/2015 Final draft: 28/04/2016 Final report: 04/05/2016	Issued to:	Simon Riley, Head of Finance & Commercial Services
Author:	Trevor Croote		Beverley Jolly, Corporate Director (Resources) <i>Cllr Grahame Spendlove-Mason, Chair of Governance and Audit Committee (final report only)</i>



FINANCIAL RESILIENCE 2015/16

EXECUTIVE SUMMARY

1. Introduction and overall opinion

Most councils are dealing with significant financial pressures resulting from ongoing reductions in government funding and rising service demand. Consequently, robust financial plans and governance arrangements are essential to ensure resources are effectively managed and prioritised.

Based upon the review conducted by Internal Audit, the Council’s financial planning arrangements have been assessed as sound. Procedures are in place to ensure that the leadership team has a clear understanding of the financial challenges facing the Council and appropriate arrangements are in place to prepare financial plans that are clear and robust. Financial planning is fully integrated with corporate and business planning processes and the level of balances and reserves is reviewed annually based on risk. Financial planning arrangements could be further strengthened through additional training and review of the format and content of team plans and financial reports.

The Council has a good track record of managing its overall spending within budget and has effective arrangements for monitoring and reporting its financial position during the course of the year. The recent introduction of new financial reporting tools meant that the quarter one financial position for 2015/16 was not reported, but action has been taken to ensure that future reports are complete and timely.

There are robust arrangements in place to identify opportunities for efficiency savings at service level which could be further strengthened through the development of mechanisms to identify cross-cutting savings.

Based on these findings, the framework of controls currently in place provide **Sufficient Assurance** that the identified risks have been appropriately mitigated. Detailed findings are set out in section 2 below. The audit was carried out in line with the scope set out in the approved audit planning record (APR). The assurance opinion is based upon testing of the design of controls to manage the identified risks and testing to confirm the extent of compliance with those controls, as summarised in Table 1 below.

Table 1 – Assurance opinion

Internal Audit Assurance Opinion	Direction of Travel				
Sufficient Assurance	N/A				
Risk	Design	Comply	Recommendations		
			H	M	L
Risk 1 - Weak or ineffective financial plans and governance arrangements.	Sufficient Assurance	Substantial Assurance	0	2	2
Risk 2 - Weak or ineffective financial control arrangements.	Substantial Assurance	Sufficient Assurance	0	0	0
Risk 3 - Inadequate arrangements for identification and delivery of efficiency and productivity improvements.	Sufficient Assurance	Substantial Assurance	0	1	0
Total Number of Recommendations			0	3	2

2. Summary of findings



Risk 1: Weak or ineffective financial plans and governance arrangements.

Management asserted that the leadership team is fully engaged in the budget setting process and understands the financial challenges of the Council. This is achieved through the delivery of various presentations and reports at corporate management team (CMT), strategy board, executive meetings and member workshops providing a range of information such as the forecast budget gap, key financial risks and opportunities.

The Head of Finance and Commercial Services (section 151 Officer) is a permanent member of CMT and involved in all key business decisions. A deputy section 151 officer has also been nominated and attends CMT as a substitute if necessary. Both the section 151 officer and deputy have suitable professional accountancy qualifications and extensive experience of local government finance.

There are several opportunities for the leadership team to scrutinise budget plans through the portfolio challenge and business and budget planning workshops. Budget plans and proposals are also subject to review by CMT as part of the budget setting process and review and sign-off of committee reports. Formal budget proposals go to the Resources and Performance Scrutiny Panel, Executive and Full Council for approval.

High level mandatory finance training is provided to Members as part of their initial induction, although not all members attended the training after the May 2015 elections. No other formal finance training was planned at the time of audit; reliance is placed on clear and transparent presentation of financial information by the Head of Finance and Commercial Services (HoF&CS). Without sufficient finance training there is an increased risk that Members will not have the necessary knowledge or confidence to effectively challenge or scrutinise financial plans. **Recommendation 1** addresses this issue.

Governance and Audit Committee has limited involvement in scrutinising financial plans but is responsible for approving the annual financial statements. A training programme for members of the committee covering audit and assurance issues was approved in September 2015 but no specific training is planned in respect of the statement of accounts. However, the HoF&CS has agreed to consider options for ensuring members of the committee are sufficiently briefed prior to consideration of the 2015/16 financial statements in September 2016.

The Council's medium term financial strategy (MTFS) was last updated and approved in August 2013 and covered a three year period from 2014-15 to 2016-17. Whilst the MTFS was not update last year, underlying forecasts and financial models remain in place and the MTFS is due to be updated and published following the outcome of the comprehensive spending review in December. The HoF&CS asserted that, whilst there is limited overall scenario and sensitivity analysis in the formal MTFS or budget reports, certain high risk and volatile elements of the budget such as the New Homes Bonus and Business Rates are subject to detailed modelling and scenario planning at an operational level. The inclusion of scenario and sensitivity analysis in formal reports and plans would further improve transparency in relation to the financial impact of certain decisions and assumptions (see **recommendation 3**).

Financial planning is fully integrated with corporate and business planning processes. The corporate plan, delivery plan and service plans are all reviewed and updated annually alongside the budget setting process. Budget and



business planning workshops are held each year and there are clear and transparent links between revenue, capital and treasury management plans.

The annual budget is underpinned by a number of financial assumptions such as inflation rates, pay awards, pension contribution increases, contractual price reviews etc. Officers asserted that all assumptions are based on the best available information at the time the budget is prepared and that contingencies are built into the budget only where necessary.

Balances and reserves are reviewed on an annual basis and the Council has a policy to maintain a General Fund (GF) balance in the range of 7.5% - 15% of net revenue expenditure. Total balances are currently in the region of £10m, of which approximately £3.5m is represented by the General Fund and the remainder is in earmarked and capital reserves. The GF balance at 31st March 2015 was £3.748m, which equates to 31.3% of net revenue expenditure; well above the recommended range. The 2015/16 budget report indicates that it is considered prudent to retain relatively high levels of reserves at this time due to the uncertainty over future government funding and other income streams. In addition, management asserted that the GF balance was distorted in 2014/15 due to the transitional aspects of accounting for business rates retention and is expected reduce next year. Analysis of key financial ratios in comparison with its CIPFA family group indicates that the level of reserves is comparable with similar councils (see appendix 2).

The annual review and recommended level of reserves is based on the professional judgement of the HoF&CS linked to the key risks and uncertainties facing the Council. However, the annual budget report does not currently provide a direct link between the related risks and the level of each reserve. Development of a more detailed annual review based on best practice principles would improve clarity and provide Members and other stakeholders with a clearer picture of the purpose and basis for each reserve (see **recommendation 4**).

Based upon these findings, the rating for the design of controls in respect of this risk is **sufficient assurance**.

Review of CMT minutes and reports for the last 12 months confirmed attendance by the section 151 Officer or deputy and that finance and budget issues are regularly discussed with specific agenda items on budget and business planning and financial monitoring. Review of budget reports and last year's MTFS provide evidence of a very clear analysis and assessment of the key financial drivers and risks associated with the budget; which are set out in a logical and easy to understand manner.

All 2015/16 team plans had been reviewed and updated, although there was no evidence of inclusion of financial aspects such as the team/service budgets, cost pressures, efficiency plans or growth items. Inclusion of financial information in team plans would improve transparency and provide a clearer link between service objectives and the financial consequences. **Recommendation 2** addresses this issue.

Review and assessment of a sample of budget assumptions confirmed that they were supported by appropriate evidence. The 2015/16 budget report provides evidence that a review of the level of reserves has been undertaken although, as stated above, there is no detailed analysis of the nature and basis for each individual reserve (see **recommendation 4**). Initial proposals included the use of £14k of the GF balance on a recurrent basis. A subsequent decision to reduce council tax by 5% increased the use of reserves by £242k. However, it is recognised that the



ongoing use of reserves to support recurring expenditure is unsustainable in the long term and the 2016/17 budget is being prepared with the intention of eliminating any reliance on reserves going forward.

Based upon these findings, the rating for compliance with controls in respect of this risk is **substantial assurance**.

Risk 2: Weak or ineffective financial control arrangements.

Budget holders and service managers have access to 'live' data showing performance against their budgets on an ongoing basis and the HoF&CS has access to all budgets. Financial performance is scrutinised by CMT through monthly review of financial highlights reports and formal budget monitoring reports are prepared and presented to Resources and Performance Scrutiny Panel and Executive on a quarterly basis.

Officers asserted that the Council has a good track-record of managing its expenditure within budget and usually under-spend by around 5% each year. Most underspends are planned and managed rather than unexpected last-minute variances and are treated as a windfall rather than relied upon to bridge any structural budget gaps. Whilst managed underspends are useful in mitigating risks associated with some of the more volatile budgets, it is recognised that minimising variances through accurate initial budgeting and realistic forecasts provides a firmer foundation for long term financial management.

Although not routinely reported as part of quarterly financial monitoring reports, the Council has established a range of targets for the collection of material categories of income and arrears such as council tax, business rates, sundry debtors and housing benefit overpayments. These are regularly monitored and reviewed as part of the Council's performance management framework.

Based upon these findings, the rating for the design of controls in respect of this risk is **substantial assurance**.

Review of 2013/14 and 2014/15 outturn reports confirmed that overall spending has remained within budget in recent years, with an overall reported underspend in the region of 5% - 6%.

Review of minutes of Scrutiny and Executive confirmed presentation of quarterly monitoring reports with the exception of quarter one for 2015/16. Officers asserted that the report was not presented as information submitted by budget holders was incomplete and it was not possible to recreate historical financial reports within the Collaborative Planning tool. The HoF&CS stated that this issue has been addressed by ensuring that an extract is taken from the system at the appropriate time and through the adoption of a business partnering approach between finance and budget managers. Internal Audit was advised that preparation of the 2015/16 second quarter monitoring report is on track.

Testing confirmed that quarterly finance reports do not include details of performance against income targets although some are reported to the Resource & Performance Scrutiny Committee as part of the collection and reporting of key performance indicators. Review of the performance monitoring system identified performance indicators and targets for the following:

- Net income from treasury management



- Sundry debt arrears
- In-year council tax collection rate
- HB overpayment collection rate
- Council Tax arrears at year-end
- NDR arrears at year-end
- In-year NDR collection rate
- Recovery rate for off-street parking penalty charges
- Symington building income

Based upon these findings, the rating for compliance with controls in respect of this risk is **sufficient assurance**.

Risk 3: Inadequate arrangements for identification and delivery of efficiency and productivity improvements.

Efficiency savings are identified primarily through the annual portfolio challenge process. Separate meetings are held for each service area involving the relevant director, service manager and portfolio holder. A range of data and information is used to inform the portfolio challenge process, including current service objectives, performance levels, service pressures and benchmarking data, where available. The outcome of the meetings is collated and scrutinised by CMT and feeds into the business and budget planning process. Agreed efficiency savings are built into base budgets and are not subject to separate monitoring or reporting, unless specifically requested.

Whilst the portfolio challenge process provides a sound basis for the identification of service specific efficiency savings, it is less likely to identify opportunities for cross-cutting or corporate efficiencies. **Recommendation 5** addresses this issue.

The Council is currently in the process of producing a corporate efficiency plan and implementation plan. Work has started on this with portfolio holders with a completion date of September 2016.

Based upon these findings, the rating for the design of controls in respect of this risk is **sufficient assurance**.

Portfolio challenge meeting notes for both the 2015/16 and 2016/17 processes were reviewed. Sufficient evidence was seen to provide assurance of the effective operation and management of the process. A standard agenda is used and data templates are prepared covering the following areas:

- Service objectives, values & outcomes
- Key performance indicators and existing budgets
- Analytical review
- VFM & benchmarking information
- Commitments, risks & opportunities
- Future shape of the service including legislative changes and demand pressures
- Innovation & service redesign opportunities
- Summary of outcomes, including savings proposals

Review of CMT minutes confirmed that the leadership team reviews and scrutinises the outcomes of the portfolio challenge process, particularly the savings and growth proposals, before they are taken forward into the business and budget planning process.



Based upon these findings, the assurance rating for compliance with controls in respect of this risk is ***substantial assurance***.

The action plan (appendix 1) provides a number of recommendations to address the findings identified by the audit. If accepted and implemented, these should positively improve the control environment and aid the Council in effectively managing its risks.

3. Limitations to the scope of the audit

This is an assurance piece of work and an opinion is provided on the effectiveness of arrangements for managing only the risks specified in the Audit Planning Record. The audit focused on the robustness of financial plans and adopted a relatively light-touch approach and high level review in respect of financial controls (risk 2) and management of efficiency savings (risk 3). A detailed review of financial management arrangement and efficiency plans was outside of the scope of this audit.

The Auditor's work does not provide any guarantee against material errors, loss or fraud. It does not provide absolute assurance that material error, loss or fraud does not exist.

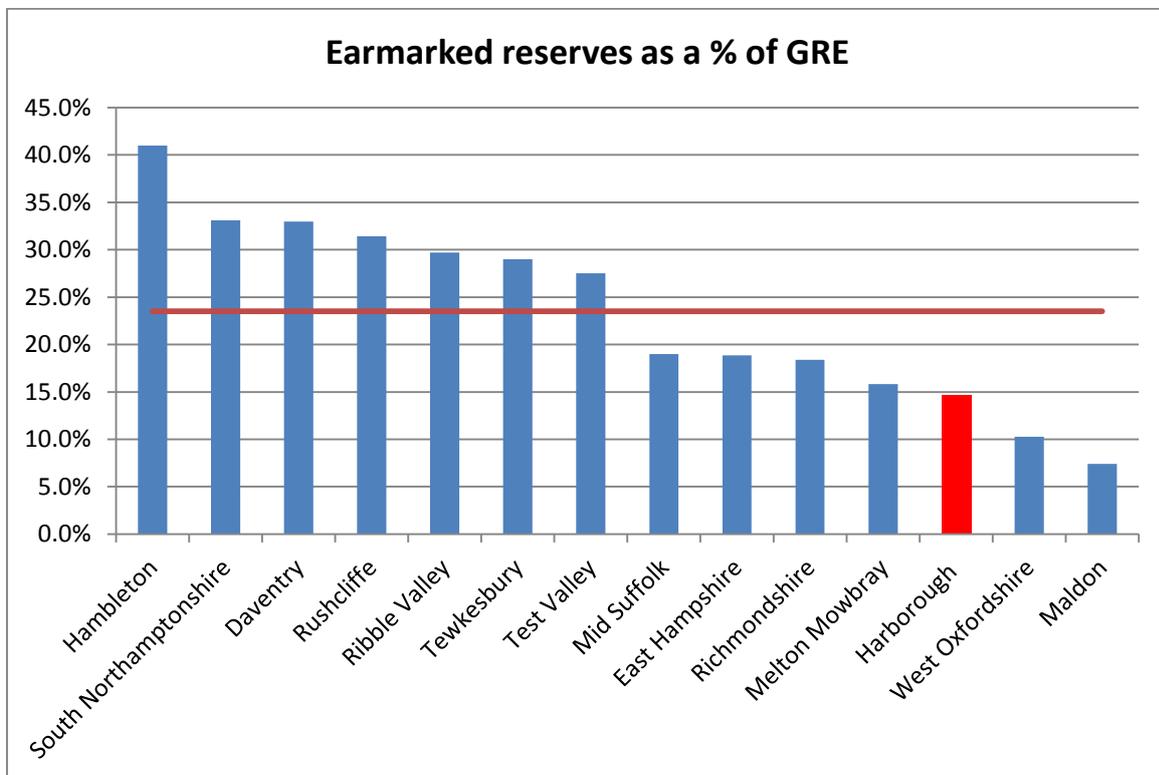
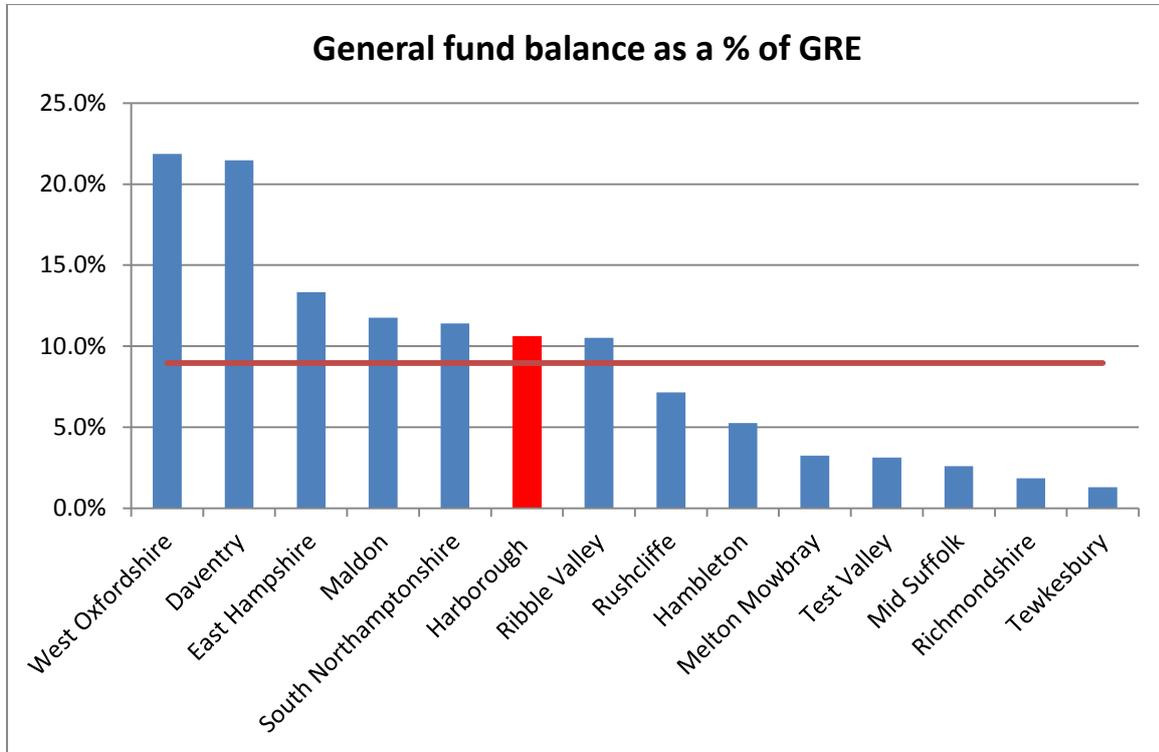
Appendix 1

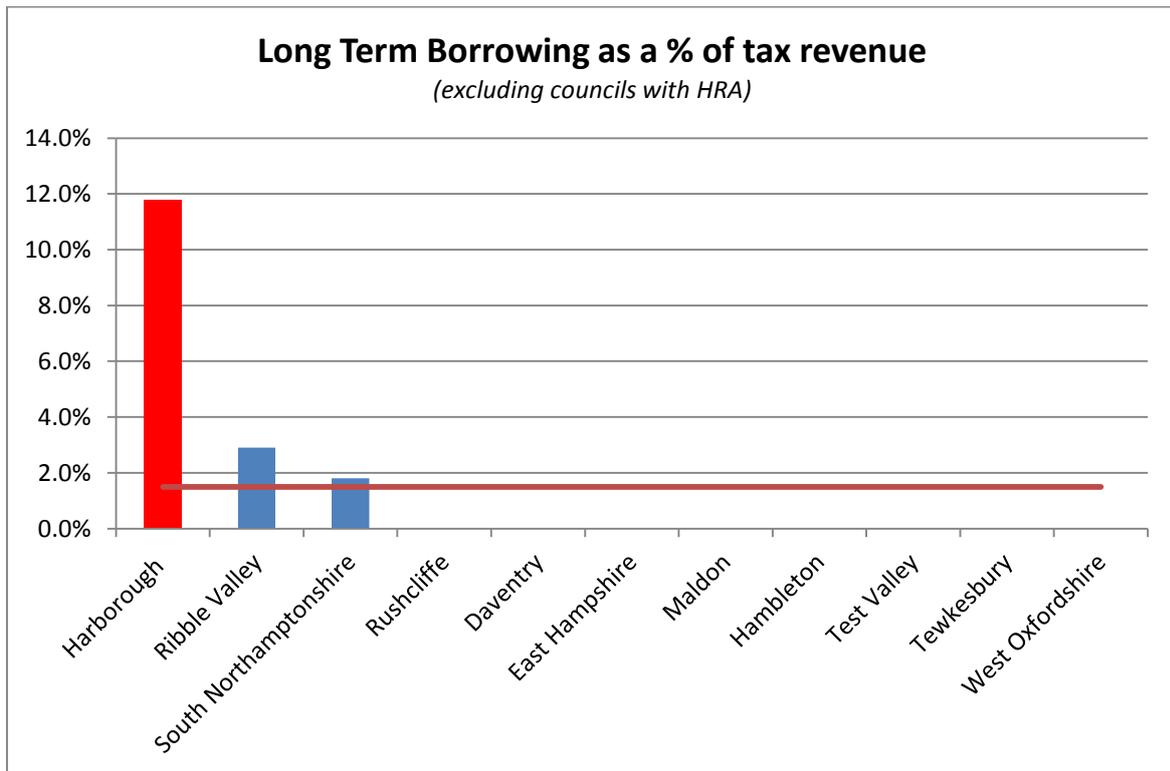
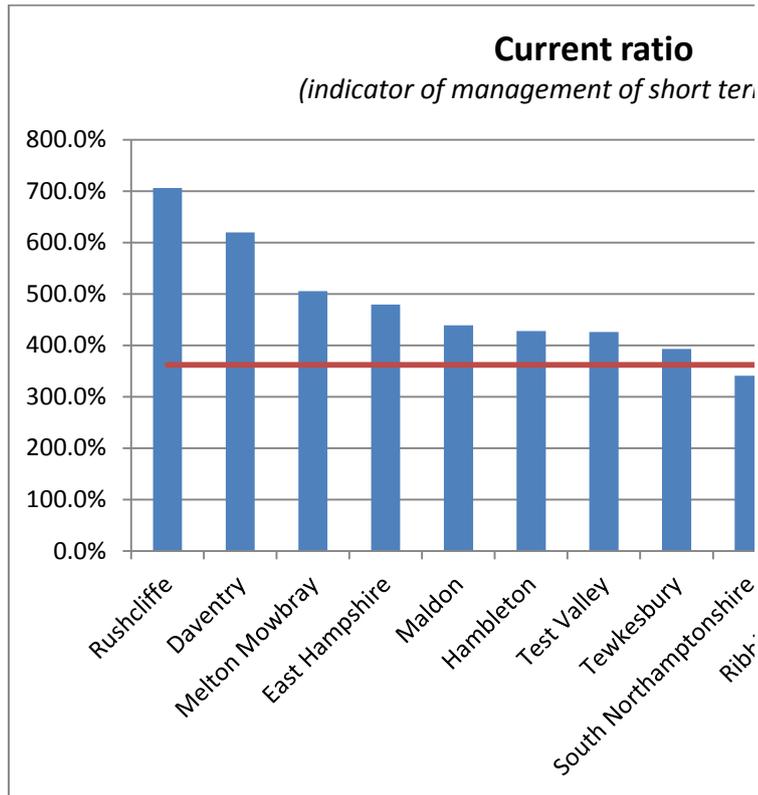
Action Plan

Rec No.	ISSUE	RECOMMENDATION	Management Comments	Priority	Officer Responsible	Due date
<i>Risk 1: Weak or ineffective financial plans and governance arrangements.</i>						
1	Financial training for members is limited to induction training and not all members attended training following the last elections. Regular training would help to ensure that members have the necessary skills and confidence to more effectively scrutinise and challenge financial plans and performance.	The member training and development programme should include periodic financial training linked to key events or changes in the local government finance regime.	<p>Opportunities will be taken to identify Members' financial training needs to effectively scrutinise budget performance and financial governance. Training planned for 2016/17 include</p> <ul style="list-style-type: none"> • Fraud and Corruption • Business Rate Retention • Treasury Management • Role of the Audit Committee 	Medium	Head of Finance & Commercial Services	31 March 2017
2	Service / team plans do not include financial details meaning it is difficult to demonstrate a clear link between service objectives and the financial implications.	Service / team plans should include financial details such as overall budgets, cost pressures, efficiency plans and growth items to provide a clear and transparent link between service objectives and the financial implications.	Agreed. Financial information has been included in portfolio challenge sessions but will now be included in team plans from 2017/18 onwards	Low	Head of Finance & Commercial Services	February 2017
3	Review of budget reports and last year's MTFS provide evidence of a very clear	Strengthen budget reports and the MTFS through the inclusion of more	In the view of the S151 Officer sufficient information is provided	Medium	Head of Finance &	February 2017

Rec No.	ISSUE	RECOMMENDATION	Management Comments	Priority	Officer Responsible	Due date
	analysis and assessment of the key financial drivers and risks associated with the budget set out in a logical and easy to understand manner. Some evidence of financial modelling has been seen but there is limited evidence of formal reporting of scenario or sensitivity analysis as part of budget reports or the MTFS.	detailed sensitivity analysis and scenario planning to support members and other stakeholders in understanding the financial impact of decisions and changes in key budget assumptions, particularly in respect of high risk and volatile items.	to Members to assist decision making and setting of budgets. However, the S151 Officer will consider where relevant inclusion of more detailed sensitivity analysis in future budget reports		Commercial Services	
4	Section 5.4 of the 2015/16 budget report discusses the adequacy of reserves and states that it is considered prudent to retain relatively high levels of reserves due to the uncertainty over future levels of government funding and other income. The report also states that all earmarked reserves have been reviewed in detail but does not include details of the basis of the review.	Include a more detailed review of all reserves and balances in future budget reports in accordance with the CIPFA Local Authority Accounting Panel (LAAP) bulletin 99. The review should set out the purpose and rationale for each reserve, how and when it can be used, management controls and the basis for setting the amount of the reserve clearly linked to the related risks and / or future commitments.	LAPP Bulletin 99 is used by the S151 Officer to inform his review. The outcomes of the review will be captured more formally with relevant extracts included within the budget report.	Low	Head of Finance & Commercial Services	February 2017
<i>Risk 3: Inadequate arrangements for identification and delivery of efficiency and productivity improvements.</i>						
5	The current approach to identification of efficiency savings through the portfolio challenge process is robust and systematic but focuses on specific services meaning there is a risk that opportunities for cross-cutting savings may be missed.	Develop the current approach to identification of savings to include mechanisms for the identification of opportunities for cross-cutting efficiency savings. For example, supplementing the existing portfolio challenge process with a corporate challenge workshop or similar process.	The approach proposed for Efficiency Planning in 2016/17 builds on existing arrangements and includes a corporate challenge workshop in line with this recommendation.	Medium	Head of Finance & Commercial Services	December 2016

Appendix 2 Benchmarking





Appendix 3

Glossary

The Auditor's Opinion

The Auditor's Opinion for the assignment is based on the fieldwork carried out to evaluate the design of the controls upon which management rely and to establish the extent to which controls are being complied with. The table below explains what the opinions mean.

Level	Design of Control Framework	Compliance with Controls
SUBSTANTIAL	There is a robust framework of controls making it likely that service objectives will be delivered.	Controls are applied continuously and consistently with only infrequent minor lapses.
SUFFICIENT	The control framework includes key controls that promote the delivery of service objectives.	Controls are applied but there are lapses and/or inconsistencies.
LIMITED	There is a risk that objectives will not be achieved due to the absence of key internal controls.	There have been significant and extensive breakdowns in the application of key controls.
NO	There is an absence of basic controls which results in inability to deliver service objectives.	The fundamental controls are not being operated or complied with.

Category of Recommendations

The Auditor prioritises recommendations to give management an indication of their importance and how urgent it is that they be implemented. By implementing recommendations made managers can mitigate risks to the achievement of service objectives for the area(s) covered by the assignment.

Priority	Impact & Timescale
HIGH	Management action is imperative to ensure that the objectives for the area under review are met.
MEDIUM	Management action is required to avoid significant risks to the achievement of objectives.
LOW	Management action will enhance controls or improve operational efficiency.