

CABINET

17 March 2010

PRINCIPAL SCRUTINY COMMITTEE

22 March 2010

DEVELOPMENT OF THE INTERNAL AUDIT PARTNERSHIP BETWEEN HAVANT BOROUGH COUNCIL AND WINCHESTER CITY COUNCIL TO INCLUDE TEST VALLEY BOROUGH COUNCIL FROM 1 APRIL 2010

REPORT OF HEAD OF FINANCE

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RECENT REFERENCES:

NONE

EXECUTIVE SUMMARY:

The business case describes the implications of moving forward to an extended Partnership arrangement to include Test Valley Borough Council for the delivery of the Council's internal audit requirements from 1 April 2010.

This business case proposes that for an interim period of one year, Test Valley BC be permitted to join the Havant BC and Winchester CC audit partnership. This will cover the financial year 2010/11. It is proposed that during 2010/11 the Audit Manager and the audit manager for the Gosport/Eastleigh audit partnership produce a joint business case for the audit partnership becoming a 5 Council audit partnership. An outline vision of the potential for this 5 Council partnership has been produced and is included in the business case.

Financial information is contained within Exempt Appendix 2, which sets out the financial and staffing implications of the proposals. It is expected that a small financial saving of circa £5,000 for 2010/11 may be achieved through the partnership working: however, the primary objective of the expansion of the partnership is to create a more resilient and robust partnership structure for 2010/11.

RECOMMENDATIONS:

To Cabinet:

- 1 That Cabinet approves the development of the Internal Audit Partnership to include Test Valley Borough Council for a period of one year from April 2010, as set out in the report.

To Principal Scrutiny Committee:

1. That Principal Scrutiny Committee considers any recommendations it wishes to make to Cabinet in respect of these proposals.

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REPORT OF HEAD OF FINANCE

DETAIL:

1 Introduction

- 1.1 Future models for service delivery in local government are a topic of consideration at a national level and across political parties. Whilst all public sector services are under pressure to be more innovative in their models of provision, it is recognised that district councils are particularly vulnerable to the changing environment and consequently this report is about providing an Internal Audit Partnership with greater resilience to future challenges.
- 1.2 The audit teams at Winchester and Havant work in partnership as a shared service, though at each site the teams are directly employed by their own Council. The Partnership with Winchester has been running successfully for just over 7 years and the current Audit Manager has been the partnership manager for just over six years.
- 1.3 Test Valley Borough Council recently went through a restructure that resulted in their joint Head of Finance and Audit being made redundant. Test Valley BC consulted with a number of councils across Hampshire for expressions of interest in providing a shared audit manager and a shared audit service. The Havant/Winchester Audit Partnership was the preferred choice for Test Valley BC.
- 1.4 A paper was submitted to Test Valley BC in the summer outlining the potential for partnership working and possible opportunities and risks arising from such a development. In November 2009, after several meetings between the Head of Finance (s151 Officer) at Winchester, the Audit Manager and representatives from Test Valley BC, Havant and Winchester were advised that Test Valley would like to join the audit partnership.
- 1.5 This business case proposes that for an interim period of one year, Test Valley BC be permitted to join the Havant BC and Winchester CC audit partnership. This will cover the financial year 2010/11. It is proposed that during 2010/11 the Audit Manager and the audit manager for the

Gosport/Eastleigh audit partnership produce a joint business case for the audit partnership becoming a 5 Council audit partnership. An outline vision of the potential for this 5 Council partnership was produced in late December and is shown in the under Appendix C of the business case (see Appendix 1 to this report).

- 1.6 The business case (Appendix 1 to this report) describes the implications of moving forward to an extended partnership arrangement to include Test Valley Borough Council for the delivery of the Council's internal audit requirements.

OTHER CONSIDERATIONS:

2 SUSTAINABLE COMMUNITY STRATEGY AND CORPORATE BUSINESS PLAN (RELEVANCE TO):

- 2.1 Internal Audit contribute through the annual audit plan to the corporate governance arrangements of Winchester City Council, which in turn supports the achievement of the objectives of the Sustainable Community Strategy and Corporate Business Plan.

3 RESOURCE IMPLICATIONS:

- 3.1 Please refer to Exempt Appendix 2 to this report which sets out the staffing/financial implications.
- 3.2. It is expected that a small financial saving of circa £5,000 for 2010/11 may be achieved through the partnership working: however, the primary objective of the expansion of the partnership is to create a more resilient and robust partnership structure for 2010/11

4 RISK MANAGEMENT ISSUES

- 4.1 A fully detailed risk assessment can be found as Appendix B to the Business Case report (see Appendix 1 to this report).

BACKGROUND DOCUMENTS:

None

APPENDICES:

Appendix 1 – Business Case for the Expansion of the Internal Audit Partnership from 1 April 2010

Appendix 2 – Exempt item – Staffing/Financial Implications

Business Case for Internal Audit Partnership expansion to include Test Valley Borough Council

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1. Introduction & Background

1.1 Introduction

All public sector services are under pressure to be more innovative and cost-effective in their models of provision and it is recognised that district Councils are particularly vulnerable to the changing environment. In response to this context the Council has set a clear direction of travel for the future and this is outlined in the Sustainable Community Strategy. The Council's strategic focus recognises that partnerships will sustain the Council into the future; it sees that alliances and partnerships across a number of organisations give the Council strength and resilience to face the challenges of budget pressures and new customer demands.

Havant Council currently provides an audit manager to Winchester City Council and 50% of the costs of the post are paid for as part of the partnership arrangement.

The audit manager has a range of responsibilities across both councils including:

1. Ensuring full compliance with the Code of Practice for Internal Audit in Local Government in the United Kingdom 2006. This provides a framework for measurement, management and monitoring of the internal audit function. The Code of Practice states that Internal Audit has to be judged not just by its adherence to the Code, but also by its contribution to the organisation that it serves. An effective internal audit service should aspire to:
 - a. understand the whole organisation, its needs and objectives
 - b. understand its position with respect to the organisation's other sources of assurance and plan its work accordingly
 - c. be seen as a catalyst for change at the heart of the organisation
 - d. add value and assist the organisation in achieving its objectives
 - e. be forward looking – knowing where the organisation wishes to be and aware of the national agenda and its impact
 - f. be innovative and challenging
 - g. help to shape the ethics and standards of the organisation
 - h. ensure the right resources are available, recognising that the skills mix, capacity, specialisms, qualifications and experience requirements all change constantly
 - i. share best practice with other auditors
 - j. seek opportunities for joint working with other organisations' auditors.
2. Compilation of an Audit Strategy and Plan.
3. Management of the annual work programme and the audit resources.
4. Regularly reporting to the Audit Committees or their equivalent.
5. Development and implementation of a monitoring and review programme for all audit work to ensure that due professional care is achieved and maintained.
6. Key member of the Governance Groups at both Councils.

7. Key member of the Risk Management Groups at both Councils.
8. Member of other management teams or project boards at both Councils.

The audit teams at Winchester and Havant work in partnership as a shared service, though at each site the teams are directly employed by their own Council. The Partnership with Winchester has been running successfully for just over 7 years and the current Audit Manager has been the partnership manager for just over six years. Before the partnership with Winchester the Council had a partnership with East Hampshire District Council but this was subsequently discontinued and East Hampshire currently have internal audit services delivered by a private sector supplier under a contract that continues for some years.

The Audit Manager restructured the Internal Service at Winchester City Council in 2007/08 to bring in more qualified and experienced auditors.

The Internal Audit Partnership currently enjoys a high level of audit experience and professionally qualified auditors.

The Audit Manager ensures that both Winchester and Havant's Internal Audit Services are annually benchmarked as part of the national CIPFA benchmarking club and has also undertaken benchmarking across Hampshire on cost and quality. Havant and Winchester have been shown to perform well on cost and quality processes.

1.2 Work to Date

Test Valley Borough Council recently went through a restructure that resulted in their joint Head of Finance and Audit being made redundant. Test Valley BC consulted with a number of Councils across Hampshire for expressions of interest in providing a shared audit manager and a shared audit service. The Havant/Winchester Audit Partnership was the preferred choice for Test Valley BC.

A paper was submitted to Test Valley BC in the summer outlining the potential for partnership working and possible opportunities and risks arising from such a development. In November after several meetings between the Head of Finance (s151 Officer) at Winchester, the audit manager and representatives from Test Valley BC, Havant and Winchester were advised that Test Valley would like to join the audit partnership.

The audit manager has undertaken some work on reviewing the audit plans, strategy, and resources for Test Valley's audit service and this has been used in the formulation of this business case.

This business case proposes that for an interim period of one year that Test Valley BC joins the Havant BC and Winchester CC audit partnership. This will cover the financial year 2010/11. It is proposed that during 2010/11 the audit manager and the audit manager for the Gosport/Eastleigh audit partnership produce a joint business case for the audit partnership becoming a 5 Council audit partnership. An outline vision of the potential for this 5 Council partnership was produced in late December and is attached under Appendix C.

1.3 Organisational Overview

The provision of an internal audit service is a statutory requirement as identified in the Accounts and Audit Regulations 2003 as amended in 2006.

Havant has provided an audit manager to Winchester City Council since 2002 and shared audit resources.

Test Valley BC has an in-house audit team and the principal auditor 22 years experience at the Council.

1.4 Business Need

Local Government continues to face significant challenges in terms of budget constraints, the drive to do more with less and rising customer expectations. In the light of the recession there is an expectation that significant reductions of local authority expenditure will be required in the next few years

The Council expects to need to achieve continuing budget reductions of a minimum of over the next three years.

There are many private and public sector organisations that provide internal audit services. Economies of scale can be provided by a larger partnership so more districts working together to provide low cost/high quality audit services is considered the best way to achieve further efficiencies. In 2010/11 the proposed three way audit partnership will provide potentially a small financial saving to Winchester but will provide a greater resilience in audit resources and business continuity because of a proposed new partnership structure.

Whilst the current audit team has never experienced delivery problems, other than when large special investigations have exceeded the contingency in the audit plan, it is recognised that there are significant inherent risks in service delivery from a small team. The proposals in this business case seek to create a more robust internal audit management framework and dynamic working environment for the auditors. Staff retention of highly experienced and qualified auditors is a key objective.

By continuing to work in partnership and further developing the partnership arrangements the internal service can be sustained and improved in an even more cost effective manner through opportunities for economies of scale, upfront and shared investment, skills and experience and driving new innovations to respond to the changing needs of customers.

1.4 Scope

The scope of the proposal is to expand the current audit partnership to include Internal Audit Services at Test Valley BC. The audit manager's time will be allocated as a 1/3rd to each council.

There is a need to retain an on site presence to allow employees and managers to have quick access to advice and assurance from internal audit and also to enable auditors to carry out their duties in the review of council services and to fulfil their role on corporate groups and projects. The internal auditors also undertake functions which can only be delivered on site on a face to face basis and involves significant review of the council computer systems and records.

The proposed split of work between the Councils is shown at Appendix A.

2. Strategic fit

The current Sustainable Community Strategy for Winchester City Council records the overarching vision of the organisation: 'Our vision for Winchester District is of diverse and dynamic communities, where people work together to ensure that everyone has the opportunity to lead a fulfilling life now and in the future'

2.1 Contribution to key objectives

The establishment of a wider internal audit partnership across Hampshire supports the Council's and Government's aspirations with regards to a more joined up approach to the delivery of services.

Moving forward with this proposal potentially only marginally reduces current costs thus making potentially a small contribution in assisting the Council's requirement to find budget reductions over the next three years. However, the current net salary costs of Internal Audit at Winchester when compared to other councils in Hampshire with an in-house service or partial outsource showed Winchester as providing one of the lowest net cost. Note: East Hants DC did not take part in the benchmarking exercise that these results were derived from.

The potential for moving to a five Council audit partnership could result in a more significant saving.

2.2 Constraints, Dependencies and Risks

The live implementation is proposed to be from April 2010. Any delay would expose Test Valley to potential risks arising from not having an audit manager in place for the new financial year.

The risk register associated with the Internal Audit Proposal is attached at Appendix B of this paper. The proposal reduces the risk of failure to deliver the service.

3. Options Study

3.1 Requirements and Specifications

The high level requirements of the service are:-

- Provision of an audit manager across the three Councils.
- Making optimum use of the audit resources across the three Councils to ensure the effective delivery of audit and compliance with the Code of Practice for Internal Audit 2006.
- Creation of Principal Auditor roles at each Council to act as a deputy to the audit manager (currently a flat line structure)

3.2 Sourcing Options

Winchester is already working in partnership for internal audit services and over the last seven years savings arising from this have exceeded £200,000.

The partnership could remain as it currently is between Havant and Winchester but there is an opportunity to make the partnership more robust, particularly retention of experienced and qualified staff by expanding the partnership to include Test Valley. This will also help in looking at the potential to move to a bigger audit partnership possibly across 5 or more Councils in 2011/12.

4. The Proposal

4.1 Summary of the Proposal

The proposal is based on Winchester City Council continuing to retain staff locally to deliver internal audit services and the provision of day to day advice to staff in Winchester City Council. The audit teams at Havant and Test Valley will continue to be directly employed by their own Council and will be managed by Havant's audit manager acting as the audit partnership manager.

There will be an increase in the overall responsibility of the audit manager. .

A critical part of the proposal is to establish a principal auditor at each Council. Part of this post will directly link to providing a deputy role to the audit manager and will involve an increase in supervisory responsibilities. However, the audit manager retains overall responsibility for the provision and management of the internal audit partnership and will attend all audit committees at each Council. The

audit manager time will be split equally across the three councils. However, it is proposed that the audit manager spends one day a week on site at Test Valley to minimise travel time. Test Valley has stated they find this arrangement acceptable.

This proposal is for an interim period of 12 months to cover the 2010/11 financial year, whilst further work is undertaken on a business case to develop a larger audit partnership for 2011/12.

4.2 Price and Funding

This is set out in the accompanying not for publication report.

4.3 Achievability

It is envisaged that the desirable date of 1 April 2010 from which to implement a three Council audit partnership is achievable. Shown below are the requirements over the next three months to meet this deadline. This timetable is considered achievable if the decision to proceed is made by the end of March 2010.

4.4 Timing and Links with Other Services

The potential for a wider audit partnership to include Gosport and Eastleigh Councils will be worked on during 2010/11 in consultation with all potential partners.

The Audit Manager for Gosport and Eastleigh and the Audit Manager for Havant and Winchester and Test Valley (if the proposal is agreed) will jointly lead on producing the business case and a lead CFO will be sought to head this up.

Please see Appendix C for vision statement for this proposal.

4.5 Governance, Roles and Responsibilities

The Audit Manager will continue to be a member of the Governance Groups at each Council and the work of internal audit will continue to support the governance arrangements of each council. It is possible that a 5 authority partnership may require more formal governance arrangements such as a Joint Committee.

5 Next Steps

5.1 Human Resources Considerations & Communication

The forming of an extended partnership with Test Valley Borough Council will further reduce the staffing requirement within the Winchester Audit Team. The Audit team will reduce from 3.5 ftes to 3.33 as a result of the audit manager's time being split across three Councils.

5.2 High Level Plan

An indicative high level plan is shown below.

Timetable	
23 February 2010	Draft business case presented to Corporate Management Team
17 March 2010	Consideration of proposal by Cabinet
22 March 2010	Presentation of business case to Principal Scrutiny Committee
Beginning April 2010	Three way audit partnership commences.

Appendix A – Scope of Work

Winchester

Performance Agreement for the Audit Manager to include:

1. Production of an Audit Strategy and Audit Plans and associated protocols.
2. Delivery of 95% of the annual audit plan.
3. Delivery of the performance of the audit team shown as a percentage of productive time to chargeable time.
4. Customer satisfaction scores of 3 out of 4 to demonstrate service delivers a valued service against a range of criteria.
5. Compliance with the CIPFA Code of Audit Practice.
6. Supporting the Governance and Risk Management Groups/Officers at each Council.
7. Further development of specialist skills across the partnership to optimise the capability of the audit partnership to undertake Financial, Contract, ICT, Systems Flowcharting, Fraud Investigations, Project Management and Risk Management.
8. To promote an anti-fraud and corruption culture at each Council.
9. Making optimum use of the partnership audit resources for the benefit of all partners.
10. Quarterly reports to the audit committee.

Havant

As Winchester.

Test Valley

As Winchester

Appendix B – Risk Analysis

Risk No.	Risk	Identification of areas where there are significant risk	Mitigation Required	Impact From 0 to 5	Likelihood From 0 to 5	Overall Score	Financial Assessment of Risk
1	Failure to meet 1 st April 2010 live date.	Project implementation delayed.	Audit Manager performance in place at each council, plus new principal auditor role.	3	2	6	Low
2	Inadequate audit management resource.	Overall role in management of audit resources and in providing adequate cover for each organisation.	Creation of principal auditor roles to provide additional supervision capacity and support to the audit manager. Potentially an increase in the overall cost of the audit manager post and the creation of principal auditors will be offset by the costs of the audit manager being divided by 3 instead of 2.	5	2	10	Low
3	Availability of the audit manager to each organisation	Physical resource due to time being divided across three councils.	Continuing to embrace flexible/smarter working practices and effective communications.	3	3	9	Low
4	Failure to address people issues as they arise.	Project perceived as a threat by staff leading to a lack of support and obstruction.	Staff to be kept informed at every stage of the implementation.	4	1	4	Low
5	Loss of confidentiality.	Personnel data.	Data sharing protocols in place as part of the formal partnership agreement – respecting confidential nature of some information and mutual assurances about respecting such confidentiality (Data Protection Officers to be consulted). All auditors covered by Code of Conduct.	4	0	0	Low

Risk No.	Risk	Identification of areas where there are significant risk	Mitigation Required	Impact From 0 to 5	Likelihood From 0 to 5	Overall Score	Financial Assessment of Risk
6	Loss of resource spent in travel time between sites.	Audit manager travelling time and auditors undertaking audits across the Councils.	An intelligent use of resources to ensure optimum use of resources in terms of skills, knowledge and experience to add value to individual audits with due consideration to the residential location of auditors to limit travel time. For the audit manager agreed with Test Valley will only be required on site one day a week.	3	2	6	low
7	Equality issues arising from different pay and conditions.	Winchester and Test Valley auditor have essential user car status. Winchester also pays professional subscriptions and a salary supplement for home working. Different rates of pay at each council.	Audit staff currently accept the differences in pay and conditions and has not been an issue because they value being employed by their own Council.	3	1	3	low
8	Partnership does not realise all potential savings	Economies of scale could produce potential savings in a larger partnership.	Business case to be developed for a 5 way or more audit partnership for 2011/12.	3	3	9	low
9	Partnership not equal between partners resulting in a detriment to the audit service at one or more of the partners.	Unreasonable demands by one or more partners on the partnership audit resources.	One performance agreement in place for the audit manager equally shared by each partner. No deficit of days to any partner because of sharing the partnership audit resources. Delivery of the audit plan at each council in the partnership.	4	2	8	low

Appendix C – Vision for 5 way (plus) Audit Partnership for 2011/12

Background

Two internal audit partnerships between councils already exist within Hampshire, both of which are considered to have been a success and continue to work effectively. A number of financial savings have already been made with a shared audit manager/head of audit between Gosport and Eastleigh and also Havant and Winchester.

Varying degrees of internal audit shared service working occurs between the partnership sites to make best use of in house resources.

The Havant and Winchester partnership is currently looking to potentially move to a three way partnership and it is proposed that it will be set up on an interim structure for 2010/11. This is to enable flexibility in considering the options for a bigger partnership to include Gosport and Eastleigh and possibly others.

Objectives and Possible Outcomes of a larger internal audit partnership

Internal Audit is a service which has a wide scope of activity in each organisation and requires good quality audit management and staff that have the skills and experience necessary to provide an adequate level of assurance and probity.

Completion of an annual audit plan at each council covering all the core financial systems and audits linked to the organisations risk registers is a key function of the internal audit service. In addition to this internal audit deliver a role in supporting corporate projects and undertaking specialist areas of audit such as ICT, Contracts, Procurement, Project Management, Risk Management and Special Investigations relating to fraud and corruption.

The high level overview (shown above) on Internal Audit is a key driver in partnership working to ensure delivery of audit services in a cost effective way and to a high quality threshold.

The vision for a larger partnership would seek to explore/achieve the following:

1. A more robust management structure with two or more Heads of Audit working in Partnership to deliver internal audit services to all councils.
2. Possible Partnership Audit Committee to manage the Partnership but separate Audit Committees at each Council for reporting audit matters to.
3. Consideration of a lead council or councils to include seeking equality of working conditions and employment terms. This could also lead to one council or two acting as possible hosts for the partnership with small satellite offices at each council. This could contribute to the reducing the overall on-costs of the audit service, through reduced accommodation costs. A key part of this would also involve embracing a flexible/smarter working concept to further reduce office space and associated overheads.

4. Scope to have specialist audit resources employed for the benefit of the whole partnership to cover areas such as ICT which can be expensive resources to have to buy-in.
5. More effective use of resources through shared working on audits, allowing auditors to build up in-depth knowledge of specific systems and corporate issues across all the partnering councils.
6. Greater efficiencies in the administration of the partnership. One shared audit handbook and set of procedures and processes would reduce the administrative work for the current Heads of Audit. Systems would be further streamlined with the possible implementation of computerised audit management software to support flexible working and to aid effective communication across the sites.
7. The retention and recruitment of auditors should be improved as a larger partnership could offer more career development opportunities.
8. Streamlining audit resources to reduce overall audit staff costs for the partnership.
9. Potential for reduced inspection regime from External Audit.

Making the Vision a Reality

The work required to develop a business case will require a considerable time commitment from the current Audit Managers. The business case will involve many detailed tasks involving full consultation with each council, costed options, risk/opportunity analysis, potential HR issues, ICT issues, etc.

The business case will need to be produced at the same time as managing the partnerships that currently exist and because of this and the factors above it is likely to take 12 months to complete.

The five way partnership if the councils agree on the business case proposals is unlikely to be in place until April 2011 as there will be significant preparation in setting it up.