

NORTHUMBERLAND COUNTY COUNCIL

AUDIT COMMITTEE

At a meeting of the **Audit Committee** held at County Hall, Morpeth on Wednesday, 26 July 2017 at 10.15 a.m.

PRESENT

Councillor G Hill
(Chair)

COUNCILLORS

A Hepple (part)
L J Rickerby

M Swinburn
D Towns

CO-OPTED MEMBERS

A N Haywood-Smith

I Walker

OFFICERS IN ATTENDANCE

B J McKie
C Mellons
A Mitchell
K Norris-
S Reid
A Stewart

Group Assurance Manager
Ernst & Young, External Auditor
Chief Internal Auditor
Democratic Services Officer
Ernst & Young, External Auditor
Finance Manager

ALSO PRESENT

Councillors B Flux (part), C Horncastle (part), G Roughead (part),
R Wearmouth (part)

1. MEMBERSHIP AND TERMS OF REFERENCE

The Chair welcomed members to the first meeting of the Audit Committee and asked everyone to introduce themselves. Details of the membership and terms of reference, as agreed by Council on 24 May 2017, had been circulated with the agenda for information.

Ch.'s Initials.....

The Chair said she would have liked to have seen the words 'robust' and 'transparency' included within the text of the Terms of Reference. Mrs Walker, Independent Member, referred to page 5, External Audit point (4), and suggested that it should read 'To commission work **in the scope of this committee** from internal and external audit. These points were noted and would be considered the next time the Terms of Reference were put forward to Council for approval as part of the next review of the Constitution in May 2018.

RESOLVED that the Audit Committee's membership and terms of reference, as agreed by Council on 24 May 2017, be noted along with the points raised.

2. APOLOGIES FOR ABSENCE

Apologies for absence were received from Councillors Castle and Simpson.

3. MINUTES

RESOLVED that the minutes of the meeting of the Audit Committee held on Wednesday, 29 March 2017, as circulated, be confirmed as a true record and signed by the Chair subject to the following amendment:

Page 2, item 3 - Value for money risks - financial planning - the last paragraph be amended to read:

Mrs Walker queried whether the increase in council tax would support delivery of planned savings in 2017/18.

4. PRESENTATION AND DISCUSSION ON THE ROLE OF AUDIT AND THE AUDIT COMMITTEE

Members of the Committee received a slide presentation from the Chief Internal Auditor, Allison Mitchell. The presentation provided details about the role of Audit Committee; reports to Audit Committee; who reported to Audit Committee; Internal Control - the Three Lines of Defence; Internal Audit; External Audit and Risk Management (a copy of the presentation is filed with the signed minutes, for information).

Mrs Mitchell said that some of the content of professional reports, such as audit and accounting reports, could be by their nature very technical. It was therefore important that report authors should seek to convey messages as clearly as possible, using 'plain English' and ensuring that technical matters were properly explained for the benefit of Audit Committee. As the year progressed and reports

were received by Committee, Mrs Mitchell invited Committee members to provide feedback to report authors to help them improve their reports and make these as helpful as possible to the Committee. Therefore one of the priorities would be to use language which was easily understood.

In response to a comment about members being kept fully informed, it was noted that risk management training for members had been arranged as part of the induction programme and would be facilitated by Zurich Municipal.

During the presentation comments/questions were raised and information was provided as follows:

- Regarding value for money, this was a matter included within the work of both Internal Audit and External Audit. Every Internal Audit report had a 'value for money' section which reflected on any value for money considerations identified during the audit. External Audit had a specific role in assessing value for money and providing an opinion thereto. External Audit would apply guidelines published in the Code of Audit Practice by the National Audit Office around informed decision making by the Authority and a set criteria which would highlight significant risks and financial sustainability. Work was currently being done on the medium term financial plan and, as events unfolded, External Audit would assess if there were any developments which would impact on value for money.
- Information regarding the rights of residents to challenge reports was published on the Council's website but the Committee considered that this was not widely known and that further publicity would be beneficial. It was suggested that information could be provided with Council Tax bills and/or in libraries.
- Both Internal and External Audit had a right to access any information they requested when necessary for the completion of their work, and have meetings with officers to corroborate evidence. Strict rules governed how these powers should be exercised, to ensure proportionality and fairness in the conduct of audit matters.
- Further information about risk management and assurances regarding processes being robust and effective within the organisation would be provided at the next meeting.
- A copy of the presentation would be emailed to all members for information.

RESOLVED that the presentation be received and a copy emailed to all members.

5. REPORTS OF THE EXTERNAL AUDITOR

(a) Interim update Report for the Year Ended 31 March 2017 (Appendix A)

Mr S Reid, External Auditor EY, introduced the above report which set out External Audit's progress against work in the Audit Plan presented to the Audit Committee on 29 March 2017(a copy of which is filed with the signed minutes as Appendix A).

It was noted that for the year ending 31 March 2018, the Council would be required to publish audited financial statements by 31 July 2018 which was two months earlier than in previous years.

It was stated that the interim report was positive and a final report to summarise findings would be brought to the next meeting.

In response to members' questions, it was noted that the external audit process was not to question policy, it was to ensure transactions were supported by evidence and that these complied with generally accepted accounting practice.

Members commented that it would be helpful to have sight of documents well in advance of the meeting (e.g. the accounts) due to the amount of information to read and understand. It was acknowledged that colleagues in finance worked to strict deadlines but the Draft Statement of Accounts had been produced on 30 June and published on the Council's website. A request would be made to Democratic Services to see if it would be possible, in future, to send it out in advance of the other agenda papers.

RESOLVED that the report be received.

(b) Sector Update (Appendix B)

The Audit Committee received a sector briefing which covered issues which may have an impact of the Local Government sector and the audits undertaken. (A copy of the report is enclosed with the signed minutes as Appendix B.)

Mr Reid, EY, stated that a general election had taken place since the update was written and drew members' attention to page 9 which listed key questions for Audit Committee. He informed the Committee that the standard practice adopted in Northumberland was for a report to be brought to the next meeting of Audit Committee, providing information to the Committee on how the matters referenced were being managed within the County. He suggested that was good practice and should be continued. A report would therefore be presented to September's Audit Committee on these matters.

Councillor Hepple referred to the section on health and social care integration and queried if that section was referring to Northumberland County Council, the Health Authority or both. In response Mr Reid stated that it needed local interpretation. Councillor Rickerby referred to information received at Health and Well Being Scrutiny Committee which showed Northumberland was well ahead due to it having

an integrated service and she did not think the implemented changes would create any problems for the Authority.

RESOLVED that the report be received.

Councillor Hepple left the meeting at 11:25 am.

6. REPORTS OF THE DIRECTOR OF CORPORATE SERVICES

(a) Draft Statement of Accounts 2016-17

Andy Stewart, Finance Manager, introduced the above report, the purpose of which was to provide an overview of the key issues related to the Council's Draft 2016-17 Statement of Accounts and to assist Members in carrying out their role in reviewing the Financial Statements.

He said it was part of the Committee's remit to review the Annual Statement of Accounts to see if there were any concerns they felt should be raised at full Council. All members had received the document which was accompanied by a summary report (a copy of which is filed with the signed minutes as Appendix C).

It was noted that the Statement of Accounts had been compiled in accordance with statutory requirements and best practice guidance. The accounts had been certified as a true and fair representation of the financial performance and position of the Council as at 31 March 2017 by the Director of Corporate Services.

The results from External Audit's audit of the draft Statement of Accounts would be reported in September.

A number of areas of the Draft Statement of Accounts were highlighted and discussed including the Comprehensive Income and Expenditure Statement, on pages 19 & 20 and the Movement in Reserves Statement, on pages 21 & 22.

It was noted that in 2016/17

- the overall net worth of the Council had increased by £68.91 million;
- capital expenditure totalled £296.99 million;
- there was a £6 million variance in the original budget;
- there was an overspend of £2.6 million;
- the earmarked general fund and HRA reserves increased by £4.17 million;
- the pension fund showed net liability of £672.1 million (estimate of pensions in future years, mortality rates, salaries etc);
- group accounts included those for Arch, Homes for Northumberland (HfN) and Generation and Innovation. It was pointed out that HfN had been taken back

in-house and Generation and Innovation had remained dormant during that time.

Councillor Swinburn raised the following issues:

- The document was a considerable size, a number of other Councils published much smaller draft statements and referenced their plans for aims and priorities rather than including them within the document. If the document focussed only on the statement of accounts, it would be quicker and easier to read.
- Page 109 stated that the Arch Group owed £246.10 million to the Council, details of group interest were set out on page 199 but it was unclear how much interest was owed by Arch. It would have been helpful to have all specifics for borrowing listed on one page.
- Page 44 provided information on Private Finance Initiative (PFI) and whilst there was a lot of information, there also seemed to be a lot missing.

In response the Finance Manager said officers were looking to reduce the size of the document. One of the reasons it was so big was that it included details of the pension fund and group accounts which other Councils did not have. Ways of streamlining the document and improving the process were being explored but the Council was bound by certain professional requirements as to the type and nature of information which must be included within the accounts.

Some other members agreed that the document should be more focussed but did not consider the size to be important.

Mrs Walker then referred to pages 7 and 8 of the report, Adult Services and Corporate Resources, in which revenue expenditure was being funded with capital and asked if that was material. In response The Finance Manager explained the process in detail and said it was an accountancy adjustment.

In response to a query regarding the level of reserves, Mr Reid stated that following the change in administration there had been some changes to assumptions. Some use of reserves had been made, however, the remaining level of reserves was well in excess of those that had been used. Although it was not good practice to continue using reserves to fund recurring revenue expenditure, the use of the reserves reflected in the accounts appeared reasonable at this stage.

Councillor Towns raised the following issues:

- In order to verify information about the group accounts relating to Arch (page 15) and the latest financial results on Arch (Corporate Holdings) Limited (page 146), a summary would have been beneficial;

- Before the election in May it had been reported that Arch had paid a £25 million dividend, where were details of that?
- More explanation was needed about the decision taken to write off £560,000 relating to the disposal of Icelandic bank deposits (page 58);
- Red ink had been used to depict surplus figures when most people would assume red meant deficit. Could the colour be changed to green, for example?

The Finance Manager acknowledged the points made and said officers could look at summarising information within the forward. Mr Reid pointed out that the general public were not accountants so it was important how the story was told at the beginning of the report and it had to be fair, balanced and accountable. It must disclose information required in a way which was easy to understand.

The Finance Manager confirmed that no dividend had ever been paid by Arch to Northumberland County Council.

Discussion then took place regarding the revaluation of the Royal Bank of Scotland (RBS) Certificates of Deposit as set out on page 12 of the report due to a previous valuation being incorrect. Mr Haywood-Smith, Independent Member, referred to the notes about gains or losses on page 13 and queried when that change would be recognised. In response the Finance Manager stated that if an asset was disposed of, and there was a gain or loss, it would be recognised at that point. He added that there was a set criteria for the review of fixed assets and that Cushman and Wakefield were employed by the Council in that regard. Each year valuation reports would be looked at to ensure adjustments were appropriate. Councillor Rickerby said there should have been an explanation of the incorrect valuation and more information was needed.

A member then referred to page 149 of the Draft Statement of Accounts and queried why the Council was holding funds on behalf of Lidl in Bedlington and Blyth. The Finance Manager replied that it was in relation to Section S278 Agreements and assumed the schemes were ongoing.

The Finance Manager advised members that if they had any further comments or questions they could forward them to him direct.

RESOLVED that the key issues within the draft 2016-17 Statement of Accounts be noted.

The Chair then adjourned the meeting for 7 minutes for a comfort break.

(b) Treasury Management Annual Report for the Financial Year 2016/17

Andy Stewart, Finance Manager, introduced the above report, which provided details of the Treasury Management Strategy Statement (TMSS) 2016-2017, approved by the County Council on 24 February 2016. The report provided a

review of borrowing and investment performance for 2016-17, set in the context of the general economic conditions prevailing during the year. It also reviewed specific Treasury Management prudential indicators defined by the (CIPFA) Treasury Management Code of Practice and CIPFA Prudential Code for Capital Financial in Local Authorities, (the Prudential Code), and approved by the Authority in the TMSS. (A copy of the report is filed with the signed minutes as Appendix D.)

The Finance Manager highlighted a number of key points including:

- Treasury Management Training had been arranged for members on 19 October.
- The Treasury Management Policy and Strategy Statement had been approved by the Council as part of its budget setting process.
- Regulations placed responsibility on members to review and scrutinise Treasury Management policies.
- By 31 March 2017 external borrowing increased by £123.37 million.
- Debts of £153.63 million were repaid and £277 million of new or replacement borrowing was taken out.
- Internal borrowing increased by £53.53 million.
- £177.90 million was used to fund the capital programme.
- Rates of return were low and, in lieu of borrowing externally, internal resources were used which was good value and saved money.
- Northumberland achieved the fourth lowest average rate of interest within its group .
- Overall interest payable last year was £21.48 million which was below budget.
- Investments conformed with the Council's approved strategy.
- Overall aims were about security and investments. Officers were also looking at liquidity issues and the best rate of return which could be achieved from investments.
- 1.72% compared favourably against the CIPFA benchmark.
- The actual interest received was lower than forecast but there was a higher balance to invest.
- There were some none treasury management investments where loans had been given to third parties such as Arch, the NHS and the Airport.
- Prudential indicators ensured that capital plans were prudent and sustainable.

The final part of the report related to Treasury Management Guidance and, following a restructure within Corporate Finance and the departure of some key officers who could previously authorise transactions, it was proposed to amend the current Treasury Management Practices so that Principal and Technical Accountants could perform the daily treasury management function. Details of the changes were set out in Appendix 3 of the report.

The Chair stated that the Committee did not have sufficient information on the implications of the proposed change to be able to make an informed decision at this juncture. It was acknowledged that the recommendations were not for Internal

Audit to approve, but the Chair asked the Chief Internal Auditor to look over them and form a view.

Discussion ensued about the principles and practices concerning the segregation of duties as set out in section 5.2 on page 33 of the report. Concerns were raised that

- there should be a delegation limit so that decisions could not be taken solely between the Section 151 Officer (the former Chief Executive) and the Leader of the Council;
- With regard to 5.2 (c), concerns were raised about setting limits and that it should not be a blank delegation;
- Section 5.4.2(i) should be extended to include Principal Accountant or the Technical Accountant as in Section 5.2 (c).
- Relating back to Section 2.2, there was concern that this would give too much freedom if limits were not specified.

In response to questions it was noted that Mrs A Elsdon, Director of Corporate Services, was the Section 151 Officer. Previously, Mr S Mason had been the Chief Executive and the Section 151 Officer and Councillor Towns said he would have queried that Mr Mason should have carried out both roles. Mrs Walker added that the committee had queried that previously, but that professional guidance had been that it was possible for one individual to take on the role of both Chief Executive and Section 151 Officer.

Councillor Rickerby stated that the committee should not approve the proposed revisions to the Treasury Management Practices until further information was provided as questions would arise when it was considered by full Council. Members agreed stating that issues needed to be addressed and further information was required regarding risk and control.

Councillor Towns proposed that the report be deferred in order that revisions could be made to address the concerns raised by members which was seconded by the Chair.

Mr Reid pointed out that the report was split into two parts and suggested an amendment so that members could receive the performance of the Treasury Management function for 2016-17 to allow it to go before full Council but strip out the review of procedures. Councillor Towns said he was happy to amend his proposal as suggested which was duly seconded by the Chair.

Upon being put to the vote it was unanimously agreed that

- 1) Members note the performance of the Treasury Management function for 2016-17 and that it be recommended to County Council.

- 2) That the proposed revisions to the Treasury Management Practices (TMPs) subject to Internal Audit approval be deferred until the next meeting, as Internal Audit's role was not to approve the revisions. However Internal Audit could review the proposed changes and feed back to Audit Committee so that concerns raised by members could be addressed before going to County Council at a later time.

7. REPORTS OF THE CHIEF INTERNAL AUDITOR

(a) Proposed Audit Committee Work Programme

Allison Mitchell, Chief Internal Auditor, introduced the above report which proposed an updated programme of core business for the Audit Committee for 2017/18, in line with its Terms of Reference as set out in the Council's Constitution (a copy of which is attached to the signed minutes as Appendix E).

It was noted that the work programme was a guide and items were not fixed. As matters changed during the year, the work programme could flex to take account of new and emerging risks.

RESOLVED that

- 1) The proposed 'core business' work programme set out within the report for 2017/18 be agreed;
- 2) It be noted that it may be necessary to change or adapt the proposed reports to be considered, to ensure the optimum timing of consideration of governance issues, and to respond to emerging trends during the year;
- 3) It be noted that the committee would receive additional reports on any ad-hoc items of business arising during the year, as these related to its responsibilities under its Terms of Reference, in the usual way.

(b) 2016/17 Opinion on the Adequacy and Effectiveness of the Framework of Governance, Risk Management and Control

Allison Mitchell, Chief Internal Auditor, introduced the above report which provided an annual opinion from the Chief Internal Auditor on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control, taking into account the expectations of the Corporate Leadership Team, Audit Committee and key stakeholders. (A copy of the report is attached to the signed minutes as Appendix F.)

Mrs Mitchell referred to the Executive Summary which stated that the organisation's internal control systems in the areas audited were satisfactory overall. This was a positive opinion on the framework of governance, risk management and control.

Reference was made to Annex A on page 20 which listed the eight main types of internal control, which formed the basis of any assurance work in respect of processes or systems. Page 10, item 4.3, referred to a framework of opinion classifications used in Internal Audit reporting and applied an overall assurance judgement to each system audited. It was noted that the Moderate Assurance level had been deleted from 2017/18, so that there were only four assurance levels and that there would be 'no fence to sit on'. A summary of the following pages was provided.

Members' attention was also drawn to page 17, item 11, Clients' Views where client feedback was sought in respect of all audit reports issued, at the conclusion of each audit assignment. It was stated that the average score was slightly down from last year, which had been extremely high, but overall feedback on the internal audit process had been consistently good and working practices were kept under continuous review.

Page 21 provided details of audit reports issued during 2016/17 and reports pending.

In response to a question it was stated that to the knowledge of those present, Active Northumberland had a board but did not have an Audit Committee.

Councillor Swinburn queried if good practice and bad practice were measured so that if something was working well it could be replicated. In response the Chief Internal Auditor said that sometimes an audit area could be so specific that the matters involved were unique and any learning points could not be replicated elsewhere. However, in some areas such as schools, common issues could be identified which might be of benefit if circulated quickly to all schools. A summary was therefore produced and circulated to all schools where this was the case.

Mrs Walker said assurances were needed that recommendations had been put in place. The Chief Internal Auditor agreed and said that audit recommendations were followed up and reported to the Audit Committee. Mrs Walker queried whether the procedure could be made more robust. Further discussion took place regarding accountability and potential ramifications if recommendations were not followed up and it was queried when an issue could be linked to performance management if it was ignored. Mrs Mitchell explained the procedure and the three lines of defence.

In response to a query regarding reports pending for Active Northumberland, it was stated that the audit team had utilised a self-assessment process, in which answers provided by Active Northumberland officers were then assured with reference to supporting documentation and evidence.

RESOLVED that

Ch.'s Initials.....

Audit Committee, 26 July 2017

- 1) The Chief Internal Auditor's 2016/17 'satisfactory' opinion on the overall adequacy and effectiveness of the framework of governance, risk management and control, attached as Appendix 1 be noted;
- 2) The opinion be considered by the organisation when preparing the Annual Governance Statement for this period; and by the Audit Committee, as a source of assurance, at the time it considers the Annual Governance Statement.

CHAIR:

DATE: