

Audit and Governance Committee

5 December 2011

Report of the Assistant Director, Financial Services

Audit, Counter Fraud & Information Governance Monitoring Report

Summary

- 1 This report provides an update on progress made in delivering the internal audit workplan for 2011/12 and on current counter fraud and information governance activity. The report also includes details of a proposed expansion of Veritau in order to allow the company to provide internal audit services to a number of North Yorkshire district councils.

Background

- 2 The work of internal audit is governed by the Accounts and Audit Regulations 2011 and the CIPFA Code of Practice for Internal Audit in Local Government. In accordance with the code of practice, the 2011/12 audit and fraud plan was approved by the Audit and Governance Committee on 19 April 2011. The plan included a programme of audit reviews, together with details of planned counter fraud and information governance activities.
- 3 This report provides an update on work undertaken against the approved plan.

2011/12 Internal Audit Plan – Progress to Date

- 4 Two of the priorities for Veritau are to deliver at least 93% of the audit plan and to ensure that the service continues to operate to recognised professional standards (as determined by the Code of Practice).
- 5 Internal audit successfully delivered 95.3% of the 2010/11 audit plan. To date, 37% of the 2011/12 audit plan has been

completed (compared to 37% at the same point last year). This figure is based on reports issued and does not take into account further audit fieldwork which has been completed. It is anticipated that the 93% target will be exceeded by the end of April 2012 (the cut off point for 2011/12 audits). Details of the audits completed and reports issued since the last report to this committee in September 2011 are given in annex 1.

- 6 There have been no variations to the audit plan since the last report in September.

Counter Fraud

- 7 Counter fraud work has been undertaken in accordance with the approved plan. Annex 2 provides details of the investigations completed to date and provides a summary of the work undertaken.

Information Governance

- 8 The team provides ongoing support and advice to service departments in managing information governance issues. This includes measures to reduce the risk of data security breaches.
- 9 So far this year (to 31 October) the team has received and tracked 479 Freedom of Information requests, up from 378 in the same period last year (a 27% increase).

Breaches of Financial Regulations

- 10 Only one minor breach of the council's financial regulations has been identified since the last report to this committee. This related to issues around the maintenance of inventory records.

Integration with North Yorkshire Audit Partnership

Background

- 11 Veritau Limited was originally formed on 19 January 2009. On 1 April 2009, the council and North Yorkshire County Council (NYCC) transferred their internal audit, counter fraud and information governance services to the new company. From this date, Veritau has been contracted to provide these services to the two councils together with a number of other

public sector bodies. The company is wholly owned by the council and NYCC, with each holding 50% of the share capital.

- 12 Veritau currently employs approximately 35 staff, organised into five teams. In addition, both the council and NYCC second staff to the company in support of their own professional training programmes (normally CIPFA or AAT). The company operates from two offices, one in York and the other at County Hall, Northallerton.
- 13 The North Yorkshire Audit Partnership (NYAP) was formed in February 1999. The partnership originally consisted of Scarborough Borough, Selby District and Ryedale District Councils. Richmondshire and Hambleton District Councils joined the partnership in May 2008. The partnership is based on a joint committee model with Ryedale District Council acting as lead authority. The existing partnership agreement ends on 31 March 2012.
- 14 NYAP currently employs 12 staff and provides internal audit and counter fraud services to the five partner councils. The staff are employed by Ryedale DC and the service is delivered via satellite offices at each council.
- 15 The NYAP Directors approached Veritau in November 2009 to discuss potential options for future collaboration. These discussions showed that there was a high level of interest in the possibility of the existing services provided by NYAP being transferred to Veritau. Details of the outline proposals were presented to this committee on 6 December 2010. Since that date, detailed plans have been developed to address the legal, financial, staffing and operational implications of any such transfer. Various options for the structure of the expanded business have also been considered, including increasing the number of shareholders in Veritau or establishing a subsidiary company. Details of the final proposals are set out below.

Drivers for Change

- 16 The NYAP member councils are facing similar challenges to the council in terms of delivering internal audit and counter fraud services at a time of financial pressures and significant

change. The main drivers for change are therefore the need to:

- deliver further efficiencies and cost savings
- ensure future service resilience and capacity so as to be able to respond to changing priorities and increasing workload demands
- retain skilled and experienced staff by creating greater critical mass and providing more opportunities for career development and specialism
- make best use of the scarce professional audit expertise available (particularly in contract and IT audit)
- establish an effective succession plan and to reduce the existing reliance on certain key staff for service continuity (particularly within NYAP).

Detailed Proposals

- 17 It is proposed that the services currently provided by NYAP to the 5 district councils are transferred to Veritau on 1 April 2012. Staff currently employed in providing those services would then transfer to Veritau in accordance with the Transfer of Undertakings (Protection of Employment) Regulations (TUPE).
- 18 Veritau will form a subsidiary company called Veritau – North Yorkshire Limited (VNY) to deliver the transferring services. The subsidiary company will be limited by shares with Veritau holding 50% of the share capital and each district council holding 10%. The subsidiary company will have a board of directors comprising an officer from each district council and two directors appointed by Veritau.
- 19 The creation and future operating arrangements of the subsidiary company will be governed by a formal shareholders agreement. The agreement will set out the rights and obligations of the shareholders and the ongoing relationship between each council and Veritau as participants in the venture. The services to be provided to each district council will be specified in separate service agreements, identical or similar to the existing service agreements which Veritau currently has with the council and NYCC. The length of the

new service agreements would be coterminous with Veritau's existing service agreements.

- 20 Each district council will nominate a client officer to oversee the delivery of services under its service agreement with VNY. The annual fee for the core service will be calculated on the basis of an agreed daily fee rate, multiplied by the agreed level of service i.e. the number of days required by each district council. The daily fee rate will be same for each district council and the rate charged by Veritau to the council and NYCC. Each district council will however be able to request additional work under its service agreement. The fee for such additional work will be calculated on the basis of rates for additional work for the appropriate grade of staff which will be specified in the relevant service agreement.
- 21 Each district council will provide serviced office accommodation on similar terms to the existing arrangements Veritau has with the council and NYCC.
- 22 Veritau will seek to ensure that the transferring staff are included in the Local Government Pension Scheme. Staff will also be given the option of transferring from their existing terms and conditions to those of VNY (which will be identical to those offered by Veritau).
- 23 The new company would be a separate legal entity but, as far as possible, the Veritau 'group' would operate as a single entity with common systems, working practices and one overall management structure. Specific governance rules will also be established to ensure that the two companies in the Veritau 'group' operate and take decisions in the context of a common understanding and shared vision. To ensure effective communication between the two boards of directors, copies of agendas and minutes of meetings will be circulated between each. In addition, at least one of the directors appointed to the board of VNY will also be a director of Veritau Limited.
- 24 The Veritau management team will be responsible for all aspects of VNY's operational management. The specific responsibilities of the Board of Directors and the management team will be set out in a scheme of delegation (similar to the one adopted for Veritau). Transfer pricing arrangements need be established between the two companies to reduce the risk

of challenge by HMRC but these will be kept simple to avoid any unnecessary additional administrative burden.

- 25 A draft budget has been prepared for the Veritau 'group'. The budget reflects the economies of scale which will be possible by operating an expanded business. For 2012/13, the proposed daily fee rate for internal audit and counter fraud services to the district councils will be £225¹. The fee represents a reduction of 4.3% on the existing fee rate chargeable by NYAP. It is also proposed that the daily fee rate charged by Veritau to the council and NYCC will be reduced to £225 in line with this revised rate. This will represent a saving to the council of approximately £13k pa (2.0%) on existing fees.
- 26 Veritau has a contract with PricewaterhouseCoopers (PWC) for the provision of specialist computer audit services. These services will be made available to the district councils on request but would be recharged at cost.
- 27 Set-up costs will be incurred as a result of the creation of VNY and the transfer of services from NYAP. These costs will include the provision of legal advice, additional licences for IT applications and support to staff through the change process. It is estimated that these costs will be approximately £16k. It is proposed that the actual set-up costs will be shared 50/50 between Veritau and NYAP. Veritau's share of the set-up costs together with an initial capital contribution of £10k will be met from the company's reserves. It is also recognised that NYAP will incur some expenditure in winding up the partnership, for example, the costs of any redundancies. These costs will be met from the partnership's reserves.
- 28 The existing support service arrangements (legal, IT, finance, HR and payroll) which are currently provided to Veritau by the Council and NYCC will be extended to include VNY.
- 29 A detailed action plan has been prepared to complete the implementation process. Subject to approval, a project board comprising officers from Veritau and NYAP will oversee the set up of VNY and complete the transfer of services and employees to the new company.

Benefits

¹ This assumes that there is no increase in the JNC national pay rate for 2012/13.

- 30 The key benefits of the proposal to the council and NYCC as shareholders in Veritau are that it will:
- help achieve greater critical mass and hence provide scope to further improve the resilience and capacity of the existing services provided by Veritau
 - deliver cost savings to the council and NYCC. These cost savings will be achieved by sharing overheads, reducing unproductive time and greater economies of scale
 - further enhance the focus on service delivery, professionalism and quality
 - further increase the opportunity for staff to specialise as well as enhancing career opportunities, resulting in greater staff satisfaction and retention
 - further reduce reliance on key members of staff for service continuity
 - enable the council and NYCC to retain full control of Veritau (whilst offering the district councils influence over VNY)
 - avoid the need for the council and NYCC to value their existing shareholding in Veritau and for the district councils to purchase a proportion of the shares
 - avoid any risk to the council's investment in Veritau should VNY encounter future financial or operational difficulties. Veritau could continue trading even if the wider 'partnership' failed
 - offer greater transparency since the different parts of the business will be trading as separate entities.
- 31 The proposed structure of the expanded business is considered less likely to be subject to challenge under EU public procurement legislation (Teckal) compared to granting the district councils a minority shareholding in Veritau itself. The approach also offers a model for any further expansion of the company, for example to accommodate other future public sector partner organisations.

Timetable

- 32 The district councils have already obtained approval from their respective member decision making bodies to wind-up NYAP and to transfer their internal audit and counter fraud services to Veritau on 1 April 2012. Formal approval to the proposed expansion of Veritau however still needs to be obtained from both the council and NYCC (as Veritau's existing shareholders).
- 33 Details of the proposals are due to be presented NYCC's Executive on 20 December 2011 and the Cabinet on 10 January 2012.
- 34 Details of the outline timetable necessary to establish VNY are set out below:

Action	Target Date for Completion
Formal consultation with NYAP staff to be completed	31/12/2011
Staffing establishment in VNY to be confirmed	15/1/2012
Pension admission agreement to be finalised	31/1/2012
Company formation and issue of share capital	31/1/2012
Appointment of directors to the board of VNY	31/1/2012
Legal agreements to be finalised	28/2/2012
Client officers to be appointed	28/2/2012
Business Plan (3 year) to be approved by board of VNY	15/3/2012
2012/13 budget to be approved by board of VNY	15/3/2012
Formal transfer of services and staff to VNY	1/4/2012

Consultation

- 35 Not relevant for the purpose of the report.

Options

36 Not relevant for the purpose of the report.

Analysis

37 Not relevant for the purpose of the report.

Corporate Priorities

38 This report contributes to the council's overall aims and priorities by helping to ensure probity, integrity and honesty in everything it does.

Implications

39 There are no implications to this report in relation to:

- **Finance**
- **Human Resources (HR)**
- **Equalities**
- **Legal**
- **Crime and Disorder**
- **Information Technology (IT)**
- **Property**

Risk Management Assessment

40 The council will fail to properly comply with the CIPFA Code of Practice for Internal Audit in Local Government if the results of audit work are not reported to those charged with governance.

Recommendation

41 Members are asked to:

- (a) Note the progress made in delivering the 2011/12 internal audit work programme, and current counter fraud and information governance activity.

Reason

To enable members to consider the implications of audit and fraud findings.

- (b) Comment on the proposals to establish a subsidiary company (Veritau North Yorkshire) to undertake work transferred from the North Yorkshire Audit Partnership, prior to consideration of the proposals by the Cabinet.

Reason

As part of the committee's responsibility to consider reports dealing with the management of internal audit

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**Report
Approved**



Date 22/11/11

Specialist Implications Officers

Not applicable

Wards Affected: Not applicable

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For further information please contact the author of the report

Background Papers

- 2011/12 Internal Audit & Counter Fraud Plan
- NYAP Integration Report and Action Plans

Annexes

Annex 1 – 2011/12 Audits Completed and Reports Issued
Annex 2 – Counter Fraud Activity