

Audit Committee – 25 September 2012

Statement of Accounts 2011/12 – Annual Governance Statement and Review of Effectiveness

Summary of Report

This report contains the findings of the review of the effectiveness of the council's systems of internal control and internal audit for consideration by Audit Committee. It contains the Annual Governance Statement (AGS) to go alongside the 2011/12 Statement of Accounts (SoA) for review and approval in accordance with the Accounts and Audit Regulations 2011.

Recommendations

Audit Committee are recommended to:

1. Note the new requirement within the Annual Governance Statement to contain a statement on whether the authority's financial management arrangements conform with the governance requirements of the CIPFA *Statement on the Role of the Chief Financial Officer in Local Government (2010)* as set out in the *Application Note to Delivering Good Governance in Local Government: A Framework*; and where they do not, an explanation of how they deliver the same impact.
2. Receive, consider and approve the findings arising from the annual governance effectiveness review, including the review of the systems of internal control and internal audit.
3. Note that the final AGS will be signed by the Chief Executive and Leader as close to the 25th September Audit Committee date as possible to ensure it is as up to date as possible and
4. Receive, consider and approve the Annual Governance Statement as set out in Appendix 1, subject to minor amendments arising from 3 above.



James T Walsh – Chief Finance Officer
14 September 2012

Background

The latest guidance, the Accounts and Audit (England) Regulations 2011, states that the council is responsible for ensuring that the financial management of the council is

adequate and effective and that it has a sound system of governance, including internal and financial control, which facilitates the effective exercise of its functions and which includes arrangements for the management of risk. The council is required to obtain assurance that its governance framework and internal control system is operating effectively in all areas of corporate governance.

The council is further required to publish a statement formally acknowledging that it has maintained effective internal control, including effective internal financial control, during the course of the financial year. The statement should include financial management, arrangements for the management of risk, and include its corporate governance arrangements. The authority must conduct an annual review of the effectiveness of its system of internal control. In addition, it must undertake an annual review of the effectiveness of its system of internal audit, which is the framework of assurance available to satisfy a local authority that the risks to its objectives, and the risks inherent in undertaking its work, have been properly identified and are being managed by controls that are adequately designed and effective in operation.

The findings of these reviews must be considered by the members of the body meeting as a whole or by a committee. This function is undertaken by the Audit Committee.

Finally, the committee must approve an annual governance statement (AGS). The AGS must accompany the body's statement of accounts for that financial year.

Resource and Legal Considerations

Council's must produce annual accounts in line with the Accounts and Audit Regulations 2011 in a timely fashion and on an annual basis. The AGS accompanies the annual accounts.

Performance Management and Risk Management Issues

Performance Management

Effective performance management is key to ensuring an effective system of internal control is maintained. Senior managers can support the framework and the assurance gathering process by ensuring that systems and processes are in place within each directorate, including ensuring directorate plans, project and individual risk registers, risk assessments and project registers are in place and regularly reviewed and service complaints are responded to and used to drive improvement. In addition, senior officers within each directorate should promptly implement agreed internal and external audit actions within the timescale planned.

Assurance statements were required from executive directors, requiring them to provide assurance that controls were in place and operating during the financial year, and where weaknesses were identified, to confirm that actions are in place which are being actively managed. All statements have been returned and where control weaknesses identified, these have been included in the AGS.

Risk Management

The key aspect of the system of internal control is the identification of key risks to the organization and key controls needed to mitigate these risks. The AGS is legally required to be signed by the Chief Executive and Lead Member. The Chief Finance Officer (CFO) also signs the AGS and has done so again this year as a significant proportion of the internal control and internal audit framework falls within his remit and to reflect accountabilities. The requirement falls on the authority and not, as previously, on an individual officer (CFO).

Equality Implications

None relating directly to this report.

Consultation

The report is prepared in consultation with the Chief Finance Officer (CFO), the Head of Internal Audit, the Monitoring Officer, the Leader of the Council, the Chief Executive and relevant managers. It has been shared with the council external auditors, Grant Thornton.

Governance

The governance framework is an interrelated system that brings together an underlying set of legislative requirements, governance principles and management processes. The framework is intended to support council's in demonstrating good governance. The framework itself is not a statutory requirement, but rather a discretionary code offered to organisations as good practice. It is important to note that the governance statement covers all significant corporate systems, processes and controls, spanning the whole range of the authority's activities, including in particular those designed to ensure that:

- The council's policies are implemented in practice
- Services are delivered efficiently and effectively
- The council's values and ethical standards are met
- Laws and regulations are complied with
- Required processes are adhered to
- Financial statements and other published performance information are accurate and reliable
- Human, financial, environmental and other resources are managed efficiently and effectively.

For the 2011/12 Annual Governance Statement, there is a new requirement to contain a statement on whether the authority's financial management arrangements conform with the governance requirements of the CIPFA *Statement on the Role of the Chief Financial Officer in Local Government (2010)* as set out in the *Application Note to Delivering*

Good Governance in Local Government: A Framework, and where they do not, an explanation of how they deliver the same impact.

The Statement sets out five principles which define the core activities and behaviors that belong to the role of the CFO and the organisational arrangements needed to support them. These are as follows:

The Chief Financial Officer in a public service organisation:

- 1) Is a key member of the Leadership Team, helping it to develop and implement strategy and to resource and deliver the authority's strategic objectives sustainably and in the public interest;
- 2) Must be actively involved in, and able to bring influence to bear on, all material business decisions to ensure immediate and longer term implications, opportunities and risks are fully considered, and alignment with the authority's financial strategy; and
- 3) Must lead the promotion and delivery by the whole authority of good financial management so that public money is safeguarded at all times and used appropriately, economically, efficiently and effectively.

To deliver these responsibilities the Chief Financial Officer:

- 4) Must lead and direct a finance function that is resourced to be fit for purpose; and
- 5) Must be professionally qualified and suitably experienced.

In assessing these five principles, it is considered that the Authority complies with all but one. This relates to Principle 1, which states further that "*the CFO is a key member of the Leadership Team reporting directly to the Chief Executive with status at least equivalent to other members of the team*". In Walsall the CFO (Assistant Director of Finance) reports to the Executive Director Resources, who reports to the Chief Executive. The CFO attends the Leadership Team (the corporate management team), has access to all confidential papers/matters, has direct access to and meets frequently with the Chief Executive, and has direct access to members, including Cabinet and Audit Committee.

Review of Effectiveness of Governance Arrangements, including the Systems of Internal Control and Internal Audit

Process

The assurance gathering process is a well-established and structured link between the strategic objectives and statutory requirements of the authority and how these objectives are to be delivered. It requires the identification of key controls that are

deemed critical to the delivery of these objectives and expects a formal review and risk assessment for the management and delivery of these key controls.

A review of the governance framework, including the internal control and internal audit environment and its' effectiveness was undertaken by the Head of Finance (Deputy Chief Finance Officer), supported by the Head of Internal Audit and Monitoring Officer, and in liaison with other senior managers, the Chief Executive and Chief Finance Officer. The findings of this review are set out in section 4 of the AGS.

Findings of the Effectiveness Reviews

The AGS was drafted, assurances were evaluated and supporting evidence gathered. The outcome of this process was a conclusion that the effectiveness of the system of internal control and system of internal audit is adequate overall. The latter is supported by the external audit conclusion within the Interim Audit report published June 2012 "*the Internal Audit service continues to provide an independent and satisfactory service to the Council and that we can take assurance from its work in contributing to an effective internal control environment at the Council*".

A number of control weaknesses were identified and these are set out in section 4 of the AGS in more detail. Those areas where there are controls which require improvement have identified action plans which are in place. In addition, the 2011/12 AGS (Appendix 1, section 5) identified two significant governance issues.

The CFO signs off the AGS and the review of effectiveness prior to endorsement and sign off by the Chief Executive and Leader of the council.

Background Papers

Local Code of Governance

CIPFA Statement on the Role of the Chief Financial Officer

CIPFA/SOLACE: Application Note to Delivering Good Governance in Local Government: A Framework

Audit and Accounts Regulations 2011

Various external and internal audit and inspection reports

Head of Internal Audit report on adequacies of the council's control environment

Various CIPFA Guidance

Various council documents and reports

Grant Thornton Annual Audit Letter and Interim Audit

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Annual Governance Statement

1. Scope of responsibility

This statement is given in respect of the 2011/12 statement of accounts for Walsall Council. Walsall Council is responsible for ensuring that its business is conducted in accordance with the laws and proper standards, and that public money is safeguarded and properly accounted for, and used economically, effectively and efficiently. Walsall Council also has a duty under the Local Government Act 1999 to make arrangements to secure continuous improvement in the way its functions are exercised, having regard to a combination of economy, efficiency and effectiveness.

In discharging this overall responsibility, Walsall Council is responsible for putting in place proper arrangements for the governance of its affairs, facilitating the effective exercise of its functions, and includes arrangements for the management of risk.

Walsall has approved and adopted a Code of Governance, which is consistent with the principles of the CIPFA/SOLACE Framework Delivering Good Governance in Local Government. A copy of the code is on our website or can be obtained from the Monitoring Officer or Chief Finance Officer. This statement explains how Walsall Council has complied with the Code and also meets the requirement of regulation 4(2) of the Accounts and Audit Regulations 2011.

2. The purpose of the Governance Framework

The governance framework comprises the systems and processes, and culture and values, by which the authority is directed and controlled and its activities through which it accounts to, engages with and leads the community. It enables the authority to monitor the achievement of its strategic objectives and to consider whether these objectives have led to the delivery of appropriate, cost-effective services.

The system of internal control is a significant part of that framework and is designed to manage risk to a reasonable level. It cannot eliminate all risk of failure to achieve policies, aims and objectives and can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of Walsall Council's policies, aims and objectives, to evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The governance framework has been in place at Walsall Council for the year ended 31 March 2012 and up to the date of approval of the statement of accounts.

3. The Governance Framework

The Council acknowledges its responsibilities in ensuring the following key elements of the governance arrangements including the system of internal control, are in place and this statement provides further information on how it achieves this, including:

- Identifying and communicating the authority's vision and intended outcomes for citizens and service users, reviewing the vision and its implications for the authority's governance arrangements
- Establishing and monitoring the achievement of the Authority's objectives, including measuring the quality of services for users and customers
- Establishing clear channels of communication with the community and stakeholders, ensuring accountability and open consultation
- The facilitation of policy and decision making

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- Complying with established policies, procedures, laws and regulation, including how risk assessment is embedded in the activity of the Authority, how leadership is given to the risk management process, and how staff are trained or equipped to manage risk in a way appropriate to their authority and duties
- Complying with the Local Code of Governance
- Ensuring the authority's financial management arrangements conform with the governance requirements of the CIPFA Statement on the Role of the Chief Finance Officer in Local Governments (2010)
- Defining and documenting the roles and responsibilities of the executive, non-executive, scrutiny and officer functions of the council
- Developing, communicating and embedding codes of conduct and defining standards of behaviour
- Undertaking the core functions of an Audit Committee
- Whistleblowing and receiving and investigating complaints from the public
- Identifying and supporting development needs of members and senior officers
- Financial management of the Authority and its reporting
- Ensuring the economical, effective and efficient use of resources and for securing continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness
- Performance of the Authority
- Programme and project management
- Incorporating good governance arrangements in respect of partnerships and other group working.

The internal control environment and governance framework is an integral part of the council's Walsall Performance Framework (WPF). The WPF (diagram 1 overleaf) sets out how the various planning processes interlink and jointly demonstrate how services and resources are managed. It is the framework within which the council operates and is underpinned by functional frameworks that provide guidance and protocols, comprising financial, performance, risk, communication and political management processes. The WPF exists to embed performance management and continuous improvement into our normal business activities and shows how services and activities are regularly measured and monitored to enable effective decision making, helping to ensure the council delivers efficient, customer focussed services that provide value for money.

It connects the following:

- Sustainable Community Strategy
- Corporate Plan, vision, pledges and values
- Service planning (of all levels) of the council and its partners
- Financial planning (of all levels)
- Local Area Plans
- Individual Employee performance assessment (EPA)

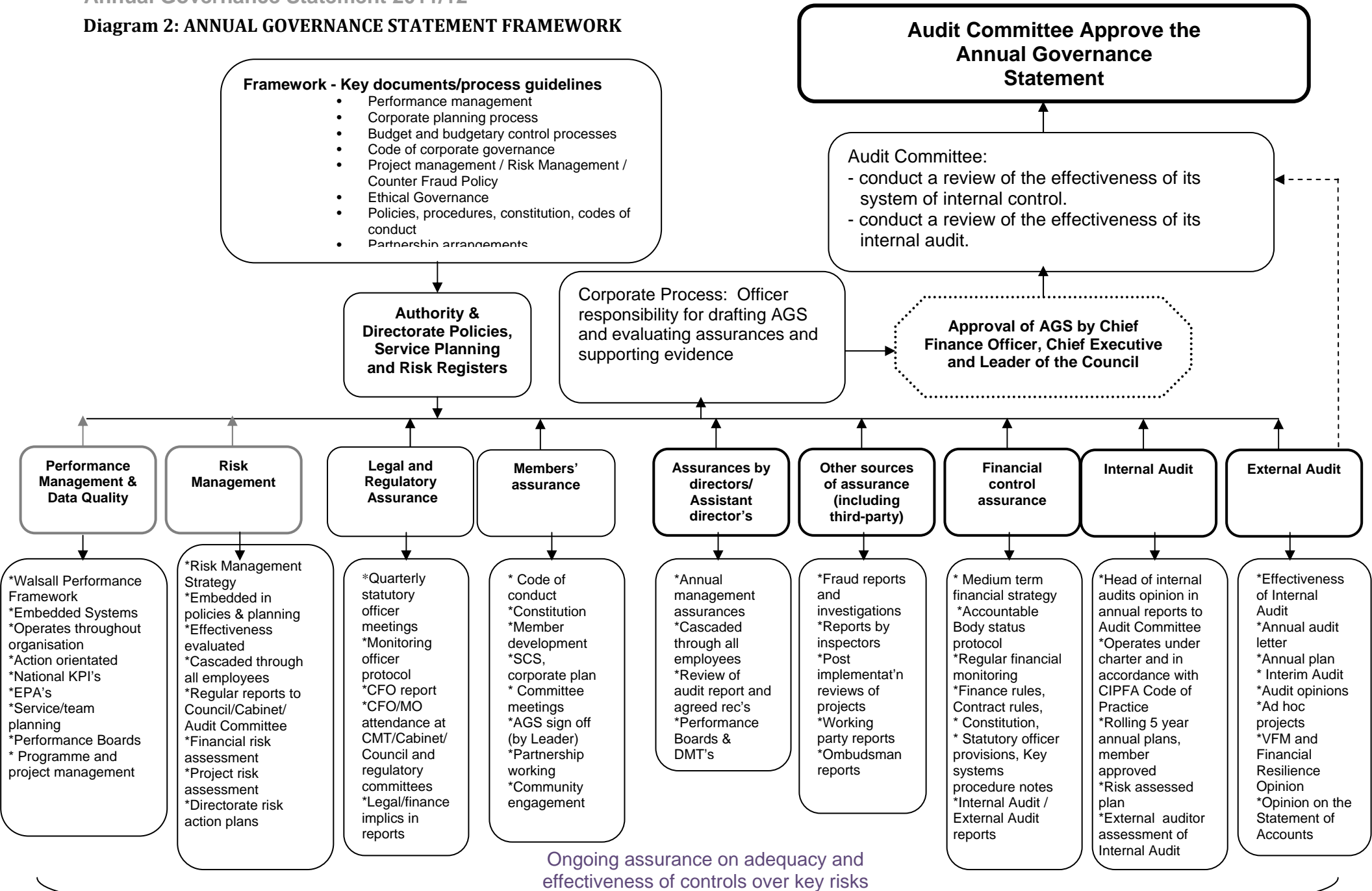
All of which take place in an environment of stakeholder influence, audit and inspection, internal control and monitoring in order to develop continuously improving services.

Diagram 1: The WPF



The governance framework consists of regular management information, financial and contract rules, established financial, budgetary, personnel and other procedures, a performance management framework, community and corporate planning, management supervision in accordance with the corporate employee performance assessment (EPA) framework, a comprehensive risk management strategy and process, project management methodology and a system of officer and member delegation and accountability and codes of conduct. Diagram 2 shows the overall governance framework which is discussed in more detail in this section.

Diagram 2: ANNUAL GOVERNANCE STATEMENT FRAMEWORK



The council acknowledges its responsibility for ensuring that effective governance arrangements, including an effective system of internal control (including financial control), are maintained and operated in connection with the resources concerned. Any system of internal control, including internal financial control can provide only reasonable and not absolute assurance that assets are safeguarded, that transactions are authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected within a timely period. Development and maintenance of the system is undertaken by managers within the council.

In particular, the system includes the following key elements:

- A sustainable community strategy, setting out ambition, objectives and priorities of the council and key partners, developed following extensive consultation with the community and stakeholders – linked to corporate and service planning.
- A comprehensive risk management strategy and framework, operating at both strategic and operational levels;
- A comprehensive programme and project management approach;
- A risk assessed Internal Audit programme which is planned in advance to cover all major systems of internal control and which is based on a risk assessment of key systems and controls;
- A comprehensive financial strategy, including budget management and control framework, supported by financial procedures and guidelines underpinning sound financial management, reporting and standing;
- An approved Constitution, including financial and contract rules and a scheme of delegation and decision making processes of the council;
- Clear measures of financial and other performance through a comprehensive performance management framework, linked to service planning and the corporate plan;
- The preparation of regular performance and financial reports to managers, executive directors, Corporate Management Team (CMT) and elected members which indicate actual expenditure against budget and highlight remedial action, where required;
- Clearly defined capital expenditure strategy and guidelines;
- Project management principles adopted as the methodology for projects, requiring projects to be managed using the same underlying principles and regular reporting of progress to CMT and directorate teams;
- Use of an accountable body status protocol when the council acts as accountable body for funds, including in relation to partnership working to ensure that activities are administered consistently and robustly across the council;
- Performance boards (in most directorates) which receive, consider and assess service planning and performance measures, financial planning and project management processes to influence and drive continuous improvement;
- Human resources and other policies and procedures, including codes of conduct (member and officer), whistle blowing policy and an anti-fraud and anti-corruption policy and strategy;
- Standards Committee, Audit Committee, scrutiny function and other regulatory committees;
- Member and officer development strategy and individual development planning processes;
- Statutory Monitoring and Chief Finance Officers ensuring the council operates within existing legislation and statutory guidance;
- Comprehensive communication and consultation arrangements both internally and externally.

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For 2011/12, the AGS is required to contain a statement on whether the authority's financial management arrangements conform with the governance requirements of the CIPFA *Statement on the Role of the Chief Financial Officer in Local Government (2010)* as set out in the *Application Note to Delivering Good Governance in Local Government: A Framework*. The Statement sets out five principles which define the core activities and behaviours that belong to the role of the CFO and the organisational arrangements needed to support them. In assessing these five principles, the Authority complies with all but one. This relates to Principle 1, in that *"the CFO is a key member of the Leadership Team reporting directly to the Chief Executive with status at least equivalent to other members of the team"*. The Statement also states that if this is not the case then the reasons should be explained publicly in the AGS and an explanation of how the actual arrangements deliver the same impact. In Walsall the CFO reports to the Executive Director Resources, who reports to the Chief Executive. The CFO attends the Leadership Team (the corporate management team), has access to all confidential papers/matters, has direct access to and meets frequently with the Chief Executive, and has direct access to members, including Cabinet and Audit Committee.

There are a number of key elements of the governance framework and internal control environment which ensures the council is able to monitor and manage the achievement of its objectives. These are included in the council's published overarching strategies and plans including; the sustainable community strategy; the corporate plan; medium term financial strategy, corporate budget plan, capital strategy, risk management strategy; treasury management strategy; programme and project management approach, and directorate strategy and planning documents.

These documents set out the council's priorities, vision and key pledges. They are supported by directorate plans, which contain measures designed to support the achievement of council objectives.

The council is committed to continuous improvement but recognises that it cannot achieve this without community and partner engagement. It is committed to working with partners through the Walsall Borough Strategic Partnership (our Local Strategic Partnership), and with the community and partners, through the Area Partnerships.

During 2011/12, the Council continued to implement the "systems thinking" methodology within services and develop its Working Smarter review programme, aimed at delivering customer service improvements, financial savings and improved staff morale. This represents a cultural shift in the way the council thinks about the design and management of its services. It starts by getting a clear understanding of "what matters" to the people who use our services, involving those employees who deliver the service. Employees, supported by their managers, critically analyse the current service to find out "what matters" and then they assess the council's capability to deliver "what matters".

Following the analysis the service is re-designed, focusing on those steps which are of value in customer terms, which releases capacity which can either be realised as cashable savings or re-invested in new or additional services.

A large number of reviews have now been completed and a number of officers have been trained in the intervention methodology. In June 2011, a lessons learned event was held where representatives from all of the reviews were asked to identify "what has worked well" and "what hasn't worked so well". The feedback from the event demonstrated the Council has yet to reach a tipping point in changing its culture from pre-dominantly command and control to one based on system thinking principles. Following the workshop and our learning from reviews undertaken to date, a revised system intervention methodology has been developed.

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The council's constitution sets out how the authority operates and refers to required procedures to be followed to ensure all activity is transparent and accountable to the local community. This includes a scheme of delegation and contract and finance rules, which set out the control environment in which the council operates.

A key aspect of the system of internal control is the identification of key risks to the organisation and key controls needed to mitigate these risks. Comprehensive, embedded and effective performance and risk management arrangements are fundamental to demonstrating good governance.

The council has an established comprehensive risk management framework, designed to identify, evaluate, manage and where possible, mitigate risks to the council in delivering its objectives. There is an ongoing programme of reporting and review of both strategic and operational risks, and this extends to an assessment of risks in financial planning and major projects and partnerships.

Strategic risks are identified, evaluated, incorporated into a corporate risk register and reported to senior management and CMT. This includes actions to mitigate risks, as appropriate, for each key strategic risk. Cabinet also receives reports on risk management. The risk management strategy is reviewed annually by Cabinet and is subject to examination by the Audit Committee as part of its established regulatory activities. In 2009/10, a review of the effectiveness of Audit Committee was undertaken by Grant Thornton, an action plan is in place to address their recommendations, and progress against this is reported to Audit Committee.

Each directorate has identified directorate risks and work continues to ensure that the actions arising from these take proper account of the balance of risk and resources to ensure that appropriate and proportionate action is put in place. Financial risks are assessed regularly and as part of the annual budget process and regular reporting of the financial position. A corporate financial risk assessment informs the medium term financial strategy and the level and appropriateness of general and other reserves. Each directorate has a risk champion and all individual posts are risk assessed within the council and are subject to review. Risk workshops are held to ensure risk champions and those involved in the assessment and management of risk are appropriately trained.

Arrangements for the provision of Internal Audit are contained within the council's Constitution. The council, via its statutory Chief Finance Officer (CFO) must ensure that there is an adequate and effective Internal Audit of accounting records and of its systems of internal control as required by the Accounts and Audit Regulations 2011.

The Constitution states that:

- The Head of Internal Audit has the right to report directly to the Chief Executive, executive directors and elected members when this is appropriate, as well as routinely reporting to the CFO and operational managers;
- Internal Audit operates in accordance with the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom under the day-to-day control of the Head of Internal Audit who acts independently;
- The Internal Audit service plans and prioritises its work through a combination of assessment and review of the council's service provision, corporate governance arrangements, risk management processes and key internal control systems, supplemented by a programme of fraud and irregularity/consultancy work and scheduled visits to council establishments;

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- The annual work plan is endorsed by CMT and Audit Committee. Reports, including an assessment of the adequacy of control and action plans to address weaknesses, are submitted promptly to executive directors, senior managers, school heads and chairs of governors as appropriate. Regular progress reports are submitted to the council's Audit Committee for review purposes;
- The Head of Internal Audit is required to report annually on her opinion in respect of the overall adequacy and effectiveness of the council's internal control environment.

Executive directors are required to provide annual assurance statements that agreed audit actions are being implemented, and where control weaknesses are identified, to put in place remedial action in a timely manner, and as agreed with audit. They are also required to provide an annual assurance statement to acknowledge that internal controls were in place and operating effectively for the financial year; and that where weaknesses were in place, corrective action was being actively and effectively taken and managed.

The Audit Committee receives reports of audits receiving a no or limited assurance opinion and external audit recommendations and actions, and on risk management and seeks to ensure that control weaknesses where identified are addressed. The Committee has a function in respect of the system of internal control and its effectiveness and the work of the Committee includes the review of the Annual Governance Statement and its approval in September of each year.

4. Review of Effectiveness

Walsall Council (via Audit Committee) has responsibility for conducting, at least annually, a review of the effectiveness of its governance framework including the system of internal control and its internal audit.

The process that has been applied in maintaining and reviewing the effectiveness of the governance framework is set out below,

Audit Committee is able to monitor the effectiveness of the governance framework and the internal control environment and the council's internal audit, and receive their assurance on these matters in a number of ways. Further detail is set out in the following paragraphs and the totality of these is reviewed and considered by Audit Committee in considering the annual review of the effectiveness of the governance framework and approving the Annual Governance Statement as required by the Accounts and Audit Regulations, 2011, section 4 (3).

The review of the effectiveness is informed by and assurance obtained from:

- The annual work programme of Audit Committee including receiving, considering and reviewing reports on the work of internal and external audit, including reports on internal controls, risk management, grants, the external auditor's Interim Audit, it's opinion on VFM and financial resilience of the council, the external audit opinion on the statement of accounts and the annual audit and inspection letter.
- The Head of Internal Audit's annual report.
- Findings of the external auditor and other review agencies and inspectorates.
- Cabinet, CMT and senior officers monitoring the effectiveness of the governance framework through receiving regular monitoring reports on performance management, financial management, programme and project management and risk management, including progress against key objectives and measures and corrective action planning; the overall financial position; updates on performance in relation to

- management of key risks to the organisation; and receive regular reports via Audit Committee on the internal control mechanisms in place and their effectiveness.
- Annual changes made to the framework or reporting therefore, approved by Audit Committee. On the 27 October 2011, CMT approved changes to the means by which Internal Audit report to Audit Committee to strengthen governance arrangements and to ensure that the information presented to Audit Committee better assists the Committee in discharging its duties, as follows:
 - A 6 monthly Internal Audit progress report with the emphasis on assurance with a summary of work finalised during the period; themes identified during the course of audit work undertaken; and resultant organisational health measures.
 - Routine reporting of audit reports which receive a no and limited assurance opinion, where accountable executive directors and their managers are asked to attend Audit Committee to give members of the Committee the necessary assurance that concerns identified are being addressed. With the emphasis focused on 'assurance', this ensures that those reports warranting attention are appropriately directed to those charged with governance.
 - The work of the executive directors and managers within the authority who have responsibility for the development and maintenance of the governance environment. For example, in order to support more effective governance, CMT on 22 September 2011 approved a new audit reporting regime. The key approved changes were as follows:
 - A new audit report format was introduced with the emphasis on assurance.
 - Problems / weaknesses which remained unaddressed from the last audit are now categorised as 'prior audit open findings'. The emphasis is no longer on the implementation of agreed actions but on whether the problems / weaknesses still exist.
 - Attached to the terms of reference issued to accountable managers prior to the commencement of each audit is the previous audit report. This acts as an aide memoir to managers of the areas identified during the last audit. This way, managers are reminded of what may potentially be an 'open' problem or weakness, on which they need to focus their attention.
 - Quarterly summary reports of audit actions confirmed by managers as being implemented are no longer sent to executive directors, and follow up memos seeking managers' 'self certification' of audit report actions are no longer issued. Executive directors and their accountable managers are now responsible for addressing issues identified within audit reports. With the emphasis focused on 'assurance', the current practice of no and limited assurance audit reports presented to Audit Committee ensures that those reports warranting attention are appropriately directed to those charged with governance. A standard early audit follow up process of all no and limited assurance audit reports issued, strengthens governance arrangements further in ensuring weak areas identified are promptly addressed by accountable managers.
 - In addition, CMT, the Leader and elected members, via the Audit Committee formally consider and approve the Annual Governance Statement (AGS) annually.

Head of Internal Audit Assessment of Governance and Internal Control Effectiveness during 2011/12

The review of the effectiveness of the system of internal control and internal audit is informed by the work of the Head of Internal Audit and her annual report on the overall adequacies of the internal control environment.

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Head of Internal Audit Assessment of Governance and Internal Control Effectiveness during 2011/12:

The review of the effectiveness of the system of internal control is informed by the work of the Head of Internal Audit and her annual report on the overall adequacies of the internal control environment. In respect of the 2011/12 financial year, the following opinion has been given by the Head of Internal Audit;

“In my opinion, formed solely on the basis of the work undertaken by internal audit and its partner organization in 2011/12, and the positive action taken or intended to be taken by managers to implement agreed audit report actions, Walsall Council’s overall system of internal control facilitates the effective provision of the council’s functions and provides a significant level of assurance regarding the effective, efficient and economic exercise of the council’s functions.

Control weaknesses were identified during the 2011/12 financial year and were reported as such to relevant managers. The opinion as to the level of assurance that can be placed on the system of internal control is based on an assurance that accountable managers address findings within the agreed audit report action plans in the areas for which they are responsible.

The system of internal control can only provide reasonable and not absolute assurance regarding the achievement of the council’s policies, aims and objectives. The opinion is based on work in the approved operational audit plan, including irregularity, consultancy and advisory work carried out in 2011/12.

All audit work is subject to agreed terms of reference, objectives and resources allocated by the council for that purpose.”

Executive Director Assurance

Executive directors each provide an assurance statement that, for AGS purposes, they are satisfied that appropriate action has been taken by managers to implement the agreed recommendations / actions arising from audits in 2011/12. In addition, they provide assurance that controls were in place and operating effectively.

One area was identified in the annual assurance statement from the Executive Director – Resources of control weakness. This relates to an Internal Audit investigation identified below relating to anonymous allegations received concerning practices within human resources. The matter has been reported to Audit Committee and actions put in place to address the findings.

Statutory Officer Assurances

Both the Monitoring and Chief Finance officers provide assurance statements on the governance and internal control environment. Other than the matter mentioned above, no other items of concern or internal control weakness were raised in respect of the internal control or internal audit environment.

Effectiveness Review of Internal Audit

The Accounts and Audit (Amendment) Regulations 2011 introduced a revised requirement for the council to conduct ‘an annual review of the effectiveness of its internal audit’. This includes the effectiveness of the internal audit function, wider assurance on the system of internal audit and the Audit Committee itself.

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A self-assessment document is produced annually by the Head of Internal Audit in respect of the effectiveness of the Internal Audit function, assessed against the CIPFA Code of Internal Audit Practice and recent CIPFA guidance. The self-assessment is reviewed independently.

In addition, the council's external auditors, Grant Thornton have undertaken a review of internal audit. In their interim report dated June 2012, they concluded that "*the 'service continues to provide an independent and satisfactory service to the council and we can take assurance from internal audit's work in contributing to an effective internal control environment at the council'.*

Audit Committee has a regulatory role in terms of receiving reports on the effectiveness of the system of internal control through receipt and consideration of Internal Audit quarterly reports. Additionally, Audit Committee receive all internal audit reports receiving a 'no' or 'limited' assurance opinion. A sample of these reports were chosen by Committee for further detailed review and scrutiny during 2011/12; and accountable officers together with their executive directors were called before the Audit Committee to provide necessary assurances.

In addition, Internal Audit has a strategic risk assessed plan which was endorsed by CMT and Audit Committee.

To support their assessment of the council's use of resources, Grant Thornton completed a review of the Audit Committee in order to appraise its effectiveness as an important part of the council's governance framework. Recommendations were made and an action plan drawn up and approved by the Committee on 25th October 2010. Implementation of this is ongoing and progress was reported to Audit Committee during 2011/12. Seven recommendations were made by Grant Thornton, all of which have been implemented.

The system of Internal Audit is assessed as satisfactory overall.

Regulatory Committee - Standards

The functions of the Standards Committee are determined by statute and the Constitution. Standards Committee have a role in ensuring and promoting good ethical conduct. The Constitution clearly sets out the role of officers and members, including the three statutory posts of the Chief Finance Officer (S151 officer), Head of Paid Service and Monitoring Officer. In 2011/12, statutory officer's meetings were held to review and oversee and ensure statutory provisions were being adhered to.

The Localism Act 2011 requires the council to reconstitute its standards committee to deal with potential issues of member conduct. There is a statutory duty under section 27 of the said act for the council to promote and maintain high standards of conduct. To do so the council has to ensure that it has in place a code of conduct for elected members, arrangements for dealing with complaints about elected members behaviour, and a Standards Committee to determine issues of conduct. The council established these processes at a special meeting of Council on 25th June 2012.

Other Supporting Evidence

The effectiveness of the council's governance framework can further be evidenced by the:

- External auditors' annual Interim Audit which includes a review of the council's overarching entity level controls, with three recommendations arising, two relating to the operation of manual journals and one relating to members statements.

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- Quality assurance controls put in place by the Head of Internal Audit and managers, in managing and delivering the Internal Audit service in accordance with the CIPFA code of practice and including such areas as discussion/agreement of the risk based audit plan and each individual audit review;
- The role of the Audit Committee in endorsing Internal Audit's work plan and in their regular review and scrutiny of audit performance and;
- The work of Audit Committee reviewing specific reports which have been awarded no or limited assurance for detailed scrutiny, ensuring the committee is able to be assured that operational and control issues are being dealt with appropriately and that managers' agreed actions are being implemented. The committee are able to seek explanation from managers failing to progress agreed actions.
- The preparation and presentation of an Annual Report to Council of Audit Committee's work, assisting it to discharge the committee duty to provide independent assurance on the adequacy of the council's risk management framework and the internal control and reporting environment.
- The regular review of Internal Audit work by the CFO including meetings with the Head of Internal Audit;
- A high performance and achievement level against targets, including a 99% delivery of the annual audit plan in 2011/12.

The review of effectiveness is also informed and evidenced by the following;

- The Interim Audit report from Grant Thornton contains an interim update on the annual value for money assessment. 3 out of 6 risk areas were assessed as Green (no cause for concern). 3 areas were assessed as Amber (potential risks and/or weaknesses in this area). No areas were assessed as Red (high risk area). The council is confident the 3 Ambers – strategic financial planning (year end outturn position, and delivery of 2011/12 savings, and the risk of legal proceedings impacting on the council's financial stability); financial control (year end outturn and impact on financial control arrangements if the outturn is adverse); and improving efficiency and productivity (in relation to reduction targets for use of natural resources) will move to Green once the final assessment has been made. Indeed the outturn for 2011/12 pre-audit is favourable with a small underspend overall. We are expecting an unqualified VFM opinion.
- The work of the council's external auditors with the 2010/11 Annual Audit letter, published December 2011, including the provision of an unqualified opinion on both the 2010/11 accounts and the council's use of resources (value for money).
- The council has introduced a Local Code of Governance which was approved by Audit Committee and Standards Committee in 2008/09. Review of the Code against the CIPFA/SOLACE framework highlighted some areas of omission (partnership protocol and need for awareness training). A partnership toolkit has now been produced along with a register.
- The Code is reviewed annually by the Chief Finance Officer and the Monitoring officer. The Code will be strengthened further during 2012/13 to include the governance requirements to support the principles in the CFO Statement.

2010/11 Identified Control Weaknesses

The review of effectiveness also covered the work undertaken in 2011/12 to address the control weaknesses identified in the 2010/11 AGS. Payroll and capital programme / project management both received borderline significant opinions. This position has not changed. See below.

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Regarding 2010/11 fraud and irregularity cases, 3 in particular gave cause for concern in the 2010/11 AGS, regarding 2 potential frauds / thefts by officers and 1 creditor payment fraud. Of the 2 frauds, both were proven and the individuals involved have received custodial sentences of 40 months and 12 months (with the option to extend for a further 6 months if the money was not paid back), respectively. Appropriate action to recover losses has taken place in both cases. With regard to the creditor payment fraud, the individual involved was found guilty and received a Community Order with 180 hours of unpaid work.

Controls within these areas have been subject to review and action taken to strengthen them as appropriate.

Internal Audit 2011/12 Identified Control Weaknesses

During 2011/12, Internal Audit reviews were undertaken of the fundamental financial systems. Internal Audit has acknowledged that these key financial systems are operating satisfactorily, all receiving a significant assurance audit opinion. Areas for improvement were noted within the reviews of payroll, accounts payable (creditors), capital programme & project management which required management attention to resolve to ensure that the control environment is fully sufficient and effective within these areas. A borderline significant assurance opinion is given in these areas.

With regard to the 'payroll' review, the summary audit opinion states:

- Generally, the design of work within the payroll service is both sufficient and effective. However with regard to management of work there continues to be significant areas for improvement in ensuring controls and processes are fully effective particularly in the processing of new starters, variations to pay and leavers. It was disappointing to note that there are a number of prior audit findings which remain unaddressed at the time of this audit.
- Areas of good practice noted include; the continuous development and improvement of HR Direct including the sickness absence reporting centre; and a segregation of duties across individual teams such as the HR payroll and training support team and transactional recruitment team.

With regard to the 'accounts payable' review, the summary audit opinion states:

- Generally, the design and management of work in operation within accounts payable is sufficient and effective, although some improvement is required. This is partly due to the introduction of Finance Direct which has been implemented across the council since the previous audit and is still being embedded and also an increase in the uptake of purchase cards. In particular improvements are required for policies and procedures, system security, officer authorisations, invoice goods receipting, payment of invoices and credit notes, delegated bank accounts, purchase cards and data protection.
- Some good practices were noted during the audit, including; robust processes and controls in place for the operation of BACS controls, reconciliations to the general ledger and system interfaces.

With regard to the 'capital programme and project management' review, the summary audit opinion states:

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- Generally, the design (sufficiency of controls) of work in operation within capital programme and project management is sufficient. Management attention is, however, required in the management of work (effectiveness of controls), most notably, in ensuring that effective project management is in place and that inconsistent working practices and controls within start up and initiation, monitoring and reporting and project closure stages of capital programming and project management are addressed. Without management attention in these areas, the risk of project failure, over spends and non-achievement of benefits (efficiencies, savings and customer satisfaction) remains a threat to the capital programme and project management operations.
- Some good practices were noted during the audit including robust processes and controls in place for the approval of the capital programme, contingency and carry forwards.

In addition to fundamental financial systems, audits were undertaken of other financial and non financial systems and processes that contribute to the council's overall corporate governance arrangements. None of these were material in the context of the statement of internal control, with the exception of the review of pay and grading which received a limited assurance opinion. The summary audit opinion for this review states:

- Generally, weaknesses have been identified in both the design (sufficiency of control) and management (effectiveness of controls) of work in operation within pay and grading, which require management attention to address. Most notably, controls require strengthening in relation to project management, ensuring that day to day procedures exist and have been appropriately communicated to relevant staff; that job evaluation and appeals procedures are strengthened with a sufficient audit trail in place; that sufficient and timely management information is in place on which informed decision making can be made; that performance management arrangements are strengthened and that robust arrangements are in place for the mainstreaming of pay and grading.

Internal audit's work identified that although in most audit assignments the processes examined were generally working satisfactorily, system weaknesses were identified in a number of areas as shown in those awarded a limited assurance opinion. Audits awarded a limited assurance opinion are routinely reported to Audit Committee and are subject to an audit follow up review. No audit reviews were awarded a no assurance opinion this year. A number of high priority suggested improvements were made during the year to address control weaknesses and all were or are being agreed for implementation by managers.

Overall 100 specific planned audit reviews were undertaken, excluding unplanned irregularity and consultancy work. Of these:

- 1 review (1%) received a full assurance opinion;
- 91 reviews (91%) received a significant assurance opinion, 9 of these were borderline;
- 8 reviews (8%) received a limited assurance opinion; and
- No reviews received a no assurance opinion.

The limited assurance opinion audits are as follows:

- Children's Fund (Exit Arrangements)
- Children's Centres
- Coroner
- Pay and Grading
- Skip Permit Income

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- Kings Hill School
- Millfield JMI School
- Rough Hay School

In addition, fraud and irregularity work was undertaken by the Internal Audit service during the year. A summary of the audit inquiry work undertaken is routinely reported to Audit Committee. While most cases were not material in the context of the Annual Governance Statement, 3 cases in particular, have given cause for concern this year, namely:

- Weaknesses in grant funding arrangements within the Walsall Arboretum restoration programme;
- Whistle blowing allegations received in respect of procurement practices within social care and inclusion; and
- Anonymous allegations received concerning financial mismanagement within a Children's Centre.
- Controls within these areas have been subject to review and action is or has been taken as appropriate. Action plans are in place for all of these audits and all will be formally followed up during 2012/13.

Two significant governance issues have been identified which are outlined in section 5 relating to whistle-blowing allegations in respect of recruitment and grading practices in HR and the outcome of the OFSTED inspection of safeguarding and looked after children services.

We have been advised on the implications of the result of the review of the effectiveness of the governance arrangement, and a plan to address weaknesses and ensure continuous improvement of the system is in place.

5. Significant Governance Issues

The identification, analysis and management of risks for the delivery of its objectives are key to maintaining an effective system of internal control. It is also recognised that there remains a further need to fully embed the internal control procedures across the organisation.

The officers who drafted this AGS, evaluated assurances and supporting evidence, concluded the effectiveness of the governance framework, including the system of internal control and system of internal audit is satisfactory overall, however, in undertaking the annual review of effectiveness, two significant governance issues have been identified. Further detail is provided below. Other areas of concern in relation to fraud and irregularity, whilst not material for the purposes of the Annual Governance Statement, have been identified and included within the previous section of this statement and action taken as appropriate.

Human Resources

An audit investigation into irregularities was undertaken during the year which concerned practices within human resources. This was concluded and reported to Audit Committee, along with an action plan, on 23rd July 2012 to address a number of significant control weaknesses in recruitment and selection, procurement, and grading practices within human resources.

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An action plan to address these issues is in place and progress in implementing the actions will be reported to Audit Committee to ensure the committee has the necessary assurance that the weaknesses are being addressed in full.

The control weaknesses, whilst significant, were contained solely within the Human Resources services and did not impact on recruitment and selection, procurement, and grading practices across the rest of the organisation.

Inspection of Safeguarding and Looked After Children Services

An inspection of safeguarding and looked after children services was undertaken in June and the findings published on 31 July 2012. The purpose of the inspection is to evaluate the contribution made by relevant services in the local area towards ensuring that children and young people are properly safeguarded and to determine the quality of service provision for looked after children and carers.

Ofsted concluded that Walsall was inadequate in 8 out of the 22 inspection areas, adequate in 12 and good in 2 areas. Services for Looked After Children were judged adequate overall with adequate capacity for Improvement. Safeguarding Services were judged as inadequate for overall effectiveness with inadequate capacity for improvement.

The report can be accessed at <http://www.ofsted.gov.uk/local-authorities/walsall>

A draft improvement plan has been produced to implement the actions outlined in the report and an independently chaired Improvement Board established to oversee the improvement plan. The first meeting of the Board is on 17th September. Progress on improvement plan actions will be reported to Audit Committee.

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Paul Sheehan
Chief Executive
Xx September 2012

In approving this statement, the views and assurances of the statutory officers and Executive Directors have been sought and appropriate evidence obtained to support it.

.....

Councillor Mike Bird
Leader of the Council
Xx September 2012

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In approving this statement, the views and assurances of the statutory officers and executive directors have been sought and appropriate evidence obtained to support it.

.....

James T. Walsh
Chief Finance Officer
Xx September 2012

In approving this statement, the views and assurances of the statutory officers and executive directors have been sought and appropriate evidence obtained to support it.