

LGSS Audit & Risk Management Service

Internal Audit Report

Governance and Financial Management

and Compliance with the Schools Financial

Value Standard (SFVS) –2012/13

Client Customers Communities
and Learning

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Date October 2012
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Status of report Final
Internal Audit Opinion Limited Assurance

Audit Committee Date 20th November 2012

Executive Summary

Assurance Summary

Process Area	No	Limited	Moderate	Substantial	Full
A: The Governing Body and School Staff					
B: Setting the Budget					
C: Value for Money					
D: Protecting Public Money					
Overall					

Note

All Internal Audit reports are available on a confidential basis to Senior Management and the Audit Committee as a matter of course. The main points of this report and the overall assurance level will be summarised for the Audit Committee in a report that is made available within the public domain.

We will follow up the agreed actions contained in this report in line with individual timescales and report on progress to Management and the Audit Committee.

1. Background to the review

The Schools Financial Value Standard (SFVS) was introduced by the Department for Education (DFE) in September 2011. This standard replaced the Financial Management Standard in Schools which was introduced in 2008. The SFVS has been designed in conjunction with schools to assist them in managing their finances and to give assurance that they have secure financial management in place. Governing bodies have formal responsibility for the financial management of their schools, and so the standard is primarily aimed at governors.

Thirty eight schools that had not met the Financial Management Standard in Schools (FMSiS) prior to its withdrawal in November 2010 had a requirement to meet the SFVS by the end of March 2012. As part of the 2012/13 Audit Plan a thematic audit was undertaken on Governance and Financial Management and Compliance with the SFVS in thirty five of these schools during the period April to July 2012. The three remaining schools were due to convert to Academy status and therefore compliance arrangements were not examined. Each school received its own audit report on the day. This report is a collation of those findings in order to provide feedback to appropriate officers within the Council on the schools compliance with the new standard.

The Section 151 Officer is required to provide the following Assurance Statement to the DFE:

"I confirm that I have in place a system of audit for schools which gives me adequate assurance over their standards of financial management and the regularity and propriety of their spending".

It is recognised that schools have local management, however we need to be aware of how well schools comply with legislation, Northamptonshire County Council (NCC) policies and guidance issued to them.

1.1 Key Risks

Service related risks identified at the start of the audit through discussions with key individuals were:

- Schools do not have appropriate Governance arrangements in place leading to inefficient management;
- Schools do not have appropriate Governance arrangements in place for Purchasing and Payments and / or Personnel and Payroll;
- Schools not complying with legislation;
- Schools not complying with NCC policies; and
- Poor Financial Management increasing the risk of fraud and weak budgetary control.

1.2 Objectives

The objectives of the review were therefore to:

- Assess the controls in place at the school to ensure compliance with the SFVS, statutory requirements, Council policy and other relevant codes of practice;
- Assess whether the systems and procedures in place promote good governance and safeguard the assets and interests of the school and Council; and
- Assess whether the systems and procedures in place ensure that the costs of payroll are appropriately monitored and controlled.

2. Internal Audit Opinion, Main Conclusions and Good Practice

Internal Audit's approach for the completion of this review was to visit each school for one day. Discussions were held with the Headteacher and the Bursar and records were examined in the schools. The findings of the audit were discussed with the Headteacher and the Bursar at the conclusion of the audit and agreed in principle. The Headteacher, Bursar and Chair of Governors were provided with a short summary report which could then be presented to the Governing Body.

2.1 Main conclusions

Based on the completion of our fieldwork we are giving **limited** assurance for the control over Governance and Financial Management and Compliance with the SFVS. The table below provides a breakdown on the level of assurance in both areas for the thirty four schools audited.

Governance and Financial Management Level of Assurance			Schools Financial Value Standard Level of Assurance		
Limited	Moderate	Substantial	Not Met	Partly Met	Met
22	8	5	10	24	1

There are key control weaknesses in all process areas, particularly with regards to the lack of management checks in place for:

- Monthly budget monitoring reports: 46% of schools non-compliant;
- Monthly bank reconciliations: 31% of schools non-compliant;
- Monthly payroll reports: 66% of schools non-compliant;
- Monitoring the sequential use of cheques: 49% of schools non-compliant; and
- Income received: 74% of schools non-compliant.

In summary, Headteachers were not completing management checks and were placing too much reliance on the work of their Bursars and Business Managers. This exposes the school to the potential risk of fraud.

In addition to this, Governing Bodies were failing to undertake the following key financial tasks:

- Discuss and agree the School Development Plan and its link to the budget: 74% of schools non-compliant;
- Discuss and review three year financial projections: 62% of schools non-compliant; and
- Ensure that any Private Funds held by the school have been audited: 58% of schools non-compliant.

Effective Governance and Financial Management is fundamental to the system of internal control. Governing Bodies are responsible for ensuring that appropriate controls are in place to reduce the risk of fraud, misappropriation of assets, budget overspends and reputational damage to the school. Governance and Financial Management processes must improve in order for schools to comply with Financial Regulations and to ensure their success in achieving critical strategic objectives.

We are now in the fourth year of having a standard that schools are not meeting. The current SFVS standard is a relaxed version of the original FMSiS which should be more achievable for schools. This report identifies that schools are still not complying with the standard.

In addition, there could potentially be a conflict for traded services such as Finance and Governor Services taking all necessary actions to ensure that there is robust governance in schools, while at the same time seeking to retain their business. And therefore perhaps it is easier for a non-traded service such as Internal Audit to deliver this message. It is therefore recommended that the Director of Customers, Communities and Learning should meet with the Section 151 Officer and the Head of Internal Audit to determine a way forward in relation to ensuring that the SFVS is complied with.

2.2 Good Practice
Areas of good practice are listed at Appendix 1.

2.3 Main recommendations

For each of the issues identified we have made suggested recommendations in the accompanying action plan. When schools comply with the advice given, this will positively improve the control environment and aid the Authority in its ability to effectively manage its risks.

2.4 Acknowledgement

We would like to take this opportunity to thank all members of staff whom we contacted during the course of this review for their time and assistance.

Findings and Management Responses

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>1.</p> 	<p><u>A: The Governing Body and School Staff</u> 37% of the schools did not have appropriate Terms of Reference in place for their Finance Committee or equivalent.</p> <p>A Scheme of Delegation specifying the decision making levels of the Governing Body, its committees and the Headteacher had not been approved in 40% of the schools.</p> <p>There is a risk that schools will fail to achieve key strategic objectives if they do not have appropriate Terms of Reference in place which defines the purpose of a committee and the limits of its authority.</p> <p>Decisions may be agreed at an inappropriate level if the delegated level of authority is not recorded formally.</p>	<p>Financial Regulations state that any delegation of powers to the Headteacher or committees must be recorded.</p> <p>Schools should be strongly advised that:</p> <ul style="list-style-type: none"> the Full Governing Body may delegate certain powers to a committee and in doing so should agree specific Terms of Reference for that committee; Terms of Reference should be reviewed annually by the committee and then taken to the Full Governing Body for approval; and Schools should record the levels of delegation and review and approve these each year in a Scheme of Delegation. 	<p>Although all these aspects are covered in governors' training, not all governors attend training and we cannot force them to. Our newsletters keep governing bodies informed about changes to legislation, etc. and we also promote finance training regularly. We will highlight in strong terms the recommendations for governors from this report in a special newsletter and ensure that all officers in the School Effectiveness team</p>	<p>Rose Kinley October 2012.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
			<p>have sight of these key recommendations also. The recommendations will also be highlighted at Governors' Briefings (although less than 1% of all NCC governors attend these).</p> <p>(For all recommendations)</p>	

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>2.</p> 	<p>46% of the schools did not have a management check in place for the monthly budget reconciliation process, while 31% of the schools did not have a management check in place for the monthly bank reconciliation process.</p> <p>Debtor reports were not provided to School Management in 55% of the schools and 23% of the schools did not provide financial monitoring reports to the Governing Body at least three times a year.</p> <p>Appropriate preventative controls must be in place if School Management are to reduce the risk of fraud, misappropriation of assets, budget overspends and reputational damage to the school. Such controls include a separation of duties and appropriate authorisation of adequate documentation.</p> <p>Governors will be unable to fulfil their financial responsibilities if they are not provided with monitoring reports. A lack of discussion and review of these reports could lead to a failure in strategic financial objectives.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • there must be a monthly reconciliation of the budget recorded on SIMS FMS6 and ERP Oracle; and • a monthly bank reconciliation must take place on a prompt basis. <p>The Headteacher should ensure that both reconciliations are being completed each month. This should be evidenced by their signature on the LB26 SIMS to Oracle Reconciliation form and the LB6 Bank Reconciliation form.</p> <p>In addition to this:</p> <ul style="list-style-type: none"> • Financial reports and a written explanatory report should be presented to the Governing Body on a regular basis; • reference should be made in the minutes to these reports and any points discussed and queried; and • copies of all reports presented should be retained with the minutes of the meeting. <p>The Governing Body agendas should include all relevant financial matters for consideration, such as budgets (original and revised), budget monitoring, financial responsibilities and regulations.</p>	<p>Main points to be raised at next series of seminars (Nov 12).</p> <p>Quarterly LB26s to be checked on receipt that monthly checks have taken place.</p> <p>Half years LB6s to be checked.</p>	<p>LGSS Schools Finance.</p> <p>LGSS Schools Finance.</p> <p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>3.</p> 	<p><u>B: Setting the Budget</u></p> <p>63% of the schools did not have a School Development Plan (SDP) which extended beyond the current year and 74% of the schools had not presented the SDP to the Governing Body for their review and approval.</p> <p>Three year financial projections had not been prepared and presented to governors in 62% of the schools.</p> <p>Schools that do not have a three year strategic SDP in place are missing opportunities to improve and increase the risk of incurring a budget overspend.</p>	<p>Schools should be strongly advised that:</p> <p>They should have a costed and prioritised development plan. The first year should be in detail and the following two years in outline covering all areas key areas i.e. curriculum, staffing and premises.</p> <p>In order to comply with Financial Regulations, schools must:</p> <ul style="list-style-type: none"> • plan on a three year rolling basis; • link the SDP to the budget and resources available; and • prepare and present three year financial projections to governors. <p>Three-year financial plans once produced need to be updated as changes occur and new developments take place.</p>	<p>Main points to be raised at next series of seminars (Nov 12).</p> <p>All schools to submit 3 year plan when Budget Proposal Form for 2013-14 in April 2013.</p>	<p>LGSS Schools Finance.</p> <p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>4.</p> 	<p>23% of the schools had not recorded the formal approval of the budget within the Governing Body minutes.</p> <p>Although 63% of the schools had identified a potential budget deficit in their latest budget plan / projections, they had not discussed it with LGSS Schools Finance and 23% of the schools had not predicted a budget outturn that was comparable to the actual budget outturn.</p> <p>Governing Bodies are responsible for formally approving the annual budget and by not doing so; increase the strategic and financial risks of the school.</p> <p>If school management do not follow guidance issued by LGSS Schools Finance Deficit Budget Policy, they risk formal intervention, which could lead to the removal of the school delegated budget.</p> <p>Appropriate detective controls must be in place if School Management are to reduce the risk of a budget deficit. Such controls include reviews, analyses and variance analyses of financial monitoring reports.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> the budget should be formally discussed and approved by the full Governing Body and this should be recorded in the minutes; a copy of the budget approved should be retained with the minutes; potential budget deficits should be discussed with LGSS Schools Finance and treated in accordance with the Deficit Budget Policy; and the estimated outturn should be appropriately reported and monitored throughout the year. 	<p>Main points to be raised at next series of seminars (Nov 12).</p> <p>Budget Proposal Forms for 2013-14 checked (April and May 2013).</p> <p>Outturn (including deficit) monitored throughout the year.</p>	<p>LGSS Schools Finance.</p> <p>LGSS Schools Finance.</p> <p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>5.</p> 	<p>An Income Policy had not been approved by the Governing Body in 49% of the schools and a Charging Policy had not been approved by the Governing Body in 31% of the schools.</p> <p>If appropriate policies and procedures are not followed for income collection and the charging of services, schools increase their financial risk which could result in incurring a loss.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • each school must have an Income Policy incorporating the administration of income and credit control procedures (if applicable); and • each school must have a Charging Policy stating the rates to be charged for services provided by the school. <p>Both of these policies must be reviewed and approved by the Governing Body annually.</p>	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>
<p>6.</p> 	<p>C: Value for Money</p> <p>34% of the schools had not clearly specified the delegated authority to the Headteacher for purchasing and 20% of the schools had not recorded the discussions on the use of balances within the minutes.</p> <p>Decisions may be agreed at an inappropriate level if the Headteachers delegated level of authority is not recorded formally.</p> <p>There is a risk that the Governing Body and its committees will not make informed decisions if essential elements of the meeting are omitted from the minutes.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • any delegation of powers to the Headteacher must be recorded; and • the minutes should provide a clear and unambiguous record of discussions undertaken at the meetings and the decisions made. 	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>7.</p> 	<p>The Asset Management Plan (AMP) issued by NCC had not been presented to governors in 69% of the schools and 47% of schools did not have a maintenance plan in place for annual and longer term projects.</p> <p>There is a risk that schools will fail to achieve key strategic objectives if they do not review and approve asset management / maintenance plans for annual and longer term projects.</p>	<p>The NCC Property Management Handbook states that the Headteacher and Governors of all Community Schools are responsible for the maintenance of all of the school premises and site. Northamptonshire schools play a vital part in the preparation, review and maintenance of the AMP through undertaking the following tasks:</p> <ul style="list-style-type: none"> • Identifying school priorities for the AMP in the context of their School Development Plan (SDP) and making clear what outputs, either physical or educational, will be achieved in meeting those priorities; • Contributing to the development of County - wide priorities; • Acting as responsible custodians of premises; • Planning, budgeting and managing projects for which they are solely responsible including those covered by devolved or formula funding and those which are self-financed, all in accordance with the AMP priorities and aims; • Assessing the contribution that capital investment makes to the attainment of pupils; and • Co-operating in the preparation of the AMP. <p>School Management should be strongly advised of these requirements and ensure that asset management / maintenance plans are appropriately approved by governors.</p>	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>8.</p> 	<p><u>D: Protecting Public Money</u> 26% of the schools had not presented the previous NCC audit report to Governors and 89% of the schools had not completed the thematic audit self assessments (Personnel and Payroll and Purchasing and Payments).</p> <p>Appropriate audit reporting and monitoring is essential if schools are to ensure that they have sufficient controls in place in order to reduce the risk of fraud, misappropriation of assets, budget overspends and reputational damage to the school</p>	<p>Schools should be strongly advised that:</p> <p>Internal controls are the whole system of controls established by management to safeguard its assets, secure its liabilities and ensure the accuracy and reliability of its records.</p> <p>In layman's terms internal controls are necessary to prevent misuse of school monies and to highlight problems as they occur.</p> <p>It is recommended that:</p> <ul style="list-style-type: none"> • NCC audit reports should be presented to the Governing Body; • a governor or senior staff member should complete two thematic audit self assessments annually with the Bursar; and • the reports should highlight any weaknesses in controls and details should be provided to the Governing Body. 	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>9.</p> 	<p>Management checks were not carried out on the payroll reports in 66% of the schools and the sequential use of cheques was not monitored by the cheque signatories in 49% of the schools.</p> <p>A management check was not in place for the income received and banked in 74% of the schools.</p> <p>Unauthorised / fraudulent activity could go undetected if School Management does not monitor, review and appropriately authorise each of these financial processes.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • a separation of duties should be in place for all financial activities; • management checks should be carried out and evidenced on the payroll reports and income records; • control should be exercised over all cheques issued including ensuring that cheques are used in a systematic manner and in number sequence; and • School Management should sign the manual cheque book stub to confirm that this management check is on place. 	<p>Main points to be raised at next series of seminars (Nov 12).</p> <p>Payroll & Recruitment Services (PRS) will remind School Management via monthly 'Payroll Matters' newsletters of the importance of checking payroll reports and passing amendments to PRS by published deadlines in order to avoid under/over payment of staff. The importance of checking these reports will be emphasised during 'induction' sessions with new bursars.</p>	<p>LGSS Schools Finance.</p> <p>V Toscano, Schools Team Leader October 2012.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>10.</p> 	<p>57% of the schools did not maintain inventory records or carry out an annual inventory check.</p> <p>Appropriate preventative and detective controls must be in place in order to reduce the risk of fraud and misappropriation of assets. Such controls include separation of duties, physical control over assets and physical inventory checks.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • a record of permanent and leased assets must be maintained; • new items should be included on the inventory when acquired; • a physical check should be made each year by someone other than the person that maintains the record. The record should be completed and evidenced by signature at the foot of each page; and • Inventory items should be security marked in case of theft. 	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>
<p>11.</p> 	<p>The private funds accounts were not audited annually in 52% of the schools and 58% of the schools had not presented the audited accounts to the Governing Body for their review and approval.</p> <p>Governing Bodies are responsible for ensuring that any private funds held by the school have been audited annually in order to mitigate the risk of fraud and misappropriation of assets.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> • the accounts for any private funds operated by the school must be audited annually; • they not do necessarily have to be audited by a qualified auditor/accountant, however, if the turnover is in excess of £100,000, it is recommended the auditor is a member of the accounting bodies; and • the annual audited accounts should be presented to the Governing Body meeting at the next meeting following the audit. This should be minuted. 	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>

Area Risk Level	Key findings	Recommendations	Management Comments / Agreed actions	Timescale / Owner
<p>12.</p> 	<p>A Whistleblowing Policy had not been reviewed and approved by the Governing Body in 37% of the schools and 91% of schools did not have a Business Continuity Plan in place.</p> <p>Serious malpractice at work may not be appropriately reported if a Whistleblowing Policy is not endorsed by the Governing Body.</p> <p>Appropriate recovery plans must be in place in order for schools to reduce their financial and operational risks in the event of a disaster.</p>	<p>In order to comply with Financial Regulations and the Schools Financial Value Standard, schools should be strongly advised that:</p> <ul style="list-style-type: none"> the Governing Body should adopt the Authority's Whistleblowing policy and ensure that all staff are aware of it; and a Business Continuity Plan including key areas such as premises, IT and staff, should be reviewed and approved by the Governing Body. 		
<p>13.</p> 	<p>54% of the schools had not checked that staff using their cars on school business had the appropriate business cover on their motor insurance policies.</p> <p>If appropriate business cover is not in place for the relevant staff, schools increase the risk of litigation, financial loss and reputational damage to the school.</p>	<p>In order to comply with Financial Regulations, schools should be strongly advised that:</p> <ul style="list-style-type: none"> School Management should check that any staff travelling on school business and using their motor cars have business cover on their motor insurance policies; this includes staff transporting pupils, visiting the bank and attending training courses; and School Management should check their insurance policies on an annual basis and record that this check has been made. 	<p>Main points to be raised at next series of seminars (Nov 12).</p>	<p>LGSS Schools Finance.</p>

Appendix 1 – Areas of Good Practice

Good practice identified (Over 80% of schools compliant)

A: The Governing Body and School Staff

- ✓ Pecuniary Interests Registers had been updated in the last twelve months.

B: Setting the Budget

- ✓ SIMS and Oracle carryforward balances agreed or alternatively, the reasons for any variances were known;
- ✓ Virements were approved by the Governors.

C: Value for Money

- ✓ Procedures were in place for the purchasing of goods and services.

D: Protecting Public Money

- ✓ Quotes and tenders were obtained to avoid corruption with, or favouritism to, contractors and suppliers;
- ✓ There was a separation of duties in place for the ordering and payment for goods and services;
- ✓ Appropriate third party insurance checks were carried out for hirers of the premises.

Appendix 2 – Level of Assurance

Internal Audit gives an overall opinion on the level of assurance provided by the controls within the area audited. The level of assurances are defined below:

Level of Assurance Definition

Full Assurance	There is a sound system of control designed to address the relevant risks with controls being consistently applied.
Substantial Assurance	There is a sound system of control, designed to address the relevant risks, but there is evidence of non-compliance with some of the controls.
Moderate Assurance	Whilst there is a basically a sound system of control, designed to address the relevant risks, there are weaknesses in the system, that leaves some risks not addressed and there is evidence of non-compliance with some of the controls.
Limited Assurance	The system of control is weak and there is evidence of non-compliance with the controls that do exist which may result in the relevant risks not being managed.
No Assurance	There is no system of internal control. Risks are not being managed.

Findings and recommendations

Prioritisation key

When assessing findings and recommendations reference is made to the Risk Management matrix which scores the impact and likelihood of identified risks.

For ease of reference, we have used a colour code system to prioritise our findings and recommendations, as follows:

	<p>Significant internal control weakness requiring priority action by School Management and/or the Governing Body. Such a control may be a legal requirement, or there may be the possibility of fraud or significant financial loss.</p> <p>The action is critical to the system of internal control and should be implemented immediately.</p>		<p>A modification or addition to the School's internal controls, necessary to safeguard assets and ensure the accuracy and reliability of records. Additionally matters that could be classified as red will be classified as amber if the sums of money involved are not material and the matter relates to a technical issue only.</p> <p>The action has a significant effect on the system of internal control and should be implemented as a matter of priority.</p>		<p>A more minor modification of current systems to further improve the School's internal controls.</p>
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