
AUDIT COMMITTEE 18-12-08

Present: Councillor Gwilym Williams (Chairman);
Councillor Ioan Thomas (Vice-chairman)

Councillors: E.T. Dogan, Huw Edwards, T.G.Ellis, Margaret Griffith, Selwyn Griffiths, Brian Jones, Charles Wyn Jones, R.L. Jones, Eryl Jones-Williams, John P. Roberts and Gethin Williams.

Also present: Dewi Morgan (Senior Audit and Risk Manager), Dafydd Edwards (Head of Finance), Gwen Carrington (Head of Social Services), Amanda Hughes (Local Manager, Wales Audit Office), Gwyn Parry Williams (Committee Officer).

Apologies: Councillors Aeron Jones, Dafydd Ll. Hughes

1. DECLARATION OF PERSONAL INTEREST

Councillor Eryl Jones-Williams declared an interest in the items involving Council housing and Social Services' care and disabilities as he was a Council house tenant and as his wife, who was disabled, received social care.

The member was of the opinion that it was not a prejudicial interest, he did not withdraw from the meeting and he participated fully in the discussion on the relevant items.

2. URGENT MATTER – A CHEQUE THAT WAS SENT TO THE WRONG ADDRESS

(This item had not been included on the agenda, but the Chairman agreed to include it under Section 100B (4) (b), Local Government Act 1972 because information regarding the matter was received after the agenda had been sent to the members)

The Senior Audit and Risk Manager reported that he had made enquiries into the incident reported in the press regarding a £31,500 cheque that had been sent to the wrong address. The cheque was made payable to the correct person and the letter was prepared by the Finance Service in accordance with usual procedures. The Senior Audit and Risk Manager was satisfied that there was nothing wrong with the Finance Service's arrangements in terms of making the payment itself but in accordance with the request to issue the cheque it was returned to the Planning and Transportation Service as it was to be enclosed with a letter. An Administrative Officer within the Planning and Transportation Service had made a mistake by noting the incorrect address on the letter.

He drew attention to the fact that it was the Committee's role to look at the Council's risks and how to manage those risks. In an attempt to avoid this type of mistake in the future it was intended to review the arrangements of

issuing cheques and of returning them to the service to be sent with a letter. A further report would be submitted to the Committee in due course.

A member referred to the fact that oil had been stolen from the Council Depot at Dolgellau. The Senior Audit and Risk Manager confirmed that the Internal Audit Section had been notified, by the Highways and Municipal Service, of the incident and that he was reviewing whether managerial weaknesses had increased the opportunity of stealing the oil.

RESOLVED to accept the report.

3. MINUTES

The Chairman signed the minutes of the meeting of this Committee held on 30 September 2008, as a true record.

4. OUTPUT OF THE INTERNAL AUDIT SECTION

a) A report to be considered at the request of the Chairman and Vice-chairman

Mental Health – Supported Accommodation

The Senior Audit and Risk Manager reported that the Chairman and the Vice-chairman of the Committee had requested for officers of the Care Directorate to attend the meeting in order for them to be able to answer any question that could arise from the “Mental Health – Supported Accommodation” audit report.

This followed a consideration of the internal audit reports released between 1 June and 31 August 2008. The officer added that the intention of the audit was to ensure that the payments made were correct and in accordance with individual service agreements for the 2007/08 financial year.

The original report had been deemed as an opinion Category “C” namely that assurance of financial propriety could not be given in the arrangements for administering Supported Accommodation payments as the controls in place could not be relied upon. From the identified risks, some points needed consideration as follows –

- a) No agreement was in place between the Council and one of its main suppliers.
- b) In terms of undertaking a review of the quality of the Mental Health Service received by the supplier, evidence would be needed to prove that this took place. Monitoring reports were not being sent to the Contracts Unit.
- c) Within the invoice certification process, officers took for granted that individuals had received the service. There was no financial portfolio for the individuals as there was with Learning Disabilities – Supported Accommodation, which created inconsistencies across the Social Services. This financial portfolio was a source that could be used in order to check the invoices.
- d) There was some concern, especially from the Dwyfor area point of view, regarding the possible deficiency in separating duties when making orders and paying invoices.
- e) That there was an expectation that any client who was not subject to Section 117 of the Mental Health Act 1983 should receive an assessment

by the Charging Policy Section. It was understood that there only one client who was not the subject of Section 117 and had not received an assessment.

- f) The Service Manager received income/expenditure reports on a quarterly basis from the accountant. As the underspend on the Residential Plan had financed the overspend on the Supported Accommodation budget during the previous two financial years, the Supported Accommodation budget, therefore, did not reflect the expected true cost for the financial year.

In response to the abovementioned points, the Head of Social Services explained that restructuring had taken place within the service during the previous 18 months which had improved the situation of the managers as they were by now able to ensure better control over managerial issues. She confirmed that the joint review had confirmed the findings of the audit, that there was a need to tighten those arrangements and to introduce procedures in order to ensure that there was improved compliance.

The Head of Social Services referred to the fact that it was endeavoured to synchronise practice across the services, not only within the Mental Health field but also that the Learning Disabilities Team and the Mental Health Team were consistent in terms of practice and that the same procedure was followed by them. Some of these processes had been undertaken and the Service Manager introduced a new procedure that would be reviewed in a meeting with other managers during the following days. In terms of the practice procedures, some were more complex and more work was needed on them.

RESOLVED to accept the reports and to support the recommendations submitted to the Care Directorate Managers for implementation.

b) The work of the Internal Audit Section for the period until 30 November 2008

Submitted – the report of the Senior Audit and Risk Manager, outlining the work of the Internal Audit Section for the period between 1 September and 30 November 2008. When presenting information about the work completed during the period, the officer referred to -

- 19 formal reports on planned audits from the annual audit plan, with the relevant opinion category being shown.
- 1 audit when memoranda had been produced, rather than a full report.
- 9 follow-up audits.

The further work of the Audit Section which was in progress was reported. This included 9 draft reports that had been released and 31 audits that were in progress.

Consideration was given to each individual report and reference was made to the following matters during the discussion –

The Effect of Financial Savings on the Control Environment

A member drew attention to the intention to close the Harlech Swimming Pool and the need to have robust arrangements in place to ensure that school

pupils as part of the national curriculum, were able to learn to swim at another location.

In response, the Head of Finance explained that the matter had been considered by the Council Board on 16 December 2008 when it was decided to extend the pool closure date until June 2009 in order to draw up and evaluate a business plan for transferring the pool to the Trust. It was explained that it was intended to ensure a decision in June in order to give schools the opportunity to arrange where the pupils would go to swim during the school year from September 2009. It was currently too early to ascertain whether appropriate procedures were in place or not.

Staff Recruitment and Appointment Procedures

A member enquired in relation to the procedure of appointing temporary staff to posts e.g. during a period of maternity leave.

In response, the Senior Audit and Risk Manager explained that because so many duties were imposed on the Council, that they endeavoured to appoint officers with the correct qualifications. The purpose of the audit was to ensure that adequate procedures were in place in order to reduce the risk of recruiting that was contrary to legislation, contrary to regulation, contrary to propriety and contrary to fairness.

Gifts to Staff at Residential Homes

A member asked whether the Council had any control in relation to staff receiving financial gifts and how to differentiate between financial gifts and other gifts.

In response, the Senior Audit and Risk Manager explained that clear guidance was needed for the staff in terms of what was acceptable and unacceptable. This case received an Opinion Category of "C" as the relevant guidelines were not in place.

RESOLVED to accept the report on the work of the Internal Audit Section for the period between 1 June and 31 August 2008 and to support the recommendations already submitted to the relevant service managers for implementation.

5. INTERNAL AUDIT PLAN 2008/09

Submitted – the report of the Senior Audit and Risk Manager providing an update of the current situation in terms of the progress on completion of the 2008/09 Internal Audit Plan.

He explained the situation as it was on 30 November 2008 as well as the time spent on each audit up to that time. Attention was drawn to the following table which revealed the current status of the work within the operational plan –

Audit Status	Number
Planned	36
Working Papers Created	10
Field Work Started	28
Field Work Ended	1
Manager Review	2
Draft Report Issued	9
Report Agreed	1
Final Report Issued	27
Total	114

He informed the Committee that the performance target for 2008/09 was 95% and at present it appeared to be an achievable target.

RESOLVED to note the contents of the report as an update of progress against the 2008/09 audit plan and to congratulate the Internal Audit Section on reaching their performance target of 95%.

6. CASH DEPOSITS WITH HERITABLE BANK PLC

Submitted - the report of the Senior Audit and Risk Manager which confirmed that the Head of Finance had reported to the Council Board on 14 October 2008 that the authority had deposited £4m in the Heritable Bank which had subsequently been placed in administration. It was explained that Gwynedd Council was amongst 100 local authorities, public sector bodies and charities in the UK to have deposits at risk, having deposited money with Icelandic financial institutions and/or UK-based subsidiaries. The Council Board had resolved:

- a) That Internal Audit was central to the work of detailed scrutiny of the situation and to request that the Senior Audit and Risk Manager held a thorough investigation of the matter and was to submit an appropriate report to the Audit Committee on 18 December.
- b) That the report of the Audit Committee should include a review of the role of the consultants in the relevant decisions.

The Senior Audit and Risk Manager went on to explain that the Council had a well-established process for the short term investment of surplus cash. The Council's balance sheet as at 31 March 2008 showed that it had £77m of short-term investments. This was not to say that the Council had £77m of reserves available – most of the money had been earmarked for revenue or capital expenditure and had been invested for the short term in order to generate interest income for the Authority. Given the amounts of money with which the Council dealt, it was prudent for the authority to invest any surplus cash it may have had on a particular day with one or more financial institutions. On 8 September 2008 the Council deposited £4m of cash for a fixed term of 136 days, until 22 January 2009, with Heritable Bank PLC, an institution listed on the List of Authorised Counterparties as being a suitable bank for deposits. On 7 October 2008 the Court of Session made an administration order in relation to Heritable Bank plc. As the bank had gone into administration, the Council was not able to draw funds from its account and the Council was to be treated as an unsecured creditor of Heritable Bank plc in the administration.

The Senior Audit and Risk Manager referred to the way the £4m had been placed with the Heritable Bank in accordance with the Council's Treasury Management Strategy and by following the CIPFA code for Treasury Management in the Public Services, by spreading risks and depending on recognised credit ratings.

He gave details of the Treasury Managements and the Annual Investment Strategy. He brought attention to the fact that the Council appointed Sector Treasury Services Ltd company as consultants in relation to borrowing and investment. He explained that the strategy conformed to the Wales National Guidelines' statutory guidelines and to the CIPFA Code of Practice for Treasury Management in the Public Services. The Council's list of authorised counterparties was based on the previous year's list, and revised when establishments were removed when they fell lower than the minimum threshold approved by the Full Council. Heritable was added as counterparty in 2007 on the basis of its adequate credit rating.

He explained that Heritable Bank Plc was a British company registered in Scotland. When it went into administration 100% of the shares in Heritable were owned by Landsbanki Holdings (UK) plc making Heritable a subsidiary of the Landsbannki Bank of Iceland.

In relation to the dependency on credit ratings, he explained that Council officers, when depositing with Heritable, had acted to the letter within the Annual Investment Strategy, which stated that the minimum credit status for Specific Period Deposits with banks and building societies including callable deposits with the maturity of less than a year was the minimum long term status Fitch F1 supported by a minimum long term credit status of "A". The Monthly Counterparties List provided by Sector on 5 September 2008 declared that Heritable had a short term status of F1 and long term status of "A". He explained that a key factor in the fall of the banking sector in Iceland was the failure of the Country's economy to support its banking sector. The Treasury and Investment Management Unit was aware of turmoil within Iceland's banking sector, following the maturity of the deposit made with Glitnir in August 2008 and no further deposits were made to Icelandic banks. It was also confirmed, although Heritable Bank had been included on the Council's list of authorised counterparties as an United Kingdom bank, officers at the Treasury and Investment Management Unit were not aware that it was a full subsidiary of another bank from Iceland, namely, Landsbanki, until after Heritable was placed in administration. It was concluded that the lack of explicit information that Heritable's owner was in Iceland had contributed to the decision to deposit money with that specific bank during September 2008.

Internal Audit was notified by another local authority, which also used Sector as a treasury management consultant, that they had withdrawn from depositing money with all banks from Iceland, including Heritable but more than 100 authorities had deposited money with establishments from Iceland, or their subsidiaries, based on their approved credit rating. On 8 September, Gwynedd Council had a balance of £20.155m cash to be deposited. Based on the predicted cash flow, £7.155m was deposited in an overnight account. Of the remaining £13m, £4m was deposited with Heritable Bank at an interest rate of 5.91%, with the other £9m spread across three Building Societies with interest rates varying between 5.76% and 5.87%. These deposits were due to mature in January 2009. The primary reason for the limits on the deposits held

within any one institution was in order to spread the potential risk and ensure that risk was minimised in case of the failure of one institution.

He noted the following recommendations which had already been submitted to the Finance Unit Manager for implementation –

- a) A two-stage methodology should be developed for placing cash deposits with institutions on the List of Authorised Counterparties, rather than the current arrangement of choosing the highest yield from any institution reaching a minimum standard. Following receiving interest rates for a variety of institutions from brokers, the interest rates offered by the brokers should be compared with the comparative risk of each one.
- b) It should be ensured that information received from the Treasury Management Consultants regarding any relevant institution was conveyed to all key personnel.
- c) The Annual Investment Strategy should state that further information including rating outlooks and rating watches – would be considered along with credit ratings for all institutions.
- d) Cash deposits must be invested on the basis of sound risk management, without being averse to risk or higher interest rates that could be generated and this should be reflected in the Annual Investment Strategy.

The Head of Finance reported that the current situation was that the £4m continued to be under threat. It appeared that it would be possible to retrieve a portion, maybe approximately half of the money, but not all of it.

It was resolved to exclude the press and public from the meeting during the discussion on the following issue because of the likely disclosure of exempt information as defined in paragraph 14, Part 4, Schedule 12A of the Local Government Act 1972. This paragraph applied because financial details would be disclosed and there was no overriding public interest that required that. Consequently, the public interest in maintaining the exemption outweighed the public interest in disclosing the information.

The Head of Finance gave further details that Gwynedd Council was amongst 115 other local authorities which had lost a total of £858m. He expatiated that the Council had gained substantial interest by depositing short term cash with banks and that the money that was available generally varied between approximately £50m and £100m. By depositing this money with banks, the Council has generated interest of around £5m per year. He referred to the possibility of investing the money in a securer place, but that would have generated an interest that was around 2% lower and a lower income of approximately between £1m and £2m per year. It was decided to deposit the money with Heritable Bank on the basis of its “A” credit rating which was construed as a safe location and a credit rating which was higher than the minimum “A-”. It was unprecedented for a bank to keep its “A” credit rating until the day before it collapsed but, upon reflection, it was obvious that there had been an over dependency on the authorised credit rating agencies.

In relation to the consultants’ contract for the future, the Head of Finance informed that Sector had been contractors, providing information, for many years. For 2009/10, quotes had already been invited and presentations arranged for January to choose a consultant for a detailed contract. It was intended for the presentations to show whether the consultants could provide better quality leadership compared to others.

The Head of Finance explained that some steps had been taken since October 2008 to reduce the risk associated with investments by looking beyond the credit rating and a strategy was agreed to reduce the level of investments and borrowing.

The Head of Finance referred to the Council Strategy for 2009/10 which would be more complex with a view to improve security. It was intended to present the draft strategy to a working group of the Resource and Corporate Scrutiny Committee and the Finance Portfolio Leader, during January 2009 to be scrutinised February 2009 following the interviews of the investment consultants companies.

In closing, the Head of Finance noted that he welcomed the main conclusion in the Senior Audit and Risk Manager's report, that the Council had not 'gambled' with the money, and that the partial loss of money was mainly due to the unprecedented situation of the banking system.

In response to a question, it was explained that neither the Council, nor the Pensions fund, had any direct investment with "Bernard L. Madoff Investment Securities" and although it was inevitable that the Council had deposited monies with some banks which would lose out due to "Madoff", it was not considered that these deposits were under threat.

RESOLVED to accept the report and to support the recommendations already submitted to the Managers of the Finance Service for implementation.

The meeting commenced at 10.30am and concluded at 12.45pm