Internal Audit Report

Active Northumberland – Evaluation of Governance Arrangements

To: Steven Mason, Chief Executive
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Summary

Active Northumberland became part of Northumberland County Council’s family of companies in October 2014. The Council’s relationship with Active Northumberland was intended to realise two significant strategic objectives. These were firstly, to transform and improve the leisure and cultural services offer across Northumberland; and secondly, to deliver significant savings for the County Council.

A sound and effective governance framework would be essential to the achievement of such strategically significant goals, covering service provision to residents throughout the whole County of Northumberland. The review of a number of key governance processes within Active Northumberland has, however, found that governance arrangements overall lack clarity and are unlikely to be effective as these currently operate. Active Northumberland management have acknowledged that these areas require attention, but comment that much of their focus in the early months of the venture was on ensuring ‘business as usual’ in service provision.

In particular, Internal Audit is concerned that the Council’s interests may not be well served by all aspects of the governance framework currently in operation. There is a significant risk of conflict of interest (between the Council’s aspirations, and those of other stakeholders) inherent in the arrangements audited. This does not assure the Council that its objectives will be realised. Given the importance of the outcomes which the arrangement with Active Northumberland is intended to deliver, it is essential that key elements of governance are strengthened as a matter of priority.

On the basis of the work undertaken, Internal Audit considers that the framework of internal control currently in operation gives no assurance to the County Council on those aspects of governance examined as part of the review.

1 Background

1.1 Following a fundamental review of leisure arrangements within the County during 2012, a number of major changes have been introduced to the management of the Council’s Culture and Leisure services. Previously, leisure services throughout the County were delivered via a number of providers originating under the former
The review of leisure resulted in the integration of five previous sets of leisure management arrangements into one Trust, called 'Active Northumberland', which became part of the County’s family of companies from October 2014. The scale of leisure operations being managed is significant. Delivery of leisure and cultural services through the Active Northumberland vehicle represents a major transformational change.

1.2 Active Northumberland is a charity and not-for-profit limited company, and until recently had Northumberland County Council as the only member, governed by a Board of 16 trustees. The Board composition has recently been revised. The turnover for service provision during 2014/15 was approximately £14m. As part of the County Council’s agreed two year budget 2015-17, a detailed savings plan (contributing to the Council’s Medium Term Financial Plan) has been agreed. This savings plan sets out proposed revenue savings of £1.77m from Active Northumberland’s management of Leisure in the period 2015-17. Additionally, further services from Culture, Libraries and Tourism transferred to Active Northumberland with effect from 1 April 2015. This transfer is intended to realise an additional £1.72m in savings in the period 2015-17.

2 Audit Objectives, Scope and Coverage

2.1 Given the increased scope and breadth of services now delivered via the Active Northumberland model, the significant combined budget of the new arrangements, and the savings proposed to be realised, it was agreed that a review and evaluation of governance arrangements in place would be helpful. Accordingly, the following objectives were agreed:

(a) To evaluate the governance arrangements established within Active Northumberland in respect of a range of key business processes, and to form an opinion to management on whether these arrangements are soundly based and likely to support achievement of business goals; and

(b) To examine whether arrangements are proportionate and fit for purpose, given the breadth and scale of operations now delivered by the Trust. To assess whether arrangements are appropriate to safeguard key stakeholder interests, and to promote effective decision making, performance management and the effective discharge of key business processes.

2.2 The Public Sector Internal Audit Standards\(^1\), defines ‘governance’ as “the combination of processes and structures implemented by ‘the board’ to inform, direct, manage and monitor the activities of the organisation toward the achievement of its objectives.” Governance therefore is not only about the ‘hard’ factors – robust systems and processes, such as risk management, financial management, performance management and internal controls, but also about the ‘softer’ characteristics of effective leadership, a culture based on openness and honesty, and high standards of behaviour. It involves a combination of both internal and external focus, understanding the needs of service users and the public and maintaining clarity of purpose.

2.3 In performing an evaluation of Active Northumberland’s governance arrangements, the agreed scope comprised as assessing whether the culture, systems and

\(^1\) Public Sector Internal Audit Standards, Chartered Institute of Public Finance and Accountancy and Institute of Internal Auditors, 2013
procedures in the following areas are soundly based and fit for purpose, and likely to support achievement of agreed business goals:

- **Decision making, delegation arrangements, separation of duties and levels of authority throughout all aspects of Active Northumberland’s key business processes** – are these correct and appropriate to the form of legal entity which is in operation?

- **Administration of arrangements in respect of the Board and management** – including reporting and accountability lines;

- **Human resources procedures** – including remuneration approval, performance appraisal, health and safety, policies on declaration of interests and acceptance of gifts / hospitality;

- **Financial management** – including arrangements for the management of expenditure, delivery of agreed savings targets as set out in the 2015-17 budget, and key financial procedures in place;

- **Financial planning** – including performance planning, revenue budgeting and monitoring processes, and capital planning and management;

- **Financial systems and procedures** – including an evaluation of data availability and quality, early warning systems for deviation from targets, the adequacy of management / audit trails, and an appraisal of key controls in systems of income and expenditure with reference to expected control objectives;

- **Procurement** – including a specific review of the arrangements in place for ordering and paying for works, goods and services, an assessment of the financial thresholds established for decision making around tendering, and whether these arrangements comply with EU and national procurement laws / directives and good purchasing practice, and an examination of whether separation of duties and limits on authority are appropriate;

- **Information governance and ICT controls** – including a review of access approval procedures, business continuity / disaster recovery arrangements, hardware and software management, perimeter security, network management, and procedures for managing and governing data; and

- **Risk management, project management and control of resources** – including procedures for safeguarding the security of assets, inventories, stocks and stores.

### 2.4

Since issue of the project brief for this review, the provision of some support services has been changed, for example with the transfer of some finance staff from Active Northumberland to the County Council’s Business Support function in September 2015. This will better assure the Council regarding the effectiveness of financial monitoring; the adequacy of decision making on financial management (which is the responsibility of Active Northumberland) will then be able to be assessed more transparently.

### 2.5

Active Northumberland has a range of stakeholders. Whilst this report may contain information which is of interest to a number of these stakeholders, Internal Audit’s responsibility is to Northumberland County Council. This report therefore focuses on matters which are most relevant to the Council as our client.
3 Overall Audit Opinion

3.1 On the basis of the work undertaken, it is the opinion of Internal Audit that the overall audit objective has not been met as the framework of internal control gives no assurance to the authority on those aspects of governance examined as part of the audit. A description of assurance levels is shown at Appendix 1.

4 Decision making, delegation arrangements, separation of duties and levels of authority throughout all aspects of Active Northumberland's key business processes

Decision Making (Board Level)

- At the time of our review, Active Northumberland had a Board comprising 16 trustees (directors); we are aware that changes to the Board structure have since been agreed. Minutes of Board meetings prior to this change demonstrated that a number of officers had also attended Board meetings. As part of our review, Internal Audit obtained a number of Board meeting papers, which included agendas, reports and minutes covering the period October 2014 to June 2015. We sought to assess the way in which decision making operated in practice at Board level, and how robust the decision making process appeared.

- Some (but not all) of the reports examined in this period had a short standard template attached, which set out briefly the purpose of the report, recommendations, key issues and background. There were also a number of ‘implications’ statements on the template, covering matters such as Policy, Finance and Value for Money, Human Resources, Equalities, Risk Assessment and Customer Considerations. While such a standard template is good practice in assisting decision makers, the quality of the information included on the templates that were completed was poor. For example, a report on Board Structures considered by the Board in April 2015 stated that Risk Assessment implications were ‘Not Applicable’. Other implications statements did not fully explain to the reader what the impact of the proposals were, for example, the same report in respect of the Finance and Value for Money implication simply stated ‘This will allow for efficient working and decision making’. Other significant implications, for example Legal implications, were absent from the template.

- A review of the minutes from these meetings did not demonstrate that there was active, informed and participative decision making in place by the Board. The minutes that were provided did not show robust discussion or overtly Board-led decisions. In the majority of agenda items, the minutes recorded that the decision of the Board was that ‘it was resolved that the report was received’.

Delegation Arrangements, Separation of Duties and Levels of Authority

- Clearly defining the limits of delegated authority should be considered a key strand of the governance framework of any organisation. However, delegation arrangements within Active Northumberland appear to have evolved on a piecemeal basis. In some areas, such as Finance, the involvement of the Council’s Corporate Services Manager has promoted the use of the Council's
corporate limits and procedures (this is discussed further in section 6 below). In other areas, proposed delegated limits have not been presented to or agreed formally by the Board. In terms of separation of duties and clarity on processes, the majority of procedures do not appear to have been formally codified or included in procedure notes / manuals.

5 Administration of arrangements in respect of the Board and management

- Perhaps the key finding from Internal Audit’s review of the Board and management arrangements is that these allow a distinct potential for tension between the interests of Active Northumberland as an entity lying outwith the Council, and the interests of Northumberland County Council as a key stakeholder. Internal Audit’s responsibility is to Northumberland County Council, and our comments below therefore outline some of the risks we have identified to the Council as our client.

- The arrangements around the Board, and Active Northumberland’s management, are complex. There is one critical post which acts in a dual role, undertaking both the duties of a Council Head of Service (Head of Leisure) and also of ‘Chief Executive’ of the Active Northumberland entity. Whereas the expectations of the roles and limits on authority of other Heads of Service within the Council are clearly specified in arrangements such as the Officer Scheme of Delegation, the powers available to the dual Active Northumberland role appear much less clearly defined and allow the postholder to act more freely.

- The governance framework developed by the Council for its Heads of Service, and accompanying procedures, therefore do not always seem to be applied in the case of Active Northumberland decisions; but the rationale for this is not always clear. The dual postholder (Council Head of Leisure / Active Northumberland Chief Executive) appears to have considerable autonomy. This level of power in one post is unlikely, given the evolving nature of the governance framework around the Active Northumberland entity, to be in the Council’s best interests as arrangements currently stand.

- The Council has agreed with Active Northumberland a number of key strategic objectives. In summary, these are to firstly deliver large scale transformational change in the leisure and cultural services offer within Northumberland; and secondly, through this transformation to deliver a significant cost reduction in the operating costs of those services, as set out in paragraph 1.2 above. However, there is no detailed business plan or management agreement in place to detail how Active Northumberland plan to deliver these two critical objectives of the Council. On the information viewed as part of this review, Internal Audit is not assured that the arrangements around the Active Northumberland delivery vehicle will deliver the Council’s stated priorities. Given the strategic nature of the services delivered, and the significance of the cost savings forecast, this aspect of governance is of particular concern. The Chief Executive of Active Northumberland has stated that the next piece of work, to set the policy framework, has now commenced; and that he considers that there was a lack of a policy framework and data of sufficient quality in place.

- The Board structure has been the subject of consideration by legal experts appointed by both Active Northumberland, and by the Council. It was widely
appreciated by both Active Northumberland and the Council that there was a need to change the structure of the Board, to help ensure compliance with the regulatory framework governing this type of entity, and to better reflect the diverse expectations of the various stakeholders. The arrangements of the Board and the legal status of Active Northumberland, as a both a charity and a not-for-profit limited company will require ongoing legal advice, whilst new Board arrangements, recently established, become embedded.

- The management arrangements of any entity will be a matter for the entity concerned. It would be expected however, that the “top team” would have a pivotal role in the governance framework by providing strategic leadership, setting strategic objectives and being held to account for the delivery of those objectives. To an extent, any judgement of performance in this area would be subjective, as it is difficult to always gauge softer measures of governance performance. The agendas, reports and minutes of the previous six Senior Management Team meetings were requested. Review of the minutes appeared to Internal Audit to show an emphasis on operational (rather than strategic) matters. The Chief Executive of Active Northumberland has advised that other meetings have taken place around strategic matters.

6 Human Resources (HR) procedures

Policies and Resources

- No HR policies and procedures specifically relating to Active Northumberland are in place. Those that do currently exist are as inherited from the previous leisure organisations (e.g. BVAL/North Country Leisure/Tees Active/Leisure Connections); this means that there are a number of different procedures, covering the same subject matter, in place which does not promote consistency or clarity. Furthermore there is no set method of communicating policies and procedures to staff across each leisure site. The Chief Executive of Active Northumberland has advised that this is now being progressed in conjunction with Human Resources.

- The Chief Executive of Active Northumberland has commented that the policies and procedures, pay rates, job evaluation and terms and conditions issues are being picked up as part of a single status exercise currently being undertaken. Internal Audit has been advised that a target date of April 2016 has been set for the job evaluation aspects of this work.

Recruitment

- There is no HR manual relating specifically to Active Northumberland.
- Controls were not followed in relation to the creation of new posts. An ‘Authority To Recruit’ form is in place that requires approval from the Chief Executive of Active Northumberland, however, in the case of the evidence provided the form had been approved by a centre manager rather than the Chief Executive.
- The procedure for establishing the grading of posts is not documented.
- The procedure for appointing consultants is not documented.
- The procedure for re-grading posts is not documented.
Performance Appraisal

- No corporate performance appraisal policy specifically relating to Active Northumberland is in place. Different versions are being used, as were in place for each previous organisation before Active Northumberland was formed.

Declaration of Interests and Acceptance of Gifts/Hospitality

- The HR Manager was unable to confirm if controls are or are not in place in this respect.

Health and Safety (sample of five sports and leisure establishments)

- Overall, the review has highlighted that the controls and procedures in operation in respect of health and safety appear to be operating satisfactorily.
- A number of the establishments visited had undertaken the Quest Assessment which reports (amongst other areas) upon various elements relating to health and safety in operation at the centre.
- Recommendations to be considered, aimed at ensuring that consistent and up to date procedures are in place across all sites, include:
  - Documenting key building information and locations, and ensuring awareness amongst all staff members;
  - Maintaining all key documents, such as asbestos management plans, building risk assessments and flood risk assessments;
  - Ensuring that chemicals / tablets used in testing swimming pool water are stored securely;
  - Ensuring that all required building inspection / maintenance programmes are undertaken regularly (e.g. Control of Substances Hazardous to Health (COSHH), asbestos, emergency lighting etc.).

7 Financial management

- Assurance can be taken from the joint approach to financial management, between Active Northumberland and the Council. The involvement of the Corporate Services Manager with Active Northumberland helps to ensure adherence / compliance with the Council’s agreed corporate procedures. This assurance should be strengthened with the transfer of staff from Active Northumberland to the Council from 1 September 2015.

- The Chief Executive of Active Northumberland has stated that the finance organisational changes (moving back into the Council) and roll out of Active Northumberland moving on to the Oracle system have impacted on a number of areas identified. The Chief Executive of Active Northumberland has stated that there is a plan to move fully on to the Oracle system, but this is taking some time. The Business Support Service has explained that to improve financial processes, Active Northumberland moved on to E-Business on 1 April 2015. Due to a short timeline, expenditure reporting was built within the County Council’s structure on the system, but there is now a project plan to create a separate Active Northumberland entity within E-Business from 1 April 2016. This will also include an interface for income which should further improve the processes in place and allow a more accurate position to be determined during any given month. This will provide much greater transparency and allow the
Council greater certainty regarding the accuracy of financial reporting, which is to be welcomed.

- There is no formal management agreement in place between the Council and Active Northumberland. It was envisaged at the point of transfer that this agreement would illustrate how Active Northumberland would meet the Council’s priorities and allow performance to be measured. The absence of this agreement prevents the Council from obtaining clarity or challenging service delivery against the management fee paid to Active Northumberland. The Active Northumberland Service Plan 2015-17 records that a Management Agreement is planned to be completed by March 2016.

- Examination of 2015-16 budget information highlighted a required reduction of £191k across Active Northumberland. A potential risk (as yet unquantified) was identified relating to achievement of required savings, as of this amount, £105k has been allocated to increased income budgets. The transfer of a range of financial work to the County Council will provide the Council with more comfort over the accuracy of financial information.

8 Financial planning

Revenue Budgeting and Monitoring

- Responsibility for proposing and approving the budget is not documented.
- Preparation of the draft budget does not follow a set timetable.
- Approval of the budget was not expressly recorded in the minutes of the relevant meeting.
- The delegated limits in place for orders, credits and write-offs have not been approved by the Board.
- Responsibility for budget monitoring is not determined.
- Individual and significant over and underspends are not reported to the Board on a regular basis.
- A scheme of virement is not documented.
- There is no procedure manual for staff to refer to with regards budget setting and monitoring.
- Budget staff have not received budget training.

9 Financial systems and procedures

Cash and Non-Credit Income procedures (sample of five sports and leisure establishments)

- Overall, the review has highlighted that the controls and procedures in operation in respect of cash handling appear to be operating satisfactorily.
- Recommendations to be considered, aimed at ensuring that consistent procedures are in place across all sites, include:
  - Documentation of agreed procedures with respect to refunds, with all monies refunded to service users appropriately authorised and recorded, in accordance with a standard policy.
  - Ensuring that there is a segregation of duties in place when cash income is reconciled and prepared for banking / transferred between officers.
One agreed system for ensuring that establishments reconcile income received and prepared for banking to entries in the general ledger system.

10 Procurement

- No clear procedures were put in place by Active Northumberland, which resulted in a degree of confusion and misunderstanding of procurement requirements. A specific incident has exposed both Active Northumberland and the Council to the risk of legal challenge, and a continued lack of clear procedures and processes will not give assurance that this situation will not recur.

- A Category Specialist within the Council’s Procurement team is now the named contact for Active Northumberland. There is now much greater dialogue between the Council and Active Northumberland over procurement and proposals for procurement, which offers the Council greater assurance over this important aspect of arrangements.

- Whilst progress has been made and awareness of procurement requirements is growing, an awareness raising programme may be beneficial to help embed understanding.

11 Information governance and ICT controls

IT Strategy, Policies and Procedures

- Active Northumberland does not have an IT Strategy in place but are meeting with the Council’s Information Services department (IS) to agree future strategy. The corporate IT strategy for the Council is currently in draft.

- BVAL (one of the former organisations which became part of the Active Northumberland entity) adopted all of the Council’s ICT policies and procedures and as other organisations have transferred to Active Northumberland they have also adopted corporate policies.

- Some recommendations should be considered, primarily referring to training and awareness for Active Northumberland employees (which replicate recommendations made in the 2014/15 NCC Information Governance audit report).

Information Governance and Compliance with Legislation

- The adoption of all Council corporate ICT policies and procedures means assurance can be taken that a consistent approach should be being applied across Active Northumberland.

- Some good practice was identified in relation to data cleansing routines in the primary leisure management system, although there appears to be a lack of focus on information governance issues which has resulted in several recommendations to be considered including:
  - Nominating an employee to attend the corporate Information Governance Working Group meetings. This employee should have specific responsibilities for data protection and freedom of information and would be responsible for raising awareness of information governance and compliance issues across Active Northumberland;
o Seeking advice from the Council’s data protection officers to determine whether the procedures in place within Active Northumberland, for example responding to subject access and freedom of information requests, are adequate and operating effectively;

o Reviewing Active Northumberland’s data protection registration to determine whether it requires amendment to incorporate the additional services it has absorbed;

o Reviewing public facing data collection forms and seeking advice from the Council’s data protection officers to determine whether they include an effective Privacy Notice;

o Determining the appropriate record retention periods for the information held and ensuring these are applied in practice.

General ICT Controls

- Systems and devices are hosted on the Council’s network and as such are subject to the corporate systems of control in place, for example anti-virus, content filtering, back up routines and disaster recovery.
- All end user devices are procured through, and built by IS to the corporate standard.
- All network user accounts are subject to strong logical access controls.
- Recommendations to be considered include:
  - Undertaking a periodic review of the user base both within Active Directory and the Gladstone system to ensure all users are current and their access permissions are correct;
  - Undertaking a periodic reconciliation between assets recorded on the IS hardware asset register and physical assets in situ;
  - Reviewing data held on the corporate network and deleting obsolete data in accordance with record retention periods once confirmed;
  - Reviewing business continuity plans to ensure that arrangements remain current and incorporate all services for which Active Northumberland is now responsible.

12 Risk management, project management and control of resources

- Active Northumberland do not have a risk management policy or strategy and do not adopt a structured or systematic process in identifying and managing corporate (strategic) risks. The only risk information held relates to health and safety.
- Operationally, risk management processes surrounding health and safety are sound and evidence of this has been provided and independently reviewed through QUEST.
- Whilst the Chief Executive of Active Northumberland was able to discuss consideration of risk in service plans, business plans and in new projects (e.g. Tyne Riverside Park and Hirst Welfare), it is not a formalised process. Risk was not referenced in the initial sample of documents supplied and examined.
- A risk workshop to develop the corporate risk register - with the Chief Executive and his senior management team facilitated by the risk management team has now taken place (during October 2015).
- Recommendations to be considered include:
  - A risk management policy and strategy to be developed and agreed – with support of the risk management team, based upon best practice principles,
using the Council’s framework as a template and building upon the Trust’s culture and processes in place in relation to health and safety; leading to

- An action plan for the implementation of the risk management policy and strategy - to be developed and agreed with appropriate milestones and timescales.

13 Conclusion

13.1 Active Northumberland in its current incarnation is a relatively new entity. It appears that governance arrangements have not kept pace with what would be expected given the values and scale of the entity that now exists. From the Council’s perspective, this is a concern as effective governance is essential to the achievement of all strategic objectives. Arrangements should be strengthened as soon as possible.

IA/AHM/KM
13 November 2015
## Opinion Statement Table

The opinion expressed by Internal Audit is in accordance with the following key:

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<thead>
<tr>
<th>Level of Assurance</th>
<th>Description</th>
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<tbody>
<tr>
<td>Full Assurance</td>
<td>The system of internal control is designed to meet the organisation’s objectives and controls are consistently applied in all the areas reviewed.</td>
</tr>
<tr>
<td>Significant Assurance</td>
<td>There is a generally sound system of control designed to meet the organisation’s objectives. However, some weakness in the design of, or occasional non-compliance with, key controls put the achievement of the organisation’s objectives at risk in some of the areas reviewed.</td>
</tr>
<tr>
<td>Moderate Assurance</td>
<td>While there is a basically sound system of control, there are some weaknesses in the system and evidence of regular non-compliance with key controls that put the achievement of the organisation’s objectives at risk in some of the areas reviewed.</td>
</tr>
<tr>
<td>Limited Assurance</td>
<td>Weaknesses in the design of, or regular non-compliance with, key controls put the achievement of the organisation’s objectives at risk in some or all of the areas reviewed.</td>
</tr>
<tr>
<td>No Assurance</td>
<td>Significant weaknesses in the design of, or consistent non-compliance with, key controls could result (have resulted) in failure to achieve the organisation’s objectives in the areas reviewed.</td>
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