



Final

Internal Audit Report

Chief Executives Unit - Strategic Finance

Review of Contract Hire and Operating Leases 2007/08

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1	DETAILED FINDINGS
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1. BACKGROUND

- 1.1 This report has been prepared following an Internal Audit review of Contract Hire and Operating Leases as part of the 2007-08 Internal Audit programme. This years audit has concentrated on reviewing and assessing actions taken to implement recommendations in the 2006/07 report and to update the position regarding other matters arising from that audit.
- 1.2 The Council leases vehicles, plant, equipment and property. The annual rental payments in 2006/07 amounted to some £2.04million. Of this amount £1.76million was classed as operating leases, where the main risks and rewards associated with ownership remain with the lessors rather than being taken on by the Council. The introduction of the Prudential Code for Capital Finance has meant that the distinction between different funding streams is far less important than it was under the Capital Consent regime, but management control over leasing remains crucial to ensure that value for money is obtained.
- 1.3 As a result of our audit work some findings were generated. These findings have been agreed with management and outlined in this report.

2 AUDIT SCOPE AND OBJECTIVES

- 2.1 The specific objectives of the audit were to assess and report on whether progress has been made in adopting recommendations arising from the 2006-2007 audit, assess any actions implemented, and obtain an update on the following matters:
 - Whether vehicle drawdown reviews are now frequently carried out;
 - Whether the Chrystal Consulting contract was renewed for a further year to March 2008, and if so what the arrangements are likely to be for the period following;
 - The cost savings calculated when Chrystal Consulting are involved in negotiating the cost of damages when returning vehicles to the lessor;
 - The outcome of the arrangements for the Cuan Sound crossing in view of the need to replace the existing ferry;
 - Whether networking of copiers has improved; and the advantages gained from making use of available advanced photocopying facilities;
 - Whether arrangements for checking photocopier invoices at schools have been improved;
 - Whether software recently purchased to carry out an analysis of printing and copying at Kilmory has proved useful;
 - What arrangements are in place to carry out a review of savings made from the Cannon contract; and

- Whether co-ordination of purchase/lease arrangements has improved;

2.2 The adequacy of the arrangements to meet the objectives has been assessed using a grading of one to five ticks (✓ 's). Five ticks indicate good arrangements and one tick inadequate arrangements are in place. The assessment is set out in section 6 (figure 1). The assessment has been made by considering the value and significance of the findings and recommendations.

3 AUDIT APPROACH

3.1 The following approach was used to satisfy the objectives of the audit:

- Discussions were held with the Development Services Departmental Finance Manager and the Senior Accountant – Strategic Finance (Development Services Finance Team), to establish progress made since last year, and the current position regarding other matters raised in the previous year by Internal Audit;
- Discussions were held with both the Exchequer Manager to establish the position regarding actions agreed last year, and with Education Service purchasing staff with regard to the contract for the supply of photocopiers, which came into operation in July 2005;
- A discussion was held with the Fleet Manager regarding the control of vehicle leases;
- Testing was carried out on arrangements relating to the possible purchase/lease by the Council of a ferry boat;
- The current position regarding the networking of photocopiers was obtained;
- All findings/matters arising were raised and discussed with the Development Services Finance Manager and the Exchequer Manager ;
- A draft report was prepared and a copy passed to the relevant Heads of Service;
- Any comments were included in the final report, which was then passed to the Chief Executive;
- The final report includes an action plan, which lists any actions agreed with management. Some of the actions arising from the audit are not directly leasing matters, but have been included in the action plan because of their perceived importance.

4 SUMMARY OF MAIN FINDINGS

Follow up of 2006/07 recommendations

- 4.1 During the previous years audit no evidence was found of a check being carried out on direct debits paid to leasing companies for vehicles. However, this year a reconciliation was carried out by Strategic Finance (Development Services Finance Team) as part of completing the year end accounts. Provided this reconciliation is carried out each year this is an acceptable control.
- 4.2 Draft guidance has been issued for consultation to services on the need for Strategic Finance to be involved where decisions are required as to lease or purchase. This guidance is due to be finalised and issued in mid January 2008.
- 4.3 Similarly draft guidance has been issued for consultation to services on the need to use the Council's lease advisors, Chrystal Consulting, to prevent unnecessary payment for advice. This guidance is due to be finalised and issued by mid January 2008.
- 4.4 Internal Audit found that the Master Agreement for vehicle leasing has been amended to include an anti-bribery clause reflecting the requirement in the current Contract Standing Orders.
- 4.5 The contract for supply of photocopiers on a lease or purchase basis is an endorsed contract. Using another supplier thus leads to a risk of prosecution for the Council. Occurrences of this practice were reported to the Procurement Project Board in October 2005, and Internal Audit found evidence of another non-compliant purchase. It was recommended in last years Internal Audit report that clear written guidance detailing the risks, and any implications for the member of staff using another supplier, be issued to all purchasing staff, including Education Service staff. The guidance was also to include the need for all orders to be placed with contracted suppliers, and to be placed via PECOS. This guidance is to be drawn up by the Exchequer Manager and put before the Procurement and Shared Services Board at its meeting on 18 January 2008, then issued by the end of January 2008. The guidance may have to be issued via "postmaster" as apparently there is not a full list of staff in place that are able to place orders.
- 4.6 It would be more satisfactory if the guidance could be better targeted and perhaps steps should be taken to persuade the Service Directors via their Heads of Service to nominate specific officers to be responsible for all ordering whether by PECOS or otherwise. Instructions could then be issued to all staff that orders can only be placed via those officers. Any officer placing orders outwith those arrangements could be subject to disciplinary action. If this action was implemented the Council would be better placed to insist on the use of PECOS.
- 4.7 The photocopier contract costs more than £100,000 annually for rental alone, with maintenance charges perhaps being as much again. Savings are expected to accrue from improved use of staff time and rationalisation of

printing. It may as yet be too early to ascertain the extent of savings, but it is understood that an exercise recording print patterns in Kilmory has been completed and the results analysed. An internal print strategy is being developed, and a report is to be issued by the Accounting & Best Value Supervisor, ICT & Financial Services, which will assess the overall value for money of the new contract based on the information available to date. This report is to examine any barriers to achieving value for money, both to inform the current contract and also any future ones. It will also be necessary at some future time to assess the impact of the Canon photocopiers on the Education Service budgets.

Cuan Sound Crossing

- 4.8 Currently the Cuan Sound to Luig is crossed by a ferry boat. The boat is 35 years old and becoming more and more expensive to maintain. It has therefore become now necessary to consider the options available to the Council to maintain links with Luig.
- 4.9 A Consultant was engaged to investigate the various options to maintain the link. The Consultant produced a Scottish Transport Appraisal Guidance (STAG) report in April 2007. This included the generation of a range of options, an initial appraisal of the options and a detailed appraisal of the short – listed options. The Consultant concluded that the best option was the construction of a high level bridge.
- 4.10 The STAG appraisal report has been put to the Scottish Government for its review and decision. The Council have been unable so far to obtain timescales from Government as to when a decision will be made. The best estimate currently is that it is unlikely to be before the end of 2007. Little more can be done until that decision is reached, and there is currently therefore no programme of action in place.
- 4.11 If the bridge option is not accepted then the likely plan is to revert to constructing new slipways and leasing or purchasing a ferry boat. Best estimates of timescales assuming the STAG decision is reached by say December 2007 are:-
- Up to 7 years for completion of bridge; or
 - Up to 5 years for provision of ferry.
- 4.12 Considering the age of the current ferry boat and the long timescales involved in implementing whatever decision is taken the Council should be preparing plans as to how to deal with the possibility of expensive repairs and long periods with the boat being out of service. Also in view of a reasonable possibility that the bridge option may not be accepted by Government, the Council should be considering taking steps to plan for the purchase or lease of a ferry boat, and the other implications flowing from that.
- 4.13 The new Capital Programme and Management Guide will need to be followed whatever course of action is planned.

Networking of Photocopiers / Advantages Gained from Advanced Photocopying Facilities

- 4.14 It was suggested last year that once the new Canon contract had been in place for say 2 years an exercise would be carried out to ascertain any benefits or savings obtained from the new contract. The Exchequer Manager says that the main savings hoped for from the new contract are through networking photocopiers throughout buildings and directing expensive desktop prints to specific machines. Manse Brae and Argyll House, Dunoon were given as examples where this has happened.
- 4.15 An exercise has been completed at Kilmory Head Quarters to record print patterns on desktop printers and the results analysed. A print strategy is being prepared and will be put in place for the whole Council.
- 4.16 Internal Audit has also been informed that networking of copying facilities is currently ongoing in schools. However the ICT Development Manager involved has informed Internal Audit that "The only way of getting a definitive statement regarding this would be to contact each school directly and find out how many, if any, printers/copiers they have. I have a team of technicians who offer support to the Primary schools and they have certainly been assisting by arranging network cabling for schools, so there has been some progress with this, but I can't say how much. The Secondary Schools have their own ICT support technicians". It would seem therefore that it will be necessary to review the position regarding networking of printing at schools, to prepare an implementation programme action plan and then to assess the impact of networking on school budgets.
- 4.17 Once all of this has been concluded it should then be possible to estimate the potential savings from the use of the advanced facilities available throughout the Council based on the experience gained from Manse Brae and Argyll House and the print usage and estimated savings at Kilmory and in individual schools. A report is currently being prepared by the Accounting & Best Value Supervisor, ICT & Financial Services, as explained at paragraph 4.7 above. The report will cover expected savings to date based on the current information available.

5 ACTION PLAN

- 5.1 The action plan attached at Appendix 2 has been compiled with the co-operation and agreement of management.
- 5.2 Internal Audit considers that, in an effort to improve the quality of information, monitoring and control, the recommendations should be implemented in accordance with the agreed action plan. Management are expected to have set achievable implementation dates and will be required to provide reasons to the Audit Committee for failure to implement within the agreed timescale. Where management decides not to implement recommendations it must evaluate and accept the risks associated with that decision.

- 5.3 A system of grading Internal Audit findings, which have resulted in an action, has been adopted in order that the significance of the findings can be ascertained. Each finding is classified as fundamental, material or minor. The definitions of each classification is set out below:-

Fundamental - major observations on high level controls and other important internal controls. Significant matters relating to factors critical to the success of the objectives of the system. The weakness may therefore give rise to loss or error;

Material - observations on less important internal controls, improvements to the efficiency and effectiveness of controls which will assist in meeting the objectives of the system and items which could be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified;

Minor - minor recommendations to improve the efficiency and effectiveness of controls, one-off items subsequently corrected. The weakness does not appear to affect the ability of the system to meet its objectives in any significant way.

6 OVERALL CONCLUSION AND ASSESSMENT AGAINST OBJECTIVES

- 6.1 The Auditee sections have a good working knowledge of the processes involved. However, during the course of the audit, some areas were identified as requiring some improvement and therefore, various recommendations have been made. These have been discussed with management and an action plan agreed. (Any issues not accepted by management are done so with their knowledge and acceptance of risk and control weakness.)

6.2 Figure one below sets out a summary of the overall conclusions arising from the audit in terms of the specific objectives detailed at section 2.1

Figure 1: Summary of overall conclusions

Specific objectives	Assessment
To Review whether progress has been made in adopting recommendations arising from the 2006-2007 audit	✓✓✓✓
To review whether action has been taken to carry out vehicle reviews more frequently ;	✓✓✓✓✓
To review whether arrangements are in place for renewal of the Chrystal contract in March 2008	✓✓✓✓
To review whether the costing of savings calculated when Chrystal are involved in negotiating the cost of damages to vehicles with the lessor is adequately controlled	✓✓✓✓✓
To review whether arrangements are in place for the renewal of the Cuan Sound transport link	✓✓✓✓
To review whether networking of copiers has improved and whether use is being made of advanced photocopying facilities available and the advantages gained	✓✓✓
To review whether arrangements for checking photocopier invoices at schools have been improved	✓✓✓
To review whether software recently purchased to carry out an analysis of printing and copying has proved useful	✓✓✓✓
To review whether there are arrangements in place to carry out a review of savings made from the Cannon contract	✓✓✓
To review whether co-ordination of purchase/leasing arrangements has improved	✓✓✓✓
<p>Key:</p> <ul style="list-style-type: none"> ✓✓✓✓✓ - Arrangements accord with good practice and are operating satisfactorily. ✓✓✓✓ - Arrangements accord with good practice, but certain minor matters noted as requiring improvement. ✓✓✓ - Adequate arrangements in place, but certain matters noted as requiring improvement. ✓✓ - Arrangements in place offer scope for substantial improvement. ✓ - Concern is expressed about the adequacy of the scope of these arrangements. 	

7 ACKNOWLEDGEMENTS

- 7.1 Thanks are due to all the staff who assisted in the completion of the Internal Audit report with special thanks to the Development Services Finance Manager and his staff and the Exchequer Manager and his staff for their co-operation and assistance during the audit and the preparation of the report and action plan.
- 7.2 Argyll & Bute Council's Internal Audit section has prepared this report. Our work was limited to the scope in paragraph 2.1 of this report. We cannot be held responsible or liable if information material to our task was withheld or concealed from us, or misrepresented to us.
- 7.3 This report is private and confidential for the Council's information only and is solely for use in the provision of an internal audit service to the Council. The report is not to be copied, quoted or referred to, in whole or in part, without prior written consent. .

APPENDIX 2

ACTION PLAN

ACTION PLAN NO	Appendix 1 PARA GRAPH	GRADE	WEAKNESSES IDENTIFIED	AGREED ACTION	RESPONSIBLE OFFICER	DATE OF IMPLEMENTATION
1	Para 1.10	Material	Staff authorising expenditure are required to follow the Council's Constitution, including the Contract Standing Orders, which means that they must use contracted suppliers. However, the risks inherent in using an unendorsed supplier are not spelt out, nor is it clear that disciplinary procedures could be invoked if staff do not follow the Constitution.	Written instructions to be issued to all staff that can authorise expenditure from external suppliers, detailing the requirement to follow Contract Standing Orders. This means that orders must only be placed with contracted suppliers when available and PECOS must be used for all such orders. Where there are no contracts in place competition should be ensured for any significant spends. A set of instructions will be drawn up and put before the Procurement and Shared Services Board at their meeting on 18 January 2008.	Exchequer Manager	31 January 2008

ACTION PLAN NO	Appendix 1 PARA GRAPH	GRADE	WEAKNESSES IDENTIFIED	AGREED ACTION	RESPONSIBLE OFFICER	DATE OF IMPLEMENTATION
2	Par. 1.12 & Para 1.28	Material	The photocopier contract is for more than £100,000 annually for rental alone, with maintenance charges perhaps being as much again, thus committing the Council to considerable expenditure for the next five years. This expenditure should however be offset by the potential savings to be made from use of the advanced facilities available from the new machines. It is however necessary for the Council to monitor the savings gained.	A value for money review is to be carried out on completion of the internal print strategy and implementation of any recommendations.	Exchequer Manager	30 June 2008
3	Para 1.26	Material	Considering the age of the current ferry boat (35 years) and the long timescales involved implementing whatever decision is taken, perhaps the Council should be preparing plans as to how to deal with the possibility of expensive repairs and long periods with the boat being out of service.	A risk management exercise to be considered prescribing the action to be taken in the event of the "MV Belnahua" ferry boat being out of service for a long period.	Head of Roads and Amenity Services	immediate

ACTION PLAN NO	Appendix 1 PARA GRAPH	GRADE	WEAKNESSES IDENTIFIED	AGREED ACTION	RESPONSIBLE OFFICER	DATE OF IMPLEMENTATION
4	Para 1.26	Material	In view of there being a reasonable possibility that the bridge option for the Cuan Sound crossing may not be accepted by the Scottish Government the Council should be considering taking steps to plan for the lease or purchase of a ferry boat and the other implications flowing from that.	Steps should be commenced by the Council to decide the action to be taken in the event of the Scottish Government deciding not to fund a high level bridge.	Director of Operational Services	Immediate
5	Para 1.31	Material	Operational Services had produced an Internal Waste Prevention Action Plan which has fallen behind with its original implementation dates	Management is now taking steps to put the action plan back on course	Head of Roads & Amenity Services	Immediate
6	Para 1.32	Material	The advantages gained from networking of photocopiers in schools are not fully known.	The networking position in schools is to be reviewed and if necessary an implementation programme and action plan prepared. An assessment should also be made of the likely impact on school budgets	Head of Secondary Education & Pupil Support & Head of Pre School & Primary Education	March 2008

ACTION PLAN NO	Appendix 1 PARA GRAPH	GRADE	WEAKNESSES IDENTIFIED	AGREED ACTION	RESPONSIBLE OFFICER	DATE OF IMPLEMENTATION
7	Para 1.34	Material	The potential savings from the use of the advanced networking facilities available throughout the Council based on the experience gained from Manse Brae and Argyll House, the print usage and estimated savings at Kilmory and the savings in schools have not yet been estimated and reported to management.	Once the potential savings have been estimated a report is to be produced for management forecasting the potential savings. This report would need to be followed up with actual savings achieved. Such reports would be useful evidence towards showing Audit Scotland that the Council is achieving BV.	Head of ICT & Financial Services Plus Head of Democratic Services & Governance	Estimated savings reported by 31 March 2008