
Meeting: AUDIT COMMITTEE

Agenda Item: 6

Date: 14th June 2010

INTERNAL AUDIT ANNUAL REPORT AND ANNUAL ASSURANCE STATEMENT FOR YEAR ENDED 31 MARCH 2010

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1. PURPOSE

- 1.1. The purpose of this report is for the Audit Committee to receive and consider the Internal Audit Annual Report and Annual Assurance Statement for the year ended 31 March 2010.

2. RECOMMENDATIONS

- 2.1. The Internal Audit Annual Report and Annual Assurance Statement for the year ended 31 March 2010 be noted.

3. BACKGROUND

- 3.1. The Accounts and Audit (Amended) (England) Regulations 2006 requires that "A relevant body shall maintain an adequate and effective system of internal audit of its accounting records and of its systems of internal control in accordance with the proper practices in relation to internal control".
- 3.2. This report summarises the Internal Audit activity in 2009/10 and the Chief Internal Auditor's Assurance Opinion in relation to the Council meeting the requirements of the above Accounts and Audit Regulation.
- 3.3. The Assurance Opinion is also provided for use within the Council's Annual Governance Statement which will be included in the Statement of Accounts for the year ended 31 March 2010.

4. REASONS FOR RECOMMENDED COURSE OF ACTION AND OTHER OPTIONS

- 4.1. From the Internal Audit work undertaken in 2009/10 it is the Chief Internal Auditor's opinion that he can provide Moderate assurance that the system of internal control that has been in place at Stevenage Borough Council for the year ended 31 March 2010 accords with proper practice. See Appendix A for detailed report.

5. IMPLICATIONS

5.1. Financial Implications

5.1.1. This report contributes to fulfilling the requirements of the Accounts and Audit (Amended) (England) Regulations 2006.

5.2. Legal Implications

5.2.1. There are no direct policy implications within the recommendations of this report.

6. BACKGROUND DOCUMENTS

- None

7. APPENDICES

- Appendix A - The Internal Audit Annual Report and Annual Assurance Statement for the year ended 31 March 2010



STEVENAGE BOROUGH COUNCIL

INTERNAL AUDIT ANNUAL REPORT

AND

ANNUAL ASSURANCE STATEMENT

FOR THE YEAR ENDED 31 MARCH 2010

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EXECUTIVE SUMMARY

Introduction

This report has been compiled to document and communicate an overall opinion based on the work undertaken by Internal Audit during 2009/10.

Our Audit Report and Assurance Statement has been structured to:

- Summarise Internal Audit activity for 2009/10;
- Draw attention to matters of particular concern, especially via individual assurance opinions; and
- Highlight areas requiring specific attention.

Management are responsible for ensuring that the financial management of Stevenage Borough Council is adequate and effective and that the organisation has a sound system of internal control, which facilitates the effective exercise of that organisation's functions and which includes arrangements for the management of risk.

Chief Internal Auditors Opinion on the Effectiveness of Internal Control 2009/10

This opinion statement is provided for the use of Stevenage Borough Council in support of the statement of accounts for the year ended 31 March 2010.

Scope of Responsibility

The management of Stevenage Borough Council is responsible for ensuring its business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

In discharging this overall responsibility, the management of Stevenage Borough Council is also responsible for ensuring, that there is a sound system of internal control which facilitates the effective exercise of its functions, and which includes arrangements for the management of risk.

The Purpose of the System of Internal Control

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate risk of failure to achieve policies, aims and objectives, and can therefore only provide reasonable, not absolute, assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks to the achievement of Stevenage Borough Council policies, aims and objectives.

To evaluate the likelihood of those risks being realised and the impact should they be realised, and to manage them efficiently, effectively and economically.

The Internal Control Environment

The CIPFA Code of Practice for Internal Audit states that the internal control environment comprises three key areas - internal control, governance and risk management processes. Our opinion on the effectiveness of the internal control environment should be based on an assessment of each of these key areas.

Review of Effectiveness

Stevenage Borough Council has responsibility for the effectiveness of the system of internal control. The review of the effectiveness of the system of internal control is informed by the work of the internal auditors and the senior managers within the Council, who have responsibility for the development and maintenance of the internal control environment, by comments made by the external auditors and other review agencies and inspectorates in the annual letter and other reports.

Chief Internal Auditor's Annual Opinion Statement

Our opinion is derived from work carried out by Internal Audit during the year as part of the agreed internal audit plan for 2009/10, including our assessment of Stevenage Borough Council corporate governance and risk management processes.

The internal audit plan for 2009/10 was developed to primarily provide management with independent assurance on the adequacy and effectiveness of the systems of internal control.

Basis of Assurance

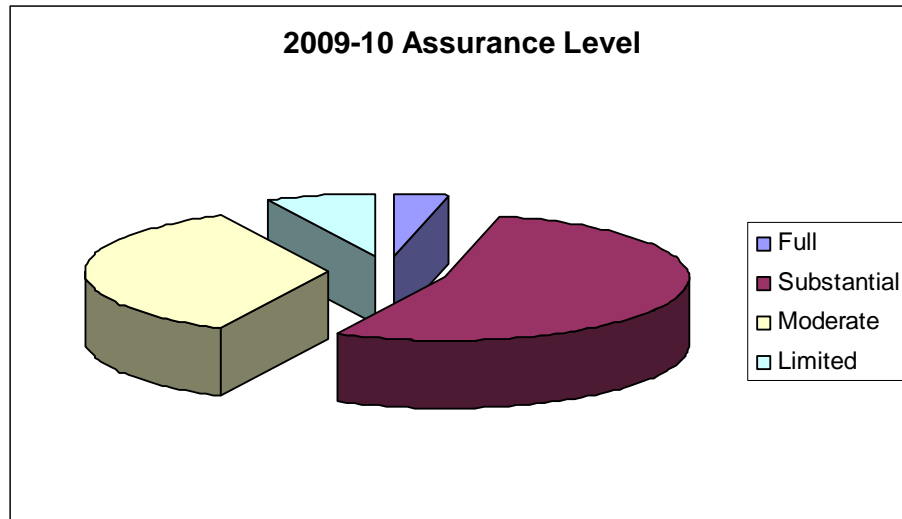
We have conducted our audits both in accordance with the mandatory standards and good practice contained within the CIPFA Code of Practice for Internal Audit in Local Government

in the UK 2006, and additionally from our own internal quality assurance systems. This programme of work is outlined at **Appendix 1**.

Our opinion is limited to the work carried out by Internal Audit during the year on the effectiveness of the management of those principal risks, identified within the Internal Audit programme. While all principal risks identified within the organisation's framework may not have been included in Internal Audit's 2009/10 coverage, we have undertaken sufficient work to allow ourselves to give a reasonable assurance, that risks are being managed effectively.

Audit Assurance Opinions

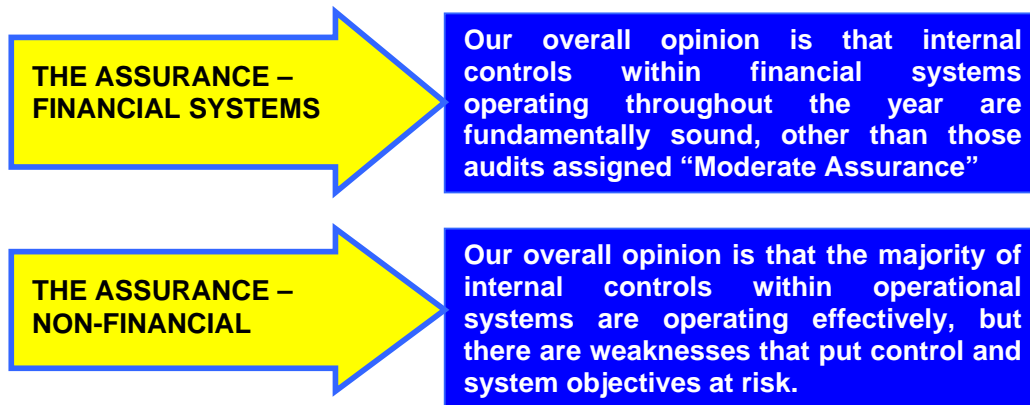
The audit work that was completed for the 2009/10 year is listed in **Appendix 1**. It shows the audits and their results in terms of the audit assurance level provided, together with the number of recommendations raised. The levels of assurance achieved on the systems audited by Internal Audit are depicted in the chart below.



A Full Assurance opinion was given for 4% of audit reports issued (one report), 53% (15 reports) were issued with Substantial Assurance opinions, 36% (ten reports) were issued with Moderate Assurance opinions and Limited Assurance opinions amounted to 7% (2 reports) of audit reports issued.

2009/10 Year Opinion

From the Internal Audit work undertaken in 2009/10 it is our opinion that we can provide **Moderate**¹ assurance that the system of internal control that has been in place at Stevenage Borough Council for the year ended 31 March 2010 accords with proper practice. The assurance can be further broken down between financial and non-financial systems, as follows:



Corporate Governance

In our opinion the corporate governance framework substantially complies with the best practice guidance on corporate governance issued by CIPFA/SOLACE.

Risk Management

It is noted that Stevenage Borough Council have developed the assessment, evaluation and documentation of risks and the focus on strategic and operational risks has improved during the year, as demonstrated in the strategic risk register and the further development of operational risk registers.

In drawing together our opinion we have relied upon our risk based audits relating to the 2009-10 financial year.

We would like to take this opportunity to formally record our thanks for the co-operation and support we have received from the management and staff during the year.

CHIEF INTERNAL AUDITOR

May 2010

¹ See Page 12 for definition of Assurance Levels

DETAILED REPORT

Introduction

This section of the report details:

- any significant control failures or risk issues that have arisen and been addressed through the work of Internal Audit;
- any qualifications to the Chief Internal Auditor opinion on Stevenage Borough Council system of internal control, with the reasons for each qualification;
- the identification of work undertaken by other assurance bodies upon which Internal Audit has placed an assurance to help formulate its opinion;
- the management processes adopted to deliver risk management;
- the effectiveness of the System of Internal Audit
- Internal Audit performance; and
- the Internal Audit work undertaken during the 2009/10 year.

Significant Control Weaknesses

Internal Audit is required to form an opinion on the quality of the internal control environment, which includes consideration of any significant risk or governance issues and control failures which arise. During the financial year 2009/10 the following significant control weaknesses were identified:

- Business Continuity and IT disaster recovery plans require further development and testing to confirm reliability; and
- There have been instances of non compliance with Contract Standing Orders. As a number of interim valuations in respect of staged payment contracts have not been submitted to Internal Audit for checking before being sent to Exchequer for payment. In addition, Internal Audit identified significant control weaknesses in relation to the verification of work undertaken, the authorisation of variations to the original contract, and the lack of payment retention or performance bonds.
- The Car Parks audit was assigned a 'Limited Assurance' opinion. The significant control weaknesses related to the lack of business user agreements, outstanding advertising income, monitoring of contractor obligations and income management.
- The Academy IT application audit was assigned a 'Limited Assurance' opinion. The significant control weaknesses related to lack of clearly define roles for system administration and non adherence to best practice in relation to access controls.

Management action plans have been agreed to address the above weaknesses.

Qualifications to the Opinion

Internal Audit has had full access to all areas and systems across Stevenage Borough Council and has received appropriate co-operation from officers and members.

Risk Management Process

The principal features of the risk management process are described below:

Risk Management Strategy

Stevenage Borough Council has established a Risk Management Strategy that sets out the organisation's attitude to risk and to the achievement of business objectives. The strategy:

- Explains Stevenage Borough Council's underlying approach to risk management;
- Documents the roles and responsibilities of Stevenage Borough Council;
- Outlines key aspects of the risk management process; and
- Identifies the main reporting procedures.

This strategy has been approved by the Audit Committee.

Risk Registers

Stevenage Borough Council has risk registers in place and these will be further developed during 2010/11.

Audit Plan

The internal audit service introduced risk based approach in preparing its annual audit plan and has moved away from a three year planning cycle for non key financial systems audits. The 2009/10 audit plan was approved by both management and the Audit Committee.

Internal Audit Assurance Levels and Recommendations

A table is provided at **Appendix 1** setting out the level of assurances achieved on each audit, as well as the number and priority of recommendations raised and agreed.

We have issued one report that was given a Full Assurance opinion, 15 reports which were given Substantial Assurance opinions, ten reports which were given Moderate Assurance opinions and two reports which were given Limited Assurance opinions.

The table also has details of the priority we give to our recommendations, together with the total number of recommendations made. Of the recommendations made 5% were high priority, 52% were medium priority and 43% were low priority.

Management action plans have been agreed to address the control weaknesses identified and the progress in implementing the action plans is monitored and reported to the audit committee.

Effectiveness of the System of Internal Audit

The Accounts and Audit (Amendment) (England) Regulations 2006 came into force from 1 April 2006. Paragraph 6 (3) states that:

“the relevant body shall, at least once in each year, conduct a review of the effectiveness of its system of Internal Audit”.

To comply with the Accounts and Audit Regulations a self assessment against the standards in the CIPFA Code of Practice for Internal Audit in Local Government in the UK was undertaken by the Chief Internal Auditor. In addition an external peer review was undertaken by the Audit Manager at North Herts District Council.

The self assessment and external peer review both concluded that the system of Internal Audit at Stevenage Borough Council is effective.

In addition the External Audit Opinion confirmed that the Internal Audit service complied with the CIPFA Code of Practice.

Internal Audit Performance

The table below compares Internal Audit's 2009/10 performance against targets and the performance in the previous year.

Performance Indicator	Target	2009-10 Actual	2008-09 Actual	Direction of travel
Percentage of planned audit days completed	95%	96%	82%	Improvement
Average Satisfaction Score (1 = unsatisfactory - 5 = excellent)	3	3.74	4.24	Decrease, but above target
External Audit Opinion	Achieving above minimal standards	Achieving above minimal standards	Achieving minimal standards	Improvement

The percentage of planned audit days completed has significantly improved from 82% in 2008/09 to 96% in 2009/10. The increased target of 95% (previously 90%) has been exceeded.

The Internal Audit satisfaction questionnaire average score was 3.74 in 2009/10 which exceeded the target score of three. There has been a significant increase in the volume of satisfaction survey returns which may explain the slight decrease in performance compared to the previous year.

Internal Audit followed up individual questionnaires which were given an average score of less than three, as a result the way in which audit assignments and findings are communicated to auditees has been strengthened.

The scoring system used by External Audit to provide their opinion was based on the Use of Resources scoring scale. Whereby level one would be inadequate, level two would be achieving minimum requirements, level three would be achieving above minimum requirements and level four would be demonstrating innovative practice.

External Audit stated that the audit service complied with the CIPFA Code of Practice and that elements of good practice in terms of regular liaison meetings, formal protocols and fraud reporting arrangements were in place which allowed them to discharge their reporting requirements to the Audit Commission, further to this they stated that some good work in collaboration with other authorities had been produced. However the key improvement area was the improved delivery of the plan, achieving 96% delivery in the year. Based on this marked improvement they thought sufficient evidence was provided to award a score of three 'achieving above minimal standards'.

Internal Audit Quality Standards

Internal Audit has comprehensive quality control and assurance processes in place that comply with the best practice standards established by CIPFA.

Working with External Audit

Grant Thornton, who are the external auditors for Stevenage Borough Council, were consulted with regards to Internal Audit coverage and further meetings and liaisons regarding future audit plans and work programmes have been planned.

Work of the Audit Committee

The Audit Committee have monitored progress in the delivery of the Internal Audit Plan through its quarterly meetings. They have strengthened their review process by requesting quarterly updates on:

- the implementation status of high priority recommendations
- the audits that have overrun by more than 100% of the budgeted time allocation

The Audit Committee have also provided effective challenge on emerging issuing, for example, the Committee commented on the revised Treasury Management Strategy following the Icelandic banking collapse.

APPENDIX 1 - ASSURANCES AND RECOMMENDATIONS 2009/10

The table below summarises the assurance opinion assigned to each Key Financial system audited and provides an analysis of the number of recommendations made in each priority category.

TABLE 1 - 2009-10 KEY FINANCIAL AUDIT ASSURANCES AND RECOMMENDATIONS

AUDIT AREA	ASSURANCE ²					RECOMMENDATIONS			
	F	S	M	L	N	Priority ³			Total
						H	M	L	
Asset Management			✓			1	8	13	22
Cash and Payments			✓			0	9	10	19
Council Tax		✓				0	4	11	15
Creditors			✓			1	2	2	5
Benefits		✓				0	6	1	7
Main Accounting System		✓				0	4	0	4
NNDR			✓			0	8	7	15
Payroll		✓				0	1	3	4
Sundry Debtors			✓			0	6	7	13
Treasury Management		✓				0	3	3	6
TOTAL	0	5	5	0	0	2	51	57	110

Note: The Council Tax, Main Accounting and NNDR audits include additional recommendations made in the Year-End controls audit.

Five of the ten Key Financial Audits were assigned Substantial Assurance opinions the remaining five were given Moderate Assurance opinions.

TABLE 2 – COMPARISON OF 2009-10 AND 2008-09 KEY FINANCIAL ASSURANCE OPINIONS

The table below summarises the assurance opinions assigned to the Key Financial Systems in 2009/10 and compares them against the 2008/09 audit opinions by outlining the travel of performance between the two years.

AUDIT AREA	2009/10 Audit Opinions	2008/09 Audit Opinions	Travel of Performance
Asset Management	Moderate	Moderate	No change
Cash and Payments	Moderate	Moderate	No change
Council Tax	Substantial	Moderate	Improvement

² See Page 12 for definition of Assurance Levels

³ See Page 13 for definition of Priority Categories

AUDIT AREA	2009/10 Audit Opinions	2008/09 Audit Opinions	Travel of Performance
Creditors	Moderate	Moderate	No change
Housing Benefits	Substantial	Substantial	No change
Main Accounting System	Substantial	Substantial	No change
NNDR	Moderate	Moderate	No change
Payroll	Substantial	Substantial	No change
Sundry Debtors	Moderate	Substantial	Decrease
Treasury Management	Substantial	Moderate	Improvement

Internal Audit work has helped to improve the internal control environment on the key financial systems through the implementation of audit recommendations. In 2009/10, 50% of the Key Financial Systems were given an audit opinion of “Substantial Assurance”; this is an improvement from 40% in 2008/09.

TABLE 3 - 2009-10 OPERATIONAL AUDIT ASSURANCES AND RECOMMENDATIONS

The table below summarises the assurance opinion assigned to each operational system audited, an analysis of the number of recommendations made in each priority category and a total.

AUDIT AREA	ASSURANCE ⁴					RECOMMENDATIONS			
	F	S	M	L	N	Priority ⁵			Total
						H	M	L	
Equality and Diversity		✓				0	4	7	11
Fleet Management			✓			0	5	10	15
National Indicators		✓				0	4	10	14
Absence Management			✓			0	8	4	12
Grounds Maintenance			✓			1	7	2	10
Performance Management		✓				0	2	1	3
Energy Management		✓				0	6	3	9
Environmental Cleansing		✓				0	4	3	7
Building Control			✓			1	21	16	38
Car Parks				✓		7	42	23	72
Licensing			✓			1	2	1	4
Elections		✓				0	2	4	6
Medium-Term Financial Strategy	✓					0	0	1	1

⁴ See Page 12 for definition of Assurance Levels

⁵ See Page 13 for definition of Priority Categories

AUDIT AREA	ASSURANCE ⁴					RECOMMENDATIONS			
	F	S	M	L	N	Priority ⁵			Total
						H	M	L	
Risk Management		✓				0	9	5	14
Corporate Governance		✓				0	3	1	4
IT Network Controls		✓				1	3	1	5
Academy IT Application				✓		4	7	0	11
Non-Main Bank Accounts		✓				0	6	3	9
TOTAL	1	10	5	2	0	15	135	95	245

In addition to the above systems audits, Internal Audit also completed the following work:

- 134 probity checks on interim valuation in respect of staged payment contracts
- 77 financial appraisals
- Formally responded to 48 requests for ad hoc advice
- Compliance with the Audit Code of Practice self assessment
- RIPA Compliance
- Input to the Annual Governance Statement
- Co-ordination of the National Fraud Initiative upload of data and investigation into the data matches
- Administration and publicity of the whistle-blowing arrangements
- Delivery of five Ethics and Probity Training courses
- Further development of Follow Up strategy, database and templates of previous audit report recommendations
- Follow Up of six previous operational audit reports, Garages, Grant Funding, Environmental Health, Taxi Licensing, Mortgages and Northgate Housing Application
- Follow Up of the previous Key Financial Systems audit recommendations
- Further development of the risk based internal audit methodology
- Update of the Internal Audit Manual
- Internal Audit work for Stevenage Homes
- Representation on the Corporate Risk Management Audit Group
- Co-ordination of two Risk Management benchmarking exercises

Assurance Levels

In order to assist management in using our reports:

We categorise our **opinions** according to our assessment of the controls in place and the level of compliance with these controls.

Assurance Opinion	Definition
Full	<p>Evaluation opinion: there is a sound system of control designed to achieve the system objectives; and Testing opinion: the controls are being consistently applied.</p> <p>Full Assurance will be attributed to a system where no recommendations are made or where in the auditor's judgement the recommendations relate to actions that are considered desirable and which should result in enhanced control or better value for money.</p>
Substantial	<p>Evaluation opinion: basically a sound system but there are weaknesses which put some of the control objectives at risk, and/or; Testing opinion: there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.</p> <p>Substantial Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered necessary to avoid exposure to significant risks.</p>
Moderate	<p>Evaluation opinion: basically a sound system of control but there are some more significant/serious weaknesses which put system objectives at risk, and/or; Testing opinion: the level of non-compliance with some controls may put certain system objectives at risk.</p> <p>Moderate Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered necessary to avoid exposure to more significant risks.</p>
Limited	<p>Evaluation opinion: weaknesses in the system of controls are such as to put the system objectives at risk, and/or; Testing opinion: the level of non-compliance puts the system objectives at risk.</p> <p>Limited Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered imperative to ensure that the Council is not exposed to high risks.</p>
No	<p>Evaluation opinion: control is generally weak leaving the system open to significant error or abuse, and/or; Testing opinion: significant non-compliance with basic controls leaves the system open to error or abuse.</p> <p>No Assurance will be attributed to a system where in the auditors' judgement they can place no reliance on the controls and procedures in operation either because they do not exist or because they are weak leaving the system open to abuse or error.</p>

Priority Categories

We categorise our **recommendations** according to their level of priority and we consider the level of risk associated with the weaknesses identified.

High	Recommendations relate to major issues that have a significant impact on achieving service objectives and are to be implemented immediately or within one month where practical.
Medium	Recommendations relate to issues that are expected to impact on achieving service objectives and are to be implemented within two months where practical.
Low	Recommendations relate to issues that have a lesser impact on achieving service objective and are to be implemented within six months where practical.