

Meeting: AUDIT COMMITTEE

Agenda Item:

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ANNUAL REPORT ON INTERNAL AUDIT 2007/08

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1 PURPOSE

The purpose of this report is for Members of the Audit Committee to receive and consider:

- year end position comparing actual audit work undertaken with the 2007/08 annual internal audit plan
- statement regarding format and content of reports produced
- table showing status of reports issued during the financial year
- work undertaken not resulting in a report being issued
- performance against indicators included in the Service Plan
- opinion of the Chief Internal Auditor based on results from summary of audit jobs completed during financial year.

2 RECOMMENDATIONS

It is recommended that Members of the Audit Committee note:

- 2.1 The opinion of the Chief Internal Auditor of a substantial to full level of assurance on the overall adequacy and effectiveness of the internal control environment at Stevenage Borough Council based on the work undertaken by Internal Audit during 2007/08.
- 2.2 The issues considered relevant for inclusion in the Annual Governance Statement.

3 BACKGROUND

- 3.1 The preparation and publication of an annual governance statement is necessary to meet the statutory requirement set out in Regulation 4(2) of the Accounts and Audit Regulations 2003, as amended by the Accounts and Audit (Amendment) England Regulations 2006. This replaces the previous Statement on Internal Control. It

requires authorities to “conduct a review at least once in a year of the effectiveness of its system of internal control”.

- 3.2 In order to assist in providing assurance on internal control, the Chartered Institute of Public Finance and Accountancy ‘Code of Practice for Internal Audit in Local Government in the United Kingdom 2006’ requires:
- 3.3 That the Chief Internal Auditor must provide a written report to those charged with governance which includes the following:
- an opinion on the overall adequacy and effectiveness of the organisations internal control environment;
 - disclose any qualifications to that opinion, together with the reasons for qualification;
 - a summary of the audit work from which the opinion is derived;
 - to draw attention to any issues the Chief Internal Auditor judges particularly relevant to the preparation of the Annual Governance Statement;
 - a comparison of work actually undertaken against work planned and a summary of performance against its performance measures and targets;
 - comment on any other matters of control or internal audit significance.
- 3.4 This report summarises the work undertaken by the Internal Audit Section during 2007/08 to formulate the opinion. It covers work planned and completed during that period and reviews the performance of the Section.
- 3.5 The report concludes with the opinion of the Chief Internal Auditor on the overall adequacy and effectiveness of the Council’s internal control environment.

4 INTERNAL AUDIT SECTION

- 4.1 2007/08 has been a year of change for the Section. In April 2007 Uttlesford DC gave notice that they were withdrawing from the Audit Partnership with this Council. Also in addition the Partnership Manager (Chief Internal Auditor) had resigned from the position as he had been successful in getting a senior post at Uttlesford.
- 4.2 A pilot audit partnership with N Herts DC started in July 2007. Their Audit Manager became the Partnership Manager and was at Stevenage for 2 days a week. For various reasons it was decided to terminate the partnership with effect from 31 March 2008. The principal reasons were the amount of slippage in the 2007/08 Audit Plan and the increase in audit work required by the newly formed SHL. The Audit Committee in January 2008 advised the Strategic Director (Resources) to recruit a full time Chief Internal Auditor.
- 4.3 As at April 2007, the establishment for the Internal Audit Section equated to 4.4 FTE. This included 0.6 FTE for the Partnership Audit Manager. This was reduced with the pilot N Herts partnership. For 2008/09 the establishment equates to 4.8 FTE. To assist in overcoming the backlog, two temporary interim auditors have been appointed.
- 4.4 The Audit Commission’s Review of Internal Audit Management Arrangements indicated insufficient resources to deliver the 2007/08 audit plan. It noted the audit

arrangements were being reviewed to address the shortfall.

5 WORK PLANNED AND COMPLETED IN 2007/08

5.1 Audit work planned to be completed during 2007/08 was included in the report to the Audit Committee on 6 March 2007 and is listed in Appendix 1. It also includes the changes to the Plan as reported to the January 2008 Audit Committee and the actual outturn of audits completed.

5.2 The breakdown of the 2007/08 audit days included in the original plan was as follows:-

Total staff days per annum	1163
less days required for leave and training	222
	941

less days required for management, audit planning and administration	188

Total chargeable days available	753

5.3 The combined impact of changed staffing circumstances, carry forward audits and special investigations was to reduce total annual productive days for planned audits in 2007/08 by 245 days from 753 days to 508 days. The breakdown of this figure is shown below:

	Productive days lost
Total Chief Internal Auditor productive days lost	19.5
Total Deputy Audit Manager productive days lost	28.5
Total Internal Auditor productive days lost	29
Adjustment for bank holidays	12
Review of productivity levels	21
Carry forward audits from 2006/07 to 2007/08	95
Special Investigations	40

Total Productive Days not available for 2007/08 Planned Audit Work	245

5.4 For the update report to the January 2008 Audit Committee an analysis was undertaken which focused on ensuring that the requirement of the Council's external auditors with regard to the audit of key financial systems in accordance with the managed audit agreement was achieved. Also the Service Level Agreement includes a target that at least 90% of the agreed Audit Plan for Stevenage Homes Ltd (SHL) be completed/in progress at the end of the financial year.

5.5 This analysis indicated a need for 311 days in order to complete key financial

systems audits, SHL audits and other work in progress before 31 March 2008. The actual available days for the four month period were only 219 days. This gave a requirement in excess of available days of 92 days.

- 5.6 Additional resources of 50 days were bought in from N Herts DC. However this still left a shortfall of 42 days which were required for three key financial systems (General Ledgers, Creditors, Housing Benefit) to be completed during 2007/08. Discussions were held with external audit and it was agreed that these audits could be carried forward into 2008/09 but had to be completed before 30 June 2008.

6 PARTNERSHIP WORKING

- 6.1 As previously mentioned Uttlesford DC withdraw from the Audit Partnership without advance notice in April 2007. A new pilot Partnership was subsequently established with N Herts DC which commenced from July 2007. For the reasons outlined above, it was not as effective as the previous partnership and both parties agreed to terminate with effect from 1 April 2008.

7 REPORTS ON INTERNAL AUDIT WORK

- 7.1 Wherever appropriate, Internal Audit Reports are produced to reflect the work undertaken from the Audit Plan. The primary purpose of the Reports is to provide management with an opinion on the adequacy of the internal control system, and to inform management of significant audit findings, conclusions and recommendations.

- 7.2 Each report is produced to a standard format that comprises the following sections:

7.2.1 Management Summary

Introduction

This includes brief details of the work covered during the audit, background information, previous audit recommendations and any still outstanding and the objectives to be achieved.

Findings and Recommendations

Detailed findings are included in the report and a completed Management Action Plan covering all the audit's recommendations.

Conclusions

The main findings of the audit are summarised under this heading together with the audit opinion which comments on whether the various systems of control are in place, are being complied with and any areas of key weakness.

7.3 Recommendations

Recommendations are reported as a problem identified together with a recommendation to address the problem. The problem identified should include the implications of the problem and the corresponding recommendation should provide a practical and constructive solution. Recommendations are categorised by using a combination of likelihood of occurrence and impact should the risk not be addressed and are entered in one of three levels of significance:

High

Essential for effective internal control and must be implemented

Medium

Highly desirable for effective internal control and should be implemented

Low

Desirable for improved internal control but where the risk associated with non-implementation is low.

- 7.4 Initially a draft report is issued to the relevant Manager so that errors or impractical solutions can be identified and corrected. Discussions with the auditee are held to confirm the accuracy of the report and to explain, if necessary, the reasoning behind recommendations made. Details of agreement/non-agreement are noted on the Action Plan (attached to each audit report), together with an agreed implementation date. The Plan also includes any comments that management have made regarding the recommendations.
- 7.5 If managers do not agree with recommendations than the courses of action for internal audit are:
- accept the non-agreement and remove the item from the report. This may be the case if the recommendation is based on a misunderstanding or is impractical to implement; or
 - include the recommendation but include the reasons for non-acceptance by managers or;
 - discuss the recommendation with more senior management in the hope of gaining agreement (see paragraph 7.6).
- 7.6 A final draft audit report is issued to Heads of Service as a matter of course in order that they can comment on the report and the auditee's responses prior to finalisation. For example, a Head of Service may consider that an implementation date is too far away and request a change to be agreed, or they may suggest an alternative solution to a problem. Final reports are sent to the Head of Service, copied to the manager for an audited area, Chief Internal Auditor and the appropriate Director.
- 7.7 The Head of Finance receives copies of all final reports. In addition, any other Officer who is responsible for a recommendation should receive a copy of the report or extract of specific points relating to them.
- 7.8 Summaries of final reports are reported to the Audit Committee so that Members are aware of the work undertaken by Internal Audit and can satisfy themselves that adequate reviews have been undertaken and that appropriate responses have been provided by managers.
- 7.9 An analysis of individual reports is shown in Appendix 2.

8 NON PLANNED AUDIT WORK

Considerable time was spent during the year on a number of areas of work that were not planned and/or did not result in the issue of a report. These included:-

- 8.1 National Fraud Initiative (NFI)
The NFI is the Audit Commission's data matching exercise that is designed to assist participating bodies to detect fraudulent and erroneous payment from the public purse. The core of NFI is the matching of data to help reduce the level of fraud experienced with housing benefits, occupational pensions, tenancies and payroll, amongst others. The Chief Internal Auditor is the key contact for the Initiative and has sole responsibility for co-ordinating the overall exercise. One main area of work carried out was with regard to duplicate payments. The participation in NFI supports the Council's Anti-Fraud and Corruption Policy, working as a fraud prevention and detection tool. The Council's NFI arrangements had been covered previously by the Audit Commission including a visit to the offices in April 2007 by one of their specialists who concluded that "the controls were largely satisfactory". This approach had been continued for the NFI exercise 2007.
- 8.2 Comprehensive Performance Assessment (CPA) - Key Lines of Enquiry (KLOE)
During May 2007, audit time was taken in providing the relevant evidence to satisfy certain KLOE required for the CPA and this involved close liaison with the Audit Commission.
- 8.3 Attendance at Groups etc
Throughout the year, the Chief Internal Auditor attended several meetings including the Hertfordshire Audit Group.
- 8.4 Special Investigations
During 2007/08, seven Special Investigations were carried out for the Council and one investigation for SHL. In total 91 audit days were spent on this confidential work.
- 8.5 Other Unplanned Work
Audit advice and guidance given included the following matters:-
SHL Building Insurance Claims
Proposed new cheque signing procedures
Process to follow when disposing of assets
Various advice on insurance, car loans redemption calculation and VAT issues regarding risk training
Over 40 financial appraisals were undertaken to support various procurement exercises
Ethics and Probity presentations
Update of Contracts Register

9 INTERNAL AUDIT PERFORMANCE

Some Performance Indicators were set for Internal Audit for 2007/08. The results are summarised over:

Performance Indicator	Actual 2006/07	Target 2007/08	Actual 2007/08	Comments
Percentage of productive time to total time available	90%	80%	71%	
Percentage of planned audits completed	71%	90%	24%	Slippage reported to 16 January 2008 Audit Committee. Also no allowance in plan for Special Investigations. The following measures have been introduced to improve performance: - appointment of new Chief Internal Auditor - two experienced temporary auditors employed up to the end of May
External Audit Opinion	Satisfactory	Satisfactory		

10 CHIEF INTERNAL AUDITOR'S OPINION 2007/08

- 10.1 During the course of the year, Internal Audit completed reviews and reported on most of the major systems identified by the Audit Commission as "material" to the figures included in the Council's Statement of Accounts for 2007/08. As explained earlier in this report three financial system audits planned for the year have been carried forward into 2008/09.
- 10.2 Audit opinion is broadly classified into one of the following four categories:
- Well controlled
 - Adequately Controlled
 - Inadequately Controlled
 - Uncontrolled
- 10.3 The majority of recommendations arising from 2007/08 audits were assessed as being of medium or low significance, which broadly means that key controls largely exist but there may be some inconsistency with compliance. The Internal Audit opinion for 2007/08 is therefore that risks identified by Internal Audit are largely adequately controlled. This reflects a substantial to full level of assurance on the overall adequacy and effectiveness of the internal control environment at the Council. The internal control environment was generally operating to a satisfactory standard in that the controls were considered to be adequate and effective for the majority of areas examined.
- 10.4 However there was some concern that the risk of error or loss was not always as well controlled in some areas reviewed and improvements in the

control environment are required. Common areas identified included the need to:

- adhere to Standing Orders/Financial Regulations, especially in respect of the ordering of Goods and Services and the control and monitoring of income
- revise, update or introduce Procedure Notes
- complete timely reconciliations between the sub-systems and the main Accounting systems
- address security issues in respect of computer access etc.

Where improvements are required, action plans have been completed and agreed recommendations have to be implemented in a timely way. (See detailed analysis in Appendix 2.)

11 COMPLIANCE WITH THE CODE OF PRACTICE

- 11.1 The Code of Practice ("The Code") sets out organisational and operational standards for internal audit in Local Government. Up to last year, previous Annual Internal Audit reports have included a general position statement on compliance with the Code. However, in accordance with amendments to the Accounts and Audit Regulations, there is now a separate report on this agenda addressing the new requirement to consider the Effectiveness of the System of Internal Audit during 2007/08. Consideration of compliance with The Code has therefore appropriately been transferred into the Effectiveness Report.

APPENDICES

Appendix 1 - Progress Against 2007/08 Audit Plan

Appendix 2 – Summary of Internal Audit Reports Issued During 2007/08