

CITY OF PLYMOUTH

Subject: Internal Audit – Annual Report 2010/11
Committee: Audit Committee
Date: 27 June 2011
Cabinet Member: Cllr Ricketts
CMT Member: Director for Corporate Support
Author: Martin Gould, Head of Devon Audit Partnership/
Sue Watts, Asst Head, Devon Audit Partnership
Contact: Tel: 01803 207320 / 01752 306710
e-mail: martin.gould@devonaudit.gov.uk, /
sue.watts@devonaudit.gov.uk
Ref: AUD/SW
Key Decision: No
Part: I

Executive Summary:

This report summarises the work undertaken by Devon Audit Partnership during 2010/11, reviews the performance and effectiveness of the Internal Audit service, and provides an audit opinion on the adequacy of internal controls. The report is particularly relevant, therefore, to the preparation of the Authority's Annual Governance Statement which is required under the Accounts and Audit (England) Regulations 2011

Corporate Plan 2011-2014:

The work of the Section assists the Authority in maintaining high standards of public accountability and probity in the use of public funds. The Section has a role in promoting high standards of service planning, performance monitoring and review throughout the organisation, together with ensuring compliance with the Council's statutory obligations.

Implications for Medium Term Financial Plan and Resource Implications: Including finance, human, IT and land

None

Other Implications: e.g. Section 17 Community Safety, Health and Safety, Risk Management, Equalities Impact Assessment etc.

The work of the Audit Service is an intrinsic element of the Council's overall corporate governance, risk management and internal control framework.

Recommendations and Reasons for recommended action:

It is recommended that:-

- 1) the report be noted
- 2) the Audit Committee endorse the adequacy and effectiveness of Plymouth's internal audit for the year ended 31 March 2011.

Alternative options considered and reasons for recommended action:

None, as failure to maintain an adequate and effective system of internal audit would contravene Accounts and Audit (England) Regulations 2011

Background papers:

Internal Audit Annual Plan 2010/11

Sign off:

Head of Fin	AB 8/6/11 MC 8/6/11	Head of Leg		Head of HR		Head of AM		Head of IT		Head of Strat Proc	
Originating SMT Member: Sue Watts, Asst Head, Devon Audit Partnership											

I INTRODUCTION

1.1 The Audit Committee, under its Terms of Reference contained in Plymouth City Council's Constitution, is required to consider the Chief Internal Auditor's annual report, to review and approve the Internal Audit programme, and to monitor the progress and performance of Internal Audit.

1.2 The Internal Audit plan for 2011/12 has already been presented and approved by Audit Committee on 25 March 2011. The following report and appendices, therefore, set out the background to audit service provision, reviews work undertaken in 2010/11, and provides an opinion on the overall adequacy and effectiveness of the Authority's internal control environment.

1.3 The Accounts and Audit (England) Regulations 2011 confirm the requirement that all Authorities need to carry out an annual review of the effectiveness of its internal audit, and need to consider the results of that review as part of its consideration of the system of internal control which is incorporated into their Annual Governance Statement (AGS) accompanying the annual Statement of Accounts.

2 BACKGROUND

2.1 Service Provision

2.1.1 The Internal Audit (IA) Service for Plymouth City Council is delivered by the Devon Audit Partnership (DAP). This is a shared service arrangement between Devon County Council, Torbay Council and Plymouth City Council constituted under section 20 of the Local Government Act 2000; the Partnership was formed on 1st April 2009. The Partnership undertakes an objective programme of audits to ensure that there are sound and adequate internal controls in place across the whole of the Council. It also ensures that the Council's assets and interests are accounted for and safeguarded from error, fraud, waste, poor value for money or other losses.

2.1.2 In carrying out its responsibilities Internal Audit liaises with all Directorates of the Authority. The Service consults with Departments in compiling its audit plans and meets regularly with Council Officers to review and monitor progress on recommendations arising out of audits and investigations. There is also close liaison with external agencies eg the external Auditors and the Police.

2.2 Regulatory Role

2.2.1 There are two principal pieces of legislation that impact upon internal audit in local authorities:

- **Section 6 of the Accounts and Audit (England) Regulations 2011** which states that:-
“.....a relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control”
“.....a larger relevant body must, at least in each year, conduct a review of the effectiveness of its internal audit”
- **Section 151 of the Local Government Act 1972**, which requires every local authority to make arrangements for the proper administration of its financial affairs.

2.2.2 There are also professional guidelines which govern the scope, standards and conduct of Internal Audit, including CIPFA's Code of Practice for Internal Audit in Local Government and the Institute of Internal Auditors' Standards and Guidelines.

2.2.3 In addition, Internal Audit is governed by policies, procedures, rules and regulations established by the Authority. These include standing orders, schemes of delegation, financial regulations, conditions of service, anti-fraud and corruption strategies, fraud prevention procedures and codes of conduct, amongst others.

2.2.4 The Internal Audit Strategy sets out how the service will be provided and the Internal Audit Charter describes the purpose, authority and principal responsibilities of the audit function.

3 OBJECTIVES AND SCOPE

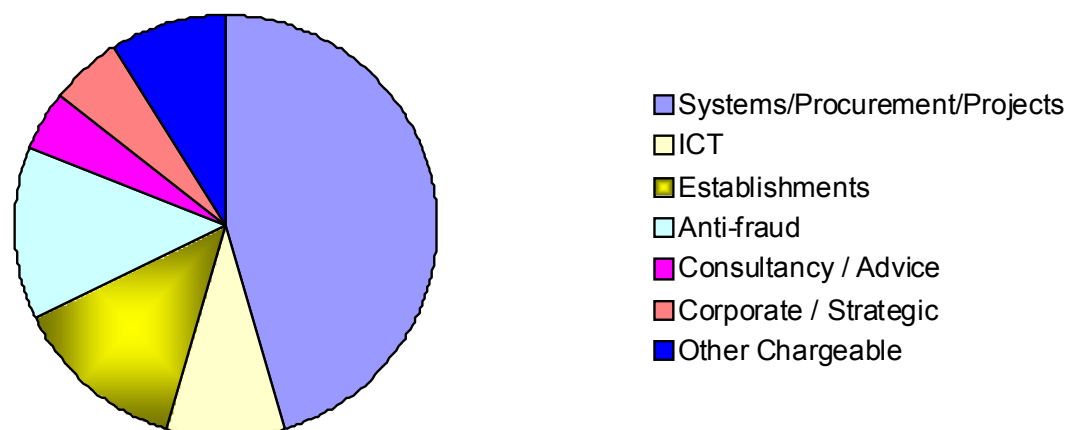
3.1 The original and updated Internal Audit Plans for 2010/11 were submitted to, and agreed by, the Audit Committee on 26 March and 15 November 2010 respectively.

3.2 This report now compares the work carried out with the work that was planned; presents a summary of work undertaken; includes an opinion on the adequacy and effectiveness of the Authority's internal control environment; and summarises the performance of the Internal Audit function against its performance measures and other criteria. The report outlines the level of assurance that we are able to provide, based on the internal audit work completed during the year.

4 INTERNAL AUDIT COVERAGE 2010/11

4.1 Delivery Against Plan

4.1.1 The following chart shows the proportion of direct audit days provided in the year ended 31 March 2011, by type of audit. Appendices 1 and 2 show, respectively, delivery of actual reviews and schools' audits against the original plan. It is pleasing to report that 94% of the 2010/11 audit plan was delivered in terms of reviews undertaken, which was achieved with greater efficiencies than in previous years and with a consequential reduction in resources deployed.



4.2 Systems / Procurement Reviews / Projects

4.2.1 Systems audits accounted for the largest element of the audit plan for the year and these are summarised in Appendix I. Further details are provided in Appendix 4, together with individual audit opinions for each review undertaken.

4.2.2 As mentioned above, the majority of the 2010/11 planned work programme was completed by 31 March, or was in progress at the end of the year. It was necessary to defer three reviews due to resource issues; whilst six additional reviews or unplanned pieces of work were added to the year's audit programme. Three systems reviews were deferred or cancelled at the clients' request.

4.2.3 Devon Audit Partnership has continued to attend and support a number of Project Boards and Project Teams set up to oversee significant and high profile procurement, construction, or system / service implementation projects. Projects include major procurements such as the South West Devon Waste Partnership, Plymouth Life Centre and Leisure Management, the construction of Tor Bridge High (the former Estover College) and Highview schools. During the year, Internal Audit was invited to join the Corporate Accommodation Strategy project.

4.2.4 Throughout the year, we have been asked to review and provide advice on these projects, in particular to emphasise the importance of good project governance, risk management as well as the compliance with robust procurement practices and procedures, careful definition and agreement of contracts and regular, robust monitoring of contracts throughout their duration. All of these are essential to protect the interests of the Council, its staff and taxpayers.

4.2.5 During 2010/11 Internal Audit continued to support the South West Devon Waste Partnership Waste PFI project as it progressed through Competitive Dialogue. This culminated in the submission of final tenders at the beginning of November and their subsequent evaluation over the following weeks, leading to the announcement of a preferred bidder in January. Internal Audit was present at the opening of the two bids and the numerous bid evaluation meetings, to witness that procedures were followed correctly. We then verified the evaluation scores and reviewed the evaluation process prior to the approval of the preferred bidder. Internal Audit was able to report to the Project Executive Board that the bids were received and opened in accordance with recognised procedures, that the evaluation process had been carried out in line with the agreed, published criteria and methodology and the overall scores reported to the Board and Joint Working Committee were correct.

4.2.6 With regard to the letting of the Leisure Management contract, Devon Audit Partnership have been engaged throughout the Competitive Dialogue process to ensure that each stage of the procurement was undertaken efficiently, effectively and transparently. We were present at the opening of bids submitted as part of the Invitation to Submit Outline Solutions (ISOS) and Call for Final Tender (CFT) stages of the procurement process. Audit can give assurance that the bid opening process was followed correctly on both occasions and DAP continued to provide support during the discussions with the preferred bidder up to the signing of contracts in May.

4.3 ICT (Computer Audit)

4.3.1 The 2010-11 ICT audit plan was created in accordance with the partnership's approach to risk based audit planning and allows us to review the Council's business-critical systems in a systematic and structured manner. The planning approach responds to emerging risks, priorities and projects and builds on our previous work.

4.3.2 We completed reviews of information management, information security, business continuity and the new data centre proposals that form part of the Council's Accommodation Strategy. We have followed up our previous work on the OLM Carefirst application and reviewed the SAP HR Payroll application.

4.3.3 Our concerns in relation to corporate information management arrangements have been previously reported to Audit Committee (November 2010). We found that although an apparently sound framework of information governance arrangements exists, effective and reliable information management practices have not yet been embedded throughout the organisation and the Council is not managing its information assets effectively at present.

4.3.4 Our work on information security management provides a similar picture in that effective arrangements at the corporate level are not embedded throughout the organisation. The arrangements for the security and eventual disposal of electronic information are of a good standard and compare favourably with the Information Commissioner's top six most frequently found causes of security breaches and remedial actions. On the other hand, this review has identified a number of weaknesses in the present arrangements for the security of the Council's physical information assets eg paper records.

4.3.5 Business continuity arrangements are of a good standard. The limitations imposed on ICT infrastructure resilience and recovery by having a single data centre have already been reported to the Head of Policies, Performance and Partnerships for consideration as part of the ongoing corporate business continuity planning process. The issue of a second data processing centre has a wider significance through its role in the Council's Accommodation Strategy and the issues associated with the future of the Civic Centre building. The Council's decisions regarding the future of the Civic Centre and Windsor House therefore impact both on the future business continuity arrangements and the progress of the ICT projects associated with the Accommodation Strategy.

4.4 Establishment Audits

4.4.1 Internal Audit fulfilled 100% of the schools' audit plan in 2010/11 by completing 34 schools' audits in the year. The requirements to meet the challenges of Financial Management Standard in Schools (FMSiS) were significant for schools in their first attempt; however the majority of schools met the standard prior to its abolition in November 2010. The FMSiS will be replaced by a simpler standard in September 2011 (the Schools Financial Value Standard) which will be applicable to all maintained schools but, now, not independent schools or academies.

4.4.2 We have been part of the DfE pilot study on the Schools Financial Value Standard (SFVS) which has, in general, received positive comment from the pilot schools. Comments have been restricted to procedural aspects of its completion and the need for training and support. We have fed back similar comments and the need for LA's to positively engage with the schools following review of their SFVS self-assessments.

4.4.3 Based on our work to date, systems and controls in schools are of a "Good to High Standard" and generally mitigate the risks identified.

The three key matters arising from schools' audits are the:

- demonstrable financing of school improvement plans;

- non-compliance with CRB checking and incomplete database records;
- incomplete and ineffective inventories.

4.4.4 Recommendations have been made to reduce risks to relevant schools; and, in other cases, recommendations have been made to strengthen what are reasonably reliable procedures.

4.4.5 One primary and eleven secondary schools have now become academies. Closure audits have been completed for two of these schools and reported issues were provided to the Department for Services to Children & Young People (as requested), and to the schools for action.

4.4.6 DAP are in the process of marketing and bidding for internal audit provision to academy schools across Devon. It is considered that retention of the internal audit for these schools would be beneficial to both the schools and the audit service as a whole.

4.5 Special Investigations and Anti-Fraud Work

4.5.1 Throughout the year, Internal Audit have been informed of instances of possible fraud or irregularities which have either led to advice being given to management on courses of action and improvements to controls, or auditors conducting formal investigations into the allegations.

4.5.2 In 2010/11, Internal Audit received 29 matters requiring investigation which came from officers and members of the public. Investigations into 21 of those concerns have now been completed and investigations are on-going in respect of the remaining cases.

4.5.3 Examples of the type of irregularities investigated include:-

- Misuse of Council resources
- Misuse of IT
- Breaches of the Council's Code of Conduct
- Financial irregularities

Results of the investigations included two members of staff resigning and five other employees receiving disciplinary sanctions.

4.5.4 Co-ordination of the work associated with the 2010/11 National Fraud Initiative (NFI) exercise has continued. The exercise, which is run every two years by the Audit Commission, requires all councils to provide data for cross-matching with information supplied by other organisations, such as the Department for Works and Pensions and the NHS, to identify potential cases of fraud and error. In October 2010, the Council provided data for areas such as payroll, creditors, care homes, various types of licences as well as parking permits and blue badges.

4.5.5 In February this year, the Council received a total of 14,548 data matches as a result of the above exercise. Of these matches, the Audit Commission categorised 2,723 as the highest priority. Since that time, Devon Audit Partnership has engaged with the departments affected and agreed action plans to deal with the matches received, and this work remains ongoing.

4.5.6 The Whistleblowing Policy, which was revised during 2010/11 and approved by the Audit Committee on 23 July 2010, aims to encourage staff to raise any legitimate concerns they have in relation to the Council's activities. The policy, which supports the Council's Anti-Fraud and Corruption Policy makes it clear that legitimate concerns can be raised without fear of reprisals.

A total of three Whistleblowers have come forward during 2010/11 of which:

- A departmental investigation into allegations regarding the personal use of hire cars led to a member of staff being issued with a written warning and a management review of associated procedures being undertaken;
- An Internal Audit investigation into allegations regarding the disposal of a Council asset found no substance to the allegations made. However, recommendations were made to tighten associated procedures;
- A departmental investigation into the alleged inappropriate promotion of 3rd party services concluded that there was no substance to the allegations made.

4.6 Consultancy / Advice

4.6.1 Internal Audit was consulted by all sectors of the Authority on many and varied topics including, for example, interpretation of financial regulations/standing orders, VAT, reclamation of funding, commercial catering controls, transfer of land to schools educational trusts, document retention, tenders etc.

4.6.2 The pro-active involvement of Internal Audit in control issues relating to new systems and changes, assists in protecting the Authority from loss, fraud and abuse. This early involvement is also intended to prevent unnecessary criticism when a formal audit review is undertaken and Departments are actively encouraged to seek advice at the outset of any changes.

5 ADDED VALUE

5.1 Devon Audit Partnership is committed to providing value for money to the Council and its stakeholders and, where possible, to identifying examples of specific, tangible benefits achieved through its work. Appendix 6 attached lists several examples of such benefits achieved by internal audit during 2010/11, but the following highlights just a couple:-

5.2 Housing Benefit Subsidy Claim

5.2.1 Internal Audit played a significant role in working with the Housing Benefit Team and Finance to mount a successful challenge to the DWP in respect of the 2008/09 Housing Benefit (HB) subsidy claim. Following qualification of the claim, the Secretary of State proposed to recover £540k from the Authority but, as a result of this collaborative working, this has subsequently reduced to £127,763 a saving of £412k.

5.2.2 As a result of observations made during the challenge exercise, Internal Audit identified a framework to mitigate the risk of the department failing to maximise its HB subsidy in the future. This was distributed to key staff from Housing Benefits and Finance who are most closely involved in the subsidy claim process to act as a check list upon which they can gain assurance that the claim process is robust in the future.

5.2.3 On receiving confirmation from the DWP of the revised figure, the Revenues and Benefits Service Manager emailed "this is fantastic news. A big thank you to all of you for the hard work

you put into this to 'make it right', it was a difficult claim and we have certainly learned a lot from this experience”.

5.3 NI 179 Value for Money

5.3.1 National Indicator 179 related to the total net value of ongoing cash-releasing value for money gains and the Council was required to submit it's efficiency savings to DCLG for 2009/10 by 22 July 2010. Once the savings for the year had been submitted by the various service areas to the Finance Dept, Internal Audit carried out a review of the arrangements in place to report on the savings achieved. Some weaknesses in the system were identified and Internal Audit worked closely with Finance officers to ensure that the Council had a robust framework in place for effectively identifying, recording and reporting efficiency savings achieved. In addition to driving improvements in business processes, Internal Audit also identified additional efficiency savings of £600k.

5.3.2 Whilst central government advised in October 2010 that the collection and submission of NI179 value for money gains was ending with immediate effect, the Council still has to make efficiency savings and the work carried out by Internal Audit supports this ongoing requirement.

6 REVIEW OF INTERNAL AUDIT SERVICE 2010/11

6.1 Staffing

6.1.1 Devon Audit Partnership operated throughout 2010/11 with an approved total establishment of 41.6 FTE. These resources were distributed throughout all clients of the partnership and staff were utilised at more than one client. Due to ongoing vacancies the partnership has not operated at full establishment during the year although, where appropriate, agency staff have been employed on a temporary basis. Arrangements are currently in hand to recruit additional auditors on fixed-terms contracts.

6.2 Audit Service Quality

6.2.1. The service we provide is designed to ensure compliance with the standards for internal audit published by the Chartered Institute of Public Finance and Accountancy (CIPFA) in its Code of Practice for Internal Audit in Local Government in the UK. The latest Code of Practice was published in December 2006, and Devon Audit Partnerships' processes continue to comply with the professional standards required.

6.2.2 Within the Devon Audit Partnership we have comprehensive procedures to ensure that all audits are conducted to the required standard. In particular, the scope of audit and audit brief are approved, before site work commences, by the appropriate Audit Manager, who also reviews each draft and final report before it is issued to ensure that all key controls have been properly evaluated and that adequate audit evidence has been obtained to support the findings. In addition, our work is subject to annual review by the Council's external auditors, Grant Thornton, who continue to rely on our work to support their audit opinion.

6.2.3 The Partnership continues to participate in the Audit Benchmarking Club administered by CIPFA. This has facilitated a comparison of our practices, coverage and costs with other council internal audit services. The most recent comparisons continue to show that we deliver a cost-effective service with a very high level of compliance with “good practice”.

6.2.4 During the year we have continued to include a “client satisfaction survey” with audit reports, for a confidential response to the Head of the Devon Audit Partnership. The vast majority of those returned have continued to be very positive about the audit service received, the audit report, and the conduct of the audit by our team members, and this is a tribute to their professional conduct of the audits.

6.2.5. Based on the responses received, 98% of the responses covering all areas of the audit were “satisfactory” or “very satisfactory”, and for a number of audits (39%) every single response was “very satisfactory”. The analysis of responses for this year shows that very high standards have been maintained, which is a very commendable achievement by the team.

6.3 Performance

6.3.1. There are no national Performance Indicators in existence for Internal Audit, but the Partnership does monitor the following Local Performance Indicators (LPI’s):

Local Performance Indicator (KPI)	2010/11	2010/11
	Target	Actual
Percentage of Audit Plan Completed	90%	94%
Percentage of fundamental / material systems reviewed annually	100%	84%
Customer Satisfaction - % satisfied or very satisfied as per feedback forms	90%	98%
Draft Reports produced within target number of days (currently 15 days)	90%	72%
Final reports produced within target number of days (currently 10 days)	90%	97%
Average level of sickness absence	2%	3%
Percentage of staff turnover	5%	0%

6.3.2 As mentioned in para 4.1.1 above, the percentage completion of the audit plan for 2010/11 was above target, and was delivered in a fewer number of days than originally planned. Efficiencies from the DAP partnership are now being realised through, for example, the use of audit management software, sharing of auditor experience and expertise between offices, functional team structures etc.

6.3.3 As is the norm, some material systems’ reports had not been issued by the end of year, but work was substantially complete and there were no matters of serious concern to be reported.

6.3.4 The customer satisfaction results derive from questionnaires completed after each audit, and the results continue to demonstrate the very high regard placed on the service by all parts of the Authority.

6.3.5 Timeliness of issuing both draft and final reports is an area which is kept under constant review. The below target draft report PI is largely due to some reports being delayed in the first half of the year because of timing issues around schools’ holidays.

7. REVIEW OF INTERNAL AUDIT BY EXTERNAL AUDIT

7.1 Internal Audit is obliged under the Accounts and Audit Regulations to meet the standards specified in CIPFA’s Code of Practice for Internal Audit in Local Government. These standards

set out specific essential requirements of an Internal Audit department which include eg independence, staffing and training, planning, recording, performance and effectiveness etc.

7.2 External Auditors use CIPFA standards as a model against which to regularly assess and report on the competency and effectiveness of Internal Audit, to enable them to place reliance on Internal Audit's work as part of the 'managed audit' arrangements.

7.3 The External Auditors have recently completed a review of the Internal Audit arrangements and have stated in their Interim Report to Audit Committee today that "overall, we have concluded that the Internal Audit service continues to provide an independent and satisfactory service to the Council and that we can take assurance from their work in contributing to an effective internal control environment at the Council".

8 INTERNAL AUDIT OPINION

8.1 The Chief Internal Auditor is required to provide the Council with an assurance on the adequacy and effectiveness of its accounting records and of its system of internal control in the Council. In giving our opinion it should be noted that this assurance can never be absolute. The most that the internal audit service can provide to the Council is reasonable assurance, based on risk-based reviews and sample testing, that there are no major weaknesses in the system of control.

8.2 A summary of Internal Audit's opinion on the individual reviews carried out during the year is included in Appendix 3, with more details provided in Appendix 4.

8.3 In carrying out systems and other reviews, Internal Audit assesses whether key, and other, controls are operating satisfactorily within the area under review, and an opinion on the adequacy of controls is provided to management as part of the audit report.

8.4 All final audit reports also include an action plan which identifies responsible officers, and target dates, to address control issues identified during a review. Implementation of action plans are reviewed during subsequent audits or as part of a specific follow-up process.

8.5 Directors have been provided with details of Internal Audit's opinion on each audit review carried out in 2010/11 to assist them with compilation of their individual annual governance assurance statements. If significant weaknesses have been identified in specific areas, these have been considered by the Authority in preparing its Annual Governance Statement which will be accompanying its published Statement of Accounts for 2010/11.

8.6 Overall, and based on work performed during 2010/11, Internal Audit is able to provide reasonable assurance on the adequacy and effectiveness of the Authority's internal control environment.

8.7 Significant Issues

8.7.1 In September 2010, the Internal Audit Service issued a report which concluded that fundamental weaknesses existed in the Council's corporate information management

arrangements. The findings of that report were accepted by the Council's Chief Information Officer and Corporate Information Manager and were discussed at Audit Committee in November 2010.

8.7.2 The report included an 'Action Plan' which is now being progressed. The Corporate Information Manager attended Audit Committee, in March 2011, to update them on the positive steps that are being taken to embed information management principles throughout the organisation and other key actions are being taken to formalise responsibilities and improve staff training and awareness.

8.7.3 Information management is a far reaching and complex process and many of the issues raised in the report are dependant upon one another. It is therefore essential that the recommendations are implemented in the correct sequence, in order to ensure that the required improvements are achieved.

8.7.4 The Audit Service has now completed a follow-up exercise to establish the extent of progress made towards implementing the recommendations contained within the report and this review has confirmed that the agreed actions are being taken in a logical and orderly fashion. Progress will continue to be monitored and reported on a regular basis. A summary of the weaknesses identified in the initial review and results of the recent follow-up is attached at Appendix 5.

9. RECOMMENDATIONS

It is recommended that:

- 1) the report be noted
- 2) the Audit Committee endorse the adequacy and effectiveness of Plymouth City Council's system of internal audit for the year ended 31 March 2011.