AUDIT AND GOVERNANCE COMMITTEE   **27 May 2011**

INTERNAL AUDIT ANNUAL REPORT 2010/2011

Report of Report of the Head of Audit, Risk and Procurement

1.   Purpose of Report

1.1   To consider the performance of Internal Audit for 2010/2011, areas of work undertaken, and the internal audit opinion regarding the adequacy of the overall system of internal control within the Council. For completeness, this report covers work completed for the Council and all associated bodies for which audit services are provided.

2.   Description of Decision

2.1   The Audit and Governance Committee is asked to note Internal Audit's performance and consider the audit opinion on the adequacy of the overall system of internal control within the Council for the financial year 2010/2011.

3.   Key Performance Indicators

3.1   The Internal Audit service measured its performance in terms of Efficiency, Quality, Client Satisfaction and Continuous Improvement. Performance during the year is shown in Appendix 1.

3.2   All Key performance indicators for the year were achieved with the following exceptions:

3.2.1   The agreed Plan for the year included 102 audits. Of these, 98 were completed (96.1%). A further 7 unplanned audits were completed within the year. The four planned audits which were not completed are as follows:

- Corporate Performance Management - The main purpose of this audit was to review the implementation of the new performance monitoring system which had been planned to be rolled out across all directorates during the financial year. This is now to be undertaken as part of the implementation of the Business Transformation Programme, and therefore this audit will be deferred to align with the programme.

- Port Governance Arrangements – This audit was to review the new governance arrangements that have developed during the financial year. As some of these arrangements were not fully in place / embedded and are to be further developed, the audit was deferred and is included in the operational plan for 2011/2012.

- Office of the Chief Executive Partnership Arrangements – This audit was to focus on the arrangements for delivering job linkage services through external partners within the city. The Government has since changed the funding arrangements for these services and therefore these services will have to be provided in a completely different way.

- Property Asset Database – The aim of this audit was to verify the accuracy of the information which was being input to a new database regarding the Council's assets. Due to a delay in implementing this project the audit has been rescheduled for 2011/2012.

3.2.2 The audit cost per £m gross turnover of the Council currently stands at £998 against a target of being lower than the average of the CIPFA comparator group, of £941. Whilst costs have been reduced since last year (the measure being £1,071) it would seem that the comparator authorities have reduced their overall costs to a greater extent. A review of the cost of the overall service has been undertaken which has reduced costs for 2011/2012 by £90,000.

3.2.3 The percentage of medium risk recommendations implemented currently stands at 85% (excluding schools) against a target of 90%. Reporting arrangements have been developed to now include a quarterly report to each Executive Director to provide them with an update in relation to Internal Audit work. This includes reporting the latest implementation rate for their directorate and an analysis of the results of each follow up undertaken. When the results of each follow up are reported to the Head of Service and Executive Director this now includes information about the effect that particular follow up has had on the overall implementation rate for the directorate. A summary of the performance by directorate for medium risk recommendations is shown in the table below:

Directorate / Body	Implementation Rate March 2010	Implementation Rate March 2011
Children's Services (non schools)	73%	90%
City Services	96%	85%
Office of the Chief Executive	86%	88%
Health, Housing & Adult Services	81%	76%
Total Council Implementation Rate Excluding Schools	**84%**	**85%**
Children's Services – Schools	83%	88%
Total Council Implementation Rate	**84%**	**86%**

4.   Summary of Internal Audit Work

4.1   The Internal Audit Strategy and Operational Plan presented to the Committee in March 2010 explained that the audit risk assessment process had been changed and that assurance was to be provided to members based on 18 key risk areas. The audits which were to contribute to the audit opinion on each of the key risk areas were identified. Appendix 2 shows the planned audits that have been completed during the year and the key risk area which they relate to. The overall opinions given are based on the results of audit work in the current and previous financial years. It can be seen from the appendix that the overall opinion for all key risk areas is either good or satisfactory apart from Information Governance. Audit work has highlighted that arrangements to govern and protect the Council's information are unsatisfactory in a number of areas.

4.2   As a result of the audits carried out in the year to date, a number of recommendations have been made to improve internal control. The numbers of recommendations made to date in relation to the Council are shown below:

Categorisation of Risk	Definition	Number Made
High	A fundamental control weakness or non-compliance, which presents material risk to the audited body and requires immediate attention by senior management.	0
Significant	There is a control issue which could have a significant impact on the achievement of the aims and objectives of the organisation, or which presents a significant risk to the organisation's reputation. Prompt management action is required to remedy the situation.	3
Medium	There is a control weakness or non-compliance within the system, which presents a significant risk to the area or service being audited, and management attention is required to remedy the situation within a reasonable period.	553
Low	There is a minor control weakness or non-compliance within the system and proportional remedial action is required within an appropriate timescale.	99

In addition, observations are also made where there are opportunities for improvements to be made but there is no weakness in internal control.

The three significant risk recommendations, which were all made in March 2011, are in relation to the following:

- Vulnerable Adults Protection Arrangements - In April 2010, the Care Quality Commission (CQC) published a report on an inspection of the Council's arrangements for safeguarding vulnerable adults. In the report it was stated '*There were weaknesses in operational and performance management arrangements which meant that the* [Safeguarding Adults Partnership] *Board could not be confident that all reported incidents were investigated promptly and action was taken to reduce further abuse'.* In response to the CQC inspection findings, the Executive Director of Health, Housing & Adult Services set out an Improvement Plan, detailing how all of the recommendations arising from the inspection would be addressed.

  One of the actions refers to the need to introduce revised business processes to ensure better information management and communication about safeguarding issues. The timescale set by the Directorate for this action to be implemented was May 2010. Satisfactory evidence was sighted to confirm that appropriate processes have been developed, and it is understood that a comprehensive package of training in the new processes has also been developed. However, the new processes and training package have yet to be implemented. Two significant recommendations have been issued in relation to this.

- HR Management / Financial Management System Consolidation – The Council's HR and Financial Management systems were consolidated into one system in July 2010. The audit covered the security and access arrangements of the consolidated system and found the arrangements to be satisfactory except in relation to disaster recovery arrangements. Appropriate disaster recovery plans were in place when the systems were separate but following the consolidation, new plans have yet to be developed, although work is ongoing in relation to this. Given that these systems currently support the Council's financial and payroll infrastructure a loss of access for an unknown period of time could have serious implications on the ability of the Council to provide and manage these essential services. The risk is therefore considered to be significant.

4.3   In relation to the audits that have been finalised to date, all recommendations have been agreed by management.

4.4   Whilst a number of recommendations to improve internal control have been made, the work undertaken did not identify any matters material to the overall internal control environment of the Council.

4.5   Results of the key areas of work are included below.

Key Systems

In relation to the Council's key systems (financial and non-financial), audits have been undertaken within the various key areas over the year.
Business Transformation Programme

Audit work has been completed in relation to the Council's Business Transformation Programme, including planned audits in relation to the management of the programme and its projects and providing advice in

relation to changes that are being made to key systems and processes, for example the review of the Blue Badge Scheme, procedures for financial transactions and the operation of the Internal Jobs Market and SWITCH.

Information Governance

As already mentioned in paragraph 4.1, concerns have been identified with the arrangements for information security and governance in a number of areas within the council. Following from audit work undertaken in 2009/2010 the physical security arrangements within the Civic Centre have improved but are still not as strong as they should be. A survey of staff working outside of the Civic Centre has identified that information governance requirements are not adequately circulated and not all staff are aware of their responsibilities. A number of recommendations have been made across the Council as well as in relation to the Corporate arrangements.

Schools

The requirement to achieve the Financial Management Standard in Schools has now been abolished by the Government. During the latter part of 2010/2011 audits of schools still continued to be carried out against the good practice guidance set out in the standard. A new standard is being prepared but this will not require any external verification or assessment. The approach to auditing schools in the future is currently being reviewed to ensure that assurance can still be given regarding the significant amount of money spent by schools.

Counter Fraud Work

Specific work aimed at detecting fraud, misappropriation or errors which may have resulted in financial loss has been undertaken in the following areas:

- Completion of the follow up of the National Fraud Initiative (NFI) data matching exercise, managed by the Audit Commission.
- Cash and bank imprest accounts to ensure that they are managed appropriately, properly reconciled, subject to adequate security arrangements and are used for legitimate Council spending.
- BACS transactions.
- Business rates and council tax refunds.
- Security of stocks of cheques.
- Gifts and hospitality.
- Payments for car mileage to leased car holders.
- Write-offs.
- Analytical review of payroll costs and creditor payments.

It was pleasing to note that no fraudulent activity was discovered and that, in general, adequate controls are in place within the areas examined to manage the risk of fraud. Where appropriate, advice was provided to improve arrangements to manage the risk of fraud.

4.6　A small number of investigations have been undertaken and action is being taken to address any issues identified. None of these investigations have an impact on the opinion on the overall system of internal control. Internal Audit was also involved in providing advice on investigations carried out by management in various Directorates.

4.7　Internal Audit has also provided support and guidance to all Directorates and associated bodies during the year in relation to systems developments, identification of risks, improvements to financial procedures and general day-to-day advice on various issues. This has included, for example, preparing a paper to senior management on the impact of the provisions of the Bribery Act 2010.

5.　Quality Assurance

5.1　Internal Audit operated a quality system which was certified to ISO 9001:2008. In July 2010 an external assessment was carried out which concluded that standards were being maintained. However, it has been decided that the external assessment no longer serves its purpose as the standards are well embedded in the procedures followed during day to day audit work. The service has therefore withdrawn from the ISO certification standard but will maintain its quality procedures in line with professional standards and undertake internal quality audits to ensure that the standards are upheld.

5.2　Post Audit Questionnaires are issued to clients after every audit to elicit their opinions on a range of areas using a scoring range of 1 (Good) to 4 (Poor) for each area. The number of questionnaires returned during the year was 47, with the average score for the overall rating being 1.2 (meeting the IAS target of achieving an average score of less than 1.5).

5.3　Within the year Internal Audit also took part in a user satisfaction survey run by the CIPFA benchmarking club. All clients who had received an audit report in the previous year were invited to complete a questionnaire which asked 35 questions covering Audit Services, Audit Staff, Conduct of Audits, Audit Reporting, and Customer Service. The questionnaire also asked for the respondent's overall rating of Internal Audit Services. The key results were as follows:

- In relation to the 35 questions, all except 2 received a performance rating of either excellent or good.
- The overall average rating was Good.
- The overall performance score received was higher than the group average and was second highest of the 20 authorities which took part in the survey.

6.　Effectiveness of the System of Internal Audit

6.1　The Audit Commission have carried out an independent review of the effectiveness of Internal Audit by reference to the CIPFA Code of Practice for Internal Audit. The Audit Commission concluded that the service continues to comply with the relevant standards.

7. Conclusion

7.1 This report provides information regarding progress against the planned audit work for the year and performance targets. Although it has not been possible to complete 4 of the planned audits within the year sufficient audit work has been completed to provide an opinion on the overall system of internal control.

7.2 Using the cumulative knowledge and experience of the systems and controls in place, including the results of previous audit work and the work undertaken within 2010/2011, it is considered that overall throughout the Council there continues to be an adequate system of internal control.

8. Recommendation

8.1 Members are asked to note the report.

Background Papers

Internal Audit Strategy and Annual Operational Plan 2010/2011 - Audit and Governance Committee, 26th March 2010.

Key Performance Indicators

Internal Audit Services' Overall Objectives, Key Performance Indicators (KPI's) and Targets for 2010/2011			
Cost & Efficiency			
Objectives	**KPI's**	**Targets**	**Actual Performance**
1) To ensure the service provides Value for Money	1) Charge per Audit Day	1) Lower cost than average within CIPFA Benchmarking Club – Comparator Group (Unitary Authorities)	1) Achieved – Sunderland Cost per man day £282 and average for comparator group £310
	2) Audit Cost per £m Gross Turnover of the Council	2) Lower cost than average within CIPFA Benchmarking Club – Comparator Group (Unitary Authorities)	2) Not achieved – Sunderland audit cost per £m gross turnover £998 and average for comparator group £941
	3) Percentage of planned audits completed (including agreed variations)	3) 100%	3) Not Achieved - 96.1%
	4) Average number of days between end of fieldwork to issue of draft report	4) 10 working days or less	4) Achieved – 7.8 working days
	5) Percentage of draft reports issued within 15 days of the end of fieldwork	5) 85%	5) Achieved – 92.2%
	6) Percentage of audits where the number of days between the start of the audit and the end of fieldwork is within a target of twice the budgeted number of days	6) 75%	6) Achieved – 76.5%

Key Performance Indicators

Internal Audit Services' Overall Objectives, Key Performance Indicators (KPI's) and Targets for 2010/2011			
Quality			
Objectives	**KPI's**	**Targets**	**Actual Performance**
1) To maintain an effective system of Quality Assurance	1) ISO9001:2000 Certification	1) Retain certification	1) Certification was retained in July 2010 although it has since been decided to withdraw from the scheme due to value gained.
2) To ensure recommendations made by the service are agreed and implemented	2) Percentage of high, significant and medium risk recommendations made which are agreed	2) 100%	2) Achieved - 100%
	3) Percentage of agreed high, significant and medium risk recommendations which are implemented	3) 100% for high and significant risk. 90% for medium risk.	3) Achieved - 100% for significant risks Below target – 85% for medium risks (exc. Schools)
	4) Opinion of External Auditor	4) Satisfactory opinion	4) Satisfactory
Client Satisfaction			
Objectives	**KPI's**	**Targets**	**Actual Performance**
1) To ensure that clients are satisfied with the service and consider it to be good quality.	1) Results of Post Audit Questionnaires	1) Overall average score of better than 1.5 (where 1=Good and 4=Poor)	1) Achieved - Overall average score of 1.2 from 47 returns
	2) Results of other Questionnaires	2) Results classed as 'Good'	2) Achieved - IPF survey of clients showed overall rating of 'Good'
	3) Number of Complaints / Compliments	3) No target – actual numbers will be reported	3) 0 complaints 14 compliments

Key Performance Indicators

Internal Audit Services' Overall Objectives, Key Performance Indicators (KPI's) and Targets for 2010/2011			
Continuous Improvement			
Objectives	**KPI's**	**Targets**	**Actual Performance**
1) To ensure that the service develops in line with modern thinking and practice on Internal Auditing	Improvement in actual performance in relation to previous years in the following areas: 1) Average number of days between end of fieldwork to issue of draft report 2) Percentage of draft reports issued within 15 days of the end of fieldwork 3) Percentage of agreed high, significant and medium risk recommendations which are implemented	Improvement in actual performance from 2009/2010.	1) Achieved Performance 2008/2009 - 10.9 Performance 2009/2010 - 10.5 Performance 2010/2011 - 7.8 2) Achieved Performance 2008/2009 - 82% Performance 2009/2010 - 87.5% Performance 2010/2011 - 92.2% 3) Achieved Performance 2008/2009 - 84% Performance 2009/2010 - 84% Performance 2010/2011 - 85%

Key Performance Indicators

Audit Coverage 2010/2011

Key Risk Area	Planned Audits	Conclusion (individual audit undertaken in 2010/2011)	Overall Opinion (current and previous 3 years work)
Corporate Governance	Annual Corporate Governance Review	Good	Good
Commissioning	Funding for 14-19 Year Olds External Placement of Children Responsive Local Services Community Development Service - Sunderland Compact Supporting People Service	Good Good Unsatisfactory Unsatisfactory Satisfactory	Satisfactory
Service / Business Planning	Responsive Local Services	N/A – scope changed	Satisfactory
Partnerships	Children's Services - Partnership Arrangements Office of the Chief Executive - Partnership Arrangements Corporate Partnership Arrangements	Satisfactory N/A Unsatisfactory	Satisfactory
Financial Management	Supporting People Grant Dedicated Schools Grant - Allocation of Funding Funding for 14-19 Year Olds External Placement of Children 39 Schools (Nursery, Primary and Special) City Services Job Costing 2 Leisure Centres Assessments for Personal Care Personal Budgets / Resource Allocation System Port Governance Arrangements Council Tax - Liability Business Rates - Liability Periodic Income - Billing BACS Arrangements Accounts payable - processing and payment Back on the Map Financial Management	Satisfactory Good Good Good Good Good Satisfactory Unsatisfactory Unsatisfactory N/A Good Satisfactory Good Good Satisfactory Satisfactory	Satisfactory

Audit Coverage 2010/2011

Key Risk Area	Planned Audits	Conclusion (individual audit undertaken in 2010/2011)	Overall Opinion (current and previous 3 years work)
Risk Management	Corporate Risk Management Framework Vulnerable Adults Protection Arrangements Port Governance Arrangements Office of the Chief Executive - Risk Management Arrangements 39 Schools (Nursery, Primary and Special)	Good Unsatisfactory N/A Satisfactory Good	Satisfactory
Programme and Project Management	Improvement Programme - Programme Management Project Management - Strategic and Shared Services Project Management - Commissioning and Service Review Project Management - Customer Services Project Management - ICT Project Management - Procurement and Third Party Spend Project Management - Organisational Development Improvement Programme - Benefits Realisation Project Management - Smarter Working	Satisfactory Satisfactory Good Good Good Good Good Satisfactory Satisfactory	Good
Local Taxation	Council Tax - Liability Business Rates - Liability	Good Satisfactory	Good
Procurement and Contract Management	BSF Contract Management - ICT Contract Corporate Procurement Strategy Supplier Relationship Management System - User Access Buy Sunderland First	Good Satisfactory Satisfactory Satisfactory	Satisfactory
Human Resource Management	39 Schools (Nursery, Primary and Special)	Satisfactory	Satisfactory
Asset Management	Property Asset Database	N/A	Satisfactory
ICT Strategy and Delivery	ICT Strategy HR Management / Financial Management System Consolidation	Satisfactory Satisfactory except DR	Satisfactory

Audit Coverage 2010/2011

Key Risk Area	Planned Audits	Conclusion (individual audit undertaken in 2010/2011)	Overall Opinion (current and previous 3 years work)
Fraud and Corruption	Counter Fraud Testing Building and Development Control 39 Schools (Nursery, Primary and Special) 2 Leisure Centres	Satisfactory Satisfactory Good Satisfactory	Satisfactory
Information Governance	Performance Regarding Under 18 Conception Rates Contact Point 39 Schools (Nursery, Primary and Special) Customer Contact Centre Assessments for Personal Care Information Sharing / NHS Partnership Vulnerable Adults Protection Arrangements Compliance with the Data Handling Guidelines	Satisfactory Satisfactory Good Unsatisfactory Unsatisfactory Unsatisfactory Unsatisfactory Unsatisfactory	Unsatisfactory
Business Continuity and Emergency Planning	Corporate Business Continuity Management Winter Maintenance	Satisfactory Unsatisfactory	Satisfactory
Performance Management	Performance Regarding Under 18 Conception Rates Community Development Service - Sunderland Compact Port Governance Arrangements Sustainability / Carbon Management Responsive Local Services	Satisfactory Unsatisfactory N/A Unsatisfactory Unsatisfactory	Satisfactory
Payroll	Payroll Processing and Payment 39 Schools (Nursery, Primary and Special)	Good Good	Good
Housing Benefits	No audits planned	N/A	Satisfactory

Audit Coverage 2010/2011