

Name of meeting and date: Standards Committee 30th September 2009

Title of report: Annual Report of Internal Audit 2008/09

Is it likely to result in spending or saving £250k or more, or to have a significant effect on two or more electoral wards?	Not applicable
Is it in the Council's Forward Plan ?	Not applicable
Is it eligible for "call in" by Scrutiny ?	Yes
Cabinet member portfolio	Finance

Electoral [wards](#) affected and ward councillors consulted: All

Public or Private: Public

1. Purpose of report

To provide information on the activity of Internal Audit in the year to 31st March 2009.

2. Key points

This report describes the activities of the Council's Internal Audit section during 2008/09. It provides

*an "opinion" on the state of financial and business control systems, and information about the type and volume of work carried out and key findings during the year to 31 March 2009.

* information about work planned for 2009/10 and issues relevant to the current year.

It concludes that the system of internal audit is effective and it recommends acceptance (by the Corporate Governance & Audit Committee) that "the Council has an adequate and effective control environment".

3. Implications for the Council

None directly

4. Consultees and their opinions

None

5. Officer recommendations and reasons

To note/determine if further action is sought on any matter identified

6. Cabinet portfolio holder recommendation

N/a

7. Next steps

None.

8. Contact officer and relevant papers

Martin Dearnley, Assistant Director (IA, Risk & Procurement) 860 1133
The Annual Report is attached.
Background papers; 4x Quarterly reports

KIRKLEES COUNCIL

STRATEGIC FINANCE SERVICE

INTERNAL AUDIT

ANNUAL REPORT OF INTERNAL AUDIT 2008/09

1. Introduction

- 1.1 This report provides a summary of the activities and performance of Internal Audit during 2008/09, an assessment of the adequacy and effectiveness of the Council's internal control environment during the year and the plans for 2009/10

2. About Internal Audit

- 2.1 The scope of Internal Audit's activity is established by the Council's Financial Procedure Rules and statements of operating practice. The majority of time spent relates to the review of financial systems and processes but the planned work includes review of a broad range of business controls. This approach is necessary to support the requirements of The Accounts and Audit Regulations (Amendments) (England) 2006 for authorities to "conduct a review at least once a year of the effectiveness of its systems of internal control", which supports the Annual Governance Statement in the Statement of Accounts. Internal Audit operates to the CIPFA/ASB standards for Internal Audit.
- 2.2 Quarterly Reports on the activities of Internal Audit have been provided to the Corporate Governance and Audit Committee,(and, as a part of consolidated performance reporting to Executive Management Group and Cabinet Briefing). These reports provide information about major and special investigations and an opinion (between 'good' and 'very unsatisfactory') from each of the programme of audits on systems, processes and establishments/locations/schools. Unsatisfactory means a single major weakness or many minor weaknesses in operations, processes or controls at the time of the audit. Implementation of the agreed recommendations should provide a satisfactory degree of control in all cases. Information on follow up of earlier internal audit work is also provided.

3. Summary of Audit Work in 2008/09

- 3.1 The following table provides information about audit work during the year. (It also includes information relating to a small number of pieces of work that have been completed since the fourth quarterly report)

	2008/09	2007/08	2006/07	2005/06
Number of Days spent on audit work	2,767	2,962	3,148	2,944
Number of Process and Systems Examined	80	99	101	81
Percentage found "unsatisfactory".	13%	13%	7%	16%
Number of location/ establishment audits undertaken.	25	23	37	49
Percentage found "unsatisfactory"	32%	30%	16%	27 %
Number of school audits undertaken (inc FMSiS assessments)	43	30	39	44
Percentage found "unsatisfactory"	2%	17%	3%	32%
Overall proportion of work found "unsatisfactory"	13%	21%	12%	28%
Follow up audit work carried out	20	16	32	30
Percentage where progress was "unsatisfactory"	10%	19%	16%	20%
Number of Business Control Audits Undertaken	23	10	18	13
Percentage found "unsatisfactory"	13%	0%	6%	23%
Number of investigations into irregularity	15	13	11	13
Number of management, governance or value for money studies	3	10	6	5
Number of grant audits, consultancy, projects	20	10	20	14
Completed formal tasks(sum of QRs)	229	223	264	252

The definition of completed work differs slightly to that used in quarterly reports

- 3.2 The overall proportion of work, which identified that systems or operations were "unsatisfactory", was 13%, although this statistic is weighted downwards by the inclusion of FMSiS(Financial Management Systems in Schools) submissions which are assessed only when they are considered to be likely to achieve a conditional pass level. If FMSiS work is excluded, there were 111 reviews of financial activity, of which 19 , or 17% were unsatisfactory, suggesting an outcome close to the longer term position that roughly one in five audits conclude with an "unsatisfactory" opinion.

- 3.3 All of the key financial systems achieved at least a "generally satisfactory" standard, and the significant majority were scored as "satisfactory". There were 'unsatisfactory' aspects of a few activity areas, e.g. some Services' misuse of purchasing cards identified in Creditor Payments and Procurement audits, though these were peripheral to the overall integrity of the Council's financial systems. The work identified no area where there appears to be a significant concern, although it must be appreciated that there is a risk attached to even the most robust systems, operated correctly, as demonstrated by the correct operation of the Treasury Management Policy, but the "loss" of £1m invested in Icelandic Banks.
- 3.4 Non-financial business control systems were either generally satisfactory, or satisfactory, although there was scope for improvement in some, for example risk management, and scope for sustained improvement in others, such as absence management.
- 3.5 Traditionally internal audit work has identified concerns about failures at operational locations. These do not prejudice the overall stability of the Council's finances or governance but do reflect weakness in operational management. Audit work this year has identified a 32% rating of "unsatisfactory" financial operations at locations, which is very similar to last year.
- 3.6 Relatively little traditional audit work on schools was performed in 2008/09 due to the introduction by the Department of Children, Schools and Families of the Financial Management Standard in Schools (FMSiS). This Standard requires schools to complete a self-assessment of their financial and governance arrangements which is then externally assessed by either Internal Audit or an accredited external assessor (to date only 1 school has chosen not to use Internal Audit).
- 3.7 All secondary schools should have demonstrated that they achieved the Financial Management Standard by 31 March 2007. 20 schools successfully achieved this target and assurances were sought from the remaining 5 that they would achieve it by 31st March 2009. In fact, none had achieved the standard by 31 March 2009. The one which has chosen an accredited external assessor has now passed the formal assessment, and at the other 4 some progress has been made at most of these schools. The FMSiS standard requires reassessment every three years, so all the existing schools also require review this year (though having achieved the standard, provided that procedures remain unchanged, this should not prove a difficult area).
- 3.8 All primary, middle and special schools are required to achieve the Financial Management Standard by 31 March 2010. A total of 48 primary schools have now been assessed out of 164. The administrative burden of completing a file of evidence has caused significant problems for many schools despite agreements to try to reduce the bureaucracy of this process. There are doubts over whether all schools will achieve the standard by the Department of Children, School and Families' 2010 deadline, but the process has no sanction.

- 3.9 The main issue in terms of IT audit continues to be that of governance, as identified through the work of the Corporate Information Security group, and the risks that this creates in respect of achieving accreditation to Government Connect, and other Council priorities around achieving flexible working.
- 3.10 In addition to the routine programme of work, a number of special investigations, value for money studies, grants and accounts analysis, and other consultancy tasks have been undertaken. These included:

Investigations

- School Meals cash theft
- Missing money at Open Markets
- Inappropriate behaviour by call centre operative

Value for Money, Management and Governance Studies

- Risk management
- National Fraud Initiative 2008-09
- VFM statements
- Validation of carbon impact statements
- Corporate Complaints

Grants and Accounts works

- LPSA, LAA, NRF
- Verification on regional grants, and a number of minor charities

Others

- Key Financial systems maps
- Support to Equal Pay Compensation and Single Status project
- Support to Building Maintenance contract arrangements

- 3.11 Our follow up work has found a strong level of implementation of agreed audit recommendations. Of 20 follow up audits, only 2 (10%) identified unsatisfactory progress had been made in implementing agreed recommendations.
- 3.12 Internal Audit was undertaken on behalf of Kirklees Neighbourhood Housing (a wholly owned Council subsidiary) as agreed with their management, in addition to that for the Council concerning the income and expenditure relating to the Housing Revenue Account. KNH has satisfactory control arrangements. Audit work on behalf of the Council has also concluded that monitoring and reporting arrangements to ensure compliance with the management and partnership agreements have been established and are reasonably robust, in respect of KNH.
- 3.13 Work has also been performed in relation to Kirklees Active Leisure, partially under contract to that organisation, and partly as a part of client side monitoring. Our work found that KALs main financial systems were operating satisfactorily.

- 3.14 Substantial resources have been devoted to dealing with questions and issues raised by Service Managers and in dealing with advice/approval for authorisation of contracting matters, and to evaluation of, or negotiation with, suppliers in accordance with CPRs.
- 3.15 Accordingly, from our work during 2008/09 we conclude that the Council has an adequate and effective control environment.

4. **Resources, Benchmarking and Performance Measures of Internal Audit**

4.1 During 2008/09 the Internal Audit function cost approximately £730,000. According to benchmarking information from CIPFA our operations continued to be in the lowest quartile of costs (based on £m gross expenditure) compared with Metropolitan and Unitary Councils.

4.2 The main performance statistics for the year are;

	Target 0809	Actual0809	Actual 0708	0607
Proportion of Key Financial Systems / Process Audits Completed	90%	73%	80%	81%
Work completed within time allowed	80%	70%	59%	66%
Draft reports issued within 10 days	85%	90%	88%	87%

Some progress was made in delivering the targets. The extent of the commitment required to supporting the resolution of equal pay compensation claims involving senior members of staff impacted significantly upon the delivery of some of the planned key financial audits and the total pieces of work undertaken. The senior finance officer who carries out a large proportion of IT related audit work has also been working on implementing the new IT system at Building Services.

- 4.3 During the year questionnaires were issued to all clients. Whilst not all were returned, those which were provided a very positive response, which like last year almost all indicating client satisfaction. Customer satisfaction was 100% (the method of calculating this is a sub regional standard)
- 4.4 Internal Audit has a documented quality control system in place. This identifies over 30 criteria that each piece of work must meet. Eight pieces of work are subject to review each quarter. All of the work reviewed during 2008/9 passed the thresholds.
- 4.5 As an attempt to improve communication, we have simplified our quarterly reporting, to give greater concentration on those areas which have identified any weaknesses, or which are potentially of strategic concern to the Council.
- 4.6 The Audit Commission carried out a Review of Internal Audit as a part of their 2006/7 audit year. This evaluated performance against the CIPFA Code of

Practice. Their report concluded that Internal Audit is providing an “economic, efficient and effective function that is continuously improving”. An action plan was agreed and action has been taken in respect of each recommendation.

- 4.7 During 2008/9 the Statement of Strategy, Ethos and Terms of Reference for Internal Audit was formally adopted by the Corporate Governance & Audit Committee.

5 Effectiveness of the systems of Internal Audit

- 5.1 The Accounts & Audit Regulations (Amendments) (England) 2006 require authorities to conduct an annual review of the effectiveness of their system of internal audit, so as to ensure the opinion of the Head of Internal Audit on the internal control environment can be relied upon as a key source of evidence in the Annual Governance Statement.
- 5.2 Members can form their opinion from a number of routes and strands including their assessment of this and other reports (particularly the four quarterly reports) to the Corporate Governance & Audit Committee. They can also gain assurance provided in respect of 2008-09 based upon the following:
- risk based audit planning process
 - performance indicators
 - quality assurance
 - CIPFA Benchmarking
 - ongoing performance benchmarking with neighbouring authorities
 - client satisfaction
 - compliance with the CIPFA Code of Practice for Internal Audit
 - consultation with Heads of Service

See appendix 4.

6. Internal Audit in 2009/10

- 6.1 The Audit Plan (days and number of reports) is attached as Appendix 1. The plan is risk based taking account of the Strategic Audit Plan in which Members have asked that all activities of the Council are reviewed over a rolling five year period, combined with new and emerging risks as identified by the corporate risk management process and individual Heads of Service concerns and priorities. The schedule of Key systems, organisational and business controls is attached as Appendix 2. The performance targets for Internal Audit are Appendix 3.
- 6.2 Priorities for 2009/10 will include;
- a) Working with all Schools who have not yet achieved the Financial Management Standard for Schools.
 - b) Promoting fraud awareness amongst Members ,managers and all staff.
 - c) Ensuring that the financial system maps continue to be kept up to date by system owners, and using these to assess standards of control of the Council's financial processes.
 - d) Work contributing to the organisational objective of improving value for money.

- e) Assessing our risk associated with partnership working, including Local Public Service Agreements and Local Area Agreements, and working with key partners to address risk in areas of mutual concern.
- f) Driving achievement of the target performance.

7. **Conclusions**

- 7.1 This report has summarised the activities of Internal Audit during 2008/09. Detailed information has been provided to Corporate Governance & Audit Committee during the year.
- 7.2 There is sufficient evidence for the Director of Finance to demonstrate that the Council's system of internal audit is effective and that the opinion of the Head of Internal Audit on the internal control environment can be relied upon as a key source of evidence in the compilation of the Annual Governance Statement.
- 7.3 The proportion of audit work which resulted in an assessment of the routine system/process examined as "unsatisfactory" is 17%.
- 7.4 Our review of the financial governance controls and our overview of the business systems controls have not identified any significant issues whereby principal risks remained unaddressed (although there is scope for improvements in some areas, such as IT governance).
- 7.5 Overall, our opinion, from the work we have performed, is that there are no apparent significant weaknesses in the overall framework of the Council's business and financial systems, processes and its management of assets.
- 7.6 We conclude that overall the Council has an adequate and effective control environment.

8. **Annual Governance Statement**

- 8.1 Information generated by Internal Audit forms a key part of the Council's assessment of the quality of its organisational and business controls and the degree of assurance that can be placed upon their operational effectiveness. This information is used by the Director of Corporate Services in preparing the Council's Annual Governance Statement which forms part of the Statement of Accounts.

Contact Officer

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APPENDIX 1

ANNUAL AUDIT PLAN 2009/10

Audit Plan	Days	Planned Audits
<u>Children & Young People's Service;</u>		
Schools	320	60
Children; Education LEA & Other	335	33
Children; Care services	5	1
Contract Management & Support	25	2
<u>Adult & Community Services</u>		
Housing (HRA)	220	9
Strategic Housing (GF)	70	5
Safer, Stronger Communities	55	6
Adult Services	200	13
<u>Finance Services</u>		
Strategic Finance	170	10
Revenues & Benefits	130	10
<u>Regeneration Services</u>		
Culture & Leisure Services	145	14
Building Control & Planning	45	6
RDS	25	4
EDS	45	6
<u>Environmental, Transportation & Property Services</u>		
Environment & Transport Services	135	9
Highways	125	9
Building Services	75	6
Catering, Caretaking & Cleaning	25	3
Design & Property Services	60	3
<u>Corporate Services</u>		
Corporate HR Service	25	2
Office of Chief Executive	25	0
Legal	15	1
InTech	75	5
Performance & Communication	25	1
Policy & Governance	30	2
Central Resource Group	5	0
Corporate Risks & Governance	200*	7
Contracts	160*	
Total	2410	227

* Corporate risk and contracts audit work is included in the service totals
A copy of the full plan is available on request.

APPENDIX 2**INTERNAL AUDIT****KEY SYSTEMS AUDIT AREAS 2009/10****Financial Systems & Controls (as agreed with the Audit Commission)**

Payroll
Cash Income
Housing Rents
Other Rents
Debtors
Creditors
Payments for Social Care
School Payments
Working Capital Management
Council Tax
NDR
Benefits
Financial Ledger
Internal Recharging - Building Maintenance
Government Grants

Organisation & Business Controls

Corporate Governance
Procurement / Contract Management
Performance Management
EMAS
HR Operations
Risk Management
IT Controls
Asset Management & Security
Complaints Procedure
Partnerships Management
Emergency & Business Continuity Planning
Information Management & Security
Health & Safety
Project Management

APPENDIX 3

KIRKLEES COUNCIL STRATEGIC FINANCE SERVICE**INTERNAL AUDIT PERFORMANCE TARGETS 2009/10**

<u>Objectives</u>	<u>Performance Measures</u>
Achieve planned audits or near substitute each year, and full coverage over 5 years.	90% of planned priority audits achieved
Achieve each planned audit within budgeted time allowed	80 % of planned work achieved within initial time budget
Achieve high level of work quality and customer satisfaction	90% good or better responses to customer questionnaires
Delivery of completed audit work	85% of draft reports issued within 10 days of completion of site work

APPENDIX 4

INFORMATION TO ASSIST WITH DETERMINATION OF EFFECTIVENESS OF SYSTEMS OF INTERNAL AUDIT

The Accounts & Audit Regulations (Amendments) (England) 2006 also require authorities to conduct an annual review of the effectiveness of their system of internal audit.

- performance indicators)
- CIPFA Benchmarking) see 3.1, section 4
- client satisfaction)
- quality assurance (see 4.4)
- consultation with Heads of Service
- compliance with the CIPFA Code of Practice for Internal Audit
- ongoing comparative work with neighbouring authorities

Extract from Financial Services benchmarking report

Audit – - CIPFA Benchmarking 2008
- South/West Yorkshire Audit Group 2007/08

	Measure	Kirklees	Comparator Group – Unitary Authorities (U): Audit Group(AG)
1. Performance	1.1 CPA – UoR Internal Control assessment	3- Performing Well	2.7(U)
	1.2 Chargeable Days per Auditor	182	171(U)
	1.3 Audit days per £m gross turnover	2.8	3.2(U)
	1.4 Percentage of draft reports issued in 15 working days	94%	83%(AG)
	1.5 Percentage of audit plan completed on time	59%	74%(AG)
	1.6 Percentage of Recommendations agreed by management	99%	98%(AG)
	1.7 Percentage of original Audit Plan completed	71%	90%(AG)
	1.8 Client Feedback – percentage satisfaction	100%	97%(AG)
2. Cost	2.1 Cost per £m Gross Turnover	£737	£866(U) £1.157 (AG)
	2.2 Cost per productive	£264	£274(U)

	day		£270(AG)
	2.3 Staff Cost per FTE	£48,070	£47,400(U)
	2.5 Time Series – Change in costs per £m gross turnover 2001 - 2007	- 17%	- 21%(U)
Conclusion			
<p>Performance is above average CPA assessment of performing well. Local comparison shows performance generally around the average but better performance in completing reports in 15 days and worse performance in completing the Audit Plan.(In part the apparently poor comparative completion rate reflects the detailed way in which the Kirklees Audit Plan is prepared, and the practice of some authorities of revising their plan regularly, and comparing achievement with the last revised rather than original plan)</p> <p>Costs are relatively low. The cost per £m budget is 15% below the Unitary Comparator average and 36% below local comparators</p>			
Areas of Improvement			
<ul style="list-style-type: none"> • Improve percentage completion rate of the Audit Plan & Improve percentage of Audit Plan completed on time (although it is apparent that some authorities do not plan to the same level of detail , and or revise their plans during the year, so enabling a higher claimed completion rate) 			