

REPORT TO: SCRUTINY COMMITTEE - 13 JUNE 2012

REPORT ON: 2011/12 INTERNAL AUDIT ANNUAL REPORT

REPORT BY: CHIEF INTERNAL AUDITOR

REPORT NO: 235-2012

1.0 PURPOSE OF REPORT

To submit to Members of the Scrutiny Committee the Internal Audit Annual Report for the 2011/12 financial year which summarises the activities of the Council's Internal Audit Service during this period and provides an opinion on the overall adequacy and effectiveness of the Council's control environment.

2.0 RECOMMENDATIONS

Members of the Committee are asked to note the information contained within this report.

3.0 FINANCIAL IMPLICATIONS

None

4.0 MAIN TEXT

4.1 The remit of the Scrutiny Committee, as laid down in Report No 370-2010, includes consideration of the strategy, plan and performance of the Council's Internal Audit Service. This Committee should also consider internal audit reports and seek assurance that appropriate action has been taken, monitor the implementation of internal audit recommendations agreed with management and receive the annual report of the Chief Internal Auditor. Attached at Appendix A is the Internal Audit Annual Report for the 2011/12 financial year and at Appendix B is a summary of the Internal Audit Reports issued during the same period.

4.2 On an annual basis the Chief Internal Auditor is also required to prepare a statement which provides an opinion on the adequacy and effectiveness of the control environment of the Council. This statement forms part of the assurance gathering process which feeds into the Annual Governance Statement included within the Council's Statement of Accounts. A copy of the Chief Internal Auditor's statement for the 2011/12 financial year is attached at Appendix C.

5.0 POLICY IMPLICATIONS

This report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality Impact Assessment and Risk Management. There are no major issues.

6.0 CONSULTATIONS

The Chief Executive, Director of Corporate Services and Head of Democratic and Legal Services have been consulted on the content of this report.

7.0 BACKGROUND PAPERS

None

Sallie Dailly, Chief Internal Auditor

DATE: 31 May 2012

2011/12 INTERNAL AUDIT ANNUAL REPORT

1. PURPOSE OF REPORT

- To summarise the key areas of activity undertaken by the Council's Internal Audit Service and highlight any matters of significance that have arisen as a result of the audit process during the 2011/12 financial year.
- To provide an independent opinion on the adequacy and effectiveness of the systems of internal control based on the work undertaken during the year.

2. INTERNAL CONTROL FRAMEWORK

- Each local authority is accountable for the way in which it discharges its stewardship of public funds. Stewardship is a function of management and, therefore, a responsibility placed upon elected members and officers of the authority.
- Such responsibility is discharged by the establishment of sound arrangements and systems for the planning, appraisal, authorisation and control over the use of resources, and by the preparation, maintenance and reporting of accurate and informative accounts.
- There are a number of aspects of corporate governance which are essential prerequisites to the traditional public sector values of impartiality, openness and transparency and the highest standards of probity and propriety appropriate to the handling of public funds. These include a sound control environment, security of key financial systems and an adequate and effective internal audit function.

3. ROLE OF INTERNAL AUDIT

- Internal audit is an independent appraisal and review function which has been set up within the Council as a service to the Scrutiny Committee, Chief Executive, Director of Corporate Services and all levels of management. The remit of the Internal Audit Service is to provide an independent and objective opinion on the control environment by evaluating its effectiveness in achieving the Council's objectives. The Service objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources throughout the Council's activities.
- The existence of internal audit does not diminish the responsibility of management to establish and maintain appropriate risk management processes, control systems, accounting records and governance arrangements and management should not depend on internal audit as a substitute for effective controls.
- The role of internal audit is to understand the key risks faced by the Council and examine and evaluate the adequacy and effectiveness of risk management processes, control systems, accounting records and governance arrangements as operated by the Council.
- Internal Audit has unrestricted access to all activities undertaken within the organisation in order to be able to effectively discharge its remit. The primary thrust of internal audit work is to review, appraise and report on a wide range of areas. The types of review undertaken can be assigned to various themes namely governance, ICT, systems, procurement/contract and financial. In addition, the service may also provide advice on systems, control and risk and specific investigations.
- The Internal Audit Service is independent of the activities which it audits. This is essential to ensure that the service provides unbiased judgements and impartial advice to management.

4. AUDIT PLANNING

- A vital element in the effective management of internal audit is planning audit work to ensure that objectives are met, priorities are established, resources are targeted and used effectively, best value is achieved and cognisance is taken of the risk associated within each area.
- The Internal Audit Plan is compiled on an annual basis and provides a summary of the areas where it is planned that work will be carried out during the forthcoming year. The Internal Audit Plan for the 2011/12 financial year was submitted to the Scrutiny Committee in June 2011

(Report No. 322-2011). In line with normal practice the Plan was prepared on the best information available at that time.

- The performance of internal audit is also reviewed by the Council's External Auditor on an annual basis. This enables the external auditor to utilise work carried out by internal audit to inform the year end accounts process where applicable and allows both parties to plan their reviews without duplication of effort and unnecessary disruption to services. During the 2011/12 financial year the Council's External Auditor changed from Audit Scotland to KPMG.

5. AUDIT REPORTS

- Each audit assignment results in an internal audit report which includes an executive summary and also details the audit findings, recommendations and management responses, where appropriate. The audit report essentially provides management with an action plan which assigns responsibility and details the timetable for the implementation of audit recommendations.
- Within all audit reports an opinion is given on the importance of each audit finding namely critical, significant or routine. On the basis of this, an overall audit opinion on the level of assurance assigned to the area reviewed is given in the report's executive summary. Broadly there are four levels of assurance namely full, reduced, limited and no assurance.
- The findings and recommendations arising from the audit assignments reported upon in 2011/12 have been discussed with appropriate officers of the Council and agreed action plans have been put in place to address areas for improvement. The executive summary of all reports finalised have also been submitted to the Scrutiny Committee for consideration.
- Internal Audit also undertakes follow-up work and progress reviews to confirm that management has discharged its responsibility for implementing audit recommendations within the agreed timescale. Such work is also formally reported upon to the Scrutiny Committee and the relevant officers of the Council.

6. KEY EVENTS DURING 2011/12

- The planning and delivery of the specific projects included within the 2011/12 Internal Audit Plan continued to be challenging due to the pace of change within the Council. This included the physical relocation of staff to the Council's new flagship headquarters, the reduction in the number of Council Departments and the associated realignment of services. However the ongoing benefits arising from the increased consultation with key stakeholders which was used to develop the 2011/12 Internal Audit Plan became evident during the course of the year particularly in the scoping and delivery of specific audit assignments.
- It is recognised that during this period of change it is essential to continue to effectively capture pertinent information which will inform the audit process. This in turn will contribute to ensuring that internal audit continues to provide an effective service. Therefore in compiling the 2012/13 Internal Audit Plan key stakeholders have once again been consulted to ensure that significant concerns of managers and areas of risk where reviews would be beneficial have been captured. This consultation exercise was initiated at the Council's Strategic Management Team in late January 2012.

7. PLAN ACHIEVEMENT

- For the 2011/12 financial year the actual number of productive days for audit work was 870 which represented a shortfall of 10% on the budgeted productive days for audit reviews included within the plan. This was due to the level of staff absence being significantly greater than had been budgeted for at the time the 2011/12 Internal Audit Plan was drafted. In terms of the overall productive days available approximately 82% were spent on direct audit activities and 18% were spent on support activities such as management, audit planning, staff training and development and the relocation of staff to Dundee House. This was broadly in line with the previous financial year.

- The 2011/12 Internal Audit Plan included 33 areas, both at a corporate and departmental level, to be reviewed. It also included allocations of audit days for follow-up reviews, progress reviews, finalisation of audit assignments which commenced in 2010/11, provision of advice to clients on systems, control and risk and specific investigations.
- As previously noted there was a shortfall in the actual productive days available during 2011/12. Despite this, work on the majority of the planned areas for corporate and departmental reviews included within the plan commenced in 2011/12. The key area of slippage was in relation to information technology where a number of reviews were deferred due to the significant demands placed on the client department who were responsible for setting up the IT infrastructure in Dundee House.

8. OVERALL ASSESSMENT OF CONTROLS

- Internal Audit activity for the Council during 2011/12 covered a wide spectrum of areas including asbestos, attendance management, car parking, control self assessment, contracting and payments, creditors standing data, debit and credit card refunds, debtors and debt management, electoral registration, fuel management, payroll, procurement, risk management arrangements, usb memory devices, winter maintenance, statutory performance indicators, year end stocks, grant claims and follow-up reviews. The wide range of subject matter covered reflects the changing nature of Internal Audit and the move away from financial audits to audits which review Council policies and areas of governance.
- The 2011/12 reviews of corporate and departmental systems identified that many of the expected controls are in place and operating satisfactorily in the areas examined. However the audit work also identified scope for improvement in systems which have either weaknesses in or lack controls.
- During the 2011/12 financial year, 36 internal audit reports were issued. Reports have generally been well received by clients with management agreeing to implement 100% of the recommendations made. Details of these reports issued and key information pertaining to these are attached at Appendix B.
- Analysis of the overall audit opinion for the reports issued highlighted that 14% of the areas reported upon were considered to be well controlled (full assurance), 50% were adequately controlled (reduced assurance) and 36% were requiring improvement (limited assurance). This shows a slight deterioration on the 2010/11 position. However once again none of the areas reviewed and reported upon were deemed to be so poorly controlled that no assurance could be placed upon the systems and controls being operated. As indicated in the 2010/11 Annual Report continuing to maintain a position of and ensuring the effective implementation of sound controls is becoming increasingly challenging for officers as the pace of change within the Council continues. A watching brief will therefore be kept on this area.
- Internal audit reports included a range of recommendations for improvement in the areas examined and action plans have been developed in consultation with management which, as they are implemented, should improve the overall control environment.
- The Code of Practice on Local Authority Accounting in the UK requires the Chief Internal Auditor to provide an independent opinion on the adequacy and effectiveness of the Council's system of internal financial control. However the Council has voluntarily adopted the preparation of an Annual Governance Statement for inclusion in its Statement of Accounts. Attached at Appendix C is the Chief Internal Auditor's annual opinion on the Council's control environment. The Chief Internal Auditor takes due recognition of the audit work carried out by the Internal Audit Service and other pertinent information. On the basis of the areas used to inform this process for the year to 31 March 2012 the overall audit opinion reached was that reasonable assurance could be placed upon the overall adequacy and effectiveness of the Council's control environment.

Summary of Internal Audit Reports Issued during the 2011/12 Financial Year

Report No.	Area Reviewed	Level of Assurance	Recommendations			
			Total No.	Importance		
				Critical	Significant	Routine
2010/10	Management of Portable Assets (Corporate)	R	1	-	1	-
2010/13	Greenmarket Car Park	L	3	-	2	1
2010/18	Business Credit Cards (Education)	R	1	-	1	-
2010/24	Starters and Leavers (Leisure & Communities)	R	1	-	-	1
2010/27	Corporate Governance	L	3	-	3	-
2010/31	Attendance Management (Secondary Schools)	R	1	-	-	1
2010/32	Management of School Transport	R	4	-	2	2
2010/33	Contracting and Payments (Social Work)	R	2	-	2	-
2010/34	Electoral Registration	R	1	-	-	1
2010/35	Insurance Arrangements for School Transport	L	1	-	1	-
2011/01	User Access to Payroll	R	2	-	1	1
2011/02	Client Services (Social Work)	L	1	-	1	-
2011/03	2010/11 Grant Claim : Local Air Quality Management	F	-	-	-	-
2011/04	Debit and Credit Card Refunds - Brown Street Kennels	R	1	-	-	1
2011/05	Payment of Pensions for Former Employees of ex List D Schools	F	-	-	-	-
2011/06	Residential Parking Permits	L	3	-	3	-
2011/07	USB Memory Devices	L	1	-	1	-
2011/09	Fuel Management - Marchbanks	L	3	1	1	1
2011/10	Debtors and Debt Management - Sundry Debtors	L	6	-	3	3
2011/11	Procurement	R	1	-	1	-
2011/12	User Access to IT Systems	R	1	-	1	-
2011/13	Performance Indicator - Current Year Income from Council Tax	F	-	-	-	-
2011/14	Performance Indicators	R	2	-	1	1
2011/15	Risk Management Arrangements	L	6	-	5	1
2011/16	Control Self Assessment for Social Work Establishments	R	1	-	-	1
2011/17	Control Self Assessment for Education Establishments	R	1	-	-	1
2011/18	Arrangements for the Management of Asbestos	L	5	-	5	-
2011/19	Amendment of Creditors' Standing Data	R	2	-	1	1
2011/20	Procurement and Management of Materials	L	2	-	1	1
2011/21	Periodicals, Publications and Subscriptions	R	2	-	-	2
2011/23	2010/11 Grant Claim : Cycling, Walking and Safer Streets Projects	F	-	-	-	-
2011/24	Winter Maintenance - Communication	L	1	-	1	-
2011/26	Debit and Credit Card Refunds - Registrars	R	2	-	-	2
2011/27	Debit and Credit Card Refunds - Ancrum Outdoor Education Centre	L	1	-	-	1
2011/28	Carbon Reduction Commitment Energy Efficiency Scheme	R	2	-	-	2
2011/41	Debit and Credit Card Refunds - Marchbanks	F	-	-	-	-

KEY : Level of Assurance

Full

Reduced

Limited

No

To the Members of Dundee City Council, Chief Executive and Director of Corporate Services

As Chief Internal Auditor of Dundee City Council, I am pleased to present my annual opinion for the year ended 31 March 2012. It should be noted that the statement does not include assurances on group activities.

Respective Responsibilities of Management and Internal Audit in Relation to the Control Environment

It is the responsibility of the Council's officers to determine, establish and maintain sound systems of internal control and to ensure that the organisation's resources are properly applied on the activities intended. This includes responsibility for the prevention and detection of fraud. Management is also charged with monitoring the continuing effectiveness of the internal control environment and taking action as appropriate. It is the responsibility of the Chief Internal Auditor to provide an annual assessment of the overall robustness of the control environment within the Council.

Control Environment

This comprises the systems of governance, risk management and internal control. The key elements include:

- Establishing and monitoring the achievement of the organisation's objectives.
- Facilitation of policy and decision-making ensuring compliance with established policies, procedures, laws and regulations.
- Ensuring the economical, effective and efficient use of resources and securing continuous improvement.
- Financial management of the organisation.
- Performance management of the organisation.

A sound control environment reduces, but cannot eliminate, the possibility of poor judgement in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances. It therefore provides reasonable but not absolute assurance that control weaknesses or irregularities do not exist or that there is no risk of material errors, losses, fraud or breaches of law or regulations. Accordingly, the Council is continually seeking to improve the effectiveness of its control environment.

The Focus of Internal Audit Work

Internal Audit is an assurance function that provides an independent and objective opinion to the organisation on the control environment by evaluating its effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources. The Council's Internal Audit Service operates in accordance with the Code of Practice for Internal Audit in Local Government in the United Kingdom, published by the Chartered Institute of Public Finance and Accountancy (C.I.P.F.A.), and which represents best practice.

The Chief Internal Auditor prepares an annual internal audit plan which outlines the work to be undertaken. This takes cognisance of the risks associated with various activities undertaken by the Council, emerging issues and requests received from departments for specific reviews. The plan needs to be flexible to be able to reflect the changing risks and priorities of the organisation. The plan, any material changes to the plan and any significant matters that may impact upon the delivery of the plan are reported to the Scrutiny Committee.

The Internal Audit Service formally reports upon the areas subject to review. Such reports, which identify system weaknesses and/or non-compliance with expected controls, are issued for the attention of departmental managers and include appropriate recommendations and agreed action plans. It is management's responsibility to ensure that due consideration is given to internal audit reports. This includes management taking remedial action where appropriate or accepting that there may be a level of risk exposure if the weaknesses identified are not addressed for operational reasons. Internal Audit has a responsibility to ensure that agreed action plans have been implemented. Matters arising from internal audit work are also reported to the Council's Scrutiny Committee, the Chief Executive and the Council's External Auditor.

Summary of 2011/12 Internal Audit Activity

During 2011/12 financial year a total of 36 internal audit reports were issued. These covered a wide spectrum of areas including asbestos, attendance management, car parking, control self assessment, contracting and payments, creditors standing data, debit and credit card refunds, debtors and debt management, electoral registration, fuel management, payroll, procurement, risk management arrangements, usb memory devices, winter maintenance, statutory performance indicators, year end stocks, grant claims and follow-up reviews. The Internal Audit Service also provided advice on the control environment as required.

The 2011/12 audit of corporate and departmental systems has identified that many of the expected controls are in place and operating satisfactorily. The audit work has, however, also identified scope for improvement in some systems which either have weaknesses in or lack controls. The Internal Audit Service has put forward a range of recommendations in the areas examined and action plans have been developed in consultation with management which, as they are implemented, should result in continued improvement in the control environment.

Limitation of Scope

In the financial year under review there was no limitation of scope placed upon the work undertaken by the Internal Audit Service.

Basis of Opinion

My evaluation of the control environment is informed by a number of sources which include the following:

- The audit work undertaken by the Internal Audit Service during the year to 31 March 2012.
- The assessment of risk completed during the preparation of the audit plan.
- Reports issued by the Council's External Auditor and also reports by other review agencies.
- Knowledge of the Council's governance, risk management and performance monitoring arrangements.
- Formal assurances received from the Council's Directors/Heads of Service in the form of a Self Assessment Checklist.

Opinion

It is my opinion, based on the above, that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's control environment for the year to 31 March 2012.

Sallie M. Dailly

**Chief Internal Auditor
Dundee City Council**

DATE

04 June 2012