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**Meeting:**           **Audit Committee**  
**Date:**             **24 June 2013**  
**Subject:**         **Internal Audit Annual Audit Opinion**  
**Report of:**       **Chief Finance Officer**  
**Summary:**        This is the annual report of the Head of Internal Audit and Risk to those charged with governance on the overall adequacy and effectiveness of Central Bedfordshire Council's financial and other management internal controls.

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Advising Officer:           Chief Finance Officer  
Contact Officer:           Kathy Riches , Head of Internal Audit and Risk  
Public/Exempt:            Public  
Wards Affected:          All  
Function of:                Audit Committee

## **CORPORATE IMPLICATIONS**

### **Council Priorities:**

The activities of Internal Audit are crucial to the governance arrangements of the organisation and as such are supporting all of the priorities of the Council.

### **Financial:**

1.       None directly from this report. However, sound systems assist in preventing loss of resources (by other wastage or fraud), thereby improving effectiveness and efficiency.

### **Legal:**

2.       None directly from this report.

### **Risk Management:**

3.       No risk management implications come directly from this report but the Audit Plan was produced using a risk based approach, following the completion of a detailed Audit Needs Assessment which took into account strategic and service area risks.

### **Staffing (including Trades Unions):**

4.       None directly from this report.

**Equalities/Human Rights:**

5. None directly from this report.

**Public Health**

6. None directly from this report.

**Community Safety:**

7. None directly from this report.

**Sustainability:**

8. None directly from this report.

**Procurement:**

9. None directly from this report.

**RECOMMENDATION:**

**The Committee is asked to consider and comment on the contents of the report.**

**Background**

10. The Accounts and Audit Regulations 2011 require the Council to maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with proper internal audit practices. The applicable standard for 2012/13 was the CIPFA Code of Practice for Internal Audit in Local Government 2006 (the Code). In accordance with the Code, the Head of Internal Audit is required to provide a written report to those charged with governance, timed to support the Annual Governance Statement, which should include an opinion on the overall adequacy and effectiveness of the Council's control environment.
- 11 This report:
- Presents an opinion on the overall adequacy and effectiveness of Central Bedfordshire's internal control environment, along with any qualifications to that opinion
  - Summarises audit work undertaken from which that opinion is derived
  - Highlights significant issues identified as part of Internal Audit's work, including those that are particularly relevant to the Annual Governance Statement
  - Compares the Internal Audit work actually undertaken with the work that was planned and summarises the performance of the internal audit function against its performance measures and criteria.

## **Responsibilities**

12. It is a management responsibility to develop and maintain the internal control framework and to ensure compliance. It is the responsibility of Internal Audit to form an independent opinion on the adequacy of the system of internal control.

## **Internal Control Environment**

13. The Code defines the control environment as comprising the Council's systems of governance, risk management and internal control.
14. In order to form an opinion on the overall adequacy and effectiveness of the control environment, the internal audit activity is planned to provide coverage of financial controls through review of the key financial systems, and internal controls through a range of operating activity both within directorates and cross cutting, using a risk based approach. The work undertaken by Internal Audit helps inform the Annual Governance Statement.

## **The Audit Methodology**

15. During 2012/13 Internal Audit complied with the CIPFA Code of Practice. There are documented Terms of Reference, as set out in the Internal Audit Charter, that specify the objectives and scope of Internal Audit. The Head of Internal Audit and Risk has undertaken a self assessment of compliance with the Code. In accordance with the requirements of the Accounts and Audit Regulations 2011 the Chief Finance Officer has carried out a review of the effectiveness of the System of Internal Audit. The scope of the review covered compliance with the CIPFA Code of Practice for Internal Audit 2006, and reporting on performance and outcomes to the Audit Committee.
16. The Internal Audit Strategy and Plan for 2012/13 was approved by the Audit Committee in April 2012.
17. The Internal Audit Plan identified the individual audit assignments. The activity was undertaken using a systematic risk based approach. The objectives for each activity were determined and risks in the processes that supported that activity were identified and set down in terms of reference that outlined the objectives and scope for each audit. The work was planned and performed so as to obtain all the information and explanations necessary to provide sufficient evidence in forming an overall opinion on the adequacy of the internal control framework.
18. Internal Audit reports provide an overall conclusion on the control environment for each system reviewed. A summary of the conclusions for each audit is attached as Appendix A to this report. The definitions of each conclusion are attached as Appendix B.

19. To provide quality assurance over the audit output, audit assignments are allocated to staff according to their skills and experience. Each auditor has a designated Audit Manager to perform quality reviews at four stages of the audit assignment: the audit brief (terms of reference), file review, draft report and final report stages. In addition, the Head of Internal Audit and Risk reviews all reports.
20. In addition to this annual report, the Audit Committee receive regular progress reports throughout the year.

### **The Internal Audit Team**

21. During 2012/13 the Internal Audit Service was delivered by a team of suitably qualified auditors, supported by external contractors. Each member of the team undertakes a regular Performance Development Review (PDR) and participates in Continuing Professional Development (CPD) as appropriate.

### **Head of Internal Audit's Opinion on the System of Internal Control**

22. The CIPFA Code of Practice on Internal Audit requires the Head of Internal Audit to provide an overall opinion on the adequacy and effectiveness of the Authority's internal control environment.
23. The Internal Audit work undertaken during the year has enabled Internal Audit to provide an objective assessment of whether systems and controls are operating effectively. In giving an audit opinion, however, it should be noted that assurance can never be absolute. However, the scope of the activity undertaken is sufficient for reasonable assurance to be placed on the work.
24. Ernst and Young, as the Council's external auditors, have reviewed the work undertaken by Internal Audit on the managed audits and have been able to place reliance on the work, and have been in agreement with the audit opinions given.
25. A summary of the work undertaken during the year, forming the basis of the audit opinion on the control environment, is shown at Appendix A of this report.
26. The opinion on the Council's System of Internal Control is that overall it continues to be adequate. In general the key controls in place are adequate and effective such that reasonable assurance can be placed on the operation of the Council's functions.

27. This conclusion is based on the following:
- A Code of Financial Governance is in place, and is incorporated within the Constitution.
  - Financial Procedures support the Code of Financial Governance and these have been refreshed and updated during the year.
  - A Financial Scheme of Management is in place.
  - Procedures and processes have been documented in a number of key areas.
  - Adequate controls were found to be in place in a number of areas.
  - Progress has been made in addressing many of the high risk Internal Audit recommendations made.
  - There has been a stable senior finance management structure in place during the year,
  - Assurances on key strategic risks have been mapped during the year.
  - Internal audit work on the fundamental systems has generally shown a positive direction of travel, and
  - Full assurance opinions were given to both the Council Tax and National Non Domestic Rates (NNDR) managed audit reviews.
28. It should be noted that most audits undertaken have resulted in reports identifying areas for improvement which have been well received by managers, and actions agreed to address weaknesses in control. The implementation of these actions is tracked by Internal Audit and the progress against the implementation of high recommendations is regularly reported to the Audit Committee.
29. In arriving at the opinion the following has been taken into account:
- The results of the audits undertaken as part of the 2012/13 plan
  - The results of follow up action in respect of previous audits
  - Whether or not any limitations have been placed on the scope of Internal Audit – of which there have been none.
30. The following key concerns were identified and these have been reflected in the Annual Governance Statement:
- Some key controls are not operating effectively in the payroll systems resulting in a limited assurance opinion. Controls in this area need to be strengthened. Some improvements on last year have been noted, however, further action is required to fully address the control weaknesses identified. The payroll service was brought back in house from 1<sup>st</sup> April 2012. This resulted in a review of processes. A SAP Optimisation project is in progress, and this will be further developed during 2013/14.
  - Significant progress was made during 2012/13 to develop a comprehensive IT Disaster Recovery Plan. Further work is currently in progress. The Audit Committee has received regular updates on this during the year.

## **Delivery of the 2012/13 Internal Audit Plan**

31. The operation of the key financial systems is a key part of the internal control environment. The table at Appendix A sets out the outcome of the reviews of these systems, and indicates whether the opinions are final or provisional, as some of the work is still ongoing. The opinions given during 2011/12 are included for comparison. The appendix also summarises other reviews undertaken during the year.
32. The reviews of the key financial systems (Managed Audits) help inform the Annual Governance Statement. From the review of 11 key systems for which an opinion has been determined, 2 have given full assurance, 8 were “adequate”, 1 was “limited” and none were “unsatisfactory”. There has been an improvement in the opinion awarded to both the National Non Domestic Rates (NNDR) and Council Tax systems. It should be noted that the opinions given reflect the controls in place across the whole year. Although several of the Phase 2 reports have still to be finalised, no new key issues of concern have been identified.
33. Audit work is not just limited to implementing the audit plan. Internal Audit is involved in other areas advising on systems development and using their skills to provide other general advice to service areas. Internal Audit has participated in a number of projects, providing advice on controls required. These projects include the Children’s Case Management System (CCMS), the Local Welfare Provision Board, SAP Optimisation, SWIFT Disaggregation and the Payment Card Industry Data Security Standard Scheme (PCIDSS). In addition, individual grant claims have been audited, where required.

## **National Fraud Initiative (NFI)**

34. During 2012/13, we continued to complete work on the National Fraud Initiative (NFI). This involves supplying data to the Audit Commission for matching purposes. Work on investigating the resulting positive matches is ongoing. Work includes matches on pension payments to registered deaths, matching payrolls between authorities, and other matches including UK visas, blue badges, private residential care and Housing Benefits.
35. The Internal Audit team has also assisted other authorities undertake their NFI enquiries by providing information to support their investigations.

## **Anti Fraud Work and Special Investigations**

36. Internal Audit finalised work on one investigation during the year. The outcome of this was reported to the January Audit Committee.
37. Internal Audit continues to operate the Fraud Hotline. None of the calls received have resulted in an audit investigation. In all cases, the calls received have related either to fraud in other organisations or allegations of Housing Benefit Fraud and the information has been forwarded appropriately.

## **Schools**

38. The rolling programme of school audits has continued during 2012/13. During the year final reports were issued to 16 schools. The opinions given for the finalised reviews are set out at Appendix A.

## **Performance Management**

39. The Internal Audit Charter approved by the Audit Committee in April 2012 requires Internal Audit to report its progress on some Key Performance Indicators (KPI). Overall, performance has been positive and where targets have not been met, action will be taken aimed at improving performance. The table below summarises the results for the year, and also includes the previous year's indicators, for comparative purposes.
40. The indicators include both CBC audit activities and school activity.

41. **Activities for 1 April 2012 – 31 March 2013**

KPI	Definition	2012/13		2011/12	
		How we performed	Our target	How we performed	Our target
KPI01	Percentage of total audit days completed.	100%	80%	94%	80%
KPI02	Percentage of the number of planned reviews completed to final report stage.	80%	80%	80%	80%
KPI03	Percentage of audit reviews completed within the planned time budget.	60%	80%	59%	80%
KPI04	Time taken to draft reports: Percentage of reviews where the first final draft report was returned by auditee within 10 available working days of receipt of the report from the Auditor.	76%	80%	58%	80%
KPI05	Time taken to issue a final report: Percentage of reviews where the final report was issued within 10 available working days of receipt of the response agreeing to the formal report.	85%	80%	100%	80%
KPI06	Overall customer satisfaction.	93%	80%	83%	80%



#### 42. **Analysis of indicators:**

KPI01 – During the year we delivered a total of 1,297 productive audit days against a total of 1,300 planned days for the year. This exceeds our target for the period.

KPI02 – This KPI measures final reports issued as at 31 March 2013. 80% of the planned reviews had been completed to final report stage, which was in line with the target. However, this excludes work on the second phase of the managed audits which was in progress as at 31<sup>st</sup> March. Performance was consistent with the previous year.

KPI03 – Only 60% of planned reviews have been completed within the planned time budgets. As agreed at the April Audit Committee this performance measure has been reviewed. Following discussions with the Chief Finance Officer, for 2013/14, the target will measure the percentage of reviews that have been completed within a one day tolerance of the planned time budget, and a target of 75% has been set.

KPI04 - This indicator measures the time taken for Internal Audit to receive a response from the auditee to the draft report. During 2012/13, 76% of draft reports were responded to within the target set. This represents a significant improvement over the previous year. Internal Audit will continue to work with departments to encourage a prompt response.

KPI05 - This indicator measures the time taken by Internal Audit to issue the final report upon receipt of an agreed response from the auditee. The reduction in performance compared to last year is due to sickness absence within the Internal Audit Team.

KPI06 – A total of 26 surveys have been sent out. 19 responses have been received to date. The responses received have been positive, and demonstrate an improvement over the previous year.

### **Review of the Effectiveness of Internal Audit and the Effectiveness of the Systems of Internal Control**

#### **Background (Accounts and Audit Regulations 2011)**

43. All councils are required to publish an Annual Governance Statement (AGS) to accompany their Statement of Accounts, in accordance with the 2011 Accounts and Audit Regulations. Assessments of the Effectiveness of Internal Audit and the Effectiveness of Systems of Internal Control are two key aspects of the AGS. Central Bedfordshire Council has reviewed both systems for 2012/13 and the findings are incorporated into the Annual Audit opinion and subsequently into the AGS.

#### **Review of the Effectiveness of Internal Audit.**

44. As referred to in paragraph 15 above, a review of the Effectiveness of Internal Audit was undertaken by the Chief Finance Officer.

## **Review of the Effectiveness of the Systems of Internal Control**

45. The Council's review of the effectiveness of the system of internal control is informed by:
- Directorate assurance based on management information, performance information, officer assurance statements and Scrutiny reports
  - the work undertaken by Internal Audit during the year
  - the work undertaken by the external auditor reported in their annual audit and inspection letter
  - other work undertaken by independent inspection bodies.
46. The Head of Internal Audit and Risk has supported the Head of Legal Services (Monitoring Officer) to collect evidence required for the production of the AGS.
47. Directors have been requested to sign statements on the Effectiveness of Internal Control for 2012/13, confirming that during the year they were:
- Ensuring that there are arrangements in place for establishing Directorate objectives and compliance to corporate priorities;
  - Ensuring compliance to the Council's governance arrangements (Constitution, Ethical Framework, and Policies & Regulations);
  - Ensuring arrangements for sound budgetary controls;
  - Effectively monitoring and managing performance;
  - Reporting to the appropriate Member Committees;
  - Responding promptly to internal & external audits & inspections;
  - Continuously managing business risks and service continuity arrangements.
48. The work undertaken by Internal Audit on the systems of internal control disclosed that generally they were effective during 2012/13. However, some areas of concern were identified and these are summarised in paragraph 30 above, and are reflected in the Annual Governance Statement.

## **Conclusion and Next Steps**

49. The work undertaken by Internal Audit has enabled the team to advise management of some of the control weaknesses identified at an early stage, and make recommendations designed to enhance and strengthen controls and mitigate risks.
50. The internal control environment operated adequately during 2012/13, although some areas of concern identified in the AGS must be addressed promptly.

**Appendices:**

Appendix A – Summary of Internal Audit Activity 2012/13

Appendix B – Definition of Internal Audit Opinions

**Background Papers:**

None.

**Location of papers:**

N/A