

**NORTH LINCOLNSHIRE COUNCIL**

**AUDIT COMMITTEE**

**INTERNAL AUDIT - ANNUAL REPORT 2008/2009**

**1. OBJECT AND KEY POINTS IN THIS REPORT**

- 1.1 The object of this report is to advise Members of Internal Audit's work during 2008/09 and to provide an audit opinion on the adequacy of the council's control environment. This provides the Audit Committee with an important source of assurance to fulfil their role.
- 1.2 The Internal Audit Annual report complies with the CIPFA Code of Practice for Internal Audit in Local Government in the UK.

**2. BACKGROUND INFORMATION**

- 2.1 As part of the requirements of the CIPFA Code of Practice 2006, Internal Audit must produce an annual report to those charged with governance summarising their work for the year. This report gives a brief description of the role of Internal Audit, the control environment within which Internal Audit operates, and also provides a summary of work carried out during the year to 31 March 2009.
- 2.2 The requirement for Internal Audit is supported by statute in the Accounts and Audit Regulations 1996 (amended 2006) and the Local Government Act 1972. The Accounts and Audit Regulations state that a "relevant body shall maintain an adequate and effective system of internal audit of their accounting records and control systems." Each year the section provides an independent appraisal of internal control as a contribution to the proper economic, efficient and effective use of resources.
- 2.3 All audit work is risk assessed to ensure it is properly prioritised and targets areas of highest risk. The work of Internal Audit is to appraise and review:
- The controls in place to manage the council's principal risks
  - The adequacy of the council's corporate governance arrangements

- The effectiveness of risk management, improvement planning and performance management arrangements
  - The completeness, reliability and integrity of information, both financial and operational
  - The systems established to ensure compliance with policies, plans and procedures, laws and regulations
  - The means of safeguarding assets
  - Anti fraud and corruption measures
  - The economy, efficiency and effectiveness with which resources are employed.
- 2.4 The level of audit coverage during the year is considered sufficient to be able to offer an opinion on the overall adequacy and effectiveness of the organisation's control environment. Notwithstanding that some of the planned reports for the year have yet to be finalised, the fieldwork for the outstanding reports has been completed, and there is nothing within the reports that would cause the overall opinion to change.
- 2.5 Based on our knowledge of the council's systems and procedures, the extent of work undertaken by Internal Audit, and as a result of the responses to audit recommendations, the overall assessment is that Internal Audit can provide assurance that the council has adequate control and governance arrangements in place. It must however be acknowledged that this statement is given to provide reasonable and not absolute assurance of the effectiveness of the system of control.
- 2.6 In reaching our opinion the following factors were taken into particular consideration:-

### **Risk Management**

We can give assurance that the system for managing risk within the council is sound. The risk management framework has developed over several years for example: the risk management strategy is regularly reviewed; risk registers are maintained and reviewed; training is in place for relevant staff and members; key business risks are being monitored and managed and reported to the Audit Committee. Although there are examples of good practice, arrangements could be improved through better compliance by some services with risk management processes such as review and updating of operational risk registers; further consideration of risk issues through Quarterly Performance Reviews and more general consideration of risk within decision making.

### **Corporate Governance**

The current Corporate Governance audit has not yet been fully completed however based on the previous audit and subsequent follow up work, corporate governance arrangements are generally adequate

and the council has procedures and policies in place to demonstrate good corporate governance. The previous audit, dated September 2008, concluded that no aspects of the 57 requirements are entirely unmet that make up the framework to achieve the core principles of the best practice framework.

Progress has been made on the 2008 report's recommendations:

- Improvements to corporate governance arrangements in partnerships continue to be made through the application of the governance framework and are reinforced in the refresh of the Strategic Plan. Further work is planned during 2009/2010 to evaluate the impact of the application of the governance protocol and toolkit (which includes risk management) on partnerships.
- The complaints procedure has been reviewed and re launched
- The Anti Fraud Theft and Corruption Strategy has been revised to meet best practice counter fraud arrangements as defined by CIPFA.
- Councillors have been provided with additional support in their community and strategic leadership roles
- The work of scrutiny in performance work is being developed.

The outcome of the 2008/2009 review will be reported to the Audit Committee on completion. The council's Annual Governance Statement (AGS) is reported elsewhere on this agenda. The AGS supports the findings of the audit review that governance arrangements are generally good. A number of opportunities for improvement have been identified along with issues highlighted as a result of recent audits and inspections; these are included in the statement's action plan.

## **Fundamental Systems**

Fundamental financial systems (agreed with external audit) were reviewed during 2008/09. Extended audit coverage was achieved on fundamental financial system reviews through better use of analytical review without additional resource. External audit look to place reliance on our work wherever possible to minimise duplication of effort and maximise the overall audit resources available. In order to achieve this, the level of testing carried out complies with the Internal Audit/ External Audit protocol.

The fundamental financial systems comprise of:

- Payroll
- Creditors
- Sundry debtors
- Local Taxation (Council and NNDR)
- Council Tax and Housing Benefits
- Accounting system (eFinancials)

- Cash Receipting
- Treasury Management
- Asset Management
- CareFirst

The systems were found to be generally sound, however, some recommendations for improvement were identified and agreed with relevant service managers. The key findings are:

- Payroll – the process of updating and monitoring authorised signatories for creditor payments and most payroll returns has been standardised. A core, up to date, list of authorised signatories for creditor and payroll payments is maintained and monitored through the council's accounting system (efinancials). Updating of authorisation lists for time sheet returns was not completed during 2008/09 but is nearing completion. Extended audit testing was carried out and no problems were identified as good budgetary control procedures and regular validation exercises provide other mitigating controls. All payroll transactions tested were found to be valid however supporting documentation could not be traced in a few cases.
- Council Tax and Housing Benefits -Although quality checks are carried out there is no written procedure for benefit checking. Recording of supporting evidence to confirm claimant identity when cheques need to be opened could be improved.
- eFinancials – interface controls were adequate however improvements to access controls are necessary in respect of 2 feeders systems (Servitor and Carefirst). Journals, internal accounts and transaction transfers were correctly authorised but improvement to supporting documentation is required.

2.7 A risk-based approach is adopted to prioritise the work undertaken. This involves evaluating the controls in place to reduce high impact / high likelihood risks. This replaces the traditional approach, which concentrates solely on financial risk and consequences. The audit plan is flexible to respond to changing circumstances and emerging risks and work is re prioritised accordingly. The 2008/09 audit plan contained 129 planned audit assignments of which 104 were substantially completed. In addition 30 unforeseen audit assignments, 20 FMSiS assessments and an audit of one grant were also completed. These are listed in appendix A.

2.8 Although recommendations for improvements were identified and agreed with relevant service managers no significant control weaknesses were identified affecting the overall audit opinion. All recommendations are followed up to ensure there is an appropriate management response to audit reports. Generally appropriate action is taken however, if necessary, slow or inadequate action in response to audit recommendations is reported to relevant service directors through Internal Audit's quarterly reports. There are no examples of poor response to audit recommendations to report to the Committee. In fact

progress has been made on slow response to audit recommendations in relation to IT controls previously reported to the Audit Committee during 2008/2009; as issues are now being addressed by managers or will be actioned through the implementation of Government Connect requirements.

- 2.9 Forty one per cent of the audits completed were schools audits (43 completed). The audits showed that reasonable assurance could be given on the adequacy of internal control arrangements although recommendations for improvements were identified at each school. There were no schools whereby no assurance could be given. The majority of recommendations relate to compliance with council procedures in relation to procurement and financial administration. Information is passed to key service officers to incorporate in newsletters and raise awareness through the schools forum of representative head teachers.

Overall there has been a slow response from schools to Financial Management Standards in Schools. All secondary schools have now achieved the standard. Primary schools are not submitting their self assessments in accordance with the agreed timetable although no school has failed to achieve the standard to date.

- 2.10 Internal audit provides the focus for the council's Anti Fraud, Theft and Corruption Strategy. It promotes awareness with service managers through individual assignments, control risk assessment questionnaires and fraud warning bulletins via the internal communication network. Each year proactive and reactive counter fraud work is identified within the audit plan and during 2008/2009 the council's arrangements were evaluated against best practice as defined by CIPFA. The outcome of this work was a review of the Anti Fraud, Theft & Corruption strategy and determination of the council's approach to Anti Money Laundering Regulation. The new strategy is being promoted through the council's website and an article has featured in Direct magazine. Further promotion is planned to launch the council's anti money laundering policy and procedures and training is being identified.

- 2.11 Internal audit operates the council's dedicated telephone hotline for whistle blowers. The hotline details were re-advertised with the revised strategy and this is believed to be a contributory factor to the increase in calls received. The total number of calls received during 2008/2009 was 194, which was an increase on the previous year of 18%. Benefits savings as a result of information received also increased significantly to £45.3k (last years figure was £3.7k).

- 2.12 The council participates in the Government's National Fraud Initiative (NFI). Internal audit co-ordinates the data matching and mismatches are investigated. The 2006/07 NFI exercise (which spans two years) was extended to include more potential matches including none financial risks such as ineligible workers and criminal activity which

bypass CRB checks. Matches were received in February 2009 and investigations are progressing well. Specifically results to date show:

- Creditor matches have not shown any duplicate payments
- Insurance matches show no serial claimants
- No matches between payroll and Home Office records on asylum seekers
- Residential placements matched against death returns have not identified any overpayments.

The outcome of investigations will be finalised and returned to the Audit Commission by the December 2009 deadline. Audit Commission's inspection, reported to the Audit Committee in April 2008, concluded that the coverage of the NFI exercise was satisfactory and suitable progress had been made in most areas. A further inspection is expected in January 2010.

- 2.13 A number of fraud and irregularity assignments were carried out during 2008/2009. These resulted in recommended improvements to cash handling procedures, safeguards to client valuables, better claims authorisation procedures and monitoring the use of/safeguarding council assets. Appropriate management action was recommended and two members of staff were dismissed, another retired. The level of potential abuse of the use of the Internet/ email reduced in 2008/2009 as a result of the withdrawal of access to social networking sites. However some cases were detected and referred to internal audit for investigation. There were 7 internal audit investigations of potential internet abuse in 2008/09, of which; 1 resulted in no action necessary; management action was taken in 4 cases and disciplinary proceedings were taken against two officers (1 case is still pending; 1 resulted in a written warning). There were 3 further instances where information was provided to HR colleagues as part of other investigations.
- 2.14 Members were previously informed of a fraud investigation at one of the council's leisure facilities which might have reached the Audit Commission's reporting threshold. The staff concerned resigned. The case has now been concluded and resulted in police cautions for the two ex employees and recovery proceedings in respect of funds stolen totalling £6k (this is below the Commission's reporting threshold). Internal Audit also reviewed cash handling, petty cash, vending and stock procedures and payroll claims at other leisure facilities to ensure internal control arrangements were adequate.
- 2.15 The internal audit section constantly strives to improve the service they provide. The section also participates in national and local benchmarking exercises. Most performance targets were met for 2008/2009. More details are provided in Internal Audit's effectiveness report elsewhere on this agenda.
- 2.16 The section provided internal audit services for the Humberside Police Authority during 2008/09 (the contract has been extended until 31/03/2010) and Connexions until 31/03/09. The contracts generate

additional income and the opportunity for professional development by carrying out work in another area of the public sector.

### **3. OPTIONS FOR CONSIDERATION**

3.1 The Committee is asked to consider whether Internal Audit's Annual Report provides sufficient assurance on the adequacy of the council's internal control environment in 2008/2009. Members may wish to ask questions and seek clarification as necessary. If it concludes that it does provide sufficient assurance the Committee is invited to approve the Internal Audit Annual Report for 2008/2009.

3.2 The Committee may decide not to approve or amend the Risk Management Strategy and action plan 2009/2010.

### **4. ANALYSIS OF OPTIONS**

4.1 The Internal Audit Annual Report 2008/2009 complies with professional guidance available and is designed to provide this Committee with the assurance required. Members should ask sufficient questions to ensure the report provides sufficient assurance to fulfil their role as set out in the Committee's terms of reference.

4.2 The option set out in 3.2 represents an opportunity missed to receive an important source of assurance to assist the Committee to fulfil its role effectively.

### **5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)**

5.1 The work of the internal audit section enhances control over the use of the council's resources through the recommendations made in audit reports.

5.2 There are no additional staffing, property or IT implications

### **6. OTHER IMPLICATIONS (STATUTORY, ENVIRONMENTAL, DIVERSITY, SECTION 17 - CRIME AND DISORDER, RISK AND OTHER)**

6.1 The requirement for an internal audit function is set out in the Accounts and Audit Regulations 2003. Internal audit will continue to assist the Chief Financial Officer discharge his statutory duty under the provisions of the Local Government Act 1972.

6.2 Internal audit's work is an important component of the Annual Governance Statement and promotes good corporate governance.

## **7. OUTCOMES OF CONSULTATION**

- 7.1 Consultation takes place at all stages of audit work. It affects the scope of audit work undertaken, the risk assessment of audit work, audit practices and products. There is also feedback to individual staff forming part of their employee development review.

## **8. RECOMMENDATIONS**

- 8.1 The Audit Committee should consider the assurance provided by the Internal Audit Annual Report for 2008/2009 on the adequacy of the council's internal control environment.
- 8.2 The Audit Committee approves the Internal Audit Annual Report for 2008/2009.

SERVICE DIRECTOR FINANCE

Pittwood House  
Ashby Road  
SCUNTHORPE  
North Lincolnshire  
DN16 1AB  
Author: C Andrews  
Date: 06/06/09

**Background Papers used in the preparation of this report**

## Appendix A

Audit Areas	Audits carried out		Audits not carried out	
	Planned	Unplanned	Deferred <sup>1</sup>	Cancelled <sup>2</sup>
<b>Fundamental Financial Systems</b>	<ul style="list-style-type: none"> <li>• Payroll</li> <li>• Creditors</li> <li>• Debtors</li> <li>• Cash Receipting</li> <li>• Main Accounting Ledger</li> <li>• Council Tax and Housing Benefits</li> <li>• Local Taxation</li> <li>• Treasury Management</li> <li>• Fixed Asset Register</li> <li>• CareFirst</li> </ul>	<ul style="list-style-type: none"> <li>• Treasury Management Review</li> <li>• Personnel Establishment &amp; Payroll Validation</li> <li>• Benefits Performance Indicators</li> </ul>		
<b>Annual Governance Statement</b>	<ul style="list-style-type: none"> <li>• In year monitoring and compilation of the Statement</li> </ul>			
<b>Corporate management</b>	<ul style="list-style-type: none"> <li>• Audit Committee</li> <li>• CPA/CAA</li> </ul>			
<b>Corporate Governance</b>	<ul style="list-style-type: none"> <li>• In year monitoring and advice. Evaluation of council arrangements against best practice standards. Revision of the council's Code of Corporate Governance</li> </ul>			
<b>Risk Management</b>	<ul style="list-style-type: none"> <li>• In year monitoring and advice, Strategic Risk Management Group work. Annual review of risk management arrangements, strategic and key operational controls.</li> </ul>			
<b>Performance Management, Performance Review &amp; Improvement Plans</b>	<ul style="list-style-type: none"> <li>• Performance Management Framework and System</li> <li>• Performance Indicators/ Data Quality</li> </ul>			
<b>IT Audit</b>	<ul style="list-style-type: none"> <li>• Access arrangements</li> </ul>	<ul style="list-style-type: none"> <li>• ePayments</li> </ul>	Project	<ul style="list-style-type: none"> <li>• eCommerce</li> </ul>

<sup>1</sup> Deferred Audits at the request of the relevant service manager or reprioritised

<sup>2</sup> Cancelled audits by agreement with the client

Audit Areas	Audits carried out		Audits not carried out	
	Planned	Unplanned	Deferred <sup>1</sup>	Cancelled <sup>2</sup>
	<ul style="list-style-type: none"> <li>Data Security</li> <li>Disaster Recovery and backups</li> <li>Overview of Governance arrangements</li> </ul>	<ul style="list-style-type: none"> <li>IT Debit Cards</li> </ul>	<ul style="list-style-type: none"> <li>management</li> <li>Procurement</li> <li>Physical controls</li> <li>Budgetary Control</li> </ul>	
<b>Contract Audit</b>	<ul style="list-style-type: none"> <li>Contracts</li> <li>Procurement in Schools</li> </ul>			
<b>Fraud Prevention and Detection</b>	<ul style="list-style-type: none"> <li>Responding to cases received via Whistleblowers Hotline and email</li> <li>National Fraud Initiative (Data Matching)</li> <li>Proactive Counter Fraud to assess and revise arrangements against best practice</li> <li>Define the council's approach to Anti Money Laundering policy and establish associated policy and procedures</li> </ul>			
<b>Environmental Audits</b>				<ul style="list-style-type: none"> <li>EMAS</li> </ul>
<b>Council-wide Systems</b>	<ul style="list-style-type: none"> <li>eProcurement</li> <li>Partnership governance arrangements</li> <li>Local Area Agreement</li> <li>Grant Claims</li> <li>Income charging policy</li> </ul>		<ul style="list-style-type: none"> <li>Corporate Manslaughter Act</li> <li>Budgetary control</li> <li>Diversity</li> </ul>	<ul style="list-style-type: none"> <li>Service Plans</li> <li>Corporate Requirements</li> </ul>
<b>Adult Social Care Services</b>	<ul style="list-style-type: none"> <li>Budgetary Control</li> <li>CareFirst</li> <li>Continuing Care</li> <li>Learning Disability</li> <li>Fit for the Future,</li> </ul>	<ul style="list-style-type: none"> <li>Blue Badges</li> </ul>	<ul style="list-style-type: none"> <li>Respite Care</li> </ul>	<ul style="list-style-type: none"> <li>Panel Process</li> </ul>
<b>Children &amp; Young People's Service</b>	<ul style="list-style-type: none"> <li>Procurement in schools</li> <li>External Funding</li> <li>Issues from school audits</li> <li>Special Needs</li> <li>Looked After Children</li> <li>Section 17 payments</li> </ul>		<ul style="list-style-type: none"> <li>Budgetary control</li> <li>2 schools</li> </ul>	

Audit Areas	Audits carried out		Audits not carried out	
	Planned	Unplanned	Deferred <sup>1</sup>	Cancelled <sup>2</sup>
	<ul style="list-style-type: none"> <li>• 43 School Audits</li> <li>• 20 Financial Management Standards in Schools</li> <li>• Youth support</li> <li>• Child protection</li> </ul>			
<b>Finance – Other</b>	<ul style="list-style-type: none"> <li>• Leasing</li> <li>• Taxation</li> <li>• Debit cards</li> </ul>			
<b>Highways &amp; Planning</b>	<ul style="list-style-type: none"> <li>• Transport</li> <li>• Car Parking</li> <li>• Materials Team</li> <li>• Searches*</li> <li>• BidTrack</li> </ul>		<ul style="list-style-type: none"> <li>• Strategic Alliance</li> </ul>	
<b>Human Resources</b>	<ul style="list-style-type: none"> <li>• CRB checks,</li> </ul>	<ul style="list-style-type: none"> <li>• Strike payment deduction</li> </ul>	<ul style="list-style-type: none"> <li>• Flexible working</li> <li>• Working Time Directive</li> </ul>	
<b>Legal &amp; Democratic Services</b>	<ul style="list-style-type: none"> <li>• Democratic Services</li> <li>• Data Protection and Freedom of Information Legislation</li> <li>• Registrars</li> <li>• Councillors Allowances</li> <li>• Search fees*</li> </ul>			
<b>Neighbourhood &amp; Environmental Services</b>	<ul style="list-style-type: none"> <li>• Homelessness</li> </ul>		<ul style="list-style-type: none"> <li>• Licensing</li> </ul>	
<b>Strategic Regeneration Housing and Development</b>	<ul style="list-style-type: none"> <li>• External Funding</li> <li>• Bees Knees</li> <li>• Crosby and Acorn Pathfinders</li> </ul>		<ul style="list-style-type: none"> <li>• Strategic Housing</li> <li>• Investment and Marketing</li> </ul>	
<b>Asset Management and Culture (excluding IT Audits)</b>	<ul style="list-style-type: none"> <li>• Leisure sites</li> <li>• Budgetary control</li> </ul>		<ul style="list-style-type: none"> <li>• Maintenance of Buildings</li> <li>• Commercial Buildings</li> <li>• Strategic</li> </ul>	

Audit Areas	Audits carried out		Audits not carried out	
	Planned	Unplanned	Deferred <sup>1</sup>	Cancelled <sup>2</sup>
			Alliance*	
<b>Community Planning and Resources</b>	<ul style="list-style-type: none"> <li>Local Performance Service Agreements</li> <li>Libraries</li> <li>Crime and Disorder Act</li> </ul>	<ul style="list-style-type: none"> <li>Complaints procedure</li> </ul>	<ul style="list-style-type: none"> <li>Consultation and Engagement</li> </ul>	

In addition to the above resources were deployed on :

- 22 cases of advice /irregularity work not listed due to confidentiality
- Follow up work
- Audit plan performance monitoring and reporting