

## SOUTH HAMS DISTRICT COUNCIL

<b>NAME OF COMMITTEE</b>	<b>Audit Committee</b>
<b>DATE</b>	<b>14th June 2012</b>
<b>REPORT TITLE</b>	<b>REVIEW OF THE EFFECTIVENESS OF THE SYSTEM OF INTERNAL AUDIT 2011/12</b>
<b>Report of</b>	<b>Chief Internal Auditor</b>
<b>WARDS AFFECTED</b>	<b>All/Corporate</b>

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**Summary of report:**

The purpose of this report is to provide members with assurance that the System of Internal Audit is in place and effective.

Its intention is to demonstrate that the Council's internal audit section continues to reach the standards set out in CIPFA's Code of Practice for Internal Audit in Local Government enabling the external auditor to place reliance on the work of the section, and that the service provided to clients continues to be well received.

The internal audit section also continues to work with its partners, West Devon as a shared internal audit service and collaboration with Teignbridge, and review its own processes to ensure that the improvements of recent years are maintained in the future.

This review also aims to demonstrate that the wider System of Internal Audit is effective and therefore contributes to the assurance provided by the Chief Internal Auditor's Opinion on the Adequacy of Internal Control, which is provided in a separate Internal Audit annual report presented to this Committee.

**Financial implications:**

There are no direct financial implications of the monitoring of the Internal Audit service. The internal audit costs for the year are as budgeted.

**RECOMMENDATIONS:**

**It is recommended that members note the findings of the Review of the Effectiveness of the System of Internal Audit set out in this report.**

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## **Background**

1.1 The **Terms of Reference** for Internal Audit were presented to the Audit Committee in April 2010 and updated at the April 2011 Audit Committee (Minute reference A.39/10). They cover:

Statutory Requirements  
Purpose, Authority and Responsibility;  
Independence;  
Audit Management;  
Scope of Internal Audit's Work;  
Audit Reporting; and  
Audit Committee.

1.2 The **Audit Strategy** was updated for 2011/12 and was approved by the Audit Committee in April 2011 (Minute reference A.39/10 refers) and covers:

Objectives and Outcomes;  
Opinion on Internal Control;  
Local and National Risk Issues;  
Provision of Internal Audit; and  
Resources and Skills.

1.3 Until 2009/10, the Chief Internal Auditor's annual report included feed back to members of the review of the effectiveness of the System of Internal Audit, and on aspects of the Internal Audit Strategy: the Provision of Internal Audit and Resources and Skills. The annual report also included the Chief Internal Auditor's Opinion on the Adequacy and the main findings from individual audits and the managers' proposed actions to address them.

1.4 Due to the size of the report, it was decided to separate the areas reported into two. The second document, the Annual Report and Opinion on the Adequacy of Internal Control 2011/12, also appears on the agenda of this Committee.

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

2.1 The process to produce the Annual Governance Statement requires the Council through the Chief Internal Auditor to review the effectiveness of the system of internal audit covering:

- Compliance with the standards set out in the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Internal Audit in Local Government 2006;
- Effectiveness of the Audit Committee;
- Reliance on Internal Audit by the external auditor;
- Client and management opinion; and
- Extent to which IA adds value and helps delivery of corporate objectives.

2.2 The Annual Governance Statement will be presented to the Audit Committee at the meeting of 31st July 2012.

## Compliance with the CIPFA Code of Practice for Internal Audit 2006

- 2.3 The Chief Internal Auditor carried out a self assessment of the Council's internal audit service against a schedule summarising the CIPFA Code kindly supplied by our internal audit colleagues at Teignbridge District Council as part of the collaboration between the teams.
- 2.4 The results were satisfactory with no significant issue arising, which was expected given that a similar assessment was made each year since the end of 2007/08 and the gaps identified closed. The audit process and key documents were changed at that time to reflect the findings and requirements of the 2006 Code of Practice.

## *Assessing Fraud Risks in the Current Financial Climate*

- 2.5 At the April 2012 Audit Committee, under Item 9 'Protecting the Public Purse', members asked for further details on audit planning in the current financial climate. CIPFA's paper Auditing in an Economic Downturn suggests that many internal audit sections are moving away from the annual plan to a more flexible approach having regard to operational risks, effectiveness of risk management, proactive anti fraud work, cost reductions and reputational risks.
- 2.6 The Council's Internal Audit Plan has always been flexible with an adequate contingency and changes for emerging risks made with the approval of the S.151 officer and confirmed by the Audit Committee. This is unchanged.
- 2.7 In addition, a further paper provides tips on areas for internal audit to take particular care over and this is referred to at the start of each audit exercise. It covers Governance, Personnel, Assets, Procurement, Payments, Creditors, Debtors, Cash and Bank, Accounting, Grants, Treasury Management etc.

## Effectiveness of the Audit Committee

- 2.8 The Audit Committee met in a 'workshop' forum in June 2011 (and has done so for a number of years), jointly with West Devon's Audit Committee, to consider a number of issues and carry out a self assessment of the effectiveness of the Audit Committee.
- 2.9 The assessment was based on a schedule from the CIPFA document 'Audit Committees: Practical Guidance for Local Authorities' and the result was satisfactory. A review of the resolutions made during the year and the actions taken as a result is also a typical agenda item.
- 2.10 A further 'workshop' is planned for June 2012 although at the date of writing this report the final details have not been completed. However, there is no reason to believe that the Effectiveness of the Audit Committee has diminished during 2011/12.

## External Audit - Assurance Provided by Internal Audit

- 2.11 We have not to date received a formal report from the Audit Commission that contains comment on the performance of Internal Audit for 2011/12, but we have had no negative feedback on the audit process or work standards from the external auditor.

## Client and Management Opinion

2.12 For some years the audit team have issued a satisfaction survey electronically to the main client officers with the final audit report for each of the audits that we undertake. Completion and return is encouraged but is discretionary.

2.13 Satisfaction surveys received for 2011/12 continue to be satisfactory, with 100% of the 13 responses (97% from 9 at West Devon) marking us good or excellent (93.6% in 2010/11 from 22 returned) for the sub criteria under Audit Planning, Quality of Audit Report and Communication as shown in table 1:

*Table 1: 2011/12 Satisfaction Survey Results.*

Survey Criterion	Excellent	Good	Total 2010/11	Target	Total 2010/11
	%	%	%	%	%
<b>Audit Planning</b> - Consultation; Objectives.	51.3	48.7	100	90	86.4
<b>Quality of Audit Report</b> Clarity; Accuracy; Value; Presentation.	55.8	44.2	100	90	93.2
<b>Communication</b> Feedback; Helpfulness; Professionalism; Timeliness.	86.2	13.8	100	90	98.2
<b>Overall %</b>	<b>67.3</b>	<b>32.7</b>	<b>100</b>	<b>90</b>	<b>93.6</b>

There were no 'poor' markings and positive comments were made by 4 managers, which included the following:

- *'A thorough audit that balanced the need for managing risk against reducing resources well';*
- *Appreciate support and help from all officers within the Internal Audit Team'; and*
- *'Yet again this has been a useful chance to review what we are doing and how far we have moved on'.*

2.14 We continue to learn from any comments made and are ensuring that, wherever possible, we take on board suggestions for improvement, such as:

One manager said:

- *'Would like to see a scoring system rather than poor/fair/good/excellent. If an audit is fair, we do not know how close it was to poor or good'.*

We now include a comment under the 'Conclusion' for audits where the Opinion is in danger of moving to a lower rating, and for 2012/13 we will establish some form of indicator in the report that confirms where in the rating the Opinion lays.

## Extent to which Internal Audit adds value and helps delivery of corporate objectives

2.15 The customer survey results and comments help to demonstrate that Internal Audit adds value.

2.16 The Audit Plan for 2011/12 (Appendix A of the 'Annual Report and Opinion' presented separately to this Committee) is linked to the Council's Priorities and Heads of Service/service managers are invited to express areas of concern to the auditor at the commencement of each audit. Wherever possible these areas are included in the audit work of undertaken.

### **Internal Audit's Performance Indicators**

3.1 The Internal Audit Strategy 2010/11 (April 2010 Audit Committee) sets out the performance indicators to be recorded.

#### *Audit Reports Issued*

3.2 The number of audit reports issued in 2010/11 were as follows:

*Table 2: Number of audit reports issued in the past 5 years.*

Audit Year	Number of Reports by Type			
	Major Systems	Other systems/ Establishments	External Bodies	Annual Total
2011/12	9	22	2	33
2010/11	9	24*	1	34
2009/10	9	30*	1	40
2008/09	9	40*	1	50
2007/08	8	33*	1	42

*\*The BVPI reports included in Other Systems contained the results a number of full systems audits but were issued as only one report in each year started.*

*The total number of reports for SHDC fell in 2010/11 due to the provision of the shared service to West Devon as reported to the Audit Committee in the audit plans in April 2010 and 2011.*

3.3 We are continuing to be alert to development in the profession of meaningful targets for the section, and monitor our performance against them and always seek to benchmark key indicators with other Devon internal audit teams whenever possible.

#### Other Indicators

3.4 Timeliness is an important element of audit reporting, and therefore we monitor against two targets for this:

- The timely issue of draft audit reports: within 10 working days of completing the audit work;
- The timely issue of finalised audit reports: within 10 working days of completing discussions on the draft report, and completing the action plan on recommendations.

3.5 We are also monitoring the % of the audit plan that is completed during the year. Completion is influenced mainly by the level of unplanned work carried out in the year, for which some contingency time is planned.

3.6 The following table shows that Internal Audit is meeting its targets, as set out below:

Table 3: Internal Audit Performance against Targets 2011/12

Performance Indicators	Target	2011/12	2010/11
% of Audit Plan completed, against target for South Hams	90%	95%	98%
% of Audit Plan completed, against target for West Devon	100%	100%	100%
Overall % of Audit Plan completed	90%	96%	98%

Performance Indicators (Cont.)	Target	2011/12	2010/11
<b>Timeliness of reports:</b>			
% of draft reports issued within 10 working days of the audit completion	100%	100%	100%
% of final reports issued within 10 working days of discussion on the draft	100%	100%	100%
<b>External Audit</b>			
Assurance gained (Reliance) on work of Internal Audit by the external auditor	Yes	Expected	Yes
<b>Costs</b>			
Direct cost of provision of service with oncosts/recharges (Gross)	-	£106.2k*	£97.5k
Oncosts added to the above e.g. use of the building, ICT etc.	-	£17.4k	£14.5k
Recharges/income	-	(£37.0k)**	(£42.8k)
Net cost of the service	£82.5k	£86.6k	£69.2k
<b>Average cost per audit day:</b>			
Average cost per audit day: Direct costs (without oncosts/recharges) and based on available days.	-	£175	£184
Average cost per audit day: direct costs with oncosts but not recharges.	-	£204	£211
<b>Follow Up</b>			
Percentage of audit reports where the agreed recommendations were satisfactorily actioned i.e. Implemented/Mainly implemented.	90%	82%***	96%

\* above: direct cost increase due to the European Grants Officer/Auditor being charged to Internal Audit budget at 50% for 2010/11, and in full for 2011/12. As a result, the 2010/11 cost per day has been restated when compared with the equivalent report last year to ensure consistency of calculation.

\*\* above: includes income from West Devon of £25.2k, LAG recharge at £10k and Dartmouth Town Council etc.

\*\*\* above: main reason cited for non implementation was the change in responsibilities following senior and middle manager reviews.

## Resources and Skills

3.7 An allowance of 13 sickness days was originally planned for 2011/12, with 9 days actually being used (10 days 2010/11), and 1 day Carers Leave.

3.8 Training provided to members of the team during the year included:

Chief Internal Auditor

- Council Contracts & Your Actions (in-house);
- Future of Local Audit (DCLG; Taunton).

Senior Auditor:

- Council Contracts & Your Actions (in-house);
- Word 2007 Introduction (E Academy);
- Excel 2007 Introduction (E Academy);
- Excel 2007 Intermediate (E Academy).

Auditor:

- Council Contracts & Your Actions (in-house)
- E Academy – various modules including Word 2007; Word 2007 Intermediate; Excel 2007; Excel 2007 Intermediate; Excel 2007 Advanced; Questioning; Listening etc.

## Other Partners

### *Dartmouth Town Council*

4.1 We again provided an internal audit service to Dartmouth Town Council in June 2011. The Town Council was recharged for the 5 days on a cost-plus recovery basis.

4.2 Our audit and any recommendations that we make for improvement of controls are formally reported to the Clerk and the Council's Chairman of Finance and General Purposes Committee.

4.3 Although the service was well received, confirmed by the survey referred to above, the Town Council has chosen not to continue the arrangement. We understand that an external supplier has been able to provide a service at a significantly lower charge.

### Shared Services West Devon Borough and Teignbridge District Councils

#### *West Devon Borough Council*

4.4 The second year of the provision of an internal audit service to West Devon Borough Council (WDBC) has been completed.

4.5 The work and findings have been reported to the WDBC Audit Committee using a similar suite of reports and with the same frequency as those received by the SHDC Audit Committee.

4.6 The relevant charges have been paid by WDBC.

- 4.7 It is intended that Members of both Council's Audit Committees will attend the workshop planned for in June 2012.

*Teignbridge District Council*

- 4.8 The Audit Committee has been provided with frequent updates on the progress of the Shared Service arrangement with our Internal Audit colleagues at Teignbridge District Council following the decision of the Joint Steering Group (JSG) in June 2008.
- 4.9 The decision has never been rescinded and so the arrangement continues, to the benefit of both teams. The majority of the proposals for the extended internal audit collaboration have been completed or are continuing and include sharing of information, audit programmes, best practice, attending and feeding back on seminars etc.

**5. LEGAL IMPLICATIONS**

- 5.1 Required under the Local Government Finance Act 1972 and subsequent Accounts and Audit Regulations – the latest being 2003, 2006, and 2011.

**6. FINANCIAL IMPLICATIONS**

- 6.1 Within existing budgets. The costs of the service are highlighted at paragraph 3.6 above.

**7. RISK MANAGEMENT**

- 7.1 The risk management implications follow after the table of other considerations:

**Other Considerations:**

<b>Corporate priorities engaged:</b>	All/Corporate
<b>Statutory powers:</b>	Local Government Finance Act 1972 Accounts and Audit Regulations 2003, 2006, 2011

<b>Considerations of equality and human rights:</b>	No specific equality and human rights issues arising from this report.
<b>Biodiversity considerations:</b>	No specific biodiversity issues arising from this report.
<b>Sustainability considerations:</b>	No specific sustainability issues arising from this report.
<b>Crime and disorder implications:</b>	No specific crime and disorder issues arising from this report.
<b>Background papers:</b>	CIPFA Code of Practice for Internal Audit in Local Government 2006; SHDC 5-year Audit Plan 2010/11 to 2015/16. Internal Audit Plan 2011/12 and Strategy (April 2011 Audit Committee); Internal Audit Terms of Reference(April 2010 and 2011 Audit Committees);

	Progress against the Internal Audit Plan reports to the Audit Committees of – September 2011, November 2011, and April 2012.
<b>Appendices attached:</b>	None

No	Risk Title	Risk/Opportunity Description	Inherent risk status				Mitigating & Management actions	Ownership
			Impact of negative outcome	Chance of negative outcome	Risk score and direction of travel			
1	Failure of the System of Internal Audit	The Council's Annual Governance Statement cannot be signed if the System of Internal Audit fails.	3	2	6	↔	<p>An annual Internal Audit Strategy reviewed by the Audit Committee at the beginning of each financial year sets out how the audit plan is to be delivered.</p> <p>A risk based Internal Audit plan is reviewed by senior managers and members, and updated to reflect emerging as appropriate through the year. The plan is linked to the Council's objectives and risks to these objectives.</p> <p>The Internal Audit approach adheres to the appropriate professional standards set by CIPFA.</p> <p>Regular monitoring of performance of Internal Audit is carried out by the S.151 Officer and the Audit Committee. Liaison with the external auditors ensures that duplication of scarce audit resources is avoided and that they are able to gain assurance on internal Audits work.</p> <p>Liaison with Heads of Service and managers ensures Internal Audit adds value.</p> <p>The Audit Committee reviews its effectiveness annually.</p>	S.151 Officer; Chief Internal Auditor; Audit Committee Chairman.