

**REPORT TO: SCRUTINY COMMITTEE - 18 AUGUST 2010**  
**REPORT ON: 2009/10 INTERNAL AUDIT ANNUAL REPORT**  
**REPORT BY: CHIEF INTERNAL AUDITOR**  
**REPORT NO: 438-2010**

## **1.0 PURPOSE OF REPORT**

To submit to Members of the Scrutiny Committee the Internal Audit Annual Report for 2009/10 which summarises the activities of the Council's Internal Audit Service for 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 2009/10 financial year.

**4.2.** On an annual basis the Chief Internal Auditor is also required, to prepare a statement on the adequacy and effectiveness of the internal control system of the Council. This statement forms part of the assurance gathering process which feeds into the Annual Governance Statement included within Dundee City Council's Annual Statement of Accounts. A copy of the statement prepared by the Chief Internal Auditor for the 2009/10 financial year is attached at Appendix B.

## **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, Depute Chief Executive and Director of Finance have been consulted on the content of this report.

## **7.0 BACKGROUND PAPERS**

None

Sallie Dailly, Chief Internal Auditor

DATE: 27 July 2010

## 2009/10 INTERNAL AUDIT ANNUAL REPORT

### 1. PURPOSE OF REPORT

- To summarise the key areas of activity of the Council's Internal Audit Service during the 2009/10 financial year.

### 2. INTERNAL CONTROLS

- Each local authority is accountable for the way in which it has discharged 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 Dundee City Council as a service to the Scrutiny Committee (and the former Audit and Risk Management Sub-Committee), Chief Executive, Director of Finance 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 to 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. Various types of review work are undertaken which includes systems work, computer audit work, location audits, contract audit, specific investigations and advice on systems, controls and risk.
- 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, and best value is achieved.
- The Internal Audit Annual Plan provides a summary of the areas where it is planned that work will be carried out during the forthcoming year. The Internal Audit Annual Plan for the 2009/10 financial year was approved by the former Audit and Risk Management Sub-Committee in

April 2009 (Report No. 73-2009). This was prepared on the best information available at that time.

- The performance of internal audit is also reviewed by the Council's External Auditor, currently Audit Scotland, on an annual basis. This allows, where appropriate, reliance to be placed on the work of internal audit and for both parties to plan their reviews without duplication of effort and unnecessary disruption to services.

## **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, if 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 reviews reported upon in 2009/10 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 former Audit and Risk Management Sub-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.

## **6. KEY EVENTS DURING 2009/10**

- Information technology is an ever expanding area and the Council is heavily reliant on various computerised systems and software packages in achieving its objectives. The audit of this area demands a specialist knowledge base. This is an area that has not been particularly well developed as the Internal Audit Service does not have staff with specialism in this area. To overcome this, the services of external specialists were procured to assist internal audit staff in reviewing the adequacy of the Council's intrusion prevention and detection systems and also the arrangements in place to meet the requirements of the payment card industry data security standard.

## **7. PLAN ACHIEVEMENT**

- During 2009/10 the actual number of productive days for the Internal Audit Service was 1,424 days which was broadly in line with the budgeted productive days. Of the actual productive days available, 86% were spent on direct audit activities and 14% were spent on support activities such as management, audit planning and staff training and development. The number of days spent on direct audit activities during 2009/10 was slightly higher than in 2008/09.
- In respect of Dundee City Council, the 2009/10 Internal Audit Annual Plan included 31 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 2008/09, provision of advice being given to clients on systems, control and risk and specific investigations. In addition, the plan also contained allocations for the provision of internal audit services to external bodies namely Tay Road Bridge Joint Board, Tayside Valuation Joint Board and Dundee Leisure Limited, as detailed in the respective service level agreements.

- Whilst work on all of the planned areas for corporate and departmental reviews for Dundee City Council commenced in 2009/10 there was slippage in relation to the anticipated time required for some projects. This was due to a number of factors which included project overruns where the fieldwork proved more problematic than originally anticipated, familiarisation by staff with computer assisted audit technique software and the actual time spent on work for outside bodies exceeding the days included in the plan. Provision has been made in the 2010/11 Internal Audit Annual Plan to complete prior year projects which still required to be finalised.
- For financial year 2009/10, 36 internal audit reports were issued on the basis of the work undertaken for Dundee City Council. In addition, 20 reports were issued in relation to the internal audit services provided to outside bodies. Reports have generally been well received by clients with management agreeing to implement 98% of recommendations made.

## **8. OVERALL ASSESSMENT OF CONTROLS**

- Activity for Dundee City Council during 2009/10 covered a wide spectrum of areas including community planning and partnership, corporate governance, council strategies, policies and initiatives, debtors and debt management, disaster recovery and business continuity, information and system security, management of hardware and software, payroll and employee expenses, statutory performance indicators, housing benefit overpayments, gas safety checks, car parking income, meals service, stocks and stores year end work, grant claims and follow-up work.
- The 2009/10 audit 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 either lack or have weaknesses in controls.
- Analysis of the overall audit opinion for the reports issued highlighted that 19% of the areas reported upon were considered to be well controlled (full assurance), 50% were adequately controlled (reduced assurance) and 31% were requiring improvement (limited assurance). 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.
- 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.
- In line with the requirements of the Code of Practice on Local Authority Accounting in the UK, the Chief Internal Auditor is required to provide an independent opinion on the adequacy and effectiveness of the Council's system of internal financial control. In compiling this statement, a copy of which is attached at Appendix B, the Chief Internal Auditor takes due recognition of the audit work carried out by the Service and other pertinent information. On the basis of the areas used to inform this process for the year to 31 March 2010 the overall audit opinion reached was that reasonable assurance could be placed on the Council's internal control system.

## **To the Members of Dundee City Council, Chief Executive and Director of Finance**

As Chief Internal Auditor of Dundee City Council, I am pleased to present my annual opinion on for the year ended 31 March 2010. 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 for 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 Audit and Risk Management Sub-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 confirm that agreed action plans have been implemented. Matters arising from internal audit work are also reported to the Council's Audit and Risk Management Sub-Committee, the Chief Executive and the Council's External Auditor.

### **Summary of 2009/10 Internal Audit Activity**

During 2009/10 financial year a total of 36 internal audit reports were issued. These covered a wide spectrum of areas including corporate governance, accounting and budgetary control, capital contracts, single status, statutory performance indicators, security of assets, disaster recovery and business continuity, intrusion detection and prevention, internet usage, management and security of cash, treasury management, non-domestic rates, fleet management, car parking income, attendance management, gas safety checks, service level agreements, post opening, the Fairer Scotland Fund, stocks and stores (including year end work), grant claims and follow-up reviews. The Internal Audit Service also provided advice on the control environment as required.

The 2009/10 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 lack or have weaknesses in 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 2010.
- The assessment of risk completed during the preparation of the audit plan.
- Reports issued by Audit Scotland, 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.

### **Opinion**

It is my opinion, based on the above, that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control system in the year to 31 March 2010.

*Sallie M. Dailly*

**DATE 17 June 2010**

**Chief Internal Auditor  
Dundee City Council**