

**REPORT TO: AUDIT AND RISK MANAGEMENT SUB-COMMITTEE - 24 SEPTEMBER 2007**

**REPORT ON: 2006/07 INTERNAL AUDIT ANNUAL REPORT**

**REPORT BY: CHIEF INTERNAL AUDITOR**

**REPORT NO: 492-2007**

**1.0 PURPOSE OF REPORT**

To submit to Members of the Audit and Risk Management Sub-Committee the Internal Audit Annual Report for 2006/07 which summarises the activities of the Council's Internal Audit Service for this period and provides an opinion on the strength of the Council's control environment.

**2.0 RECOMMENDATIONS**

The Sub-Committee Members are asked to note the information contained within this report

**3.0 FINANCIAL IMPLICATIONS**

None

**4.0 MAIN TEXT**

**4.1.** Attached at Appendix A is a report pertaining to the Council's Internal Audit Service which provides a broad summary of the work carried out and circumstances that have impacted on the service during the 2006/07 financial year. For this period the actual days available for direct audit work totalled 1,195 compared to a budget of 1,160 days

**4.2.** In terms of the work undertaken in 2006/07, a total of 51 Internal Audit Reports have been drafted covering a wide range of systems across the Council. The Executive Summaries for these reports have been reported to the Members of the Audit and Risk Management Sub-Committee.

**5.0 POLICY IMPLICATIONS**

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

**6.0 CONSULTATIONS**

The Chief Executive and Head of Finance have been consulted on the content of this report.

**7.0 BACKGROUND PAPERS**

None

Sallie Dailly, Chief Internal Auditor

DATE: 13 September 2007

**2006/07 INTERNAL AUDIT ANNUAL REPORT****1 PURPOSE OF REPORT**

- 1.1 To summarise the activities of the Council's Internal Audit Service for the 2006/07 financial year.

**2 INTERNAL CONTROLS**

- 2.1 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 an authority.
- 2.2 That 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.
- 2.3 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**

- 3.1 Internal audit is an independent appraisal and review function which has been set up within Dundee City Council as a service to the Audit and Risk Management Sub-Committee, Chief Executive, Head 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.
- 3.2 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.
- 3.3 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.
- 3.4 Internal Audit has unrestricted access to all activities undertaken within the organisation in order to review, appraise and report on a wide range of areas which includes system reviews, computer audit work, location audits contract audit, specific investigations and advice on systems, controls and risk. The Internal Audit Service is also 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**

- 4.1 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.
- 4.2 The Internal Audit Annual Plan provides a summary of the audit reviews to be carried out during the forthcoming year. The Internal Audit Annual Plan for the 2006/07 financial year was approved by the Audit and Risk Management Sub-Committee in May 2006 (Report No. 320-2006).

## **5 AUDIT REPORTS**

- 5.1 Each audit assignment results in an internal audit report which details the audit findings, recommendations and management responses, if appropriate. The reports essentially provide management with an action plan which assigns responsibility and details the timetable for the implementation of audit recommendations.
- 5.2 The findings and recommendations arising from the audit reviews reported upon in 2006/07 have been discussed with appropriate officers of the Council and agreed action plans have been put in place to address areas for improvement.
- 5.3 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.

### **KEY EVENTS IMPACTING ON THE INTERNAL AUDIT SERVICE DURING 2006/07**

## **6 STAFFING LEVELS WITHIN THE INTERNAL AUDIT SERVICE**

- 6.1 For 2006/07 the Internal Audit Service establishment consisted of 9 posts namely that of the Chief Internal Auditor, Principal Internal Auditor, two Senior Internal Auditors and five Internal Auditors. During 2006/07 one of the Senior Internal Auditor Posts and one of the Internal Auditor Posts remained vacant throughout the year and the other Senior Internal Auditor Post was vacant until the end of November 2007. In order to maximise availability of resources due to vacant posts and staff absence and to assist in achieving the audit plan, temporary staff were appointed for predetermined periods during the first and last quarters of the financial year.

## **7 PLAN ACHIEVEMENT**

- 7.1 The following statistics have been collated from the internal audit management systems in relation to 2006/07 financial year:
  - 86% of the actual productive days was spent on direct audit activities, with the remaining 14% being spent on support activities such as management, audit planning, staff training and development. This is broadly in line with the figures for 2005/06.
  - Actual days available for audit reviews were 1,195 days against a budget of 1,160 days. Overall the days available for 2006/07 as compared to 2005/06 fell by approximately 12%. The figures for 2005/06 were 1,345 days and 1,330 days respectively. This decrease reflects the fact that it was anticipated at the time the audit plan was drafted that there would be posts that would remain unfilled during the financial year.
  - Work carried out during 2006/07 included of the order of 25 major reviews and 20 areas where advice on systems control and risk was provided or specific investigations were undertaken. This compares to 35 and 25 respectively for the previous financial year.
  - 51 internal audit reports have been prepared on the basis of the work undertaken and have generally been well received by departments with management agreeing to implement the vast majority of recommendations made. This compares to 45 for the previous financial year.
  - 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 system of internal financial control. In compiling this statement, a copy of which is attached at Appendix B, the Chief Internal Auditor has taken due recognition of the audit work carried out by the Service and other pertinent information.

## **8 OVERALL ASSESSMENT OF CONTROLS**

- 8.1 Work carried out during 2006/07 covered a wide spectrum of areas which included corporate governance, freedom of information, performance management and monitoring, cash collection and receipting, debtors and debt management, ordering, receipting and creditors' payments, general ledger systems, verification of grant claims and year end stocks and stores. There was internal audit coverage across most departments of the Council and work was also undertaken for the Tayside Valuation Joint Board.
- 8.2 The 2006/07 audit of corporate and departmental systems has identified that many of the expected controls are in place and operating satisfactorily in the areas examined. The audit work has, however, also identified scope for improvement in systems which either lack or have weaknesses in controls.
- 8.3 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 overall control environment.

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

As Chief Internal Auditor of Dundee City Council, I am pleased to present my annual statement on the adequacy and effectiveness of the internal control system of the Council for the year ended 31 March 2007. It should be noted that the statement does not include assurances on related group activities.

**Respective responsibilities of management and internal audit in relation to internal control**

It is the responsibility of the Council's Senior Management to determine, establish and maintain a sound system of internal control and to ensure that the organisation's resources are properly applied in a manner and on the activities intended. This includes responsibility for the prevention and detection of fraud. Senior Management is also charged with monitoring the continuing effectiveness of the internal control framework 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 internal control system within the Council.

**Sound internal controls**

The main objectives of the Council's internal control systems are as follows:

- To ensure adherence to management policies and directives in order to achieve the organisation's objectives.
- To safeguard assets.
- To secure the relevance, reliability and integrity of information, thereby ensuring as far as possible the completeness and accuracy of records.
- To ensure compliance with statutory requirements.

A sound system of internal control 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 systems of internal control.

**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 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 a risk-based annual audit plan which outlines the work to be undertaken. The plan and also any significant matters that may impact on the delivery of the plan or require changes to the plan are reported to the Audit and Risk Management Sub-Committee.

Internal audit 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 proper 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 Audit and Risk Management Sub-Committee, the Chief Executive and the Council's External Auditor

## **Summary of the 2006/07 internal audit activity**

The work carried out during 2006/07 included both major reviews and areas where advice on systems control and risk was provided or specific investigations were undertaken. A wide spectrum of areas were covered including corporate governance, freedom of information, risk management, debtors and debt management, cash collection and receipting, ordering, receipting and creditor payments, fixed assets and capital expenditure, statutory performance indicators, partnering, recruitment and selection, council tax recoveries, insurance and common good funds, establishment reviews, year end stocks and stores, grant claims and follow-up reviews.

The 2006/07 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.

## **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 internal audit during the year to 31 March 2007.
- The assessment of risk completed during the preparation of the audit plan.
- Reports issued by Audit Scotland, the Council's External Auditors 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.

## **Limitation of Scope**

Material transactions with related parties have not been dealt with as part of the Council for the purposes of this statement: The specific related parties include, Dundee City Developments Limited, Dundee Contemporary Arts Limited, Dundee Cultural Developments Limited, Dundee Energy Recycling Limited, Dundee Ice Arena Limited, Dundee Incubator Limited, Dundee Leisure Limited, Dovetail Enterprises (1993) Limited and Discovery Education Companies.

## **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 2007.

Sallie M. Dailly  
**Chief Internal Auditor**  
**Dundee City Council**  
**28 Crichton Street**  
**Dundee, DD1 3RF**

**DATE**      **25 June 2007**