

**REPORT TO: SCRUTINY COMMITTEE - 24 AUGUST 2011**

**REPORT ON: 2010/11 INTERNAL AUDIT ANNUAL REPORT**

**REPORT BY: CHIEF INTERNAL AUDITOR**

**REPORT NO: 384-2011**

## **1.0 PURPOSE OF REPORT**

To submit to Members of the Scrutiny Committee the Internal Audit Annual Report for 2010/11 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 2010/11 financial year and at Appendix B is a summary of the Internal Audit Reports issued during the same period.

**4.2.** On an annual basis the Chief Internal Auditor is also required, to prepare a statement which provides an opinion 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 Chief Internal Auditor's statement for the 2010/11 financial year is attached at Appendix C.

## **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: 08 August 2011

## 2010/11 INTERNAL AUDIT ANNUAL REPORT

### 1. PURPOSE OF REPORT

- To summarise the key areas of activity undertaken by the Council's Internal Audit Service and highlight any matters of significance that have arisen as a result of the audit process during the 2010/11 financial year.
- To provide an independent opinion on the adequacy and effectiveness of the systems of internal control based on the work undertaken during the 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, 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, best value is achieved and that cognisance is taken of the risk associated with each area.
- 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 2010/11 financial year was submitted to the former Audit and Risk Management Sub-Committee in

January 2010 (Report No. 48-2010). 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 enables the external auditor to utilise work carried out by internal audit to inform the year end accounts process where applicable and allows 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 2010/11 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 either the Scrutiny Committee or 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 to the Scrutiny Committee and the relevant Officers of the Council.

## **6. KEY EVENTS DURING 2010/11**

- During the course of planning and delivering the specific projects included within the 2010/11 Internal Audit Plan it became increasingly evident that in line with all other public sector bodies, the Council was facing major challenges. In order to ensure that internal audit continued to provide an effective service during this period of significant change it was essential to identify the key concerns of managers. In particular cognisance would require to be taken of the planned organisational restructure, remodelling of service delivery, relocation of staff, introduction of new working practices and the prevailing economic climate facing the Council. It was recognised that an increased consultative approach was required at the audit planning stage and the Chief Internal Auditor set up a series of meetings with key stakeholders to identify significant areas of risk where reviews would be beneficial.
- The consultation exercise which underpinned the compilation of the 2011/12 Internal Audit Plan was initiated at the Management Team (Operational Issues) in late January 2011 and thereafter meetings were held with various management teams and other key stakeholders such as Audit Scotland. Of the order of sixty stakeholders were consulted and the outcomes from this exercise assisted in informing the reviews to be included in the 2011/12 Internal Audit Plan submitted to the Scrutiny Committee in June 2011.

## **7. PLAN ACHIEVEMENT**

- During 2010/11 the actual number of productive days for the Internal Audit Service was 1,296. This represented a shortfall of 7% on the budgeted productive days due to staff vacancies which were not anticipated at the time the 2010/11 Internal Audit Plan was compiled. 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. This was in line with the previous financial year.

- In respect of the Council, the 2010/11 Internal Audit Annual Plan included 32 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 2009/10, provision of advice to clients on systems, control and risk and specific investigations. In addition, the plan contained allocations for the provision of internal audit services to external bodies namely Tay Road Bridge Joint Board and Tayside Valuation Joint Board. However due to the promotion of one of the Senior Internal Auditors to a post within another section of the Finance Department and the non-filling of the resulting vacancy it was agreed that this work would be undertaken by an external provider of internal audit services.
- As previously noted there was a shortfall in the actual productive days available during 2010/11. Despite this work on the majority of the planned areas for corporate and departmental reviews for Dundee City Council included within the plan commenced in 2010/11. However the planned reviews in Information Technology and Risk Management were deferred until 2011/12 as a result of the shortfall in available days and also at the request of the client Department.

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

- Internal Audit activity for the Council during 2010/11 covered a wide spectrum of areas including business continuity planning, electronic payments, income collection, major contracts, mobile phones, public private partnership, sundry payments, statutory performance indicators, control self assessment, establishment reviews, housing benefit overpayments, meals service, portable assets, property management, rent recovery, school transport, stocks and stores (including year end work), grant claims and follow-up reviews. The wide range of subject matter covered reflects the changing nature of Internal Audit and the move from merely financial audits to audits which review Council policies and areas of good governance.
- The 2010/11 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.
- For financial year 2010/11, 39 internal audit reports were issued. Reports have generally been well received by clients with management agreeing to implement 100% of recommendations made. Details of the reports issued and key information pertaining to these is attached at Appendix B.
- Analysis of the overall audit opinion for the reports issued highlighted that 13% of the areas reported upon were considered to be well controlled (full assurance), 62% were adequately controlled (reduced assurance) and 25% 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. It is recognised that maintaining this position and ensuring the effective implementation of sound controls will be increasingly challenging for Officers as the Council's Changing for the Future Programme is taken forward.
- 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 C, 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 2011 the overall audit opinion reached was that reasonable assurance could be placed on the Council's internal control system.

## Summary of Internal Audit Reports Issued during the 2010/11 Financial Year

Report No.	Area Reviewed	Level of Assurance	Recommendations			
			Total No.	Importance		
				Critical	Significant	Routine
2009/14	Property Management	R	3	-	-	3
2009/28	Online Payments (Finance)	R	2	-	-	2
2009/30	Meals Service	L	3	-	3	-
2009/32	Housing Benefits Overpayments	R	2	-	-	2
2009/33	Business Continuity	L	3	-	3	-
2009/34	Authority Purchasing	L	2	-	2	-
2009/35	Cash Imprests	R	5	-	-	5
2009/36	School Transport	R	4	-	-	4
2009/37	Sundry Payments	R	4	-	-	4
2009/39	Major Contracts	R	1	-	1	-
2009/40	Energy Management	R	6	-	6	-
2009/42	Control Self Assessment	R	1	-	-	1
2009/43	Penalty Charge Notice Evader Vehicle Uplift Scheme	L	2	-	1	1
2009/44	Online Payments (Information Technology)	R	3	-	-	3
2010/01	Nursery Fees	R	7	1	1	5
2010/02	School Placing Requests	R	4	-	3	1
2010/03	Pensions for Former Employees of List D Schools	F	-	-	-	-
2010/04	Rent Recovery	R	2	-	1	1
2010/05	Telecommunications - Mobile Phones	L	6	-	5	1
2010/06	Completeness of Data Fields in Resourcelink	R	2	-	1	1
2010/07	Business Credit Cards	R	2	-	1	1
2010/08	Assessment of Debtors' Income and Expenditure	R	1	-	-	1
2010/09	Benefits Sanction Policy	R	1	-	-	1
2010/11	Service Level Agreements (Finance)	F	-	-	-	-
2010/12	Public Private Partnership - Operational Phase	R	2	-	2	-
2010/14	Authority Purchasing - General Ledger	L	1	-	1	-
2010/15	Attendance Management (Primary Schools)	F	-	-	-	-
2010/16	Fuel Management (Camperdown Park)	F	-	-	-	-
2010/17	2009/10 Grant Claim: Cycling, Walking & Safer Streets	F	-	-	-	-
2010/19	Council Tax Refunds	R	3	-	-	3
2010/20	Cash Collection at Golf Courses	R	3	-	-	3
2010/21	Performance Indicators (Finance)	R	4	-	3	1
2010/22	2009/10 Performance Indicators (Housing)	R	1	-	1	-
2010/23	2009/10 Performance Indicators (City Development)	R	1	-	1	-
2010/25	Establishment Reviews	R	1	-	-	1
2010/26	BACS	L	5	-	4	1
2010/28	Management of Portable Assets - Contract Services	L	2	-	1	1
2010/29	Management of Portable Assets - Land Services	L	2	-	-	2
2010/30	Camperdown Wildlife Centre - Cash Handling	L	1	-	1	-

KEY : Level of Assurance

Full

Reduced

Limited

No

## **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 for the year ended 31 March 2011. 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 Scrutiny Committee. The Scrutiny Committee subsumed the former Audit and Risk Management Sub-Committee in June 2010.

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 ensure that agreed action plans have been implemented. Matters arising from internal audit work are also reported to the Council's Scrutiny Committee, the Chief Executive and the Council's External Auditor.

### **Summary of 2010/11 Internal Audit Activity**

During 2010/11 financial year a total of 39 internal audit reports were issued. These covered a wide spectrum of areas including business continuity planning, electronic payments, income collection, major contracts, mobile phones, public private partnership, sundry payments, statutory performance indicators, control self assessment, establishment reviews, housing benefit overpayments, meals service, portable assets, property management, rent recovery, school transport, 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 2010/11 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 2011.
- 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 for the year to 31 March 2011.

*Sallie M. Dailly*

**Chief Internal Auditor  
Dundee City Council**

**DATE**

**27 June 2011**