

APPENDIX 1



Annual Report

2006/07

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Introduction

The Accounts and Audit Regulations 2003 and subsequent CIPFA Code of Practice for Internal Audit in Local Government (the Code) require Internal Audit to report annually to *'those charged with governance'* on their findings and conclusions and provide an overall opinion on the adequacy and effectiveness of the internal control environment. This opinion is also significant in support of the Statement of Internal Control which is a statutory requirement of the Act.

In order to give validity to this opinion Internal Audit must be managed and conducted in accordance with 'proper internal audit practices' and therefore the first part of this report contains a self-assessment on the Section's compliance with the key elements of the Code of Practice and a summary of the performance of the Section during 2006/07. The second part of the report provides a summary of the results of audit assignments and my overall opinion on the internal control environment.

It is important to be aware that the system of internal control is designed to manage risk to a reasonable level rather than eliminate it altogether and therefore this report and my opinion can provide only reasonable assurance on the effectiveness of internal control.

The overall opinion contained in this report is my own, which I have prepared without fear or favour and which is based upon the findings of internal audit work carried out throughout the 2006/07 financial year.

PART 1

1. CIPFA Code of Practice

1.1 The Code is recognised by the Accounts and Audit Regulations as the definition for 'proper audit practices' and consists of eleven standards. Only when internal audit work is managed and conducted in accordance with the Code can it be deemed as being of sufficient quality to inform an annual report and the Council's Statement of Internal Control. Where internal audit is not managed or operated in accordance with the Code then the reliability of opinions and the level of assurance provided may be compromised.

1.2 In December 2006 CIPFA issued a revised and updated Code of Practice which included one new standard and additional requirement within existing standards. The 2006 Code also include a checklist for assessment against the standards which is more prescriptive in the evidential requirements for full compliance.

2. Self-assessment against the Code of Practice

2.1 I have performed a self assessment of Internal Audit's compliance with the Code using the checklist provided and my findings are as follows.

	Standard	Assessment
1	Scope of Internal Audit	Compliance
2	Independence	Compliance
3	Ethics for Internal Auditors	Compliance
4	Audit Committees	Compliance
5	Relationships	Partial Compliance
6	Staffing, Training and Continuing Professional Development	Compliance
7	Audit Strategy and Planning	Partial Compliance
8	Undertaking Audit Work	Partial Compliance
9	Due professional care	Compliance
10	Reporting	Partial Compliance
11	Performance, Quality and Effectiveness	Compliance

2.2 The result of my self-assessment is that Chester-le-street Internal Audit Section is **WORKING TOWARDS** full compliance with the eleven standards of the CIPFA Code of Practice for Internal Audit 2006.

2.3 I must stress that Internal Audit were fully compliant with the previous code of practice and that the areas where the section does not fully comply with the standards are minor matters in relation to the new or more prescriptive requirements of the 2006 Code.

2.4 An Action Plan to achieve full compliance has been developed and is incorporated within the Internal Audit Service Plan; progress will be monitored by the Audit Committee.

3. External Audit Review

3.1 During 2006/07 the Audit Commission carried out a review of Internal Audit in order to assess whether they can place reliance upon our work and contribution to the Statement on Internal Control (SIC).

3.2 The overall conclusion of this assessment was that they are satisfied that the Council has appropriate constitutional and management arrangements in place for the internal audit service. However there were recommendations made as part of the audit and the implementation of these have been incorporated within the Internal Audit Service Plan.

4. Quality assurance

4.1 In order to ensure consistency and compliance with professional standards and audit procedures, all audit work is reviewed and signed off by the Chief Internal Auditor at appropriate stages throughout the audit. The purpose of the review is to ensure that:

- the objectives of the audit have been fulfilled and that the conclusions are sound and are demonstrably supported by relevant, reliable and sufficient audit evidence.
- all work undertaken complies with the requirements of professional best practice and appropriate audit techniques have been used
- audit files are complete and properly structured
- the related audit report is complete, accurate, objective, clear, concise, constructive and timely
- the audit assignment has been completed within the allocated time budgets or that appropriate time variations have been authorised.

4.2 All internal audit staff have a Personal Development Plan in accordance with the corporate policy and procedure and all identified training needs have either been met or will be met during 2007/08. Team meetings and one-to-one sessions to discuss progress on audit assignments and emerging issues are held regularly.

4.3 Internal Audit processes and procedures are currently under review as part of the actions to ensure compliance with the Code of Practice; as a result a bespoke audit manual is currently under development and will be introduced in a phased approach during the year.

5. Customer Surveys

5.1 Although the essential criteria for measuring the quality of internal audit are the standards contained in the CIPFA Code of Practice, the views of customers is essential to service improvement and I have consulted with our customers in two ways.

- Customer Perception Survey
- Post Audit Questionnaire

5.2 The results of both surveys were very positive and show that the customer base is confident in the quality of the internal audit service and the professionalism of the auditors.

5.3 The perception survey did reveal that there is a lack of awareness the nature and function of the Audit Committee. An action plan to address this, as well as other less significant issues raised by the survey has been agreed and required actions are included, where appropriate, in the Internal Audit Service Plan.

PART 2

6. Internal Audit performance against the 2006/7 Audit Plan

6.1 The performance of Internal Audit against the Audit Plan is reported on a quarterly basis to the Audit Committee.

Activity	Planned	Actual
Planned audits	490	309
Investigations & advice		108
Management	151	159
Corporate activities	75	92
Total productive days	716	668
Non productive	184	232
Total available days	900	900

6.2 Performance against the audit plan for 2006/07 was affected by investigative work, sickness within the section and the commitment by all audit staff to take part in the organisational development programme. Nevertheless the section still delivered 93% of the number of productive days, although the number of planned audits actually completed was reduced. The audit work plan was continually reviewed during the course of the year to ensure that all core and high-risk financial systems were covered and to limit the slippage in the planned work to lower risk and non-financial areas.

7. Performance indicators

7.1 Internal Audit set 11 local performance indicators in its 2006/09 Service Plan and monitors 3 indicators on a quarterly basis. The results for 2006/07 are as follows:

Performance Indicator	Target	Out turn
Percentage achievement of the 2005 Audit Plan	90%	85%
Percentage of productive days	60%	54%
Percentage of recommendations agreed	80%	98%

7.2 The further 8 local performance indicators have been included in the 2006/09 Service Plan and will be collected and monitored during 2007/08.

Performance Indicator	Target
Compliance with CIPFA Code of Practice	Compliance
PDPs completed on time	100%
% variance from budget	0%
Post Audit satisfaction	85%
Customer satisfaction	85%
% usage of CAATS in audits	70%
Audits addressing risks from Risk Register	30%
% days for consultancy	15%

8. Results of audit assignments

8.1 On conclusion of each assignment a report is produced which evaluates the control environment under review and gives one of four opinions on the effectiveness of the control environment. These opinions are discussed and agreed with the relevant manager and they are: 1- ineffective, 2- adequate, 3- effective and 4-strong.

8.2 During 2006/07 Internal Audit have given the following opinions:

Score and opinion 2005/06		Audit assignment	Score and opinion 2006/07	
MATERIAL SYSTEMS				
3	Effective	Housing Benefits & Rent Allowances	4	Strong
3	Effective	Cash & Banking	3	Effective

2	Adequate	Council Tax and NDR	3	Effective
2	Adequate	Accounts Payable (Creditors)	2	Adequate
2	Adequate	Accounts Receivable(Debtors)	3	Effective
2	Adequate	Main Accounting	3	Effective
4	Strong	Rent Collection & Accounting	4	Strong
3	Effective	Best Value Performance Indicators		Not yet complete
3	Effective	Loans and investments	4	Strong
2	Adequate	Payroll	3	Effective
3	Effective	IT Controls		Not yet complete
2.6		MATERIAL SYSTEMS AVERAGE	3.2	
		IT Disaster Recovery	3	Effective
		Car Park Income	2	Adequate
		Industrial Units	2	Adequate
		OVERALL AVERAGE	3	

9. Internal Audit Recommendations

9.1 During 2006/07 Internal Audit made 87 recommendations (77 in 2005/06) to address identified weaknesses in internal control and all of these were initially accepted by managers however during the year one recommendation was subsequently disputed on implementation.

9.2 Audit Committee has received quarterly update reports on the implementation of recommendations. In circumstances where agreed actions have not taken place Audit Committee has sought assurance by inviting managers to attend special meetings to discuss the issues and agreeing actions to address the risk exposure.

10. Investigations

10.1 During the year Internal Audit have reacted to 4 allegations of irregularity (3 in 2005/06), of which only 1 was dismissed through lack of evidence. Two were pursued and dealt with as disciplinary action and the third referred to the police and another investigative body for further investigation, this is still ongoing.

11. Advice and consultancy service

11.1 Internal Audit acts in an advisory capacity and during the year have replied to 32 requests for advice (57 in 2006). In the main this advice still relates to advice on the requirements of the Financial Regulations and Standing Orders relating to Contracts but advice on other issues such as consultation on policy and procedure development and more general issues of internal control have also been provided.

12. Key findings and qualifications

12.1 There are no particular issues arising from internal audit assignments that, in my opinion, are significant enough to be considered as part of the Statement on Internal Control.

12.2 No system of internal control can provide absolute assurance against material misstatement or loss and nor can Internal Audit give that assurance. This statement is designed to provide reasonable assurance on the adequacy of the control environment.

12.3 Failure to comply with the Code of Practice for would usually be an appropriate qualification to my opinion but given the circumstances outlined previously I do not think it appropriate to attach such a qualification at this time.

13. Overall Opinion

13.1 Based upon the results of the audit assignments carried out during 2006/07 my opinion is that the internal control environment has improved to a position where it is both **ADEQUATE** and **EFFECTIVE**.

13.2 I am satisfied that there are sufficient and robust action plans in place to rectify the weaknesses that have been identified and I am confident that the Audit Committee will support my actions to ensure that those plans are implemented as agreed.

Jacqueline McConnell
Chief Internal Auditor