

CITY OF DURHAM

AUDIT OVERVIEW COMMITTEE

6th APRIL 2006

REPORT OF DIRECTOR OF STRATEGIC RESOURCES

1. PROGRESS REPORT FOR THE PERIOD 1ST APRIL 2005 TO 28TH FEBRUARY 2006

1.1 Introduction

This report will compare the actual work undertaken by Internal Audit with that planned for the period 1st April 2005 to 28th February 2006.

1.2 Progress Report

1.2.1 In the period 1st April 2005 to 28th February 2006, the following work was undertaken and compares to the plan as shown below:

Annual Plan Audit Days		Cumulative Planned Audit Days	Cumulative Actual Audit Days	Variance Audit Days
445.50	Non productive time	410.73	369.87	(40.86)
183.00	Management & Administration non chargeable	167.75	194.10	26.35
89.00	Management & Administration chargeable	81.58	55.57	(26.01)
625.50	2005/2006 Audit Plan	625.50*	455.96	(169.54)
40.00	Follow Up work	40.00	39.87	(0.13)
120.00	Contingencies & Special Investigations	110.00	180.77	70.77
1503.00	Total	1435.56	1296.14	(139.42)

A more detailed analysis is given in Appendix 'A'. Where items of concern have been specifically highlighted for your attention.

*Please note that the audit plan is broken down into quarters, therefore at the start of the final quarter in the year (1st January) the cumulative planned audit days for the year for all planned audits will be fully allocated. The audit variance only takes account of actual audit days worked until the end of February and this will be reduced in the out-turn plan by the audit days worked throughout the month of March.

- 1.2.2 The original 2005/2006 Audit Plan is comprised of 80 specific audit assignments. At the 28th February 2006, 29 assignments (36.25%) had been completed of which 7 were at the draft stage. Of the 9 assignments covering the main financial systems, 7 have been completed, 2 to draft stage, with the remaining 2 expected to be completed towards the end of March 2006. It is anticipated that a total of 45 audits will be completed by the end of the year, this will be the same number that were completed in 2004/05 although the percentage of audits completed in relation to the original plan will reduce from 72% in 2004/05 to 56.25% in 2005/06. This is a direct result of the job shadowing carried out as part of the training requirements for new staff previously reported. It is inevitable that some of these assignments will be finalised in 2006/07 and time in respect of such work will be taken from the contingency provision.
- 1.2.3 The number of audit days spent on audit assignments in 2005/06 is expected to be 575 (92%) approximately, this compares to 452 (82%) in 2004/05
- 1.2.4 As previously reported it has been agreed with relevant Heads of Service to delete 3 audit assignments from the plan - these relate to bonus, recycling and markets and reflect the amended operational responsibilities of each department. 1 additional assignment for subscriptions has been added which has now been completed.
- 1.2.5 There are also a number of minor changes to the plan as follows:-
- ◆ Housing benefit performance standards was delayed due to an inspection by the Benefit Fraud Inspectorate in October and November 2005. This audit is now underway and should be completed by the end of March 2006.
 - ◆ Salaries and wages have been combined into one single audit, with a new combined target of 25 audit days.
 - ◆ BACS has now been fully implemented, however It is anticipated that this audit will be carried forward to 2006/07
 - ◆ Freedom of Information/Data Protection – Work only carried out on the Freedom of Information aspect of this audit. Data protection will be carried forward to 2006/07.
 - ◆ Stores (VFM) - a delay to this audit was requested by the department, to allow them to finalise the business plan in respect of this service. This audit will now be carried forward to 2006/07
 - ◆ RIPA – As this policy is currently under review by Legal and Administrative Services the audit will not be carried out until the policy has been approved and implemented. This audit will now be carried forward to 2006/07.
 - ◆ Food Safety and Hygiene – This audit has been split over a number of headings, for 2005/06 these were Registration, Inspection and sampling. Other audits under this heading will be carried forward to future years assessed on the basis of risk.
 - ◆ Travelling expenses – this audit has been extended to include unfinished work on Conferences and Seminars carried forward from 2004/05. Target audit days have therefore been increased to reflect this from six days to fifteen days.

- ◆ Money Laundering – This audit has been delayed due to the need to review and update the existing policy. This audit will be carried forward to future years.
- ◆ High Level Action Plan – This audit has been carried forward to 2006/07
- ◆ Durham City Arts – this audit was delayed at the client's request due to staffing problems.
- ◆ Citizens Advice – This audit has been completed to draft stage, but we are awaiting the results of a public satisfaction survey, before finalising the audit. It is anticipated that the final audit will be issued in May 2006.
- ◆ Complaints – The policy in respect of complaints is presently under review, therefore this audit will be carried forward to future years.
- ◆ Fleet management and vehicle maintenance have been combined into a single audit, with a new combined target of 15 audit days.

1.2.6 The shortfall of 139.42 audit days shown in the above table is the result of a delay in filling vacant posts during the current year as previously reported, the unusual high levels of sickness this year and the time spent by audit staff with bank and income reconciliation during the year.

1.2.7 A temporary experienced Agency worker has been appointed and commenced work on the 16th January 2006. He has been tasked with 3 fairly large audits including fleet management and vehicle maintenance, Housing Benefits, and Micro-computing. All 3 audits should be completed by the end of his fixed term contract on the 31st March 2006.

1.2.8 In total 24.83 days have been spent completing a number of audits relating to the 2004 / 2005 audit plan. This has been met from the contingency provision. All work in this respect has been completed, apart from the audit relating to Conferences and Seminars which will now be carried out as part of the audit on travelling expenses in 2005/06 as mentioned above.

1.2.9 A number of projects over the year not included in the original audit plan have been carried out. All of this work has been met from the contingency provision and the main areas examined are summarised below: -

- ◆ Interviews for Audit and Accountancy posts (5.74 days) This includes interviews carried out with Agency staff in December 2005 and January 2006.
- ◆ Preparation of Business plan for Internal Audit and review of other service business plans (6.29 days)
- ◆ Accounting Year end and Bank reconciliation's (78.64 days). This exercise has involved a lengthy reconciliation process of the cash receipting and income management system, balancing receipts both to the bank, to control funds and to FMS to satisfy queries raised by the Audit Commission. Additional work has also been carried out to embed new processes and procedures to prevent future problems.
- ◆ Development of data base to support audit follow ups and performance management (9.39 days)

- ◆ The preparation of key controls for all systems to assist Heads of Service in offering assurance on internal controls that informs the end of year statement of Internal control.
- ◆ Benefit Fraud Inspectorate (3.55)
- ◆ Data matching and cleansing of data transferred from Northgate to SX3.

1.2.10 Further audit awareness training and training in the completion of the control risk self assessment form for Heads of Service will take place in 2006/07

1.2.11 The following local performance indicators for the period 1st April 2005 to the 30th November 2005 are shown below:-

i) Number of audits undertaken and complete	29 (7 at draft stage)
ii) Number of recommendations made	172
iii) Number of recommendations agreed	167 (97%)
iv) Number of recommendations not agreed	0
v) Number of recommendations partly agreed	5 (3%)
vi) CPA target - % of Audit Plan completed (audit time)	72.90%
vii) Number of draft reports issued within 10 working days of closure meeting	36.67%
viii) Number of final reports issued within 5 working days of the post audit meeting	86.67%
ix) Number of recommendation action plans signed off and returned within 5 working days of issue	12.50%

1.2.12 Recommendations partly agreed are shown in Appendix B

1.2.13 There are no recommendations not agreed

1.2.14 There will be four more LPI's added with effect from 1/04/2006, namely:-

- ◆ Number of recommendations implemented
- ◆ Number of Post Audit Questionnaires completed and returned
- ◆ Post audit meeting to be held within 10 working days of the issue of the draft report
- ◆ Final report and recommendation action plan to be issued within 3 working days of the agreement of the draft report and recommendation action list.

The compulsory return of Post Audit Questionnaires has been agreed and these will be closely monitored in 2006/07.

1.3 2005/2006 Audits Completed (excluding items already reported)

1.3.1 Internal audit reviewed the following systems where given the nature of the risks involved in the achievement of the control objectives, key controls and other parts of the internal control system are working effectively and provides full assurance that risks material to the achievement of the control objectives are adequately managed.

◆ CCTV

A very well run Service, main recommendations included CRB checks for staff, the need for written protocols for contingency arrangements; and confidentiality of information. All recommendations were agreed and accepted by management.

1.3.2 Internal audit reviewed the following systems where key controls and other parts of the internal control system provide reasonable assurance that the control objectives will be achieved. Some corrective action is required. These audits have been assessed as satisfactory and awarded an audit opinion score of three.

◆ Play-schemes

Main recommendations related to the improvement of some written procedures, appropriate retention of documents, recording of cheques, incident reporting and adequate insurance cover. All recommendations were agreed and accepted by management.

1.3.3 Internal audit reviewed the following systems where given the nature of the risks involved in the achievement of the control objectives, neither the key controls or the other parts of the internal control system are working effectively, and some corrective action is needed in both areas. This provides only limited assurance that risks material to the achievement of the control objectives are adequately managed.

◆ Abbey Sports Centre

Main recommendations included cashing up procedures, stocktaking procedures, and adherence to financial regulations. All recommendations were agreed and accepted by management.

1.3.4 Internal audit reviewed the following systems where key controls and other parts of the internal control system are inadequate and provide little or no assurance that the control objectives will be achieved. Significant corrective action is required in both areas. These audits have been assessed as unsatisfactory and awarded an audit opinion score of five.

◆ Homelessness (Operational)

A number of recommendations were made including; the importance of obtaining and retaining evidence to support an applicants eligibility; periodic checks on control book accuracy; staff training; recording and storage of information; health and safety concerns at homelessness units; revision of application form in line with best practice; retention of evidence regarding the monitoring and review of work; and that all homelessness officers should be required to undertake a criminal records bureau disclosure check. All recommendations have been accepted by management.

◆ Cash collection

Main recommendations were in respect of security, standardisation of documentation, training, procedures for collection and banking, including under and over-bankings. All recommendations have been accepted by management.

◆ Housing Rents

Recommendations included, an urgent review of access permissions, adherence to financial regulations, written procedure notes, and separation of duties. All recommendations have been accepted by management.

1.3.5 Four further reviews were carried out, which did not require an audit opinion.

◆ Benefits Accuracy Q3 and Q4

Internal Audit undertakes a quarterly review of the accuracy of benefit claims. These aim to meet three objectives:

- Completion of the Department for Work and Pensions Stats 128 Return.
- Enable client management to monitor performance against BVPI 79a
- Enable client management to monitor performance against the standards of evidence requirements of the Verification Framework

The Q3 audit identified that 125 of the 125 (100%) determinations were compliant with the Verification Framework Requirements.

For Q4 audit identified that 123 of the 125 (98.4%) determinations were compliant with the Verification Framework Requirements.

◆ Financial Management System Feeders

This audit was carried out to identify and map all systems which fed into the main financial system. Each feeder system was then examined to highlight any log-jams, or inefficient working methods, to enable the process to be streamlined for efficiency purposes.

Recommendations were made in respect of absence coverage, timeliness of information, minor amendments to charging policy, and the use of electronic information.

◆ Subscriptions

This audit was used to identify the number of regular subscriptions that had previously been set up by the Authority over the years, with a clear remit to critically evaluate and challenge the necessity for subscriptions in the future. Recommendations included amendments to the system for paying subscriptions, and the identification of a number of efficiency savings.

1.4 2006/2007 Annual Audit Plan

1.4.1 Best practice in relation to the Audit Planning process is changing, and measures to improve the process in line with the new requirements are outlined below.

1.4.2 The Audit Strategy

The audit strategy is the high-level statement of how the Internal Audit service will be delivered and developed.

The audit strategy comprises two parts. The first part deals with how the service will be delivered, and the second part of the strategy deals with the more detailed plan of the assignments to be carried out during the period of the plan.

Historically, Internal Audit has produced a strategic audit plan that attempts to identify the audit environment and then, on a cyclical basis, determined over what period of time every part of the audit environment is subjected to an audit review. For example, a risk assessment would determine which systems would be audited on an annual basis, which would be audited every two years, and so on. Increasingly this approach is losing favour and being replaced by a process called continuous planning. This involves an in-year assessment of risk that effectively makes a strategic (say, five-year) plan redundant. In short, unless the subject of an audit review is considered to be a key risk, there is little point in planning to provide audit coverage in three or four years' time.

The focus of internal audit has changed fundamentally in recent years and its role and planning process must now embrace the provision of independent assurances over risk management (that is that risk exposures are understood and are being managed to an acceptable level). In fulfilling this role, Internal Audit must methodically review and provide an opinion on the :-

- ◆ Design and operation of the risk management process
- ◆ Responses from management adopted to reduce risks to an acceptable level
- ◆ Adequacy and effectiveness of the system of internal control in sufficiently mitigating risks

Effective internal audit also remains an agent for the promotion and implementation of best practices and process improvements in the management of risks.

It is my intention to move towards a continuous planning, risk based strategy over the next few years. To facilitate this properly, however, a knowledge of the Council's strategy, objectives and targets, a sound understanding of the environment in which it operates, and the challenges that the Council faces; as well as the effective identification, analysis and management of risks faced by the Council is required. To introduce such a process, there must be fully established links between the Council's corporate objectives via its Corporate Plan and Performance plan, its strategic and operational business plans, and its strategic and operational risks. The risks identified in this way will be used to inform the audit plan and the level of audit coverage for the year. This will be in addition to the areas identified by the Audit Commission which are already subject to annual review.

As the Council's business plans have not yet been fully completed, and risk management processes not yet fully embedded the plan for 2006/07 will be mainly based on the existing audit risk matrix. The Plan will consist of all identified critical business systems agreed with the Audit Commission as a result of the new International standards on auditing (see later), any specific requests from Heads of Service, and other audits (based on their level of risk) that can be accommodated in the audit time available. It is anticipated that all items currently identified as low risk will be removed from the plan unless the Head of Service has any specific objections to this. When business plans and strategic and operational risk registers have been fully implemented, some of these low risk items may well be re-classified and brought back into the planning process where necessary.

- 1.4.3 Details of the plan have been circulated for consultation in accordance with the Audit Charter and best practice. A copy of the plan is attached at Appendix C. Late advice by the Audit Commission regarding the new International Standards on Auditing has led to a delay in the audit planning process for 2006/07. This has prevented the Head of Internal Audit from meeting with Heads of Service to discuss the plan in detail, however copies of the draft plan have been circulated to all relevant senior managers for comment. All comments and feedback have been taken into account when compiling this years final plan. A copy of the final plan has also been provided to the Audit Commission.
- 1.4.4 For the first time in 3 years the section will be fully staffed at the commencement of the new financial year. It is hoped that a period of stability will reflect an increase in the number of audits completed in 2006/07.
- 1.4.5 The Internal Audit staffing structure is shown below: -
- ◆ Head of Internal Audit
 - ◆ Principal Auditor (with responsibility for IT)
 - ◆ Principal Auditor (with responsibility for VFM)
 - ◆ Auditor
 - ◆ Auditor
 - ◆ Audit Assistant
- 1.4.6 The plan is based on the availability of 620 audit days, of which 40 audit days have been set aside for follow up work. This leaves a total of 580 audit days, a reduction of 45.5 days on the previous year. The number of audits to be carried out, total 68.
- 1.4.7 The plan will be split into quarters and work will be distributed as far as possible on this basis.

- 1.4.8 A contingency provision of 150 audit days has been set. This will cover any special investigation work and additional work required by departments not included in the plan. A further contingency of 30 days has been set to cover any vacancies that may arise during the year. As in previous years a reserve list of audits has been compiled to be carried out should the contingency provision not be used up over the course of the year. By increasing the provisions for vacancies and sickness, within the section, the level of audit work required (68 audit assignments, 580 audit days) has been set at a more realistic and achievable level and gives the section more flexibility to deal with any unexpected events should they arise.
- 1.4.9 The Chief Executive, Executive Director and Heads of Service have also been asked to review areas of auditable activity that is considered to be of such a low risk that any audit review would be of little value to the Authority. These areas will be removed from the strategic and annual plan for future years. It is important to recognise, however, that managers will still be responsible for ensuring that internal controls in these areas are still working effectively.

1.5 Service Improvements

- 1.5.1 In accordance with Best Value guidelines, and in line with the CPA, City of Durham Internal Audit is striving to continuously improve our service to users.
- 1.5.2 New procedures, regarding the follow up of audit work carried out and recommendations made, implemented during 2005/06 have been relatively successful once the section was fully staffed.

However, managers must ensure that responses to follow up audits must be timely, and must contain a clear explanation of why any recommendation has not been implemented. Heads of Service must also agree and provide a new implementation date, to enable internal audit to update their follow up data base which will impact upon future follow up audits.

- 1.5.3 The audit plan will be split into quarters, and managers notified at the beginning of the year of the anticipated start date. Managers are requested to table internal audit work into their calendars to enable them to plan audit work well in advance.
- 1.5.4 Following a meeting of the Business Plan working group it was suggested that the return of post audit questionnaires should be compulsory, and this has been incorporated into the audit plan and local performance indicators which will also include the following.
- i) Draft report to be issued within 10 working days from the closure meeting of the audit.
 - ii) Post audit meeting to be held within 10 working days of the issue of the draft report
 - iii) Final report and recommendation action plan, to be issued within 3 working days of the agreement of the draft report and recommendation action plan.
 - iv) Recommendation action plan to be signed off by lead officer and returned to Internal Audit within 5 working days of issue.
 - v) Return of post audit questionnaires.

For this to be achievable line managers must be willing to prioritise audit reports and ensure that they make the necessary time available. All local PI's will be reported to OMT and the Audit Overview Committee, together with details of the most persistent offenders.

- 1.5.5 To facilitate the increasing importance of the risk management process, governance arrangements and the introduction of the statement of internal control, as well as the publication by CIPFA of a new standard procedures manual, Durham City Council's Internal Audit Procedures manual will be reviewed and where appropriate updated to reflect recent legislative changes and current best practice.
- 1.5.6 Audit awareness training was carried out for a number of Services in 2005/06. Further training will be carried out in 2006/07 for those officers and members who wish to take advantage of this training. In addition some training on how to complete the control risk self assessment form will also be carried out.
- 1.5.7 Good working relationships with departments is important to Internal Audit. Managers have a number of ways in which they can communicate their opinions on the internal audit service.
- ◆ Post audit questionnaire
 - ◆ Consultation process for the audit plan
 - ◆ Annual audit survey
 - ◆ In person to the Head of Internal Audit.

Managers are actively encouraged to provide feedback on any part of the audit process. Without this feedback it is difficult for Internal Audit to provide continuous improvement to its quality service.

- 1.5.8 Heads of Service are asked to provide the Head of Internal Audit with the names of lead officers and the department/section for areas of responsibility before the start of the new financial year.

Changes to working practices

- 1.5.9 Following criticism of internal audit by the Audit Commission regarding their involvement in assessing and approving access to major computer systems and the impact that this has on audit independence has led to the need for new arrangements to be introduced for 2006/07.

It will now be the responsibility of individual Heads of Service (or their designated line manager) to assess and approve access to computer systems under their area of responsibility. They will then need to communicate this information to the IT section, who will continue to amend and set up access rights as required.

Internal audit will continue to review access rights to computer systems as part of the normal audit process.

Policies and Procedures

1.5.10 In addition to the work outlined in the audit plan, it is proposed that the Head of Internal Audit will compile, finalise and review a number of policies and procedures throughout the year to reflect changes in legislation, and best practice.

The main areas of work will be: -

- ◆ Quality procedures manual (revise)
- ◆ Retention and Disposal Policy (revise)
- ◆ Audit Charter (revise)
- ◆ Confidential reporting policy (revise)
- ◆ Fraud and Corruption policy (revise)
- ◆ Fraud Response plan (revise)

2. AUDIT 2004/05 SAS610 REPORTING

The above letter from the Audit Commission is attached at Appendix D.

3. CITY OF DURHAM COUNCIL – USE OF RESOURCES JUDGEMENT

The above document from the Audit Commission is attached at Appendix E.
We are still awaiting the full report, and this will be reported to Audit Overview in due course together with an action plan to address all of the issues raised.

4. RECOMMENDATIONS

- i) The Audit Overview Committee is asked to note the contents of this report.
- ii) The Audit Overview Committee is asked to approve the audit plan for 2006/07