Audit Committee

31 May 2013

**Internal Audit Progress Report
Quarter Ended 31ˢᵗ March 2013**

Durham
County Council

Report of Manager of Internal Audit & Risk

PURPOSE OF THE REPORT

1   The purpose of this report is to inform Members of work carried out by Internal Audit during the period July 2012 to March 2013.

2   The report aims to:

- Provide a high level of assurance, or otherwise, on internal controls operated across the Council that have been subject to audit

- Advise you of significant issues where controls need to improve to effectively manage risks

- Advise you of any other types of audit work carried out such as grant certification or consultancy reviews where an assurance on the control environment may not be applicable

- Advise you of amendments to planned work

- Advise you of unplanned work carried out or to be carried out

- Track progress on the response to audit reports and the implementation of agreed audit recommendations

- Advise you of any changes to the audit process

- Provide an update on our performance indicators comparing actual performance against planned

3   Appendices attached to this report are summarised below. Those marked with an asterisk are not for publication (Exempt information under Part 3 of Schedule 12a to the Local Government Act 1972, paragraph 3.)

Appendix 1   Report Implications
Appendix 2   Background to preparation and approval of the 2012/13 plan
Appendix 3   Audit methodology
Appendix 4   Progress on plan
Appendix 5   Final reports issued this quarter
Appendix 6   High and medium priority actions raised and implemented
Appendix 7   *Overdue actions
Appendix 8   Performance Indicators

BACKGROUND

4   Internal Audit is an independent, objective assurance and consultancy activity designed to add value and improve an organisation's operations.

5   The background to the preparation and approval of the 2012/13 annual audit plan and the approved risk based audit strategy to be applied to deliver it is attached at Appendix 2.

6   The audit methodology used to determine the risk priority for addressing audit findings and how we arrive at our assurance opinion is given in Appendix 3.

PROGRESS AGAINST PLANNED WORK

7   A summary of the approved annual plan for each service grouping, updated to reflect work in progress and/or brought forward from last year's plan, is attached at Appendix 4. The status of each audit as at 31st March 2013 is indicated.

8   The status of each type of planned audit, as shown in Appendix 4, is summarised below:

Status	Assurance	Advice & Consultancy	Counter Fraud
Not Yet Started	5	3	5
Planning & Preparation	14	0	4
TOR agreed	10	1	2
Fieldwork in progress	13	15	3
Complete (draft or final report stage)	61	11	3
Postponed	1	0	0
Agreed Defer/Cancelled	13	1	0
Total	**117**	**31**	**17**

9   Where work is finalised the resultant assurance opinion, if applicable, is also shown in Appendix 4.

10   A summary of final audit reports issued this quarter is given in Appendix 5.

SIGNIFICANT ISSUES ARISING THIS QUARTER

Amendments to the approved 2012/13 Audit Plan

11   The following amendments to planned work have been agreed with Corporate Directors this quarter:

Service Grouping	Audit	Audit Type	Type of Amendment	Reason
ACE	Business Continuity Planning (BCP)	Assurance	Defer	ACE has commenced a new project to review business continuity arrangements. New procedures not expected to be in place until later in 2013.
CAS	Children's and Families Trust	Assurance	Defer	The Service is to review the joint working arrangements

Service Grouping	Audit	Audit Type	Type of Amendment	Reason
				relating to the governance of the Children and Families Trust. Audit review to be deferred until 2013/14 and considered as part of the rolling programme of assurance on significant partnerships agreed following the annual self-assessment exercise co-ordinated by ACE each year (Part of the Corporate Partnership Governance Framework).
	Personalisation	Assurance	Defer	The risks associated with Personalisation have been assessed and reduced following confirmation that the resource allocation process for commissioned services was not going to be subject to fundamental change. Internal Audit has already reviewed and reported upon processes associated with Direct Payments. The Service is to look again however at its arrangements in this area through its transformational change programme and Internal Audit will agree with responsible managers a timeframe when a review of these revised arrangements would be undertaken.
	School Surplus / deficit Balances	Assurance	Defer	Arrangements in place to support and challenge schools on their use of balances are currently being reviewed by the service. The effectiveness of these new arrangements will be reviewed in 2013/14.
RED	Visit County Durham County	Assurance	Defer	Service request to defer to 2013/14
	Development Control – Mystery Shopping to test compliance and consistency of procedures	Advice & Consultancy	Defer	Service request to defer to 2013/14 pending implementation of staff movements
	Markets	Assurance	Defer	The service is currently developing the management models required to deliver the the market strategy. Review of new arrangements deferred to 2013/14
RES	Oracle EBS	Assurance	Defer	Service request to defer as the new system (upgrade) is now planned to be implemented in Feb2014.

Service Grouping	Audit	Audit Type	Type of Amendment	Reason
	Card Terminal	Assurance	Defer	A gap analysis on PCI compliance is to be carried out by the service. It was agreed to defer the audit so that assurance can be provided on progress made in implementing the agreed action plan during 2013/14.
	Contract Register	Assurance	Cancel	Work planned has been incorporated into the scope of the Counter Fraud review of the award of contracts
	Information Security Policy Review – Systems development and management	Assurance	Cancel	The scope of the review of Forensic Readiness has been widened to include a review of Systems Development & Maintenance.
	Information Security Policy Review – Security Incident Management	Assurance	Cancel	The scope of the Public Services Network assurance review has been widened to include a review of the framework for managing information security.
	Information Security Policy Review – Warranty	Assurance	Cancel	The scope of the Public Services Network assurance review has been widened to include a review of the framework for managing information security.

12   18 unplanned reviews have been added to the plan this quarter. Of these 16 relate to potential fraud or irregularity investigations. Details of progress on all investigations will be provided in the 6 monthly fraud and irregularity update that will be reported to the next meeting of the Committee on 27 June 2012.

13   The 2 unplanned reviews which have been added to plan from the contingency provision within the plan are:

Service Grouping	Audit	Audit Type
ACE	Business Continuity Planning Project Support	Advice & Consultancy
NS	Verification of payments made to Competition Line (Leisure Services Partner) to fulfil contract obligations of Income Sharing Agreement	Advice & Consultancy

Outstanding Management Responses to Draft Reports

14   Responses to the following draft reports were overdue as at 31 March 2013

Service Grouping	Audit	Date Issued	Key Contact	Assurance Opinion	Comment
CAS	Procurement in Schools	30 Oct 2012	Head of Education	Moderate	IA progressing matters with Corporate Procurement and School Funding Managers.
	PARIS System	4 Oct 2012	Strategic Manager Performance and Systems	Substantial	Service requesting response from TEWV Partner before report can be finalised

Response to audit findings and recommendations

15   Details of the numbers of High and Medium priority ranking recommendations raised and overdue, by Service Grouping and Audit Year, are given in Appendix 6. A summary of progress on actions due by the 31 March 2013 is given below:

Service	Actions Due by 31/03/13	Overdue Actions by Original Target Dates		Overdue Actions where revised date agreed		Revised overdue actions	
		No	%	No	%	No	%
ACE	9	1	11	1	100	0	0
CAS	137	12	9	8	67	7	8
NS	414	42	10	21	50	25	6
RED	300	7	2	7	100	0	0
RES	353	14	4	14	100	0	0
TOTAL	**1213**	**76**	**6**	**51**	**67**	**32**	**3**

16   Your attention is drawn to the 32 actions, which are overdue by either their original date or their revised date, where this has been set. These are highlighted in bold in Appendix 7.

17   Those recommendations reported last quarter as overdue, where revised target implementation dates have still not been agreed and are therefore still overdue, are highlighted in bold italics.

Limited / No Assurance Opinion Audits

18   There were no audits finalised this quarter that resulted in a Limited or no assurance opinion.

PERFORMANCE INDICATORS

19 A summary of our actual performance at the end of March 2013 compared to agreed target performance indicators is given in Appendix 8.

20 This is the third quarter of the 2012/13 audit plan (July 2012 - June 2013). 61 out of 117 planned assurance reviews are complete. Work has commenced on another 31 which on average are estimated to be 48% complete. 13 reviews have been deferred/cancelled in agreement with management. Consequently of the 104 reviews planned to be complete 30 June, the annual target to deliver 90% after 9 months is on track. However some slippage on delivery is expected in the final quarter due to a reduction in the forecast of audit days available for the rest of the year.

21 The resource gap is being managed through a combination of agency staff and/or work being allocated to external partners. Following a procurement exercise, Audit North has been appointed as our IT audit partner wef April 2013. Our existing contract with PriceWaterhouseCoopers has also been extended for a further 12 months to allow completion of planned work for the Pension Fund and any additional ad hoc service support.

RECOMMENDATIONS

22 Members are asked to note,:

- The amendments made to the 2012/13 Annual Audit Plan
- Work undertaken by Internal Audit during the quarter ended March 2013 and
- Note the progress made by service managers in responding to the work of Internal Audit

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Appendix 1: Implications

Finance

There are no direct financial implications arising for the Council as a result of this report, although we aim through our audit planning arrangements to review core systems in operation and ensure through our broad programme of work that the Council has made safe and efficient arrangements for the proper administration of its financial affairs.

Staffing

None

Risk

This report requires no decision and so a risk assessment has not been carried out

Equality and Diversity

None

Accommodation

None

Crime and disorder

None

Human rights

None

Consultation

None

Procurement

None

Disability Discrimination Act

None

Legal Implications

None

Background to the preparation of the 2012/13 Annual Audit Plan

1   The 2012/13 annual audit plan was developed in consultation with each service grouping's senior management team and was endorsed by CMT and the Audit Committee on the 6th June 2012 and the 28th June 2012 respectively.

2   The planned assurance work included in the plan reflects the agreed audit strategy to review each key service activity and each key system over a five year rolling programme.   In applying a risk based approach we aim to support managers embed operational/inherent risk management through the development of Control Risk Assessments (CRAs).

3   Through the development of CRAs in consultation with nominated key contacts, as part of the planning and preparation stage of each planned assurance review, we will add value by helping service managers to:

- Identify and assess risks

- Document service objectives, risks and existing controls

- Assess the adequacy of the existing control framework (control design) and identify additional controls to improve operational risk management and /or highlight controls that are unnecessary

- Identify and assess the reliability of assurance provided from other sources to avoid any unnecessary duplication and highlight any assurance gaps

4   Through independent testing of expected controls we add value by providing reliable and objective assurance that controls established by managers are operating in practice and that they are effective in reducing the likelihood and / or impact of agreed risks occurring.

5   Through the identification and assessment of operational risks we are also able to add value to the strategic risk management process. This is done by providing assurance that controls identified to manage strategic risks are both adequate and effective. Potential new or emerging strategic risks may also be identified.

6   Applying a risk based audit approach ensures that audit resources are focused on the right things.   The planning and preparation stage of each audit review with the right key contact(s) is essential. It is not until this planning and preparation stage is complete that we can determine the scope and timing of each audit.

7   Following initial planning and preparation discussions, draft terms of reference specifying the proposed scope of each audit will be issued for the agreement of the key contact.   The planned start date (fieldwork) and planned completion date (issue of draft report) will also be shown. It should be noted

that wherever possible any timing preferences expressed by service managers at the audit planning and preparation stage will be considered when determining planned start dates but these cannot be guaranteed.

8   Confirmation of actual start dates and expected completion dates will be given to key contacts prior to fieldwork commencing. It should be noted that these timescales are subject to the following assumptions:

- All relevant documentation, including source data, reports and procedures will be made available promptly on request
- Staff and management will make reasonable time available for interviews and will promptly follow-up questions or requests for documentation and
- Assistance will be available in scheduling meetings and interviews where required

9   Should audit staff not be able to commence the fieldwork as planned, the key contact will be advised accordingly. Wherever possible advance notice will be given but there may be circumstances when this cannot be done e.g unplanned leave of absence. Likewise, we request that should a key contact become aware of something that may prevent the fieldwork starting as planned that they immediately let us know so that if necessary audit resources can be reallocated.

10   Should any problems be encountered in progressing an audit these will be reported to the relevant head of service and /or the Corporate Director, and if necessary the Audit Committee.

11   In accordance with our Internal Audit Charter, we will give an assurance opinion on the effectiveness of internal controls each time we complete an assurance review.

12   The % of planned assurance reviews completed is monitored through the Council's quarterly performance reporting framework and is challenged by the Audit Committee. Failure to deliver the agreed plan may prevent an annual audit opinion being given and the Council failing to meet its statutory requirements. It will also delay the embedding of operational risk management exposing the Council to potential greater risk.

13   It is managers' responsibility to ensure that effective controls operate within their service areas. To provide independent assurance that adequate progress is made in the implementation of agreed recommendations at the appropriate service operational level, all high and medium recommendations contained within actions plans within individual audit reports are followed up by internal audit. The method of audit follow up will vary according to the priority of the recommendation. In addition, listings of all recommendations outstanding at the end of each month are produced and issued to nominated representatives to assist managements own internal monitoring processes.

14   Audit recommendations are allocated a priority ranking reflecting the significance of the audit findings to which they relate.

Findings

Individual findings are assessed on their impact and likelihood based on the assessment rationale in the tables below:

Impact Rating	Assessment Rationale
Critical	**A finding that could have a:**
	Critical impact on operational performance (Significant disruption to service delivery)
	Critical monetary or financial statement impact (In excess of 5% of service income or expenditure budget)
	Critical breach in laws ands regulations that could result in significant fine and consequences (Intervention by regulatory body or failure to maintain existing status under inspection regime)
	Critical impact on the reputation of the Council (Significant reputational damage with partners/central government and/or significant number of complaints from service users)
	Critical impact on the wellbeing of employees or the public (Loss of life/serious injury to employees or the public)
Major	**A finding that could have a:**
	Major impact on operational performance (Disruption to service delivery)
	Major monetary or financial statement impact (1-5% of service income or expenditure budget)
	Major breach in laws, regulations or internal policies and procedures (non compliance will have major impact on operational performance, monetary or financial statement impact or reputation of the service)
	Major impact on the reputation of the service within the Council and/or complaints from service users
Minor	**A finding that could have a:**
	Minor impact on operational performance (Very little or no disruption to service delivery)
	Minor monetary or financial statement impact (less than 1% of service income or expenditure budget)
	Minor breach in internal policies and procedures (non compliance will have very little or no impact on operational performance, monetary of financial statement impact or reputation of the service)

Likelihood	Assessment criteria
Probable	Highly likely that the event will occur (>50% chance of occurring)
Possible	Reasonable likelihood that the event will occur (10% - 50% chance of occurring)
Unlikely	The event is not expected to occur (<10% chance of occurring)

Overall Finding Rating

This grid is used to determine the overall finding rating.

LIKELIHOOD			
Probable	M	H	H
Possible	L	M	H
Unlikely	L	L	L
	Minor	Major	Critical
	IMPACT		

Priority of our recommendations

We define the priority of our recommendations arising from each overall finding as follows;

High	Action that is considered imperative to ensure that the service/system/process objectives are not exposed to **significant risk** from weaknesses in critical or key controls
Medium	Action required to ensure that the service/system/process objectives are not exposed to **major risk** from weaknesses in controls
Low	Action required to ensure that the service/system/process objectives is not exposed to **minor risk** from weaknesses in controls
Advisory	Action that is considered desirable to address minor weaknesses in control that if implemented may not reduce the impact or likelihood or a risk occurring but should result in enhanced control or better value for money.

Overall Assurance Opinion

Based upon the ratings of findings and recommendations arising during the audit as summarised in risk matrix above we define the overall conclusion of the audit through the following assurance opinions:

Full Assurance	There is a sound system of control designed to achieve the process/system/service objectives and manage the risks to achieving those objectives. (No H, M or L findings/recommendations)
Substantial Assurance	Whilst there is a sound system of control, there are some weaknesses, which may put some of the system objectives at minor risk. (No H or M findings/recommendations)
Moderate Assurance	Whilst there is basically a sound system of control, there are some weaknesses, which may put some of the system objectives at major risk. (No H findings/recommendations)
Limited Assurance	There are weaknesses in key areas in the system of control, which put the system objectives at significant risk.(H findings/recommendations)
No Assurance	Control is weak as controls in numerous key areas are ineffective leaving the system open to significant risk of error or abuse