

**MAIDSTONE BOROUGH COUNCIL**

**AUDIT COMMITTEE**

**MONDAY 15 JULY 2013**

**REPORT OF HEAD OF INTERNAL AUDIT PARTNERSHIP**

**Report prepared by Brian Parsons**

**1. INTERNAL AUDIT ANNUAL REPORT 2012/13**

1.1 Issue for Decision

1.1.1 The report is provided in order to allow the Audit Committee to consider the work of the Internal Audit Team over the financial year 2012/13 and the opinion of the Head of Audit Partnership in relation to the Council's control environment, in the context of the Annual Governance Statement.

1.1.2 The Audit Committee must consider whether the outcomes of the Internal Audit work and the other matters referred to in this report provide evidence of a substantial level of internal control within the Authority, which can inform the Annual Governance Statement for 2012/13.

1.1.3 The Audit Committee must decide whether the matters referred to in the report provide evidence of an effective internal audit.

1.2 Recommendations of Head of Audit Partnership

1.2.1 That the Audit Committee note the Head of Audit Partnership's opinion that substantial reliance can be placed on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control.

1.2.2 That the Committee note the results of the work of the Internal Audit Team over the period April 2012 to March 2013, as shown in the report and the appendices and that this is the prime source for the Head of Internal Audit's opinion.

1.2.3 That the Committee agree that the summary of the work and the other matters referred to in this report supports 'the opinion' and that the report can be used to inform the Annual Governance Statement for 2012/13.

1.2.4 That the Committee note the improvements in control that occur as a result of the audit process.

1.2.5 That the Committee consider the effectiveness of the Internal Audit service as part of the consideration of this report, and express an opinion accordingly.

### 1.3 Reasons for Recommendation

#### **Background**

1.3.1 Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes. A professional, independent and objective internal audit service is one of the key elements of good governance, as recognised throughout the UK public sector.

1.3.2 The principal objective of the Internal Audit Service is to examine and evaluate the adequacy of internal control within the various systems, procedures and processes that are operated by the Council. The results of the work allow an opinion to be formed on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

1.3.3 The report allows Members to consider the outcomes of the work of the Internal Audit Team over the financial year 2012/13 and the opinion of the Head of Internal Audit in relation to the Council's framework of governance, risk management and control and whether the report can be used to inform the Annual Governance Statement for 2012/13.

1.3.4 The report provides an opportunity for the Audit Committee to assess the effectiveness of the Council's internal audit arrangements.

#### **The Public Sector Internal Audit Standards**

1.3.5 A report on the new Public Sector Internal Audit Standards was provided to the Audit Committee meeting on 25 March 2013. The Standards became effective from 1 April 2013. This report has therefore been written to reflect the requirements which necessitate that:

- The chief audit executive must confirm to the board, at least annually, the organisational independence of the internal audit activity.
- The chief audit executive must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement.
- The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.
- The annual report must incorporate:
  - the opinion;
  - a summary of the work that supports the opinion; and
  - a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.
- Progress against any improvement plans, agreed following external assessment, must be reported in the annual report.

## **The Annual Internal Audit Report**

### **Independence**

- 1.3.6 Internal Audit is provided through Mid Kent Audit, which is a shared service partnership between Ashford, Maidstone, Swale and Tunbridge Wells.
- 1.3.7 Independence is the freedom from conditions that threaten the ability of the internal audit activity to carry out internal audit responsibilities in an unbiased manner.
- 1.3.8 At Maidstone Borough Council, the Head of Audit Partnership (HAP) has direct and unrestricted access to senior management and the Audit Committee. Reports to Heads of Service are issued in the name of the HAP who is responsible for the final content of the report.
- 1.3.9 Any potential threats to independence are managed at the individual auditors, engagement, functional and organisational levels.
- 1.3.10 Organisationally the Head of Audit Partnership now reports to the Director of Environmental and Shared Services who is a member of the Corporate Leadership Team (CLT). Previously the Head of Audit Partnership reported to the Chief Executive. On no occasion has the Director, the Chief Executive or CLT sought to restrict the scope of audit work or to change any report prepared by the HAP.
- 1.3.11 It is considered that Internal Audit is organisationally independent and fully meets the necessary standard for independence and objectivity.

### **The annual internal audit opinion**

- 1.3.12 It is the opinion of the Head of Audit Partnership that substantial reliance can be placed on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control. This opinion covers the period from 1 April 2012 to date.
- 1.3.13 The opinion takes account of all related projects including the reliance on other assurance providers; principally the external auditors Grant Thornton (and previously the assurance provided by the Audit Commission).
- 1.3.14 The opinion takes account of the risk, control and governance framework.
- 1.3.15 The evidence to support the opinion is contained within this report. The opinion and this report can be used by the Council to inform its governance statement.
- 1.3.16 The Annual Governance Statement appears elsewhere on the agenda for this evenings meeting.
- 1.3.17 The Accounts and Audit Regulations 2011 also require that the Council 'must, at least once a year, conduct a review of the effectiveness of its internal audit'. It is considered that this report provides evidence of the effectiveness of internal audit and the Committee is therefore asked to treat consideration of this report as 'the review'.

### **Summary of the work that supports the opinion**

- 1.3.18 The opinion on the control environment is principally formed through the results of Internal Audit work during the financial year.
- 1.3.19 The equivalent of thirty-two significant audit projects were completed between April 2012 and March 2013, as listed at Appendix A.
- 1.3.20 The original audit plan showed thirty-six projects but was reduced to thirty-four to acknowledge that a post within the audit team was vacant for two months.
- 1.3.21 Thirty-two completed projects represent the delivery of 94% of the adjusted audit plan.
- 1.3.22 Appendix B shows an audit where at the time of the audit 'limited' control assurance was in place.

1.3.23 Appendix C shows the audit projects where at the time of the audit, 'substantial' or 'high' levels of control assurance was in place.

1.3.24 The *equivalent* of eleven of the audit projects did not include a control assurance assessment as it was not appropriate to the project at the time of the audit. These projects were:

- A review of the fundraising arrangements for the Maidstone Museum East Wing development (treated as the equivalent of two projects)
- A consultancy review aimed at improving the financial reporting arrangement for Park and Ride
- The co-ordination of the National Fraud Initiative on behalf of the Council
- A 'governance review' of the Council's Scrutiny arrangements, working with the Head of Change and Scrutiny
- Fraud review – an analysis of the performance of the fraud teams across the four partner authorities to assist the consideration of the potential creation of a shared service partnership fraud team
- Risk Management Policy Review
- Teammate administration – an ongoing project for the administration of the Teammate audit management system
- Teammate development – improving the functionality of the system
- Investigation – following an apparent breach of the rules relating to the Government Connect Secure eXtranet
- Investigations at Tunbridge Wells (this was 'repaid' by an audit by a TWBC auditor at Maidstone)

1.3.25 Summaries of these projects and 'other audit work' are shown at Appendix D.

1.3.26 The work of the Internal Audit Team has established that for the majority (95%) of the areas examined (where an assurance opinion was given), satisfactory controls were in place at the time of the original audit.

1.3.27 Where weaknesses have been identified, the appropriate Head of Service has since agreed the action to be taken to rectify those weaknesses.

1.3.28 The external auditors have been able to place reliance on the work of Internal Audit.

### **The results of external audit work during 2012/13**

1.3.29 The main part of the external auditor's work relates to the Council's financial accounts. The auditors will be considering the accounts for 2012/13 shortly. The External Auditor has not raised any issues with

Internal Audit that would give concern in relation to the Council's internal controls.

1.3.30 The external auditor's Annual Governance report for 2011/12 (which was reported to the meeting of the Audit Committee on 17 September 2012), included the statement 'I have not identified any significant weaknesses in internal control'.

### **The Council's risk management arrangements**

1.3.31 A revised Strategic Risk Register was adopted by Cabinet at its meeting on 13 February 2013.

1.3.32 The current register shows six risks, being:

- Having the right resources which are used in the right way
- Resident satisfaction with place and the way that services are provided
- Economic downturn/austerity agenda
- Creating the place we want to be
- Delivering services in partnership with others
- Impacts arising from political change

1.3.33 The risk management process requires that the allocated 'risk owners' must complete management action plans, which are subject to review and amendment every six months.

1.3.34 The process of obtaining management action plans commenced in March 2013. However, there was a limited response from the respective 'risk owners' at that time in terms of creating action plans. It is therefore proposed that the process will be recommenced in July, with a view to reporting the action plans to Cabinet in August and to the Audit Committee in September.

1.3.35 Internal Audit takes the role of facilitators of the risk management process but do not have responsibility for the individual risks or for the corporate risk register.

### **The effectiveness of internal audit process**

1.3.36 Heads of Service are required to respond to every audit report where recommendations are made, by completing an action plan which sets out the action that will be taken to address the audit recommendations. The response is assessed for adequacy; to ensure that the proposed actions are sufficient and that any weakness will be addressed within a reasonable period.

- 1.3.37 Only one report was issued during 2012/13 relating to an area where a 'limited' control assurance was assessed as being in place. The responsible Head of Service subsequently completed an action plan setting out comprehensive and timely actions to address the audit recommendations.
- 1.3.38 Internal Audit carries out a follow-up to each audit to ensure that actions have been taken in practice.
- 1.3.39 Twenty-four follow-ups took place during 2012/13. These are shown at Appendix E, which also shows the 'direction of travel', i.e. the improvements in control that occur as a result of the internal audit process.
- 1.3.40 Based on the generally prompt and positive responses received from senior management and the results of follow-up work, it is considered that senior management is effective in resolving control weaknesses.
- 1.3.41 It is considered that the internal audit process is effective.

### **Informing the Annual Governance Statement (AGS)**

- 1.3.42 The opinion of the Head of Internal Audit on the internal control environment is particularly relevant to the preparation of the Annual Governance Statement. In that context, it is not considered that there are any significant internal controls issues which are still outstanding and need to be referred to as outstanding control weaknesses in the AGS.

### **Performance of the internal audit function against its performance measures and targets**

- 1.3.43 During 2012/13 the internal audit function had two principal internal performance targets. The targets were:  
Completion of the annual internal audit plan (90% target)  
Achievement of customer care targets (85% positive response target)
- 1.3.44 The revised target for completion of audit projects within the internal audit plan for 2012/13 was 34 projects. In practice the number of projects completed during 2012/13 was 32, which is a 94% achievement of the plan and a performance in excess of the set target.
- 1.3.45 Customer surveys are issued to clients (service managers) following each internal audit to assess satisfaction with the audit service. The responses have been very positive. Positive levels of satisfaction help to confirm that customers/clients value the service that they receive

and the positive responses therefore provides evidence of 'value for money'

- 1.3.46 An annual survey of Chief Executives/Directors and Heads of Service is carried out across the four-way Internal Audit Partnership in order to obtain responses on the quality of the internal audit service. The most recent survey was carried out in June 2013.
- 1.3.47 The survey of the partner Chief Executives/Directors focuses on satisfaction with the overall service. Of the eleven responses received (which is all of those senior officers in this category), the answers to the question 'Are you satisfied with the service that you receive from Internal Audit', five were 'satisfied' and six were 'very satisfied'.
- 1.3.48 The survey of Heads of Service produced twenty-one responses over the four-way partnership, of which eight were 'satisfied' with the service and eleven were 'very satisfied' (two responders did not answer the question).
- 1.3.49 The survey of Heads of Service is quite detailed and includes questions on the quality of the various elements of the audit process. The main purpose of the survey is to identify aspects of the service that can be improved. The detailed responses will therefore be very carefully reviewed over the coming months and action will be taken to introduce improvements where appropriate.

**Statement on conformance with the Public Sector Internal Audit Standards (PSIAS) and the results of the quality assurance and improvement programme**

- 1.3.50 As stated earlier, the PSIAS has only been in place since 1 April 2013.
- 1.3.51 The PSIAS sets out the standards that the Internal Audit team has to comply with in order to meet the statutory requirement. A copy of the PSIAS has been provided to each auditor and each auditor has confirmed that they have 'read, understood and will work to the Public Sector Internal Audit Standards'.
- 1.3.52 The PSIAS requires that a Quality Assurance and Improvement Programme is in place. This requires both internal and external assessments. The internal assessments include ongoing monitoring of the performance of the internal audit activity, which is already in place, and 'periodic self-assessments or assessments by other persons within the organisation with sufficient knowledge of internal audit practices. CIPFA has recently published a 'Local Government Application Note for the United Kingdom Public Sector Internal Audit Standards', which includes a checklist. It is intended to use the



checklist to aid periodic self-assessments of conformance with the Standards.

1.3.53 The PSIAS also require that an external assessment must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the organisation. It is intended to seek an external assessment later in the year. The proposals for doing so will be reported to a future meeting of the Audit Committee.

1.3.54 The implementation of the PSIAS on 1 April 2013 means that aspects of the current service arrangement need to be changed in order to ensure full compliance. It is intended that the necessary actions will be taken during the current financial year so that the service will fully comply by 31 March 2014 at the latest. In particular, Internal Audit is required to operate to an approved Charter. It is intended that a draft Charter will be prepared and brought to the meeting of the Committee in September for approval.

#### **Assurance levels**

1.3.55 Internal Audit use 'assurance levels' or assurance statements to provide the overall audit opinion for the service or area that has been reviewed. The use of an assurance level is consistent with the requirement for managers (and Members) to consider the degree to which controls and processes can be relied upon to achieve the objectives of the reviewed activity. There are four assurance levels, as set out at Appendix F. The consistent use of assurance levels allows a balanced view to be taken of the overall adequacy of control within the Council.

1.3.56 In the financial year 2012/13, a total of twenty-one audit reports included an assurance assessment for the area that had been audited (the equivalent of eleven did not). The initial assurance assessments were categorised as follows:

	2012/13	Previous year
High	3	1
Substantial	17	21
Limited	1	7
Minimal	0	0
Not given	11	6
Total	32	35

1.3.57 The collective assurance level, which can be extracted from the audit work performed during 2012/13, provides considerable evidence to support the statutory Annual Governance Statement, with 96% of the

reports having a positive assurance assessment, identifying control assurance as 'substantial' or 'high' at the time of the audit.

### **Reporting of Internal Audit work to the Audit Committee**

1.3.58 Internal Audit work is reported at six-monthly intervals. An interim report, showing the first six months work of the financial year 2012/13, was provided to the Audit Committee meeting on 26 November 2012. A number of the audit projects shown in the appendices have therefore already been brought to the attention of the Committee.

### **Other issues - Staffing**

1.3.59 The team of operational auditors comprises three staff plus a management resource. Each auditor is expected to complete twelve audit projects during the year.

1.3.60 The management resource (which is shared across the audit partnership) is used for audit planning, review of audit reports, supervision of audit staff, strategic management, risk management, various aspects of governance and for reporting to the Audit Committee and the Corporate Leadership Team.

### **1.4 Alternative Action and why not Recommended**

1.4.1 The Audit Committee needs to have an awareness of the work of Internal Audit in the context of its Terms of Reference. The only alternative would be to provide a less detailed report; however this would be at odds with the Council's commitment to transparency.

### **1.5 Impact on Corporate Objectives**

1.5.1 The work of Internal Audit contributes to the quality of the Council's governance arrangements and helps to achieve the objective of Corporate and Customer Excellence.

### **1.6 Risk Management**

1.6.1 Internal Audit reviews the adequacy of the controls that are in place to manage risk. An ineffective Internal Audit service would mean that weaknesses in internal control are not identified or rectified.

1.6.2 It is considered that Internal Audit is effective.

## 1.7 Other Implications

### 1.7.1

1.	Financial	X
2.	Staffing	X
3.	Legal	X
4.	Equality Impact Needs Assessment	
5.	Environmental/Sustainable Development	
6.	Community Safety	
7.	Human Rights Act	
8.	Procurement	
9.	Asset Management	

1.7.2 Financial – The work of Internal Audit includes reviews of the main financial systems.

1.7.3 Staffing – The work of Internal Audit impacts on staffing issues and leads to changes in working practices.

1.7.4 Legal – There is a statutory requirement for the Council to undertake an adequate and effective internal audit of its accounting records and its system of internal control in accordance the proper practices in relation to internal controls (Accounts and Audit Regulations 2011).

## 1.8 Relevant Documents

### 1.8.1 Appendices

Appendix A – Audit projects completed between April 2012 and March 2013

Appendix B – Audit projects completed between April 2012 and March 2013 where controls were unsatisfactory

Appendix C – Audit projects completed between April 2012 and March 2013 where controls were satisfactory

Appendix D – Audit projects where the control assurance was not assessed – and 'other audit work'

Appendix E – Audit follow-ups during 2012/13

Appendix F – Assurance levels definition

1.8.2 Background Documents

1.8.3 None

<b><u>IS THIS A KEY DECISION REPORT?</u></b>		<b><u>THIS BOX MUST BE COMPLETED</u></b>	
Yes	<input type="checkbox"/>	No	<input checked="" type="checkbox"/>
If yes, this is a Key Decision because: .....			
.....			
Wards/Parishes affected: .....			
.....			