



**Report to: Audit Sub Committee**

**Subject: The Annual Internal Audit Report 2007-08**

**Date: 24<sup>th</sup> June 2008**

**Author: Manager of Resource Services**

## **1. PURPOSE OF THE REPORT**

To report on the activity of the Internal Audit section during the 2007-08 financial year.

This report will also provide assurance on the internal control systems across the Authority to support the Annual Governance Statement provided within the Annual Statement of Accounts.

## **2. BACKGROUND**

The Accounts and Audit Regulations 2003 (amended 2006), and the Code of Practice for Internal Audit in Local Government in the United Kingdom make detailed and specific requirements for the Annual Internal Audit report in support of the Annual Governance Statement. These requirements are:

“The Head of Internal Audit’s formal annual report to the organisation should:

- Include an opinion on the overall adequacy and effectiveness of the organisation’s internal control environment,
- Disclose any qualifications to that opinion, together with the reasons for the qualification,
- Present a summary of the audit work undertaken to formulate the opinion, including reliance placed on work by other assurance bodies,
- Draw attention to any issues the Head of Internal Audit judges particularly relevant to the preparation of the Annual Governance Statement,
- Compare the work actually undertaken with the work that was planned and summarise the performance of the Internal Audit function,

- Comment on compliance with these standards and communicate the results of the Internal Audit quality assurance programme”.

### **3. RECOMMENDATION**

The Annual Internal Audit report is attached at Appendix 1 and indicates that the Council’s systems and controls are generally operating adequately. This conclusion is of importance in reviewing and supporting the Annual Governance Statement in support of the Annual Statement of Accounts.

Members are requested to note the contents of the report.

## Appendix 1



GEDLING BOROUGH COUNCIL

Annual Report of the Internal Audit Service

2007-08

For presentation at the Senior Management Team (10<sup>th</sup> June 2008), Cabinet (19<sup>th</sup> June 2008) and the Audit Sub-Committee (24<sup>th</sup> June 2008)

Prepared by: Vince Rimmington, Manager of Resource Services  
Date: May 2008

# **1: Introduction**

## **The Role of the Internal Audit Service**

- 1.1 The role of the internal audit service is to provide management with an objective assessment of whether systems and controls are adequate and working effectively. It is a key part of the Gedling Borough Council's internal control system because it measures and evaluates the adequacy and effectiveness of controls so that:
- The Council and senior management are aware of the extent to which they can rely on the whole system of control; and
  - Individual managers are aware how reliable the systems and controls are for which they are responsible.
- 1.2 The internal control system comprises the whole network of systems and controls established to manage Gedling Borough Council to ensure that its objectives are achieved. It includes financial and other controls, and also arrangements for ensuring that Gedling Borough Council is achieving value for money from its activities.

## **Definition of Internal Audit**

- 1.3 The definition of internal audit, as described in the CIPFA's Code of Practice for Internal Audit in Local Government in the United Kingdom is set out below.
- Internal Audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment comprising risk management, control and governance 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.
  - Whilst Internal Audit "primarily" provides an independent and objective opinion to the organisation on the control environment, it may also undertake other, non-assurance work at the request of the organisation subject to the availability of skills and resources. This can include consultancy work; indeed, Internal Audit intrinsically delivers consultancy services when making recommendations for improvement arising from assurance work, and fraud-related activity.

## **Statement on Internal Control / Annual Governance Statement**

- 1.4 Under Regulation 4(2) of the accounts and Audit Regulations 2003, as amended by the Accounts and Audit (Amendment) (England) Regulations 2006, authorities are required to publish a Statement on Internal Control (SIC). From 2007-08, authorities should publish an Annual Governance Statement (AGS) in line with the CIPFA/SOLACE Good Governance Framework to meet that statutory requirement. The statement brings a number of benefits to government organisations, including:

- Increased awareness of internal controls and control weaknesses, and risk management among Section 151 Officers, Councillors and senior management,
- Greater awareness of the importance of risk identification and monitoring amongst staff at all levels,
- Better appreciation of the benefits of a strong internal audit function,
- Greater awareness of other internal and third party assurance sources that operate within the organisation and the importance of the role that they fulfil, and
- Increased and encouraged audit committee activity.

As Gedling Borough Council's internal audit provider, the assurance opinions provided in each audit review undertaken throughout the year are part of the framework of assurances that assist in the preparation of the Annual Governance Statement.

Our work for the 2007-08 financial year is summarised in this report, and we have highlighted in section 2.4 any specific issues that we are aware of and that should be reflected in the 2007-08 Annual Governance Statement.

## **Significant Events / Factors During the Year**

- 1.5 There have not been any significant events or factors during the financial year that have affected the extent of our internal audit work or needed to be addressed as part of our internal audit plan.

## **2: The Statement of Assurance**

### **Background**

- 2.1 As the provider of the internal audit service to Gedling Borough Council we are required to provide the Council with assurance on the whole system of internal control. In providing our opinion it should be noted that the level of assurance given can never be absolute. The internal audit service can only provide reasonable assurance that there are no major weaknesses in risk management, governance and control processes.

In arriving at the audit opinion, consideration has been given to:

- The results of all audits undertaken during the financial year,
- The results of follow-up action taken in respect of audits from previous years,
- Whether or not any high or medium risk recommendations have not been accepted by management and the consequential risks,
- The effects of any material changes in the organisation's objectives and activities,
- Any limitations have been placed on the scope of internal audit,
- Whether there have been any resource constraints imposed upon internal audit which may have impinged on our ability to meet the full internal audit needs of the organisation,
- The proportion of the organisation's internal audit requirements that have been covered to date.

### **2.2 Internal Audit Opinion**

Internal Audit are satisfied that sufficient internal audit activity has been undertaken to allow us to draw a reasonable conclusion as to the adequacy and effectiveness of Gedling Borough Council's risk management, governance and control processes.

It is internal audits opinion that, for the 12 months ending 31<sup>st</sup> March 2008, Gedling Borough Council has adequate and effective risk management, control and governance processes to manage and achieve the organisations objectives.

- 2.3 In reaching this opinion the following factors were taken into particular consideration:

### **Risk Management**

The Authority introduced a revised Risk Management Strategy during 2007-08. Key enhancements include the introduction of a standard approach (common language) to risk terminology, the formalisation of reporting procedures and the introduction of Key Performance Indicators to measure how effectively risks are being managed and the extent to which risk management procedures are embedded across the organisation.

Strategic and operational risk registers are reviewed bi-annually by management. All identified risks are aligned to the 11 corporate risks identified against the Authority's objectives. All audit recommendations are also aligned to these corporate risks, which, when considered with other internal and external sources of assurance, provide the Authority with an integrated and holistic assurance process.

The outcomes from these multiple assurance sources are consolidated into the Authority's Corporate Risk Scorecard and reported into the Senior Management Team and Audit Sub-Committee on a quarterly basis.

This approach provides a well-organised system and methodology to underpin the arrangements made by the organisation to address and mitigate the risks arising from its environment.

Overall, it is Internal Audit's opinion that Gedling Borough Council has adequate and effective risk management processes to manage the achievement of its business objectives.

### **Governance**

The CIPFA/SOLACE guidance note and framework - Corporate Governance in Local Government defined corporate governance in local authorities as "the system by which local authorities direct and control their functions and relate to their communities". The guidance issued a framework for local authorities and recommended that they draw up a Local Code of Corporate Governance.

Gedling Borough Council has established a Local Code of Corporate Governance and developed a Governance Framework based on the principles within the CIPFA/SOLACE guidance. The Framework is subject to an annual review, led by the S151 and Monitoring Officer, who produce a report for the consideration of members and senior managers.

In addition to the Governance Framework review signed Assurance Statements are obtained from all Section Heads, with specific statements made by the Chief Executive, Deputy Chief Executive, S151 Officer and the Monitoring Officer. The statements are based directly on assurances given with respect to compliance with Authority's Financial Regulations. Section Head's are encouraged to involve their section heads in the process, particularly where day-to-day responsibilities are delegated.

Overall, it is Internal Audit's opinion that Gedling Borough Council has adequate and effective governance processes to manage the achievement of its business objectives.

### **Internal Control**

A summary of Internal Audit activity during 2007-08 is provided in section 3.4.

Overall, it is Internal Audit's opinion that Gedling Borough Council has adequate and effective control processes to manage the achievement of its business objectives.

- 2.4 The overall internal audit opinion statement provided in section 2.2 should be used by the Authority in the preparation of the Annual Governance Statement.

The internal audit statement is further evidenced by external evaluators such as CPA inspection, the Use of Resources assessment, the Audit Commissions annual audit and inspection letter and other inspectorate reports such as the Planning Inspectorate.

During the 2007-08 financial year the following issues were identified via the Authorities risk management, governance and internal control processes as being relevant to the preparation of the Annual Governance Statement:

- **Register of Interests** - recommendations relating to the development of an Authority wide Register of Interests for Employee's have been addressed with the development of a policy. Once approved this will be rolled out across the authority with supporting guidelines.
- **Business Continuity Plan** - has been reviewed and updated. Resource requirements for all critical systems have been identified and a Disaster Recovery plan developed. A contract has been entered into with a third party supplier and neighbouring authorities to provide contingency arrangements. The contract includes the provision of an annual test of the recovery arrangements, with the first live test to be undertaken during quarter 2 of 2008-09.



- **LSVT** – following the comprehensive positive vote by the residents, a transfer date for November 2008 has been set. The authority will need to ensure it manages the benefits accruing from the transfer through effective cost absorption.
- **Partnership Risk** – the authority has identified its key partnerships and undertaken a risk assessment of these as part of its Risk Management process. The ongoing development of a formal partnership risk register will further enhance the governance arrangements associated with these.
- **Data Security** – recent high profile and well-publicised incidents of data loss and breaches has significantly raised awareness and concerns of data security issues. Whilst the authority has not experienced any significant data breaches, a Data Security Working Group has been established with the key objective of undertaking a thorough review of data security arrangements to provide assurance to members and officers that procedures are adequate and effective.

Action plans have been formulated to address the weaknesses identified and, once action has been fully implemented, will ensure that controls associated are adequate and operate effectively.

Internal Audit will monitor the progress of the action plans and evaluate the effectiveness of the actions in addressing the issues identified.

### **3: Audit Activity & Performance**

#### **The Resource Services Section**

- 3.1 The following are the established posts with the Resource Services Section:

Manager (F/T)  
Principal Internal Auditor (9.5 hours)  
Resource Management Officer (18.5 hours)  
Risk Management Administrator (F/T)  
Internal Auditors (2.5 FTE)

The activity of the section covers Corporate Governance, Risk Management, Insurance, Business Continuity Planning and Internal Audit.

Over the past four years the section has had a partnership arrangement with the County Council for the provision of Internal Audit work to ensure that the annual plan is achieved. The cost of this partnership arrangement has been met by vacancy savings in relation to the part time Principal Auditor post and 0.5 FTE Internal Auditor post.

The agreement for 2007-08 with the County was for 65 days of audit work to be undertaken. In addition, a vacancy at Internal Auditor level has continued throughout the year. Delivery of the audit plan within the financial budgetary limits was achieved by engaging RSM Bentley Jennison to provide 95 days of audit activity.

This approach to partnership work and co-sourcing audit resource will continue during 2008-09, as it provides the Authority with greater flexibility to meet the challenges ahead and access to a greater skill set and knowledge base.

#### **Effectiveness of Internal Audit**

- 3.2 The Audit Commission undertakes an annual review of the Internal Audit function and the quality of its work. When undertaking the review they ensure compliance with the CIPFA Code of Practice and, where relevant, make recommendations on how compliance can be improved or developed further.

In addition, the Audit Commission undertakes a detailed review of Internal Audit work every 3-4 years. This was last completed in July 2006. The Audit Commission identified no issues.

The Accounts and Audit (Amendment) (England) Regulations 2006 came into force on the 1<sup>st</sup> April 2006. Two of the amended regulations have an impact on the preparation of the Annual Governance Statement.

Regulation 6 requires the Authority to undertake an annual review of the effectiveness of their system of internal audit, and under Regulation 4 for the findings of the review to be considered by a committee of the Authority (or by the Authority as a whole).

A review of the Authority's system of internal audit was completed during April/May 2008. The review comprised a self-assessment against the standards outlined in the CIPFA Code of Practice. The individual criteria within the standards were prioritised into 4 levels to provide a formal conclusion and a benchmark comparator to monitor future progress.

The review was completed by the Authority's Chief Financial Officer, Chair of the Audit Sub Committee and via an external peer review conducted by the Audit Manager at Mansfield District Council.

The review concluded that:

"Following completion of the self-assessment and peer review process, it is considered that the system of internal audit is operating to an excellent professional standard and is providing a good level of effectiveness for the Authority. Overall performance is considered to be excellent, with robust plans in place to further enhance the effectiveness of the service".

This represents an improvement on the conclusion reached during 2006-07, with the professional standard opinion moving from a good to an excellent, resulting in an overall improvement from a good to an excellent rating. A summary of the review is provided in **Appendix A**.

### **Analysis of Audit Activity 2007-08**

- 3.3 Within the Authority's aims and objectives, the Internal Audit section has a performance target of 26 audit reports to be issued during the financial year.

During the year 29 reviews were undertaken, 2 of which did not produce formal audit reports, but provided information for management consideration. 27 audit reports were issued against the target of 26.

There is 1 review being carried forward to the 2008-09 audit plan, namely a review of data security arrangements. This was purposely delayed to support the remit of the Data Security Working Group. 20 days have been carried forward to the 2008-09 annual audit plan to complete this review.

Of the 27 reviews generating audit reports 21 provided a formal assurance statement. These are summarised below.

### 3.4 Summary of Audit Report Conclusions and Recommendations

Ref.	Title	Plan Days	Actual Days	Audit Recommendations			Assurance Level
				High	Medium	Low	
Audit reviews providing a formal assurance statement							
IAR0708-03	Register of Interests	25	25	0	1	0	Substantial
IAR0708-05	Cash Receipting	10	12	0	1	5	Substantial
IAR0708-06	Leisure Income	15	15	2	7	2	Limited
IAR0708-07	Housing Rents	15	15	0	1	0	Substantial
IAR0708-08	Creditors	10	10	0	0	8	Substantial
IAR0708-09	Trade Waste Procedures	30	40	0	3	2	Limited
IAR0708-10	Capital	10	10	0	1	4	Substantial
IAR0708-11	Stock Control (Direct Services)	15	15	0	1	5	Substantial
IAR0708-12	Fleet Mgmt (Direct Services	15	15	0	1	8	Substantial
IAR0708-13	Housing Benefits	30	30	0	2	7	Substantial
IAR0708-14	Payroll	15	7	0	0	1	Substantial
IAR0708-15	Debtors	10	16	0	13	5	Limited
IAR0708-16	NDR	15	15	0	0	5	Substantial
IAR0708-17	Council Tax	15	15	0	0	5	Substantial
IAR0708-18	Bank Accounts	5	6	0	1	3	Substantial
IAR0708-19	Housing Repairs (Draft)	40	40	0	8	4	Limited
IAR0708-20	FMS	10	10	0	0	4	Substantial
IAR0708-21	Insurance & Inventory	10	10	0	1	2	Substantial
IAR0708-22	Lending & Borrowing	5	5	0	0	0	Substantial
IAR0708-23	Post Procedures	5	5	0	0	3	Substantial
IAR0708-24	Officers Disbursements	10	10	0	0	3	Substantial
Totals		315	326	2	22	66	

Ref.	Title	Plan Days	Actual Days	Audit Recommendations			Assurance Level
				High	Medium	Low	
Audit reviews not providing a formal assurance statement							
IAR0708-01	Cash Ups (Civic Centre)	2	1	N/a	N/a	N/a	N/a
IAR0708-02	Cash Ups (Leisure Centres x 5)	3	5	N/a	N/a	N/a	N/a
Other Work							
	Audit Follow-up Activity	40	42				
	06-07 work brought forward	25	25				
	Performance Indicators / Data Quality	30	24				
	Risk Management / Corporate Governance	10	13				
	Contract (final check)	15	18				
	Contingency / Grant Work	50	40				
	IT / IS	10	10				
	Departmental Activity	15	9				
Work carried forward to 2008-09							
	Computer Audit	20					
Grand Totals		535	515				

Assurance definitions are provided in **Appendix B**.

## Trend Analysis of Audit Activity

- 3.5 The table below highlights the trend in the level of assurance provided from internal audit reviews completed over the last 2 financial years. The assurance provided from internal audit activity clearly shows a marked improvement in the control environment reviewed.

Assurance	Substantial	Limited	No
<b>2007-08</b>	17	4	0
	81%	19%	0%
<b>2006-07</b>	14	7	0
	67%	33%	0%

The table below summarises the total number of audit recommendations by risk category emanating from completed audit reviews over the last 2 financial years.

The table highlights a reduction in total recommendations from 132 (2006-07) to 102 (2007-08). This equates to a 23% reduction in the number of recommendations within internal audit reports. This improvement in the control environment is further evidenced by the reduction in the number of medium and high risk audit recommendations as a percentage of the total recommendations made (from 39% in 2006-07 to 31% in 2007-08).

Recommendations	High	Medium	Low
<b>2007-08</b>	2	30	70
	2%	29%	69%
<b>2006-07</b>	1	50	81
	1%	38%	61%

## 4: Conclusion

- 4.1 Internal Audit can confirm that adequate resources have been made available to allow sufficient internal audit activity to be undertaken so as to provide reasonable assurance regarding the adequacy and effectiveness of Gedling Borough Council's risk management, governance and control processes.
- 4.2 Overall, internal audit activity identifies an improvement in the control environment during 2007-08 in comparison to the preceding financial year.

## Annual Review of the Effectiveness of the System of Internal Audit 2007-08

### Assessment Definitions

Level		Requirement	Standard
1		Not all green criteria achieved.	Performing below minimum standards.
2		All green criteria achieved.	Performing at minimum standards.
3		All green criteria plus 70% of the pink.	Performing at a good standard.
4		All pink criteria plus 50% of the blue.	Performing at an excellent standard.

### Assessment Summary

#### CiPFA Standards

Criteria	Total Number	Total Achieved	Percentage
	26	26	100%
	24	24	100%
	13	10	76.9%

Internal Audit is currently achieving Level 4 with respect to Standards.

#### CiPFA Effectiveness

Criteria	Total Number	Total Achieved	Percentage
	2	2	100%
	7	6	85.7%
	4	2	50%

Internal Audit is currently achieving Level 3 with respect to Effectiveness, and has plans in place to enable it to achieve Level 4.

# Overall Performance Assessment

## Standards

4	A	C	D (GBC 07-08)	D
3	A	B	C (GBC 06-07)	D
2	A	B	B	C
1	A	A	A	A
	1	2	3	4
	Effectiveness			

A = Unacceptable – performing below minimum standards.

B = Satisfactory – performing at minimum standards.

C = Good – performing to a good standard.

D = Excellent – performing to an excellent standard.



### Risk & Assurance – Standard Definitions

#### Audit Recommendations

Audit recommendations are categorised, depending upon the level of associated risk, as follows:

Level	Category	Definition
1	<b>High</b>	Action is essential to manage exposure to fundamental risks.
2	<b>Medium</b>	Action is necessary to manage exposure to significant risks.
3	<b>Low</b>	Action is desirable and should result in enhanced control or better value for money.

#### Assurance Statement

Each report will provide an opinion on the level of assurance that is provided with respect the risk emanating from the controls reviewed. The categories of assurance are as follows:

Category	Definition
<b>No</b>	The majority of the significant risks relating to the area reviewed are not effectively managed.
<b>Limited</b>	There are a number of significant risks relating to the area reviewed that are not effectively managed.
<b>Substantial</b>	The risks relating to the objectives of the areas reviewed are reasonably managed and are not cause for major concern.