

PART A

AGENDA

ITEM **6**

Report to: Audit Committee
Date of Meeting: 6 March 2007
Report of: Audit Manager
Title: Internal Audit Service Plan and Annual Plan 2007/08

1. **SUMMARY**

This report presents Internal Audit's Service Plan and sets out the proposed work programme for the Internal Audit Service for the coming financial year.

2. **RECOMMENDATIONS**

The 2007/2008 Internal Audit Service Plan and Annual Plan be approved.

Contact Officer:

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Report approved by Janice Maule – Director of Finance

3.0 DETAILED PROPOSAL

- 3.1 Each year this Committee approves Internal Audit's Service and Annual Audit Plans (work programme) for the coming financial year. The Service Plan sets out Internal Audit's objectives for the year and how they link to the corporate objectives. The Annual Plan shows the programme of audits it is proposed to carry out to achieve the service objectives.
- 3.2 The 2007/2008 Audit Plan takes account of the risks faced by the Council and is based on:
- (i) Available resources – estimated number of productive auditor days after allowing for leave, sickness, training etc.
 - (ii) A review of risk registers.
 - (iii) Internal Audit's own risk-based assessment of auditable areas. This is continually updated and is based on the CIPFA model. It takes into account materiality (level of income and expenditure), control environment/vulnerability (assessment of controls based on date and findings of last audit, low/high staff turnover etc), sensitivity (assessment of the likely impact of failure of the area under review) and management concerns (e.g. known problems).
 - (iv) Discussions with Heads of Service.
 - (v) Information gained from Service Plans, Medium Term Plans, committee reports etc.
- 3.3 Even though this is a plan for the coming year only there still needs to be an element of flexibility in the approach to the work to be undertaken to cater for unforeseen changes in circumstances. Should it be necessary to make any significant changes to the work programme they will be reported to Committee.

4. IMPLICATIONS

4.1 Financial

The Director of Finance reports there are no immediate implications in this report as there is sufficient budgetary provision to fund the proposed work programme given current staffing arrangements.

4.2 Legal Issues (Monitoring Officer)

The Head of Legal Services reports that there are no specific legal issues in the report. The Council has a responsibility to ensure that it has proper arrangements for the management of the internal control environment, this includes an appropriate internal audit presence.

4.3 Staffing

There are no implications in this report.

4.4 Accommodation

There are no implications in this report.

4.5 Equal Opportunities

There are no implications in this report.

4.6 Community Safety

There are no implications in this report.

4.7 Sustainability

There are no implications in this report.

4.8 Potential Risks

Failure to maintain an adequate internal audit of the Council's accounting records and system of internal control would be in contravention of the Accounts and Audit Regulations 2003 (as amended in 2006) and would make it impossible for the Audit Manager to provide an annual opinion on the overall adequacy and effectiveness of the internal control environment. This opinion feeds into the statutory Statement of Internal Control.

Background papers:

The following background papers were used in the preparation of this report:

Audit Files

If you wish to inspect or take copies of background papers please contact the officer named on the front page of the report.

File reference: None

WATFORD BOROUGH COUNCIL

Internal Audit Service

SERVICE PLAN 2007/2008

The purpose of this service plan is to demonstrate the link between key corporate priorities (as set out in the Community Plan), Internal Audit Service priorities and the work of individual auditors and to record how the Service's priorities have been determined and are to be achieved.

1 Service Centre

Internal Audit Service – in-house provision.

2 Lead Officer

Barry Austin – Audit Manager

3 Service Statement

Internal Audit is an assurance function that primarily provides an independent and objective opinion to the Council on the control environment (comprising the systems of governance, risk management and internal control) by evaluating its effectiveness in achieving the Council'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.

4 The Nature of the Service

- 4.1 The Service's broad objective is to provide an adequate and effective system of internal audit of the Council's accounting records and systems of internal control in accordance with the "proper practices in relation to internal control" as set out in the Accounts and Audit (Amendment)(England) Regulations 2006.

- 4.2 “Proper internal audit practices” (non-statutory) are found in CIPFA’s *Code of Practice for Internal Audit in Local Government in the UK*, published in 2003 and revised in 2006. This Code requires the Audit Manager to “provide a written report to those charged with governance timed to support the Statement on Internal Control”. It sets out various matters to be commented on in the report, including the requirement to give “an opinion on the overall adequacy and effectiveness of the Council’s control environment”. The work the Service undertakes throughout the year is planned to enable the Audit Manager to provide such an opinion.
- 4.3 Internal control systems are all those processes which are set up by management to safeguard assets, ensure reliability of records, promote operational efficiency and monitor adherence to policies, regulations and directives. Internal Audit is not confined to the review of financial processes but has the freedom to review any council activity.
- 4.4 Internal Audit is an aid to management and is not a substitute for good management.
- 4.5 The Code of Practice also states that the audit work plan must be fixed for a period of no longer than one year. 2007/2008 will be the third year in which a formal five-year Strategic Plan has not been produced for Member approval. This is a reflection of the difficulty in predicting changes over the longer term when the range of services provided and the manner of service provision is likely to change substantially. The annual work plan enables Internal Audit to concentrate on issues of immediate significance to the Council as well as covering the external auditor’s requirements under the “Managed Audit” approach. A working version of a longer term plan is still maintained as a database of potential areas of audit.
- 4.6 Increasing use is being made of key risks, as identified through the Council’s risk management process, as the basis for the audit planning process. Total reliance on this process will not occur until the Audit Manager is satisfied that risk management is suitably embedded in the culture of the Council and service and corporate risk registers become sufficiently robust. In the transition, the Audit Manager will continue to maintain the audit risk assessment register as a supporting element of the planning process.
- 4.7 In addition, reference has been made to the Medium Term Plan, individual service plans, the programme of procurement projects and the capital budget (to identify contracts for

review) as sources of information for determining issues to be covered by Internal Audit. Relevant national, professional and local publications are also used as a source of planning material to ensure possible external developments are also accounted for.

- 4.8 The work to be undertaken in any year will continue to be discussed in advance with Heads of Service and Corporate Directors and with the external auditors.
- 4.9 The nature of work carried out includes systems reviews, computer audit, contract audit and the investigation of fraud (excluding Benefit fraud) and other irregularities. Establishment audits did not form part of the 2006/07 plan due to the relatively low risk attached and the closures brought about by the new leisure facilities. There will however be some establishment work in 2007/08 because of the increased use of the remaining leisure facilities.
- 4.10 Work in 2007/2008 will concentrate on systems reviews, including working in conjunction with the Audit Commission/Robson Rhodes to meet the requirements of the International Standards on Auditing. Time will be set aside to review the risk management processes (compilation of risk registers, risk mitigation etc) and corporate governance (quality and effectiveness) arrangements. The Audit Manager is responsible for supervising the work of the Risk and Insurance Manager and is a member of the RM Working Group. He also oversees the work of the Fraud Team (investigating Benefit fraud). Contract auditing will be stepped up to cover monitoring of new and established contracts.
- 4.11 A number of external reviews have taken place recently and time will be set aside in 2007/08 to review the action taken in response to these. They include the Zurich Municipal risk management health-check, the Benefit Fraud Inspectorate examination of security and the National Fraud Initiative, a national data matching exercise intended to uncover cases of fraud in the areas of payroll, benefits, housing rents and creditor payments.
- 4.12 Time has been set aside for work on the Housing Stock Transfer. It has been categorised as high risk because of the size of the transaction, not because there are concerns over how it will proceed.

- 4.13 Agreement has been reached in principle with Dacorum Borough Council for collaboration in the audit of our respective fraud investigation teams. Dacorum will review the work of Watford's team and vice-versa. This will help maintain the independence of the two Audit managers.
- 4.14 The allocation for fraud investigations is based on past experience, the time allowance in the audit plan being reduced from previous years. Any fraud investigation will also include an assessment of the adequacy of internal controls within that particular area. It is management's responsibility to ensure that adequate control procedures are in place to deter and detect fraudulent activity, not Internal Audit's. Audit resources will be directed towards detecting fraud in those activities which are widely recognised as being susceptible to fraud.
- 4.15 Consultancy work undertaken in the past has largely consisted of providing advice and has generally been of a reactive rather than proactive nature. It is likely to continue in this way. Internal Audit will not positively seek consultancy type work, given the other demands on time. If such work is undertaken the terms of reference will make it clear that it is not being carried out in the capacity of auditors and the Audit Committee will be advised.
- 4.16 The allocation of resources will be set out in the annual audit plan. This service plan and the audit work plan will be presented to the Audit Committee for approval.
- 4.17 All High and Medium Risk recommendations will be followed up to ensure implementation. This will occur either through seeking written confirmation from Heads of Service on a quarterly basis or by review during the next audit of that activity. Unsatisfactory progress will be reported to CMB.
- 4.18 At the end of the year the work undertaken will be sufficient to enable the Audit Manager to provide an opinion on the effectiveness of the internal control environment during 2007/2008. Measures to evaluate the level of improvement in internal controls have been implemented e.g. by comparing the number of high risk recommendations made in respect of certain key systems on an annual basis.

5 How has the service translated the key corporate priorities into service delivery?

5.1 In overall terms the Internal Audit Service seeks to support all corporate objectives by promoting the economic, effective and efficient use of limited resources through a continuous process of service reviews. In addition, the Service will place increasing emphasis on reviewing the effectiveness of actions taken to mitigate those key risks likely to prevent the achievement of corporate objectives.

5.2 The key corporate objectives are:

- (i) An efficient, effective, value for money Council.
- (ii) A town with a high quality environment.
- (iii) A safer town.
- (iv) A healthy town.
- (v) A good town for business, skills and learning.
- (vi) A well-informed community where everyone can contribute.
- (vii) A town to be proud of

Internal Audit's contribution to the achievement of these objectives can be most clearly directly demonstrated in respect of item (i) because of the emphasis on financial systems reviews and value for money. Audit also examines the integrity and accuracy of data produced by the various systems as this forms the base on which decisions re future service provision and other initiatives are made and will be involved in the implementation of data quality and information security strategies.

Audit can also contribute by reviewing risk management arrangements and business continuity planning thereby reducing the risk to the achievement of those objectives and ensuring that the Council is able to provide continuity of service. The control implications of any new procedures are reviewed and value for money issues commented on.

Internal Audit can have an indirect effect on changing the culture of the organisation by promoting more effective and efficient ways of working.

Details of the work to be undertaken by Internal Audit are set out in the 2007/2008 work plan.

6 Key Service Priorities for 2006/2007

- 6.1 The following priorities are seen as crucial to the development of the service and its contribution to improved internal control. The Audit Manager will take the lead in these with the assistance of other members of the team.
- (i) Expectations of Internal Audit are continually evolving e.g. CIPFA's guidance for Internal Audit in Local Government set out in the 2003 Code of Practice has now been revised with the publication of the 2006 version. The Audit Manager will ensure that the Service operates in accordance with expected standards. This is a continuing review process. Procedures will also be compared to Audit Commission guidelines for the review of internal audit. The extent to which the external auditors continue to place reliance on the work of Internal Audit will act as measure of success in achieving this objective.
 - (ii) The International Standards on Auditing require the external auditors to have an understanding of how transactions and processes within the council operate, culminating in the transfer of data to the general ledger and final accounts. Discussions between internal audit and the Audit Commission had led to an agreement for co-operation between the two sets of auditors which had furthered the external auditor's understanding of key Council systems. Discussions will take place during the year with the new external auditors (Robson Rhodes) to ensure that the same level of co-operation continues.
 - (iii) Internal Audit has now documented and flowcharted all key systems and will review these during the year to ensure their continuing accuracy. Detailed testing of these systems will continue for the coming year at least until the expectations of Robson Rhodes are known.
 - (iv) The Audit Commission have requested that Internal Audit continue to carry out detailed testing of the Benefit Subsidy Claim especially as the housing stock

transfer will have a significant impact on the claim and could affect the availability of the Housing Accountant at the very time the Audit Commission will be carrying out their own work.

- (v) Internal Audit will continue to assist in the development of risk management arrangements within the Council and will seek to integrate the corporate risk assessment process into the audit planning process, eventually leading to a risk based audit approach. The Audit Manager is a member of the RM working group and is also directly responsible for the supervision of the Risk and Insurance Manager. The R&IM is directly responsible for RM and the Audit Manager will ensure that his role in the RM process does not jeopardise the independence of Internal Audit when it comes to auditing RM arrangements.
- (vi) Now that the Benefit Fraud Team reports to the Audit Manager there will be a move towards incorporating the fraud investigation work of the two teams into a corporate anti-fraud team. This will not occur however until the Audit Manager is satisfied that the Fraud Team is operating satisfactorily. As with risk management, care will be taken to ensure the independence of Audit from the investigation function.
- (vii) The Audit Manager will amend the audit approach as necessary in response to changes in service provision and Council structures brought about by Member/Corporate Management Board decisions.

7 Resource Requirement

(i) Staff

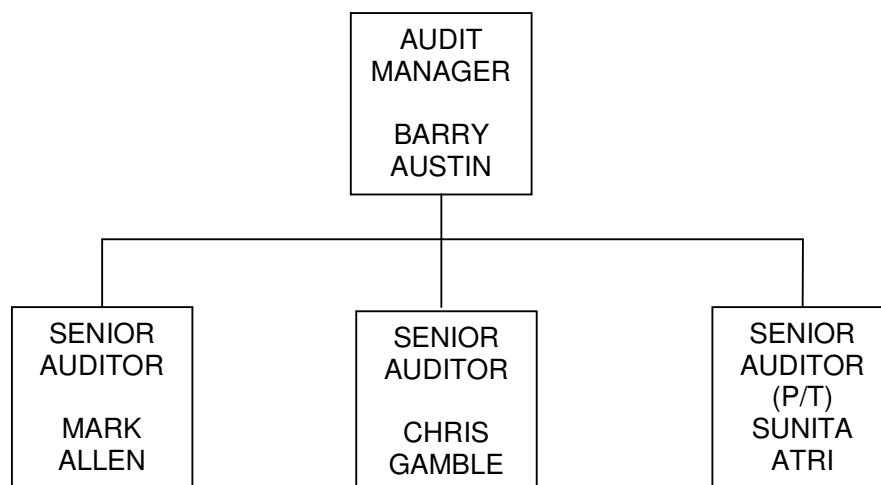
Staffing levels have remained constant since Internal Audit was re-established in 2001 although one post has been re-designated from Auditor to Senior Auditor to reflect the changing responsibilities of the Service. This level is felt to be sufficient to enable the Audit Manager to give an annual opinion on the adequacy of controls.

Although one of the Senior Auditors works on a part-time basis (25 hours per week) there has been provision for a full time post in the establishment and the balance of salary has been used to buy in external IT audit expertise. This funding has now been given up as part of the budget savings for 2007/08 but it is anticipated that the level or quality of service provided will not suffer as a result. Work on the Housing Service will greatly reduce and a new Senior Auditor has recently been appointed whose qualification and experience will be used to replace the external IT auditors. The long-term objective is to develop all Internal Audit staff to enable them to take on more technical IT work.

Two of the Senior Auditors are qualified as members of the Institute of Internal Auditors (IIA), one of the two also being an IIA qualified computer auditor. The third is studying for membership

One member of the team has the Association of Accounting Technicians qualification (AAT) and is studying for membership of the Institute of Internal Auditors (IIA) and two have recently passed the IIA examinations. The Audit Manager is a member of CIPFA and is participating in CIPFA's Continuing Professional Development (CPD) scheme.

(ii) **Structure**



(III) Annual Budget

Employees	£164,520
Supplies/Services	£ <u>2,560</u>
	<u>£167,080</u>

8 Monitoring and Evaluation

8.1 The Audit Manager will exercise continuing monitoring of progress against the Audit Plan and local performance indicators. Progress on a range of issues will be reported to the Audit Committee on a quarterly basis.

8.2 Performance Indicators:

Indicator	Target
Actual "chargeable" days as % of planned	85%
% Audit plan completed (based on number of projects)	90%
% Final audit reports issued on time	100%
Client satisfaction score	85%

8.3 Staff performance will be reviewed during and at the completion of individual audits and during the corporate performance appraisal process. The Audit Manager is assessed through the Council's Management Development Programme.

8.4 The external auditors review the work of Internal Audit annually to ensure that they can continue to rely on our work. No doubt Robson Rhodes will carry out a detailed review in the first year of their operations.

8.5 Watford will continue to benchmark itself against other Herts authorities to help maintain best practice in its operations and benefit from the exchange of ideas.

9 Risk Assessment

See below for significant risk. This risk materialised in 2006/07 when one of the Senior Auditors resigned. The vacancy was covered by buying in external assistance.

Audit Manager
February 2007.

Risk Ref	Risk	Consequence	Likelihood 4=Catastrophe 1=H. Unlikely	Impact 4=Catastrophe 1=H. Unlikely	Risk Rating	Responsibility	Existing Control Procedures	Likelihood 4=Cat 1= H. U	Impact 4=Cat 1=H. U	Risk Rating
IA 1	Loss of staff for an extended period.	Failure to achieve audit plan. Failure to complete work on key systems. Criticism from external auditors and loss of internal credibility.	3	4	12	Audit Manager	Use of contingency allowance. Forward planning e.g. early advertisement for replacement. Reorganise work to ensure key systems are prioritised.	3	3	9
Risk Ref	<u>Options for additional/replacement control procedures</u>						<u>Cost/Resources</u>	Likelihood 4=Cat 1=H. U	Impact 4=Cat 1=H. U	Risk Rating
	Buy in additional resource to achieve minimum cover required for the provision of an audit opinion re adequacy of the internal control environment.						Depends on experience of auditor and length of time involved but likely to be costly.	3	2	6

**WATFORD BOROUGH COUNCIL
INTERNAL AUDIT SERVICE
AUDIT PLAN 2007/2008**

Appendix 2

Audit	Outline of work	Proposed Time Allocation. Days
Managed Audits	As agreed with the Audit Commission, the audits will include reviewing and testing controls in place and updating system notes/flowcharts for all key systems	
Accounting system (Aptos)		15
Treasury management		6
Creditors		15
Income collection (Radius)		15
Housing rents	Follow up on previous work	7
Payroll	Includes IT access controls	25
Asset Management		15
Sundry Debtors		15
Benefits Administration	Includes IT access controls	30
Council Tax		15
NNDR		15
Support Service Recharges		8
Reconciliations:		
a) Bank reconciliations		5
b) Data transfer between systems		25
Budgetary Control		10
Total Managed Audits		221
Grants Work	Review of grants claims/ government returns, as agreed with Audit Commission. To include Benefits Subsidy claim, e-govt grant, NNDR – scope to be agreed with Audit Commission.	40
Other High Risk – As Assessed by Internal Audit.	Based on IA's own risk assessment, discussions with front line Heads of Service, review of Corporate and Service Risk Registers and draft Medium Term Plan.	

Performance indicators	Review of procedures/calculations for 06/07 PIs and arrangements for new/amended 07/08 indicators.	30
Repairs service	Follow up on previous work	5
Corporate Governance Arrangements	Implementation of best practice including comparison with CIPFA/Solace latest guidance	15
Risk Management	Implementation of risk management arrangements and mitigation of risks. Review of business continuity plans and implementation of Zurich Municipal recommendations.	20
Fraud Investigation team	Review implementation of Benefit Fraud Inspectorate recommendations	7
Fraud Awareness	Review arrangements for maintaining awareness	6
National Fraud Initiative (NFI)	Investigate potential duplicate/incorrect payments identified by NFI data match.	10
Housing Stock Transfer	Work to be undertaken because of the size of the transaction, not as a result of any preconceived concerns.	20
Partnership working	a) comparison with CPA/Use of resources criteria	10
	b) review of current/proposed partnerships	15
Total Other High Risk		138
Medium Risk Audits	Review of operational controls, concentrating on income collection.	
Bill Everett Centre		8
Westfield	As above plus VFM review of equipment investment.	9
Colosseum		5
Building Control		8
Parking Control		8
Charter place market		5
Cashiering Function		5
Recovery of Benefit overpayments		5
Total Medium Risk		53
IT Audit	Review corporate, management	

	and technical controls based on a rolling programme of audits.	
Policies/Strategies	Information Security	10
Home working	Post implementation review	10
Software licensing	Check on legality of software on PCs	10
Total IT Audit		30
Contract Audit		
Leisure facilities		10
Fleet management/servicing		15
Total Contract Audit		25
Contingencies		
Fraud Investigations		30
Other	Time over-runs and unforeseen circumstances	25
Total Contingencies		55
Total Resource Requirement		562

Available Resources (Estimate)

Gross Working days		959
Less		
Annual Leave/Bank Hols	150	
Sickness	16	
Other/Special	6	
Training	<u>25</u>	<u>197</u>
Net working days		762
Less		
Admin, planning, appraisals working groups, team meetings etc		<u>200</u>
Total Available days		<u>562</u>

