

WATFORD BOROUGH COUNCIL
ANNUAL INTERNAL AUDIT REPORT 2011/2012

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1 Introduction

This report summarises the work undertaken by Internal Audit in relation to the 2011/2012 audit plan to the end of May 2012. It covers functions performed directly by Watford Borough Council and by Shared Services on its behalf. The report meets the requirements of the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 by:

- (i) including an opinion on the overall adequacy and effectiveness of the Council's control environment
- (ii) disclosing any qualifications to that opinion, together with the reasons for the qualification
- (iii) presenting a summary of audit work undertaken to formulate the opinion, including reliance placed on the work of other assurance bodies
- (iv) drawing attention to any issue the Head of Internal Audit judges particularly relevant to the production of the Annual Governance Statement
- (v) comparing the work actually undertaken with the work that was planned and summarising the performance of the Internal Audit team against its performance measures and
- (vi) commenting on compliance with the CIPFA standards and communicating the results of the Internal Audit quality assurance programme.

The Accounts and Audit (Amendment) (England) Regulations 2006 require the Council to maintain an adequate and effective system of internal audit of its accounting records and of its systems of internal control in accordance with proper practices in relation to internal control.

The Council is responsible for ensuring its business is conducted in accordance with the law and proper standards and that public money is safeguarded, properly accounted for and used economically, efficiently and effectively. The work undertaken by Internal Audit must not be seen as a substitute for management's responsibility for maintaining sound management practices, including robust controls.

The report is one of the key sources of assurance used in the production of the Annual Governance Statement.

2 Audit Opinion

Having reviewed the work undertaken by Internal Audit to date I am able to give a satisfactory assurance of the adequacy and effectiveness of the internal control environment.

There have been no significant new concerns arising from the majority of the audits undertaken in 2011/12 that would necessitate an adverse overall opinion. However, some of the concerns reported in the previous Annual Report have remained a concern in 2011/12. I list these concerns in Section 3 of this report. Reference to these must be considered for inclusion in the Annual Governance Statement.

The factors taken into account in forming the opinion are set out in more detail in sections 3, 4 and 5 below.

Every internal audit report contains an audit opinion on the effectiveness of controls within the system/function/activity reviewed, highlighting any significant weaknesses which could affect the Council's control environment. The opinion provided in each report falls into one of the following categories:-

Full Assurance – sound controls that are consistently applied.

Qualified Assurance – a satisfactory report - basically sound controls but some inconsistent application puts some control objectives at risk.

Limited Assurance – unsatisfactory controls or their application puts some control objectives at risk.

No Assurance – fundamental failure of control.

These individual opinions feed into the overall opinion provided in this report.

3 Audit Qualifications

It is the practice to carry out audits of the key financial systems towards the end of the financial year in order to be able to give an opinion on the effectiveness of controls within each system throughout the whole year. This allows assurance to be given not only to service heads but also to the external auditors when they carry out their final accounts work. Consequently, shortcomings associated with those systems are now being identified/verified by Internal Audit.

- **Recovery of Overpaid Benefits**

Internal Audit work in January 2012 identified that repeated failure of the scheduler within the Academy system had prevented the production of recovery letters for overpayments of Housing and Council Tax benefits since March 2011 and prevented the printing of invoices for benefit overpayments since August 2011. Whilst good rates of recovery of overpaid benefit have continued to be achieved through deductions to ongoing benefits wherever possible, the scheduler failures within Academy have hindered the recovery of overpaid benefit.

The scheduler issues are now reported to have been resolved but this situation must be closely monitored during 2012/13 to ensure that the system remains stable and that any recurrence of the problems is resolved promptly.

The Council is allowed to keep any recovered overpayments in addition to any benefit subsidy it receives from the government on those overpayments. It is in the Council's interest therefore to consistently use the full range of processes at its disposal to undertake recovery of those overpayments promptly.

- **Reconciliations to the Financial Management System (eFinancials)**

An audit of reconciliations between the various feeder systems (revenues, benefits, payroll etc) and eFinancials was in progress at the conclusion of 2011/2012.

The implementation of a new income management system (Axis) has, understandably, required significant input from the Finance Managers throughout 2011/2012. Axis automates a number of processes that previously required significant manual input and it is anticipated that the efficiency benefits of this new harmonised system will be fully realised in 2012/13. Ultimately, this will have a positive impact on the production of regular reconciliations for cash and banking through the automation of many elements of the reconciliation process. For 2011/12, the prioritisation of the income management system implementation work has limited the resource available for producing in-year reconciliations of both cash/banking systems and the revenues and benefits systems to the general ledger.

It was noted that there had been no full reconciliation carried out between the Academy Revenues and Benefits systems (for Council Tax, NNDR and Housing and Council Tax Benefits) and eFinancials during 2011/12. This is a similar position to that reported last year.

A significant piece of work has been undertaken within Revenues & Benefits to develop reporting routines that will provide expenditure data from the Academy system in a format that will simplify the updating of the general ledger and also demonstrate data integrity between the components of the Academy suite.

The importance of in-year reconciliations as a source of assurance is fully recognised and an action plan has been developed within Finance to ensure that in-year reconciliations will be produced between the general ledger (eFinancials) and all associated feeder systems throughout 2012/13 and beyond.

- **ICT**

An external consultant's report (Actica Consulting) produced in May 2011 identified a range of significant infrastructure and governance changes that are required to ensure that the capacity, security and resilience of hardware, software and service delivery are adequate for current and future requirements. These changes have started to be implemented.

The Joint ICT Steering Group now has responsibility for prioritising the project work of ICT, defining technical standards and supporting development of the ICT strategy.

Investigations into alternative models of service delivery were started in July 2011, with the intention to go live with the new service model from early 2013.

Pending a decision on the future provision model for ICT services, an Infrastructure Improvement Programme was initiated in October 2011 to stabilise and strengthen the existing infrastructure. The first phase of this programme ended in January 2012 and included improvements to back-up arrangements and network monitoring, development of a new virtual server farm and the replacement of some critical hardware.

The success of the ongoing Infrastructure Improvement Programme is central to ensuring that the capacity, security and resilience of the infrastructure reach the required levels regardless of how the service is provided in the future.

Delivery of future phases of the Infrastructure Improvement Programme, and the transition to the future model of service provision will require continued strong management to maintain the improvement momentum and manage the risk of significant disruption to ICT availability that would affect delivery of other Council services.

- **Separation of Duties**

Separation of duties in the processing of financial transactions is a key element of a strong control environment. Reductions in staffing levels brought about by the ongoing requirement to find savings makes it increasingly difficult to maintain previously enjoyed levels of separation. Heads of Services and Service Managers must ensure that where staff numbers are reduced, appropriate compensating controls are put in place to mitigate the additional risk of error or fraud that may arise from increasing reliance on individuals to perform all or the majority of stages of transactions that were previously performed by separate officers.

4 Basis of Opinion

4.1 Work Undertaken

The work undertaken by Internal Audit during the 2011/2012 financial year was in accordance with the Audit Plan as approved by the Audit Committee. This has been a transitional year for Internal Audit and although this has resulted in a number of planned audits currently remaining at draft stage or as work in progress, the work completed has been sufficient to enable me to provide a reasoned opinion on the overall adequacy and effectiveness of the control environment.

Should the completion of work on the Audit Plan for 2011/2012 identify any issues that affect my opinion, I will issue a revised Annual Report to the September 2012 Audit Committee accordingly. On the basis of the work performed to date however, it is my opinion that this step will not be necessary.

Details of the audits undertaken and a note of the progress on each one are shown in Appendix 1.

4.2 The Scope of the Audit Plan

The 2011/2012 Audit Plan was prepared by the previous Audit Manager after reviewing service plans and risk registers, completing a fraud risk assessment and consulting with senior officers. It was based on an assessment of the risks facing both councils and was designed to meet the requirements of the external auditors.

The draft plan was approved by the Audit Committee in March 2011.

The planning process should therefore help ensure that all key systems and significant risks have been taken into account.

4.3 Implementation of Recommendations

When an audit is completed weaknesses/areas requiring improvement are discussed with senior management. This leads to an action plan being drawn up which shows agreed measures to be taken and the timescales within which they will be implemented.

All recommendations are followed up to ensure that action has been taken, or where not, that there is an acceptable reason. Occasional follow up visits are carried out and all recommendations relating to key systems are routinely followed up during the next planned audit. The results of the follow up process, and in particular any failure to implement recommendations, is reported to each meeting of the Audit Committee.

These arrangements should ensure that action is taken to remedy any issues identified during the year.

4.4 Other Factors

- My observations arising from requests to Internal Audit for assistance, attendance at meetings, committee agendas and minutes etc
- Internal Audit has had sufficient resource to enable it to complete the majority of its work programme.
- The absence of material changes in the Council's objectives or activities in the year under review.
- There have been no limitations placed on the scope of work undertaken by Internal Audit, on its access to records and information or on the provision of explanations as necessary.

4.5 External Assurance

I have also taken into account the outcome of work undertaken by the external auditors and where appropriate I have ensured that the scope of individual Internal Audit assignments incorporates any concerns raised by the external auditors.

5 Fraud Investigations/Awareness

With the exception of benefit fraud, which is investigated solely by the Benefit Fraud Team, Internal Audit is responsible for investigating suspected cases of fraud and corruption in collaboration with the Fraud Team.

It is management's responsibility to ensure that adequate control procedures are in place to deter and detect fraudulent activity, not Internal Audit's or the Fraud Team's. Internal Audit's responsibility includes providing an opinion on the effectiveness of the Council's arrangements to prevent and detect fraud, remaining vigilant on the potential for fraud in all areas audited and making recommendations to address weaknesses in controls that could give (or have given) rise to frauds.

One significant fraud attempt was made during 2012/2013 that affected the payment of creditors by the Shared Finance Service. Fraudulent documents were submitted requesting changes to bank account details for a large supplier on the payments system. These changes were processed and a large payment was sent to the fraudulent bank account by BACS. On discovery of the loss, prompt action by the Fraud Manager led to the full recovery of the diverted funds.

An Internal Audit report on the circumstances surrounding the fraud made recommendations to bring the procedures for controlling changes to payment details into line with best practice. These recommendations have been implemented by Finance, significantly reducing the risk of a similar attempt being successful.

There are no other frauds of which Internal Audit is aware that should be reported to the Audit Committee.

6 Internal Audit - Quality Assurance

The Internal Audit team seeks to operate in accordance with the standards laid down by CIPFA in the Code of Practice for Internal Audit in Local Government in the UK (2006) which sets out auditing standards under the following eleven headings:

- Scope of Internal Audit
- Independence
- Ethics for Internal Auditors
- Audit Committees
- Relationships
- Staffing, Training and Continuing Professional Development
- Audit Strategy and Planning
- Undertaking Audit Work
- Due Professional Care
- Reporting
- Performance, Quality and Effectiveness.

Based on reviews undertaken to date, I am satisfied that there are no material areas of non-compliance with the Code.

Internal Audit's work is subject to review by the external auditors on an annual basis. There has been no criticism of our work over the past year.

Internal Audit has its own quality assurance controls. Standard procedures and working papers are used. For every audit I review the working papers and all versions of the audit report. Any concerns/queries are discussed with individual auditors.

Work on individual audits is carried out by auditors with the appropriate level of skill and experience.

Use is made of customer satisfaction questionnaires as a means of gaining independent comment on our service. Any issues raised are discussed with the customer and the auditor. We try to learn from any mistakes we may make or from suggestions for improvement.

Mark Allen
Audit Manager
29th May 2012

Internal Audit Plan 2011/12

Position as at 29th May 2012

INTERIM ANNUAL PLAN 2011/2012

Audit	Progress
Shared Audits	
Payroll	Work in progress
Recruitment	Draft report stage
NNDR	Draft report stage
Council Tax	Draft report stage
Benefits	Work in progress
Creditors	Draft report stage
Debtors	Draft report stage
FMS Reconciliations	Draft report stage
Insurance	Final report 09 12 11
IT - Network Controls – follow up	Moved to 2012/13 Audit Plan
IT - Disaster Recovery and Back-up	Draft report stage
IT – Project Management	Final report 15 11 11
IT - Asset Management	Draft report stage
IT - Virus Protection	Draft report stage
COA – Post Implementation Review	Final report 30 03 12
WBC	
Income Collection	Work in progress
Benefits Subsidy Claim	Final report - 17 10 11
Benefits Overpayments	Management letter issued 29 02 12
Treasury Management	Work in progress
Budget Monitoring	Work in progress
CIS	Final report - 03 01 12
S. 106	Final report - 14 11 11
Financial Procedure Rules	Draft report stage
Hospitality	Final report - 12 03 12
Money laundering	Final report - 11 01 12
Current Contracts	Final report - 15 02 12
Home Improvement Grants	Final report - 02 09 11
Museum	Final report - 12 08 11
CSC	Final report - 14 03 12
External Audit Recommendations follow up	Moved to 2012/13 as part of Corporate Governance audit
ADDITIONAL AUDIT:	
West Herts Crematorium	Final report - 14 07 11

Appendix 2

LOCAL PERFORMANCE MEASURES 2011/2012

Criteria	Target p.a. (as per Audit Plan)	To 31 st March 2012	Comment
% of annual audit plan achieved. Based on number of audits.	92%	83%	Output was affected during this transitional year with staff reducing from 4 to 3 and adapting to new management arrangements. The outstanding audits will be finalised.
Sickness – average days per employee.	4	2.52	
Training – average days	4	10.36	Time includes for internal and external seminars/training. All auditors hold a relevant qualification and two are studying for a higher qualification.

Criteria	Target p.a.	Actual To 31 st March 2012	Comment
Final audit reports issued within 10 available working days of agreement to draft report.	100%	100%	
Level of customer satisfaction	94%	97.11%	Based on 8 satisfaction surveys received.