

**INTERNAL AUDIT YEAR-END REPORT 2011/12****OVERVIEW OF WORK UNDERTAKEN**

1. Overall the Internal Audit Team have achieved 85% of the 2011/12 Annual Audit plan and as 15% of work is still in progress expect to complete 100% in due course. This included 100% achievement of the core financial systems reviews relied upon by the council's External Auditors for their risk assessment of the authority.
2. The original 2011/12 plan contained 58 projects, during the year 11 projects were removed (as a result of a change in requirements or to allow for emerging risks), and 12 new emerging risk projects were added. As a result the actual plan contained 59 projects. Of these 50 (85%) have been completed and 9 (15%) are still in progress.
3. In addition to this 90 days have been spent on projects carried forward from 2010/11, 62 days have been spent on investigating suspected financial irregularities (38 days less than the annual allocation), 62 days have been spent on providing professional advice on internal control and risk mitigation (2 days more than the annual allocation) and 36 days have been spent on standard follow-ups of audit recommendations with a further additional 12.5 days spent on non-standard follow-ups that required further audit testing (28.5 days over the annual allocation). The annual allocation for follow-up is an estimate of how many days will be required for following up red and amber reports based on 2 days per report and is dependent on how many reports are issued. The mid-year report flagged up that results at mid-year indicated that this allocation needed to be increased for the second half of the year.

**Summary of Key Issues**

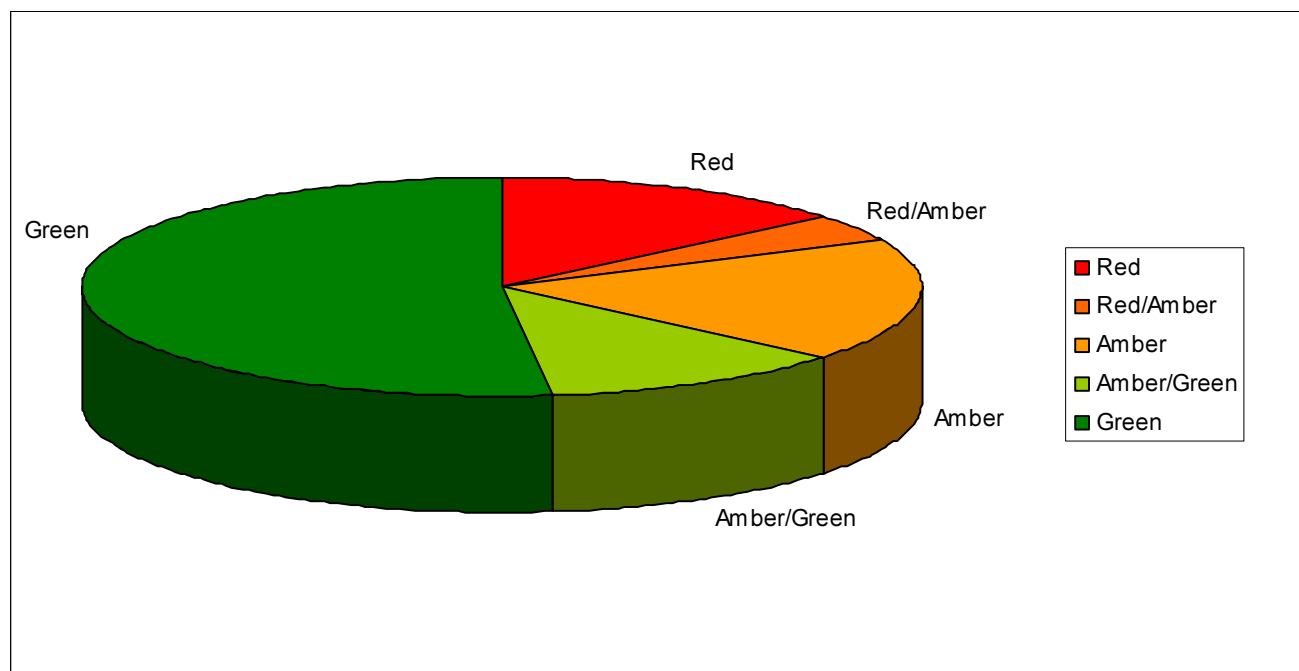
4. The key issues highlighted by Internal Audit work undertaken in 2011/12 include the continuation of inconsistent practices across the Council and across schools e.g. the control of income and petty cash and the monitoring of contracts and an inconsistent level of compliance with Financial Regulations/Contract Procedure Rules as demonstrated by the work on the raising of orders and payment of invoices.

**Assurance Reports**

5. Audit reports are traffic lighted to indicate the level of assurance that can be obtained from the system under review. This ranges from green reports indicating that a system is well controlled and therefore a low risk to the authority to red reports indicating that a system represents a high risk to the authority needing immediate attention to improve the control environment.
6. As the Internal Audit Plan is risk based it concentrates on systems that have been identified as high risk by management via inclusion in the corporate risk registers or during consultation on the audit plan or by internal audit based on cumulative audit knowledge and audit risk assessment. As a result there is an expectation that a higher number of audits will be given a red or red/amber assurance and this has been borne out by the results over previous years: In 2008/9 41% of assurance levels were red or red/amber; in 2009/10 it was 50% and in 2010/11 it was 42%. However during 2011/12 this fell to 30%.
7. A total of 50 internal Audit reports were issued during the year 7 red assurance, 2 red/amber assurance, 9 amber assurance, 6 amber/green and 26 green assurance

Table 1 below illustrates the mix of the assurance levels given to reports issued in 2011/12.

**Table 1 – Traffic Light Reports 2011/12**



8. The table shows that 70% of the traffic lighted systems reviewed during 2011/12 were given an amber, an amber/green or a green assurance rating i.e. over 61% expected controls operating at the time of review.
9. A total of 310 recommendations were made of which 306 were agreed (or alternative actions agreed) for implementation which meets the 95% performance target.
10. During 2011/12 a total of 220 recommendations have been followed up. The follow-up of 189 have been completed and the follow-up of the remaining 31 are still in progress. Of those completed a total of 120 have been implemented, 52 were partially implemented/in the process of being implemented, 3 were planned for implementation, 1, although originally agreed by management, was not implemented and 11 were no longer applicable due to system changes. This represents a 67% implementation (of recommendations still applicable) however a further 31% are in progress or were planned at the time of follow-up thus it is expected that in due course 98% will be implemented. It was identified that the majority of those not yet implemented was due to a slower than agreed implementation.

### Emerging Risks

11. Emerging risks are areas of risk arising during the year that were not apparent at the time of the annual planning process but that are considered significant enough by management/internal audit to warrant audit input. The emerging risk areas arising during 2011/12 were:
  - Financial Regulations Consultation/Amendment
  - CRC Annual Report Sign Off
  - School Financial Value Standards
  - Energy Bills
  - Capital Testing
  - Gated Alleyways

- Localisation of Council Tax Support\*
- Integration of Public Health\*
- Business Support Hub\*
- Modernising Terms and Conditions
- CIPFA Financial Management Review
- Shop4Support\*

\* These emerging risk have become projects in the 2012/13 Internal Audit Plan.

## COMPLIANCE WITH STANDARDS/DELIVERY PLAN

12. The CIPFA Code of Practice for Internal Audit in Local Government in the UK defines the way in which the internal audit service should undertake its functions. The code includes a checklist to test compliance with the code that is used as a self-assessment tool to review the IA each year. The results of this self-assessment indicated that the section complied fully with 89% of the standards and partially with a further 6% during 2010/11. It was identified that key areas to be addressed were the review and update of the Internal Audit Terms of Reference and a formalisation of some audit protocols e.g. around partnership working. These were included as actions planned in the Internal Audit Delivery Plan for 2011/12 however due to the low level of Internal Audit resources and the demand for Internal Audit work less time has been available for the development of the service and as such the level of compliance with the CIPFA Standards remained the same for 2011/12. The actions will be carried forward to the 2012/13 Internal Audit Delivery Plan.

## INTERIM OPINION ON THE OVERALL CONTROL ENVIRONMENT

13. This is an interim opinion based on internal audit risk based work and will be updated once the core financial systems work for 2011/12 has been completed and the results of the management assurance exercise for 2011/12 are available.
14. The adequacy and effectiveness of the organisation's control environment for the 2011/12 financial year has been assessed as "adequate" based on the following:
  - 70% of the traffic lighted systems reviewed during 2011/12 were given an amber, an amber/green or a green assurance rating;
  - 99% of recommendations made during 2011/12 were agreed for implementation;
  - 67% of recommendations followed-up have been implemented, 31% are in progress or are planned at the time of follow-up thus it is expected that in due course 98% will be implemented. 100% of follow-ups resulted in an improved assurance rating.
  - 19 suspected financial irregularities were reported to Internal Audit during 2011/12, the majority of irregularities investigated by Internal Audit were either caused by a break down/lack of control or where fraud was involved this was a contributing factor. In 9 (47%) cases there was no loss or the loss has been recouped (e.g. from banks, insurance or individuals); in 3 (16%) cases there was a loss of over £2000 and in 7 (37%) cases work is ongoing to establish whether a loss has occurred and/or the level.

## SUMMARY OF WORK UNDERTAKEN

**Audit of Core Financial Systems – Updated Report**

15. As part of the 2011/12 Annual Plan Internal Audit undertook a key control review on the following systems as part of the agreed approach to the audit of the Authority's core financial systems for the financial year 2010/11 (reported in detail in the mid-year report):
- Housing Benefits
  - NDR
16. Overall out of a total of 19 key controls reviewed 14 (74%) were fully operating, 3 (16%) were substantially operating and 2 (10%) were partially operating. In total 4 recommendations were made, which were all medium risk. All 4 recommendations have been agreed for implementation.
17. The position for each system reviewed is shown below.

SYSTEM	NUMBER OF CONTROLS	FULLY OPERATING	SUBSTANTIALLY OPERATING	PARTIALLY OPERATING	NOT OPERATING	OVERALL RATING <sup>1</sup>
Housing Benefits	8	4	3	1	0	93%
NDR	11	10	0	1	0	95%
<b>Overall</b>	19	14 (74%)	3 (16%)	2 (10%)	0 (0%)	94%

18. For the HB system overall, 80% of the elements of the controls were operating effectively, with a further 3% substantially operating and 17% partially operating. Each of the 8 key controls is made up of a number of individual elements that were each tested. Therefore 4 key controls are fully in place, 3 key controls are substantially in place and 1 key control is partially in place. 3 recommendations have been made to address the weaknesses identified which are all rated as medium risk.
19. For the NDR system overall, 92% of the elements of the controls were operating effectively, with a further 4% substantially operating and 4% partially operating. Each of the 11 key controls is made up of a number of individual elements that were each tested. Therefore 10 key controls are fully in place and 1 key control is partially in place. 1 recommendation has been made to address the weakness identified, and 1 weakness identified was immediately actioned during the review and no further recommendation is therefore made. The 1 recommendation made is rated as medium risk.
20. In addition to satisfy additional requirements of the External Auditors, Control self-assessments were obtained from the relevant managers for the following core financial systems:
- Housing Rents
  - Corporate Accounts Payable
  - Corporate Accounts Receivable
  - Council Tax
  - Payroll
  - Treasury Management

<sup>1</sup> Operating controls given a weighting of 2 and partially operating controls given a weighting of 1

and systems documentation was reviewed/updated and walkthrough tests were undertaken to confirm the actual system in operation for all the above core financial systems.

21. For 2010/11 Treasury Management was included in the core financial systems reviews for the first time as agreed with the External Auditors. A full review was carried out in 2010/11 and this was a green report. Overall 90% of the expected controls were found to be in place and operating effectively, 4% were substantially in place with a further 6% partially in place. 6 recommendations have been made to address the weaknesses identified, 4 were rated as medium risk and 2 was rated as low risk. The most significant weakness related to a loan for 20 million pounds only having authorisation via an email. As part of the 11/12 Audit Plan the systems documentation was reviewed and updated and walkthrough tests were carried out.
22. In addition, it has also been agreed that as part of the 2011/12 Audit Plan capital expenditure will also be included in the core financial systems reviews. The capital expenditure review is currently still in progress.

### **Reliance**

23. The Authority's External Auditor's, Deloitte LLP, placed reliance on the work undertaken by Internal Audit as part of the 2011/12 Annual Plan in relation to the Authority's core financial systems in operation during 2010/11 for their risk assessment of the Authority.

### **Other Reliance/Risk Reviews undertaken in 2011/12**

24. Appendix C details all the final reports, draft reports and follow ups issued in 2011/12.

### **Other Work**

25. Other work undertaken annually in the first quarter includes the completion of reviews from the previous years plan, the completion of the annual Management Assurance exercise and the annual governance review feeding into the authority's Annual Governance Statement (AGS). Both of these were successfully completed with the results already reported to the GARM committee.
26. Management Assurance: Completion of the 2010/11 annual management assurance exercise including preparation of the summary report, reality checking and input to the 2010/11 Annual Governance Statement plus follow - up of action planned.
27. Corporate Governance Working Group – lead by the Service Manager Internal Audit, reviews governance arrangements across the Council, undertakes the annual review of governance feeding into the Annual Governance Statement and reports to the Corporate Governance Group.
28. Corporate Strategic Risk Group: Set up to assist the Council in embedding and enhancing the risk management process to ensure that risks are actively managed so that the council can achieve it's objectives, take advantage of opportunities and serve Harrow's community better. The Service Manager, Internal Audit attends quarterly meetings.
29. Information Governance Board: Internal audit attends and contributes to the Information Governance Board.

30. Improvement Boards: Provision of information on the production of draft and final IA reports and follow-ups undertaken to support quarterly improvement boards.

### Professional Advice

31. A range of professional advice was provided by the IA Team across the council during the year covering controls, risks, compliance with Financial Regulations and Contract Procedure Rules and systems' development. Areas covered included advice to schools, grants, apprenticeship scheme, community lettings, council tax refunds, delegations, and virements.

### Suspected Financial Irregularities

32. During 2011/12, 19 suspected financial irregularities were reported to Internal Audit. Investigations into 75% of these have been concluded with no significant loss to the Council. 1 of the 19 SFIs has resulted in the issue of an Internal Audit report. See Appendix B.

### FOLLOW-UP OF AUDIT RECOMMENDATIONS

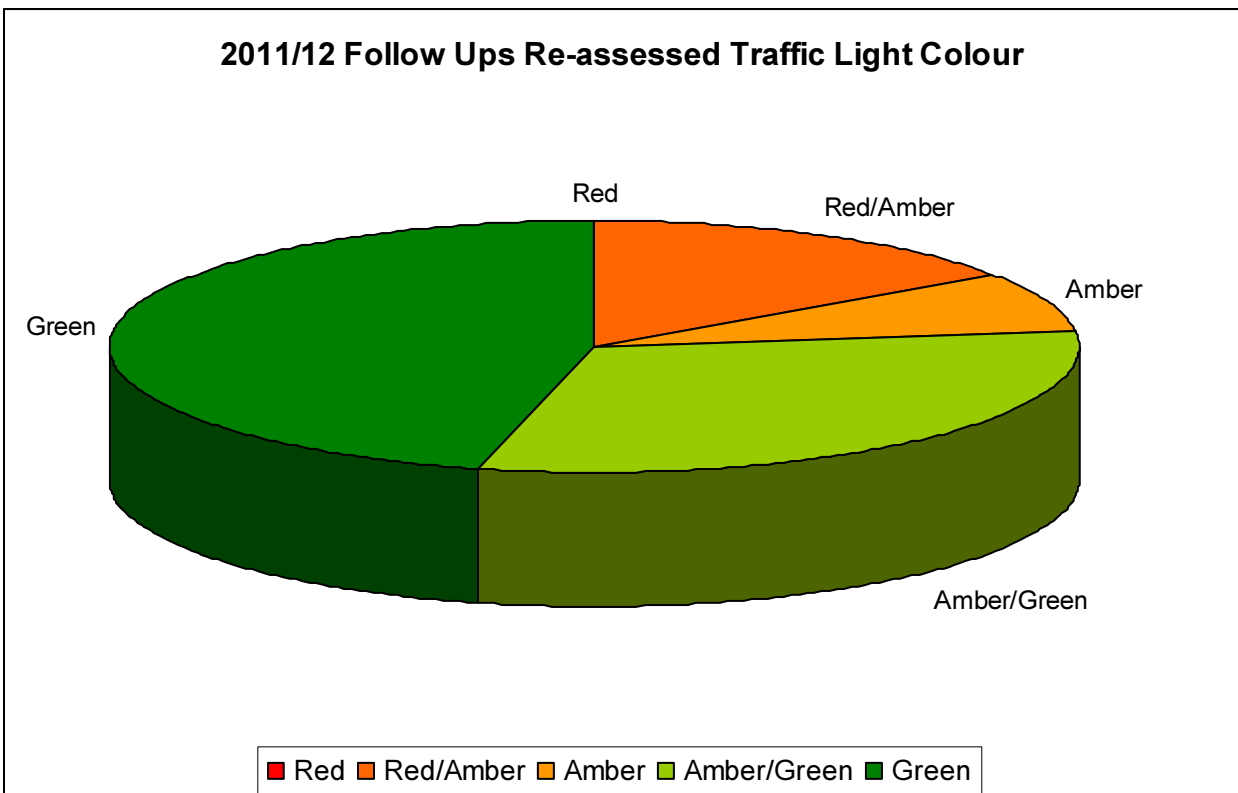
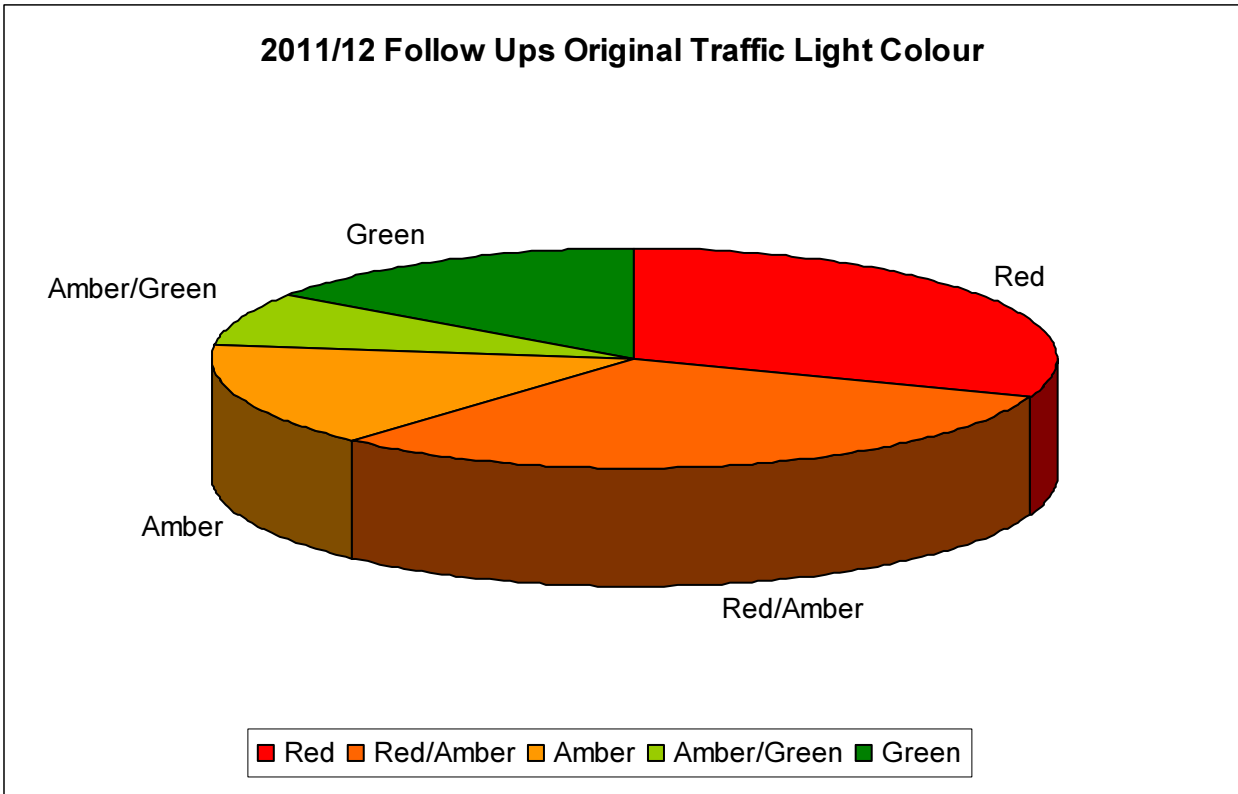
33. The Internal Audit policy on follow-up is to follow-up red and red/amber reports after 3 months and to follow-up amber and amber/green reports after 6 months, reassessing the traffic light of each report. Green reports are not followed up as they are low risk unless it is a core financial system review.
34. During 2011/12 a total of 220 recommendations have been followed up of which 189 have been completed and 31 are still in progress. Of those completed a total of 120 have been implemented, 52 were partially implemented/in the process of being implemented, 3 were planned for implementation, 1, although originally agreed by management, was not implemented and 11 were no longer applicable due to system changes.
35. Of the 18 reviews where the follow up has been completed, 4 were red reports, 4 were a red/amber report, 2 were amber reports, 1 was an amber/green report, 2 were green reports (key control systems) and 5 were reports that had not been traffic lighted. In accordance with the Internal Audit policy on follow-ups the reports shown in table 2 and the pie charts below were reassessed as part of the follow-up and a new audit opinion issued showing the updated traffic light position:

**Table 2 – Re-issued Audit Opinions**

<b>Report</b>	<b>Original Traffic-light</b>	<b>Re-assessed Traffic Light</b>
Asbestos Management – Housing Stock	Red/amber	Amber/green
Libraries – 1 <sup>st</sup> Follow up	Red	Red/amber
Stock Control – Libraries	Amber/green	Green
Camrose Primary	Amber	Amber/green
Sickness Absence – 2 <sup>nd</sup> Follow up	Red/amber	Amber
Housing Benefits – Quality, Overpayments & Write Offs	Red	Amber/green
Capability Procedure	Amber	Amber/green
Leaseholders Electricity	Red	Red/amber
NDR Key Control	Green	Green
Housing Benefit Key Control	Green	Green
Libraries – 2 <sup>nd</sup> Follow up	Red/amber	Green

Heathland CCTV	Red/amber	Green
Krishna Avanti – SFI	Red	Green

36. All re-assessed reports showed an improved assurance rating; however 2 reports followed up were already a green assurance, but were reviews of core financial systems and hence followed-up and therefore remain unchanged.



## Productivity

37. The days available to implement the internal audit annual plan are based on an estimation of the team's productive time. To enable this estimation to be made, and to feed into performance indicator 3 (see section below), each auditor is required to record a breakdown of their time spent each day. Each element of productive time (i.e. every project/element of the annual plan plus any additions e.g. emerging risks) and each element of non-productive time (e.g. annual leave, training, audit management) is allocated a unique code and time is recorded against each code to the nearest 15 minutes. During 2009/10 the criteria for determining what constitutes productive time was revised to bring us inline with CIPFA guidelines and it was found that we had been recording many elements as non-productive that CIPFA's revised guidelines suggested could now be recorded as productive time e.g. annual planning and audit committee reporting.
38. The number of audit days available for the 2011/12 plan was determined via a detailed resource calculation for each auditor taking into account available days, actual days 2010/11 and allowances for annual leave, training etc. A challenging target was set for each member of the team and the combination of these targets determined the days available for the Internal Audit Plan. 900 audit days were identified for the 2011/12 plan based on 200 productive days per Auditor and 100 days for the Service Manager.
39. The year-end position shows that overall the team have achieved 939 productive days which exceeds the target of 900 days by 39 days. On average each auditor (excluding the manager) achieved 190 productive days with the manager achieving 170 productive days. CIPFA guidance and benchmarking data indicates a range of average productive days from as low as 171 (average actually attained by comparator London Boroughs in 2009/10) to as high as 200 days (CIPFA target) per experienced auditor and recognises that this would be less for trainees and managers and the 2009/10 PwC review of Internal Audit indicated that 50% of the experienced auditors productive time would be reasonable for the manager.
40. In conclusion overall the Internal Audit team have performed extremely well in terms of productivity during 2011/12, however a consequence of this has been less time spent on development of the Internal Audit Service (see paragraph 12) and on training.

## PERFORMANCE INDICATORS

41. The Internal Audit Quality Assurance and Performance Indicators Framework was developed in compliance with the CIPFA Code of Practice and has been operating since 2007/08 (although reviewed/updated at least annually). The aim of the framework is to demonstrate that the internal audit service is:
- meeting its aims and objectives
  - compliant with the CIPFA Code of Practice
  - meeting internal quality standards
  - effective and efficient, continuously improving
  - adding value and assisting the organisation in achieving its objectives.
42. The performance and the effectiveness of internal audit is monitored by the Service Manager Internal Audit to ensure that it improves over time, in terms of both the achievement of targets and generally in terms of the quality of the service provided to the user and to identify areas for improvement.



43. Table 3 below outlines the seven indicators agreed for 2011/12, including the key indicator covering achievement of the IA operational plan and the results achieved.

**Table 3 – Internal Audit Performance Indicator Results 2011/12**

	<b>Indicator</b>	<b>Target</b>	<b>Mid Year Results</b>	<b>Year End Results</b>
1	Recommendations agreed for implementation	95%	95%	99%
2*	Final reports issued on/ahead of time	85%	100%	100%
3	Projects completed within budgeted time allowance	85%	90%	91%
4*	Target met for issue of draft report after end of fieldwork	85%	80%	100%
5	Follow-up undertaken	100%	100%	100%
6	Plan achieved for Key Control reviews	100%	100%	100%
7	Plan achieved overall (Key indicator)	90%	48%	85% - 100%

### Analysis of Results

44. 2 (29%) of the targets have been met, 4 (57%) have been exceeded and 1 (14%), whilst slighter under target at year–end will be fully met in due course.

45. With regard to the monitoring of positive and negative feedback, below are some of the positive comments received so far this year:

- Thanks - that was a very helpful session today
- Thank you for all your help and support in this matter. I hope that the school is able to move on now in a positive way.
- Thank you once again for your time and hard work

As reported in the Mid-year Report negative feedback was however received from one school during the first half of the year. This related to the fact that the Auditor had provided positive verbal feedback on the day of the audit visit but that during the quality check of the review a control issue had been highlighted and included in the report. This had not been verbally reported back to the school before the formal report was issued. This highlighted a training issue for the temporary Auditor concerned which will be address should he be employed in the future.

46. Although the implementation of audit recommendations is always reported at year end and has been reported in this years mid-year report it has not been a formal performance indicator. The Assistant Chief Executive has now requested that it be included and reported as a formal performance indicator and this was actioned in the second half of the year. In addition he has requested that auditee response times to draft audit reports and follow-ups be measured and reported as a formal performance indicator and this was also actioned in the second half of the year.

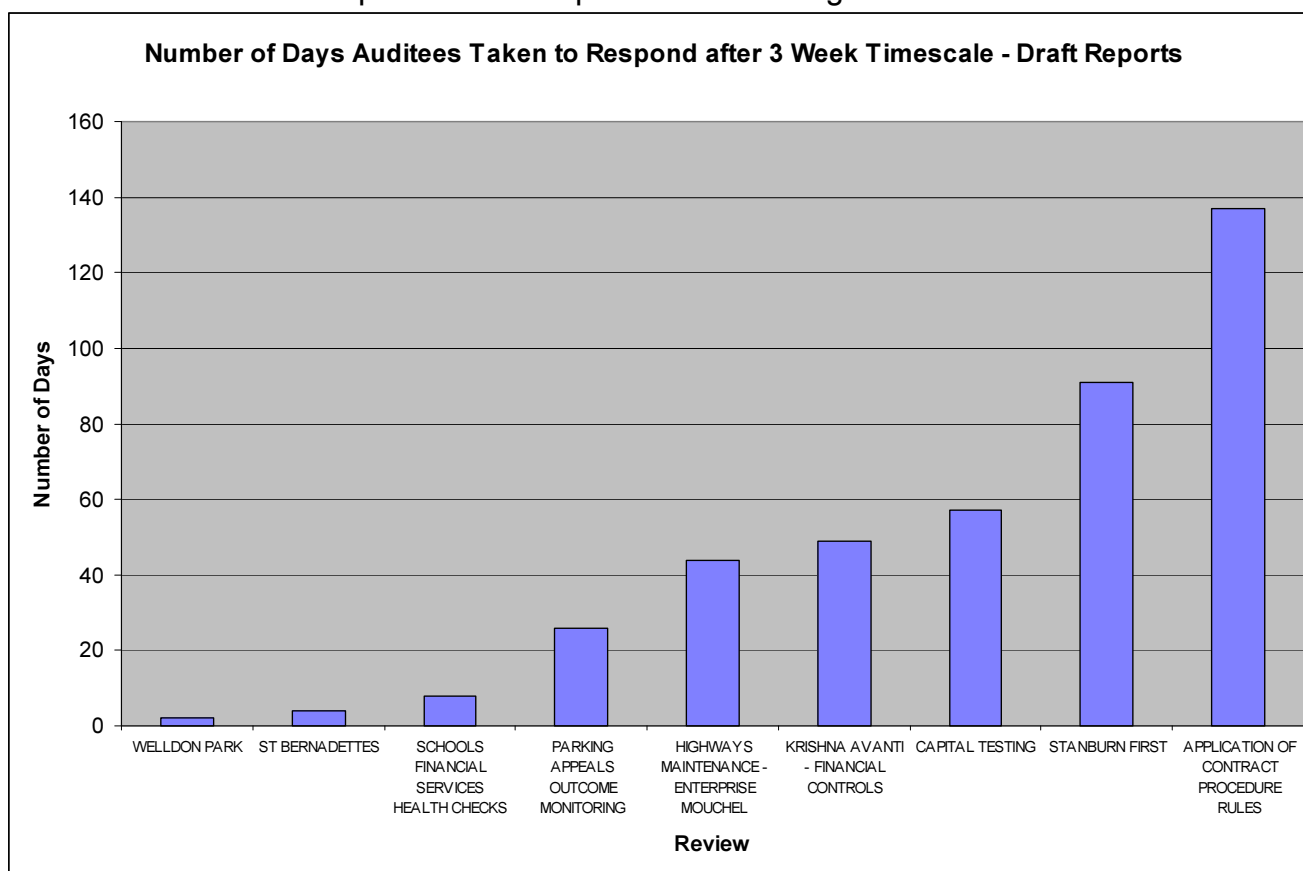
47. These indicators are reported below and have been separated from the Internal Audit Performance Indicators above as the implementation of audit recommendations and the responsibility to respond to draft audit reports and follow-up information requests falls to management. To reflect this they have been labelled Corporate Audit Indicators.

**Table 4 – Corporate Audit Indicators**

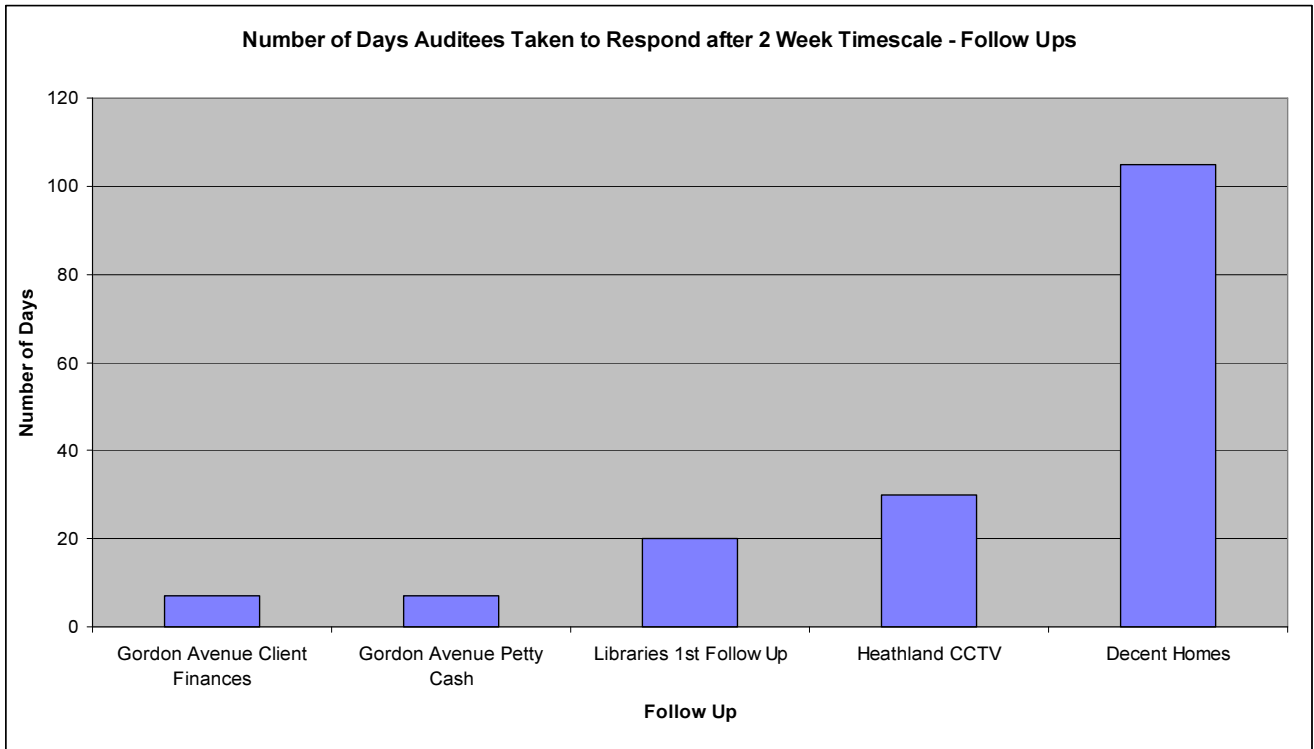
	Indicator	Target	Mid Year Results	Year End Results
1	Implementation of recommendations	90%	64% (expected to be 100%)	67% (expected to be 98%)
2	Auditee response times to draft reports within 3 weeks	80%	-	47%
3	Auditee response times to follow ups within 2 weeks	80%	-	72%

### Analysis of Results

48. As detailed in paragraph 10 of those recommendations where follow-up has been completed a total of 120 have been implemented, 52 were partially implemented/in the process of being implemented, 3 were planned for implementation, 1, although originally agreed by management, was not implemented and 11 were no longer applicable due to system changes. This represents a 67% implementation (of recommendations still applicable) however a further 31% are in progress or were planned at the time of follow-up thus it is expected that in due course 98% will be implemented. It was identified that the majority of those not yet implemented was due to a slower than agreed implementation.
49. The actual time taken for responding to draft reports within 3 weeks is well below the target and the table below identifies the number of days taken over the three weeks for auditees to respond to draft report where the target was not met.



50. The actual time taken to respond to follow-ups is below the target by 8% and the table below shows the number of days taken over two weeks for auditees to respond to the follow-ups where the target was not met.



51. There are a variety of reasons why auditees may take longer to respond to draft audit reports or follow-ups, many of them quite reasonable. However, although we do usually receive a response eventually chasing responses is not the best use of Internal Audit time.

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June 2012