**AUDIT AND ACCOUNTS
COMMITTEE
8 DECEMBER 2005**

ITEM 6

DERBY CITY COUNCIL

Report of the Head of Audit and
Risk Management

QUARTERLY INTERNAL AUDIT REPORT

RECOMMENDATION

1.1   To note the activity and performance of Internal Audit in the period 31 August to 18 November 2005 and to comment accordingly.

1.2   To review the proposed changes to the 2005/6 Internal Audit Plan.

1.3   To determine which if any audit report should be subject to a follow up report to the March 2006 Audit and Accounts Committee meeting.

1.4   To approve the revised approach to school audits.

1.5   To comment on the timetable for producing the 2006/7 Internal Audit Annual Plan

SUPPORTING INFORMATION

2.1   This report summarises the internal audit work completed in the period 31 August 2005 to 18 November 2005, identifies changes required to the internal audit plan and seeks a decision by the Committee to determine the audit reports it wishes to review in more detail at the meeting in March 2006.

Summary of internal audit activity – 31 August 2005 – 18 November 2005

2.2   Appendix 2 summarises the output of internal audit for the period. During the period, a further 20 of the audits that commenced before April 2005 were completed. This leaves 5 audits to be completed. In respect of audits that commenced from April 2005, the current year, a further 4 audits have been completed. The situation at the 18 November 2005 was that 35% of current year audit reviews had not been allocated. These remaining audits have all been categorised according to priority to ensure that all the priority one audits are completed before the 31 March 2006. The prioritisation of audit reviews is detailed in Appendix 3. Priority 1 audits are those which will be the focus of audit resources. The Priority 2 audits are still subject to postponement if insufficient audit resource is available to undertake them.

2.3   Appendix 4 provides full details of the number of recommendations in each category by audit for all final reports issued in the period. Table 1 provides a summary of the number of recommendations made by Internal Audit and those accepted by Management for all completed audits

Table 1: Classification of Recommendations Made

	Fundamental	Significant	Merits Attention
Recommendations Made	0	55	91
Recommendations Accepted	0	52	90

2.5   Table 1 shows that there has been a 97.3% acceptance rate for Internal Audit's recommendations. The difference between the number of recommendations made in the draft report and those accepted for inclusion in the final report occurs where the responsible managers can demonstrate that they have insufficient resources to meet the control recommended i.e. the introduction of separation of duties in a system requires additional resources or are able to demonstrate limitations in the system used that prevent the suggested control from being addressed.

2.6   Appendix 4 also provides details of Internal Audit's overall opinion on the adequacy of the level of internal control for each system reviewed. Table 2 below provides an analysis of audit opinion on the system of control. The Head of Audit and Risk Management will also brief members further on the main issues relating to each completed audit.

Table 2: Overall Audit Opinion, by Department

Department	Good	Satis-factory	Marginal	Unsatis-factory	Unsound	No Opinion	Total
Finance	2					2	4
Contract Audit							
Dev & Cultural Services		1					1
Governance	1						1
Commercial Services							
Schools						5	5
Education	1		1	1			3
Social Services			1	1			2
Policy						3	3
IT Audit						1	1
Total	4	1	2	2	0	11	20

Note: No opinion includes audits carried out prior to the introduction of the internal control environment assessment framework, all investigation work and audits where no report was written.

2.7   As a general policy, all audits rated as "unsound" or "unsatisfactory" will be brought to the Committee's specific attention. Members should therefore note from Appendix

4 that the audit review of Direct Payments within Social Services and the Schools Procurement review in Education have both been rated as "unsatisfactory". The Committee can be briefed further on these audits as necessary.

2.8   The Home to School Transport audit report was called in by the Committee at the September meeting. Development and Cultural Services are looking to ensure that they implement the recommendations as far as possible. However, they have been hampered by the recent departure of Transport Procurement Manager. In the current circumstances, they would find it difficult to adequately respond to the report to the Audit and Accounts Committee. The Director of Development and Cultural Services has, therefore, asked that Committee delay consideration of the report until the meeting in March 2006. In the meantime, the full report will be made available to the Committee in preparation for the March meeting.

Changes to the 2005/6 Internal Audit Plan

2.9   The audit plan is a flexible document and it is inevitably subject to some changes during the year as a result of emerging issues. Members will note in Appendix 2 that the number of "audit jobs" for 2005/6 has decreased from 107 to 95. This shows the net effect of new jobs added in and planned jobs removed as a result of the need for audit involvement in areas such as investigation work, additional assurance work, and advice on new systems.

2.10   Audit has a finite staffing resource, therefore, to take on this additional work, we have to review the audit plan and make amendments to the remaining planned audits. This can take the form of reducing audit coverage in a specific area or postponing the audit to the following year. To balance the available resources for 2005/6, it has been necessary to postpone several planned audit areas. Audit has also been asked by Chief Officers or managers to postpone specific audit areas because of changes currently taking place in those areas. The changes to the audit plan are detailed in Appendix 5.

2.11   A number of planned follow up audits will not now necessarily be undertaken using the normal follow up audit methodology. This process is the subject of a separate report on the Agenda.

Developments impacting on the Internal Audit Plan

Schools Audit Programme

2.12   At the September Committee it was agreed to bring back a report setting out the new approach that has been developed to schools audits, and this has been incorporated within the quarterly report.

2.13   Following Local Government Reorganisation in April 1997, Internal Audit embarked on a cyclical programme of school audits, which entailed a full review of all aspects of management and financial control within each of Derby's schools. This approach meets the expectations of the DfES. More recently there have also been a small number of cross cutting single-issue audits over a sample of schools, for example a general review of school procurement.

2.14   There are some weaknesses in the cyclical programme. The audits are lengthy and testing needs to be better focused on the most significant risks to the school, particularly in terms of major governance risks. The length makes the frequency low and even the 5 year primary school cycle is difficult to deliver within available resources. Turnaround of draft reports is also slow. The approach also needs to adapt to new expectations – from March 2007 there is a new requirement to provide an assurance that all secondary schools meet a Financial Management Standard drawn up by DfES, with the expectation that this will eventually be extended to primary schools.

2.15   A major revision to the approach to schools audits and the schools programme has therefore been undertaken, and piloted. Testing has been revised after benchmarking against practices in other authorities. To aid efficiency, schools are now provided with an advance checklist prior to the audit visit which details all documents which require examination during the visit. The revised programme requires an intensive 2 to 3 days on site in order to assess the controls and undertake appropriate testing. Visits now conclude with an immediate closing meeting at which the auditor communicates all findings, advises on control improvements and seek management's agreement to proposed recommendations. Improved documentation has also led to better turnaround of the reports. An overall opinion is also now given, determined by the number of control weaknesses identified, weighted by the significance of the risks. School audits will be subject to the same new follow-up process as proposed for all other audits included in the audit plan. Once finalised, audit reports will also be communicated to the relevant school governors as well as the headteacher. Initial results from the pilots are encouraging.

2.16   A summary of the control objectives examined in a visit to one of the pilot schools is listed in Appendix 6.

2.17   The pilot programme is being further revised to take account of the specific requirements of the new Financial Management Standard for Schools, as much of the assurance required will be dependent on audit testing. To ensure that all 13 secondary schools are meeting the standard, Internal Audit needs to carry out the reviews early enough to allow the schools sufficient time to implement improvements. It is anticipated that visits to secondary schools will be undertaken over the next 4 months to provide them with an independent assessment of their current compliance. The timing of the visits will also allow sufficient time for a follow-up before the March 2007 deadline. The timetable for the primary schools compliance with the standard has yet to be confirmed by the DfES. It is envisaged that any lessons learnt from the secondary school assessments will be given consideration when the approach to primary school assessments is determined.

2.18   It is still intended to supplement this approach with a small programme of single-issue reviews, as the reviews to date have been successful in highlighting issues of general concern.

Managed Audit

2.19   The Council's external auditors have scheduled their interim audit which reviews the work of internal audit for a 3 week period commencing 6 March 2006. They have requested that all internal audit work on the key financial systems is completed to draft report stage by the time they commence their interim audit work, or at the latest

by the end of the second week of their visit. To ensure internal audit meets this target, those key financial systems that have not been started have been allocated a priority one status and audit resources will be dedicated to this work over the next 3 months.

Annual Audit Plan 2006/7 - Timetable

2.20   The annual audit plan has usually gone to Cabinet in May or June each year. The Head of Audit and Risk Management would like to get the Plan agreed as close to the start of the new audit year (April 2006) as possible. The Committee is scheduled to meet on 6 April 2006 to consider the 2006/7 Audit Plan.

2.21   To achieve this target, a timetable has been drawn up. A copy is attached at Appendix 7. The key element is the gathering of information on any changes affecting the internal control environment within the Council. The intention is to contact managers in early December to revise the audit risk assessment.

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Background papers:	Internal Audit Annual Plan 2005/6
List of appendices:	Appendix 1 - Implications
	Appendix 2 - Internal Audit output - Summary
	Appendix 3 - Prioritisation of audit reviews
	Appendix 4 - Opinion/ No of Recommendations made in final audit reports issued in the period 31 Aug – 18 Nov 05 – By Audit
	Appendix 5 – Changes to 2005/6 Audit Plan
	Appendix 6 – Control objectives examined in school audits
	Appendix 7 – Audit Plan 2006/7 - timetable for production

IMPLICATIONS

Financial

1.   None arising directly.

Legal

2.   Under the Accounts and Audit Regulations 2003, the Council is required to maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper internal audit practices.

Personnel

3.   None directly arising.

Equalities impact

4.   None directly arising.

Corporate objectives and priorities for change

5.   Internal Audit contributes through its review work on the major corporate risks to the Council achieving corporate objectives and priorities. This is achieved by the audit of key systems and corporate governance issues and the associated risks. The work of Internal Audit is also relevant to the priority of 'value for money'.

Internal Audit Output – 2005/6 Audit Reviews

Current Year	No. of Jobs	Actual to 30 August 2005							
		Not Allocated	Allocated	Started	Awaiting Review	Reviewed	Draft Report	Final Report	Total
Contract Audit	3	2		1					3
Development & Cultural Services	10	4	3	1	1			1	10
Education	28	22		3	3				28
Finance	21	12	1	4				4	21
Corporate Governance	2	1	1						2
Derby Homes	6	6							6
IT Audit	7	1	3	2			1		7
Commercial Services	5	5							5
Policy	4	3		1					4
Fire Authority	5	2	2					1	5
Social Services	12	10			1			1	12
Corporate Services	2			1	1				2
External Bodies	2	2							2
TOTAL	**107**	**70**	**10**	**13**	**6**		**1**	**7**	**107**

Current Year	No. of Jobs	Actual 1 April 2005 to 18 November 2005							
		Not Allocated	Allocated	Started	Awaiting Review	Reviewed	Draft Report	Final Report	Total
Contract Audit	2	1			1				2
Development & Cultural Services	9	2	1	4	1			1	9
Education	24	12	2	3	4	1		2	24
Finance	23	5	5	6	3			4	23
Corporate Governance	2			2					2
Derby Homes	6	3	1	2					6
IT Audit	7		2	2	2		1		7
Commercial Services	3	3							3
Policy	2			1				1	2
Fire Authority	5	2		2				1	5
Social Services	7	4		1	1			1	7
Corporate Services	2			1	1				2
External Bodies	3	1		1				1	3
TOTAL	**95**	**33**	**11**	**25**	**13**	**1**	**1**	**11**	**95**

Internal Audit Output – Brought Forward Work

B/Fwd	No. of Jobs Planned	Actual to 30 August 2005								
		Not Allocated	Allocated	Started	Awaiting Review	Reviewed	Draft Report	Final Report	Audit Completed No Report	Total
Contract Audit	1							1		1
Development & Cultural Services	2					1		1		2
Education	12						6	6		12
Finance	13			2	1	2	1	7		13
Corporate Governance	4				1		1	2		4
Derby Homes	8						1	7		8
IT Audit	4			1				3		4
Commercial Services	2							2		2
Policy	7						2	5		7
Fire Authority	5						2	3		5
Social Services	5				1	2	1	1		5
Corporate Services										
External Bodies	1							1		1
B/FWD TOTAL	**64**			**3**	**3**	**5**	**14**	**39**		**64**

B/Fwd	No. of Jobs Planned	Actual 1 April 2005 to 18 November 2005								
		Not Allocated	Allocated	Started	Awaiting Review	Reviewed	Draft Report	Final Report	Audit Completed No Report	Total
Contract Audit	1							1		1
Development & Cultural Services	2							2		2
Education	12							12		12
Finance	13				1		1	10	1	13
Corporate Governance	4						1	3		4
Derby Homes	8							8		8
IT Audit	4							3	1	4
Commercial Services	2							2		2
Policy	7							5	2	7
Fire Authority	5							5		5
Social Services	5				1	1		3		5
Corporate Services										
External Bodies	1							1		1
B/FWD TOTAL	**64**				**2**	**1**	**2**	**55**	**4**	**64**

Prioritisation of 2005/6 Audit Reviews Yet To Be Allocated

Priority 1	Priority 2	Priority 3
Creditors	Contract Procedure Rules	Social Services – Adult establishment visit
Secondary Schools/Cheque Book Schools (11)	Building Control	
Treasury Management	Waste Disposal	
Finance Directorate - HR/Payroll	Education – HR/Payroll (FU)	
Debtors	Commercial Services - Electronic Invoicing	
Debtors IT	Commercial Services - Business Processes	
Derby Homes (3)	Commercial Services – Fleet Management	
Derbyshire Fire Authority (2)	Social Services – Voluntary Sector Liaison	
CLASP	Children in Foster Care	
	Child Protection	
22	10	1

Recommendations Made and/or Accepted in Final Audit Reports Issued in the period 31 August 2005 to 18 November 2005 – By Audit

Job Name	Overall control rating	Recommendations Made			Recommendations Accepted		
		Funda-mental	Signif-icant	Merits Attention	Funda-mental	Signif-icant	Merits Attention
Development & Cultural: Brought Forward							
On & Off Street Parking: Income & Fees	Satisfactory	0	2	9	0	2	9
Finance: Brought forward							
Treasury Management – Prudential Code	Good	0	0	6	0	0	6
Creditors – Central Function	Good	0	0	2	0	0	2
Cash and Bank (Follow Up)	N/A	0	0	0	0	0	0
Schools : Brought Forward							
Reigate Primary		0	5	10	0	5	9
Springfield Primary		0	6	11	0	4	11
Cherry Tree Hill Infants		0	8	9	0	8	9
Beckett Primary		0	4	4	0	4	4
St Chads CE Infant		0	6	10	0	6	10
Education : Current Year							
Osmaston/Allenton SureStart Cafe	Marginal	0	5	6	0	5	6
Pupil Numbers (PLASC)	Good	0	0	2	0	0	2
Education : Brought Forward							
Schools Procurement	Unsatisfactory	0	4	3	0	3	3
Governance : Brought Forward							
Accommodation Planning	Good	0	0	0	0	0	0
Policy : Current Year							
Community Safety Partnership – Budget Monitoring Statements (Advice)	N/A	0	0	0	0	0	0
Social Services : Brought Forward							
Debt Management	Marginal	0	6	4	0	6	4
Direct Payments	Unsatisfactory	0	9	15	0	9	15
Total Recommendations Made – Final reports		0	55	91	0	52	90

Note: This Appendix does not include the 4 reports issued in respect of external contracts.

Changes to the Internal Audit Plan 2005/6

Jobs removed from Plan	
Dept	**Job Details**
D&CS	Home to School Transport Follow Up (F/U)
D&CS	D & CS Starters, Leavers and Variations F/U
D&CS	On & Off-Street Parking: Income & Fines F/U
Education	Schools - Ordering & Invoice Processing F/U
Education	Schools Procurement - 1 Apr 2003 to 30 Sep 2004 F/U
Education	Primary / Junior / Infant Schools (3)
Education	Funding
Finance	Grants - Corporate Strategy F/U
Finance	Payroll - Central Function F/U
Finance	Benefits - System Logs & Trails F/U
IT Audit	Wireless Network
IT Audit	Firewall Configuration
Comm S	HR/Payroll: Starters, Leavers & Variations (London Road) F/U
Comm S	Housing Repairs & Maintenance Contract
Comm S	Trade Refuse F/U
Policy	Supporting People
Policy	Supporting People - Contracts F/U
Policy	Youth Offending Service
Soc Serv	HR/Payroll: Starters, Leavers & Variations F/U
Soc Serv	Social Services Debt Management F/U
Soc Serv	Adoption & Fostering F/U
Soc Serv	Assessment & Care Management
Soc Serv	Assessment & Collections (Financial Assessments)
Soc Serv	Direct Payments F/U
Soc Serv	Adult Establishment - The Knoll Hostel F/U
Corp Serv	Members Services

New Audit Jobs not in 2005/6 Original Audit Plan	
Job No	**Job Details**
244	BVPI 82a,82b & 84 (Household Waste Collection)
509	Parking Services Project Assurance
414	Interreg III B Interim to 30/6/05
213	Inv. Sinfin Community School
422	Investigation 2005-6 - TES Officers Travel Claims
493	Springwood LC - Security
298	Establishment Visit Osmaston / Allenton Sure Start
483	TR17 Teachers Pension Return
58	HR / Payroll / Costing: Remote System Access
307	Creditors - Cheque Requisitions
63	Council Tax - Online Balance Enquiry
474	Investigtion: Cheque Fraud
484	Investigation: Alleged Payment
307	Creditors Advice
504	Accounting Systems: Payroll Control Accounts
505	Financial Services: Control Accounts
500	Sharepoint Project
501	Community Safety Partnership - Budget Monitoring
498	Asian Over 60's Grants Verification
476	Investigation: Moorfields Childrens Centre
485	Allenton Market
496	East Midlands Centre of Excellence

Control Objectives Examined in Schools Audits

Control Objectives Examined
Corporate Governance - To ensure the school has adequate corporate governance arrangements in place.
Budgetary Control - To ensure that adequate and effective procedures are in place for the preparation, monitoring and control of school budgets.
Purchasing - To ensure that procedures for processing orders and invoices are in compliance with internal rules. Payments are made only in respect of goods and services received that have been properly certified and that value for money is obtained from non-approved suppliers.
Staffing - To ensure that arrangements made for the recruitment and selection of staff and absence monitoring are in compliance with the LEA guidance.
Computer Security - To ensure the security of the computer system is adequate, any confidential information including pupil and staff data is restricted and secure and there are adequate back-up procedures in place.
Security of Assets - To ensure that school equipment and assets are appropriately recorded and disposed of and a physical check of all inventory items is carried out on a periodic basis.
Private School Funds - To ensure that arrangements are made for the proper administration of unofficial funds and that the annually audited financial statement and accounts are submitted to the Governing Body.
Income - To ensure that all income received is in accordance with approved charges, is properly recorded, secured, and promptly banked in full. Any debts raised are issued promptly, payments monitored and reminders issued for unpaid invoices.
Imprest – To ensure that the local bank account is being managed and administered in accordance with the local payments scheme and Financial Regulations.

Audit Plan 2006/7 - Timetable

Action	Who	Deadline
Review existing methodology	RB/KS/AM	2 December 2005
Arrange meetings for January 2006 with Departmental Management Teams to discuss emerging issues, risks etc	RB	2 December 2005
Review and update existing information on auditable areas	KS/AM	16 December 2005
Meet with AD (Corp Finance), Heads of Finance, Group Accountants, Strategic Planning and Performance Unit	KS/AM	January 2006
Identify and evaluate new auditable areas	RB/KS/AM	20 January 2006
Determine available audit resource	KS/AM	20 January 2006
Prepare initial draft audit plan	RB/KS/AM	3 February 2006
Arrange meetings with Depts to discuss draft plan for w/c 13 February 2006	RB – Chief Officers KS/AM – ADs etc MM/AF GW – IT Audit	3 February 2006
Audit management meeting to discuss Draft Plan	PW/RB/KS/AM/MM/AF	6 February 2006
Meet with ADs to discuss draft plan	KS/AM/MM/AF GW – IT Audit	W/c 13 February 2006
Meet with COs	RB	W/c 13 February 2006
Produce revised draft plan	RB/KS/AM	24 February 2006
Discuss draft plan with PwC	RB/KS/AM	7 March 2006
Audit Plan report to Audit Committee 6 April 2006	RB	23 March 2006 for Pre-Agenda