

ANNUAL REPORT OF THE INTERNAL AUDIT SERVICE 2006/07**1. Introduction**

In accordance with the Council's adoption of the CIPFA Code of Practice on Internal Audit this report is submitted to the Audit Sub-Committee. The areas covered are objectives, resources, management, non-audit functions, planned audits, fraud and irregularity, contract audit, computer audit, the audit plan and special investigations / assignments.

2. Strategy and Objectives

The strategy and objectives are detailed in the Internal Audit Service Strategy 2004-07 a supporting document of the Financial and Property Services Service plan that is, in turn, submitted to committee as part of the Corporate and Service Planning process. The role and responsibilities are also included.

3. Resources

The section comprises three auditors and has been fully staffed throughout the year. The service has access to all systems and endeavours to undertake audits, with minimum disruption to services, by using computer resources and other technology.

4. Management

A long-term strategic plan is produced, using risk assessment as an evaluator to determine audit coverage. The plan is reassessed every year and an annual work plan produced. These audit plans are prepared on assessed need and based on the audit establishment.

Internal Audit operates the Managed Audit concept in conjunction with our external auditors, the Audit Commission. Managed Audit primarily concentrates on the fundamental financial systems and those core financial control systems that form the basis of the Authority's accounts. Each year joint working arrangements are agreed with the Audit Commission to enable them to rely on the work of Internal Audit.

The Audit Commission also undertakes a comprehensive annual review of Internal Audit and in the 2006/07 review adjudged the service to be satisfactory.

5. Non-Audit Functions

The section undertakes a number of routine control and administrative functions. Some of these are primarily areas in which an audit presence is considered vital but there are others that could be transferred to other sections, which will be reviewed during 2007/08.

In addition the Audit Manager is involved in other managerial responsibilities including corporate governance, fraud awareness, security and public interest issues.

6. Planned Audits

Of the systems reviewed the following are worthy of specific note:-

Fundamental Financial Systems

- a. **Payroll (value of transactions processed £10.6m)** – In addition to the standard audit, Criminal Record Checks and Contracts of Employment have been examined. There were no major weaknesses found in this system
- b. **Council Tax (value of transactions processed £35.0m)** - All key controls were operating in the Council Tax system, no significant weaknesses were found and previous recommendations have been implemented.
- c. **NNDR (value of transactions processed £16.7m)** – The system has been operating effectively and any problems have been addressed during the course of the audit. Void inspections are undertaken by Derby City on both Council Tax and NNDR properties and are up to date.
- d. **Creditors (value of transactions processed £19.0m)** – The Creditors system operates with a high degree of internal control but, although no major weaknesses were found, the procedure for invoice submission is not being consistently applied, this is being addressed.
- e. **Housing Benefits (value of transactions processed £14.6m)** - This system continues to operate efficiently with only a slight dip in performance that has been recovered. The current computer system plays a big part in this function particularly within the processing routines for application assessment. The Authority has been considering a replacement system for several years. Last year Anite's Pericles system was our contracted solution but difficulties have seen a move to the Capita Academy system and this is to be implemented from October 2007. The importance of having a reliable and accurate benefits system cannot be overstated.

Core Financial Control Systems

This section covers the three main processes of the Accounts audit namely, the Main Accounting System, the Budgeting and Budgetary Control System and the Final Accounts closedown. Internal Audit undertakes the first two audits and External Audit undertakes the Final Accounts audit. There are also some ancillary functions such as the Capital Accounting process that are integral to these major systems. Bank reconciliation plays a major part in verifying the integrity of the main accounting system and is also included in this section.

Main Accounting System - This was examined and all controls employed were reviewed.

From April 2004 the Authority implemented the *Agresso New World* financial system, which includes Ledger, Creditors, Debtors and Budgetary Control modules. On implementation of the new ledger problems arose most of which were

associated with our co-hosting arrangements with Derbyshire Dales. Many of these security and control issues were removed with the cessation of this arrangement.

Difficulties have been experienced in agreeing the cash book to the general ledger during 2004/05 and 2005/06. This has occurred as a result of integrating existing systems with new systems without fully testing the outcomes. This in turn has affected the bank reconciliation process and consequentially verifying the integrity of the ledger.

Recommendations were made in last years audit for a monthly reconciliation of the cash book to the ledger. It is pleasing to report that this process has been implemented with great success.

Budgetary Control - The budget setting and budgetary control system has been examined, in general all controls proved to be operating satisfactorily. The Authority uses a spreadsheet system to provide managers with budgetary control information. Internal audit have recommended greater use of the Agresso system to provide this information on line. Improving management information, in this respect, is currently being developed within an Agresso development programme.

The three-year forecast is predicting balances close to our minimum recommended level on the general fund account. The Housing Revenue account works on a much longer forecast period in determining reserves. The use of a longer period of forecast for the general account is being considered.

Bank Reconciliation – During 2005/06 a number of difficulties arose in agreeing the cash book to the Agresso Ledger and verifying the reconciliations. A number of recommendations were made to improve the process and integrate the reconciliation with the ledger.

The financial year 2006/07 has seen considerable improvements in the ledger/cash book reconciliation process and the bank to cash book reconciliation is up to date. Monthly verification between the ledger and the cash book is now a regular control feature. This latter process ensures that the cash book is complete. The only issue still to be resolved is monthly completion of the payments account reconciliation, which is being addressed.

Local Systems

Planning and Building Regulation Fees – The overall administration and controls were found to be satisfactory with the exception of the recording and banking of cheque payments. Recommendations have been made to ensure corporate payment procedures are adhered to and these are being implemented.

Housing Renewal Grant – Whilst there were several issues concerning minor administrative errors and omissions these did not give audit reason to doubt the overall adequacy and administration of the system. The calculation and payment of grants are controlled with secondary officer checks and evidence to support the payments. Administrative improvements are being introduced to ensure the completeness of grant records.

Etwall Leisure Centre – The Centre was found to be operating in line with the expected controls for 2006/07 with good management and administrative procedures overall. All recommendations are being implemented.

Rosliston Forestry Centre – The business plan and the proposal to extend the management contract were examined during 2005/06. The financial forecasts for the Centre were seen as ambitious and not tied into the Authority's own budgets; this in itself represented a risk to the Authority and consequently the other partners. As a result of the audit a more pragmatic approach has been adopted to the Business Plan financial forecasts. During 2006/07 the situation has been monitored and whilst the forecasts have not quite been achieved this review has confirmed that the level of control over the Centre's operations has improved and its aspirations are on a more realistic footing.

Car Allowances – The car allowance system including procedures and claim forms is sound and available to both users and authorisers on the intranet. In addition guidance is available to supervisors and managers on how to verify the authenticity of a claim. The system contains all the appropriate controls but the audit revealed that a significant number of claims were poorly and incorrectly completed signifying an adherence problem. On average the Authority's pays around £120k to staff and £20k to members each year in allowances. It was clear from this audit that the authorisers responsibility in certifying claims was not being diligently applied, as a consequence managers/supervisors with responsibility for authorising mileage claims were subsequently reminded that ultimate responsibility over the authenticity of a claim rests with them.

Car Loans – There are very few staff car loans and no weaknesses were found in the system

Local Area Agreement (LAA) – The financial and control aspects of the Safer South Derbyshire Partnership were examined and the claim to the accountable body verified. A number of recommendations were made regarding corporate control over the LAA and partnerships in general. These are presently under consideration.

7. Fraud and Irregularity

Five operational areas (Benefits, Renovation Grants, Cash Collection, Council Tax, and Cheques) were examined. There were no major issues raised and the Authority's anti-fraud and corruption controls in these areas are sound.

8. Contract Audit

The Financial Regulations and Procedure Rules including the Purchasing Code of Practice are being updated to include procurement and e-purchasing requirements.

9. Computer Audit

Annual Key Control audit checklists were completed on the system network, network management, internet/e-mail monitoring and management and security in general.

The IT Strategy and Communications Policy have been updated. The security policy is being updated in line with BS 7799 requirements as part of an ongoing programme.

10.Special Investigations

A number of investigations have been undertaken during the year. These included cash payments, security, expenses, car allowances, contracts and credit card thefts.

11.Statement Of Internal Control (SIC) - Internal Audit Assurance Statement

The Annual Report has traditionally covered the work undertaken by the service in a particular financial year i.e. April to March. Prior to 2003 all fundamental financial systems audits, affecting the accounts, were undertaken in the year following the year of account (May-October). There has been a move, over recent years, to undertake these in the latter part of the year of account. Therefore these audits have been progressively brought forward to enable this to occur. The final accounts closure date has also been brought forward and there is now a requirement to produce an Annual Audit Assurance Statement to support the Statement of Internal Control.

The Annual Audit Assurance Statement required for the 2006/07 year has to be produced in June and will include work undertaken in April and May 2007 relevant to the year-end core financial systems (Main Accounting, Budget setting and control, bank and feeder system reconciliations).

The Internal Audit Assurance Statement for 2006/07 can be found in Annexe A to this report.

12.Conclusion

The service has performed well during 2006/07 achieving 100% of the Managed Audit (completed audits to the External auditor's satisfaction) with 79% of the planned audits making 91% of the overall plan completed, against a target of 90%.

The Authority's ambitious programme of system replacement has shaped recent audit plans with all major financial systems scheduled to be replaced during the period 2003-2007. The demise of the Derbyshire Revenue and Benefits Consortium has seen the Authority procure its own system from Capita. There is a need to document and evaluate this new revenue package, as the level of internal control is unknown. This will be achieved in partnership with other Derbyshire authorities.

The service is moving more to Corporate Governance issues and initial system work has been carried out on partnerships with a series of checklists also being developed for various areas such as risk management, corporate framework, statement of internal control.

The service received the co-operation of all departments throughout the year.

Audit Manager