

ANNUAL REPORT OF THE INTERNAL AUDIT SERVICE 2010/11

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, a supporting document of the Corporate Services 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 Internal Audit establishment comprises three auditors, however in April 2010 our Senior Auditor retired from the Authority. This post has remained vacant throughout the year pending a review of service delivery options. Derby City Council Internal Audit Service has undertaken a number of audits during this period as part of an arrangement to supply additional days. 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, in conjunction with our external auditors, a managed audit approach which primarily concentrates on the material financial systems, these financial control systems form the basis of the Authority's accounts. Each year arrangements are agreed with the external auditors to enable them to rely on the work of Internal Audit, our current external auditors are Grant Thornton.

Since 2005 the service has been reviewed by a number of external bodies including the Audit Commission, Pritchard Stone and Price Waterhouse Coopers, all have adjudged the service to be satisfactory. Grant Thornton undertook an initial review when they were appointed and annual reviews in 2008/09 and 2009/10, their assessment also being satisfactory. Grant Thornton has undertaken a three year review of the service against the code of practice during 2010/11. The findings arising out of this work, including any recommendations, will be reported to Committee in June 2011.

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, in particular internal check functions, where there are operational difficulties in maintaining separation of duties. 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:-

Material Financial Systems

- a. Creditors (value of transactions processed £32.8m)** - The current Creditors System is a payment module of the *Agresso* main accounting system version 5.4 which is to be replaced by version 5.53 in 2011/12 with a purchase to pay facility offering paperless certification and payment among other benefits. The audit undertaken was the last audit on the existing system.

This year's testing encompassed invoice administration, segregation of duties, cheque despatch, Cash Book / Ledger reconciliation, payment by BACS and CHAPS, compliance with the Authority's Purchasing Code of Practice/Procurement guidance and security of the computer system. The audit covered the annual controls for 2009/10 and the key controls for 2010/11, all key controls were in place with no significant weaknesses encountered.

The system has been operating with a mix of interim and temporary ordering systems in place leading to differing certification approaches. Whilst this can be onerous in operation an acceptable level of control has been achieved. The introduction of the new version of *Agresso* should result in a standardised ordering approach. Related audits have also been undertaken on Cheques and VAT with no issues arising.

- b. Treasury Management** - This audit examines the Authority's short-term investments, loan activity and how the controls over these activities operated during the financial year. The Authority is relatively debt free in terms of loans from the financial markets with the exception of a £1M LOBO loan. The Authority uses its Treasury Management policy to help manage its cash flow throughout the financial year by borrowing or investing funds on a short-term basis. The loan system, policy statement, investments, loans, authorities, cash flow, interest calculation, bank transfers, registers and control accounts were examined. Apart from some minor issues the level of control was adjudged high.
- c. Debtors** - A review of the system controls has been undertaken, no major weaknesses were found and the day to day operation of the Debtors function is operating well. The management control information has been examined in detail and the year end control totals for 2010/11 have been verified.

The current Debtors System is an accounts receivable module of the *Agresso* main accounting system version 5.4 and like creditors it is to be replaced by the later

version in 2011/12. This new system will need to be examined in depth during 2011/12.

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 therefore is also included in this section.

Main Accounting System - This was examined and all system controls employed were reviewed. The ledger/cash book reconciliation and the bank reconciliation processes are up to date. The new payments account cheque reconciliation process is operating well. The introduction of the Agresso accounting system version 5.5 is included in the Corporate Services Partnering Contract and is presently being implemented.

Budgetary Control - The budget setting and budgetary control system has been examined; in general all controls proved to be operating satisfactorily. The budget profiling introduced a few years ago is working reasonably well on the revenue budgets but some problems have occurred when budgets have been applied to Capital expenditure. Poor communication and the suitability of the adopted method of profiling has meant the ledger budgets have not always been synchronised with the Capital Programme, this is being addressed. The budget setting working papers are of a high standard and thus the assurance level for this system remains high with no major weaknesses found.

Bank Reconciliation – The financial year 2010/11 has seen a new payments account and consolidated bank reconciliation in regular operation and no issues have arisen with the bank reconciliation process. During 2011/12 a new cash receipting/posting system and the Agresso cash book facility are programmed for implementation by Northgate PS; this will significantly change the bank reconciliation process. A system review will be necessary once these are implemented.

Local Systems

Improvement Grants – The function covers mainly Disabled Facilities and Home Repair Plus grants, the audit primarily concentrated on Disabled Facilities grants. The audit examined guidance/procedural documentation, departmental grant records, processing applications, approving grant works, inspection process, accounting records, reconciliation to the ledger and management information. The audit confirmed the overall level of control is good with no major weaknesses detected.

Partnership – This audit examined the governance arrangements in place for partnership working within the Authority. The audit aimed at highlighting any control weaknesses and risks in the Authority's overall approach to the governance of

partnerships. The control objectives covered policy and procedures, roles and responsibilities, partnership agreements, risk management and performance monitoring. The controls within these objectives have been evaluated. The issues raised are centred on policy and regular review of the Authority's Partnerships. These are being addressed and this is being reported to the Finance and Management Committee.

Growth- Point Partnership – an audit was undertaken to confirm that expenditure on Growth Point Projects in South Derbyshire for 2009/10 has been properly incurred and meets the eligibility requirements of the fund within the Derby Housing Market Area. The audit focussed on the grant related expenditure and the level of control within the systems used to manage and monitor that expenditure. Apart from some minor issues no significant weaknesses were found and all expenditure was properly incurred and conformed to the grant conditions.

Etwall Leisure Centre – audit work on the new Centre was undertaken in two phases with a number of recommendations being made. Phase one concentrated on the financial and administrative systems and phase two examined the construction of the Centre and how this affected running costs. The Leisure Centre is a much larger operation than previous offering additional, as well as improved, facilities. These establishment audits identified a number of weaknesses many of which were resolved during the course of the audit. The booking and receipting system had some issues but additional training, user permissions and administrator rights solved most of them. A follow-up audit has confirmed that security collections have been established and the CCTV system has been installed.

Housing Maintenance – a system audit has been undertaken on the responsive repairs function examining the process from initial reporting of the repair to completion of the job. Plumbing, brickwork and carpentry are the main trades provided by our own workforce and this is supplemented by electricians. Testing has been undertaken on all aspects of the process namely tenant repair request, job sheet, completion, tenant satisfaction, inspection and charging the majority of which were operating satisfactorily.

7. Fraud and Irregularity

Six operational areas (Cheques, Creditors, Cash, Treasury Management, Car Loans and Allowances) 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

Less time has been available in this area due to the retirement of the Senior Auditor. The service has concentrated on current contract requirements and the contract records. This includes tender opening attendance and administration, tender documentation, arithmetic checks, bank references, company searches, financial vetting, assessing accounts, director/individual checks, sealed document notification, contract payment register and individual contract records. Work has also been undertaken on the Corporate Services Partnering Project contract.

9. Computer Audit

The introduction of new systems requires audit time in their development and implementation stages to evaluate and assess the controls. Agresso version 5.53 accounting system, Academy's Cash receipting and posting system and Northgate's Resource-link HR and Payroll systems are planned for the first quarter of 2011/12. Control audit checklists were completed and assistance given on the PCI procedure and government portal assessment.

10. Special Investigations

A number of investigations have been undertaken during the year. These included capital accounting, income management, cash queries and summaries including over and under bankings. Assistance given to other auditing bodies, including the Audit Commission, County Council and Districts within Derbyshire.

11. Annual Governance Statement - Internal Audit Assurance Statement

The Annual Report covers the work undertaken by the service in a particular financial year i.e. April to March. In addition there is a requirement to produce an Annual Audit Assurance Statement as a supporting document for the Governance Statement. This includes any assurances from work undertaken in April and May 2011 relevant to the year-end financial systems.

The Internal Audit Assurance Statement for 2010/11 can be found in Annexe A to this report.

12. Conclusion

The service has operated with a reduced establishment this year pending a review of the service delivery. Derby City Council Internal Audit Service has undertaken a number of audits during the year as part of an arrangement to supply additional resources.

Overall the service has completed 78.06% of the planned days against a target of 90%. Although this is less than last year and the current year's target it is considered reasonable given the reduced level of resources.

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

Audit Manager