

To: POLICY AND RESOURCES (FINANCE) SUB-COMMITTEE	Subject: INTERNAL AUDIT ANNUAL PLAN 2005-2006
From: AUDIT MANAGER	
Date: 25 February 2005	Ref: KA/CEAG

1 Purpose of Report

- 1.1 To seek approval for the Internal Audit Annual Plan for 2005-2006.

2 Background

- 2.1 Internal Audit is an assurance function that primarily provides an independent and objective opinion to the Council on the control environment comprising risk management, control and governance by evaluating its effectiveness in achieving the organisation's objectives. Internal Audit objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources.
- 2.2 The Committee is asked annually to approve the Internal Audit Annual Plan for the coming financial year. Responsibility for the production and execution of the audit plan and subsequent audit activities rests with the Council's Audit Manager. The Audit Manager consults with relevant stakeholders, but is solely responsible for the preparation of internal audit plans.
- 2.3 The plan (at Appendix A) details scheduled audit assignments for the year and is derived from a five-year strategic plan prepared by the Audit Manager and approved by the Chief Executive's Audit Group (CEAG) and the P&R (Finance) Sub-Committee in March 2003. A number of changes have been made from the strategic plan as a result of new initiatives, changes to the control environment, revised assessment of risks and other factors including further discussions with Departments.
- 2.4 The main objectives of the Council's Internal Audit service are to:

- Independently review and appraise systems of control throughout the authority and to make recommendations for improvement;
- Ascertain the extent of compliance with procedures, policies, regulations and legislation;
- Provide reassurance to management that its agreed policies and procedures are being carried out effectively;
- Facilitate good practice in managing control and risk;
- Recommend, where appropriate, improvements in control and performance in the achievement of corporate objectives;
- Review the value for money processes, including Best Value arrangements within the authority;
- Work in partnership with the external auditors; and
- Identify and investigate fraud and other irregularities brought to its attention.

- 2.5 The Internal Audit section will report progress against plan during 2005-2006 to the newly established Audit and Governance Panel. Progress reports will include the reporting of

significant matters that the Audit Manager considers it necessary to bring to the attention of members. The Internal Audit section has also recently produced a range of service standards and it is intended that performance against these standards will also be regularly reported to the Panel (see Appendix C).

- 2.6 There is a formal requirement for the Council's Audit Manager to prepare an annual report that contains an opinion on the overall soundness of the Council's internal control system.

The control environment is defined as the Council's policies and operations in place:

- To establish, and monitor the achievement of, the Council's objectives;
- To identify, assess and manage the risks to achieving the Council's objectives;
- To facilitate policy and decision making;
- To ensure the economical, effective and efficient use of resources;
- To ensure compliance with established policies (including behavioral and ethical expectations), procedures, laws and regulations;
- To safeguard the Council's assets and interests from losses of all kinds, including those arising from fraud, irregularity or corruption; and
- To ensure the integrity and reliability of information, accounts and data, including internal and external reporting and accountability processes. This encompasses elements of corporate governance and risk management.

- 2.7 Internal Audit is located within the Finance Department. The Audit Manager reports directly to the Director of Finance and to the Chief Executive's Audit Group and the Policy and Resources (Finance) Sub-Committee (from 1 April 2005, to the Audit and Governance Panel).

- 2.8 Internal Audit activity is governed by policies, procedures, rules and regulations established by the Council including the Council's Financial Regulations and other policies including guidance notes on Fraud and Defalcation. The Internal Audit Section is expected to meet the standards laid down by the Chartered Institute of Public Finance and Accountancy (CIPFA) in the *Code of Practice for Internal Audit in Local Government in the United Kingdom* (2003).

3 **Planning considerations**

- 3.1 The Internal Audit Strategic Plan was prepared in 2003 following a comprehensive review of all major Council activities. The list of auditable areas was discussed with Directors and incorporated all current activities and planned new initiatives, such as Modernising Government, Corporate Governance and Risk Management, Community Planning and joint working with the NHS, that require audit input. Further detailed discussions have been held with Directors in the preparation of the proposed annual plan for 2005-2006.
- 3.2 It is essential that scarce resources be deployed according to the areas of greatest risk. The strategic planning process involves a standard risk formula being applied by Internal Audit staff to each activity reflecting the scale and complexity of systems, previous experience of the control environment and the potential financial and other consequences of failures in internal controls. The plan also takes into account, proposed coverage of Audit Scotland, the Council's appointed external auditors, together with planned work of other regulatory functions such as Communities Scotland, Her Majesty's Inspectorate of Education and the Benefit Fraud Inspectorate.
- 3.3 In time, Internal Audit would wish to base its plans on line management's own assessment of risk and to compare the results of its own risk assessment process with the Council's Corporate and Departmental risk registers. These risk registers are, however, not yet complete and are currently being developed by line management as part of the Council's

corporate governance arrangements. Therefore the 2005-2006 Plan continues to be based on Internal Audit's assessment of risks as the Audit Manager considers that Corporate and Departmental risk management arrangements are not yet sufficiently developed for Internal Audit to consider basing its work on them. It is hoped that this will be possible when preparing the 2006-2007 Annual Plan.

- 3.4 Internal Audit also recognises that it is important that it remains focused on ensuring that its work on internal controls contributes towards the effective delivery of the Council's corporate and departmental/service objectives. The Scottish Executive's recent publication *Building a Better Scotland: Efficient Government – Securing Efficiency, Effectiveness and Productivity* emphasises the need to ensure that local authority processes are not unduly bureaucratic and that regulation and performance monitoring are proportionate and do not obstruct innovation.
- 3.5 Internal Audit welcomes this development and is mindful when conducting its work that structures, controls and processes put in place should also be proportionate and focused on the achievement of planned outcomes and effective service delivery. To this end, Internal Audit will continue to work with Departments to ensure that controls put in place by management are appropriate and effective and that we provide independent assurance on those control arrangements designed to ensure effective and high quality service delivery.
- 3.6 The Scottish Executive publication also encourages joint working and Internal Audit continues to work closely with partners and other service providers to ensure the delivery of an effective and efficient internal audit service to the Council. We work closely with the Council's external auditors to ensure that our activities are properly co-ordinated and to minimise any duplication of work. We also work closely with Internal Audit sections in other local authorities to share experience and good practice and to ensure that, where appropriate, we make good use of audit methodologies and approaches used elsewhere. We are also currently exploring a range of options for joint working and sharing of resources with South Lanarkshire Council's Internal Audit section and would expect formal proposals for joint working arrangements to be brought forward for consideration by senior management and elected members during 2005-2006.
- 3.7 A number of key financial systems have been identified in our strategic planning processes including financial management and budgetary control, general ledger control, payroll, creditors and debtors. The Strategic Plan has been assembled so that all these key systems are audited at least once every three years. In addition, a number of areas such as Housing and Council Tax Benefits, Statutory Performance Indicators, Corporate Governance, Contract Management and Compliance with Contract Standing Orders are included in each year of the plan. The approved audit strategy is that all other systems will be audited at least once every five years. The proposed 2005-2006 Annual Plan remains consistent with this approved strategic approach.
- 3.8 The Internal Audit Section currently consists of 15 full time posts together with a seconded trainee at various times of the year, (excluding three value for money audit staff who are currently seconded to the Modernising Government team). The section currently has 1.5 unfilled vacant posts.
- 3.9 The staffing structure within the Internal Audit section has remained broadly unchanged since local government re-organisation and Audit Scotland has recommended that management should undertake a review to ensure that the section continues, in the future, to be able to respond to the changing demands being placed on internal audit. The Audit Manager will therefore be reviewing the existing structure of the section including existing staff numbers and their experience and skills mix and likely future requirements. The review will be undertaken during the early part of 2005-2006 and consequently, it is not expected that steps will be taken to fill the existing vacancies until the results of the

review are known. Therefore, although the plan has been prepared on the basis of the current staff complement, a greater than normal allowance has been included for days lost as a result of vacancies.

- 3.10 Internal Audit reports regularly on the results of its work to the Director of Finance, the Chief Executive's Audit Group and the Policy and Resources (Finance) Sub-Committee (from 1 April 2005 by reporting to the Audit and Governance Panel). The Audit Manager is accountable for:
- Providing regular assessments on the adequacy and effectiveness of the Council's systems of risk management, internal control and governance arrangements based on the work undertaken;
 - Reporting significant control issues and potential for improvements in risk management and control processes; and
 - Periodically providing information on the status and results of the annual audit plan and the sufficiency of Internal Audit resources.
- 3.11 Internal Audit activity is planned to provide assurance to senior management and to enable an independent annual opinion to be given by the Audit Manager on the adequacy and effectiveness of internal controls within the authority. This includes the systems that achieve the corporate objectives of the Council and those that manage the material risks faced by the authority.
- 3.12 Fulfilling the requirement to present an annual report on the adequacy and effectiveness of the Council's internal controls requires the Audit Manager to consider information from a variety of sources. The opinion is presented to Members, the Chief Executive and the Director of Finance and is intended to provide assurance to these different stakeholders as to the adequacy and effectiveness of internal control within the Council.
- 3.13 The evaluation of the control environment for 2005-2006 will be informed by a number of sources:
- The results of the body of audit work undertaken by Internal Audit during the year to 31 March 2006;
 - The assessment of risk completed during the preparation and revision of the strategic audit plan;
 - Reports issued by the Council's external auditors, Audit Scotland, and other review agencies such as HM Inspectorate of Education, the Care Commission, Communities Scotland, Benefit Fraud Inspectorate etc;
 - Assessments of the general control environment within individual Departments undertaken by Service Directors; and
 - Internal Audit management's knowledge of the Council's governance, risk management and performance monitoring arrangements.
- 3.14 In bringing together these different sources of evidence, the Audit Manager will consider whether any key controls are absent or inadequate and whether the existence of any weaknesses identified, taken independently, or with other findings, significantly impairs the overall system of internal control. Wider issues relating to the Council's general arrangements for internal control, including corporate governance arrangements will also be considered.
- 3.15 The nature of individual audit assignments is such that it is expected that most Internal Audit reports will identify some weaknesses or areas where an element of control is missing or only partial in nature and will make recommendations for improvement. However, the Audit Manager will assess the existence of the weaknesses identified by Internal Audit during the year, taken with other findings and reach conclusions on whether

the Council's overall system of internal control was significantly or materially impaired. Where it is necessary to highlight any specific concerns, appropriate comments will be included in the formal opinion.

4 **Main Areas of the Annual Plan**

- 4.1 The major category of work within the Annual Plan remains systems reviews, which involve Internal Audit in assessing the adequacy and effectiveness of the internal controls within individual financial and non-financial systems. In 2005-2006 key financial systems which are to be reviewed include Payroll, Non-Domestic Rates, Cash Collection and Council Tax.
- 4.2 Additionally, a smaller number of compliance or regularity exercises will be undertaken within Departments concentrating on the level of adherence to expected procedures in common financial systems such as payroll, debtors, creditors and travel and subsistence.
- 4.3 Significant audit resources continue to be devoted to capital expenditure projects and other contract audits where compliance with the Council's Contract Standing Orders is assessed. The emphasis on this area has increased in recent years to reflect the significant additional resources going into the Council's capital programme following the introduction of the Prudential Code.
- 4.4 Other work included within the plan include topics where Internal Audit reviews are undertaken on an annual basis reflecting the significant nature of the activities and the need to provide assurance to senior management and elected members. This includes work on corporate governance, risk management, business continuity planning and best value.
- 4.5 We have also included significant resources across a number of corporate and departmental headings that involve reviews of joint working and partnership activities. This reflects the increasing number and importance of such arrangements and the need to ensure that appropriate accountability and control arrangements are operated to enable the Council to properly discharge its responsibilities. It is intended that part of this work will involve the development of a self-assessment tool for managers who are entering into such arrangements.
- 4.6 We continue to devote considerable resources to activities where internal audit activity is required or expected by other stakeholders. For example, we continue to undertake a significant number of exercises reviewing the operation of the Council's Housing and Council Tax Benefits service reflecting the expectations of the Department of Work and Pensions. We have also reflected the resource implications associated with the increased number of grant claims requiring certification by the Audit Manager.
- 4.7 We have also identified the need during 2005-2006 for internal audit activity looking at aspects of the Council's two major new PPP projects, Education 2010 and the Lanarkshire Waste Management Project.
- 4.8 An appropriate allowance has also been made within the plan for dealing with possible frauds and irregularities, which are investigated as they arise. Stocks and inventories and the safeguarding of Council assets will continue to be addressed both by attendance at year-end stocktakes and as part of routine audit coverage within Departments.
- 4.9 The Internal Audit function is seen by many Departments as a corporate source of advice on control and risk issues and the Internal Audit function is keen to develop a proactive role working with Departments as appropriate. This is also recognised in the plan.

- 4.10 The programme of value for money studies for the coming year has not been included within the plan and will require to be determined separately by the Chief Executive's Audit Group/Audit and Governance Panel following discussions with Departments. The agreed programme will form part of the Council's programme of continuous improvement.

5 **Corporate Considerations**

5.1 Although Internal Audit sits within the Finance Department and reports directly to the Director of Finance, it fulfills a corporate role as well as providing a service to each Council Department. Departments have been consulted during the preparation of the plan and their views taken on board where appropriate, subject always to the need to fulfill corporate responsibilities, to achieve a reasonable balance of work across the Council and to ensure the independence and integrity of the Internal Audit function.

5.2 It should be noted that it is primarily the responsibility of line management to establish appropriate internal controls. Internal Audit activity is planned to provide assurance to senior management and elected members on the Council's control environment and to enable an annual opinion to be given by the Audit Manager on the adequacy and effectiveness of internal controls within the authority.

6 **Recommendation**

- 6.1 The Committee is invited to approve the 2005-2006 Annual Internal Audit Plan.



Audit Manager

Appendix A Annual Internal Audit Plan 2005-2006

Audit Area	Planned Days
General Control Environment	
Maintenance of Authorised Signatories (in process of being transferred to Revenue Services)	30
Ad hoc advice on control and risk issues	50
Business Continuity Planning – key financial and non-financial systems	25
Updating Financial Regulations and Contract Standing Orders	25
Sub-total - General Control Environment	130
Asset management	
Asset Management – inventory process and control over assets	40
Stocks – Attending year-end stocktakes and work on stock systems during year	50
Sub-total – Asset Management	90
Regularity Audits	
Performance Monitoring/Performance Management – Regularity	20
Purchasing / Creditors – Regularity	30
Payroll/Employee checks – Regularity	30
Debtors – Regularity	30
Travel and Subsistence – Regularity	25
Sub-total – Regularity Audits	135
Contract Audits/Capital Expenditure	
Compliance with Contract Standing Orders/Tendering Arrangements	40
Capital Expenditure - Contract management	50
Sub-total – Contract Audit/Capital Expenditure	90
Corporate	
Incomplete jobs brought forward	50
Follow-up of agreed action plans from previous audits	80
Risk Management – corporate and departmental arrangements	25
Corporate Governance	25
Freedom of Information - compliance	25
Statutory Performance Indicators	40
Effective partnership working – review of existing partnerships and joint working arrangements	50
Waste Management PPP	40
Community Councils - facilitating external audit and issues arising	20
National Fraud Initiative (NFI) 2004 – including follow-up reporting	25
Debt recovery arrangements	25
Certification of grant claims	40
Best Value/2003 Local Government Act	25
Sub-total – Corporate	470
Contingency for investigating, frauds and irregularities	200
Finance	
Payroll – Teachers	30
Payroll – Administrative, professional and clerical staff	40
North Lanarkshire Municipal Bank	20
ICT Service Delivery/Contracting arrangements	20
ICT Environmental Controls	15
Non-Domestic Rates – (valuation, billing and collection)	40
Council Tax (valuation, billing and collection)	40
Cash Collection	30
Sub-total – Finance	235

Appendix A Annual Internal Audit Plan 2005-2006 (continued)

Audit Area	Planned Days
Housing and Council Tax Benefits	
Housing and Council Tax Benefits – Private and Council tenants	60
Housing Benefit – Subsidy Claim (areas of responsibility to be agreed with Audit Scotland)	20
Performance against DWP Performance Standards	30
Sub-total - Housing and Council Tax Benefits	110
Homelessness – (compliance with legislative requirements and expected procedures)	25
Asset Management Planning – (follow-up to external audit report)	25
Community Energy Partnership	10
Communities Scotland – Single Regulatory Framework (follow-up/monitoring of agreed actions)	20
Transfer of Development Funding (subject to approval by Communities Scotland)	40
Sub-total - Housing and Property Services	120
Social Work	
Departmental quality and monitoring arrangements	40
Direct payments	25
Criminal Justice (compliance with legislative requirements and expected procedures)	30
Residential Accommodation - Regulatory/compliance with financial procedures	25
Sub-total – Social work	120
Fleet Management (including purchasing/leasing/hiring, depots, fuel, spare parts, payroll, income etc)	40
Community Education Projects	20
Leisure and Recreation (including NL Access scheme)	30
Sub-total – Community Services	90
Education	
Education 2010 (scope to be agreed pending external audit review)	30
Education financial arrangements (including arrangements at HQ and schools)	25
Education Maintenance Allowance	25
Contracting – provision, supplies etc	25
Sub-total – Education	105
Administration	
Legal Services – Licensing Board (alcohol and gaming)	20
Personnel – equal opportunities (corporate compliance with legislation and expected procedures)	25
Sub-total – Administration	45
Planning and Environment	
European Funding	30
Economic development/regeneration - project management and accountability arrangements	20
Sub-total - Planning and Environment Department	50
Chief Executive	
Community Planning/Partnership arrangements	25
Public Private Partnerships – Corporate management arrangements	25
Sub-total - Chief Executive	50
Contingency – unallocated	31
GRAND TOTAL	2071

Appendix B Internal Audit staff resources

	Gross Days	Annual Leave	Public Holidays	Training	Allowance for sick leave	Allowance for staff turnover / vacancies	Management and other indirect activities	Total net direct days	Direct as % of gross days
Audit Manager	260	20	12	5	5	10	123	85	33
2 x Senior Auditors	520	60	24	10	15	20	106	285	55
5 x Auditors	1300	120	60	25	35	140	130	790	61*
5 x Audit Technicians	1160	130	58	30	30	90	80	742	64*
2 x Audit Clerks	520	40	24	10	15	20	307	104	20
0.5 x Trainee	130	10	6	30	5	5	9	65	50
Total	3890	380	184	110	105	285	755	2071	53

Notes:

- (1) 1.0 Audit Technician post is currently vacant. One other Audit Technician is currently on flexible working terms, which effectively reduces her working time by approximately 50 days per year.
- (2) 1.0 Auditor post and 0.5 Auditor (job-share) post are currently vacant.
- (3) Allowance provided for sick leave at 2.5 per cent of gross days rounded to the nearest multiple of five. Management will proactively manage sickness and a lower than expected outturn will result in audit topics from 2006-2007 being brought forward.
- (4) Allowance for vacancies occurring during the year is traditionally provided and shown at 3 per cent of gross days but no specific targets are set per grade. For 2005-2006, for the reasons outlined at paragraph 3.9 an additional allowance has been included in the 2005-2006 Plan of 90 days at Auditor grade and 40 days at Technician grade. A lower than expected outturn will result in audit topics from 2006-2007 being brought forward.

Appendix C Service Standards

We think it is important that you know what service standards you can expect from the Internal Audit Section. Our Service Standards pledge is proof of our commitment to provide you with a high quality internal audit service.

Who we are and what we do

We are part of the Finance Department. We are responsible to the Director of Finance. We provide an independent and objective internal audit function and provide assurance to senior management and elected members on the adequacy and effectiveness of the Council's control environment.

Our Service Standards Pledge

1. We will provide an internal audit service that complies with the '*Code of Practice for Internal Audit in Local Government in the United Kingdom (2003)*' published by the Chartered Institute of Public Finance and Accountancy (CIPFA).
2. We will commission independent reviews of the quality of our work annually and report the results of these reviews.
3. We will prepare an annual Internal Audit Plan for approval by the Chief Executive's Audit Group and elected members by 28 February each year and will consult Departments during the preparation of the plan.
4. We will complete annually at least 90 per cent of the planned outputs detailed in the approved Internal Audit Annual Plan.
5. We will provide an annual opinion on the adequacy and effectiveness of the Council's internal control framework by 31 May each year.
6. We will observe high standards of personal conduct (including politeness, fairness and sensitivity) and will demonstrate integrity, objectivity, competence and confidentiality in carrying out our work.
7. We will agree the scope and objectives for all audit reviews with appropriate senior management prior to undertaking work.
8. We will issue draft reports to Departments within 10 working days of completing fieldwork.
9. We will issue final reports within five working days of receiving satisfactory responses from management to draft reports.
10. We will deal with all enquiries and requests for advice promptly, efficiently and politely. Where an immediate response is not possible, we will agree within three working days a timescale for responding to requests and will comply with these agreed timescales.
11. We will provide opportunities for those using our service to provide us with complaints, comments and suggestions on how we might improve our services and we will publish this feedback and show how we have responded.
12. We will provide regular progress reports on the work of Internal Audit to the Chief Executive's Audit Group and elected members and will make these reports available via the intranet.

We are committed to achieving and maintaining high standards of service delivery and will monitor our performance against our service standards and publish the results regularly. We will investigate the reasons for any failure to achieve the expected standards or for downward trends in performance and, where appropriate, will take remedial action.