

# The EIT Task and Finish Final Report

## Internal Audit

### 1. Executive Summary

This report provides Members with an assessment of the current Internal Audit function. It demonstrates current performance levels, and its interaction with customers and the Council. It concludes with the assessment of a number of options for the way forward, and makes a recommendation on the option that is believed to be the most appropriate.

### 2. Recommendations

That Members recommend to Cabinet approval of the option to reduce the Internal Audit section and merge the function with Financial Planning.

#### Background

The Comprehensive Spending Review has revealed that reductions in funding to Local Government will be larger and happen more quickly than was previously anticipated. In light of this Stockton has approved a number of Task and Finish reviews in the Value For Money Programme. This review is one of those and the presentation of this report to Members follows the agreed guidelines for such reviews.

#### Baseline

##### ***What service and how the service is provided***

Internal Audit is an assurance function that provides an independent and objective opinion to the organisation on the control environment, by evaluating its effectiveness in achieving the organisation's objectives. It 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.

Its primary role is to act as a critical friend in improving the overall quality and efficiency of the Council's control environment. At present this is carried out via;

- Systems/probity audits,
- Computer systems audits,
- Contract and capital schemes audits,
- Partnership audits, including Xentrall partnership reports to DBC and the THL board,
- School Financial Management Standards in Schools (FMSiS) accreditation, and
- Ad-hoc/ special investigations work.

The Accounts and Audit Regulations (2006) state all principal local authorities must make provision for an internal audit service that complies with the CIPFA Code of Practice for Internal Audit in Local Government in the UK (2006).

Internal Audit is one of the cornerstones of effective governance. The evidence gathered in the course of its work is a key source of supporting evidence for the annual governance statement and corporate governance working groups.

The service also produces the Council's anti-fraud manuals (4) and the Council's partnership toolkit manual. It also gives advice and guidance to all services which has resulted in such things as producing a user's guide to Personalisation.

***What influences impact on the service (political social economical, technological)***

The service reports to the Audit and Standards Committees. The Audit Committee approve and monitor the completion of the annual audit plan, challenge/ approve the annual audit opinion statement and take reports from the Audit Commission and peer reviews from within the Council on the perceived quality of the internal audit service. Under the CIPFA Code of Practice the Chief Internal Auditor has rights of access to the Chief Exec and Chairperson of the Audit Committee whenever necessary.

Once completed all audit reports, unless justified and specifically excluded, are public documents.

All audit work is undertaken by assessing risks on all testing of systems undertaken. This risk based approach is based on a dataset which has been set up to analyse the results of testing and automatically produce an assurance level for each audit. In turn, these combined help to support the annual audit opinion statement.

***What service costs and what resources it uses people buildings etc***

The service is based in two relatively small offices in Bayheath House. The current staffing structure is for 10 members of staff as follows.

1 x Chief Internal Auditor	- Grade Q
1 x Senior Audit Team Manager	- Grade N
1 x Audit Team Manager	- Grade M
1 x Auditor	- Grade L
1 x Auditor	- Grade K
2 x Auditor	- Grade J
2 x Audit Technicians	- Grade I
1 x Admin Assistant/ Trainee Auditor	- Grade F

The budget for Internal Audit for 2010/11 is £370,356.

***What does consultation tell us***

Consultation from a Council perspective on the service includes the following.

There have been a number of peer reviews into the performance of the function by service officers within Stockton. These have also produced positive reports. This assessment is formally reported to the Audit Committee. The function also consults with the Audit Committee on its work programme and any policy changes.

As well as the above, consultation by the service also takes place, on a regular basis, with clients and stakeholders as to their perceived audit needs.

The section also consults with its clients on how satisfied they are with the level and content of audits during each financial year. For 2010/11 the average satisfaction level is at 87%.

***What do complaints and compliments***

Satisfaction surveys are asked for on each audit. Where these score low there are procedures in place for investigation. They are rare occurrences. The returned surveys are consistently achieving satisfactory scores. There are a considerable number of examples of staff being complimented for the quality and spirit of their work.

### 3. Service Evaluation and Findings

***Is the service needed is it statutory what level of service is needed***

As stated in the baseline section there is a statutory need for the service under the Accounts and Audit Regulations 2006. The level of service should be enough to give sufficient evidence to provide reliable assurance statements.

***What options are there for changing the way the service is delivered e.g. structurally, technologically***

The delivery of the service is based on a 5 year rolling audit plan that assesses risk and programmes audit frequency and duration within that period on the level of risk for each area to be audited. The forthcoming changes that will occur in local government because of legislation, organisational and funding reduction occurrences will have a significant impact on both the content and the risk assessment of this plan.

In terms of technology the section use the MK Insight computer system. This has been in use for a number of years and has lead to the introduction of computerised audit reports and streamlining of processes. It is anticipated that in the future this continued use of technology will lead to more efficient ways of working to reduce the amount of administrative time required, thus releasing more productive audit time.

***Benchmarking how does the service perform – costs - can you demonstrate that the service is cost effective.***

The Audit Commission has, for many years, consistently assessed and reported the service as reliable.

Regular benchmarking, for many years, has taken place both at national and local level. The national benchmarking is mainly on quantity issues but there is an anonymous survey of clients as to their satisfaction with the services which has always given a positive response. The last set of results from 2009/10 showed Stockton as being both the least costly and most productive in the Tees Valley. Cost per auditor for Stockton was £40,800 for the other 3 Tees Valley authorities in the survey the cost was £47,917, £50,450 and £54,430 respectively. Productive days per auditor were 200 for Stockton in comparison to 199,175 and 162 for the others. A confidentiality clause associated with the benchmarking means we cannot name the authorities.

Local benchmarking has concentrated more on quality issues which has helped in the development of the service. It is also worthy of note that the service has usually taken the lead on local benchmarking and been a key source of identifying best practice.

***What does inspection tell us***

The adequacy of the Internal Audit service is constantly examined by the external Audit Commission and formally reported on in its Governance assessment of the Council. This assessment has never been anything other than satisfactory.

The section also holds an ISO quality accreditation, and is re-assessed annually to ensure it is complying with those standards. The section has been successful every year in retaining that accreditation.

As mentioned above the section is subject to an internal officer peer review. The outcomes of these reviews when reported to Audit Committee have been positive in their assessment of the function.

***Who are the customers and what impact would changes have on them.***

On a day to day basis, the main customers are Directors and Heads of Service. Directors, in particular, are getting independent assurances on all significant services under their control either annually or every 2 – 3 years. On occasions, Directors have asked either for additional work or a return visit in some areas within a short period of time. This demonstrates the added value of the service.

The s151 officer, the Audit and Standards Committees rely on the scope and depth of audit work to give them assurances on the robustness of the Council's control environment. It is worthy of note that Audit Committee members have said they find out more about the services they are responsible for from Internal Audit than from the other Committees they are on.

In delivering any changes to the function it is essential that the section produces an audit plan that sufficiently examines the internal control environment and gives adequate assurance this is operating satisfactorily.

***What is likely to impact on demand for these services in the future***

The audit plan for the authority is determined by a risk assessment of its current functions. There are a number of proposals from the current Government that will mean functions move in or out of local government. In addition there are funding reductions that will inevitably have an impact. Where services disappear, or are reduced, because grant funding or capital allocations have been ceased, or reduced, these will impact on the plan. There is also the possibility that the core revenue funding reductions will impact in a similar although correlation to current services is not as obvious here and the 2011/12 MTFP will need to be determined before this area is as clear. There is little doubt that for future years the plan will be subject to more variation than has previously been the case.

## **4. Options**

***What options are there for service reconfigurations***

Other authorities have Internal Audit sections although they do not all operate as a single function. This does raise the possibility of looking at partnering in this area, with collaboration with the Tees Valley authorities being the most obvious place to explore. However as we have seen from the benchmarking data above Stockton's audit function is both the least expensive and most productive. This would then raise some questions as to any savings that would be realised from this option and the possible impact on productivity. It is suggested this option is not followed.

Within North Yorkshire some authorities have outsourced their Internal Audit function to an organisation called Veritas. From what is known about this organisation the flexibility that we currently have, and will require even more with all the future changes, is not so readily available. As might be anticipated in such a set up there is quite a degree of focus on contractual arrangements, something that is almost inevitable when this type of delivery occurs. There is also the issue that in these circumstances some element of cost saving/profit must go to the private provider. It is recommended therefore that we consider an in house solution retaining the flexibility that we currently have and ensuring all savings come to the Council.

The recommended option is to reduce the numbers in the audit team and amalgamate the team with the financial planning team. The reductions can take place by not filling vacancies.

In November 2010 an auditor is due to leave the section, this post will not be replaced. In July 2011 the Chief Internal Auditor will retire. This post will also not be replaced and the audit team will be merged with the financial planning section, with the current Chief Financial Planner managing both functions. This will mean we will have an audit plan based on 8 audit employees and a partial section head in comparison to 9 current audit employees and a full time section head. We have mentioned above that some functions within the council will be disappearing and reducing, and so require less auditing. In addition we will no longer be required to audit Tristar when it changes its status. Again mentioned above are plans to reduce time spent on administrative tasks to release more productive time. In addition within the financial planning function some capacity should be come available within the treasury management area, as the number of funding streams coming into the authority are dramatically reduced under the Government's future proposals. This can be used to bolster the capacity to undertake audits. When all of this is evaluated it is believed we can deliver the 2011/2 audit plan with the numbers suggested. This will deliver annual savings of £91,000 to the council. Not all of this will be realised in 2011/12 as the Chief Internal Auditor will be here until July reducing the saving to £76,000 in this year. There is also the issue that the role of the Chief Financial Planner will have to be re-assessed against the job evaluation criteria and any increase in grade would reduce the savings by the amount of the increase.

## **5. Conclusions and Recommendations**

It is the conclusion of this review that the internal solution of not filling vacancies and amalgamating the two sections is the best way forward for the council. Not only does it generate substantial savings, but it allows the service to remain in house and retain the flexibility that will be so vital with all the changes the council will face in the future. This option is recommended to Members.