Internal audit Strategy and Plan 2011-12 DRAFT

Herefordshire Council
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Contents

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1. Executive summary

1.1 Purpose of this report

This report meets the requirements under the Code of Practice for Internal Audit in Local Government (2006) ("the Code") for the Head of Internal Audit to produce a Internal Audit Strategy together with an annual Internal Audit Plan.   The Strategy is a high level statement of how the internal audit service will be delivered and developed. The annual Internal Audit Plan sets out the number and types of review which will be undertaken to deliver the Internal Audit Strategy.

Under the Code there a number of areas that the Strategy must detail. We have set these out below:.

• Internal Audit objectives;

• How the Head of Internal Audit will form and evidence the opinion on the control environment to support the Annual Governance Statement;

• How Internal Audit's work will identify and address significant local and national issues and risks;

• How the service will be provided, ie internally, externally, or a mix of the two; and

• The resources and skills required to deliver the strategy.

We have set out detail to support each of these requirements within the main body of our report.

1.2 Internal Audit's objectives

The core role of Internal Audit is to provide assurance to senior management that there are adequate and effective internal control arrangements in place to mitigate key risks and achieve objectives. In performing its role, Internal Audit aims to, where appropriate:

•contribute to the improvement of the internal control environment;

•identify opportunities for performance improvement;

•evaluate where systems are over controlled or inefficient; and

•identify cost saving opportunities.

The detailed terms of reference for Internal Audit are set out within the Audit Charter.

1.3 Key issues and Risks

The Council is facing a number of significant challenges over the next financial year as it continues to implement the 'Rising to the Challenge' programme and its innovative joint working arrangements with NHS Herefordshire whilst operating within a very financially constrained public sector economy (which includes the newly merged Integrated Care Organisation – Wye Valley NHS Trust).

The Council needs to continue to work closely with its functional partner NHS Herefordshire, its new acute and community provider and emerging GP consortia to tackle key challenges around commissioning, care quality and public health whilst at the same time continuing to modernise, improve and streamline core Council services. All of the developments proposed and in progress present you with opportunities to improve the quality of services available to the population the Council serves - but they do also represent significant change and potential risk.

During this period of change, the effectiveness of the Council's routine control and governance processes such as risk management, performance management and financial management are as important as ever. We have therefore produced an internal audit plan for 2011-12, which considers each of these areas and demonstrates how we will assist you and provide you with the assurances you need to manage the risks you face in the current financial year. Our plan also includes reviewing other key risk areas including Social Care (planning, commissioning and quality) and the implementation of the Shared Services company.

1.4 Developing the plan

We have compiled a risk based plan that takes account of the Council's key issues and objectives.   This plan has been compiled through discussions with the Chief Officer (Finance and Commercial Services), our knowledge of the sector, a desk top review of key documents, such as the Council's risk registers and a review of findings from previous internal audits.

We have also held conversations with the HPSLT and have fed in comments and issues arising to this plan.

1. Executive summary (cont)

The Internal Audit Plan includes reviews of key financial, operational and corporate systems. We believe that a total of 750 – 900 days of internal audit input is required to deliver the plan. This input will ensure that a fully comprehensive internal audit service is provided to the Council. We have set out our draft Internal Audit Plan at Appendix 1 and have provided further information on this area in Section 4.

1.5 Resources

The Audit Service is currently being led by secondees from KPMG, Sav Della Rocca as Interim Head of Audit and Mukhtar Khangura as Internal Audit Manager, with support from the in-house team. All staff have considerable experience of providing an effective and efficient internal audit service.

1.6 Audit Approach

We have a comprehensive audit approach and quality assurance process that meets the Code of Practice for Internal Audit in Local Government (2006). This process is set out in our Audit Charter and is summarised in Section 6. This process ensures that our work is of a high standard and delivers a quality internal audit service to the Council.

2. Internal Audit objectives

2.1 Internal Audit Objectives

Internal Audit is an assurance function that provides an independent and objective opinion to the Council on risk management, control and governance by evaluating their effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a proper economic, efficient and effective use of resources.

The need to maintain an internal audit function is implied by Section 151 of the Local Government Act 1972 under which local authorities are required to make proper arrangements for the administration of their financial affairs and to delegate responsibility for those arrangements to one of their officers. The Accounts and Audit Regulations 2003 amended by the Accounts and Audit (Amendment)(England) Regulations 2006 are explicit about the requirement to maintain an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control.

2.2 Core Role of Internal Audit

The core role of the Internal Audit is to provide assurance to Members and senior management that there are adequate and effective internal control arrangements in place to mitigate key risks and achieve objectives. In these ever changing time we believe that Internal Audit should not only provide its core role but provide a added value service. In performing its role, Internal Audit aims to, where appropriate:

•contribute to the improvement of the internal control environment;

•identify opportunities for performance improvement;

•evaluate where systems are over controlled or inefficient; and

•identify cost saving opportunities.

Internal Audit is not responsible for ensuring that adequate and effective internal controls are established to manage the key risks – that responsibility lies with senior management.

2.3 Independence of Audit Services

The Interim Head of Audit reports directly to the Chief Officer (Finance and Commercial Services). The Chief Officer (Finance and Commercial Services) is the Council's Responsible Financial Officer under the terms of Section 151 of the Local Government Act 1972.

The Interim Head of Audit is responsible for the day to day management of the Audit Services Team.

3. Developing the Plan

3.1 Developing the plan

All local authorities face a very challenging environment with pressures to both increase performance and decrease costs. We believe that a responsive and effective internal audit function can help the Council in meeting these challenges while assisting the Council achieve its objectives. This can only be achieved through developing a comprehensive Internal Audit Plan in which the resources available to the internal audit function are allocated to areas of greatest need. We have developed the draft plan taking into consideration the issues below:

3.2 Desktop review

In developing the Internal Audit Plan, we have taken account of the following:

- The Council's risk register's (The Council Assurance Framework, The Partnership Assurance Framework and The Board Assurance Framework documents);
- Discussions with officers including the views of the Chief Officer (Finance and Commercial Services);
- Emerging issues and risks facing the sector;
- The Council's objectives detailed within its Corporate Plan 2011-14;
- Existing projects, strategies and initiatives that the Council is undertaking;
- Input from the Internal Audit Team;
- The performance of the Council from a review of its Key Performance Indicators; and
- The Council's "Rising to the Challenge" project.

3.3 Views of HPSLT and other officers

We have met with members of SLT and have factored in their views to the existing plan. In some instances, Strategic Directors have asked that further meetings are held to determine the exact nature and scope of individual reviews. For example, we have allocated time in the plan to focus on issues in relation to Integrated Commissioning, quality of care and public health. The precise coverage of these reviews will be addressed through further discussions with relevant officers.

3. Developing the Plan

3.3 Liaison with the External Auditors

We understand the importance of the good working relationships with the External auditors in order to minimise duplication of effort. We are due to meet with the external auditors shortly in order to build their requirements into the audit plan, where appropriate, through our joint working protocol.

3.4 Liaison with the other assurance providers

We recognise that there are other assurance providers (both internal and external) who provide some assurance over aspects of the Council's operations e.g. OFSTED, Care Quality Commission, Benefits and Exchequer, LMS and Finance Team. Where possible we will seek to place reliance on such work and reduce internal audit coverage appropriately. For example, the level of audit work on schools is being reduced from approximately 300 days in the prior year to 50 days this year as the LMS and Finance Team are doing checks on quarterly returns from bank account schools.

We are also liaising with the internal audit team within NHS Herefordshire to ensure that effective working relationship is established and to identify areas for joint review. We have identified a number of potential areas including shared services, and commissioning.

4. Key Issues and coverage

4.1 Overview

The Council is facing a number of significant challenges and risks over the next financial year as it continues to implement a number of key programmes and initiatives. The Council has identified these risks within its Corporate Risk Register's. These include:

• Failure to deliver the £10.3 cost savings outlined for 2011/12;

• Not achieving £1m worth of efficiencies as part of the Benefits Realisation programme;

• Inadequate commissioning of services which are not delivered to the appropriate cost and quality;

• Failure to progress with the Integrated Waste Management PFI Scheme; and

• Ineffective implementation of the Shared Services Project.

The Council will need assurance that the controls it has in place to mitigate these risks are being effectively applied and that its control environment is robust.

4.2 Councils control environment

We have summarised below the Council's overall control environment. The control environment is the collection of systems and processes that helps the Council manage the above risks and achieve its objectives. These groupings form the key strands to our internal audit work:

Core support: these include systems that support the Council's service delivery, such as its financial, IT and HR systems;

Corporate systems: these are the core business processes that give the Council direction and provide oversight over its activities. For example, the risk management, performance management and corporate planning processes; and

Operational systems: these include the main systems associated with the Council's core activities and functions.
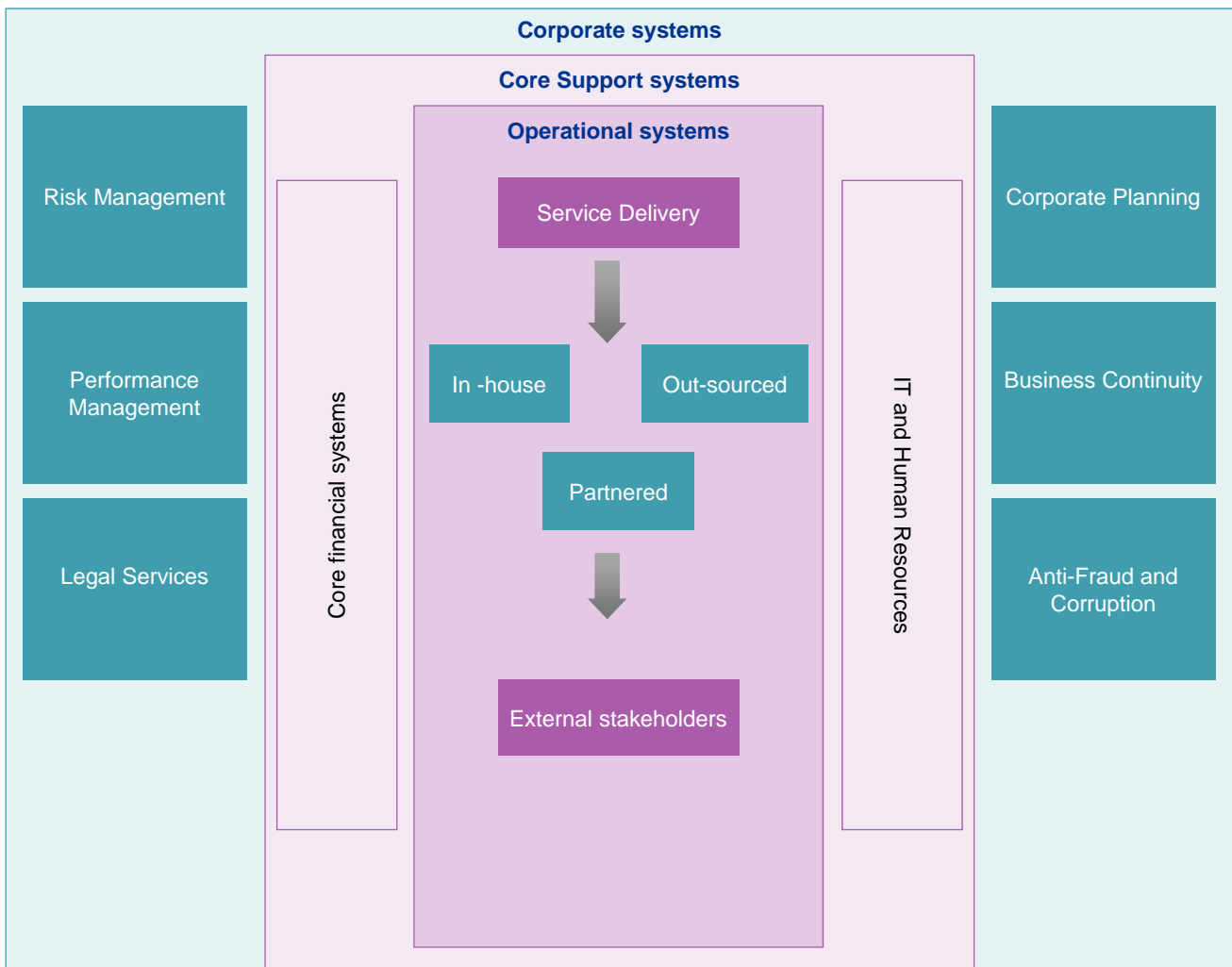
4. Key Issues and coverage (cont)

4.3 Audit Reviews

We have summarised the key areas of our internal audit plan below. The indicative resource allocations for these is shown in Appendix 2.

Area	Internal audit work in 2011-12
Core support systems	We have spilt this work into Core Support Systems – Financial and Other. We have provided further details on both of these areas below.
Core support systems - Financial	These reviews will include work on the Council's core financial systems, such as its Payroll, Creditors and Bank and Income systems. These reviews will be carried out either as detailed reviews or audits that focus on key high level controls. The approach for each of these audits will be agreed with management prior to the commencement of the review. By adopting this approach we believe that we can prioritise audit resource to areas where it can best be utilised.
Core support systems – Other	These reviews will include work on other core systems within the Council including Education Transport, the AMEY contract and Children Services (Early Years).

Support system - IT Systems	Effective and efficient IT systems are key to ensuring that the Council fulfils its Corporate Objectives. Our work within this area will include reviews of the Council's key applications such as Agresso. In addition we will review the Council's Business Continuity Plan and its IT Strategy to ensure that they are fit for purpose. Our work in this area will also focus on the Council's compliance with ISO27001.
Corporate system - Anti-Fraud and Corruption	The Council has a duty to ensure that its resources are safeguarded against theft, mis-use or loss. One of the ways in which it can do this is through the promotion of an effective anti-fraud and corruption environment. Our work in this area will be split into three areas. These will be: •helping the Council develop an effective anti-fraud and corruption environment through training Council employees on their responsibilities ; •reviewing the Council's policy documents within this area, such as its Code of Conduct and its Whistleblowing policy; •assessing how the Council could be affected by current issues within the Anti Fraud and Corruption area. For example, we will be reviewing how the Council is implementing the requirements of the Bribery Act 2011.
Corporate system - Governance	Clear and effective governance processes are vital to ensure that the Council efficiently manages its business functions. Our work in this area will review the Council's Risk Management and Performance Management functions. In both these areas, the Council is proposing changes to existing arrangements. In addition we will also review the controls and processes by which the Council's Director Assurance Statements are compiled and feed into the Annual Governance Statement.

4. Key Issues and coverage (cont)

Area	Internal audit work in 2011-12
Operational systems/risk reviews	Within this area of our plan we include the main systems associated with the Council's core activities and functions. The work in this area will include reviews of: •Shared Services; •Adult and Social Care; •Integrated Commissioning; •Public Health; •Sustainability; •PFI Project Management; •Fees and Charges; •Licensing •Planning; and •The HALO Leisure Contract We will agree the specific terms of reference for each of the above reviews as part of our discussions with management.
Schools	Our work in this area will include a review of the work undertaken by the Shared Services function over Schools bank accounts. As part of our work on Schools we will also sample review a selection of schools based on input from the Directorate of Children and Young Services. This work will involve a detailed review of a schools financial and operational functions.
Follow Up	This work in the area will entail following up high risk recommendation's made within previous year's report and assessing the progress the Council has made in implementing them.
Contingency	A number of days will remain unallocated to ensure that there is sufficient flexibility built within the plan to account for unexpected issues which may arise during the year and which require Internal Audit's input.
Management	Our management time will cover planning, quality control, client meetings, attendance at the Audit and Governance Committee and preparation of our Annual Opinion.

5. Resources

5.1 Audit team

The core members of your audit team are set out below. The team will be led by Sav DellaRocca as the Interim Head of Audit. Sav will be supported by Mukhtar Khangura who will act as the interim Internal Audit Manager. Both Sav and Mukhtar have been seconded into their roles from KPMG LLP.

Your internal audit team

Sav DellaRocca
Interim Head of Audit

Mukhtar Khangura
Interim Internal Audit Manager

Other members of the Audit Team

Julie Jones	**Gary Williams**	**Vicky Roissetter**	**Sharon Williams**
Senior Auditor	*IT Auditor*	*Principal Auditor*	*Principal Auditor*

All of the core Audit team members have significant experience of providing internal audit services. Sav and Mukhtar will be supported by four in-house staff who have been providing internal services to the Council for a number of years and have considerable experience and knowledge of the organisation.

In addition to these core members of your team we will draw on other resources from KPMG to complete our reviews. These staff will report to Sav to ensure that their work is co-ordinated and to ensure that there is seamless delivery of the internal audit service.

6. Our Audit Approach and Performance Indicators

6.1 Our Audit Approach

We aim to provide a service that not only meets your needs but also maintains consistently high standards and meets the requirements of the Code of Internal Audit.   Our detailed audit approach is set out in our Internal Audit Manual, however, we summarised some aspects of the process below:
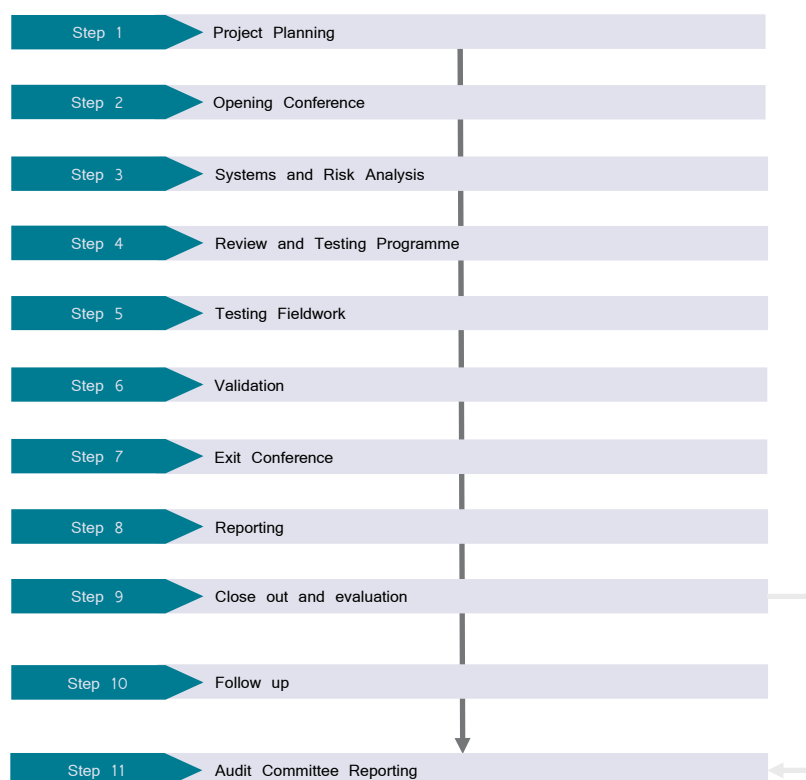
• Preparation of a detailed audit plan;

• Preparation of terms of reference which are provided to you two weeks prior to the audit commencing;

• The use of qualified, highly trained and experienced staff;

• Regular review of progress against the plan to ensure we are delivering the work we have promised;

• A tailored audit approach using a defined methodology and assignment control documentation which is subject to the firm's review protocol; and

• The review of all audit files and reports by a Manager and Head of Audit as part of Quality Assurance process.

6.2 Operating principles – the assignment process

We will utilise a risk-based approach to the individual reviews in line with the Code. This involves:

• Identifying the risks that may impact on the systems achieving their objectives and identifying and evaluating the systems of internal control designed by management;

• Compliance testing of the operation of controls;

• Making appropriate recommendations and advising management on how systems of internal control may be streamlined or strengthened.

The different delivery stages of the audit process are shown below. Our approach to individual reviews recognises that different approaches will be required in different circumstances, for example in some cases as systems are being developed or revised it may be beneficial for us to defer detailed testing until a later date, but instead focus on understanding and contributing to the development of the design of the control framework.

Step 1	Project Planning
Step 2	Opening Conference
Step 3	Systems and Risk Analysis
Step 4	Review and Testing Programme
Step 5	Testing Fieldwork
Step 6	Validation
Step 7	Exit Conference
Step 8	Reporting
Step 9	Close out and evaluation
Step 10	Follow up
Step 11	Audit Committee Reporting

6. Our Audit Approach and Performance Indicators

6.3 Reporting

On completion of our individual reviews, we will produce a report for management that will outline the objectives and scope of our work, risks considered during our review, an assessment of the effectiveness of internal controls and considerations for performance improvements. Each report will include an implementation plan.

Following our internal audit work for the year we will produce an annual internal audit report. This will summarise the work completed and will provide an overall opinion in respect of risk, control and governance arrangements.

6.4 Performance Indicators

Our internal procedures ensure that the service we deliver is of an appropriate quality and in compliance with the Code. Over the year, we will also be working to a number of performance measures, these include ones detailed below:

Performance Measure	Target
The percentage of Audits completed within plus 10% of target times.	80%
Managers review drafts reports within 15 working days of receipt	80%
Finals issued within 10 days of agreement by client	80%
Independent review of Audit Services against the CIPFA Code for Internal Auditors	N/A
CIPFA Audit Satisfaction Survey sent out	N/A
The percentage of Service managers satisfied with the Service	90%
Percentage of recommendations accepted by management	95%

We will report performance against these indicators as part of our Annual Assurance Report.

Appendix 1 - Resource allocation for 2011-12

Our overall audit plan is detailed on the following pages. We have explained below how this has been structured and the how the elements of the plan relate to our planning processes:

System	Internal audit risk assessment				Year
	Inherent	Control	Materiality	Aggregate	11-12

The first part of our analysis shows which area is being reviewed (i.e. operational, corporate or support system) and the specific system proposed for review.

The second part of our analysis considers our internal audit risk assessment and uses the following risk assessment process to analyse the system under review:

The third part of our analysis shows the audit coverage.

Inherent risk	Control risk	Materiality and risk	Aggregate
Our assessment of the overall level of risk associated with the audit area – this is effectively a gross relative risk of the potential impact on you in this area.	Our assessment of the risk that exists within a particular area based upon the controls that we are aware you have put in place – effectively the likelihood of the risk being realised. This is informed by previous internal audit reports and discussions with officers, but will be refined over time.	Our assessment of the potential financial or organisational consequence to you. This might be judged by the potential for a monetary loss or the extent to which it impacts on core business objectives.	This is our overall assessment of risk associated with each of the audit areas. It is reached with regard to each of the previous assessment of risks.

We have set out below audits for 2011/12 based on our risk assessment process above. We have also set out (where applicable) reviews which link into the Council's risk register's (detailed by "Yes").   Audit reviews which do not explicitly link into the Council's risk register are detailed as shaded areas. These reviews are required for a number of reasons including, to inform the overall opinion on the Council's internal controls system's given by the Head of Audit.

Annual plan 2011/12							
		Linked to Risk Register's	Internal audit risk assessment				Audit coverage
			Inherent Risk	Control Risk	Materiality	Aggregate	Days
Core support systems	Payroll （inc Members allowances）		M	M	H	M	
	Creditors		M	M	H	M	
	Treasury Management	Yes	H	H	H	H	
	Debtors and other Income Streams		M	M	H	M	
	Accountancy and Budgetary Control		H	M	H	H	
	NNDR	Yes	M	M	H	M	
	Council Tax	Yes	M	M	H	H	
	Housing Benefit		M	M	H	H	
	Asset Register	Yes	M	M	M	M	
	Cash and Deposits		M	M	M	M	
	FMS	Yes	M	M	M	M	
	Procurement	Yes	M	M	M	M	

Appendix 1 - Resource allocation for 2011-12

Annual plan 2011/12						
		Internal audit risk assessment				Audit coverage
	Link to Risk Register	**Inherent Risk**	**Control Risk**	**Materiality**	**Aggregate**	**Days**
Core support systems						
Education Transport	Yes	M	M	M	M	
Children Services – Early Years	Yes	M	M	M	M	
AMEY Contract	Yes	M	M	M	M	
Total for Core Support Systems						200-250
IT systems						
ISO 27001	Yes	M	M	M	M	
Application Testing (inc IDOX and Academy)		M	M	H	M	
ICT Disaster Recovery	Yes	M	L	H	M	
IT Strategy	Yes	H	M	M	M	
Total for IT systems						80-100
Anti-Fraud systems						
Anti-Fraud and Corruption Awareness Training	Yes	M	M	M	M	
Anti-Fraud and Corruption – Audit		M	M	H	M	
Anti-Fraud and Corruption – Hot Topics		M	L	H	M	
Total for Anti-Fraud systems						50
Governance systems						
Director Annual Assurance Statements		M	M	M	M	
Risk Management		M	M	H	M	
Performance Management	Yes	M	L	H	M	
Benefits Realisation	Yes	M	M	H	M	
Project Management	Yes	M	M	H	M	
Governance – (Standing Orders etc)	Yes	M	M	M	M	
Annual Governance Statement	Yes	M	M	M	M	
Total for Governance systems						80-110

Appendix 1 - Resource allocation for 2011-12

System		Link to Risk Register	Internal audit risk assessment				Audit coverage
			Inherent Risk	Control Risk	Materiality	Aggregate	Days
Operational systems	Shared Services Project Management	Yes	M	M	M	M	
	Shared Services – Governance (on-going)	Yes	H	M	H	H	
	Rising to the Challenge – Project Monitoring	Yes	M	M	M	M	
	Framework I – Adult and Social Care and Children	Yes	M	H	M	M	
	PFI Project Management	Yes	M	M	M	M	
	Integrated Commissioning	Yes	H	M	M	M	
	Public Health	Yes	H	H	M	H	
	Implementation of Agresso	Yes	M	M	M	M	
	Business Continuity	Yes	M	M	M	M	
	Planning	Yes	M	M	M	M	
	Fee and Charges	Yes	M	M	M	M	
	HALO Leisure Management	Yes	M	M	M	M	
	Licensing	Yes	M	M	M	M	
	Total for Operational systems						140-190
	Schools		M	M	M	M	50
	Contingency						30
MGT	Follow up		N/A for contract management aspects of our work				30
	Contract management and Audit and Governance Committee attendance						90
	Total						750-900

We will allocate days for each audit shortly, once we have agreed the scope of each review with the appropriate officer.

Appendix 2 - Opinion and description of levels of assurance

Audit Opinion

The audit opinion on the Council's systems of internal control will be based on a review of the following:

• Core Systems, both Financial and Other;

• Anti-Fraud Systems;

• Corporate Systems;

• Governance Systems;

• IT Systems;

• Level of recommendations agreed for action by management.

• Results of the recommendations follow-up review.

An audit conclusion will be given to each audit review, which will inform the Head of Internal Audit's overall opinion on the Council's system of internal control.

Regular progress reports will be presented to the Audit and Governance Committee, with the Annual Assurance report presented in the June following the financial year to which it relates.

We will use the following conclusions as the basis of the levels of assurance that we provide you with after each review (although it should be noted that these represent an indicative approach as the overall assurance provided are a matter of professional judgement).

Conclusion	Definition
No assurance	One or more priority one recommendations and fundamental design or operational weaknesses in more than one part of the area under review
	(i.e. the weakness or weaknesses identified have a fundamental and immediate impact preventing achievement of strategic aims and/or objectives; or result in an unacceptable exposure to reputation or other strategic risks).
Limited assurance	One or more priority one recommendations, **or** a high number of medium priority recommendations that taken cumulatively suggest a weak control environment
	(i.e. the weakness or weaknesses identified have a significant impact preventing achievement of strategic aims and/or objectives; or result in an unacceptable exposure to reputation or other strategic risks).
Adequate assurance	One or more priority two recommendations
	(i.e. that there are weaknesses requiring improvement but these are not vital to the achievement of strategic aims and objectives - however, if not addressed the weaknesses could increase the likelihood of strategic risks occurring).
Substantial assurance	No or priority three only recommendations.
	(i.e. any weaknesses identified relate only to issues of good practice which could improve the efficiency and effectiveness of the system or process).

Appendix 2 - Opinion and description of levels of assurance

We have also agreed the following definitions for the priority of the recommendations that we may raise within our reports:

Priority	Definition
Red *(Priority 1)*	A **significant** weakness in the system or process which is putting the Council at **serious risk** of not achieving its **strategic** aims and objectives. In particular: significant adverse impact on **reputation**; non-compliance with key statutory requirements; or substantially raising the likelihood that any of the Council's strategic risks will occur. Any recommendations in this category would require **immediate attention**.
Amber *(Priority 2)*	A **potentially significant** or **medium level** weakness in the system or process which **could** put the Council at risk of not achieving its strategic aims and objectives. In particular, having the potential for adverse impact on the Council's reputation or for raising the likelihood of the Council's strategic risks occurring, **if not addressed.**
Green *(Priority 3)*	Recommendations which could **improve** the efficiency and/or effectiveness of the system or process but which are **not vital** to achieving the Council's strategic aims and objectives. These are generally issues of **good practice** that we consider would achieve better outcomes.