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# Internal Audit Annual Report 2012-13

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Internal Audit

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## Internal Audit Annual Report 2012/13

### 1 Introduction

- 1.1 The Chartered Institute for Public Finance and Accountancy Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 (The CIPFA Code) established the expected professional standards for internal audit in local government. This was the Code under which Internal Audit operated in 2012/13.
- 1.2 In accordance with the CIPFA Code, the Internal Audit Annual Report 2012/13 for Cheshire East contains the following:
- an opinion on the overall adequacy and effectiveness of the organisation's control environment (Section 2)
  - any qualifications to that opinion, together with the reasons for the qualification (Section 2)
  - a summary of the audit work from which the opinion is derived, including reliance placed on work by other assurance bodies (Section 3)
  - any issues judged particularly relevant to the preparation of the Annual Governance Statement (AGS) (Section 4)

- comparison of the work actually undertaken with the work that was planned and a summary of the performance of the internal audit function against its performance measures and targets (Section 5)
- comments on compliance with these standards and communication of the results of the internal audit quality assurance programme (Section 6)

### 2 Opinion on the Control Environment

- 2.1 Internal Audit is required to form an annual opinion on the adequacy and effectiveness of the Council's internal control environment, which includes consideration of any significant risk or governance issues and control failures that have been identified.
- 2.2 It should be noted that the assurances given by Internal Audit are never absolute because it is impossible to examine every activity and every transaction and, audit reviews are at a point in time. The most Internal Audit can provide is a reasonable assurance that there are no major weaknesses, or that the weaknesses identified have been addressed.



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- 2.3 During the course of 2012/13 Internal Audit identified, and was made aware of, a number of issues with regard to the adequacy and effectiveness of the Council's system of internal control. Although it is pleasing to note that a significant amount of work has been done in response to these issues, there is still some way to go to ensure that risk management and internal controls are fully embedded into the Council's operations and that governance arrangements provide assurance with regard to compliance.
- 2.4 It should be noted that the actions that Management has agreed to take in response to these issues will, if implemented satisfactorily, resolve them appropriately. The challenge going forward is the inherent risk of the breakdown in control especially where responsibilities and systems are changing in response to the Council's ambitious plan to transform service delivery and realise significant savings.

### Opinion on the Control Environment

Therefore, in the opinion of the Head of Internal Audit, as represented currently by the two Audit Managers, the Council has, generally established an adequate framework of risk management, control and governance.

Evidence throughout 2012/13 would, however, indicate that although appropriate strategies and policies are in place and have been communicated, understanding, application and compliance is inconsistent across the organisation. Action has been, or is being taken to address the issues.

This opinion is based upon:

- the programme of audit reviews and in particular opinion based work undertaken during the year
- Management's response to advice and recommendations
- the AGS process
- The Council's Annual Report on its Risk Management Arrangements

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### 3 Summary of Audit Work 2012/13

- 3.1 The Council is responsible for establishing and maintaining appropriate risk management processes, control systems, accounting records and governance arrangements. Internal Audit plays a vital part in advising the organisation that these arrangements are in place and operating properly.
- 3.2 The provision of assurance is, therefore, the primary role for internal audit. This role requires the Head of Internal Audit (HIA) to provide an annual internal audit opinion based on an objective assessment of the framework of governance, risk management and control.
- 3.3 A risk based Internal Audit plan is produced each year to ensure that:
- the scale and breadth of audit activity is sufficient to allow the HIA to provide an independent and objective opinion to the Council on the control environment.
  - audit activity focuses on areas where assurance is most needed.
- 3.4 The plan is broadly split into two main areas as follows:
- those audits that deliver an opinion report on the risks and controls of the area under review and will inform the Annual Internal Audit Opinion.
  - work that will not deliver an opinion report but will help inform the Annual Internal Audit Opinion.
- 3.5 During 2012/13, interim reports on progress against the Internal Audit Plan were regularly brought to this Committee. A summary of the audit work carried out during the year and the relative outputs from that work is shown below on page 4.

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### Summary of Audit Work from which the opinion is derived

Para Ref	Area	Description of Audit Work	Output
3.6 – 3.13	Assurance Work	Audits with formal assurance level	Audit Reports
3.14	Schools	Assessment against Schools Financial Value Standard	Audit Reports
3.15 – 3.18	Lyme Green	Investigation of issues re: proposed waste transfer station	Report and Action Plan Updates to Audit & Governance Committee
3.19 – 3.21	Supporting Corporate Governance	Support and contribution to production of the Annual Governance Statement, including assurance statements from Heads of Service	Annual Governance Statement, and supporting evidence
		Support and contribution to update reports from the Corporate Governance Group	Reports to Corporate Management Team
		Support and contribution to AGS Action Plan, Lyme Green Action Plan and Compliance with Contract Procedure Rules reports	Reports to Audit & Governance Committee
3.22 – 3.23	Risk Management	Support and Contribution to the Corporate Risk Management Group including update reports	Reports to Audit & Governance Committee
3.24 – 3.29	Counter Fraud	Review of Anti Fraud and Corruption arrangements	Report to Audit & Governance Committee
		National Fraud Initiative – co-ordination of matches and investigation work	Results published on Audit Commission secure website/update reports to Corporate Risk Management Group/Investigation Reports
		Investigations	Investigation Reports
3.30	Consultancy & Advice	Ad-hoc consultancy and advice provided to services	Various – reports etc.
3.31	Statutory Returns/ Grant Claims	Audit/assurance work on programme/project and subsequent report to statutory/funding body	Return/Claim sign off
3.32 – 3.36	Follow Up Audit Work	Targeted follow up of audit recommendations based on audit opinion/recommendation	Follow Up reports/action plans

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### Assurance Work

- 3.6 During 2012/13, Internal Audit introduced a new report format, including for the first time, a formal audit assurance level. A summary of the reports produced during 2012/13 with the formal assurance level is included below (some of the audit reports are still at draft stage i.e. awaiting management comments):

Assurance Level	Audit Reports 2012/13
Good	0
Satisfactory	14
Limited	11
No	1

- 3.7 The assurance levels reported in the table above include a combination of opinions at a broad level for the Council as a whole (macro-level opinion, see 3.8 – 3.12) e.g. Housing Benefits, Procurement and opinions on individual business processes or activities within a single organisation, department or location (micro-level opinion, see 3.13) e.g. Social Care establishment, Library.

- 3.8 At the macro level, satisfactory assurance with regard to the risks identified within the terms of reference, has been given in all cases in 2012/13, except the following which have been given 'limited assurance', and are covered in the paragraphs 3.9 – 3.12, or interim Internal Audit reports previously reported to Committee:

- Procurement (detailed in report to Committee in September 2012)
- Duplicate Payments (as above)
- Purchase Cards (as above)
- Schemes of Delegation (Local and Financial) (para 3.9 - 3.11)
- Asset Registers/Inventories (para 3.12)

- 3.9 The Schemes of Delegation audit focussed on both local schemes (which set out sub delegations from the delegated functions contained in Officer Schemes of Delegations) and financial schemes (which documents approval limits for financial transactions).

- 3.10 The audit concluded that Schemes of Financial Delegation (SoFD) had all been brought up to date and published on the intranet by the end of July 2012. However, many have not



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been updated regularly since and some are still incomplete and/or inconsistent with system limits. The management response stated that SoFD were the subject of an ongoing review and that understandably, the structure would need to be revised as part of the current management review; briefings on SoFD to Extended and Corporate Management Teams were planned.

- 3.11 The audit concluded that Local Schemes of Delegation (LSoD) were inconsistent across the Council, in terms of the level to which they delegate, and recommended that all Constitutional delegations are delegated to Heads of Service, with further delegations set out in local service schemes. Subsequent to the report and management response, it has been agreed at Council (15<sup>th</sup> May) "that, in order to ensure that the Council's decision-making arrangements properly reflect the emerging officer structure under the management review, all existing delegations shall remain effective pending further review and shall accrue to the relevant post holders as appropriate, such arrangements to have effect until 1st September 2013".

- 3.12 The audit of Asset Registers/Inventories found that although basic requirements for maintaining inventories were contained in the Council's Finance Procedure Rules, there was a lack of detailed guidance on inventories and disposal of assets. It also found that generally inventories were well maintained and kept up to date in establishments but that this was not the case for corporate services. Recommendations have been made accordingly and a management response is awaited.

- 3.13 At the micro level, assurance in the majority of cases is limited because improvements are required in some or all of the following areas: cashing up procedures, authorisation of expenses, contract monitoring, and payments and the review of purchase card transactions. In many cases, this is as expected as, in the majority of instances, management were aware of control issues prior to the audit commencing. At the micro level, there has been one instance of 'no assurance' in 2012/13, which has been previously reported to Committee:

- Third Sector Payments (detailed in report to Committee in September 2012).



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### Schools

- 3.14 During 2012/13, Internal Audit carried out an assessment against the School's Financial Value Standard (SFVS) at 9 (out of 139) schools in order to determine whether assurance could be placed upon the returns submitted by schools. The Department for Education require the Section 151 officer to sign off an Annual Assurance Statement confirming the number of School's SFVS self assessment returns received and also that there is an appropriate audit programme in place to provide adequate assurance over the standard of financial management, and the regularity and propriety of spending in schools. The review concluded that reasonable assurance could be placed on the SFVS returns submitted as an accurate representation of the financial management arrangements at Cheshire East schools.

### Lyme Green

- 3.15 The Audit and Governance Committee on 31st January 2012 resolved that "a thorough and robust investigation of all issues surrounding the expenditure incurred on the proposed waste transfer station at Lyme Green be added to the work plan; in particular to identify any governance

issues and whether all financial and contractual regulations have been complied with."

- 3.16 A special meeting of the Audit and Governance Committee was held on 14<sup>th</sup> June 2012 to consider the outcome of the review. The report considered management's compliance with established policies, procedures, laws and regulations particularly with regard to the use of assets and resources entrusted to it. In summary the review established that controls, procedures and policies had been compromised and identified the steps that needed to be taken to prevent a reoccurrence.
- 3.17 The Committee resolved, among other things, that the findings and recommendations of the Internal Audit review and the agreed Action Plan be noted and endorsed, and that progress reports against the identified actions in the Action Plan be submitted to the Committee on a quarterly basis. Progress reports were received by the Committee in September 2012 and January 2013 and a report that provided an update on programme and project management and other compliance issues was received in March 2013.





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- 3.18 "Issues and Actions arising from Lyme Green" was one of the significant governance issues identified in the Council's Annual Governance Statement (AGS) for 2011/12. Progress against the actions in the AGS Action Plan were monitored throughout the year by the Corporate Governance Group and reported to the Audit and Governance Committee.

### Supporting Corporate Governance

- 3.19 In accordance with Regulation 4 of the Accounts and Audit Regulations the Council is required to conduct a review at least once a year of the effectiveness of its governance arrangements and publish an Annual Governance Statement (AGS).
- 3.20 Internal Audit has assisted Management in the production of the Council's AGS for 2012/13 by:
- collecting evidence for and production of the Annual Governance Statement
  - contribution to and production of Audit & Governance Committee reports on AGS Action Plan, Lyme Green Action Plan, Delegated Decisions and Non compliances etc.

- Audit Manager representation on and contribution to the Corporate Governance Group (CGG) in order to advise on risk management, control, and governance issues that have been identified through audit work and ensure that the findings have been considered when determining the 2012/13 AGS action plan.
- Audit work in contribution to and production of CGG reports to Corporate Management Team

- 3.21 This report draws attention to issues that the Head of Internal Audit, as represented by the two Audit Managers, have been made aware of during the preparation of the Annual Governance Statement (see paragraphs 4.1 – 4.3).

### Risk Management

- 3.22 Internal Audit has assisted in the Management of Risk through:
- Delivery of a risk based audit plan
  - Audit Manager representation on and contribution to the Corporate Risk Management Group (CRMG) in order to



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advise on risk management, control, and governance issues that have been identified through audit work

3.23 Formal reports with regard to the risk management process are made throughout the year to Corporate Management Team, Cabinet and the Audit and Governance Committee. In accordance with the Annual Report on Risk Management from the Corporate Risk Management Group (June 2013 Agenda, Audit and Governance Committee):

- At the end of February, Cabinet and the Corporate Management Team (CMT) undertook a risk and opportunity workshop and began to review the key corporate risks to achieving the Council's objectives and outcomes. Work is presently underway to assess these risks and to record existing and future planned mitigating actions; these risks will then be prioritised accordingly and a risk heat map produced.
- Cabinet and CMT agreed that the Council should strive to consistently reach the level of maturity of risk managed (Enterprise approach to risk management developed and communicated, risk embedded in key processes. Active

engagement and risk based decision making), as a minimum standard. At present, the level of risk maturity for Cheshire East is judged to be between risk aware (Scattered silo based approach to risk management using standalone processes, reactive approach) and risk defined (Risk appetite defined. Strategy and policies in place and communicated. Some understanding and application but passive acceptance and compliance with reliance on risk registers) which gives a good foundation to further embed risk management and improve the quality of risk identification.

### Counter Fraud

3.24 The anti-fraud and corruption arrangements were reviewed against the National Fraud Authority (NFA) document 'Fighting Fraud Locally: The Local Government Fraud Strategy (FFL)' and the findings reported to the Audit and Governance Committee (September 2012). The review identified a small number of improvement opportunities, the implementation of actions to address gaps with best practice are currently being monitored by the Fraud Member/Officer Group.



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- 3.25 A review of the Whistleblowing arrangements was carried out with the outcome, and a breakdown of the number of concerns raised, reported to Audit and Governance Committee in March 2013. In summary, the review concluded that there is clear evidence that the Council's Whistleblowing arrangements remain in line with best practice and, as such, no changes were proposed. It was, however, acknowledged that, in order to ensure that the arrangements remain effective, further review work would be carried out during 2013/14. This includes a survey of staff awareness of and views on the arrangements. The arrangements are currently being monitored by the Fraud Member/Officer Group.
- 3.26 The Member/Officer Fraud Sub Group continues to meet on a regular basis, to provide further detail to members on emerging fraud risks and anti fraud work carried out by Internal Audit.
- 3.27 During 2012/13, Internal Audit carried out a number of investigations across the Council with appropriate action taken where necessary and also provided support and

advice to investigations where management had appointed an Investigating Officer.

- 3.28 Internal Audit has produced a Fraud Risk Assessment, in consultation with the Performance and Risk Manager. This was endorsed by the Corporate Risk Management Group and will inform the proactive anti fraud work in the 2013/14 Internal Audit Plan.
- 3.29 Work has been undertaken on the National Fraud Initiative during the year including the coordination of data extracts leading up to the submission of data to the Audit Commission in October 2012. Since the release of the latest data matches in January 2013, Internal Audit has been coordinating and monitoring the investigations of matches by services, in addition to carrying out the investigations into a number of the Payroll and Creditors matches.

### Consultancy and Advice

- 3.30 During the year Internal Audit provided advice to Management; such work was performed at the specific request of the organisation. The nature and scope of the



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engagements are generally aimed to improve governance, risk management and control and contribute to the overall opinion. e.g. Advice on new systems, application of Finance & Contract Procedure Rules etc.

### Statutory Returns/Grant Claims

- 3.31 Internal Audit are sometimes required as stipulation of funding or similar, to carry out an audit/give assurance on the programme/project or aspects, thereof, and report back to the statutory/funding body e.g. Growing Places Fund, Bus Services Operators Grant etc.

### Follow Up Audit Work

- 3.32 Throughout 2012/13, Internal Audit have performed various follow up exercises to ensure recommendations are being implemented. This is carried out in a number of different ways:
- Major pieces of audit work, such as the Lyme Green Report and the Annual Governance Statement have detailed action plans which are monitored and reported separately to the Committee.

- Investigations – the form of follow up is dependent on the nature of the investigation and the resultant recommendations e.g. follow up audit carried out on request of management.
- Formal assurance audits (see 3.33 - 3.36).

- 3.33 As previously reported to the Committee in January 2013, Internal Audit have further developed the follow up procedure for formal assurance reports, whereby managers self assess recommendations implemented. Dependent on resources, more detailed checks will be carried out on a sample of implemented recommendations. Audits with 'limited' or 'no' assurance are subject to more detailed follow ups. In addition, key systems audits such as Payroll, Accounts Payable, Council Tax etc. are carried out on an annual basis and recommendations are followed up as part of the next year's audit.

- 3.34 In May 2013, the Chief Operating Officer (COO) introduced a new process to monitor any outstanding actions for the Council; this includes recommendations from both Internal and External Audit. The Consolidated Action Plan (CAP) will be monitored on a monthly basis, with managers providing

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progress reports back on the implementation of actions assigned to them.

- 3.35 The process has been extremely useful in establishing the current status of Internal Audit actions. The following table shows the figures as at 1 May 2013; the majority of actions are being followed up now or in the coming months:

### Status of Internal Audit Agreed Actions (at 1 May 2013)

Agreed Actions	Total	High	Medium
Implementation date not yet due	16	4	12
Internal Audit follow up either in progress or due in next quarter	59	10	49
Follow up response overdue or implementation date passed	14	2	12
<b>Total Agreed Actions</b>	<b>89</b>	<b>16</b>	<b>73</b>

- 3.36 There has been some slippage of actions, which are now overdue and these are being progressed through the normal follow up and escalation process.

### Emerging Work

- 3.37 The following audits commenced during 2012/13, with work ongoing in the first quarter of 2013/14 and reports either issued or are due to be issued shortly:

- Assets – Project Management Arrangements
- Corporate Complaints
- External Inspections
- Foster Payments
- Freedom of Information
- Licensing
- Safer Recruitment
- Schools – various

### Reliance placed on Work by Other Assurance Bodies

- 3.38 Assurance is placed on the work of the External Auditors, OFSTED, and other external bodies where appropriate. Work has begun on formally mapping the assurance



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framework of the Council as a whole, in order that the current range of assurances can be established and any areas where additional assurances are required can be identified.

### 4 Annual Governance Statement 2012/13

4.1 In compiling the AGS, significant issues that are considered to fall short of the expected standards are commented on in the Statement. Management has identified the following significant governance issues, further detail of which can be found in the draft 12/13 AGS:

- Management Structure and Organisational Culture
- Embedding Corporate Policies and Procedures and Ensuring Compliance

4.2 The AGS has an action plan to address these issues which includes actions already in place along with other planned actions. In a number of these areas, Internal Audit is already involved in ensuring that improvements are being implemented and time has been allocated in the 13/14 Audit Plan to review the other areas. In addition, progress

against the 12/13 AGS Action Plan will be monitored by Internal Audit and reported back to this Committee.

4.3 There are no outstanding significant control issues identified through the work of Internal Audit that require disclosure in the Council's 2012/13 Annual Governance Statement.

### 5 Internal Audit Performance

5.1 A summary comparison of the 12/13 Audit Plan with Actuals is shown on page 14 below (with comments on variances).

5.2 For the majority of 2012/13, Internal Audit reported to the Director of Finance & Business Services. Following recent changes as part of the Council's organisational redesign, Internal Audit now reports to the Head of Governance and Democratic Services. The Head of Internal Audit post and a Senior Auditor post presently remain unfilled, pending the outcome of the Council's current ongoing Management Review.

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### Summary Comparison of Audit Plan 2012/13 and Actuals

Area of Plan	Plan	Actual	Comments on coverage
Corporate Governance/AGS	4%	6%	Higher than planned due to Internal Audit leading on a number of areas within Corporate Governance work programme.
Key Financial Systems	6%	11%	Higher number of days than planned. Included some testing of systems so that External Audit may place reliance on work for 11/12 audit.
Shared Services	12%	3%	Key systems work undertaken. Planned work on Separate Legal Entity (SLE) lower than planned as decision delayed.
Corporate Cross-Services	12%	18%	Higher than planned including including additional coverage on areas highlighted through AGS and Lyme Green work e.g. Procurement/Project Management/Schemes of Delegation
Children, Families & Adults	18%	20%	Broadly as planned.
Places & Organisational Capacity	9%	10%	Broadly as planned.
Partnerships	3%	1%	Lower than planned, although significant partnerships work included within AGS coverage.
Anti Fraud and Corruption	12%	16%	11% is proactive and 5% is reactive.
Special Project	0%	6%	Lyme Green work.
Consultancy & Advice	9%	9%	Management requests as planned.
Contingency	12%	0%	Full 12/13 contingency of 200 days used.
Follow Up	3%	0%	Follow up work is charged against the project in question. Coverage as planned. Future follow ups will link in with the new CAP process (see 3.34).
<b>Total</b>	<b>100%</b>	<b>100%</b>	

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5.3 Internal Audit has a number of Performance Indicators that are measured and reported on:

Performance Indicator	2012/13 Actual	2012/13 Target	2011/12 Actual	Comments
Percentage of Audits completed to user's satisfaction	94%	90%	90%	Above target. Any below average scores/feedback is looked at by Audit Managers.
Percentage of significant recommendations agreed	93%	85%	98%	Above target. New report format requires an explicit 'Yes' or 'No' against each action.
Productive Time (of Chargeable Days)	84%	80%	86%	Above target.
Draft report produced promptly (per Client Satisfaction Form)	90%	90%	85%	On target and positive improvement.

5.4 At the beginning of the year, a new report format with a formal audit opinion was introduced. Feedback on the format was sought via an additional client questionnaire with positive results received. Since the end of 2012/13, the wording and layout of the report has been reviewed within Internal Audit and further improvements made.

### 6 Compliance with the Code of Practice for Internal Audit

- 6.1 Regulation 6 of the Accounts and Audit Regulations 2011 requires relevant bodies to conduct an annual review of the effectiveness of its internal audit and for a committee of the body to consider the findings.
- 6.2 In accordance with the Regulations the performance of Internal Audit has been measured using the checklist appended to the Code of Practice for Internal Audit in Local Government in the United Kingdom 2006. (A separate assessment of the Audit Committee has been undertaken).
- 6.3 The review has concluded that, although there are areas for improvement, the internal audit service is being delivered to the required standard. This review contributes to the assurances received for the 2012/13 AGS and will be shared





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with members of the Committee as part of the AGS training workshop in September.

- 6.4 An action plan for improvement has been developed that is separate from the AGS action plan, as the latter should only include significant weaknesses. Consequently, the review has established that the opinion, contained within this report, may be relied upon as a source of evidence in the AGS.
- 6.5 In March 2013 the Audit and Governance Committee received the Audit Plan for Cheshire East Council from Grant Thornton. The results of interim audit work concluded that overall the Internal Audit service continues to provide an independent and satisfactory service to the Council and that the external auditors could take assurance from the services work in contributing to an effective internal control environment at the Council.