

Internal Audit Annual Report 2011/2012

Cherwell District
Council

May 2012

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| Joint Management Team |
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| Members of the Accounts, Audit and Risk Committee |
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This document has been prepared only for Cherwell District Council and solely for the purpose and on the terms agreed with Cherwell District Council.

1. *Executive summary*

Background

CIPFA's Audit Code of Practice requires that the Head of Internal Audit provides a written report to the management and the Accounts, Audit and Risk Committee timed to inform the organisation's Annual Governance Statement. As such, the purpose of this report is to present our view on the adequacy and effectiveness of Cherwell District Council's system of governance, risk management and control.

Whilst this report is a key element of the framework designed to inform the Annual Governance Statement, there are also a number of other important sources to which management and the Accounts, Audit and Risk Committee should look to gain assurance. This report does not supplant the Council's responsibility for forming their own view on governance, risk management and control.

This report covers the period to the year ended 31st March 2012.

Scope

Our findings are based on the results of the internal audit work performed as set out in the 2011/12 Internal Audit Plan approved by the Accounts, Audit and Risk Committee. All changes have been outlined in our update reports taking to this committee during the year

Our opinion is subject to the inherent limitations of internal audit (covering both the control environment and the assurance over controls) as set out in Appendix 1.

Our internal audit was performed in accordance with *CIPFA's Audit Code of Practice*. *CIPFA's Audit Code of Practice* is not designed or intended to conform to the International Standards on Assurance Engagements issued by the International Auditing and Assurance Standards Board. As a consequence our work was not designed to comply with the International Standards on Assurance Engagements. Our work was designed to comply with CIPFA's Audit Code of Practice which must be followed for local government

Opinion

Our opinion is based solely on our assessment of whether the controls in place support the achievement of management's objectives as set out in our 2011/12 Internal Audit Plan.

We have completed the program of internal audit work for the year ended 31st March 2012 with the exception of the following reviews:

- Year end support (ongoing)
- Joint Management Group Systems workshop (deferred to 2012/13)

Our opinion is based on our assessment of whether the controls in place support the achievement of management's objectives as set out in our 2011/12 Internal Audit Plan.

We have completed the program of internal audit work for the year ended 31st March 2012 with the exception of the planned Joint Member workshop. Our work identified 22 low, 19 moderate and 1 high rated findings. Based on the work we have completed, we believe that there is some risk that management's objectives may not be fully achieved. Improvements are required in those areas to enhance the adequacy and / or effectiveness of governance, risk management and internal control.

The key factors that contributed to our opinion are summarised as follows:

Creditors

- One high risk issue was noted relating to non purchase orders. Our audit showed that no purchase order was in place for 84% of invoices received in year. In the majority of cases, these relate to purchases with small suppliers or invoices received for repairs works where it is felt that an initial cost cannot be estimated. Performance in this area is comparable to prior year (85%). If purchase orders are not raised, there is an increased risk that unauthorised purchases may not be identified until invoices are received. In addition, the Council is not able to monitor commitments unless a purchase order is posted to the system. This increases the risk that the budget position is not fully understood.

A summary of the key findings are described in further detail on page 3.

On pages 4 and 5 we show the direction of travel for both individual review areas and for the number of audit recommendations in each risk category (critical, high, medium and low). Both show very positive signs on the overall control environment at the Council.

For almost all areas reviewed in the year, the rating this year was either better or the same as last year. The number of internal audit findings and recommendations has reduced considerably with a total number of 42 findings in 2011/12 compared to 98 in the previous year. Although the mix and focus of our internal audit work have differed between years and therefore results may not be directly comparable, the significant reduction in findings, particularly in the high and medium rated findings from 50 to 20, should be source of considerable comfort.

Acknowledgement

We would like to take this opportunity to thank all audit sponsors, the Joint Management Team and members of the Accounts, Audit and Risk Committee for their co-operation and assistance provided during the year.

2. Summary of findings

Our annual internal audit report is timed to inform the organisation's Annual Governance Statement.

A summary of key findings from our programme of internal audit work for the year work is recorded in the table below:

| <i>Description</i> | <i>Detail</i> |
|---|---|
| <p>Overview</p> <p>We completed 19 internal audit reviews. This resulted in the identification of 0 critical, 1 high, 19 medium and 22 low risk findings to improve weaknesses in the design of controls and / or operating effectiveness.</p> | <ul style="list-style-type: none"> • Our audit plan was scoped to address the Council's key risks and strategic objectives. We mapped each review to these areas in our 2011/12 Internal Audit plan • We have completed our internal audit plan in line with the set timescales and have supported the Council with their year-end close down procedures and in their assessment of fraud. We have delivered training on fraud awareness, audit committee effectiveness and risk management in year. • Our plan included four "value enhancement" reviews and we have mobilised specialists in the areas of ICT and finance in year. |
| <p>Internal Control Issues</p> <p>During the course of our work we identified one high risk issue which has been outlined in the next cell. Given the materiality of this issue you should consider inclusion of this area in your Annual Governance Statement</p> | <p>Creditors</p> <p>The Council has issued a number of reminders on the importance of raising purchase orders in year. However, our audit showed that no purchase order was in place for 84% of invoices received in year. In the majority of cases, these related to purchases with small suppliers or invoices received for repairs works where it is felt that an initial cost cannot be estimated. This issue was also raised in 2010/11.</p> |
| <p>Good practice</p> <p>We also identified a number of areas where few weaknesses were identified and / or areas of good practice.</p> | <p>The following reviews were classified as low risk for 2011/12:</p> <ul style="list-style-type: none"> • Debtors • Payroll • Budgetary Control • Housing benefits • Cashiers • Risk Management • Legal and Democratic Services • Car Parking • Performance Management • Firewall |

3. Internal Audit work conducted

Introduction

Our internal audit work was conducted in accordance with our letter of engagement, CIPFA's Audit Code of Practice and the 2011/12 Internal Audit Plan.

The table below sets out the results of our internal audit work and implications for next year's plan. The direction of travel is also analysed so management can consider whether they should take action to reverse a trend or address stagnation.

We also include a comparison between planned internal audit activity and actual activity, to assist with budgeting and forward planning.

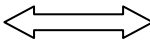




Results of individual assignments

| Audit unit | Report status | Direction of Travel | Report classification | Number of findings | | | |
|-------------------------------|---------------|---------------------|-----------------------|--------------------|----------|-----------|-----------|
| | | | | Critical | High | Medium | Low |
| General Ledger | Final | ↓ | Medium | 0 | 0 | 4 | 3 |
| Debtors | Final | ↑ | Low | 0 | 0 | 2 | 0 |
| Creditors | Final | ↔ | Medium | 0 | 1 | 0 | 2 |
| Payroll | Final | ↑ | Low | 0 | 0 | 1 | 0 |
| Budgetary Control | Final | ↔ | Low | 0 | 0 | 0 | 3 |
| Collection Fund | Final | ↑ | Medium | 0 | 0 | 3 | 2 |
| Cashiers | Final | ↑ | Low | 0 | 0 | 1 | 2 |
| Housing Benefits | Final | | Low | 0 | 0 | 1 | 3 |
| Car Parking | Final | ↑ | Low | 0 | 0 | 1 | 1 |
| Risk Management | Final | ↑ | Low | 0 | 0 | 1 | 1 |
| Legal and Democratic Services | Final | ↔ | Low | 0 | 0 | 1 | 1 |
| Performance Management | Final | n/a | Low | 0 | 0 | 1 | 1 |
| Firewall Follow Up | Final | ↑ | Low | 0 | 0 | 1 | 1 |
| Trade Waste and Vehicles | Final | n/a | Medium | 0 | 0 | 2 | 2 |
| | | | Total | 0 | 1 | 19 | 22 |

In addition we have carried out the following value enhancement reviews where no risk rating has been provided. No significant issues were noted in these reports for consideration in the Annual Governance Statement:

- Year end support (secondment)
- Shared ICT Provision – critical friend review
- Shared Management Milestone Validation
- Eco Town Governance and Spend
- Fraud Awareness Training

Direction of control travel

| <i>Finding rating</i> | <i>Trend between current and prior year</i> | <i>Number of findings</i> | | |
|-----------------------|---|---------------------------|----------------|----------------|
| | | <i>2011/12</i> | <i>2010/11</i> | <i>2009/10</i> |
| Critical |  | 0 | 0 | 0 |
| High |  | 1 | 4 | 6 |
| Medium |  | 19 | 46 | 76 |
| Low |  | 22 | 48 | 55 |
| Total |  | 42 | 98 | 137 |

It should be noted that the mix and focus of our internal audit plans have differed between years and therefore these results may not be directly comparable.

Management should look to concentrate on those areas of stagnant or deteriorating performance (e.g. General Ledger and Creditors) to ensure that controls in these areas are improved. Actions may include raising awareness, training, increasing compliance checks or improved escalation processes.

Comparison of planned and actual activity

We have provided a comparison of the planned and actual activity for the 2011/12 plan by review. One review (Group Systems workshop) has been deferred from the 2011/12 plan to 2012/13. This is a value enhancement piece of work and therefore does not impact on our ability to provide a year-end opinion on Internal Control.

| <i>Audit Unit</i> | <i>Audit Type</i> | <i>Budgeted days</i> | <i>Actual days</i> | <i>Reason for variance</i> |
|-------------------|-------------------|----------------------|--------------------|----------------------------|
| General Ledger | Value Protection | 5 | 5 | - |
| Debtors | | 5 | 5 | - |
| Creditors | | 5 | 5 | - |
| Payroll | | 5 | 5 | - |
| Budgetary Control | | 7 | 7 | - |
| Collection Fund | | 10 | 10 | - |

| | | | | |
|--|-------------------|-----|-----|---|
| Cashiers | | 5 | 5 | - |
| Housing Benefits | | 8 | 8 | - |
| Fixed Assets | | 5 | 0 | Days utilised for year end secondment |
| Car Parking | | 5 | 5 | - |
| Risk Management/Governance | | 5 | 5 | - |
| Transparency Agenda | | 5 | 5 | - |
| LDF Partnership Review | | 5 | 0 | Days utilised for year end secondment |
| Performance Management | | 10 | 10 | - |
| Finance – Year end | Specialist | 5 | 15 | Days increased to reflect year end requirements |
| Firewall and Disaster Recovery | | 10 | 10 | - |
| Critical Friend support | | 10 | 10 | - |
| Trade Waste and Vehicles | Value Protection | 5 | 5 | - |
| Validation of key milestones | Value Enhancement | 10 | 10 | - |
| Eco Town – Governance and Finance | | 5 | 5 | - |
| Fraud Awareness Training | | 5 | 5 | - |
| Shared Management – Group Systems Workshop | | 10 | 0 | Deferred to 2012/13 |
| Follow up | - | 5 | 5 | - |
| Audit Management | - | 30 | 30 | - |
| | - | 180 | 170 | |

4. Follow up work conducted

Introduction

Within the Annual Audit Plan for 2011/12, 5 days were assigned for following up recommendations raised during previous years in order to assess whether agreed actions had been implemented by management. Recommendations raised in previous reports were followed up within the 2011/12 scope. The table below summarises the follow up work performed.

Results of follow up work

| Audit unit | Number of agreed actions | Status of agreed actions | | | |
|--------------------------------|--------------------------|--------------------------|-----------------------|-------------|-------------|
| | | Implemented | Partially Implemented | Outstanding | Not yet due |
| General Ledger | 5 | 2 | 0 | 3 | 0 |
| Debtors | 6 | 4 | 1 | 1 | 0 |
| Creditors | 3 | 1 | 0 | 2 | 0 |
| Payroll | 2 | 2 | 0 | 0 | 0 |
| Budgetary Control | 3 | 1 | 0 | 2 | 0 |
| Collection Fund | 9 | 4 | 2 | 3 | 0 |
| Cashiers | 2 | 1 | 0 | 1 | 0 |
| Housing Benefits | 5 | 3 | 0 | 2 | 0 |
| Car Parking | 5 | 3 | 0 | 2 | 0 |
| Risk Management | 7 | 5 | 0 | 1 | 1 |
| Firewall and Disaster Recovery | 8 | 6 | 0 | 2 | 0 |
| TOTAL | 55 | 32 | 3 | 19 | 1 |

Please note follow up work was only undertaken for those areas reviewed in 2011/12 and 2010/11 where the scope was directly comparable.

We recommend that further work is conducted by the Council to ensure all previously agreed recommendations are implemented at the earliest opportunity.

Appendices

Appendix 1: Limitations and responsibilities

Limitations inherent to the internal auditor's work

We have prepared the Internal Audit Annual Report and undertaken the agreed programme of work as agreed with management and the Accounts, Audit and Risk Committee subject to the limitations outlined below.

Opinion

The opinion is based solely on the work undertaken as part of the agreed plan which provided for 180 audit days. The work addressed the control objectives agreed for each individual internal audit assignments as set out in individual assignment reports.

There might be weaknesses in the system of internal control that we are not aware of because they did not form part of our programme of work, were excluded from the scope of individual internal audit assignments or were not brought to our attention. As a consequence management and the Accounts, Audit and Risk Committee should be aware that our opinion may have differed if our programme of work or scope for individual reviews was extended or other relevant matters were brought to our attention.

Internal control:

Internal control systems, no matter how well designed and operated, are affected by inherent limitations. These include the possibility of poor judgment in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

Future periods:

Our assessment of controls relating to Cherwell District Council is for the year ended 31st March 2012. Historic evaluation of effectiveness may not be relevant to future periods due to the risk that:

- the design of controls may become inadequate because of changes in operating environment, law, regulation or other; or
- the degree of compliance with policies and procedures may deteriorate.

The specific time period for each individual internal audit is recorded within section 3 of this report.

Responsibilities of management and internal auditors

It is management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.





We endeavour to plan our work so that we have a reasonable expectation of detecting significant control weaknesses and, if detected, we shall carry out additional work directed towards identification of consequent fraud or other irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected, and our examinations as internal auditors should not be relied upon to disclose all fraud, defalcations or other irregularities which may exist.

Appendix 2: Basis of our classifications

Report classifications

The report classification is determined by allocating points to each of the findings included in the report

| <i>Findings rating</i> | <i>Points</i> |
|------------------------|-----------------------|
| <i>Critical</i> | 40 points per finding |
| <i>High</i> | 10 points per finding |
| <i>Medium</i> | 3 points per finding |
| <i>Low</i> | 1 point per finding |

| <i>Report classification</i> | | <i>Points</i> |
|---|---------------|--------------------|
|  | Critical risk | 40 points and over |
|  | High risk | 16– 39 points |
|  | Medium risk | 7– 15 points |
|  | Low risk | 6 points or less |

Individual finding ratings

| Finding rating | Assessment rationale |
|-----------------|---|
| Critical | <p>A finding that could have a:</p> <ul style="list-style-type: none"> • Critical impact on operational performance (quantify if possible); or • Critical monetary or financial statement impact (quantify if possible = materiality); or • Critical breach in laws and regulations that could result in material fines or consequences (quantify if possible); or • Critical impact on the reputation or brand of the organisation which could threaten its future viability (quantify if possible). |
| High | <p>A finding that could have a:</p> <ul style="list-style-type: none"> • Significant impact on operational performance (quantify if possible); or • Significant monetary or financial statement impact (quantify if possible); or • Significant breach in laws and regulations resulting in significant fines and consequences (quantify if possible); or • Significant impact on the reputation or brand of the organisation (quantify if possible). |
| Medium | <p>A finding that could have a:</p> <ul style="list-style-type: none"> • Moderate impact on operational performance (quantify if possible); or • Moderate monetary or financial statement impact (quantify if possible); or • Moderate breach in laws and regulations resulting in fines and consequences (quantify if possible); or • Moderate impact on the reputation or brand of the organisation (quantify if possible). |
| Low | <p>A finding that could have a:</p> <ul style="list-style-type: none"> • Minor impact on the organisation's operational performance (quantify if possible); or • Minor monetary or financial statement impact (quantify if possible); or • Minor breach in laws and regulations with limited consequences (quantify if possible); or • Minor impact on the reputation of the organisation (quantify if possible). |
| Advisory | <p>A finding that does not have a risk impact but has been raised to highlight areas of inefficiencies or good practice.</p> |



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