

**To the Chair and Members of the
AUDIT COMMITTEE**

ANNUAL REPORT OF THE HEAD OF INTERNAL AUDIT – 2012/13

EXECUTIVE SUMMARY

1. This report provides information on the role of Internal Audit, the work undertaken by the Section during 2012/13 and its overall opinion on the Council's system of internal control. The report also refers to the formal review of the effectiveness of Internal Audit required to be completed in accordance with the Accounts and Audit Regulations 2011.

Head of Internal Audit Annual Report 2012/13

2. It is a requirement of the CIPFA Code of Practice for Internal Audit in the United Kingdom that an annual report is produced by the Head of Internal Audit on the work undertaken by the Audit Section. The report for 2012/13 is attached at **Appendix 1**.
3. The report covers details of work done during the year April 2012 to March 2013.
4. During the year:
 - Internal Audit achieved 92% days input, compared with the original plan, with the main reasons for the shortfall being a significant increase in the sickness absence rates and associated return to work changes during the year. This increase was the result of 2 unexpected and unforeseeable long term sickness issues.
 - The Service carried out a range of investigations during the period, some of which resulted in disciplinary and / or Police action.
5. Based upon the audit work undertaken it has been possible to complete an assessment of the Council's overall control environment. This assessment takes account of the work of the External Auditor and the result of any inspections carried out. The Head of Internal Audit is able to confirm that the Council's system of internal control for 2012/13 was adequate and operated satisfactorily during the year. Internal Audit has identified two items to be considered for inclusion in the Council's Annual Governance Statement – these are:
 - Managing Attendance – failure to achieve meaningful reductions in the Council's sickness absence rates.
 - Fostering Overpayments – recent overpayments made to carers.

6. Some further weaknesses have been highlighted by Internal Audit's work during the year and these have been brought to management's attention. Internal Audit is satisfied with management's response to its recommendations and will continue to monitor progress in implementing improvement actions. The weaknesses do not change Internal Audit's overall opinion on the control environment.

Review of the Effectiveness of Internal Audit

7. The Accounts and Audit Regulations 2011 include a requirement for local authorities to:

"... undertake 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" Reg 6(3), and:

The findings of the review referred to in paragraph (3) must be considered, as part of the consideration of the system of internal control..." Reg 6(4).

8. No further guidance has been issued by CIPFA about how authorities should fulfil this requirement. We will comply with any CIPFA guidance when this is issued. For this year the review of the effectiveness of the system of Internal Audit has been informed mainly by:

- Internal Audit's annual report.
- Customer satisfaction
- An external audit review of Internal Audit, the outcomes of which were reported to the Audit Committee in January 2011.

9. The main features from these reports that contribute to this statutory review of Internal Audit are summarised below:

Internal Audit Annual Report

10. The annual report is referred to above and is attached at Appendix 1.

Customer Satisfaction

11. At the end of every completed audit, clients are asked to feedback their rating of the auditor's performance. Based upon the team's customer survey responses, the service was rated as 'satisfactory or very satisfactory' in 100% of all surveys received.
12. The Head of Internal Audit is very satisfied with this excellent level of customer feedback.

External Audit Review of Internal Audit

13. The Council's external auditor periodically reviews the effectiveness of Internal Audit including assessment of Internal Audit's compliance with professional audit standards. The most recent review, carried out by the Audit Commission in January 2011, concluded that "*the Council's Internal Audit section provides an effective service that contributes to the Council's system of Internal Control through the work it undertakes*".
14. Additionally, the external auditors take into account Internal Audit's work on key financial systems, controls and reconciliations each year to inform their opinion on the Council's statement of accounts. No issues have been raised by the external auditor with any internal audit work reviewed to date.

Conclusion

15. It is concluded that:
 - Internal Audit has effectively planned its work and has completed sufficient work to be able to provide an opinion to the Council on its system of internal control environment
 - Based on the planning and completion of audit work described in the annual report, customer feedback and review by external audit, it can be confirmed that there has been an effective internal audit during 2012/13.

RECOMMENDATIONS

16. The Audit Committee is asked:
 - To note the Internal Audit Annual Report for 2012/13, including confirmation that the Council's system of internal control was adequate and operated satisfactorily during the year
 - To support the conclusion from the report that there was an effective internal audit in place for 2012/13.

IMPACT ON THE COUNCIL'S KEY OBJECTIVES

17. The Internal Audit function works with managers in reviewing the adequacy and effectiveness of their governance and internal control arrangements. Where these can be made more robust, then risk management is improved and the more effective these arrangements are, the greater the chance of achieving objectives, in an effective and efficient manner.

RISKS & ASSUMPTIONS

18. This report, in presenting information about the state of the Council's internal control environment, allows Members to form an opinion about risks within the Council. The risk to the Council arises if there is inadequate or ineffective action to improve the risk management arrangements identified as unsatisfactory during

the year. Information detailed in this report on the implementation of internal audit recommendations gives Members an insight into the extent to which the management of risk is being improved.

LEGAL IMPLICATIONS

19. There is a statutory requirement on the Council to have in place an adequate and effective internal audit function.

FINANCIAL IMPLICATIONS

20. There are no financial implications arising from this report. The budget for the Internal Audit function is contained within the budget for the Resources Directorate.

CONSULTATION

21. This report has no specific significant implications in terms of the following:

Procurement	N/A	Crime & Disorder	N/A
Human Resources	N/A	Human Rights & Equalities	N/A
Buildings, Land and Occupiers	N/A	Environment & Sustainability	N/A
ICT	N/A	Capital Programme	N/A

BACKGROUND PAPERS

Internal Audit TeamMate files, CIPFA Code of Practice for Internal Audit in Local Government 2006, Internal Audit Customer Survey Responses, Internal Audit Management Information System.

REPORT AUTHOR & CONTRIBUTORS

Colin Earl, Head of Internal Audit, Telephone 01302 862939
E-Mail; colin.earl@doncaster.gov.uk

Colin Earl
Head of Internal Audit

ANNUAL REPORT OF THE HEAD OF INTERNAL AUDIT 2012/13

1. Purpose of the Report.

- 1.1 The purpose of the report is to present the Head of Internal Audit's annual report, which supports the Council's Annual Governance Statement.
- 1.2 The report also contributes to the requirements of the Accounts and Audit [England] Regulations 2011, for the Council to conduct an annual review of the effectiveness of Internal Audit [IA].

2. Introduction.

- 2.1 The report has been prepared by the Council's Head of Internal Audit. The aim of the report is to provide information on the role of IA and the work undertaken during the past year, and to support the statement prepared by the Council on its System of Internal Control.
- 2.2 It is not the intention of this report to give a detailed summary of each of the audits that have been undertaken during the year but to provide a broad review of the Council's control arrangements.

3. Legislation Surrounding Internal Audit.

- 3.1 Internal Audit is a statutory requirement for all local authorities in accordance with Section 151 of the Local Government Act 1972 and more recently the Accounts and Audit [England] Regulations 2011. The main thrust of these statutes is that every authority shall have arrangements for the proper administration of its financial affairs and that an officer be designated responsible for this task. To comply with these requirements the Council, in common with most other authorities, has delegated responsibility for this task to the Chief Financial Officer of the Council who, for Doncaster, is the Director of Finance and Corporate Services. It is for this reason the Director of Finance and Corporate Services is sometimes referred to as the Section 151 Officer.
- 3.2 The Accounts and Audit Regulations require councils to undertake 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. Further, councils must, at least once in each year, conduct a review of the effectiveness of its internal audit.
- 3.3 It is a requirement of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice for IA in the United Kingdom that an annual report is produced by the Head of Internal Audit on the work undertaken by the Audit Section.

4. Reviewing the Service.

4.1 IA Resources

Internal Audit's net expenditure in the year was £485,500 *¹ compared with a budget of £498,500. Income was generated by providing a comprehensive Internal Audit service to St Leger Homes. During 2012/13, Internal Audit had an establishment of 13.26 full time equivalent (FTE) staff which was broadly in line with similar sized Authorities in South and West Yorkshire. This will reduce to 11.90 (FTE) for 2013/14.

4.2 Audit Work Undertaken

A breakdown of time spent in the year April 2012 to March 2013 is summarised below:

Internal Audit Plan v Actual Days April 2012 to March 2013:

Strand	Activity	Planned Days	Planned Days	Actual Days	Actual Days
Mandatory	Corporate	134		91	
	Core financial systems	190		212	
	Financial admin	183		247	
	Previous year completions	83		110	
	School financial admin	110	700	108	768
Must do work	Governance	195		132	
	Grant and performance Certification	62		56	
	IT Audit	123		66	
	National Fraud Initiative	21		16	
	St Leger Homes	140	541	140 * ²	410
Follow-up work			87		55
	Responsive and risk related work		624		567
Total Plan			1,952		1800

Overall, 92% of planned time was delivered, with the main reason for the shortfall being a significant increase in the sickness absence rates which were due primarily to 2 unexpected and unavoidable long term sickness issues.

*¹ Estimate at March 2013

*² Contracted days

There were +/- variances across the original categories of work, but priority was given to ensuring sufficient work was completed to enable the Head of Audit to form an opinion on the internal control environment and be responsive to management for their requests for advice and support. The Head of Internal Audit, as last year, is grateful for the effort and commitment shown by the internal audit team to achieve a positive outcome despite this resource position.

Excluding the exceptional long-term sickness absences, Internal Audit maintained its year on year increase in chargeable time as a % of overall time available. It increased to 78% in 2012/13, compared with 76% in 2011/12 and 74% in 2010/11.

4.3 Implementation of Recommendations

The Internal Audit Team continues to work closely with managers to encourage a high level of implementation of recommendations that are aimed at improving the level of internal control. The extent to which managers within the Council implemented recommendations within agreed timescales is as follows:

Implementation of Recommendations – (Excluding Schools):

	Implemented %	In Progress but still in time %	Not yet Implemented / out of time %	Action Date not Reached %
2012/13	57	29	6	8
<i>Comparable data for 2011/12 and 2010/11:</i>				
2011/12	52	47	0	1
2010/11	45	29	22	4

The above table demonstrates that since 2011/12 management overall is responsive to and takes action to implement audit recommendations. The 6% of recommendations not yet implemented / out of time are relating to recommendations made in reports covering; specification and monitoring of voluntary sector services, planning policy, foster care payments & liquid logic system, payroll reconciliations and electoral services. Most outstanding recommendations were due to be completed in late 2012 / early 2013, although a small number have slightly older implementation dates.

Internal Audit will continue to closely monitor progress on these and bring any relevant matters to the Audit Committee's attention in its progress reports to the Committee.

4.4 Customer Satisfaction

At the end of every completed audit, clients are asked to feedback their rating of the auditor's performance. Based upon the team's customer survey responses, the service was rated as 'satisfactory or very satisfactory' in 100% of all surveys received.

4.5 Performance Indicators

At its meeting in June 2011, the Audit Committee agreed the key performance indicators that should be reported to it relating to the performance of the Internal Audit service. The indicators are shown below along with current performance for the year April 2012 to March 2013.

Performance Indicator	Target	April to March 2013	Variance
Percentage of planned audit work completed	90%	90%	0
Draft reports issued within 15 days of field work being completed	90%	82%	-8%
% of critical or major recommendations agreed	100%	100%	-
Cost per Chargeable Day	£326	£308	-£18
Percentage of Customer Satisfaction Surveys rated satisfactory or very satisfactory	90%	100%	10%

Ten reports were issued late during the year; two due to leave, two due to an urgent priority and six schools reports held over Christmas. Internal Audit is taking steps on improving this performance indicator.

Results relating to major recommendations and customer satisfaction remain extremely positive.

4.6 Quality Review

Quality review checks have been carried out and lead to an improvement in the standard of records maintained, by electronically recording feedback comments between supervisor and individual auditor.

4.7 External Audit Review of Internal Audit.

The Council's external auditors, KPMG, have a responsibility to review periodically the effectiveness of IA and specifically IA's compliance with CIPFA professional audit standards. (NB These reviews have been carried out every 3 years by the Council's previous external auditors, the Audit Commission).

The most recent examination of IA by the Audit Commission took place in 2010 and was reported to the Audit Committee in January 2011. That review concluded that *"the Council's Internal Audit section provides an effective service that contributes to the Council's system of Internal Control through the work it undertakes"*.

5. Planning Processes.

5.1 The 2012/13 plan was derived from the following sources:-

- The Council's risk registers
- Review of budgets and budget changes
- External reviews / inspections of Council activities
- Cumulative audit knowledge and experience
- Review of key plans, reports and press coverage
- Existing management and control environments, including information relating to any systems' changes
- Views on the risk of fraud or error
- A risk assessment of activity within each service area
- Priorities identified by strategic directors and directors
- Mandatory work on the Council's fundamental systems
- Legislative / Government requirements
- A provision was also made for unforeseen issues – 'responsive work'

5.2 We are satisfied that the coverage undertaken of the Council's activity by Internal Audit in the past year has been sufficient to be able to give an overall opinion on the Council's internal control environment.

6. Summary of Findings from Audit Reviews.

6.1 Main Financial Systems.

As part of the annual audit plan IA and the Audit Commission undertake a programme of reviews that covers the main financial systems of the Council. IA work in these areas is examined by the Council's External Auditors, who seek to place reliance on this work to assist their own audit of the Council's annual accounts. The systems reviewed by IA are set out below.

System	Conclusion / Findings
Cashbooks and Bank Reconciliation	There were no major or critical findings raised in this audit.
Council Tax	There were no major or critical findings raised in this audit.
Creditors	There were no major or critical findings raised in this audit.
Payroll	This work is ongoing and will be fully reported upon when the work is concluded.
Benefits	Audit work is being concluded in this area. There are no significant weaknesses identified so far.
Treasury Management	There were no major or critical findings raised in this audit.

System	Conclusion / Findings
Housing Rents	Audit work is being concluded in this area. There are no significant weaknesses identified so far.
Works Costing	Substantial assurance was reported in this area
Business Rates	There were no major or critical findings raised in this audit.
Debtors	There were no major or critical findings raised in this audit.

6.2 Significant Issues Arising

6.2.1 IA provides an 'opinion' on the control environment for all systems which are examined. A limited / no assurance opinion is given where one or more 'major / critical risks are identified in the area under examination. During 2012/13 the vast majority of areas audited by IA received positive audit opinions. There have been two areas audited during the year where weaknesses have been identified and consideration should be given as to whether these are significant enough to be included in the Council's Annual Governance Statement (AGS).

These areas are as follows;

a) Managing Attendance

Our audit noted very limited success in reducing the staff sickness/absence rates for the 2012/13 year with a projected number of days lost estimated at 13.98 against 14.56 days lost in 2011/12. The target for 2012/13 is 10.92.

Doncaster council entered into a shared service arrangement with Rotherham Council for the provision of HR Services. The HR self service portal is where managers administer their staff sickness absences.

However, Doncaster Council is not yet obtaining the full benefit from the implementation of the HR Self Service System, as phase one of the 3 year implementation plan focused primarily on the overall transfer of data from the Council's out-dated payroll system onto the new shared HR portal system. The absence module will, however, be fully implemented from 1st April 2013.

All managers must fully utilise the self service aspect of the HR System , i.e. ensuring all absences are fully and accurately recorded and monitored. This will enable them to subsequently manage staff absence better following corporate policies and procedures.

Until the above becomes fully embedded within Manager culture and sickness levels become significantly lower, we consider that additional

controls need to be put in place to complement and strengthen those already within the Self Service System. These include monitoring of departmental input to the HR System and the implementation and monitoring of Departmental Improvement Action Plans.

b) Payments to Foster Carers

In November 2011 we issued an audit report identifying overpayments to foster carers amounting to over £200k and gave no assurance over the systems in place as we considered that there was exposure to critical risks.

A follow up audit was undertaken and we reported in November 2012 that agreed management actions relating to the major risk exposures were being implemented.

However, in February and March 2013 management identified a number of new overpayments arising primarily through Social Workers failing to update the new case management system Liquid Logic. Checks designed to prevent duplicated payments or payments for Children reaching the age of 18 failed to operate.

A series of actions are being put in place to prevent more overpayments being made and to recover these newly identified overpayments

6.2.2 Other areas with limited assurance audit opinions but which, in Internal Audit's view, are not sufficiently significant to require consideration for entries in the AGS are summarised below.

a) Financial Transaction Processing 2011/12

The Council's Financial Procedure Rules provide a framework for the financial governance arrangements of the Council and more detailed guidance is available within the Finance Manual. However, this report concludes that most of the fifteen establishments / service areas did not comply fully with the requirements therein. This exposed the Council overall to the risk of fraud and error.

The main weaknesses were:

- Budget profiling and commitment accounting were not in use and known spending / profile changes were not being made to budgets for monitoring purposes.
- Inadequate controls, monitoring and guidance in place for the Councils procurement procedures and procurement advice provided to establishments.

It should be noted that the Core Financial Processes - Local Transaction Processing audit for 2012/13 has been completed. The audit opinion has improved on that given in 2011/12 and substantial assurance has been

provided that the financial processing arrangements for payroll, creditors and debtors are generally sound.

Partial assurance has been provided for the remaining two areas, purchase card and cash transactions, which are exposed to a higher risk in terms of VAT processing, adequate authorisation methods and segregation of duties.

b) Rowena House Care Home

The audit highlighted weaknesses in the management of residents' funds and the amenities funds, where a small number of irregular transactions were detected e.g. lack of supporting documentation such as invoices or receipts and arithmetical errors in records. However, no evidence of fraudulent transactions was detected.

Steps will be taken to ensure that lessons learnt at Rowena House will be rolled out to other care homes.

c) Emergency payments -Section 17 and Regular payments (CYPS)

The audit identified that the current systems for paying 'Emergency' and 'Regular' payments made by Children's Services under Section 17 of the Children's Act 1989 by cash or bank transfers were weak. There was a lack of consistency in procedures used by the various social worker teams. This has now been addressed through revising policy and procedures.

d) Section 117 After Care (Payments re Mental Health Care, Adults and Communities)

In July 2003 the Local Government Ombudsman issued a special report that concluded all Local Authorities should actively try to identify clients who had been wrongly charged for S117 after-care in the past and should reimburse them, or their estate. Section 117 payments are made to people in receipt of certain mental care services.

In 2006/07 the Council put in place resources to ensure that refunds were made / offered to all relevant service users. However, in 2009/10, the work on refunding eligible users ceased, leaving a large number of refunds not dealt with. The audit work confirmed that approximately half of eligible users had not received a refund offer.

Management has agreed to complete the exercise and bring this situation to a resolution. A provision of £631k has been set aside in the Council's accounts for settling the remaining cases.

e) Home Care Services

From the review undertaken it has been found that there are sufficiently sound plans in place to ensure that service users are receiving the care they require as soon as necessary and that monitoring is undertaken

to ensure that the care provided is as per the care plan and meets the correct standards.

There are, however, weaknesses with the payment processes that are in place as:

- Although the system will not allow payments to be made above the stated care plan, weaknesses in manual reconciliations and checking processes mean we may pay for services that have not actually been provided.
- This has also resulted in over £500,000 of disputed payments being withheld from care providers.

While we found no irregular payments during the audit, the weaknesses found expose the Authority to the risk of inaccurate or fraudulent payments being made.

f) Safeguarding Adults – Safeguarding Adults Personal Assets Team

The Safeguarding Personal Assets Team collects and manages the estates and possessions of vulnerable service users. Following referral of weaknesses to audit by the Head of Service, our review confirmed controls surrounding the access to, collection of and storage of personal property were weak and it was not possible to trace the movement of personal items and valuables or their eventual disposal / return.

A better electronic case management system is needed and payment and cash holding arrangements need to be improved.

There was no evidence found to suggest clients' needs were not being met as a result of these weaknesses. An action plan is being put in place to address to risk exposures.

g) Electoral Services

Skills and knowledge gaps in the department following key members of staff leaving and an absence of written procedures resulting placed the Council at risk of not achieving its statutory requirements with regard to Election Services.

Furthermore, the Elections team were functioning with a lack of efficient processes and procedures in place.

Steps are being made to resolve the problems in the form of a new staffing structure and recruitment process and improved systems.

h) Local Transaction Processing - Contact Centre

The Contact Centre appears to be running with sound controls in place. However, two weaknesses were found relating to the holding and protection of confidential information.

i) **Payroll Operations Audit**

Doncaster Council entered into a shared service arrangement with Rotherham Council on the 1st April 2012 to deliver HR services which included payroll processing. Doncaster payroll employees were transferred to Rotherham and all Doncaster Council and St Leger Homes staff are now paid via the Rotherham payroll system.

Due to the transfer priority had to be given to ensuring that the migration of information was successful. Our current audit is assessing the potential risks faced by the Council and the existence and operation of controls in place to mitigate the risks. Our findings and conclusions will be fully reported on in our next progress report.

6.3 **Schools**

The Schools Financial Value Standard (SFVS) replaced the Financial Management Standard in Schools (FMSiS). The SFVS is a requirement for local authority maintained schools. Governing bodies have formal responsibility for the financial management of their schools, and so the Standard is primarily aimed at governors.

Internal Audit has spent considerable time during the year helping schools to meet the Standard by providing help and support including training sessions for School Governors and staff and also providing information through the DMBC website.

A specific requirement of the SFVS was for schools to have adequate Anti-fraud and Corruption arrangements in place. To assist, Internal Audit designed and provided a model Anti-fraud and Corruption Policy and Strategy for schools to adopt to help meet the above requirement.

Routine audits were carried out at 6 primary schools during the year. No schools have received an unsatisfactory opinion following our audit.

6.4 **Responsive Work.**

6.4.1 Approximately 32% of Internal Audit time is used to address issues which arise during the year. This work can be sub-divided into two categories:-

- Investigative work - This is where some form of non-compliance with Council regulations (Contract Procedure Rules / Financial Procedure Rules / Codes of Conduct etc) including potential fraud is suspected. Investigations of this type are by their nature time consuming because of the need for attention to detail and accurate recording on the understanding the evidence could be used in formal disciplinary hearings or by the Police in any subsequent prosecutions. A number of these issues are reported under the Council's confidential reporting code. These range from allegations

of minor pilfering to potentially more serious issues relating to failure to follow appropriate procedures relating to the awarding of contracts.

- Requests for assistance / advice – We respond positively throughout the year to managers requests for advice and assistance relating to governance, internal control and other risk related issues. Feedback from managers indicate this is a much appreciated service provided by the team.

6.4.2 Some of the more significant issues reviewed of this nature IA has addressed during 2012/13 include:

- **Fraudulent Payments**

In 2011/12, management of a sports facility raised suspected irregularities regarding some of its operations. The issues have been investigated and referred to the Police and a decision on potential prosecutions for fraud is expected in April 2013.

- **Fraudulent falsification of benefits**

As part of work undertaken on the National Fraud Initiative, a match was identified between the address of a benefit claimant and that of an employee.

Following investigation the employee was dismissed and the claimant is being prosecuted for benefits fraud.

- **Fraudulent claims for falsified work**

Concerns have been received from two schools regarding potential fraudulent invoices received from a contractor. The indication is that false invoices have been raised and submitted for payment by the two schools for work that had not been done.

No payments were made and the contractor is investigating the role of one of its employees. The Council reserves the right to report the case to the Police, subject to satisfactory investigation and explanation from the contractor.

6.4.3 Overall, despite the current economic context, the Council is experiencing relatively little fraudulent activity. The examples stated above do not change the audit opinion that, overall, the arrangements in place for preventing and detecting fraud and corruption are satisfactory and do not have a detrimental impact on the overall control environment.

7. Assessment of the Control Environment for Year to 31st March 2013.

7.1 Based upon the audit work undertaken it has been possible to complete an assessment of the Council's overall control environment. Accordingly, based upon the IA work undertaken this year we can confirm that the Council's control environment for 2012/13 was adequate and operated satisfactorily during the year.