

# **INTERNAL AUDIT STRATEGY AND ANNUAL AUDIT PLAN 2004-2007**



## **1. Role of Internal Audit**

1.1 All local authorities must make proper provision for internal audit in line with the 1972 Local Government Act (S151) and the Accounts and Audit Regulations 2003. The latter states that authorities must “maintain an adequate and effective system of internal audit of its accounting records and of its system of internal controls in accordance with the proper internal audit practices”.

1.2 East Sussex County Council has delegated responsibility for ensuring that statutory internal audit arrangements are in place to the Deputy Chief Executive and Director of Corporate Resources. These arrangements form a key element of the County Council's framework for corporate governance. On a day to day basis the Assistant Director (Audit and Performance) serves as the County Council's Chief Internal Auditor and the Audit and Performance Division provides internal audit services to the County Council on behalf of the Deputy Chief Executive and Director of Corporate Resources.

1.3 Internal audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment, comprising risk management, control and governance, by evaluating its effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources. To carry out this role the Audit and Performance Divisions Internal Audit Service (IAS) aims to:

- satisfy legal requirements and professional standards;
- examine, evaluate and report objectively on the adequacy of arrangements to secure proper economic, efficient and effective use of resources;
- assist management with its responsibility for establishing and maintaining internal control systems and for ensuring that resources are properly applied, risks are appropriately managed and outcomes are achieved;
- investigate allegations of fraud and corruption in line with the Council's Anti-Fraud and Corruption Strategy; and
- provide an annual opinion to Members and Officers on the adequacy of the Council's control environment, and regular reports on key audit findings.

1.4 The key service objectives for the IAS as set out in the 2004/05 Council Plan are to:

- prepare, maintain and deliver the annual risk based internal audit plan;
- promote risk management through proactive audit involvement in key service developments; and
- play an active role in developing the Council's approach to corporate governance.

1.5 The delivery of these objectives is underpinned by the Audit and Performance Divisional Business Plan and the objectives agreed with individual members of the IAS through the performance appraisal process.

## **2. Risk assessment**

2.1 The County Council's three year rolling audit strategy is updated on an annual basis. This is based on a risk assessment of all the County Council's major systems and other auditable areas. This allows us to prioritise those areas to be included within the plan on the basis of risk.

2.2 The risk assessment and update of the annual plan has been informed by extensive consultation with the following stakeholders to ensure that their views and the risks within their departments are reasonably identified and reflected within the plan, where appropriate:

- the Deputy Chief Executive and Director of Corporate Resources;
- members of the Audit and Best Value Scrutiny Committee;
- Departmental Management Teams (including Chief Officers);
- key contacts within departments and lead officers for key corporate projects;
- E-business managers
- the Council's external auditors, the Audit Commission, to ensure that audit resources are used to the best effect, reliance can be placed on the work of internal audit and duplication is avoided; and
- other bodies internal audit providers, where joint working is proposed.

In times of significant transformation organisations must both manage change effectively and ensure that core controls remain in position. The Council is currently engaged in a challenging transformation programme and therefore internal audit must be in a position to give an opinion/assurance that covers the control environment in relation to both new developments and existing systems. This has been a key driver in developing this strategy and plan.

2.3 The key factors, which have driven our assessment of risk and audit needs for 2004/07, are:

**Financial excellence** – the need to ensure that adequate and effective arrangements exist across the Council to monitor and control both capital and revenue budgets, its key financial systems and to manage the Council's financial resources in support of service outcomes;

**CBOSS and other major systems developments** – the need to ensure that sufficient audit resources are made available to provide clear guidance on the control issues and risks arising from new systems developments or major changes to existing systems. CBOSS is the Council's most significant systems development which involves the replacement of the Council's core financial and human resources systems and managed services;

**Partnership working** – the need to ensure that the growing number of partnerships with other public, private and voluntary sector bodies have in place robust financial controls and governance arrangements, and that risks to the County Council are identified and managed;

**Governance arrangements** – the need to independently review and give an opinion on the Council's arrangements for both corporate governance and risk management, to support the production of an annual statement of assurance within the statement of accounts;

**E-government and ICT** – the need to provide proactive guidance on internal control issues arising from the Council's development of e-government agenda through the IEG3 Statement. This is coupled with the need to ensure that adequate arrangements exist to ensure the security and integrity of new ICT systems;

**Procurement and contract management** – the need to ensure that the County Council's systems for all aspects of procurement, including contract management, are efficient and effective, particularly for major new contracts eg post Owen Williams and Waste Management PFI, and in the light of national initiatives like Rethinking Construction;

**Performance management** – the need to ensure that effective systems are in place to deliver the performance outcomes against which the County Council is increasingly assessed eg BVPIs, CPA and PSA, particularly the information systems which underpin the measurement and reporting of performance;

**Internal control environment and specific risks** – the need to ensure adequate internal audit coverage across all departments which supports the achievement of good governance, effective risk management and financial excellence.

2.4 The key risk issues within each department which are included in the audit plan for the coming year are set out below:

**Corporate Body (including ICT audit):**

- CBOSS – to support the development of the control environment within the CBOSS project;
- Fundamental accounting systems - full coverage in line with managed audit approach, taking account of the impact of new systems implementation during the year;
- Pension Fund – a number of reviews planned as part of a separate programme of work specific to the Council's role in administering the East Sussex Pension Fund;
- Anti-Fraud and Corruption – a review of the Anti-Fraud and Corruption Strategy and the processes that underpin it. A key element of the Council's governance framework, the review will examine the adequacy and effectiveness of current arrangements;
- Budgetary control – a themed review across the Council which will report on the outcomes of a self assessment exercise and also carry out detailed work assessing improvements in control resulting from the financial excellence programme;
- E-government – a range of reviews in support of developments planned within the IEG3 Statement, particularly roadmap and premier projects.
- Capital – building on previous work this review will focus on the effectiveness of arrangements for managing capital projects, particularly the roles and responsibilities of different departments and other bodies such as schools.

**Chief Executive's**

- Corporate Governance – carry out annual reviews of corporate arrangements and give an opinion in support of the preparation of a corporate assurance statement. This approach will be underpinned by the provision of a separate report for each department giving an opinion on its internal control environment based on work completed during the year;
- Corporate performance indicators – using the same methodology as the review carried out in 2003/04 we examine a range of high risk indicators prior to the annual external audit review of BVPIs;
- Area Investment Framework and Global Grants Intermediary – a review of the financial and governance controls in place under those schemes where the Council has taken on accountable body status;
- Freedom of Information Act – reviewing the processes in place to meet the requirements of this legislation, prior to it coming into force in 2005.

### ***Education and Libraries***

- PFI arrangements – a review of the contract management arrangements for the Peacehaven PFI;
- Early Years and Childcare – to review the financial controls in this expanding service area which has also seen recent changes in funding arrangements;
- School Improvement Service – to review the effectiveness of the management arrangements for this significant outsourced service;
- Audit of Schools – this year will see the final phase of roll out of the financial self assessment programme for schools, supported by a smaller number of school visits and themed reviews of financial management and catering income;
- Libraries – work to roll out financial self assessments for libraries will begin.

### ***Transport and Environment***

- Waste Management PFI – a programme of audits continuing the approach already in place jointly with Brighton and Hove City Council; our work will focus on reconciliation of payments;
- Renewal of Outsourced Contracts (ROCS) – support of this major ongoing project work which will include a review of the contract specification;
- Passenger Transport – building on the work carried out in 2003/04 this review will focus on arrangements for home to school transport;
- Road Maintenance – a contract audit of roads maintenance will review current controls, but also inform the ROCS project.

### ***Social Services***

- Pooled budgets – a continuing programme of work to review financial and governance controls, and where possible to establish joint arrangements with NHS Internal Audit providers;
- Mental Health Services – reviews of joint commissioning arrangements and integrated service provision to assess the robustness of financial and governance controls;
- PFI Project – to provide support to this project for Older Person's Services drawing on our experience in schools and waste.

## **3. Audit Needs Assessment**

3.1 The risk assessment process identifies all auditable areas and assesses the level of risk associated with each. In order to produce the County Councils audit needs assessment the following key principles are then applied:

- All core financial systems (including the main accounting systems, creditors, debtors, payroll, pensions) are subject to annual audits of compliance against key controls;
- All systems and auditable areas which are identified as high risk in our risk analysis are reviewed each year (except where the risk is short term e.g. exit arrangements from a current contract or new systems development) – this may include the use of shorter interim audits in some years;
- Systems assessed as medium risk – a full review every three years with a shorter follow up review in the subsequent year;
- Systems assessed as low risk – a full review every five years;
- Systems assessed as weak or unsatisfactory during 2003/04 which are not subject to annual audit should be considered for a follow up review to assess the effective implementation by management of agreed audit recommendations;
- Where common areas of risk are identified across several departments then the use of corporate themed reviews is considered to ensure an approach which is both consistent and makes effective use of resources;

- Where a system is assessed having risks which require both systems audit and ICT audit input then joint reviews should be carried out to ensure an approach which is both consistent and makes effective use of resources;
- The development of new systems or significant changes to existing systems should be separately identified within the audit needs assessment.

#### 4. Matching audit needs to resources

4.1 The audit needs assessment has been matched with available internal audit resources to produce the three year strategic plan and the annual plan for 2004/05. Resource planning assumptions for 2004/05 have been fully reviewed following consultation with staff to ensure that sufficient time is allocated for indirect work, for example training and development. It is assumed that some audit work will be carried forward from 2004/05 for completion within resources available in 2005/06 and that this will not exceed that carried forward from 2003/04. This reflects a reasonable level of work in progress.

4.2 Resources have also been allocated to the three external bodies for whom Audit and Performance Division provides internal audit services: East Sussex Fire Authority, Sussex Magistrates Courts Committee and Plumpton College. Our contract with Sussex Magistrates Courts Committee ends on 31 March 2005 upon national restructuring of the service.

4.3 The resource plan assumes successful recruitment to two of the three current vacancies during the year. We will continue to use agency staff where appropriate to help deliver the plan. Consideration will also be given to using specialist external resources potentially including forensic computer work and security reviews of the new SAP system. When fully staffed, the IAS will have 13.7 full time equivalents, in addition to the Chief Internal Auditor role of the Assistant Director (Audit and Performance).

4.4 The total number of planned audit days for 2004/05 is 2,129. Whilst this is lower than the agreed plan in previous years, it is in the range of actual days delivered as set out in the table below. This level of resource is sufficient to allow the IAS to deliver its risk based plan in line with the standard set out in 2003 Code of Practice for Internal Audit in Local Government.

*Table 1: Annual Internal Audit Plan – Plan and Actual Days Delivered*

	2000/01	2001/02	2002/03	2003/04	2004/05
Plan Days	2,366	2,420	2,598	2,294	2,129
Actual Days	2,147	1,910	2,191	2,047	-

#### 5. Audit Approach

5.1 The approach of internal audit is to use systems based reviews, supplemented in some areas by the use of regularity audits, control self-assessment and themed reviews. All audits have regard to management's arrangements for:

- securing the proper, economic, efficient and effective use of resources;
- achieving key performance indicators, where appropriate;
- preventing fraud and irregularity.

5.2 In addition to these audits and the advice on controls given on specific development areas, which are separately identified within the plan, there are a number of generic areas where demands upon internal audit cannot be planned in advance. For this reason time is built into the plan to cover the following areas:

- Contingency – an allowance of 275 days to provide capacity for anti-fraud and corruption work including special audits and the investigation of potential irregularities. This contingency also allows some flexibility within the plan for any unplanned audit work and for the completion of work in progress from the 2003/04 plan;
- Discretionary and development work – an allowance of 50 days to support the development of the corporate approach to governance and risk management; and
- Advice to departments – an allowance against each department to cover the provision of ad hoc advice on audit and control issues.

A summary of the allocation of audit resources across the 2004/05 audit plan is shown at Appendix A. Appendix B shows the coverage of the audit plan in more detail.

5.3 One outcome of the risk assessment described earlier in the strategy is that both the absolute and relative number of days planned within Corporate Body has increased for 2004/05. This reflects the significant impact of CBOSS. We will continue to engage with and support the project as it is developed and rolled out. We will also carry out reviews of those core systems which are being replaced as part of the project. With the agreement of our external auditors, under our managed audit arrangements, these reviews will focus mainly on the new systems and processes that result, although some work will also need to be carried out in relation to legacy systems.

## **6. Training and development**

6.1 The effectiveness of internal audit service depends significantly on the quality, training and experience of its staff. Training needs of individual staff members are identified through the performance appraisal process, and delivered and monitored as part of the CRD's Training and Development Plan. As well as basic training in audit techniques, and the acquisition of specialist audit skills, the IAS is committed to coaching and mentoring its staff, and to providing opportunities for appropriate professional development. During 2004/05 five members of the team will be supported in studying for the Institute of Internal Auditors (IIA). The IAS will also provide a work placement for CRD's CIPFA trainee from February 2005.

## **7. Quality and performance**

7.1 The IAS maintains a Quality Manual, which sets out the standards to which all audit assignments are completed. Following a review against the revised Code of Practice for Internal Audit in Local Government issued by CIPFA in 2003 we have identified a number of improvements to our processes which will be implemented during the year. The revisions to the Quality Manual will also reflect the implementation of the Galileo package for planning, performance monitoring and working papers.

7.2 The performance of the IAS is measured against the key service targets and objectives set out in the Council Plan, the CRD Business Plan and the Audit and Performance Division's Business Plan. At a detailed level each audit assignment is monitored and customer feedback sought. There is ongoing performance appraisal and supervision for all IAS staff during the year to support them in achieving their personal targets. External review of the IAS is carried out by the County Council's external auditors and reported on in the Audit and Inspection Annual Letter and within the CPA.

7.3 In addition to the individual report to management for each audit assignment, quarterly reports on key audit findings and the delivery of the audit plan against key performance indicators are made to both COMT and the Audit and Best Value Scrutiny Committee. These key performance indicators and targets for 2004/05 are shown in appendix C.

7.4 The IAS will continue to liaise closely with other internal audit services through the Sussex Audit Group, Home Counties Chief Internal Auditors' Group and the County Chief Advisors' Network.

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## Annual internal audit plan by customer

<b>Service</b>	<b>2004/05 Plan Days</b>	<b>% of 2004/05 Plan Days</b>	<b>2003/04 Plan Days</b>
East Sussex County Council			
Corporate Body (incl CRD)	443	20.8%	403
Computer Audit	260	12.2%	340
Education & Libraries	394	18.5%	479
Social Services	300	14.1%	376
Transport & Environment	175	8.2%	202
Legal & Community Services	-	-	58
Chief Executives	125	5.9%	59
Contingency (incl. carry forward)	275	12.9%	200
Discretionary and corporate projects	50	2.3%	70
<i>Sub total – internal customers</i>	<i>2,022</i>	<i>95.0%</i>	<i>2,187</i>
Fire Authority	60	2.8%	60
Magistrates	20	0.9%	20
Plumpton College	27	1.3%	27
<i>Sub total - external customers</i>	<i>107</i>	<i>5.0%</i>	<i>107</i>
<b>Total audit days</b>	<b>2,129</b>	<b>100.0%</b>	<b>2,294</b>

**Strategic Audit Plan 2004/07 – Detailed analysis of coverage**

***See attached spreadsheet***

## Internal Audit Performance Indicators

Performance Indicator	Target
Planned days delivered (%)	100%
Planned audits completed = final reports issued (%)	90%
Actual v Plan time on completed audits (%)	102%
Direct time (%)	71.3% <sup>1</sup>
External Audit reliance on internal audit	Achieved
CPA score maintained	4/4
Recommendations accepted (%)	90%
Customer feedback forms scoring 3 out of 5 or higher (%)	95%
Reports to Chief Officers and Members	Quarterly

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<sup>1</sup> The calculation of this indicator has been revised for 2004/05 and is therefore not comparable with previous years.