

Report to: **Audit and Best Value Scrutiny Committee**

Date: **20 November 2008**

By: **Deputy Chief Executive and Director of Corporate Resources**

Title of report: **Internal Audit Progress Report – Quarter 2 (1 July 2008 – 30 September 2008)**

Purpose of report: **To provide Members with a summary of the key audit findings, progress on delivery of the audit plan and the performance of the internal audit service during Quarter 2**

RECOMMENDATIONS: Members are recommended to consider and agree any action that should be taken in response to the issues raised as a result of the audits carried out during Quarter 2

1. Financial Appraisal

1.1 There are no direct financial implications arising from the recommendations in this report.

2. Supporting Information

2.1 The current annual plan for internal audit is contained within the Audit & Performance Division's Internal Audit Strategy and Annual Plan 2008-09. This was prepared after consulting Chief Officers and senior managers and was endorsed by Audit and Best Value Scrutiny Committee (19 June 2008) and Cabinet (8 July 2008). It is updated each year.

2.2 An annual internal audit report, which gives Members and Chief Officers an opinion on the efficiency and effectiveness of the Council's internal control environment, is prepared each year, usually in June. This progress report covers work completed between 1 July 2008 and 30 September 2008.

3. Summary and Key Audit Findings

3.1 Key audit findings from final reports issued during quarter 2 are summarised in Appendix A. Overall, a total of 32 formal reports have been issued, of which 2 received 'Full Assurance', 1 received 'Substantial Assurance' and 4 received 'Partial Assurance'. Of the remaining 25 reports, which did not require standard assurance based opinions, 22 were schools, all of which successfully passed the Financial Management Standard in Schools, and 3 related to ongoing projects.

3.2 All reviews subject to 'Partial Assurance', 'Minimal Assurance' or 'No Assurance' audit opinions will, as a matter of course, be subject to formal follow up during 2009/10 to ensure satisfactory implementation of internal audit recommendations. In addition, an ongoing exercise is undertaken to monitor implementation of all high risk recommendations (regardless of the overall audit opinion).

3.3 Details of all completed audits and other key activity from quarter 2 are provided within Appendix A. Members' attention is also drawn to our work on:

- National Fraud Initiative (NFI) – As reported on in quarter 1, Internal Audit have been working with Legal Services and the Freedom of Information Officer to put in place Fair Processing Notices as part of the NFI. This work has now been successfully completed. In addition, following extensive preparatory work with data owners, all data sets have now been submitted to the Audit Commission via their secure website within the October deadline. The results from the national data matching are expected in January 2009.

- Anti Fraud and Corruption – as part of a programme of anti fraud and corruption activity, Internal Audit have been working with Legal Services and Corporate Communications to raise

awareness amongst staff of the County Council's Confidential Reporting ('Whistleblowing') Policy. A new leaflet entitled 'Don't Turn a Blind Eye – Tackling Fraud, Corruption and Other Wrongdoing' has been distributed to all non-school staff with the October 2008 payslips and is supported by new guidance for managers on how to respond when receiving such reports.

4 Performance against targets

4.1 During quarter 2 of 2008/09 we delivered 624.5 productive audit days, an increase of 61.9 over what was delivered in quarter 1. Overall, a total of 1187.1 days have therefore been delivered to date, equating to 50.1% of the plan days. A total of 36.3% of the audit assignments in the plan have been finalised in the year to date, which includes a number of larger pieces of work e.g. SAP upgrade (70 days), and we still anticipate meeting our target by year end. Performance against both of our effectiveness targets is strong with 96.9% of recommendations being accepted and customer satisfaction running at 91.1%. During the quarter we achieved one of our key performance targets, as our new external auditors PKF confirmed in their Annual Governance Report that they were able to place reliance on the work of internal audit.

5. Other Issues

5.1 As explained within Appendix A, a significant amount of time has been spent during the past quarter working with the project team on the SAP Upgrade, including providing an audit opinion prior to the go-live decision. As anticipated the upgrade project has had a major impact on the delivery the annual programme of fundamental accounting systems reviews, in terms of both resources and timing. With the go-live in October 2008, it has not been possible to complete any of the reviews prior to this, resulting in a potential workload pressure on both Internal Audit and key client staff in the remaining months of the year. This issue was raised with our external auditors, PKF, as part of audit planning earlier in the year. Following detailed discussions we have agreed with them, and the Deputy Director of Corporate Resources to perform key control reviews only on HR/Payroll, Accounts Payable, Accounts Receivable and General Ledger in 2008/09, with full systems reviews being undertaken in 2009/10. Where possible, the testing of controls as part of these audits will utilise the work already performed by Internal Audit as part of the SAP Upgrade project. This approach should provide the necessary assurance whilst minimising the workload on those involved during quarters 3 and 4.

6. Priorities for Quarter 3

6.1 Priorities for the period 1 October 2008 – 31 December 2008 include:

- Commencement of fundamental accounting system reviews;
- FMSiS – continuing the programme of primary school assessments;
- Phased implementation of the new Internal Audit structure;
- Anti Fraud and Corruption – continued work to implement identified actions.

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BACKGROUND DOCUMENTS –
Internal Audit Strategy and Annual Plan 2008-09

Appendix A

Summary of key audit findings

Treasury Management System (Corporate Resources Directorate)

This review sought to give assurance that Treasury transactions are authorised properly, in accordance with ESCC's Treasury Management Policy and with advice from approved advisers, that transactions are recorded accurately in the accounts, that they are made only with approved organisations, that investment performance is monitored effectively, and that there is satisfactory internal control within the money transfer systems.

This report was finalised in September 2008, prior to the recent and severe uncertainties within the world banking systems, and recognised that the Council's Treasury Management Strategy had been recently updated, to reduce further the risk of loss in the event of the financial collapse of one of its counterparties.

From the audit work completed during this review, Internal Audit provided **full assurance** that there is a sound system of controls in place. A number of minor recommendations have been agreed with management, and implemented.

Pension Fund Investments (Corporate Resources Directorate)

The objectives of this review, which forms part of our Pension Fund Audit Strategy, were to ensure the following:

- Pension fund investments are recorded completely, accurately and correctly, that fund manager performance is monitored, and appropriate remedial action taken where necessary;
- Short term investments held by the Council on behalf of the Fund are apportioned accurately, with all income from interest and dividends received promptly and completely;
- Risks to the availability, integrity and security of data are managed adequately.

From the audit work completed during this review, Internal Audit is able to provide **full assurance** that there is a sound system of controls in place, with only one minor recommendation being made. This was agreed with management.

SAP Future Phases (Corporate Resources Directorate)

During the year, audit advice, support and challenge has been provided in relation to SAP developments, including most recently the major upgrade of SAP early in October 2008. Internal audit were actively involved in this project from the outset, which included providing assurance to management that the control environment in the upgraded system would be at least as sound as its predecessor. The system and the hardware have now been upgraded successfully following extensive testing by management and internal audit.

A series of internal audit control reports were issued throughout this project providing assurance to management on internal controls and providing recommendations to further improve the general control environment. These have all been agreed with project managers.

Ongoing ICT Audit Advice and Support (Corporate)

The ICT Audit Plan for 2008/09 includes the provision of internal audit advice and support in relation to a number of ongoing projects and developments to ensure technical control issues are addressed as the activities progress. During quarter 2, this has included:

SIMS Learning Gateway - A report has already been issued with respect to the review of the Learning Gateway pilot. Internal Audit continues to review controls for the wider deployment of the Gateway to all schools by the end of August 2009. Areas of assurance as part of this work include back-up arrangements, user administration and project management.

Carefirst 6 – In addition to the review of the current Carefirst System, as reported above, work is continuing on the development and testing of CareFirst 6.

Business Continuity (Chief Executive's Department)

This review sought to provide assurance that the Council's business continuity and disaster recovery arrangements are sufficient to respond adequately to any foreseeable emergency or disaster, maintaining reasonable continuity of service for those applications and services which are deemed to be critical. It also sought to provide assurance that agreed level and speed of recovery/business continuity is acceptable to the Authority for all critical functions.

From the audit work completed during this review, Internal Audit is able to provide **partial assurance** that there is a sound system of controls in place. Whilst the Emergency Planning function and the individual departments have addressed business continuity and disaster recovery positively and clear improvements have been made, examples were found where business continuity was not always viewed as an ongoing process and that testing and updating arrangements could be improved further.

Recommendations for improvement were made in relation to the following areas:

- Developing a regime for the regular conduct of a Business Impact Analysis;
- Implementing specific arrangements for the regular review of the "Corporate" list of critical services (e.g. Reception facilities, IT Services, Property, Telephony);
- Improving awareness of the plan to ensure all key staff are aware of their roles and responsibilities in relation to it;
- Ensuring that the testing of the Business Continuity Plan continues at least annually, each time testing the response to a different type of invocation.

These recommendations have been included in a comprehensive action plan which has been agreed with management and which will be subject to a follow up review during 2009/10.

Carefirst – ICT Audit (Adult Social Care)

Carefirst represents the core system for recording the care needs of vulnerable adults and children, with the system data also being relied upon for income and payments processes. The objective of this review was to give assurance to management on the overall effectiveness of ICT security controls within the system, including:

- Access controls and user permissions;

- Support and maintenance arrangements;
- Disaster recovery.

Based on the activity carried out as part of this review, Internal Audit is able to provide **Partial Assurance** that there is a sound system of controls in place. The main reasons for this opinion are as follows:

- Individual accountability within the system is undermined as a result of:
 - The use of generic, shared user accounts by temporary staff;
 - The failure to enforce strong password criteria.
- User administration rights are retained by departmental representatives, bypassing the CareFirst System Administration team.

Recommendations have been made to address the weaknesses identified, and these have been incorporated within an agreed management action plan. This will be subject to a formal follow up review during 2009/10.

Business Transformation (Adult Social Care)

Internal Audit continued to provide ongoing support to the Business Transformation Programme at overall project progress meetings and at individual project module level, providing advice on internal control, risk and ICT issues.

During the quarter, Internal Audit work focussed on providing assurance and advice relating to:

- Aegis System closedown, specifically:
 - The development and testing of an in-house developed database application for Direct Payments and confirmation that data has been properly transferred from Aegis into the new application;
 - Other data transfers from Aegis into Abacus as part of the switch-off process;
- The development and testing of system modules e.g. Controcc, Mobile Financial Assessments and the Interactive Resource Monitor;
- The continued development and testing of Abacus and Controcc interfaces;
- Ensuring proper implementation of previous audit recommendations relating to the AEGIS closedown.

No significant issues were identified through this audit activity and effective progress has been made implementing audit recommendations.

Putting People First (Adult Social Care)

Putting People First (PPF) is a major project being undertaken by Adult Social Care to implement a nationwide government initiative to tailor care services to people's individual needs. The project must ensure that all revised and new systems are in place by 2011.

Part of the project will include the need for Adult Social Care to review and radically change the ways in which it provides care services across the County.

A PPF project framework is currently being developed and put in place. The role of Internal Audit will be to provide support and advice on an ongoing basis as well as seeking assurance on control issues associated with new ways of working. Internal Audit advice and support is currently provided through attendance at Project Management Team meetings.

Sourcing System (Adult Social Care)

The Sourcing System is an in-house system used by the Service Placement Team (SPT) to source care packages that are agreed as part of the funding approval process. At present it is only being used to source residential and nursing care services, although in the near future the system will be extended to cover domiciliary care.

The audit reviewed key controls within the system to ensure that:

- Access to the system was controlled and appropriate segregations of duties was evidenced;
- Amendments to standing data were carried out by properly authorised staff;
- Placement arrangements were timely and the most appropriate providers were selected;
- The negotiation of fee levels with individual care providers was open and followed agreed protocols.

Based on the audit work carried out, **substantial assurance** was given that the system is an effective means of supporting SPT in its role of sourcing approved care home placements. Two minor recommendations were made both of which were agreed with management.

Blue Badges (Adult Social Care)

The Blue Badge Scheme is a national scheme providing parking concessions for disabled people. There are around 30,000 badges currently in issue in East Sussex, which are issued either on an individual client basis or to an organisation, such as a care home. All badges are valid for a maximum of a three year period.

This review covered the accuracy and integrity of the systems that confirm applicants' eligibility for badges and their subsequent issue. Controls on the renewals process and the appeals process were also reviewed as was partnership working with Parking Enforcement Officers and other associated agencies to highlight and deal with the possible misuse of badges.

The Blue Badge Team had recently undergone a change of management and had begun its own review of processes and procedures. The audit provided **partial assurance** on the systems' controls and both confirmed and identified areas for improvement.

One of the key findings of the audit was that whilst the system for issuing permits was well established, inadequate measures have been taken to actively deter the fraudulent use of badges.

Additionally, the roles and responsibilities of the Blue Badge Team were not fully defined and the guidance that they were working to required updating.

A number of recommendations were included in the audit report to assist the Team's overall review process. All of the recommendations were agreed with management and supplemented the positive action taken by the Team to strengthen controls. A follow up review will be undertaken to ensure satisfactory implementation during 2009/10.

Conflict of Interest Investigation (Adult Social Care)

During the quarter 2, Internal Audit reported on the outcome of a recent investigation into alleged conflicts of interest involving a consultant working on a large departmental project.

Whilst the investigation did not find evidence to warrant further action, it has led to a review of the relevant contractual relationships by Adult Social Care.

Blue Badge Scheme Investigation (Adult Social Care)

Internal Audit received a report concerning the Blue Badge Scheme and specifically that a badge holder had made multiple applications and was holding more than one permit. Following contact with other authorities in whose area the blue badge holder had lived since 2002, records maintained confirmed that this person met the criteria for obtaining a Blue Badge and only one badge was ever in issue at any one time.

Direct Payments Scheme Investigation (Adult Social Care)

An allegation was received from a member of the public that a Direct Payments Scheme user was claiming wages for a carer no longer employed. Following an investigation involving a detailed analysis of claim forms submitted no evidence was found that supported the allegation received. Despite this, management have agreed to monitor closely future returns submitted by this Direct Payments service user.

Highways Maintenance – Contract Management (Transport and Environment)

The contract for highways maintenance is with May Gurney Integrated Services plc and forms the basis of the East Sussex Highways Partnership which is currently in its fourth year of a seven year arrangement. The budget for the contract with May Gurney for 2008/09 is £13.1m.

Highways maintenance includes:

- Planned maintenance (e.g. major resurfacing);
- Schemes (e.g. traffic calming, improvement schemes);
- Basic maintenance, including reactive (small works such as the correction of pot holes) and cyclical work (grass cutting, gulley emptying, etc);
- Structures (bridge repair maintenance etc) and traffic (road markings and signs).

This review focussed on the adequacy of risk management arrangements, the monitoring of May Gurney's performance, processes and procedures for ordering works and payments to the contractor and the financial monitoring of the contract.

As a result of the audit **partial assurance** was given that there is a sound system of controls in place. The main areas where the need for improvement was identified included:

- Introducing a formal risk management process;
- The further development and collation of key performance indicators;
- Improving the works ordering process and checking of works completed;
- Reviewing business continuity arrangements following the Departmental re-structure;
- Introduction of the new Highways software system, Exor.

In total 22 recommendations were made and with the exception of two, all were accepted by management and incorporated within a comprehensive action plan which will be followed up in 2009/10. The two recommendations not accepted were of a low risk nature with management considering these risks acceptable.

Waste Management Investigation 2003 Update (Transport and Environment)

In 2003, Internal Audit conducted an investigation into fraud and corruption within the Waste Management Group of Transport and Environment Department. This investigation led to the County Council pursuing both civil and criminal proceeding against the two individuals concerned. During the July 2008, the case was concluded with the two perpetrators both found guilty of conspiracy to defraud and corruption in Lewes Crown Court. Both received a 2 year suspended prison sentence which represents the conclusion of 5 years of activity by Internal Audit and Legal Services, in conjunction with Sussex Police.

Children's Centres - Programme and Project Management Review (Children's Services)

The County Council's overall programme for providing Children's Centres has been split into three phases and includes work ranging from brand new buildings to smaller adaptations or refurbishments. The overall plan is to have Children's Centre services available to every community in the County by 2010.

Internal audit conducted a high level review of the project management arrangements relating to the Phase 2 implementation. Phase 2 was £7.23m of capital grant to be spent in 2006/07 and 2007/08 and was for the provision of 19 Children's Centres by the 31st March 2008.

All nineteen Phase 2 Children's Centres had gained designation by the end of March 2008, meaning that the services had been planned, staffing identified and budget set aside for the delivery of service.

From the capital grant allocated, there was £560k unspent for schemes that had been subject to "slippage" during the period. The Department for Children, Schools and Families has been notified as required.

From the review work undertaken, project management arrangements were considered to be appropriate, although some recommendations were made to ensure that Phase 3 complies fully with the County Council's Project Management Toolkit. All recommendations were agreed with senior management with Children's Services.

Computer Misuse Investigations (Children's Services)

During quarter 2 internal audit conducted an investigation into the inappropriate, and potentially illegal, use of a school laptop computer by a member of the teaching staff. The investigation involved working with external agencies to conduct a forensic examination of the computer in question in order to ensure evidential integrity. The investigation found no evidence of illegal material on the computer with the initial concerns having been caused as a result of a computer virus.

Financial Management Standard in Schools (FMSiS)

Internal Audit has continued to carry out external assessments to ensure that schools are meeting the standards laid down by the Department for Children, Schools and Families (DCSF).

During the quarter external assessments were carried out at 20 primary and 2 special schools as part of the three year programme for all schools to achieve the standard by 31st March 2010.

It is pleasing to report that all 22 schools were found to comply with the Financial Management Standard. The schools will receive accreditation in due course from the DCSF, which will last for three years, when the process will need to be revisited.

67 primary schools are due to submit their self evaluation questionnaires for external assessment during 2008/09 and 48 (just over 70%), have submitted by the end of the quarter 2.

Since commencement of this initiative, external assessments have now been completed at 80 schools from the total of 192 and it is hoped that the target date of 2010 will be achieved. Although there is evidence that some schools, for a variety of reasons, are finding it difficult to meet submission deadlines, Internal Audit is continuing to work with Children's Services Finance to support them through the process.

The awareness training, provided jointly with Children's Services, for Governors and Bursars has continued during the quarter and is well attended by the schools.

Draft Reports

At the time of issuing this progress report, the following audit reports were in draft awaiting a response from client departments:

- Hastings and St Leonard's Excellence Cluster
- Imprest Account Review

Internal Audit Performance Indicators

| Performance Indicator | Target | Actual Performance | | | |
|--|-----------|--|---------|----------|----------|
| | | At 30/6 | At 30/9 | At 31/12 | At 31/03 |
| Economy & efficiency | | | | | |
| Planned days delivered (%) | 90 | 23.7% | 50.1% | | |
| Planned audits completed = final reports issued (%) ¹ | 90 | 20.1% | 36.3% | | |
| Actual v Plan time on completed audits (%) ² | 105 | 91.8% | 103.4% | | |
| Effectiveness | | | | | |
| External Audit reliance on internal audit | Achieved | Achieved – see PKF Annual Governance Report | | | |
| Maintain a CPA score of at least 3 / 4 for internal control. | 3/4 | Results of 2008 Use of Resources Assessment expected in Quarter 3. | | | |
| Recommendations accepted (%) | 90 | 95.0% | 96.9% | | |
| Customer feedback forms scoring 3 out of 5 or higher (%) | 80 | 87.4% | 91.1% | | |
| Reports to Chief Officers and Members | Quarterly | Quarterly reports issued. | | | |

¹ Excludes FMSiS Assessments

² Excludes FMSiS Assessments

Analysis of actual days delivered against the annual internal audit plan

| Service | Plan Days | Amend - ments | Revised Plan | Actual Q1 | Actual Q2 | Actual Q3 | Actual to date | % plan delivered |
|--------------------------------|-----------|---------------|--------------|-----------|-----------|-----------|----------------|------------------|
| East Sussex County Council: | | | | | | | | |
| Corporate Body | 561.0 | | 561.0 | 124.0 | 93.1 | | 217.1 | |
| Computer Audit | 165.0 | | 165.0 | 58.0 | 95.6 | | 153.6 | |
| Children's Services | 460.0 | 10.0 | 470.0 | 163.4 | 166.9 | | 330.4 | |
| Adult Social Care | 375.0 | | 375.0 | 99.1 | 107.5 | | 206.6 | |
| Transport & Environment | 240.0 | | 240.0 | 59.7 | 89.4 | | 149.1 | |
| Chief Executive's | 215.0 | -10.0 | 205.0 | 34.4 | 30.2 | | 64.5 | |
| Contingency ³ | 250.0 | | 250.0 | - | - | | - | |
| Sub total – internal customers | 2266.0 | 0.0 | 2266.0 | 538.6 | 582.7 | | 1121.3 | 49.5% |
| | | | | | | | | |
| External customers | 105.0 | | 105.0 | 24.0 | 41.8 | | 65.8 | |
| | | | | | | | | |
| Total audit days | 2371.0 | 0.0 | 2371.0 | 562.6 | 624.5 | | 1187.1 | 50.1% |

³ Contingency days delivered include completion of audits carried forward from 2007/08 and unplanned work e.g. investigations, and are included in the total for the department to which the work related.