



ESPO FINANCE SUBCOMMITTEE – 22 August 2012

AGENDA ITEM NO. 10

ANNUAL INTERNAL AUDIT PLAN 2012-13

REPORT OF THE CONSORTIUM TREASURER

Purpose of Report

1. The purpose of this report is to provide information on the work to update the Internal Audit Service Strategic Plan, which is then used as the basis for the Annual Internal Audit Plan 2012-13.

Background

2. ESPO's Consortium Agreement sets out the role of the Servicing Authority (Leicestershire County Council). This states that the Servicing Authority will provide ESPO with appropriate professional support services; this encompasses mainly payroll, internal audit, HR and legal services. The key documents which underpin the Consortium are currently under review and progress will be reported to Management Committee in autumn.
3. The County Council's Internal Audit Service (IAS) adheres to the CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006. Members should note that there is currently consultation on the IAS adopting combined UK Public Sector Internal Audit Standards from April 2013. A report to the Subcommittee will follow in due course.
4. Under the current Code of Practice, there is a requirement for the Head of Internal Audit (HIA) to give an opinion on the overall adequacy and effectiveness of the organisation's 'internal control environment'. To do this, internal audit coverage needs to be wider than the traditional audit of the financial systems. There is also a requirement that the Internal Audit Service prepares a risk based audit plan which takes account of the organisation's risk management process.

Role Finance and Audit Subcommittee

5. At the ESPO Management Committee meeting, on 2 March 2012 it was agreed that 'a Finance Subcommittee be established to work with the Director and Consortium Treasurer prior to consideration of the 2013/14 budget to consider how future budgets should be developed and presented'.

6. In developing draft terms of reference for the Subcommittee, it had become evident that there was merit in establishing its role as a standing Subcommittee. Members of the Finance Subcommittee, at its first meeting on 14 June 2012, agreed to recommend the Management Committee to establish the Subcommittee as such and agreed that the role of the Subcommittee should be widened to include both finance and audit functions.
7. Proposed terms of reference for the 'Finance and Audit Subcommittee' are included elsewhere on the agenda (marked item 5, report 'B'). Subject to the comments of members of this Subcommittee and final approval of the terms of reference by the Management Committee at its meeting on 27 September it is intended for the Finance and Audit Subcommittee to receive and note the annual internal audit plan, and to receive regular progress reports against the plan.

Planning Methodology

8. The methodology underpinning the audit planning strategy incorporates two main components. These are the 'audit universe' and the 'MILE' scoring system. A summary of the concept of the 'audit universe' and its subheadings is given in Appendix 1. This Appendix shows the potential types of loss that could arise over the various subheadings. The same methodology is used for all clients and Leicestershire County Council Internal Audit Plan
9. The second main component of the methodology is the scoring system, 'MILE'. MILE stands for materiality, impact, likelihood and exposure. Audit areas are risk assessed through an analysis of four factors; materiality, impact, likelihood and exposure (MILE). MILE scores are calculated by rating each of the 4 factors between 1 (low) and 5 (high). The formula $(M+E) * (I+L)$ is then used. The maximum score is 100. Materiality can be rated against financial value; number of service users and importance of the service to them; importance as a departmental or corporate objective. Impact can be rated against loss, financial, reputation or legal. Where a mix occurs, the highest score is chosen. Likelihood is an assessment of the inherent probability of this scale of loss occurring in the 4 year cycle. Exposure is a measure of the controls management has put in place to reduce this probability or insurance to compensate for loss. A low MILE score reflects information available that the risk is managed, containing good controls
10. Like all risk based scoring systems, it is not possible to be totally objective in allocating scores. Consultation with Senior Managers at ESPO and the Consortium Treasurer is an important feature in arriving at a score and more importantly a frequency of audit category.

11. The Internal Audit Service also undertakes work on behalf of External Auditor (PricewaterhouseCoopers) under the heading 'joint audit'. Joint audits reflect the external auditor's priorities. When drawing up the annual audit plan, an allowance will be made both for the time needed for the managed audit and for its impact on potential Internal Audit coverage.

Updating the Strategic Plan

12. The strategic plan is designed to cover a 4 year period from 2010 to 2014 and provides the basis for allocating days in the annual plans over this period. The aim is to link the allocation of audit resources to identified risk areas. The assessment allows for continual updating. 2012/13 is the third year in the current cycle.
13. A number of sources of information are used to undertake the review. Firstly, information derived from audits undertaken during the current year is assessed in relation to the 'exposure' score given. This is the case especially in relation to reports with high importance recommendations. Information from committee reports is used to inform, particularly on 'materiality' scores and developments planned. Finally, and most importantly, consultation takes place with senior management about emerging risks and planned changes.

Progress against the Audit Plan

14. It should be stressed that responsibility for the development and correct operation of internal controls rests with Senior Officers and operational managers. The Internal Auditor's task is to carry out an independent review, highlight weaknesses and make recommendations to improve controls where appropriate. The proposed audit scope is included in the annual audit plan but these are further discussed and agreed at the engagement stage of each audit
15. Internal audit reports are issued to Senior Officers and the Director on completion of the final audit report. A summary of all audit findings is currently reported to the Management Committee by the Interim Director, although the Finance and Audit Subcommittee is expected to become involved in this process; this will be for determination by the Management Committee. Although management have the responsibility for implementing the recommendations, Internal Audit Service will follow up all High Importance recommendations to ensure that they are actioned. A copy of those reports containing High Importance recommendations is also forwarded to the Consortium Treasurer.

Resources Implications

16. The budget for the provision of the Internal Audit Service is contained within ESPO budget under charges by the Servicing Authority.
17. Previously, the Plan provided around 100 days but coverage was raised during 2010-11 year to 140 days to incorporate areas arising from the business strategy review of ESPO. A comparison has been undertaken recently which indicated that the Internal Auditors for Yorkshire Purchasing Organisation (YPO) prepared a 200 day plan for YPO. Given all the transformational changes taking place at ESPO, the planned days for 2012/13 are now around 200 days which should enable the Head of Internal Audit to provide sound assurance to the Consortium Treasurer that risks are being managed.

Conclusion

18. The details of the 2012-13 internal audit plan, including a summary of the days allocated, is attached in the Appendix 2 to this report. The plan has been presented to the Interim Director (ESPO) and the Consortium Treasurer for comment.

Recommendation

19. Members are requested to:
 - a) Support the risk based methodology used as a basis for developing the internal audit planning strategy
 - b) Note the ESPO Internal Audit Service Plan for 2012-13.

Equal Opportunities Implications

20. At this stage there are no known direct implications resulting from the audit plan strategy, although both 'personnel' and 'potential liabilities' are subheadings

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Appendices

- Appendix 1 - Audit Universe Summary
- Appendix 2 - Internal Audit Plan 2012-13

