

AUDIT AND RISK COMMITTEE

24 September 2013

REVIEW OF INTERNAL AUDIT

Report of the Assistant Director (Finance)

STRATEGIC AIM	All
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1. PURPOSE OF THE REPORT

- 1.1 To brief the Committee on the outcome of the external review of Internal Audit (report number 142/2013) and some initial work undertaken into alternative potential options.

2. RECOMMENDATIONS

- 2.1 **That Committee notes the action plan and agrees to receive a report on progress at the next meeting.**
- 2.2 **That the Committee defers any consideration of alternative internal audit options pending the anticipated delivery of the Internal audit improvement plan but notes the issues raised in paragraph 3.8.**

3. BACKGROUND

The findings of the Independent Review

- 3.1 It was agreed that the Council would commission an independent review of the Internal Audit function (report 142/2013). The Welland Internal Audit Board commissioned RSM Tenon to undertake this review.
- 3.2 The full findings of the review are attached at Appendix A. The findings, although disappointing, are broadly as expected following the Head of Internal Audit's own self-assessment as reported in the Annual Report (139/2013).
- 3.3 The review acknowledges that improvements are required across a number of areas. In particular:

- Internal Audit needs to use risk based auditing and move away from using expected controls in order that the actual controls being operated are evaluated;
- Internal Audit needs to be clearer in their planning and reporting on what their opinions cover, including a better structure to the scope and limitations of the review.
- Internal Audit should look to proactively seek out every opportunity to add value by providing information on “good practice” operated across the Consortium’s client base or to undertake thematic reviews across the Councils.
- The Consortium should improve the transparency of reporting to the Internal Audit Board and Audit Committees with regards the time spent on each assignment and subsequent changes to internal audit plan. This will lead to more focus on outputs and outcomes instead of the current focus on internal audit resource input.

3.4 Since the report was issued, the Welland Internal Audit Board has held two meetings to discuss the findings with the Head of Internal Audit. The view of the Board is that it wishes to continue with the existing shared service model but that the Head of Internal Audit must deliver the required improvements. Should these improvements not be made, the Board will consider its options which include looking at different delivery models or reviewing the way in which the team is led and managed.

3.5 The Assistant Director has agreed with the Board to undertake a short follow up review in late 2013/14.

Potential future options

3.6 By way of background and further to comments made at the last Committee, the Assistant Director has undertaken some initial research into future options.

3.7 The potential service delivery options are:

1. Full outsource – the procurement of an internal audit service from an external provider;
2. Co-source – combination of an in-house team and one or more external providers;
3. Shared service (the current model) – internal audit delivered by an internal team, employed by one of the member organisations, and who work across member organisations; and
4. In-house provision – internal audit delivered by an internal team who are employees of the organisation.

3.8 Each model has different strengths and weaknesses but all are prevalent in the public sector and can work effectively. Moving to models 1 or 2 would require the following considerations:

- *Procurement/tendering* - any alternative provision would need to be tendered via OJEU or a Government framework based on the current annual cost. This would take up to 6 months to complete and require officer and Member time in drafting a specification, tendering and evaluating bids;
- *TUPE* - staff currently employed would TUPE transfer to a new provider. In the internal audit market where most prospective firms can normally deliver a service through their existing resources, the prospect of a TUPE transfer can make smaller contracts less appealing. The Assistant Director has spoken to a number of contacts who have confirmed this. The issue of TUPE can also serve to increase the overall costs as local authority staff tend to have better pension packages than staff in the private sector. Tenderers would normally seek to recover the additional pension costs through their fees;
- *Value for Money (VfM)* - how local authorities assess VfM of the internal audit service has been a long standing debate. Whilst all organisations understand how much they pay for internal audit, very few can quantify the value/benefit/outcomes they derive from high quality internal audit. Typically, local authority in-house and shared service team delivers lots of audit days at a low day rate (our rate is c£220-£230 giving a cost of approx £77,000) and measure value through customer feedback, completion of audit plans etc. Outsourced providers operate a different model: they charge a higher daily rate, deliver less days but charge a similar overall cost. The argument being that they have better quality staff, more specialists and are more productive. This is not always the case and one of the challenges the Council would face through any procurement is satisfying itself that it would get a better service through fewer audit days whilst paying a higher day rate.
- *Audit need* – in simple terms, the more complex, varied and specialist the audit need, the more difficult it is to deliver this need through a small in house team or shared service. Outsourced providers usually have access to a greater pool of technical resource. The Council's need is not dissimilar to other authorities and whilst specialist resource is needed from time to time, the core requirement is fairly basic.

3.9 In light of the above considerations, the officer recommendation is that the Council awaits a further report on Internal audit as set out in paragraph 3.5.

4. RISK MANAGEMENT

RISK	IMPACT	COMMENTS
Time	High	Action to address the issues must be taken immediately.
Viability	Medium	The Council should be able to deliver the expected improvements.
Finance	Low	There are no financial implications at present.
Profile	High	The profile of Internal audit is high following payroll overpayments
Equality and Diversity	Low	EIA screening produced a low result; therefore a full EIA was not required.

Background Papers: Nil

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