**REPORT TO A MEETING OF DUSTON PARISH COUNCIL TO BE HELD ON 26 JUNE 2018**

**AGENDA ITEM 13 – INTERNAL AUDIT REPORT 2017/18**

**1. PURPOSE OF THE REPORT**

To present the report of the Internal Auditor and to ask the Council to review the effectiveness of Internal Audit regime.

**2. BACKGROUND INFORMATION**

2.1The Parish Council currently uses Northamptonshire Association of Local Council’s (NALC) to undertake it’s Internal Audit and the findings of the Auditor are reported to Full Council each year. The Council recently agreed to continue the current arrangements but to expand the scope of the Internal Audit to ensure that the Council is provided with adequate reassurance as to the robustness of its internal controls.

2.2 It is important for the Council to recognise that internal audit’s function is to test and report to them on whether the Council’s system of financial control put in place by management is adequate and working satisfactorily.

2.3 It is not for the external auditor, nor is it a matter for internal audit, to actively seek evidence of fraud, corruption, error or mistake. Internal audit’s role is to assist the Council in fulfilling its responsibility to have and maintain proper internal control arrangements and those for the prevention and detection of fraud, error or mistakes

**3. SCOPE OF INTERNAL AUDIT PLAN PROPOSAL**

3.1 Accounts and Audit Regulations (SI 2006 No. 564), requires all Parish Councils to review the effectiveness of the system of internal audit at least annually. The following five standards need to be addressed in order for Internal Audit to be considered effective and should be clearly defined in the Internal Auditor’s engagement letter:

**3.1.1 Scope of Internal Audit**

What should be included in the audit plan, or, in other words, what is it that the Council wants the internal audit to do. It is recommended that the minimum requirements contained in “Governance and Accountability in Local Councils in England and Wales – A Practitioners Guide” (attached as Appendix A)are required of Duston’s internal audit*.* The Council may also wish to consider additional areas of work to be undertaken by the Internal Auditor as a one off or as a result of previously discovered system failures or discrepancies. Whatever the works required, or terms of reference, they should be approved by the Council and communicated to the auditor.

The work should take account of the risk management processes (e.g. the annual Financial Risk Assessment) and also the wider internal controls (the whole system of checks and controls, financial or otherwise, established by management in order to provide assurance regarding the achievement of the organisations objectives). Good examples of internal controls are robust and regularly review Financial Regulations, regular financial reporting to Council and Councillor conducted bank reconciliation.

**3.1.2 Independence**

The Internal Auditor should be allowed to have direct access to those charged with governance (i.e. the Council/Clerk/Responsible Financial Officer) where this is thought necessary by the auditor.

The Internal Auditor should have no other role within the Council and the Council should confirm this. This is not to say that he/she cannot be an employee of the Council. This may happen within larger local Councils and certainly does happen in principle authorities, but the Internal Auditor should have no role in the financial or decision-making processes.

The Internal Auditors report should be made in his/her own name and addressed to the Council. It is perfectly feasible to prepare the audit report on a “negative” basis, i.e. only those items which require amendment or improvement to be mentioned, but where the auditor finds that no matters have arisen from the audit which necessitates bringing to the attention of members, then the report should reflect this.

**3.1.3 Competence**

The Council must be satisfied that the Internal Auditor is competent to carry out the work. The Internal Auditor does not have to possess any qualifications but the following essential competencies to be sought should be:

* understanding of basic accounting processes;
* understanding of the role of internal audit in reviewing systems rather than undertaking detailed checks that are more appropriately the responsibility of management;
* awareness of risk management issues; and
* understanding of accounting requirements and the legal framework and powers of local councils.

**3.1.4 Relationships**

The Parish Clerk and Responsible Financial Officer (RFO) of the Council should be consulted on the content of the audit plan and all concerned should agree this beforehand. Responsibilities for officers and internal audit should be defined in relation to risk management, internal control and fraud and corruption matters. These will be clearly set out in such documents as job descriptions and the auditors’ engagement letter.

Council members should be clear on their own responsibilities for the “protection of the public purse” within the internal audit framework. The Council has a duty to consider the annual internal audit report and to demonstrate that consideration by inclusion in the minutes. Each item mentioned in the report should be fully addressed. There may be a need for Councillor training to ensure that all members fully understand this role and budget provision should be made where necessary.

**3.1.5 Audit Planning and Reporting**

The audit plan should properly take account of the corporate risk i.e. controls and procedures within the Council which minimise the risk of the body not being able to function or carry out what it sets out to do. The Council should approve the plan. Internal audit should report in writing in accordance with the plan.

A good internal audit will comprise 2 parts done at different times of the year. The interim audit is usually done part way through the year, and is an audit of the Councils processes and procedures.

The final audit is undertaken after completion of the year-end, so that balances within the accounts may be verified, the auditor will submit written reports to the Council after the interim and final audit.

The Internal Auditor is appointed by and reports to the Council not the Clerk/RFO. The auditor should have up-to-date and adequate professional indemnity insurance and provide or agree a letter of engagement with the Council.

3.2 In order to satisfy all of these requirements the Council approved an audit plan in accordance with the above mentioned “Governance and Accountability in Local Councils in England and Wales – A Practitioners Guide” and approved an Audit Engagement letter.

**4. REPORT OF THE INTERNAL AUDITOR**

The report of the Internal Auditor is attached to Appendix B and is self-explanatory. All points raised by the Auditor have either been addressed or are in the process of being addressed. In order to ensure full compliance and to ensure on-going robustness of the Audit, the Internal Auditor has been asked to return and conduct an intermediate audit later in the year.

**5. REVIEW OF INTERNAL AUDIT**

The Council has recently reviewed the scope and effectiveness of the Internal Audit and made significant changes and therefore it is recommended that the Council reapprove the current scope of Audit and confirm that it considers the new Audit requirements to be effective.

**6. RECOMMENDATIONS**

It is **RECOMMENDED** that:

1. The Council receive the report of the Internal Auditor
2. The Council agrees that the scope of Internal Audit remains appropriate and
3. The Council agrees that the Internal Audit regime is effective

Report by: Nina L Villa, Assistant Parish Clerk

**INTERNAL AUDIT PLAN SCHEDULE**

This Internal Audit Plan runs from 1st April to 31st March of each year. It actually covers three financial years – a review of the audit of the previous financial year, the audit of the current financial year and the appointment of the Internal Auditor for the new financial year that starts in April

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| JANUARY | 1. The Finance and General Purposes Committee Meeting:  * review the Councils system for internal financial control * review the audit plan for recommendation to Full Council * review Terms of Reference for the Internal Auditor for recommendation to Full Council  1. The Finance and General Purposes Committee to check that the Council has carried out a risk assessment in the last twelve months |
| FEBRUARY | 1. Full Council to approve the audit plan 2. Full Council to approve the Terms of Reference for the Internal Auditor 3. Full Council to approve the appointment of the Internal Auditor for the next 12 months commencing 1st April. |
| APRIL | **START OF THE NEW FINANCIAL YEAR** |
| MAY | 1. The Internal Auditor to receive the accounts for the last 12 months. 2. Full Council to receive a copy of the Annual Return to the External Auditor and approve it |
| JUNE | The Internal Auditor to meet with the Clerk and the Chairman of Finance and General Purposes Committee to note any issues raised by the Internal Auditor |
| JULY | 1. Full Council to review any issues raised by the Internal Auditor 2. Full Council to review if the Internal Audit has been carried out ethically and with integrity and objectivity 3. Full Council to receive a report from the Parish Clerk on the effectiveness of the Internal Audit 4. Full Council to note any issues that need to be addressed in the next audit cycle |
| OCTOBER | Council to receive a report from the External Auditor |

**Governance and Accountability for Local Councils - A Practitioners' Guide (England) March 2014**

**Appendix 9 – An approach to internal audit testing**

1. The Council will determine the scope and coverage of the work to be carried out by internal audit in accordance with proper practices guidance. Internal audit testing of internal controls will be sufficient for the proper completion of the annual internal audit report. The annual internal audit report should provide an adequate level of assurance for the Council to complete assertions 2 and 6 in its annual governance statement.
2. In completing the annual report at section 4 of the annual return *(see appendix B*), internal audit will have planned and carried out the work necessary to give the assurances called for. The ten key control tests in the annual report represent the minimum level of internal audit coverage required. Additional testing and reporting should be tailored to local circumstances.
3. Internal audit work always requires the application of judgement and should only be carried out following risk assessment. The scope and frequency of testing should reflect that assessment, and therefore should always be in proportion to the likelihood of fraud, error or misstatement that could occur. It should be directly related to the size and level of business activity of the council.
4. The following schedule suggests an approach to the testing of key internal controls to provide assurance that the minimum level of coverage has been met.

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| Internal Control | Suggested testing |
| Proper bookkeeping | * Is the cashbook maintained and up to date? * Is the cashbook arithmetic correct? * Is the cashbook regularly balanced? |
| 1. standing orders and financial   regulations adopted and applied; and   1. payments controls | * Has the council formally adopted standing orders and financial regulations? * Has a Responsible finance officer been appointed with specific duties? * Have items or services above the de minimus amount been competitively purchased? * Are payments in the cashbook supported by invoices, authorised and minuted? * Has VAT on payments been identified, recorded and reclaimed? * Is s137 expenditure separately recorded and within statutory limits? |
| Risk management arrangements | * Does a review of the minutes identify any unusual financial activity? * Do minutes record the Council carrying out an annual risk assessment? * Is insurance cover appropriate and adequate? * Are internal financial controls documented and regularly reviewed? |
| Budgetary Controls | * Has the Council prepared an annual budget in support of its precept? * Is actual expenditure against the budget regularly reported to the council? * Are there any significant unexplained variances from budget? |
| Income Controls | * Is income properly recorded and promptly banked? * Does the precept recorded agree to the Council Tax authority’s notification? * Are security controls over cash and near-cash adequate and effective? |
| Petty cash procedures | * Is all petty cash spent recorded and supported by VAT invoices/receipts? * Is petty cash expenditure reported to each Council meeting? * Is petty cash reimbursement carried out regularly? |
| Payroll Controls | * Do all employees have contracts of employment with clear terms and conditions? * Do salaries paid agree with those approved by the Council? * Are other payments to employees reasonable and approved by the council? * Have PAYE/NIC been properly operated by the council as an employer? |
| Assets controls | * Does the council maintain a register of all material assets owned or in its care? * Are the assets and Investments registers up to date? * Do asset insurance valuations agree with those in the asset register? |
| Bank Reconciliation | * Is there a bank reconciliation for each account? * Is a bank reconciliation carried out regularly and in a timely fashion? * Are there any unexplained balancing entries in any reconciliation? * Is the value of investments held summarised on the reconciliation? |
| Year-end procedures | * Are year-end accounts prepared on the correct accounting basis (Receipts and Payments or Income and Expenditure)? * Do accounts agree with the cashbook? * Is there an audit trail from underlying financial records to the accounts? * Where appropriate, have debtors and creditors been properly recorded? |