

Bath & North East Somerset Council		
MEETING:	Corporate Audit Committee	
MEETING DATE:	25th June 2013	AGENDA ITEM NUMBER
TITLE:	INTERNAL AUDIT – FUTURE SERVICE DELIVERY OPTIONS	EXECUTIVE FORWARD PLAN REFERENCE: E
AN OPEN PUBLIC ITEM		
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Appendix 1 – High Level Assessment Summary		

1 THE ISSUE

- 1.1 The Committee has previously received reports in 2010 and 2011 regarding a project to review future options for service delivery for Internal Audit.
- 1.2 This report sets out an updated position, including latest assessment of future options with recommendations and asks the committee to endorse these for consideration by the Cabinet.

2 RECOMMENDATION

- 2.1 The Corporate Audit Committee is asked to comment on the report and specifically the options for future service delivery.

3 FINANCIAL IMPLICATIONS

- 3.1 Financial implications, where they are known, are detailed within the report. Any of the options aside from the in-house one will require some form of one-off funding to implement. However, there are no current plans to make any further reductions to the Internal Audit budget for the period 2013/14 to 2015/16, following delivery of savings of over 25% of the Internal Audit budget in the previous two years.

4 THE REPORT

- 4.1 Appendix 1 details a high level summary of the options appraisal, whilst the remainder of the report provides fuller detail of the options assessment and recommendations.

1. Introduction & Background

- 1.1 Internal Audit is defined by the CIPFA Guideline as;

“.....an independent appraisal function established by the management of an organisation for the review of the internal control system as a service to the organisation. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources”.

- 1.2 Auditors in the public sector have a pivotal role to play in ensuring that public funds are administered properly, economically, efficiently and effectively, in the interests of the public and there is an expectation by the community that audit is protecting the public purse.

- 1.3 In Local Government, an internal audit service is a mandatory requirement; and all principal authorities in England and Wales are required by statute (under the Accounts and Audit Regulations and section 151 of the Local Government Act 1972), to have an adequate and effective internal audit function.

- 1.4 Since the last round of local government reorganisation in 1996, the Bath & North East Somerset Council Internal Audit has been delivered by an in-house team. The team currently stands at 9.5 FTE having been reduced from a staffing number of 15 in 1996.

In addition the team also carries out Internal Audit provision for the Avon Pension Fund, all Local Authority controlled Schools (including the responsible officer role for a number of Academy Schools) and works with counter fraud services in the NHS.

- 1.5 In terms of benchmarking, the service has for the last ten years, participated in a national exercise co-ordinated by CIPFA (IPF).

In summary, in terms of cost, the team has consistently demonstrated a cost per day at approximately the median to 5% lower than the Unitary average and in relation to quality, productivity and coverage it is at average levels.

- 1.6 The budget for the service in 2013/14 is £381K, including a number of recharges historically built into the budget since 1996 and is part of the Risk & Assurance service, which is one of the service blocks for the whole of Resources and Support Services.

- 1.7 Some of the key issues affecting medium term future service delivery include:

- a) The continued ability to provide 'reasonable assurance' over the whole of the Internal Control framework with a small in-house service in light of previous budget reductions and the continuing very tough financial outlook increasing risks more broadly;
 - b) Maintaining sufficient skills mix, capacity and resilience in light of unplanned major Investigations, cross-sector requests (i.e. NHS), system implementation or change projects and any sickness;
 - c) Meeting new IIA/CIPFA professional Internal Audit standards from April 2013, notably those involving organisational independence, reporting lines and status;
 - d) Delivering satisfactory productivity and coverage of key risks within the organisation which is currently at average levels with limited ability to innovate;
 - e) Dealing with skills gaps which are evidenced, primarily in IT, Major Projects and Procurement audit;
 - f) Assessing and understanding the risks emanating from the impacts of on-going government initiatives, notably in Health, Welfare, Education and Regeneration;
 - g) Maintaining an overview and understanding of the changes in complexity of Service Delivery across the Council, especially where there is a mixed economy of provision and heavy reliance on complex IT systems as part of the internal control framework.
- 1.8 The medium term plan for Resources & Support Services portfolio was set out at the end of 2012 prioritising its services as those which enabled the Council as a whole to achieve excellence and support the 'one-council' approach. It also specifically mentioned that it would aim to provide excellent, low cost and integrated support services for the Council as a whole and for other partners as appropriate.
- 1.9 As part of delivering these outcomes in the medium to long-term, Resources & Support Services has been assessing solutions to models for service delivery and the outcomes of this work supported the recommendations from the initial project in 2010/11 to move to a partnership model, i.e. sharing services with other local authorities.
- 1.10 It is however prudent to refresh the assessments previously undertaken in light of the many changes affecting the local government sector and the rest of the report focuses on these and the recommended way forward.

2. Original Objectives

2.1 To review a range of options for the delivery of Internal Audit services in the medium to long-term and recommend an option for implementation

2.2 Original Options Assessed (and now refreshed):

- In-House Model
- Outsourced Model
- Co-Sourced Model
- Partnership Model

2.3 Scope:

To cover the whole range of Internal Audit Services for the Council:

- Risk Based Planning
- Core Systems/Risk Based Audit
- Grant Return Audit
- Responsible Officer roles for Schools
- Specialist Audit, i.e. Pensions, IT or Procurement Audit
- Fraud & Investigation Reviews
- Policy & Procedural Guidance
- Joint working with External Auditor & Inspectorates
- Joint working on Annual Governance Review
- Joint working with NHS Internal Audit & Counter-Fraud Services
- Joint working with Audit teams within the South West region
- Reporting to Corporate Audit Committee

3. Original Approach

3.1 A project team was formed and an external Project Manager appointed to manage the process and provide specific independent challenge. The same Project Manager was used to help refresh the assessments of the options detailed below.

3.2 The key stage of options appraisal was based around assessing each of the models against the following key headings (see Appendix 1).

- A) Standards & Quality
- B) Systems, Staff & Management
- C) Costs & VFM
- D) Organisational Fit

4. Summary of Options Appraisal

The scores were originally assessed through a mix of objective and subjective data collected through the different phases of the project including interviews with providers, clients and customers. These were then independently challenged by the Project Manager.

All of these scores were then reviewed and refreshed in the last 3 months based on latest comments from clients and providers and a further two years learning since the original project was completed.

The sections below provide more detail of the alternative options to an in-house model and high level scoring is detailed in Appendix 1.

4.1 Partnership Model

4.1.1 This model scored the highest and was assessed as being the most flexible and sustainable form of service delivery in the long-term.

4.1.2 Key Issues:

- There are a number of options for delivery through this model. These include the South West Audit Partnership, Devon Audit Partnership or creation of a new partnership.
- The Devon Partnership has been established for almost 5 years providing audit services to a number of partners across Devon, including 1 County Council, 2 Unitary Councils, a number of district councils and the Devon & Cornwall Fire Service;
- Devon Partnership is particularly strong in IT Audit, a current recognised weakness of the existing in-house service and has a strong Unitary ethos within its methodology and approach;
- The Devon Partnership is also actively looking to expand, change its name and consider alternatives to its current arrangements;
- The South West Audit partnership (SWAP) was originally hosted from South Somerset District Council in the same way as the Devon model but has now formed into a Limited Company from April 2013;
- It has over 15 partners including 2 Counties (Somerset and Dorset) and a number of District Councils from the Forest of Dean all the way down to Weymouth and Portland. It has however only one Unitary Authority (Wiltshire) which it recently took over responsibility and its ethos emanates from its origins around District Councils;

- Whilst it's not actively looking for partners it will consider additional partners, especially Unitary Authority's. The partnership is now the largest in the South West for Local government and has an extensive set of governance and legal arrangements in place;
- Geographically the partnership is spread over a vast distance so organisationally existing teams primarily stay serving their original authority with some minimal flexibility outside of this, in terms of working for different partners;
- Its key advantage is that it is already in existence and delivering audit services and therefore set-up and implementation is a smoother process and relatively straightforward;
- However its recent move to Ltd Company status will need to be checked to ensure there are no new barriers to joining as entry to a local government partnership model is exempt from any external procurement process, which is a key advantage;
- Providing Internal Audit through an independent Partnership also strengthens both its profile and independence and enables a pooling of skills and resources which cannot be achieved when delivering services to only one organisation;
- Integrating resources through partnership strengthens standards and improves opportunities for staff and career development and ultimately provides greater resilience for the future.

4.2 Co-Sourcing & Outsourcing

4.2.1 Co-Sourcing is effectively downsizing the team by approximately 10% to 50% and then letting out that part of the audit service to external providers, i.e. IT Audit or Core Systems Audit. Outsourcing is transferring the whole function to an external provider.

Key issues:

- In theory both these models should work well, with the ability to replace skills gaps and invest in areas of highest risk;
- Key advantages are an ability to flex costs, seek private sector expertise and enable standards to rise, however both models are relatively rare in the local government market;
- Research identified that the co-sourced model had been generally inconsistent and sometimes ineffective in relatively small audit functions with occasional poor standards, inconsistent management and effectively two different sets of methodologies being employed;

- It would also involve cost and use of management capacity in preparing for, specifying and then letting a contract as well as then having to establish separate client management arrangement to run alongside the in-house service;
- Significantly compulsory redundancies would be required to further reduce the audit function to create the resource to externalise. This reduction would be both costly (and unaffordable) and therefore it was considered costs would significantly outweigh benefits;
- In terms of full outsourcing the market told us their preference would be to use their own resources and not TUPE existing staff into their own organisation and that the relative size of our service was not therefore attractive enough to make it a viable proposition. This would therefore need to be factored into any bids;
- There was therefore unlikely to be any cost advantages based on the current cost of the in-house service, a severe loss of organisational knowledge, little in the way of any track record of positive service delivery and an uncertain future for staff transferred. Indeed there was no history of a sustainable and quality service being delivered by an external firm for a Unitary Authority in the region;
- Implementation, including downsizing the existing resource would take at least six to twelve months and involve a significant amount of management capacity and the value of either exercise was not considered beneficial;

4.3 Recommendations:

A) To endorse in principle the partnership model of service delivery as the appropriate way forward for the Internal Audit Service in the medium to long-term;

B) To recommend the Council enter into a period of due diligence to assess whether a partnership model can be implemented within existing budgets and by or within the 2014/15 financial year subject to the appropriate financial and legal checks and controls;

C) That the Divisional Director reports back to the Audit Committee with regular updates on progress to ensure it is kept up-to-date and comment on any parts of any implementation process as appropriate.

5 RISK MANAGEMENT

- 5.1 A proportionate risk assessment has been carried out in relation to the Councils risk management guidance and the risks to the choice of each option have been laid out in the report above.

6. EQUALITIES

- 6.1 A proportionate equalities impact assessment has been carried out using corporate guidelines, no significant issues to report.

7 CONSULTATION

- 7.1 Consultation has been carried out with the Cabinet Member for Resources, Strategic Director for Resources and Section 151 Finance Officer.

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Background papers	Feb 2011 Audit Committee – Internal Audit Options for Future Service Delivery
Please contact the report author if you need to access this report in an alternative format	

Appendix 1 – High Level Assessment

Overall Summary of Options			In House	Partnership Model	Co-Sourced	Fully Outsourced
Standards & Quality	SCORE	30%	55%	85%	80%	90%
Audit Methodology						
Quality Control						
Innovation						
Access to specialist skills						
Systems, Staff & Management	SCORE	20%	60%	80%	80%	73%
Investment in People & Operational Flexibility						
Use of audit automation/software						
Management & Leadership						
Costs & VFM	SCORE	20%	75%	67%	47%	47%
Readiness & Procurement Costs						
Implementation Costs						
Cost of Delivery/Future Flexibility						
Organisational Fit	SCORE	30%	85%	65%	50%	45%
Strategic fit to Target Operating Model						
Track Record in delivery to Unitary Councils						
Organisational/Local Knowledge						
Influence & Control						
SCORING	TOTAL SCORE	100%	70%	75%	65%	65%
RANKING			2	1	3=	3=