

**REPORT RE FIRST YEAR OF PARTNERSHIP AGREEMENT WITH KPMG AND PROPOSALS FOR THE SECOND YEAR**

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**1. SUMMARY**

This report details the progress of the internal audit partnering agreement in its first year of operation and explains KPMG's proposals for the forthcoming year.

**2. RECOMMENDATIONS**

- 2.1 That this committee notes the progress of the agreement in its first year and approves the proposals for the forthcoming year.
- 2.2 The committee notes the opinion of Audit Scotland in relation to the reporting lines of internal audit.

**3. DETAILS**

- 3.1 Following a review of the internal audit function at all Scottish Local Authorities performed by Audit Scotland and a consequent review of the internal audit provision at Argyll and Bute Council by Professor Arthur Midwinter of the University of Strathclyde, the Council entered into a partnership agreement with the accounting and advisory firm KPMG.
- 3.2 The objective of the partnering arrangement is to develop the internal audit function at the Council to a position where:
  - It services the Council's internal audit requirements in accordance with good practice; and
  - In any follow-up review of internal audit functions at Scottish Local Authorities by Audit Scotland, that of Argyll and Bute will be classed as amongst the best.
- 3.3 A plan for the first year of the contract was divided into the following activities:
  - Conducting a Risk Assessment as a basis for the development of an internal audit strategic plan;
  - Management and professional support;
  - Formal and informal training;
  - Information Technology audit;
  - Audit Committee attendance; and
  - Meetings/relationship management and audit functioning
- 3.4 The following actions have been delivered during the first year of the contract:
  - A three-year risk based strategic plan was produced, following extensive

consultation throughout the Council, from which was drawn a work programme for the year 2002/2003.

- The arrangements for the provision of internal audit services at Argyll and Bute Council were examined and recommendations made surrounding the positioning, relationships and processes of the internal audit function. These recommendations were implemented by the Head of internal Audit.
- A training needs assessment was compiled to identify training requirements. One full days training on governance and risk management, strategic and assignment planning, assignment fieldwork and computer audit issues was delivered to staff at KPMG's Glasgow office. Two half-day training sessions were held at Kilmory covering governance, risk management, internal control, value for money (vfm) and Best Value.
- A review of the Council's IT environment was completed using KPMG specialist IT auditors.
- All meetings of the Audit Committee were attended by at least one member of the KPMG team.
- Ad-hoc advice to the Head of Internal Audit and the Director of Finance concerning issues as they arose. For example, the position of internal audit in the newly structured council, and Statements of Internal Financial Control.
- KPMG and the Head of Internal Audit undertook a "self-assessment" review of the compliance of the Argyll and Bute Council audit team with good practice, and in particular, the guidelines likely to be used by Audit Scotland in any follow-up review. They concluded that improvement could be demonstrated against most of the criteria used. KPMG have since conducted in depth reviews against particular areas of guidance, making recommendations designed to ensure that such improvement is both demonstrable and auditable.

Overall, KPMG are pleased with the progress being made towards the achievement of the objectives outlined at paragraph 3.2.

3.5 During the course of this first year the manager responsible for servicing the agreement at KPMG decided to change his career direction within the firm. He was replaced by a manager who was previously a Chief Internal Auditor at a Scottish Local Authority.

3.6 KPMG propose the following activities for the second year of the agreement:

- Management and professional support (development of the role of the internal audit function in relation to Best Value and Statements of Internal Control/Compliance with a local code of Corporate Governance);
- Formal and informal training (both to the Audit Committee regarding their role and to the audit team on systems auditing particularly in relation to IT);
- Direct audit time (allocated to a vfm study of education transport);
- Audit Committee attendance;
- Meetings/relationship management and audit functioning (in particular continuing reviews of compliance with good practice and guidance – it is proposed to produce a consolidated report covering all reviews in the

- Autumn of 2003); and
- Assistance with a review of risk for the development of a revised strategic plan.

3.7 In relation to the review of compliance with good practice and guidelines, KPMG have contacted the Controller of Audit for his opinion on the position of internal audit within the Authority. His and our view is that the Head of Internal Audit should report directly to a first tier officer (Chief Executive or departmental director) such as the S.95 officer who, in terms of CIPFA guidance, is a full member of the senior management team. If the S.95 officer is not a senior officer but reports via the Chief Executive the controller of audit would have some concerns that the Chief Executive would have direct responsibility for all the financial and operational activities of the council so it would be important for the audit committee to address the risks of this arrangement and for the Head of Internal Audit to be able to directly access the audit committee. Any other arrangement could impact on a “5 star” grading being achieved against one of the criteria likely to be used by Audit Scotland in their follow-up review of internal audit sections. The Audit Committee, other elected members and senior management should bear this in mind when deciding or approving the reporting lines of internal audit in any Council re-structure.

## **5. IMPLICATIONS**

5.1	Policy:	None
5.2	Financial:	None
5.3	Personnel:	None
5.4	Legal:	None
5.5	Equal Opportunities:	None

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