
Report to Scrutiny Committee

Date of Meeting: 1 December 2011

Subject: Internal Audit Options Appraisal - Phase 2

Report by: Revenues and Payments Manager

1.0 Purpose

- 1.1. This report presents the second phase of the Options Appraisal on the Reconfiguration of the Internal Audit Service to members.

2.0 Recommendations

- 2.1. Members are asked to
- note the report and discuss where appropriate
 - indicate their preferred option, which will be included in a report to Council on 15 December 2011.

3.0 Considerations

Engagement with Scrutiny Committee Members

- 3.1. At the Scrutiny Committee meeting on 24 February 2011, the Revenues and Payments Manager made a presentation to members on the current progress of the 2010/11 Internal Audit Plan, together with presenting options on the plan of work between April and September 2011.
- 3.2. As part of this presentation, the Revenues and Payments Manager intimated her intention to undertake a formal Options Appraisal on the Internal Audit Service and asked Members to comment. This was formally agreed the Revenues and Payments Manager agreed to bring the updated options appraisal back before the Summer Recess.
- 3.3. The Internal Audit Options Appraisal was formally presented to Members at the Scrutiny Committee Focus Group meeting on 19 May 2011 where seven different options were considered. Detailed discussion took place between members, the Revenues and Payments Manager and the Director of Finance on the seven options. Members selected three options and requested that these be investigated in more detail.

- 3.4. These three options were
1. Integrated Inhouse Audit and Fraud Team
 2. Shared Service with another organisation(s)
 3. Contract Out full service provision
- 3.5. The Director of Finance provided a verbal update on the progress of the Appraisal at the reconvened September 2011 Scrutiny Committee Focus Group meeting and confirmed that the preferred option for delivery of the audit service would be presented at the December 2011 Scrutiny Committee meeting.
- 3.6. The attached Internal Audit Options Appraisal lays out the three options considered in more detail. For each option the costs, governance arrangements, service delivery, risks and timetable have been considered.

Outcome of Appraisal

- 3.7. The preferred option is Option 1, an integrated audit and fraud service. The appraisal demonstrates that this model will provide the quality internal audit service required by the Council. It offers value for money, which is evidenced by a daily audit rate of £229 in year one, rising to an average of £236 over three years, against a market rates of £400 - £500 per day. It will also provide a professional service, and this new service will be operational in quarter 1 of 2012-13. This option will also clearly demonstrate the independence of the service, particularly in respect of service leadership and this option also addresses the historical capacity issues, raised by external audit.
- 3.8. Members will note from the appraisal that the shared service option provides a daily cost of £238 per day, which is £9 higher, however the earliest that the service could be operational would be September 2012. There is also a risk of unanticipated costs occurring which could reduce the possible savings. There is an additional risk that unanticipated delays in identifying a partner and agreeing the infrastructure arrangements for a shared service, would further delay the start of an operational audit service. It is considered that these risks outweigh the immaterial difference of £9 per day in value for money between the two options.
- 3.9. The saving of £189,391 that is generated by the integrated audit and fraud service recognises the benefits and efficiencies on the combined operating activities of both the audit and fraud services.

Next Steps

- 3.10. An indicative timetable for implementation of each of the options is provided within the appraisal. If option one is selected as the preferred option, the audit service could be operational by the start of April 2012. The Revenues and Payments service reconfiguration is currently ongoing and the restructure of the audit service would dovetail into this.
- 3.11. If option one is not selected as the preferred option, the date that the audit service could be in place and operational varies from April 2012 to January 2013, for the other models.

Conclusion

- 3.12. The options appraisal demonstrates that the preferred mode for delivery of the audit service is an integrated audit and fraud team. This model will provide the quality internal audit service required by the Council, offers value for money, and will clearly demonstrate the independence of the service.
- 3.13. Members are asked to indicate their preferred option, which will be reported to Council on 15 December for approval.

4.0 Sustainability Implications

- 4.1. The Options Appraisal lays out the recommendation for the provision of a sustainable effective internal audit service.

5.0 Resource Implications

5.1. Financial Details

- 5.2. The full financial implications of the recommendations are set out in the report. This includes a reference to full life cycle costs where appropriate. Yes ☒

- 5.3. Finance have been consulted and have agreed the financial implications as set out in the report. Yes ☒

5.4. Staffing

6.0 Exempt Reports

- 6.1. Is this report exempt? Yes ☐ (please detail the reasons for exemption below) No ☒

7.0 Declarations

The recommendations contained within this report support or implement our Corporate Priorities and Council Policies.

- (1) **Our Priorities 2008 - 2011** (Please double click on the check box ☒)

- | | |
|--|-------------------------------------|
| The area has a positive image and attracts people and businesses | <input type="checkbox"/> |
| Our communities are more cohesive and inclusive | <input type="checkbox"/> |
| People are better skilled, trained and ready for learning and employment | <input type="checkbox"/> |
| Our communities are safer | <input type="checkbox"/> |
| Vulnerable people and families are supported | <input type="checkbox"/> |
| Substance misuse and its effects are reduced | <input type="checkbox"/> |
| Health is improving and health inequalities are reducing | <input type="checkbox"/> |
| The environment is protected and enhanced for all | <input type="checkbox"/> |
| The Council is effective, efficient and recognised for excellence | <input checked="" type="checkbox"/> |

(2) Council Policies (Please detail)

None

8.0 Equalities Impact

8.1 Have you undertaken the required equalities impact assessment to ensure that no groups are adversely affected by the recommendations?

Yes ☐ No ☒

9.0 Legality

9.1 It has been confirmed that in adopting the recommendations contained in this report, the Council is acting within its legal powers. Yes ☒

10.0 Appendices

10.1 Please list any appendices attached to this report. If there are no appendices, please state "none".

Appendix A - Options Appraisal on the Delivery of the Internal Audit Service.

11.0 Background Papers



11.1 Have you used other documents to compile your report? (All documents must be kept available by the author for public inspection for four years from the date of meeting at which the report is considered)

Yes ☐ (please list the documents below) No ☒

Author(s)

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Approved by

NAME	DESIGNATION	SIGNATURE
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**Clackmannanshire
Council**

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Phase 2

Detailed Options Appraisal on Provision of Internal Audit Service

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

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INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

1. EXECUTIVE SUMMARY

Introduction

This paper sets out the second phase of the options appraisal for the reconfiguration of the Internal Audit service.

In February 2011, Scrutiny Committee agreed to the undertaking of an options appraisal for the delivery of the audit service. In May 2011, the Internal Audit Options Appraisal Report was presented to the Scrutiny Committee Focus Group. In this appraisal, seven different models were considered and Scrutiny Committee agreed that three models should be worked up in more detail and brought back to them.

This second paper sets out those three models in more detail.

Options Appraisal

The three options that Scrutiny Committee requested be investigated in more detail included:-

1. Integrated Inhouse Audit and Fraud Team
2. Shared Service with another organisation(s)
3. Contract Out full service provision

Each option has been considered in more detail in Section 2 of this report with the costs, governance arrangements, risks and implementation timetable defined. A comparison of all the options has been undertaken in Section 3, where different measures have been provided which have helped identify the preferred option.

Preferred Option

The preferred option for the delivery of the internal audit service is option 1; an integrated in-house audit and fraud team. This service would provide 600 audit days and between 250 to 300 fraud days per annum. The cost of the service is £210,066 in year 1 with £137,950 attributable to audit and £72,476 attributable to fraud. This option would allow the Council to demonstrate value for money and provide a professional quality audit service. It would also deliver a saving over three years of £189,391. Finally, the service could be reconfigured and in place for the start of the new financial year 2012-13.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

2. DETAILED OPTIONS APPRAISAL

Scrutiny Committee selected the following three options to be investigated in more detail:-

1. Integrated Inhouse Audit and Fraud Team
2. Shared Service with another organisation(s)
3. Contract Out full service provision

In assessing each option in more detail, the following has been included

- governance arrangements
- detailed costings
- risks
- steps and timescales to implement

Each of the options appraises a different model for delivery of a professional, independent and sustainable internal audit service. Once the preferred option is approved and embedded, the audit service will provide Council and Scrutiny Committee with the necessary assurance. It will also support the governance framework and address the recommendations raised by External Audit.

Description of Service

At a strategic level, the remodelled audit service would comply with CIPFA's Code of Practice for Internal Audit in Local Authority. It would also support the annual assurance requirements within the Governance Strategy and Annual Governance Statement.

Operationally, an Annual Plan would be prepared in advance of the financial year which quantified the resource allocation for audits work (planned, reactive and follow up). This would be reviewed annually and would continue to be presented to Scrutiny Committee for approval.

The Audit Plan would be risk based focussing on both the strategic and key operational risks for the Council and would define the nature, scope and indicative number of days of each audit.

The individual/organisation leading the service would oversee the audit provision and be responsible for :-

- the delivery of the annual audit assurance statement
- supporting the corporate governance arrangements jointly with the Governance Manager through the Governance Improvement Plan.

The audit team would be comprised of qualified Internal Audit professionals and ongoing professional development would be embedded within the service.

The Audit Plan, undertaken by the audit team would provide approximately 600 audit days per annum, which would give an average of 14 audits per year, in addition to follow ups and other audit work.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

Costs for the Service

The implementation costs for each model assume that all existing staff are either redeployed or matched into new posts within the Audit service or in the Revenues and Payments service costs. This is reflected as "one off costs of implementation".

Timetable for Implementation

Once Scrutiny Committee has selected the preferred option, the new service model will be implemented. This will take place during 2012 and actual date of implementation will be dependant on the model selected. An indicative timetable for each option is provided. Depending on which option is selected, Council approval may be required prior to the advertising and recruitment of posts.

It is expected that once the service is operating effectively, it will transfer from the Revenues and Payments service into the Governance service. This would ensure the independence of the team is maintained and address external audit recommendations on this issue. It will also further support the Council's governance framework.

Audit Provision Required

An assessment has been undertaken to determine the level of audit service required by the Council. This assessment is also normally undertaken by the Audit Manager on an annual basis, as part of the planning and preparation of the Audit Plan and would consider:-

- the size and nature of the organisation
- the environment that the organisation is operating within
- the financial, strategic and operational risks facing the organisation
- opinions and feedback by regulators or other assurance providers

From the review of the required level of audit service, it is estimated that Clackmannanshire Council requires 600 audit days per annum. This is a consistent service provision with other similar sized Local Authorities. It is on this basis that each of the three options have been prepared.

Based on a requirement of 600 audit days, an indicative audit plan would include the following:-

	Days
• Audits 14 x 30 days	420
• Annual Governance Statement	50
• Value for Money/Policy Review	40
• Follow Up	40
• Reactive/Project Work	<u>50</u>
	600

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

2.1 EXISTING STRUCTURE

There have been capacity issues within the service for a number of years. This has resulted in a variable audit service and inconsistent delivery of the Annual Plan. An Annual Plan was approved by Scrutiny Committee for 2010-11 and audits which have not yet been completed from this plan have been rolled forward into 2011-12. In consultation with Scrutiny Committee, a separate Annual Plan was not completed for 2011-12 and it was proposed that an options appraisal of the service be undertaken.

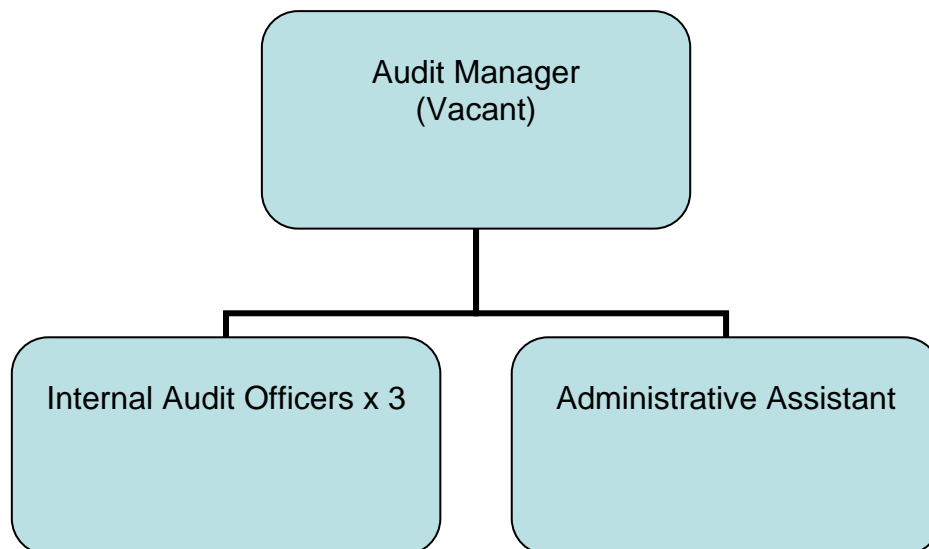
With the ongoing service restructuring, the Audit Manager post is currently vacant and the Revenues and Payments Manager is overseeing the completion of audits. Audits are being completed by the Internal Audit Officers. Each officer has an individual plan which is pulled from the Annual Plan. This should average 6 audits per year, per Auditor. The Administrative Assistant also supports the Officers in the audit and also undertakes administrative audit functions such as the quarterly Follow Ups.

Quarterly reports are presented to the Scrutiny Committee during the year on the progress of the Annual Plan and the follow up of previous recommendations.

Improvements have been made within the service but are not sufficient to deliver a sustainable service for the future.. Undertaking the options appraisal will allow a sustainable professional service to be delivered.

Description and Structure of Service

The existing Internal Audit Structure is as follows:-



INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

Costs of Service

The current budget for the service is:-

				£
	Grade	Salary	Emp'ler Costs	Total
Audit Manager (Vacant)	11	45,628	13,506	59,133
Internal Audit Officer	6	25,884	7,662	33,546
Internal Audit Officer	6	25,884	7,662	33,546
Internal Audit Officer	6	25,884	7,662	33,546
Administrative Assistant	3	14,299	4,233	18,532
		137,579	40,723	178,303
Supplies and IT Costs				3,090
Total				181,393

Costs will rise year on year for the next three years to £186,470 in 2014-15 through increasing increments on salary costs.

Governance, Accountability and Reporting Arrangements

The Revenues and Payments Manager oversees the Internal Audit Service on an interim basis and is responsible for the delivery of the Annual Plan. It is recognised that this could affect the independence of the audit team and has also been highlighted as a risk by External Audit.

Performance of the Service

Historically, completion of the Annual Plan was poor with between 50 - 60% of the plan being completed and work regularly being rolled forward. In 2009/10, 100% of the Audit Plan was completed, however progress has regressed in 2010/11 with only 50% of the Plan being started by March 2011.

At end of March 2011, 429 chargeable days had been spent on audit work of which 281 days related to the audit work for 2010/11. Of this 281 days, only 224 delivered work within the budget and timescales defined in the Annual Plan. In addition the work delivered by the members of the internal audit team equates to an average actual daily rate of £810, while current market daily rates are between £400 to £500 per day.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

2.2 OPTION 1 - INTEGRATED IN-HOUSE AUDIT AND FRAUD TEAM

Description of Service

The integrated in-house fraud and audit service would comprise one team providing both the Council's internal audit and corporate and benefit fraud arrangements. An Annual Fraud Plan would be incorporated into the Annual Internal Audit Plan presented to Scrutiny Committee which reflects benefit and fraud investigation work.

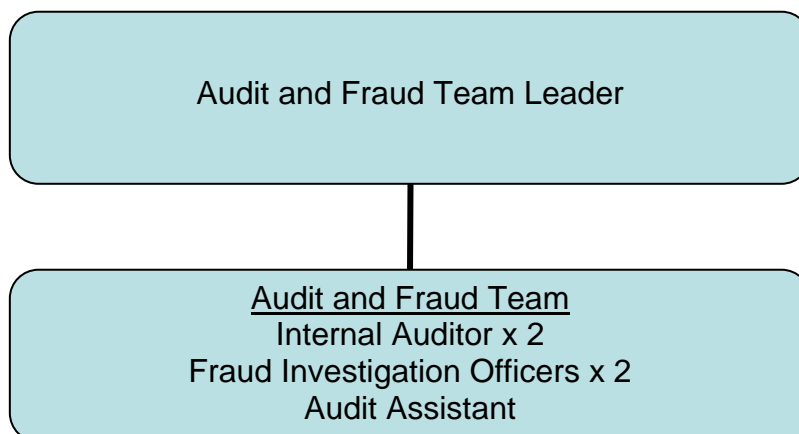
The Fraud Plan would also be risk based and would include corporate and benefit fraud. The Fraud Plan would include corporate fraud policies and arrangements, fraud awareness and training, data matching and fraud detection and investigation. It is estimated that the Council requires 250 - 300 fraud investigation days per annum.

Structure of Service

In addition to the audit responsibilities, the Audit and Fraud Team Leader would be responsible for :-

- meeting the Council's statutory responsibility to investigate benefit fraud and recover amounts on behalf of DWP,
- preparing and implementing the corporate fraud prevention policy,

The structure of the service would be as follows:-



INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

Cost of the Service

The cost of this service in year 1 would be as follows:-

Option 1 - Integrated Fraud and Audit Team				
	Grade	Salary	Emp'ler Costs	Total
Audit and Fraud Team Leader	10	39,317	11,638	50,955
Senior Fraud/Auditor	9	34,386	10,178	44,564
Fraud/Auditor	8	30,078	8,903	38,981
Audit/Fraud Officer	6	24,411	7,226	31,636
Audit/Fraud Officer	6	22,993	6,806	29,800
Total Salaries		151,185	44,751	195,936
Supplies and IT Costs				14,130
Total Annual Cost				210,066
One off Implementation Costs				
Redeployment Costs				12,874
Advertising of posts				3,000
				15,874
Total Cost in Year 1				225,940

The annualised service costs would rise year on year for the next three years to £222,040 in 2014-15 through increasing increments on salary costs.

Timetable for Implementation

Corporate restructuring is currently ongoing and this is progressing within the Support Services. The restructure of the internal audit service would dovetail into the Revenues and Payments restructure which is currently under consultation with the Unions.

The key milestones in the restructure would be as follows:-

Milestone	Date
Consult with Staff and Unions	Ongoing
Complete Staff Consultation	November 2011
Preferred Option to Council	December 2011
Advertise for posts	December 2012
Interview for posts	January 2012
Annual Plan to Scrutiny Committee	April 2012
Commence Audit Service	April - June 2012

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

Benefits and Risks

Benefits	Risks
<ul style="list-style-type: none"> • The Revenues and Payments Portfolio is currently being restructured so the restructure of Internal Audit would align with this. • The independence of the team would not be compromised. • A qualified audit team will provide a professional quality audit service with a more focused strategic approach on the corporate risks with added value provided. • Staff would have greater opportunities for career development through skills transfer and a broader knowledge base. • The integrated internal model provides flexibility and allows specialist audits to be completed. • Recommendations by External Audit on the independence of the service would be addressed. 	<ul style="list-style-type: none"> • Unplanned staff absence could have an impact on delivery of the annual plan within a small dedicated internal audit team. • There is currently uncertainty around what is to happen with the Fraud sections funded by DWP, as part of the Welfare reforms.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

2.3 OPTION 2 - SHARED SERVICE WITH ANOTHER ORGANISATION(S)

The internal audit service is delivered through a shared service with another organisation(s).

There are two possible models for this service:-

- Aligned Service where there are internal audit staff in both organisations, but they are managed by one Audit Team Leader
- Integrated Service where one fully integrated team provides audit service to both organisations

Identification of Internal Audit Shared Service Partner

In identifying a shared service partner, Clackmannanshire Council has requested notes of interest from the Internal Audit sections of the thirty two Scottish Local Authorities. Seven authorities confirmed that they would be interested in an initial discussion.

From the initial discussion, the Council would enter into dialogue with the relevant authorities and work at agreeing consensus on a shared vision and principles of a shared audit service. The preferred partner(s) would be selected on the basis of

- shared expectations of audit service provision
- shared expectation of corporate governance arrangements
- anticipated benefits to Clackmannanshire Council on service delivery, staff opportunity and development and Scrutiny Committee support.

Option 2A - Aligned Audit Service

Description of Service

The audit service would be provided by an audit team based within the Council, however this team would be managed by an Joint Audit Team Leader who also has joint responsibility for providing audit services to the second organisation and is jointly accountable to both organisations Audit/Scrutiny Committees.

Depending on the organisation that the Council shares the provision of its service with, there may also be the opportunity to share the provision of the fraud arrangements. Accordingly the Joint Audit Team Leaders responsibility could also include:-

- meeting the Council's statutory responsibility to investigate benefit fraud and recover amounts on behalf of DWP
- preparing and implementing the corporate fraud prevention policy

Structure of Service

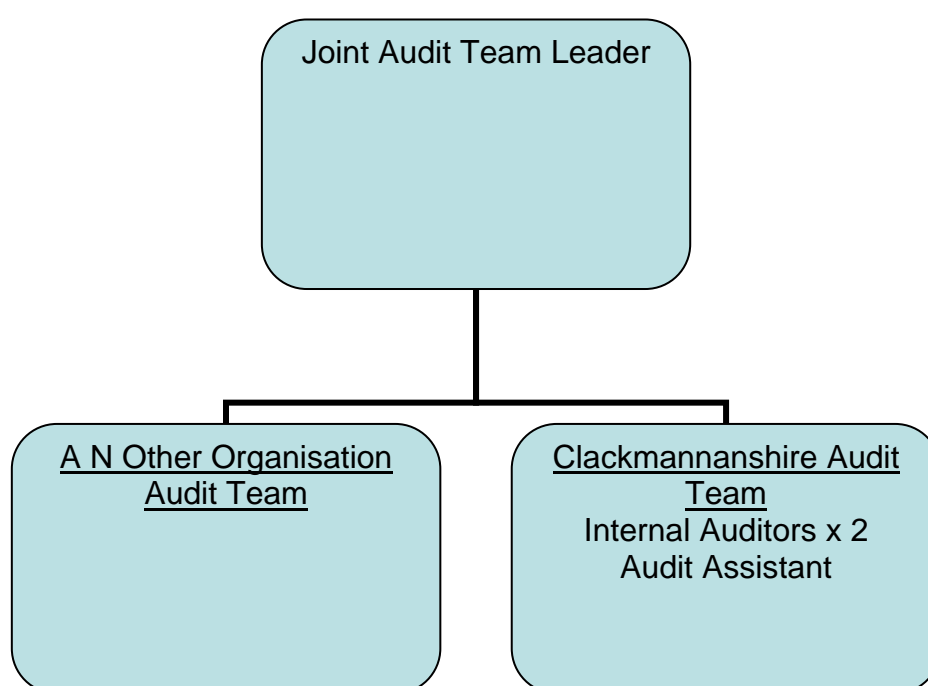
Each audit team would be employed by the respective organisation working to different terms and conditions, but would move to consistent shared audit practices and processes. It is expected that there could also be some overlap

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

of audits within the two organisations annual plans allowing audit teams to audit both organisations in the same year, however the plans would still be focused around each Council's risks with the balance of the plan tailored to the individual Council's risks and priorities.

It is expected that the efficiencies from a shared service through economies of scale and aligned working practices could deliver efficiencies on the annual plan after 3 years resulting in a small increase in the number of days deliverable in the annual plan.

The structure of a shared service would be as follows :-



Cost of the Service

The cost of this service in year 1 would be as follows:-

Option 2a - Aligned Shared Service with Another Council				
	grade	Salary	Emp'er Costs	Total
Joint Audit Team Leader (Half FTE)	10	19,658	5,819	25,477
Internal Auditor	9	34,386	10,178	44,564
Internal Auditor	9	34,386	10,178	44,564
Audit Assistant	5	19,517	5,777	25,294
Total Salaries		107,948	31,952	139,900
Supplies and IT Costs				3,090
Total Annual Costs				142,990
One off Implementation Costs				
Redeployment Costs				12,874
Advertising of posts				3,000
				15,874

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Total Cost in Year 1

158,864

The annualised cost of this service would increase year on year to £151,595 in 2014-15 due to salary increments.

Under the aligned model, the budget and costs for the audit service would remain with respective organisation.

Timetable for Implementation

The audit service is part of the Revenues and Payments service reconfiguration which is currently in consultation with the Unions. A suitable organisation would need to be identified with which to share the internal audit service.

The key milestones in the restructure would be as follows:-

Milestone	Date
Consult Staff	Ongoing
Scrutiny Committee Agree to shared service	November 2012
Identify partner	December 2011
Complete Staff Consultation	December 2011
Paper to Council asking for approval on shared service delivery of internal audit, including shared service and design principles	March 2012
Paper to Council on shared service structure	April 2012
Annual Plan approved by Scrutiny Committee	April 2012
Advertise vacant posts	May 2012
Interview for posts	June 2012
New Shared Service Commences	September - November 2012

Benefits and Risks

Benefits	Risks
<ul style="list-style-type: none"> A high quality service could be provided with a more focused strategic approach on the corporate risks There is a shared service commitment already in place within the Council. Shared service would allow a more effective and efficient service through the sharing of 	<ul style="list-style-type: none"> There could be differences in operational audit working practices which will require to be aligned. There could be differences in employee terms and conditions, work environments and grades, which the Audit Manager will have to manage. Failure in the governance

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<p>good practice and work processes.</p> <ul style="list-style-type: none"> • Staff may have greater opportunities for career development through close working with a larger audit team. • Savings could be realised through shared service arrangements with another organisation. • Independence of internal audit would be clear and easily demonstrable. • Recommendations by External Audit on the independence of the service would be addressed 	<p>arrangement could undermine the delivery and quality of service.</p> <ul style="list-style-type: none"> • Problems in identifying a shared service partner would further delay the delivery of the audit service. • Potential for any unknown or unquantified costs of implementation of a shared service to push up cost of service. • There could be a loss or breakdown in local accountability
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Option 2B - Integrated Service

Description and Structure of Service

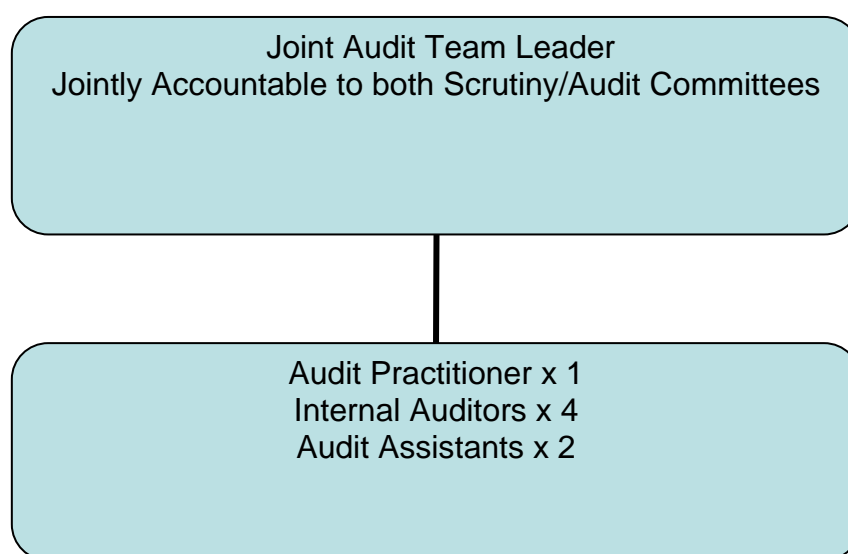
The audit service would be provided by a fully integrated team based within either of the organisations or by an Arms Length Organisation. This integrated team would be managed by Joint Audit Team Leader who also has joint responsibility for providing audit services to both organisations and is jointly accountable to both organisations Audit/Scrutiny Committees.

The integrated team would adopt the same audit practices and processes. It is expected that there could also be some consistency of audits within the two organisations Annual Plans allowing audit teams to audit both organisations in the same year. Audit plans would still be focused around each Council's risks with the balance of the plan tailored to the individual Council's risks and priorities.

It is expected that the integrating of two or more audit teams in a shared service could deliver efficiencies through economies of scale and aligned working practices. These savings are likely to be realised in the more medium term; 3 to 5 years.

The structure of the service would be agreed as part of joint discussions, however a possible structure could be as follows:-

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Cost of the Service

The cost of this service have been estimated at £142,990, with additional implementation costs of £15,874, totalling £158,864, which is consistent with the aligned shared service in 2A above. This is indicative and would be dependant on the organisation that the Council enters into the shared service with. On this assumption, the salary and service costs would be expected to increase year on year to £151,595 in 2014-15 due to salary increments

Under the aligned model, the budget and costs for the audit service would be pooled together and commitments would need to be made by both organisations around the treatment of savings and how this could affect the shared service.

Timetable for Implementation

The audit service is part of the Revenues and Payments service reconfiguration which is currently in consultation with the Unions.

The key milestones in the restructure would be as follows:-

Milestone	Date
Consult Staff	Ongoing
Scrutiny Committee Agree to shared service	November 2012
Complete Staff Consultation	November 2011
Identify partner	February 2012
Paper to Council asking for approval on shared service delivery of internal audit, including shared service and design principles	April 2012
Annual Plan to Scrutiny Committee	April 2012
Paper to Council on shared service	June 2012

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

structure
 Advertise vacant posts
 Interview for posts
 New Shared Service Commences

July 2012
 August 2012
 November - January 2013

Benefits and Risks

Benefits	Risks
<ul style="list-style-type: none"> • A high quality service could be provided with a more focused strategic approach on the corporate risks with added value provided • Shared service would allow a more effective and efficient service through the sharing of good practice and work processes. • Staff may have greater opportunities for career development through close working with a larger team of audit colleagues. • Savings could be realised through shared service arrangements with another local authority. • Independence of internal audit would be clear and easily demonstrable. • Recommendations by External Audit on the independence of the service would be addressed 	<ul style="list-style-type: none"> • There could be differences in working practices which will require to be aligned. • Failure in the governance arrangement could undermine the delivery and quality of service • Problems in identifying a shared service partner would further delay the delivery of the audit service • Potential for any unknown or unquantified costs of implementation of a shared service to push up cost of service. • There could be a loss or breakdown in local accountability.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

2.4 OPTIONS 3 - OUTSOURCE FULL INTERNAL AUDIT PROVISION

Description and Structure of Service

The internal audit service would be delivered by a external internal audit provider, most likely a national accounting or auditing firm, however another Local Authority could also be successful in bidding for the contract. All responsibility for fulfilling the Audit Team Leader role, establishing an audit team and delivering the service would fall within the supplier's remit.

The external provider would be procured through existing procurement routes. Given the level of the anticipated spend over three years, the supply of internal audit services would be advertised for competitive tender in compliance with Council Contract Standing Orders.

Aberdeen City Council completed a similar tender exercise in 2010 and the accounting firm Price Waterhouse Coopers (PWC) was awarded the contract. It is understood that the five members of Aberdeen City Council's audit staff team were TUPE transferred to PWC as part of this arrangement. The cost of this contracted service is £490 per day. This contract was procured through the Public Contract Scotland Portal, which gives any Scottish local authority, including Clackmannanshire, the opportunity to call off against specification and agreed rates.

If the Council sought to use the existing tender specifications, up to two members of the audit team could be TUPE transferred to PWC.

If the Council chose not to apply the existing tender specification with PWC, a formal specification for the Clackmannanshire audit service would need to be agreed prior to the start of the procurement process and this would form the basis of the contract with the successful tenderer. The specification would include:-

- cost of service, quality of service, performance standards, audit days to be provided,

The key service that the External Provider would be responsible for would be:-

- the delivery of the annual audit assurance statement
- supporting the corporate governance arrangements jointly with the Governance Manager through the Governance Improvement Plan.

The selected provider would prepare the Annual Plan based on planning and preparatory work undertaken onsite at the Council. This would involve discussions with the Senior Executive team, Senior Management teams and Scrutiny Committee to discuss the Council and service objectives and associated risks. The Plan would be presented to Scrutiny Committee in advance of the financial year laying out the audit work for the year. The cost of carrying out this preparatory work would be included in the total cost of internal audit services.

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Regular progress reports would be continue to be presented to Scrutiny Committee and completion of audits would be arranged directly with the relevant Service Manager. The External Providers audit staff would base themselves at Council's office for the duration of the audit, similar to the current arrangements with the External Audit Provider.

The Audit Plan would provide 600 audit days per annum, however this may need to include an allocation for the external provider to set up the service, so may deliver only 11 - 14 audits per year.

Cost of the Service

Using the current PWC schedule of rates of £490 / day and an average annual provision of 600 days, the cost of this service would be £294,000 per annum. "One off implementation costs" costs of £12,874 would be on top of this in year 1.

It is not expected that the contract costs would rise significantly each year as the Council would seek to procure on a fixed contract for three years.

Timetable for Implementation

The internal audit service is currently within the Revenues and Payments service which is currently undertaking is service reconfiguration. As part of this, revenues and Payments is currently in consultation with the Unions. If the Council was to call on the existing tendered specification with PWC, this would dovetail into the existing reconfiguration and consultation arrangements with the key milestones in the restructure would be as follows:-

Milestone for Audit Reconfiguration	Date
Consult with Staff and Unions	Ongoing
Complete Staff Consultation	November 2011
Initial Discussion with PWC on IA service	December 2011
Agreement of service provision with PWC	February 2012
Commence Audit Service	April - June 2012

If it was decided that the existing tender specification and Schedule of rates with PWC would not be used, the timetable would need to be extended by an additional 6 months. This would be needed to allow the time to prepare Clackmannanshire's audit tender specification, advertise, evaluate and award the contract. Accordingly the earliest that any externally provided service would be commencing would be October to December 2012.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

Benefits and Risks

Advantages	Risks
<ul style="list-style-type: none"> • There would be a consistent service delivery with the annual plan being delivered • There would be more access to audit specialism such as computer audits and CAAT • Penalty clauses can be included in the contract for delays in delivering the plan • There would be investment in training, development and best practices • Recruitment, absence management and professional capability would not be an issue for the Council. • Independence of internal audit would be clear and easily demonstrable. 	<ul style="list-style-type: none"> • Procurement could require the full competitive tender process which takes on average 6 months to advertise, evaluate and accept. • It would take time for the external provider to get an indepth understanding of the Council's risk and internal control environment and build up a relationship with the officers, members and Scrutiny Committee. • The service would only be tendered for 3 to 4 years, so another procurement process would be necessary in the medium term which may increase costs.

INTERNAL AUDIT OPTIONS APPRAISAL - PHASE 2

COMPARISON OF OPTIONS - TABLE 1

		1	2	3	4	5	6	7	8	9	10
	Structure	Cost of Service				Ave No of Audit days	Average Budget Increase	Value for Money			Service Start From
		Year 1	Year 2	Year 3	Total			Cost per day (Year 1 only)	Cost per day (over 3 years)	Increase/ (Saving) over 3 years	
		£	£	£	£			£	£	£	
	Current Structure	181,393¹	183,156	186,470	551,018	600²	1.36%	302.32	306.12	0	-
1	Audit Fraud Full Integrated Team	137,590	141,582	145,817	424,990	600	2.73%	-	-	(126,028) ³	April - June 2012
		72,476	74,311	76,222	223,009	-	2.73%	-	-	(63,363) ³	
		210,066 ¹	215,893	222,040	647,999	600	2.73%	229.32	236.11	(189,391) ³	
2a	Aligned Shared Service	142,990 ¹	147,153	151,595	441,738	600	2.84%	238.32	245.41	(109,280)	Sept - Nov 2012
2b	Integrated Shared Service	142,990 ¹	147,153	151,595	441,738	600	2.84%	238.32	245.41	(109,280)	Nov 2012 - Jan 2013
3	Outsourcing	294,000 ¹	294,000	294,000	882,000	600	0%	490.00	490.00	330,982	April - June 2012

¹ The Year 1 figures do not reflect the "one off implementation" costs.

² This reflects performance of a full staff complement with the current structure achieving the Annual Plan

³ Reflects the saving on both the Internal Audit and Fraud budgets as below :

Over Three Years	£
Existing Audit Budget	551,018
Existing Fraud Budget	286,372
	<u>837,390</u>
Less cost of Integrated team	<u>(647,999)</u>
Saving	189,391

3. SUMMARY

Each of the different options has been summarised and compared in Table 1 above. Three Value for Money measures have been shown in column 7 to 9 to help identified the preferred model of internal audit for the Council.

Value for Money Measures

These three measures help quantify and demonstrate the value for money for each option and include the average daily cost of audit provided (column 7), the average daily cost of audit provided over the three years (column 8) and the increase/decrease in the current audit budget (column 9). Both the one year and three year figures for the daily cost of audit provide have been included to illustrate the short and medium term impact.

Comparison of Value for Money Measures

For each of these three measures, the most cost effective provision of audit is the integrated audit and fraud services at £229 per day. Both shared service models (option 2A and 2B) provides the next greatest value for money at £238 per audit day. This is an difference of £9 per day on the shared service or £5,400 over the course of the year. Finally, the outsourcing is the highest cost at £490 per day. This is an additional cost of £151,200 per annum over the best value for money service option.

The second value for money measure takes into account inflationary increases over 3 years on the daily cost of the audit. The integrated audit and fraud service still returns the best value for money at an average of £236 per day over the three years, with the shared service option £9 higher at £245 per day. The outsourcing option provides the lowest value for money, with an average daily rate of £490.

The final measure quantifies the saving/additional resource required for each of the three options, when compared to the existing audit budget of £181,393 for 2012-12.

The integrated audit and fraud service provides the greatest saving over three years of £189,391 with the shared service offer a saving of £109,280. The saving for the audit and fraud also incorporates the potential savings available on the remaining existing fraud budget of £94,000 per annum.

The outsourcing service is the most expensive over the three years. It will not offer any savings and will require an additional £330,982 over three years.

Start of Audit Service Delivery

Column 10 summaries for each option, the expected earliest date that the audit service would start to operate. Option 1 would allow the audit service to be operating in the first quarter of 2012-13. Option 3 would also allow the audit service to be operating in the first quarter of 2012-13, provided that the PWC contract is called upon and a formal tender is not required. If a formal tender is required, this would push the start of the audit service back to September - November 2012.

Option 2A would allow the audit service to be operational from September to November 2012.

Option 2B would allow the audit service to be operational from November 2012 - January 2013.

Although a reduced audit service has been provided during 2011-12, the external auditors have highlighted the risks to the Council in not having a professional audit service. The longer the Council is without a full complement of audit staff, the greater risk to the Council. Both option 1 and 3 would provide the quickest models to reduce the Council's risk.

Preferred Option

Taking into account both value for money and the need for the Council to mitigate the risks of having an reduced audit service, as soon as practically possible, the preferred option is Option 1. This delivers a saving of £189,391 over three years and allows the audit service to be operating in the first quarter of 2012-13.

While Option 2A and 2B also delivers savings over three years, the service would not be operational until quarter 2 or 3 of 2012-13. There is also a risk of unanticipated costs occurring which could reduce the possible savings. There is an additional risk that unanticipated delays in identifying a partner and agreeing the infrastructure arrangements for a shared service, would further delay the start of an operational audit service.

Option 3, while able to deliver a service from April - June 2012, would require additional budget allocation of £330,982 and does not demonstrate value for money against the other options.