APPENDIX D

WEST YORKSHIRE PASSENGER TRANSPORT AUTHORITY

Report to the Audit & Governance Committee
to be held on 29 June 2007

SUBJECT: INTERNAL AUDIT – ANNUAL REPORT

1. PURPOSE OF REPORT

1.1 To consider the annual report of the Internal Audit Manager and provide details of significant issues arising as a result of work performed in the Annual Audit Plan 2006/07.

2. INFORMATION

2.1 The Annual Reporting Process

Management is responsible for the system of internal control and should set in place policies and procedures to help ensure that the system is functioning correctly. The Passenger Transport Authority utilises the internal audit section established within the Passenger Transport Executive to provide an internal audit function and contribute to the operation of the overall control framework for the Authority. Due to this arrangement, reporting requirements are that both the Executive's Audit Committee and the Authority's Audit & Governance Committee consider work performed and, as a result, any issues raised by internal audit On behalf of the Director of Corporate Services, Internal Audit review, appraise and report on the efficiency, effectiveness and economy of financial and other management controls. This report is the culmination of the work during the course of the year and seeks to:

- provide an opinion on the adequacy of the control environment
- comment on the nature and extent of significant risk
- report the incidence of significant control failings or weaknesses

2.2 Requirement for Internal Audit

There is a statutory requirement under the Accounts & Audit (Amendment) (England) Regulations 2006 for an internal audit function. Regulation 6 states that a "relevant body shall maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control". This role is complemented by initiatives aimed at promoting effective corporate governance, such as the Audit Commission's emphasis on risk management in their Code of Audit Practice.

In December 2006 CIPFA published their revised code of practice for internal audit in local government in the U.K. This has been adopted as “proper internal audit practice” for the Authority.

2.3 How Internal Control is Reviewed

Internal Audit continues to embrace the risk assessment approach to audit. During the course of the year the risk profile of Metro has been continually updated and used to form the basis of Internal Audit’s operational plan for the coming year. The review process draws on key indicators of risks to the organisation and attempts to ensure that suitable audit time and resources are devoted to review the more significant areas. Factors used in the risk assessment include financial materiality, legislative requirements, Audit’s previous experience, and the potential for fraud. This risk based approach to audit planning results in a comprehensive range of audits that are undertaken during the course of the year to support the overall opinion on the control environment.

2.4 Opinion 2006/2007

From the work undertaken during the year, Internal Audit has reached the opinion that satisfactory arrangements were implemented to ensure the effective, efficient and economic operation of the Authority’s financial affairs**.**

No system of control can provide absolute assurance against material misstatement or loss, nor can Internal Audit give that assurance; this statement is intended to provide reasonable assurance. There is an ongoing process for identifying, evaluating and managing the key risks.

2.5 Statement on Internal Control (SIC)

The Accounts and Audit Regulations 2003 that came into force on 1st April 2003 established requirements related to systems of internal control and the review and reporting of those systems. Accordingly, the Authority needs to have in place a process for establishing, maintaining and reviewing the system of internal control and risk management. Regulation 4 of the Accounts and Audit Regulations requires that;

“The relevant body shall be responsible for ensuring that the financial management of the body is adequate and effective and that the body has a sound system of internal control which facilitates the effective exercise of that body’s functions and which includes arrangements for the management of risk”

Further amendments to the regulations that bring PTE's into the scope of the Act took effect from 31 March 2006. Changes in relation to the provision of statements on internal control are as follows;

"The relevant body shall conduct a review at least once in a year of the effectiveness of its system of internal control and shall include a statement on internal control, prepared in accordance with proper practices, with the Statement of Accounts

The findings of the review shall be considered by a committee of the relevant body, or otherwise by the members of the relevant body meeting as a whole, which shall approve a statement on internal control, prepared in accordance with proper [internal control] practices.

For the SIC 2006/07 Internal Audit has provided an opinion for the SIC based upon the risk based audit plan coverage during the year.

3. SIGNIFICANT ISSUES ARISING 2006/2007

The following section provides a summary of the more significant issues that have been identified and reported during the year:

3.1 Monitoring of Controls.

Further enhancements to the monitoring of the operation of key financial controls have been made with the introduction of self-assessment based reports. These are provided at quarter year intervals to the Audit Committee by the Assistant Director Finance (PTE) and the Deputy Chief Financial Officer (PTA).

3.2 Ordering Systems

The review of new ordering systems identified a weakness relating to the segregation of duties within the process. However, other high level controls were found to operate which should detect any inappropriate expenditure. These measures included budgetary control, the review of orders by the Purchasing section and recording of computer and other high value potable equipment on a subsidiary system.

3.3 I.T. Systems – Third Party Access

An audit of ICT management processes highlighted that the Executive's systems may be vulnerable when access is allowed to third parties in order to carry out maintenance or upgrades to software applications. It was agreed that policies, contracts and procedures require updating to clarify responsibilities, determine the scope of access and obtain assurances in relation to third parties.

3.4 Summary of Whistleblowing Cases

The Section continues to act as the primary contact point for Metro's Whistleblowing Policy. Arrangements to improve accessibility to information and mechanisms to make protected disclosures have been made provided on the Authority's web site.

During the period no referrals were made to Internal Audit.

4. AUDIT PERFORMANCE

4.1 Ensuring Quality

We work closely with the external auditors, The Audit Commission. They rely heavily on the work that we do on key financial systems to gain assurance that the systems are operating as intended. Such assurances contribute to them being able to "sign off" the Accounts and contribute to their 'conclusions' on the arrangements for securing economy, efficiency and effectiveness in the use of resources.

4.2 Review of Internal Audit

The Audit Commission completed a review of Internal Audit in November 2006. It concluded that they were able to continue to place reliance on the work performed by internal audit. However, a number of improvements were identified in order to meet changed requirements caused by the introduction of new international standards of auditing, ISA+ and the revised CIPFA code of internal audit practice. A plan was produced to address these issues and action has been taken on the following key themes:

Reviewing the resource requirements for internal audit.

Formally stating the responsibilities and scope of internal audit for both the Executive and the Authority.

Determining a joint audit approach between the Audit Commission and Internal Audit.

Increasing the level of audit supervision and review.

Clearly mapping internal audit plans to the risk management process.

4.3 Reporting

Arrangements for reporting on internal audit activities to the Authority were established with the creation of the Audit & Governance Committee. This group primary roles are to deal with the Authority's arrangements relating to it's financial accounts, the adequacy of corporate governance arrangements and to consider arrangements relating to internal and external audit.

4.4 Client Feedback

As part of Internal Audit's commitment to ensuring the highest professional standards and to ensure that we are continually improving the quality of work produced, a customer satisfaction questionnaire is issued. The responses have been analylised and indicate good scores in all criteria with the exception of significance of recommendations, which produced an average score. It should be stressed that the rate of return of these questionnaires was quite low, around 30 %, and measures to increase this response are being considered for 2007/08.

Over 170 employees completed the corporate survey including their experience and perception of the Internal Audit service provided within Metro. The results of this questionnaire support responses received from audit client feedback returns. Overall the customer satisfaction score was 3.70 in the scale from 1 to 5, 5 being an excellent rating. Although this is a small decrease on the previous years score, there is still a good perception of internal audit amongst staff within Metro.

5. ADDING VALUE

Throughout the year the section have provided advice over and above the core objectives of giving internal control assurance and recommending effective systems improvements to management.

This included offering pragmatic advice to officers on the application of new ordering system, Proactis, and working with the Purchasing section on the e-tendering pilot project.

Internal Audit has also played a lead role in coordinating risk management arrangements within Metro.

6. CONTINUING PROFESSIONAL DEVELOPMENT

In a changing environment it is important that Internal Auditors are kept abreast of the latest audit methodologies, changes in legislation as well as changes to the public sector arena so they can have the necessary skills and knowledge to fulfil their role. This is provided through Continuing Professional

Development. To support this process, each Internal Auditor is assessed against CIPFA's skills and competences guide. This enables strengths and weaknesses to be identified so that training can be focused on individuals specific requirements.

7. EQUAL OPPORTUNITY IMPLICATIONS

7.1 None resulting from this report.

8. RECOMMENDATIONS

8.1 That this report be noted.