

**CITY OF MARION
AUDIT COMMITTEE MEETING
4 July 2006**

**REPORT RELATING TO:
Excellence in Governance**

Originating Officer: Kathy Jarrett, Manager Governance
Director: Jeff Rittburger, Director Governance
Subject: Internal Audit Service Provision
Reference No: AC040706F01
File No: 9.14.1.4

If the Audit Committee so determines, this matter may be considered in confidence under Section 90 (3)(d) of the Local Government Act 1999 on the grounds that the report details commercial information of a confidential nature.

Jeff Rittberger
Acting Chief Executive Officer

RECOMMENDATION:

1. That pursuant to Section 90(2) and (3)(d) of the Local Government Act 1999 the Council orders that all persons present, with the exception of the following persons Mark Searle (Chief Executive Officer), Jeff Rittberger (Director Governance), Kathy Jarrett (Manager Governance), Linda Graham (Senior Adviser Governance) and Sue Pirone (Manager Contracts and Purchasing), be excluded from the meeting as the Committee receives and considers information relating to the tender for the provision of Internal Audit Services upon the basis that the Committee is satisfied that the requirement for the meeting to be conducted in a place open to the public has been outweighed by the need to keep consideration of the matter confidential given the information is of a commercial nature.

CORPORATE OBJECTIVES:

EG1.7 Embrace a culture of Continuous Improvement for all operations to enhance the value to the community through processes such as:

- *Internal and external audits*
- *Reviews and measurement of the organisations services, systems and processes*
- *Continuous Improvement Projects*

EXECUTIVE SUMMARY / REPORT OBJECTIVE

On 9 May 2006, the City of Marion issued an invitation to tender for the provision of Internal Audit Services on an ongoing basis as a service to Council and management. The objective of the tender process was to seek a firm that could demonstrate a commitment to working with, and assisting in the achievement of strategic outcomes for the City of Marion.

An evaluation team was established to review tenders submitted and prepare a recommendation for consideration by the Audit Committee.

Four firms tendered for the contract and the purpose of this report is to provide the outcomes of the evaluation and make a recommendation to the Audit Committee as to a preferred supplier of Internal Audit Services for the City of Marion.

RECOMMENDATIONS:

That the Audit Committee recommends to Council:

- 1. The appointment of Ernst and Young as the provider of Internal Audit Services to the City of Marion for a period of three years subject to the resolution of contractual issues to the satisfaction of the Manager Contracts and Purchasing.**
- 2. In accordance with Section 91(7) and (9) of the Local Government Act 1999 the Committee orders that this report, the minutes arising from this report and any other information distributed at the meeting having been considered in confidence under Section 90(2) and (3)(d) of the Act be kept confidential and not available for public inspection for a period of 12 months from the date of this meeting. This confidentiality order will be reviewed at the last Audit Committee meeting for 2006.**

DUE DATES:

1. Appointment of Ernst and Young as the provider of Internal Audit Services. 11/7/2006

BACKGROUND

The City of Marion's current internal audit function is delivered by Deloitte. The relationship between Deloitte and the City of Marion is managed by the Governance Department. This model of delivery has been in place for a number of years and is considered appropriate given the City of Marion does not have any internal resources with the skills or experience necessary to undertake this function.

Given the relationship with Deloitte has been in place for a number of years, it was determined to test the market for the provision of Internal Audit Services. A tender for the provision of Internal Audit Services was therefore issued on 9 May 2005.

Outcomes expected from the provision of Internal Audit Services were identified within the tender as follows:

- Assurance that risk management policies, systems and procedures are sound.
- Achievement of the objectives established in the Internal Audit Charter.
- Contribution to the achievement of the City of Marion's Strategic Plan.
- Assistance in meeting the requirements of the Local Government Act 1999 and contracts, other relevant legislation, and relevant policies, procedures and instructions.
- Adequate addressing of business risks and adopting a risk based approach in the conduct of audits.
- Achievement of adequate and effective systems of internal control.
- Assessment of the quality of the City of Marion's performance in carrying out its responsibilities.

DISCUSSION

The Tender Process

Tender documentation comprising a Project Brief, General Conditions of Tender, Tender Forms, and a Professional Services Agreement were developed and made available to the market via advertisement on 9 May 2006 in the Adelaide Advertiser and placement on the South Australia Government's tender website. Records indicate that a total of 17 firms downloaded a copy of the documentation. Refer to Appendix 1 for a copy of the tender documentation and details of the firms who accessed the documentation.

A tender briefing session was held on 16 May 2006 to provide prospective tenderers with additional information concerning the City of Marion's expectations and to provide points of clarification as requested.

The tender closed at 2.00pm on 26 May 2006 at which time, two staff from the City of Marion Contracts Unit opened and recorded the tenders received.

Tenders Submitted

At the close of tenders, four (4) firms submitted proposals for the provision of Internal Audit Services to the City of Marion:

- Deloitte Touche Tohmatsu
- Ernst & Young
- KPMG
- PKF Chartered Accountants & Business Advisers

Of these firms, PKF submitted a non-conforming tender as they did not provide completed tender forms as required by the tender documentation.

Evaluation Criteria

In order to evaluate the tenders, an Evaluation Team was established comprising:

Manager, Governance – Kathy Jarrett
Manager Information Management and Technology – Karen White
Major Projects Planner – Hugh Dixon
Contracts Officer – Stan Orlovski
Governance Business Officer – Jaimie Thwaites

Prior to the tender closing, the evaluation team met to review the evaluation criteria identified within the tender documentation and to determine the relative scoring/weightings to be assigned to each criteria (refer to Appendix 2).

Assessment of Tenders

In order to assess the proposals, each member of the Evaluation Team individually scored the tenders against the evaluation criteria. The Team then met to discuss the strengths and weaknesses of the tenders and review individual scores. At this time, it was agreed to eliminate PKF from the process as their tender did not sufficiently conform with the Conditions of Tendering.

All Team members expressed a degree of disappointment with the tenders particularly in the area of integration with the City of Marion. None of the tenders appeared to focus on developing a partnership approach that was aligned with the City of Marion culture. Rather, each tender appeared to present an "off the shelf" model with little reference to strategies such as the Business Excellence Framework or Constructive Culture.

Although disappointed, the Evaluation Team proceeded to assess the three (3) remaining tenders and the combined result of the assessment is provided at Appendix 3 for information. As can be seen, the Ernst & Young tender achieved the highest rating primarily as a result of their lower overall hourly rate.

Given the concerns regarding the potential for partnership with the provider of Internal Audit Services, it was determined to meet with representatives of Ernst & Young on Wednesday 28 June 2006 to discuss their proposal and gain a better insight as to their "fit" with the City of Marion. The meeting provided the opportunity for Ernst & Young to elaborate their model of delivery including how they see their services could be integrated within the City of Marion. During the meeting, Ernst & Young acknowledged that it would take time for them to learn about the City of Marion, and demonstrated a preparedness to develop their approach in alignment with the direction being taken by the City of Marion. A copy of the Ernst and Young tender is provided at Appendix 4 for information.

Conditions of Contract

The Ernst & Young tender included a number of suggested amendments to the City of Marion's Professional Services Agreement (refer to pages 26-27 and 47-48 of the Ernst & Young tender). The amendments have been reviewed by the City of Marion's Contracts Unit and concerns were raised particularly in the areas of liability, use of reports and insurances.

During the meeting with Ernst & Young on 28 June 2006 discussion was held on the Professional Services Agreement and it appears that a mutually agreeable position can be attained (refer to Appendix 5 for details of the issues raised by the City of Marion with Ernst & Young).

Brief Comment on All Tenders

Ernst & Young:

- strong IT focus however access to local specialist resources
- numerous suggested changes to the Professional Services Agreement
- self suggested Key Performance Indicators
- good approach to Internal Audit methodology
- preparedness to work with the City of Marion to develop methodologies
- value for money

KPMG

- numerous suggested changes to the Professional Services Agreement
- good internal audit methodology
- collaborative approach
- linking of various corporate systems/initiatives
- significantly higher costs than the Ernst & Young proposal

PKF

- non-conforming tender received therefore not evaluated

Deloitte

- submission seemed to struggle with understanding of cultural aspects. This was surprising given Deloitte's previous work with the City of Marion
- some suggested changes to the Professional Services Agreement
- seemed to be proposing an off the shelf solution
- higher costs than the Ernst & Young proposal

Referees

The City of Adelaide was consulted as it has also recently engaged the services of Ernst & Young as internal auditors. Good feedback was received particularly regarding the collaborative approach taken by senior staff at Ernst & Young in carrying out audit assignments.

CONCLUSION:

It is the view of the Evaluation Team that the Ernst & Young proposal represents best value for money to deliver services required under this contract. It is therefore recommended that Ernst & Young be appointed as the City of Marion's Internal Audit Service provider, subject to the resolution of contractual issues to the satisfaction of the Manager Contracts & Purchasing.

- Appendix 1 – Tender Documentation and list of firms accessing the documentation
- Appendix 2 – Tender Evaluation Criteria and associated weightings
- Appendix 3 – Tender Evaluation outcomes
- Appendix 4 – Ernst & Young Tender
- Appendix 5 – City of Marion issues with the Professional Services Agreement