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**Meeting:**        **Audit Committee**

**Date:**            **30 June 2014**

**Subject:**        **Internal Audit Annual Audit Opinion**

**Report of:**      **Chief Finance Officer**

**Summary:**      This is the annual report of the Head of Internal Audit and Risk to those charged with governance on the overall adequacy and effectiveness of Central Bedfordshire Council's financial and other management internal controls.

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Advising Officer:        Chief Finance Officer

Contact Officer:        Kathy Riches , Head of Internal Audit and Risk

Public/Exempt:        Public

Wards Affected:        All

Function of:             Audit Committee

## **CORPORATE IMPLICATIONS**

### **Council Priorities:**

The activities of Internal Audit are crucial to the governance arrangements of the organisation and as such are supporting all of the priorities of the Council.

### **Financial:**

1.        None directly from this report. However, sound systems assist in preventing loss of resources (by other wastage or fraud), thereby improving effectiveness and efficiency.

### **Legal:**

2.        None directly from this report.

### **Risk Management:**

3.        No risk management implications come directly from this report but the Audit Plan was produced using a risk based approach, following the completion of a detailed Audit Needs Assessment which took into account strategic and service area risks.

### **Staffing (including Trades Unions):**

4.        None directly from this report.

**Equalities/Human Rights:**

5. None directly from this report.

**Public Health**

6. None directly from this report.

**Community Safety:**

7. None directly from this report.

**Sustainability:**

8. None directly from this report.

**Procurement:**

9. None directly from this report.

**RECOMMENDATION:**

**The Committee is asked to consider and comment on the contents of the report.**

**Background**

10. The Accounts and Audit Regulations 2011 require the Council to maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with proper internal audit practices. The applicable standards for 2013/14 were the Public Sector Internal Audit Standards (PSIAS) which came into effect on 1<sup>st</sup> April 2013. In accordance with the standards, the Head of Internal Audit and Risk is required to deliver a report to those charged with governance, timed to support the Annual Governance Statement, which must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

11. This report:
- Presents an opinion on the overall adequacy and effectiveness of Central Bedfordshire's framework of governance, risk management and control for the 2013/14 financial year,
  - Summarises audit work undertaken that supports that opinion
  - Highlights significant issues identified as part of Internal Audit's work, including those that are particularly relevant to the Annual Governance Statement
  - Compares the Internal Audit work actually undertaken with the work that was planned and summarises the performance of the internal audit function against its performance measures and criteria, and
  - Includes a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.

## **Responsibilities**

12. It is a management responsibility to develop and maintain the internal control framework and to ensure compliance. It is the responsibility of Internal Audit to form an independent opinion on the adequacy of the system of internal control.

## **Internal Control Environment**

13. The internal control environment comprises the Council's systems of governance, risk management and internal control.
14. In order to form an opinion on the overall adequacy and effectiveness of the control environment, the internal audit activity is planned to provide coverage of financial controls through review of the key financial systems, and internal controls through a range of operating activity both within directorates and cross cutting, using a risk based approach. The work undertaken by Internal Audit helps inform the Annual Governance Statement.

## **The Audit Methodology and Basis of Assurance**

15. During 2013/14 Internal Audit was bound by the Public Sector Internal Audit Standards. The purpose, authority and responsibility of the internal audit service is set out in the Internal Audit Charter, approved by the Audit Committee in January 2014.
16. In order to ensure that the Internal Audit Service operates in accordance with the PSIAS, the Head of Internal Audit and Risk has undertaken a self assessment of compliance with the standards. In accordance with the requirements of the Accounts and Audit Regulations 2011 the Chief Finance Officer has also carried out a review of the effectiveness of the System of Internal Audit. The scope of the review covered compliance with the PSIAS, and reporting on performance and outcomes to the Audit Committee. The PSIAS require the Annual Audit opinion to include a statement of conformance with the standard, and this is set out later in the report.

17. The internal audit work undertaken during the year has been conducted in accordance with the mandatory standards and good practice.
18. The Internal Audit Plan for 2013/14, approved by the Audit Committee in April 2014, was compiled using a risk based approach and was informed through:
  - reference to the previous Audit Needs Assessment undertaken
  - consultation with senior management
  - Internal Audit's own analysis of risk areas
  - reference to the strategic and operational risk registers, and
  - the outcome of the assurance mapping exercise on the risks documented within the Strategic Risk Register.
19. The Internal Audit Plan identified the individual audit assignments. The activity was undertaken using a systematic risk based approach. The objectives for each activity were determined and risks in the processes that supported that activity were identified and set down in terms of reference that outlined the objectives and scope for each audit. The work was planned and performed so as to obtain all the information and explanations necessary to provide sufficient evidence in forming an overall opinion on the adequacy of the internal control framework.
20. Internal Audit reports provide an overall conclusion on the control environment for each system reviewed. A summary of the conclusions for each audit is attached as Appendix A to this report. The definitions of each conclusion are attached as Appendix B.
21. The overall annual audit opinion is derived from the work undertaken during the year, as determined by the Audit Plan. However, it is also recognised that there is a risk management assurance framework in place that provides reasonable assurance that other significant risks have been identified and are managed effectively.
22. To provide quality assurance over the audit output, audit assignments are allocated to staff according to their skills and experience. Each auditor has a designated Audit Manager to perform quality reviews at four stages of the audit assignment: the audit brief (terms of reference), file review, draft report and final report stages. In addition, the Head of Internal Audit and Risk reviews all reports.
23. In addition to this annual report, the Audit Committee receive regular progress reports throughout the year.

### **The Internal Audit Team**

24. During 2013/14 the Internal Audit Service was delivered by a team of suitably qualified auditors. Each member of the team undertakes a regular Performance Development Review (PDR) and participates in Continuing Professional Development (CPD) as appropriate.

## Head of Internal Audit's Annual Opinion Statement

25. The Internal Audit work undertaken during the year has enabled Internal Audit to provide an objective assessment of whether systems and controls are operating effectively. In giving an audit opinion, however, it should be noted that assurance can never be absolute. However, the scope of the activity undertaken is sufficient for reasonable assurance to be placed on the work.
26. Ernst and Young, as the Council's external auditors, have reviewed the work undertaken by Internal Audit on the fundamental system audits and have been able to place reliance on the work, and have been in agreement with the audit opinions given.
27. A summary of the work undertaken during the year, forming the basis of the audit opinion on the control environment, is shown at Appendix A of this report.
28. The opinion on the Council's Internal Control environment is that overall it continues to be adequate. In general the key controls in place are adequate and effective such that reasonable assurance can be placed on the operation of the Council's functions.
29. This conclusion is based on the following:

### Framework of governance:

- A Code of Financial Governance is in place, and is incorporated within the Constitution.
- Financial Procedures support the Code of Financial Governance and these have been refreshed and updated during the year.
- A Financial Scheme of Management is in place.
- Procedures and processes have been documented in a number of key areas.
- Outcome of governance audits

### Risk Management Arrangements:

- Assurances on key strategic risks have been mapped during the year. Assurances considered include a range of management controls, corporate functions and third party assurances.
- A risk management framework is in place, including a documented strategy, risk co-ordinators within directorates, a Risk Matters Group and regular monitoring and reporting on strategic risks to senior management and the Audit Committee.

#### Internal Control:

- Each of the fundamental system reviews finalised has received an adequate audit opinion.
- The Payroll system has received an adequate opinion for the first time since the inception of the Council, having previously received limited opinions.
- Adequate controls were found to be in place in a number of other areas
- Progress has been made in addressing many of the high risk Internal Audit recommendations made, and
- There has been a stable senior finance management structure in place during the year.

30. It should be noted that most audits undertaken have resulted in reports identifying areas for improvement which have been well received by managers, and actions agreed to address weaknesses in control. The implementation of these actions is tracked by Internal Audit and the progress against the implementation of high recommendations is regularly reported to the Audit Committee.

31. In arriving at the opinion the following has been taken into account:

- The results of the audits undertaken as part of the 2013/14 plan
- The results of follow up action in respect of previous audits
- Whether or not any limitations have been placed on the scope of Internal Audit – of which there have been none.

32. The following key concerns were identified and these have been reflected in the Annual Governance Statement:

- Significant progress was made during 2013/14 to develop a comprehensive IT Disaster Recovery Plan. Further work is currently in progress. The Audit Committee has received regular updates on this during the year.
- A limited audit opinion was given to the review of Council procedures relevant to the employment of contractors and consultants, and Internal Audit has worked with officers across the Council to address the issues identified.
- The audit reviews of both direct payments and housing repairs commissioning also identified weaknesses in the current processes and management have agreed actions to address these issues.

#### **Delivery of the 2013/14 Internal Audit Plan**

33. The operation of the key financial systems is a key part of the internal control environment. The table at Appendix A sets out the outcome of the reviews of these systems, and indicates where the work is still ongoing. The appendix also summarises other reviews undertaken during the year.

34. The reviews of the key fundamental systems help inform the Annual Governance Statement. Each of the 10 key systems finalised has received an adequate audit opinion. It should be noted that the opinions given reflect the controls in place across the whole year. Although several of the Phase 2 reports have still to be finalised, no new key issues of concern have been identified.
35. Audit work is not just limited to implementing the audit plan. Internal Audit is involved in other areas advising on systems development and using their skills to provide other general advice to service areas. Internal Audit has participated in a number of projects, providing advice on controls required. These projects include the Local Welfare Provision Board, ESS/MSS and Routewise. In addition, individual grant claims have been audited, where required.

### **National Fraud Initiative (NFI)**

36. During 2013/14, we continued to complete work on the National Fraud Initiative (NFI). This involves supplying data to the Audit Commission for matching purposes. Work on investigating the resulting positive matches is ongoing. Work includes matches on pension payments to registered deaths, matching payrolls between authorities, and other matches including UK visas, blue badges, private residential care and Housing Benefits.
37. The Internal Audit team has also assisted other authorities undertake their NFI enquiries by providing information to support their investigations.

### **Anti Fraud Work and Special Investigations**

38. Internal Audit undertook four investigations during the year. The outcome of three were reported to the March 2014 Audit Committee. A further investigation has been finalised and this is summarised at Appendix C.
39. Internal Audit continues to operate the Fraud Hotline. None of the calls received have resulted in an audit investigation due to the nature of the calls. However, in all cases, appropriate advice was given.

### **Schools**

40. The rolling programme of school audits has continued during 2013/14. During the year final reports were issued to 12 schools. The opinions given for the finalised reviews are set out at Appendix A. Four schools received a limited audit opinion.

## Performance Management

41. The Audit Committee has agreed some Key Performance Indicators (KPI), which are regularly reported to the Committee. Overall, performance has been positive and where targets have not been met, action will be taken aimed at improving performance. The table below summarises the results for the year, and also includes the previous year's indicators, for comparative purposes.
42. The indicators include both CBC audit activities and school activity.
43. **Activities for 1 April 2013 – 31 March 2014**

KPI	Definition	2013/14		2012/13	
		How we performed	Our target	How we performed	Our target
KPI01	Percentage of total audit days completed.	97%	80%	100%	80%
KPI02	Percentage of the number of planned reviews completed to final report stage.	75%	80%	80%	80%
KPI03	Percentage of audit reviews completed within the planned time budget, or within a 1 day tolerance.	74%	75%	60%	80%
KPI04	Time taken to draft reports: Percentage of reviews where the first final draft report was returned by auditee within 10 available working days of receipt of the report from the Auditor.	80%	80%	76%	80%
KPI05	Time taken to issue a final report: Percentage of reviews where the final report was issued within 10 available working days of receipt of the response agreeing to the formal report.	100%	80%	85%	80%
KPI06	Overall customer satisfaction.	90%	80%	93%	80%



#### 44. **Analysis of indicators:**

KPI01 – During the year we delivered a total of 1224 productive audit days against a total of 1260 planned days for the year. This exceeds our target for the period.

KPI02 – This KPI measures final reports issued as at 31 March 2014. 75% of the planned reviews had been completed to final report stage, which is below the target. Work is progressing on the outstanding reviews.

KPI03 – 73% of planned reviews have been completed either within the planned time budgets, or within a 1 day tolerance. This is slightly below the target agreed for the year, but does represent an improvement on the previous year.

KPI04 - This indicator measures the time taken for Internal Audit to receive a response from the auditee to the draft report. During 2013/14, 80% of draft reports were responded to within the target set. This represents an improvement over the previous year and reflects a continuing cooperation from auditees.

KPI05 - This indicator measures the time taken by Internal Audit to issue the final report upon receipt of an agreed response from the auditee. .

KPI06 – A total of 51 surveys have been sent out. 23 responses have been received to date. The responses received have been positive.

#### **Conformance with the Public Sector Internal Audit Standards**

45. The Public Sector Internal Audit Standards require the Annual Internal Audit Opinion to include a statement on conformance with the PSIAS and also the results of the quality assurance and improvement programme.
46. The January 2014 Audit Committee received a report on PSIAS which included the outcome of an initial self assessment against the standards undertaken using the guidance and checklist provided by CIPFA in the recently published Local Application Note. The self assessment demonstrated that Internal Audit substantially complies with the new standards, and an action plan was produced. During the year, action has been taken to move towards compliance, for example, the Internal Audit Charter has been documented and internal audit processes have been reviewed. Guidance on the interpretation of the standards is still being developed by CIPFA and any future guidance published will be reflected when further developing the internal audit service.

47. A Quality Assurance Improvement Programme is being developed. This programme is intended to ensure that the internal audit service continues to develop and improve. As such, it is envisaged that work will be on going in this area. An initial action plan has been produced, aimed at improving the efficiency and quality of internal audit work and this will be regularly monitored. Following the current cycle of Personal Development Reviews (PDR) a comprehensive training plan for the internal audit service will be collated.
48. There are no significant areas of non compliance. Areas which require further action include:
- Making provision for external as well as internal assessment of Internal Audit. This is planned for year ending March 2016
  - Further developing assurance mapping to ensure appropriate account is taken of other sources of assurance when providing overall assurance to the Council. Currently, strategic risks have been mapped and it is intended to also map key operational risks
  - Developing the documentation of the risk based audit plan in accordance with PSIAS. This will be addressed when developing the plan for 2015/16 and onwards. This is an area where further guidance from CIPFA is envisaged.

## **Review of the Effectiveness of Internal Audit and the Effectiveness of the Systems of Internal Control**

### **Background (Accounts and Audit Regulations 2011)**

49. All councils are required to publish an Annual Governance Statement (AGS) to accompany their Statement of Accounts, in accordance with the 2011 Accounts and Audit Regulations. Assessments of the Effectiveness of Internal Audit and the Effectiveness of Systems of Internal Control are two key aspects of the AGS. Central Bedfordshire Council has reviewed both systems for 2013/14 and the findings are incorporated into the Annual Audit opinion and subsequently into the AGS.

### **Review of the Effectiveness of Internal Audit.**

50. As referred to in paragraph 16 above, a review of the Effectiveness of Internal Audit was undertaken by the Chief Finance Officer.

## **Review of the Effectiveness of the Systems of Internal Control**

51. The Council's review of the effectiveness of the system of internal control is informed by:
- Directorate assurance based on management information, performance information, officer assurance statements and Scrutiny reports
  - the work undertaken by Internal Audit during the year
  - the work undertaken by the external auditor reported in their annual audit and inspection letter
  - other work undertaken by independent inspection bodies
52. The Head of Internal Audit and Risk has supported the Chief Legal and Democratic Services Officer (Monitoring Officer) to collect evidence required for the production of the AGS.
53. Directors have been requested to sign statements on the Effectiveness of Internal Control for 2013/14, confirming that during the year they were:
- Ensuring that there are arrangements in place for establishing Directorate objectives and compliance to corporate priorities;
  - Ensuring compliance to the Council's governance arrangements (Constitution, Ethical Framework, and Policies & Regulations);
  - Ensuring arrangements for sound budgetary controls;
  - Effectively monitoring and managing performance;
  - Reporting to the appropriate Member Committees;
  - Responding promptly to internal & external audits & inspections;
  - Continuously managing business risks and service continuity arrangements.
54. The work undertaken by Internal Audit on the systems of internal control disclosed that generally they were effective during 2013/14. However, some areas of concern were identified and these are summarised in paragraph 32 above, and are reflected in the Annual Governance Statement.

## **Conclusion and Next Steps**

55. The work undertaken by Internal Audit has enabled the team to advise management of some of the control weaknesses identified at an early stage, and make recommendations designed to enhance and strengthen controls and mitigate risks.
56. The internal control environment operated adequately during 2013/14, although some areas of concern identified in the AGS must be addressed promptly.

**Appendices:**

Appendix A – Summary of Internal Audit Activity 2013/14  
Appendix B – Definition of Internal Audit Opinions  
Appendix C – Investigations finalised since last Committee

**Background Papers:** None