

## Central Bedfordshire Council

Audit Committee

27 June 2016

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### 2015/16 Internal Audit - Annual Audit Opinion

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#### Purpose of this report:

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.

#### RECOMMENDATION

The Committee is asked to:

1. Consider and comment on the contents of the report.

#### Overview and Scrutiny Comments/Recommendations

1. This report is not scheduled to be considered by Overview and Scrutiny, as it is a matter for the Audit Committee under the delegations of the Constitution.

#### Background

2. The Accounts and Audit Regulations 2015 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 2015/16 were the Public Sector Internal Audit Standards (PSIAS) which came into effect on 1st 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.

3. This report:
  - Presents an opinion on the overall adequacy and effectiveness of Central Bedfordshire's framework of governance, risk management and control for the 2015/16 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**

4. 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.

### **Independence and Accountabilities**

5. Internal Audit remains independent of the activities that it audits to enable auditors to perform their duties in a manner which facilitates impartial and effective professional judgements and recommendations.
6. In addition, the Head of Internal Audit and Risk has direct free and unfettered access and freedom to report in her own name and without fear or favour to all officers and members, particularly to those charged with governance (including the Chief Executive and the Chair of the Audit Committee).

### **Internal Control Environment**

7. The internal control environment comprises the Council's systems of governance, risk management and internal control.
8. 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**

9. During 2015/16 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.
10. The internal audit work undertaken during the year has been conducted in accordance with the mandatory standards and good practice.
11. The Internal Audit Plan for 2015/16, approved by the Audit Committee in March 2015, 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.
12. 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.
13. 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.
14. 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.
15. 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.
16. In addition to this annual report, the Audit Committee receive regular progress reports throughout the year.

## **The Internal Audit Team**

17. During 2015/16 the Internal Audit Service was delivered by a team of suitably qualified auditors. Due to maternity leave, one senior auditor position was covered by a temporary member of staff, who is professionally qualified. Each permanent member of the team undertakes a regular Performance Development Review (PDR) and participates in Continuing Professional Development (CPD) as appropriate. There was a vacancy within the team for a period of approximately six months, and this did have an impact on the number of reviews finalised.

## **Head of Internal Audit's Annual Opinion Statement**

18. 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.

19. 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.

20. 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.

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.

21. 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. These are regularly refreshed and updated.
- 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:

- The audit opinion for each of the fundamental system reviews finalised has been positive. Two have received a full assurance opinion and the remaining reviews received an adequate audit opinion.
- Adequate controls were found to be in place in a number of other areas. The majority of audit reviews of these areas other than the fundamental systems have received Adequate Assurance opinions. Where weaknesses in the current processes have been identified actions have been agreed with management to address these issues.
- Progress has been made in addressing almost all of the high priority Internal Audit recommendations made, and
- There has been a stable senior finance management structure in place during the year.

22. 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.

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

- The results of the audits undertaken as part of the 2015/16 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.

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

- The change of provider for agency staff effective from November 2014 resulted in interim control procedures being introduced with a reduction in the control environment for a significant area of activity for the latter half of 2014/15 and the first half of 2015/16. Revised management controls were introduced in October 2015. A detailed audit review is scheduled for 2016/17
- Internal Audit has continued to track the implementation of high priority recommendations. This work has identified that, although

progress was made during 2015/16 to develop a comprehensive IT Disaster Recovery Plan, this work has still to be finalised. The Chief Information Officer has undertaken a review of the data centre provisioning at CBC and ICT is undertaking to deliver a refreshed and renewed DR Plan. However, he has reported that an OJEU tender to replace the existing data centre capacity with professionally managed capacity returned offers that were deemed to be too expensive, and an internal process is now underway to move to CBC managed cloud capacity. Internal Audit undertook a further audit review of IT Disaster Recovery during 2015/16, and the audit opinion remained Limited Assurance. The Audit Committee has received regular updates on this during the year, and it was resolved at the April 2016 Audit Committee that the Chief Information Officer be invited to attend the September Committee to provide an update on the progress made in developing and approving the Information Technology Disaster Recovery Plan.

- The audit reviews of ICT Governance, Teachers Pensions', SAP Access and Security and Section 278 Agreements, undertaken during 2014/15 identified weaknesses in the current processes and management have agreed actions to address these issues. For each of these reviews, follow up audits are either in progress or planned to provide assurance on whether the control environment has improved.

### **Delivery of the 2015/16 Internal Audit Plan**

25. 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.
26. The reviews of the key fundamental systems help inform the Annual Governance Statement. Two reviews have received a full assurance audit opinion and the remaining 8 key system reviews finalised have received an adequate audit opinion. It should be noted that the opinions given reflect the controls in place across the whole year. With the exception of the issue relating to the change in agency provider referred to in paragraph 24 above, no new key issues of concern have been identified.
27. 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 supporting the highways contract retender and working with colleagues to identify the controls

needed for future European Social Fund Programmes. In addition, individual grant claims have been audited, where required.

28. Work has either been finalised or nearing completion for the majority of the audits in the plan, however, as was reported at the April 2016 Committee meeting, no work has yet started on 4 reviews originally planned for 2015-16. These audits have been deferred to either 2016/17 or 2017/18.

- School Transport
- Compliance- Assets
- Care Fund/Better Care Fund Integration
- Review of Leisure Services outcomes
- Housing Repairs Follow Up

The explanations for deferring the audits were reported to the April Committee. It is not considered that the deferral of these reviews exposes the Council to any unacceptable risks that would impact on the overall Internal Audit Opinion.

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

29. During 2015/16 we continued to complete work around the National Fraud Initiative (NFI). The overall responsibility for this exercise has now passed from the Audit Commission to the Cabinet Office. Data sets are supplied when requested and matches investigated as required.

30. 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**

31. Internal Audit concluded two investigations during the year. The outcome of these were reported to the September 2015 and January 2016 Audit Committees.

32. During the year, Internal Audit has continued to work closely with colleagues within the Corporate Fraud Team on reviewing existing counter fraud arrangements and raising awareness of fraud risks across the Council.

### **Adding Value**

33. Although Internal Audit is primarily an assurance function, internal audit activity should also add value to the Council. The opportunities to add value are included at the planning stage for all audit activity and service areas are requested to consider how internal audit can assist. The audit reports have included areas for process improvement and have highlighted specific areas where value for money could be improved.

## **Schools**

34. The rolling programme of school audits has continued during 2015/16. During the year final reports were issued to 11 schools. The opinions given for the finalised reviews are set out at Appendix A. One school received a limited audit opinion.

## **Performance Management**

35. 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.
36. The indicators include both CBC audit activities and school activity.



## Activities for 1 April 2015 – 31 March 2016

| KPI   | Definition  | 2015/16          | 2014/15          | Our target |
|-------|---|------------------|------------------|------------|
|       |   | How we performed | How we performed |            |
| KPI01 | Percentage of total audit days completed.   | 90%              | 93%              | 80%        |
| KPI02 | Percentage of the number of planned reviews completed to final report stage.  | 75%              | 76%              | 80%        |
| KPI03 | Percentage of audit reviews completed within the planned time budget, or within a 1 day tolerance.  | 77%              | 81%              | 75%        |
| 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. | 79%              | 64%              | 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%             | 96%              | 80%        |
| KPI06 | Overall customer satisfaction.  | 93%              | 92%              | 80%        |

### 37. Analysis of indicators:

KPI01 – During the year we delivered a total of 1130 productive audit days against a total of 1260 planned days for the year. This exceeds our target for the period, but is lower than for the same period last year. This reflects that there was a vacancy within Internal Audit for the period April – end October 2015.

KPI02 – This KPI measures final reports issued as at 31 March 2016. 75% of the planned reviews had been completed to final report stage, which is below the target but consistent with the previous year, and also reflects the vacancy earlier in the year. However, this KPI does not reflect work in progress. Work is progressing on the outstanding reviews.

KPI03 – 77% of planned reviews have been completed either within the planned time budgets, or within a 1 day tolerance. This is above the target agreed for the year.

KPI04 - This indicator measures the time taken for Internal Audit to receive a response from the auditee to the draft report. During 2015/16, 79% of draft reports were responded to within the target set. This represents a significant improvement over previous years.

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

KPI06 – A total of 47 surveys have been sent out. 27 responses have been received to date. The responses received have been positive. The overall response rate was 57% to date.

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

38. 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.

39. In order to ensure that the Internal Audit Service operates in accordance with the PSIAS, the Head of Internal Audit and Risk undertakes an annual self assessment of compliance with the standards. The Accounts and Audit Regulations 2015 require that there is a review of the effectiveness of the System of Internal Audit. An external assessment was undertaken during 2015/16 by CIPFA. The outcome of the external assessment was reported to the April Audit Committee.

40. The PSIAS require the Annual Audit opinion to include a statement of conformance with the standard. Following the implementation of the recommendations made by the assessor, the Internal Audit service is fully compliant with the standards.

41. A Quality Assurance Improvement Programme (QAIP) is in place. Following the cycle of Personal Development Reviews (PDR) a comprehensive training plan for the internal audit service was collated and incorporated within the QAIP. 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, and the programme will be regularly refreshed and updated.

42. The Head of Internal Audit and Risk will continue to regularly review internal audit activity against the standards and any areas of development identified will be addressed.

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

### **Background (Accounts and Audit Regulations 2015)**

43. All councils are required to publish an Annual Governance Statement (AGS) to accompany their Statement of Accounts, in accordance with the 2015 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 2015/16 and the findings are incorporated into the Annual Audit Opinion and subsequently into the AGS.

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

44. As referred to in paragraph 39 above, a review of the Effectiveness of Internal Audit was undertaken by CIPFA.

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

45. 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
46. The Head of Internal Audit and Risk has supported the Monitoring Officer to collect evidence required for the production of the AGS.
47. Directors have signed statements on the Effectiveness of Internal Control for 2015/16, 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.

48. The work undertaken by Internal Audit on the systems of internal control disclosed that generally they were effective during 2015/16. However, some areas of concern were identified and these are summarised in paragraph 24 above, and are reflected in the Annual Governance Statement.

### **Corporate Implications**

### **Legal Implications**

49. None directly from this report.

### **Financial Implications**

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

### **Equalities Implications**

51. None directly from this report.

### **Conclusion and next Steps**

52. 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.

53. The internal control environment operated adequately during 2015/16, although some areas of concern identified in the AGS must be addressed promptly.

### **Appendices:**

Appendix A – Summary of Internal Audit Activity 2015-16

Appendix B – Audit Opinion Definitions

### **Background Papers:**

None