

## AUDIT AND RISK COMMITTEE REPORT

<b>TYPE OF REPORT:</b> Audit	<b>Portfolio:</b> Leader
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**Committee:** Resources and Performance – Audit & Risk Committee  
**Date:** 21<sup>st</sup> July 2015  
**Subject:** Internal Audit Annual Report and Opinion 2014-15

<b>Summary</b>	This report provides Members with an overview of the work undertaken by the Internal Audit Section during the 2014-15 financial year against the Strategic Audit Plan, and provides an assurance opinion to support the Annual Governance Statement
<b>Recommendation</b>	To note the report.

### 1.0 INTRODUCTION AND BACKGROUND

- 1.1 Under the Accounts and Audit 2015, the Council '*must conduct a review of the effectiveness of the system of internal control*'. The work of Internal Audit forms part of the assurance provided to Councillors and Management Team.
- 1.2 Public Sector Internal Audit Standards (PSIAS), which are mandatory for all principal local authorities and other relevant bodies subject to the Accounts and Audit Regulations 2015, state that the Audit Manager '*must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement*'. This report fulfils that requirement.
- 1.3 The Internal Audit Annual Report describes the work conducted by Internal Audit and states the Audit Manager's opinion on the system of internal control and the sources of assurance used to form this opinion.

- 1.4 To support the stated opinion, this report describes the work carried out by Internal Audit during 2014-15 and summarises the resulting findings. It also reflects on the performance against the strategic plan and the effectiveness of the internal audit team.

## **2.0 Audit Manager's Opinion**

- 2.1 This Internal Audit Annual Report provides an independent opinion on the adequacy and effectiveness of the Council's system of financial control, including in particular:

- the key controls operating within and around the core financial systems
- financial management in each Directorate and corporately
- arrangements for the letting and monitoring of contracts
- controls over information management and security.

- 2.2 On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However Internal Control systems are only designed to manage risk to a reasonable, and cost effective, level. Subsequently the Audit Manager's opinion can only provide a reasonable, not absolute, level of assurance as to the adequacy and effectiveness of these systems.

- 2.3 Bearing this in mind, in the Audit Manager's opinion, the Council's control arrangements were adequate and effective in 2014-15, with sound controls in all key areas.

## **3.0 Resources and Sources of Assurance**

- 3.1 The Internal Audit team consists of a full time Audit Manager, 1.8 FTE Auditors and 1 FTE Investigation Officer/Internal Auditor. The Audit Manager is a Chartered Member (CMIIA) of the Chartered Institute of Internal Auditors (CIIA). The Internal Auditors have either achieved a Practitioner status of the IIA or hold qualifications equivalent to the CMIIA. The Investigation Officer/ Internal Auditor is PINS (Professionalism in Security) qualified and also an Accredited Counter Fraud Manager, and is currently training as an Internal Auditor.

- 3.2 All members of the team undertake training as part of their Continued Professional Development (CPD). This can take the form of attending externally run courses or in-house provision. A list of the courses attended is attached as **Appendix 1**. The training covers not only technical audit issues, but also subjects that the team have to consider as part of the various audits. This all forms part of the 'Knowledge of the Business' that is fundamental to the conduct of constructive audits. The team are also expected to be aware of reports going to the various panels and committees.

- 3.3 Until February 2014, the team included a specialist IT auditor. To replace this resource, the Audit Manager recorded an interest in using the IT audit services provided under the Norfolk Internal Audit Consortium (based at South Norfolk District Council) contract with TIAA Ltd. There is budget provision to enable the Audit Manager to call on this resource if required as part of the Strategic Audit plan.
- 3.4 The Internal Audit service is independent of any operational responsibilities and manages its own budget. During 2014-15 line management was through the Deputy Chief Executive, but direct access to the Chief Executive, Leader or Chair of the Audit and Risk Committee was available if required.
- 3.5 Internal Audit have Terms of Reference which were approved by the Audit and Risk Committee on 25<sup>th</sup> June 2013. These describe the scope and objectives of the service, confirm the independent status, authority and standards by which the team operate, and define the responsibilities. The audit style and content, reporting lines and resources are also included. The next review is due in 2016.
- 3.6 All work in 2014-15 has been performed according to the PSIAS. The standards, which are based on the mandatory elements of the CIIA's International Professional Practices Framework, are intended to promote further improvement in the professionalism, quality, consistency and effectiveness of internal audit across the public sector.
- 3.7 To ensure the internal audit function meets the PSIAS requirements, an independent external quality assessment is required every five years. Such a review was carried out in 2014 by the CIIA and the subsequent report was presented to the Audit and Risk Committee on 28<sup>th</sup> October 2014. In summary the report concluded that the Internal Audit team conformed to 50 of the 56 principles. Of the remaining six principles, two partially conformed and four did not conform. A copy of the recommendations within the report is attached at **Appendix 2** and action taken to improve compliance is included.
- 3.8 The Audit Manager and the Council's external auditors, Ernst and Young, continue to discuss their respective work plans to ensure they complement and support each other.

#### **4.0 Basis of Assurance**

- 4.1 Each year a Strategic Audit Plan is prepared by the Audit Manager, showing specific audits for the next financial year and proposals for the next two years. This is then presented to the Audit and Risk Committee to endorse. The plan for 2014-15 was agreed on 25<sup>th</sup> February 2014.
- 4.2 When setting the Strategic Audit Plan for the year, the Audit Manager has regard for:
- Discussions with the Executive Directors
  - Internal Audit's own risk assessment system

- Corporate Risk register
- Comments from the external auditors
- Date and result of the previous audit of an area
- Any other reviews relating to specific services.

4.3 At the end of each audit a formal report is issued, containing an action plan agreed with the relevant managers to address any control weaknesses identified during the audit. The audit reports were entered in to a restricted area of InSite for members of the Management Team and the Audit and Risk Committee to view.

4.4 Each report attributes a level of assurance gained for the area being audited as below:

Full Assurance	A sound system of internal control that is likely to achieve the system objectives, and which is operating effectively in practice.
Substantial Assurance	A sound system of internal control, but there are a few weaknesses that could put achievement of system objectives at risk.
Limited Assurance	A system of internal control with a number of weaknesses likely to undermine achievement of system objectives, and which is vulnerable to abuse or error.
No Assurance	A fundamentally flawed system of internal control that is unlikely to achieve system objectives and is vulnerable to serious abuse or error.

4.5 The audit plan for 2014-15 was not fully completed by the end of March 2015. The Senior Auditor had left the Council in February 2015 and his replacement was unable to start until August 2015. This resulted in a significant reduction in resources for nearly half the year. In addition the new auditor has had to familiarise himself with the Council's systems and procedures which has inevitably meant that audits have taken longer to complete.

From November 2014 to February 2015, the Audit Manager was also absent, which again is a reduction in resources. This absence has also resulted in the late development of the 2015-16 audit plan, which was presented to the Audit and Risk Committee on 23<sup>rd</sup> June 2015. In the meantime work has continued on the outstanding audits from the 2014-15 plan.

On returning to work, the Audit Manager has reviewed the audit files completed during her absence and has assured herself that the work carried out is to the standard expected from the team.

4.6 Additional assurance has been obtained from external sources such as Bedford Borough Council (for payroll processing) and AmberOne Consultancy Services (for Health and Safety). Copies of the final reports are supplied to Internal Audit to inform the risk assessment relating to audit planning.

4.6 During the year 15 internal audit reports have been issued and assessed as shown in the table below:

<b>Audit title</b>	<b>Overall Conclusion</b>
Project to establish the Leisure Trust and Local Authority Company	Substantial assurance
Housing Benefits (2013-14)	Full assurance
King's Court Shared Accommodation	Substantial assurance
General Ledger and Budgetary Control	Substantial assurance
Environmental Quality – Flood and Water Management	Limited Assurance
NORA – Joint Venture	Substantial assurance
Cremator Refurbishment Project	Substantial assurance
Planning Support	Substantial assurance
Care and Repair	Limited Assurance
Property Services – Asbestos	Limited Assurance
Property Management – Building Maintenance	Substantial assurance
Policy and Partnerships	Substantial assurance
Democratic Services	Substantial assurance
Housing Benefits (2014-15)	Substantial assurance
Inventories and Asset Management	Substantial assurance

Each audit is followed up approximately six months after the report has been issued to establish if recommendations are being implemented in accordance with the agreed action plan. Follow-up reports for 2014-15 indicate a good level of implementation with no major concerns raised and I would like to thank all managers for being receptive to our comments and recommendations.

4.7 Progress against the strategic plan, including summaries of the reports issued and any amendments to the plan, were reported to the Audit and Risk Committee. The final report for 2014-15 was presented to the meeting on 23<sup>rd</sup> June 2015.

## **5.0 Anti-Fraud and Anti-Corruption Procedures**

5.1 The Council's Anti-Fraud and Anti-Corruption Strategy, Whistleblowing Policy and Fraud Response Plan were reviewed and updated during the year, with the final versions being approved by Cabinet in May 2014.

5.2 One abuse of position investigation was undertaken during 2014/15, which resulted in a member of staff leaving the Council. Although there was little material loss to the Council (£1,879), the investigation identified some significant control weaknesses which have now been addressed. The case was originally brought to the attention of Internal Audit by a whistleblower.

5.3 Work with the National Fraud Initiative (NFI) has continued this year. The results arising from the latest exercise were released in January 2015 and are being investigated by various sections throughout the Council as appropriate. During 2014/15 the Committee received a 6-monthly report in May 2015 from the

Investigations Manager which included a section on other matches identified by the NFI. However Benefits investigations remained the most active in this area, with very little arising from the other matches.

- 5.4 The Investigations Unit concentrated on Housing Benefit and Council Tax Benefit fraud and this role, together with two members of staff, transferred to the Department of Work and Pensions (DWP) on 1<sup>st</sup> April 2015. A final report on the results for the 2014-15 year was presented to the Audit and Risk Committee on 23<sup>rd</sup> June 2015 to conclude the service. An Investigation Officer was retained when the work transferred to maintain some investigation skills within the Council.

## **6.0 Risk Management**

- 6.1 Responsibility for risk management lies with the Senior Management Team (SMT). As well as receiving the Internal Audit reports for their respective areas, which provide an indication of any weaknesses in the control environment, the SMT also review the Corporate Risk register on a 6-monthly basis in April and October. If any significant issues arise in the intervening period, they are discussed at the time and the register amended. The Audit and Risk Committee receive the Corporate Risk Register after it has been updated at the regular 6-monthly intervals.

## **7.0 Conclusion**

- 7.1 The system of internal control is designed to manage risk to a reasonable level, and therefore cannot provide absolute assurance.
- 7.2 Notwithstanding the above, based on the audit work completed during 2014-15, it is the opinion of the Audit Manager that:
- Adequate assurance can be gained in respect of the overall systems of internal control operating within the council.
  - Risk management systems and corporate governance arrangements are satisfactory.

Training undertaken by Internal Audit 2014/15 included:

Procurement training – Specification & Selection and Contract Management  
Introduction to accounts and VAT  
Collection Fund theory  
Corporation Tax training  
ArcGIS Basics (Council's mapping software)  
Payment Card Industry Data Security Standard (PCI-DSS)  
Effective Minute taking  
Applied LEAN training  
Financial Management Risk and Financial Controls

In addition more corporate wide training was completed relating to:

- Political Awareness – Introduction to working with Councillors
- IT security
- Data Protection, Freedom of Information and Environmental Information Regulations
- Child Protection training
- Equalities – what employees need to know



### Recommendations to achieve conformance to the Standards

Standard 2010 Planning	Response & action date	Action to date
<p>To comply with the PSIAS there should be a risk-based plan which must take into account the requirement to produce an assurance framework. The risk based plan must identify how it links to organisational objectives and priorities.</p> <p>Currently there are elements that partially meet the standard eg consideration given to the Corporate Risk Register (which the Audit Manager is responsible for) but there are a number of flaws :</p> <ul style="list-style-type: none"> <li>• The internal audit's assessment of risk is done <u>after</u> the audit;</li> <li>• A standard set of risk criteria is used for every audit, regardless of the actual potential risks;</li> <li>• There was no documented linkage from the Audit Plan through to the Corporate Risks or Business Plan</li> <li>• Nine areas were identified to be fundamental and are carried out on an annual basis, and considered to "...present a significant risk...". Yet a number of the core areas are well established with robust controls in place eg payroll, sundry debtors, general ledger etc. It is probable that a number of these audits could be combined into one annual review to cover ' Finance &amp; Accounting '</li> </ul>	<p>A new method of assessing risk as part of the preparation of the Strategic Audit Plan will be established, based on the use of a risk assurance framework at a high level to produce a Council-wide assessment of risk.</p> <p>A more specific assessment at individual audit level will reflect the level of risk at the start of the audit and again after the follow-up to produce a direction of travel.</p> <p>Using the risk assurance framework, the strategic plan will be developed and where possible the planned audits will be linked to the Corporate Business Plan.</p> <p>The Core/ fundamental audits need to continue on an annual basis so that external audit can reduce the amount of testing they need to carry out. However the scope and extent of the audits will be re-considered after discussion with external auditors.</p> <p>April 2015</p>	<p>An Assurance Framework has been devised within Internal Audit and risk assessments are carried out for each service area of the Council, resulting in a grading of High, Medium or Low risk. The Strategic Audit Plan for 2015/16 has been prepared based on the results of the risk assessment.</p> <p>It was not possible to link the audit plan to a corporate business plan for 2015/16 as the latter had not been developed following the Election in May.</p> <p>However this will be used in future plans.</p>
Standard 2120 Risk Management	Response & action date	Action to date
<p>The PSIAS and this Standard requires internal audit evaluate the effectiveness and contribute to the improvement of risk management processes, a responsibility that is highlighted in the</p>	<p>The potential for re-assigning corporate risk management within a Council of this size is limited. There is no separate risk management function and historically responsibility has been allocated to Internal Audit as a</p>	<p>The role of co-ordinating the review and update of the Risk Register remains with the Audit Manager. Ultimate responsibility</p>





<p>Audit Charter.</p> <p>The Audit Manager is required to express a view upon risk management and the effectiveness of risk management, and it is recommended that within the Annual Report the Audit Manager should provide an annual opinion upon the maturity and application of risk management across the Council.</p> <p>The Audit Manager is also responsible for reviewing and updating the Council’s high level Risk Register, and securing the agreement of senior management and the Audit &amp; Risk Committee to the amendments. This moves the Audit Manager into a position where she has responsibility for the content of the Risk Register and for providing assurance on her work. This role and responsibility should be reviewed.</p> <p>The maturity of risk management within the Council was not assessed but there was no standard Council wide risk management system for internal audit to use to develop the internal audit strategy and plan. In addition the indications from interviews undertaken were that risk management is a bit fragmented across the organisation.</p> <p>To fully comply with this standard internal audit should also be more proactive in promoting risk management across the Council so that internal audit can place greater reliance on management’s view of risk when developing the internal audit strategy. Risk assessment should be a foundation when planning audits.</p>	<p>result of this lack of options. It is also noted that a review of neighbouring Councils suggests that this is not an unusual arrangement.</p> <p>It is accepted that there are some conflict of interests on the part of the Audit Manager in co-ordinating the updates for the Corporate Risk register and at the same time expressing an opinion on the adequacy of the process. However there are other methods of assessing risk management within the Council in order to gain assurance. An assessment of risk management processes can be built into most audits. This enables the Audit Manager to build up a Council-wide picture of risk management at an operational level.</p> <p>In terms of developing risk management within the Council, it is anticipated that by incorporating risk assessment into each audit, the level of risk awareness will be raised generally throughout the Council.</p> <p>April 2015</p>	<p>for the contents of the register lies with the Senior Management Team.</p>
<p><b>Standard 2201 Planning Considerations</b></p>	<p><b>Response &amp; action date</b></p>	<p><b>Action to date</b></p>
<p>The Standard requires that internal auditors in developing a plan for an engagement must consider objectives, scope, timing and resource allocation.</p> <p>Currently planning considers some of the requirements but there is a standard terms of reference to “fit all”. The file review showed that the objectives and scope did not meet the circumstances of the</p>	<p>The planning process for each audit will include an analysis of risk in the audit area. In turn this will define the scope and set the audit objectives. To assist in this process a template will be developed for use in all audits that will lead the Auditor through the process of defining the scope and identifying the objectives for the audit</p>	<p>The Terms of Reference template has been redesigned so that it can be written specifically for each audit, reflecting what elements of work lie within and outside of the</p>



<p>engagement, and in some instances were not relevant to the engagement eg the audit of Refuse &amp; recycling – the scope coverage on the terms of reference was wide but the actual work was specific to an audit of the management of the contract. The terms of reference made no mention that this was the focus of the audit.</p>	<p>within that scope. Terms of Reference will then be specifically created for each audit. April 2015</p>	<p>scope and what the objectives of the audit are. The new templates will take effect from the start of the 2015/16 audit plan.</p>
<p><b>Standard 2210 Engagement Objectives</b></p>	<p><b>Response &amp; action date</b></p>	<p><b>Action to date</b></p>
<p>This Standard requires that objectives must be established for each assignment. This happens by undertaking an assessment of the risks <i>relevant to the activity under review</i>, auditors are also to consider the probability of significant error, fraud, non-compliance and other exposures. Auditors must evaluate whether criteria needed to evaluate governance, risk management and controls.  Objectives were established but the weakness of the process was that the objectives were not always developed from a structured analysis directly linked to the activity under review.</p>	<p>As above. The risk analysis will help to define the audit objectives and guide the work of the Auditor. A template document is being devised to enable the Auditor to work through from the initial risk analysis, through scoping and identifying the audit objectives and onto preparing the audit programme.  April 2015</p>	<p>The process of establishing the objectives of the audit will entail an assessment of the risk relevant to the service being audited. To this end a Control Risk Analysis (CRA) template will used based on the PESTLE model.  A template for recording the objectives of the audit has been developed and will be used from the start of the 2015/16 plan.</p>
<p><b>Standard 2220 Engagement Scope</b></p>	<p><b>Response and action date</b></p>	<p><b>Action to date</b></p>
<p>The Standard requires that scope must be sufficient to satisfy the objectives of the engagement, and include consideration of relevant systems, records, personnel and physical properties.  The objectives and scope were combined into one paragraph which did not differentiate between the two, a standard terms of reference had a Section headed “Objectives and Scope”. Mostly the same objectives and scope being applicable to all audits. On file there was a separate document which included some elements of scope.</p>	<p>The scope of the audit will be defined by the results of the risk analysis and consideration of any other more cross-cutting corporate audits. For example an audit of Accounts Receivable will impact on the audit of any area that receives income.  April 2015</p>	<p>The scope of the audit defines what aspects are included and what will not be covered by the audit.  A template for recording the scope of the audit has been developed and will be used from the start of the 2015/16 plan</p>



<b>Standard 2240 Engagement Work Programme</b>	<b>Response and action date</b>	<b>Action to date</b>
<p>The Standard requires that the auditors must develop and document work programmes that achieve the engagements objectives. This will include procedures for identifying , analysing, evaluating and documenting information about the assignment. It must be approved prior to its implementation</p> <p>This document is developed from analysing and consolidating the results of preliminary work – the planning, the objectives and the scope. It is a road map for the fieldwork which properly developed and used will contribute to an efficient and effective audit</p>	<p>Once the scope and objectives of an audit have been defined, an audit plan will be created, stating how the audit will be conducted.</p> <p>April 2015</p>	<p>Once the scope and objectives have been defined, an audit programme can be prepared detailing what testing will be done and for what purpose. Again a template has been developed, which will be used for the start of the 2015/16 audit plan.</p>