

AUDIT COMMITTEE

Internal Audit Annual Report and Assurance Statement 2013/14 18 June 2014

Report of Internal Audit Manager

PURPOSE OF REPORT

To inform the Committee of the extent and outcome of Internal Audit work during the 2013/14 financial year and to present an annual Statement of Assurance regarding the Council's framework of governance, risk management and control.

This report is public

RECOMMENDATIONS

1. That the report be noted.
2. That the Internal Audit Manager's Assurance Statement and Annual Internal Audit Opinion (paragraphs 2.20 to 2.35) be accepted and considered by the Committee in relation to the annual governance review and Annual Governance Statement, which will be presented to the September meeting of the Committee.
3. That Members consider and provide initial views on the requirement for an external assessment of Internal Audit's compliance with proper practice standards (as set out in paragraphs 2.13 to 2.16)

1.0 Introduction

- 1.1 The terms of reference of the Audit Committee include: *To receive the annual Internal Audit Report and Controls Assurance Statement (the Constitution, part 3 section 8, TOR 11).*
- 1.2 Proper practices for Internal Audit in local government¹ specify that *"The chief audit executive (the Internal Audit Manager) must deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement", and that "The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control."*

¹ *Public Sector Internal Audit Standards (PSIAS) and Local Government Application Note (LGAN) (CIPFA 2013)*

2.0 Report

Annual Audit Plan 2013/14

- 2.1 Internal Audit plans and assignments are developed on a risk-based approach, seeking to identify and devote resources to the areas of greatest significance to the Council. The 2013/14 Internal Audit Plan was approved by the Audit Committee at its meeting on 24th April 2013. Adjustments to the plan were approved by the Committee at its meetings on 26th June 2013, 18th September 2013 and 22nd January 2014.
- 2.2 The annual outturn position against the 2013/14 annual plan is summarised in the following table.

Area of work	Resources (days)		
	Original Plan	Revised Plan (22/01/14)	Actuals
Assurance Audit			
Core Financial Systems	100	38	33
Revenues & Benefits Shared Services	60	76	86
Core Management Arrangements	80	55	28
Risk Based Assurance Audits	140	217	248
Follow-Up Reviews	60	66	64
Sub-Total, Assurance Work	440	452	459
Advice & Support Work	105	90	98
Corporate Service Reviews	0	50	37
Investigations	30	25	16
Audit Management	50	50	57
Other Duties (Non-Audit)	15	8	7
Work for Other Bodies (LDNPA)	10	25	26
General Contingency	40	5	0
Total Chargeable Days	690	705	700
Non-Chargeable Activities (note1)	108	109	117
Total Available Days	798	814	817

Note 1. Non-chargeable activities include team meetings, section and service management, general administration, EDPA, regional audit group meetings, etc.

Explanation of Major Variances

- 2.3 The summary shows that the number of available days increased by 19, this primarily being due to the section not having recorded any sick leave during the year. The number of chargeable days delivered were up by 10 on the original plan.
- 2.4 Within the main programme of assurance work, there was a significant re-direction of resources to the Risk Based Audit section. This reflected the identification of a number of emerging risk areas during the year and a commitment to some wide-ranging reviews, including one of corporate "working time arrangements" and another programme considering arrangements for fees and charges across the Council.
- 2.5 Overall, 19 more days than originally planned were delivered on the core programme of assurance audit work.

- 2.6 Outside of the core assurance programme, a new area of work was added to the plan during the year relating to work on 'Corporate Service Reviews'. This reflects the increasing financial pressures on the council and the associated need to reorganise operations, identify efficiencies and make savings. Whilst the number of days actually delivered in this area of work (37) was less than envisaged, Internal Audit has an ongoing involvement in reviews which will continue throughout 2014/15. Further proposals to provide resources for this type of work are made in the Internal Audit Plans elsewhere on this agenda.
- 2.7 As reported to the Committee during the year, the Internal Audit team provided the Lake District National Park Authority with part of its internal audit service for 2013/14, this amounting to 26 days of work. This arrangement has operated very successfully and the proposed Internal Audit Plan elsewhere on the agenda refers to arrangements to extend the service during the current financial year.
- 2.8 Elsewhere in the plan, there has been little call for formal investigative work and no other major variations in workload. The general contingency of 40 days has been sufficient to cover any changes.

Compliance with Professional Standards

- 2.9 From 1st April 2013, Internal Audit in local government is required to be established and operate in accordance with 'proper practices' as set out in the *Public Sector Internal Audit Standards (PSIAS)* and the associated *Local Government Application Note (LGAN) (CIPFA 2013)*.
- 2.10 The PSIAS require the Internal Audit Manager to maintain a 'Quality Assurance and Improvement Programme' (QAIP) which includes periodical internal and external assessments of compliance with the Standards. Furthermore, standard 1322 of the PSIAS requires the council to consider disclosing any significant deviations in its annual Governance Statement.
- 2.11 The most recent internal assessment was reported to the Audit Committee's meeting on 22nd January 2014. At that meeting, Members approved a revised Internal Audit Charter, considered the results of the internal assessment and noted the resulting action plan. Based on this most recent assessment, full compliance with the PSIAS and LGAN has not as yet been achieved. However, it is the Internal Audit Manager's view that none of the points of non-compliance or partial compliance represent a deviation of such significance as to warrant disclosure in the annual Governance Statement.
- 2.12 The next monitoring and internal assessment of compliance with the PSIAS is scheduled to take place during the summer and the results will be included in the information provided to the September 2014 meeting of the Audit Committee to consider its annual review of the effectiveness of Internal Audit (as mentioned in § 2.17 below). This self-assessment will review the position on all areas of non-compliance and re-consider whether there is a need to disclose in the Governance Statement.

External Assessments

- 2.13 Advice received from CIPFA is that the first external assessments, which are required every five years by the PSIAS, should have been undertaken by 1st April 2016. External assessments must be carried out by a competent assessor or assessment team, but within this constraint, the selection of assessor, as well as the form and scope of the assessment, is a matter for the Internal Audit Manager to discuss and agree with the Audit Committee.
- 2.14 This requirement is being considered collectively by the heads of Internal Audit of the 15 Lancashire local authorities comprising the Lancashire Chief Auditors Group, with the two main options identified being:

- a) Engaging a professional third party accountancy/audit provider; or
- b) Setting up a programme of peer reviews within the Lancashire districts.

2.15 At this stage, each head of Internal Audit has agreed to seek the initial views of their authority's key sponsors of internal audit, i.e. the chief financial officer and the Audit Committee (or equivalent). Whilst it is not possible at present to say what level of resources (and cost) the assessment would entail, the outline advantages, disadvantages and risks associated with these two options are set out in the following table.

	Option 1 Third Party Provider	Option 2 Peer Review
Advantages	Organisational independence and freedom from any conflict of interest.	Independence can be built through having peer groups of three or more, with rotation of roles.
		Reciprocal arrangement - no additional financial cost.
	Potential for the authority to learn from the provider's experiences and knowledge.	Potential for the authority to learn from its peers' shared experiences and knowledge.
		Opportunity for IA managers to develop skills, knowledge and experience.
Disadvantages	Cost of engaging a provider (currently unbudgeted) Note: Some economies of scale might be achievable if services are procured on behalf of group of authorities	Additional workload when providing peer review service to other authorities.
	Provides limited potential for staff development.	
Risks		The robustness of the assessment might diminish if sufficient independence is not established. (Low)
		Additional workload might impact IA plans and provision of assurance (Low)





2.16 At this stage, Members are asked to consider the above and provide views and direction to the Internal Audit Manager to feed into the deliberations of the Lancashire Chief Auditors Group.

Review of the Effectiveness of Internal Audit

- 2.17 The Accounts & Audit (England) Regulations 2011 require the Council to conduct an annual review of the effectiveness of internal audit and for a committee of the Council to consider the findings. This process is part of the wider annual review of the effectiveness of the system of internal control and governance. A report on this review will be included within the report on the annual review of governance to be considered at the next meeting of the Committee in September 2014.

Results of Assurance Work





- 2.18 In all cases, completed assurance audits have resulted in the production of a report and action plan, agreed by managers and submitted for consideration by the Audit Committee. The assurance system uses four levels of opinion, as follows:

Level of assurance	Image	Definition
Maximum		The Authority can place high levels of reliance on the arrangements/controls. Best practice is demonstrated in some or all areas.
Substantial		The Authority can place substantial (i.e. sufficient) reliance on the arrangements/controls. Only relatively minor control weaknesses exist.
Limited		The Authority can place only limited reliance on the arrangements/controls. Significant control issues need to be resolved.
Minimal		The Authority cannot place sufficient reliance on the arrangements/controls. Substantial control weaknesses exist.

- 2.19 The Table in Appendix A sets out the assurance opinions issued from audits and follow-up reviews completed since 31st March 2013, and any subsequent changes in assurance level.

Assurance Statement

- 2.20 It must be recognised that Internal Audit can be expected to provide reasonable and not absolute assurance that risk is being effectively managed and that control weaknesses or irregularities do not exist.
- 2.21 This assurance statement is drawn from both the results of individual internal audit assignments and the results of follow-up reviews into previously completed audits, as reflected in the contents of Appendix A. The following table summarises the assurance opinions covered in the appendix, based on the most recent review, with the previous year's totals, for comparison.

Assurance Level (most recent review)	Number of Audit Opinions				
	2013/14				2012/13
	Financial Audits	Governance Audits	Other Audits	Total	
Maximum 	1	0	0	1	1
Substantial 	12	1	5	18	17
Limited 	3	1	5	9	6
Minimal 	0	0	0	0	1
Totals	16	2	10	28	25

- 2.22 Through established procedures, the Audit Committee will continue to receive updates on progress with those audits which have not reached at least the “substantial” assurance level. At present this consists of the nine audits listed in Appendix A whose assurance ratings stand as “limited”.
- 2.23 In addition to these audits, the assurance opinion on an audit of “Information Security and Use of Emails” from the 2012/13 audit programme has not yet been raised from its original level of “Minimal”. A formal review of this audit has been on hold pending completion of the significant body of work required over the past 12 months by the ICT service to meet organisational and technical requirements relating to the Government’s Public Services Network (PSN). Having achieved the necessary accreditation in May 2014, there remains a body of work to be picked up regarding wider corporate information governance arrangements. A formal review of the original audit findings will be undertaken in the coming months and the results reported to the Audit Committee.
- 2.24 These procedures for reporting and following up audits and reporting progress to Audit Committee continue to operate effectively.

Financial Systems Audits

- 2.25 This relates to sixteen financial system audits, including six audits relating to the council’s various income streams and the associated fees and charges. Assurance levels on the Council’s core financial systems remain consistently high. A “maximum” assurance opinion was issued in relation to the council’s arrangement surrounding Housing Benefit and Welfare Reforms. Three audits resulted in a “limited” assurance opinion, these being in relation to:
- Purchase ordering and creditor payment processes – Environmental Services;
 - Debt Management – Council Housing; and
 - Grounds Maintenance, Nursery and Cleansing Income Streams.
- 2.26 In the first two of these, systems are being reviewed under projects within the council’s programme of service reviews. Internal Audit is playing an active role in one of these projects and keeping a ‘watching brief’ on the other. It is anticipated that these pieces of work will over time subsume or supersede the outcomes and action plans from the original audits. In the case of the Grounds Maintenance, Nursery and Cleansing Income Streams audit, whilst some of the operations covered may also be affected by service reviews; a formal follow-up of the audit will be undertaken as scheduled in January 2015.
- 2.27 Given the work undertaken, it is the Internal Audit Manager’s opinion that effective internal controls exist to ensure the accuracy and integrity of the key financial systems and that no significant unmanaged risks or ongoing control weaknesses have been identified.

Governance Arrangements

- 2.28 An updated assurance opinion of “substantial” was issued during the year following a second follow-up of a 2012/13 audit of the council’s complaints policy and procedures, which had originally been assessed as “minimal”.
- 2.29 An audit of arrangements relating to officer gifts, hospitality and interests resulted in an opinion of “limited”, reflecting a need to strengthen the role of managers, raise awareness generally and promote greater consistency across the authority.
- 2.30 There remain a number of outstanding considerations from earlier audit work relating to the council’s information governance arrangements (referred to in § 2.23).

- 2.31 In the Internal Audit Manager's opinion, the remaining issues surrounding information governance arrangements, and recognition of the council's achievements in achieving PSN compliance, warrant specific mention in the annual governance statement.

Other Audits

- 2.32 This section covers ten audits, five of which resulted in a "limited" assurance opinion, these being in relation to:
- Salt Ayre Sports Centre, Williamson Park and Other Recreational Facilities – Income Streams;
 - Working Time Arrangements;
 - CCTV;
 - Corporate Property Related Service Contracts; and
 - Affordable Warmth.
- 2.33 Again, the first three of these areas are under consideration in service reviews and arrangements have been made to feed the results of audit work in to those pieces of work.
- 2.34 In the Internal Audit Manager's opinion, no unmanaged risks or control weaknesses have been identified which are so significant as to warrant disclosure in the Council's Annual Governance Statement. Where weaknesses have been identified, remedial action has been agreed and arrangements are in place to monitor the implementation of those actions and the level of assurance provided.

Annual Internal Audit Opinion

- 2.35 Drawing on the work undertaken and the above summaries, it is the Internal Audit Manager's opinion that, subject to the individual matters highlighted, the council has reliable and effective framework of governance, risk management and control.

3.0 Details of Consultation

- 3.1 No specific consultation has been undertaken in compiling this report.

4.0 Options and Options Analysis (including risk assessment)

- 4.1 The proposal is that the Committee accepts the Internal Audit Manager's assurance statement as a contribution to the overall assessment of the internal control environment and the Annual Governance Statement. No alternative options are identified.

5.0 Conclusion

- 5.1 The work of Internal Audit seeks to provide assurance to the Council as to the appropriateness and effectiveness of its internal control and corporate governance arrangements. During the 2013/14 financial year, Internal Audit's work has provided assurance in a variety of areas as well as incorporating input and contribution to the development of a number of key systems and processes and the conduct of service reviews.

CONCLUSION OF IMPACT ASSESSMENT

(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)

This report has no direct impact on these areas.

FINANCIAL IMPLICATIONS

None arising directly from this report.

SECTION 151 OFFICER'S COMMENTS

The Section 151 Officer has been consulted and has no further comments.

LEGAL IMPLICATIONS

None arising from this report

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and has no further comments.

BACKGROUND PAPERS

Internal Audit Plan 2013/14

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