

# AUDIT COMMITTEE

## Internal Audit Annual Report 2018-19

12 June 2019

### Report of the Internal Audit and Assurance Manager

#### PURPOSE OF REPORT

To approve the Internal Audit Annual report for 2018/19.

**This report is public**

#### RECOMMENDATIONS

1. **That the Internal Audit and Assurance Manager's (IAAM) Internal Audit Annual Report for 2018/19 be accepted and considered by the Committee as a key source of assurance which will be reported in the Annual Governance Statement (AGS), which is to be considered by the Committee later in the agenda.**

#### 1.0 Introduction

1.1 The Internal Audit Annual Report is produced in order to meet the requirements of the Public Sector Internal Audit Standards and to assist in meeting the Accounts and Audit Regulations 2015. The report provides details of audit coverage and of the work carried out by the section and contains the IAAM opinion of the overall level of control in operation.

1.2 The Audit Committee's role in relation to reviewing the work carried out includes formal consideration of summaries of work done, key findings, issues of concern and actions in hand as a result of audit work. A key part of the role is receiving and reviewing regular reports from the IAAM in order to reach an overall opinion on the internal control environment and the quality of internal audit coverage. The Audit Committee has a clear role in relation to the authority's internal audit function and this involves:

- Formally approving, but not directing, the overall strategy to ensure that it meets the council's overall strategic direction;
- Agreeing the annual audit plan (paying particular attention to whether there is sufficient and appropriate coverage); and
- Monitoring progress against the plan and assessing whether adequate skills and resources are available to provide an effective audit function.

#### 2.0 Proposal Details

2.1 The Internal Audit Annual Report attached at Appendix A seeks to demonstrate that effective leadership of audit and governance are in place across the organisation and that the necessary arrangements are in place to maintain a sound system of internal 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 IAAM's Internal Audit Annual Report as a contribution to the overall assessment of the internal control environment and the AGS.

4.2 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, risk management and corporate governance arrangements. During the 2018/19 financial year, internal audit's work has gained the necessary assurances to be able to state the council has in place satisfactory controls to be able to maintain an adequate and effective internal control environment. However it should be noted that the IAAM has stated that risk management should be reported in the Council's AGS for the year 2018/19 as an area requiring attention.

### **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 directly from this report.

### **MONITORING OFFICER'S COMMENTS**

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

### **BACKGROUND PAPERS**

Internal Audit Plan 2018/19

**Contact Officer:** Joanne Billington

**Telephone:** 01524 582028

**E-mail:** jbillington@lancaster.gov.uk

**Ref:**

**INTERNAL AUDIT ANNUAL REPORT 2018/19**

The Internal Audit and Assurance Section is responsible to the Head of Financial Services (S151 Officer) for carrying out a continuous examination of the accounting, financial and other operations of the council in accordance with Section 151 of the Local Government Act 1972 and the Accounts and Audit Regulations 2015. The latter states that **'A relevant authority must ensure that it has a sound system of internal control which facilitates the effective exercise of its functions and the achievement of its aims and objectives, ensures that the financial and operational management of the authority is effective and includes effective arrangements for the management of risk'**.

Members of the Audit Committee should note that copies of internal audit reports are published on the council's intranet. Access to the supporting files is available to members of the Audit Committee on request.

Lancaster City Council continues to be represented on the Lancashire District Council's Audit Group and we continue to participate in the National Fraud Initiative data sharing exercise.

Internal Audit continues to provide the council with the necessary assurance about its various activities and associated systems, as outlined in the council's Internal Audit Strategy and Audit Charter. In addition, the audit service has received validation following a peer review on its self-assessment of effectiveness of internal audit. Details of this peer review can be found later in this report.

The allocation of audit days for 2018/19 was originally 464 days. However, following the resignation of the Deputy IAAM in December 2018 and a discussion around the risks in each instance, a decision was made to roll six audits to the following 2019/20 audit plan. In addition, two pieces of work (20 days) were completed by Fylde Council covering council housing; asbestos management and pre-employment checks at a daily rate of £365.

Internal feedback is requested after each audit review. All feedback received in 2018/19 indicated that the work of internal audit continues to be highly regarded.

## Audit Work Performed in 2018 / 2019

Summarised below are the reviews that have been performed and reports issued in 2018/19. Final reports are published in full on the Council's Intranet site.

### Lancaster City Council

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.

### Fylde and Preston City Council

Level of assurance	Image	Definition
Full		There is a sound system of control designed to achieve the system objectives and manage the risks to achieving those objectives.
Substantial		While there is basically a sound system of control, there are some minor weaknesses, which may put some of the system objectives at risk.
Moderate		While there is basically a sound system of control, there are some more significant/serious weaknesses, which may put some of the system objectives at risk.
Limited / None		There are significant weaknesses in key areas in the systems of control, which put the system objectives at risk and leaves the system open to significant error or abuse.

**2017/18 Audit Plan Work Finalised in 2018/19**

TITLE	STATUS	Level of Assurance	Summary
<b>Budgetary Control</b>	<b>Final Report Issued October 2018</b>	<b>Substantial</b> 	Substantial assurance has been given on the basis that good controls are in place to ensure that budgets are set, monitored and controlled effectively. However, controls surrounding the appointing and training of Responsible Spending Officers need to be strengthened to ensure that they have the understanding, knowledge and skills to facilitate effective financial management and are fully conversant with their roles and responsibilities. Actions have been agreed to address this.
<b>Main Accounting</b>	<b>Final Report Issued July 2018</b>	<b>Substantial</b> 	Substantial assurance has been given on the basis that arrangements for ensuring the accurate, authorised and efficient recording of financial transactions in the general ledger are robust, with only minor issues identified for improvement.
<b>Salt Ayre Leisure Centre</b>	<b>Final Report Issued April 2018</b>	<b>Substantial</b> 	Substantial assurance has been provided on the basis that the collection, storage and banking of income at the Centre is generally well controlled. A number of areas were identified where arrangements could be strengthened, however the majority of these were addressed during the course of the audit, staff being keen to make improvements necessary. Actions have been agreed to address the small number of issues which remain outstanding, all of which are planned for implementation by the end of the financial year.
<b>Housing Benefit E-Claim</b>	<b>Final Report Issued May 2018</b>	<b>Substantial</b> 	Substantial assurance has been awarded on the basis that the processes surrounding the online housing benefit e-claim form are sufficiently robust and the module is fit for purpose.
<b>Procurement and Contract Management Arrangements</b>	<b>Final Report Issued September 2018</b>	<b>Limited</b> 	Limited assurance has been given on the basis that there are a number of significant control weaknesses that need to be addressed. Procurement and contract management arrangements require improvement with a view to ensuring that the council maximises savings and quality of service, while ensuring that all parties involved in the contract fully understand their obligations and responsibilities and fulfil them as efficiently and effectively as possible.

			A further follow-up review is therefore to be carried out in June 2019.
<b>Performance Management</b>	<b>Final Report Issued May 2018</b>	<b>Limited</b> 	<p>Limited assurance has been given on the basis that whilst a performance management framework is in place, it is not yet fully embedded, this being in part due some recent revisions to its key elements. Consistent quarterly reporting has now been introduced, but current indicators are in need of review to ensure they align with the new Council Plan, and there is scope to improve arrangements for the collection and reporting of data. Accountability also needs strengthening. An action plan has been agreed with a view to improving arrangements, which once implemented should result in substantial assurance being provided.</p> <p>A further follow-up review has now been completed. See below.</p>
<b>Learning and Development</b>	<b>Final Report Issued May 2018</b>	<b>Limited</b> 	<p>Arrangements are in place to ensure the council is compliant with statutory requirements in relation to the Apprenticeship Levy. The role of line managers in developing staff is clearly understood, and measures are being taken with a view to identifying learning and development needs of the workforce. However, there is scope to improve arrangements for maximising current investment in learning and development activity. Aims and objectives for developing the skills, knowledge and competencies of staff also need to be clearly defined. A learning and development officer is to be appointed in the near future who will play a key role in taking forward the agreed actions, which once implemented should result in a substantial assurance being provided.</p> <p>A further follow-up review is therefore to be carried out in July 2019.</p>
<b>2018/19 Audit Plan Work</b>			
<b>TITLE</b>	<b>STATUS</b>	<b>Level of Assurance</b>	<b>Summary</b>
<b>Treasury Management</b>	<b>Final Report Issued December 2018</b>	<b>Substantial</b> 	Substantial assurance has been provided on the basis that the council's arrangements for ensuring compliance with CIPFA principles and recommendations on Treasury Management are robust, and associated risks are well managed.

<b>Disabled Facilities Grant</b>	<b>Final Report Issued May 2018</b>	<b>Substantial</b> ✓	Substantial assurance has been given as robust arrangements and processes are in place for administering grants in accordance with legislation. Effective arrangements are also in place to maximise increased funding allocations.
<b>Pre-Employment Checks</b>	<b>Draft Report Issued</b>	<b>Substantial</b> ✓	This piece of work was carried out by Fylde Council. Their work established that the controls in place in relation to the pre-employment checks are generally operating effectively and that the 1 <sup>st</sup> line of defence is reliable. Members of the HR Team are knowledgeable and experienced, and have developed a comprehensive recruitment policy, procedures and guidance for managers to follow. There are a couple of minor improvements which should be considered and for this reason, a substantial assurance rating has been awarded.
<b>Election Accounts</b>	<b>Final Report Issued September 2018</b>	<b>Substantial</b> ✓	Substantial assurance has been given on the basis that good controls were in place in relation to the financial administration of both the County Council and the Parliamentary elections that took place in 2017.
<b>Council House – Gas Safety</b>	<b>Final Report Issued October 2018</b>	<b>Substantial</b> ✓	Substantial assurance has been given on the basis that good arrangements are in place to ensure the council, as a landlord, complies with the requirements of the Gas Safety Regulations. An effective gas safety maintenance programme has been developed, and arrangements for ensuring gas safety checks take place are robust. There is scope to further strengthen arrangements in relation to record keeping, and there is potential to improve the efficiency of current procedures through the use of a more automated system. Actions have been agreed to address these issues.
<b>Council Tax Lancaster</b>	<b>Final Report Issued March 2019</b>	<b>Substantial</b> ✓	Substantial assurance has been given on the basis that the Authority has good systems and processes in place to ensure that council tax transactions are appropriate, correct and effectively managed. There is scope to strengthen arrangements further in relation to evidencing the checks carried out when determining liability, discounts and exemptions and controls surrounding the suspense account. Actions have been agreed to address these issues.
<b>Housing Benefit Lancaster</b>	<b>Final Report Issued August 2018</b>	<b>Substantial</b> ✓	Substantial assurance has been given on the basis that manual payments made between 16/07/18 and 03/08/18 have been calculated and administered in accordance with guidance provided.

<b>Creditors</b>	<b>Final Report Issued May 2019</b>	<b>Limited</b> 	Limited assurance has been given on the basis that there are some significant control issues that have been identified that need to be resolved to ensure that creditor transactions are appropriate, correct and effectively managed. An action plan addressing all concerns raised has been produced and is to be delivered as part of the ongoing 'purchase to pay' lean process review currently being carried out in partnership with consultants - Ad Esse.  A further follow-up review is therefore to be carried out in August 2019.
<b>Payroll</b>	<b>Draft Report Issued</b>	<b>Limited</b> 	Limited assurance has been given on the basis that there are a number of significant control weaknesses that need to be addressed. Actions are in the process of being agreed which when implemented will address all concerns raised.  A further follow-up review is therefore to be carried out in Oct/Nov 2019.
<b>Council Housing – Asbestos Management</b>	<b>Final Report Issued May 2019</b>	<b>Moderate</b> 	This piece of work was carried out by Fylde Council. Their work established that the controls in place in relation to asbestos management are generally operating effectively and that the 1st line of defence is reliable. Staff in the Repairs and Maintenance Section are knowledgeable, experienced and well trained in managing the risk of asbestos, and have developed comprehensive asbestos policy, procedures and guidance for both managers and staff to follow. The review highlighted some areas for improvement and for this reason, a Moderate assurance rating has been awarded.  A further follow-up review is therefore to be carried out in August 2019.
<b>White Lund Nursery Income Management</b>	<b>Final Report Issued July 2018</b>	<b>Limited</b> 	Limited assurance has been given on the basis that the lack of clear policies and procedures, roles and responsibilities and appropriate training for staff working at the Nursery, leave the council vulnerable to inappropriate/unauthorised transactions taking place and/or theft of income.  A further follow-up review has now been completed. See below.
<b>Dog Seizure and Kennelling Service</b>	<b>Final Report Issued November 2018</b>	<b>Limited</b> 	Limited assurance has been given on the basis that there are a number of significant control weaknesses that need to be addressed. Policies and procedures covering dog seizure and kennelling arrangements need to be

			fully reviewed with a view to ensuring that arrangements are clear, open and transparent and can be consistently applied. A number of actions have therefore been agreed which when implemented will address all concerns identified during the course of the review. A further follow-up review is therefore to be carried out in June 2019.
<b>Insurance</b>	<b>Fieldwork in Progress</b>	<b>Unknown</b>	A report will be published in July 2019
<b>VAT</b>	<b>Fieldwork in Progress</b>	<b>Unknown</b>	A report will be published in July 2019

<b>Follow-up work completed in 2018/19</b>			
<b>TITLE</b>	<b>STATUS</b>	<b>Level of Assurance</b>	<b>Summary</b>
<b>White Lund Nursery</b>	<b>Final Report Issued March 2019</b>	<b>Limited</b> 	Whilst the majority of agreed actions have been implemented effectively and considerable work has been completed to introduce training manuals and strengthen procedures and processes, there are still a number of issues surrounding the consistency of their application, and for that reason a limited assurance opinion has been provided.  A further follow-up review is therefore to be carried out in July 2019.
<b>Asset Management</b>	<b>Final Report Issued December 2018</b>	<b>Limited</b> 	Whilst there has been good progress with implementation of the agreed action plan, a number of key actions are still in the process of being implemented. Therefore, the level of assurance which can be provided at present remains at limited. Revised target implementation dates have been agreed to take into account work in progress, which once complete should result in substantial assurance being provided.  A further follow-up review is therefore to be carried out in July 2019.

<b>Performance Management</b>	<b>Final Report Issued December 2018</b>	<b>Limited</b> 	<p>Whilst there has been good progress with implementation of the agreed action plan, a number of key actions are still in the process of being implemented, or have yet to be addressed. Therefore, it is Internal Audit's view that the level of assurance which can be provided at present remains at limited.</p> <p>A further follow-up review is therefore to be carried out in July 2019.</p>
-------------------------------	--	---	--

**Other work completed in 2018/19**

<b>TITLE</b>	<b>STATUS</b>	<b>Level of Assurance</b>	<b>Summary</b>
<b>Canal Quarter – Health Check</b>	<b>No Report Issued</b>	<b>N/A</b>	Internal Audit attended a number of officer group meetings in a project assurance role. Regular health checks will continue once the project is underway.
<b>Pest Control</b>	<b>Position Statement Issued</b>	<b>N/A</b>	Whilst Pest Control was identified as a piece of work to be completed in the 2018/19 Audit Plan, the service had recently undergone an external assessment which had provided adequate assurances and therefore an audit was not considered necessary.
<b>Council Housing Voids</b>	<b>Position Statement Issued</b>	<b>N/A</b>	The Council commissioned an external body to carry out an extensive lean system review. A comprehensive action plan was produced and Internal Audit will monitor the implementation of the actions periodically.
<b>Ethical Governance Survey</b>	<b>No Report Issued</b>	<b>N/A</b>	An ethical governance survey has recently been completed by the Internal Audit Team to test staff knowledge and understanding of the Council's key counter fraud policies. An action plan of the findings and any subsequent actions required to address any gaps in knowledge and understanding will be published in July 2019.

## **Other audit work undertaken:**

### **Investigations**

There have been no internal investigations carried out by Internal Audit or the Corporate Enquiry Team during 2018/19.

### **Corporate Enquiry Team**

The Council has a duty to protect public funds and has a shared Corporate Fraud Team with Preston and Fylde Councils. The team is called the Corporate Enquiry Team and its role is to investigate allegations of fraud against the Council, undertake pro-active investigations in high risk areas, act as single point of contact between the Council and the Department for Work and Pensions fraud team and to participate in multi agency working to prevent and detect crime with partner agencies. A detailed report of the outcomes will be reported to the Audit Committee and is attached later in this agenda.

### **Information governance – judgement of security and use of business assets**

The Council's Information Governance (IG) Team continue to work on compliance with the General Data Protection Regulations which came into force on the 25 May 2018. Whilst a considerable amount of work has been completed, the team are still working through the comprehensive action plan and the Information Governance Manager has highlighted that there is still a lot of work to be completed to ensure the Council is GDPR compliant.

This year, the IG Team have had to respond to Council Departments numerous requests for assistance with essential project work. This has taken resource away from the IG action plan. In addition, the team have had to dedicate a significant amount of resource on management of the Council's FOI Requests as the Council has seen a 20% increase in FOI requests from 2017/18 to 2018/19.

### **Counter Fraud and Corruption Policies**

The Council has a number of counter fraud polices in place across the organisation, namely; Raising Concerns at Work, Gifts, Hospitality and Registering Interests Policy, Anti-Money Laundering, Corporate Prosecution Policy. Whilst some of these polices are managed and reviewed by the Internal Audit Team and the Corporate Enquiry Team, and are therefore subjected to regular review and approval by the Audit Committee, a number of the council's counter-fraud polices sit with other services, e.g. Human Resources and Democratic Services and therefore may not be subject to regular review.

Given the Audit Committee have delegated responsibility for ensuring adequate counter fraud arrangements are in place throughout the organisation, and Internal Audit is an independent, objective body, it is in my opinion that all the council's counter fraud polices, should sit with either the Internal Audit Team or the Corporate Enquiry Team to ensure they are regularly updated, approved and rolled out to all staff. This has been highlighted as a weaknesses in the 'minor issues' action plan of the Annual Governance Statement for 2018/19.

## **Effectiveness of Internal Audit Review**

In accordance with the Accounts and Audit Regulations 2015, paragraph 6 (1) requires the relevant body, each financial year to conduct a review of the effectiveness of its system of internal audit. The review recognises the important role that internal audit play in the assurance process and the need to continually ensure that it remains effective. The last self-assessment was carried out in May 2019 (and is attached later in this agenda) using the 'Public Sector Internal Audit Standards' and 'Local Government Guidance Note' issued by CIPFA. Although overall compliance has been achieved, one minor observation has been made and this will be addressed immediately. In addition, there are a number of 'partial' completed actions in relation to risk management. Actions in relation to risk will be documented in more detail in the Annual Governance Statement minor issues action plan and will be subsequently monitored by the Executive Team and Internal Audit.

In order to comply with the PSIAS an external assessment must be conducted at least once every five years by a qualified independent assessor or assessment team from outside the organisation. External assessments can be in the form of a full external assessment (peer review), or a self-assessment in-house with independent external validation. It was agreed by the Lancashire District Chief Auditors group and validated by the Audit Committee, that peer reviews would be used to obtain the independent external validation. Lancaster City Council's assessment was completed in March 2018. The peer review team (Allerdale Borough Council and Burnley Borough Council) concluded that the Internal Audit Team are fully compliant with the PSIAS. The report was presented to the Audit Committee in May 2018. Only four minor areas were identified, all of which have been considered and implemented where appropriate.

## **Quality Assurance Improvement Programme**

In accordance with the PSIAS, the Chief Internal Auditor (Internal Audit and Assurance Manager) must develop and maintain a quality assurance and improvement programme (QAIP) that covers all aspects of the internal audit activity. The QAIP must include both internal; and external assessments.

The internal assessments include the following:

- An annual self-assessment of the effectiveness of the audit service using the PSIAS; and
- Day-to-day monitoring of compliance with the Definition of Internal Auditing and the Code of Ethics documented within the section's Audit Charter and also in the PSIAS.

### External assessments include:

- A 5 yearly independent assessment of compliance to the PSIAS;
- An annual review of the Council's Annual Governance Statement which accompanies the Statement of Accounts;
- Regular attendance at the Audit Committee by the Council's External Auditor with the opportunity to meet in private with the Committee; and
- The External Auditors and the Audit Committee review and challenge all internal audit reports.

### **Compliance to the Public Sector International Audit Standards (PSIAS)**

In April 2014, the International Standard setters developed a comprehensive set of standards (PSIAS) that are expected to be in place within any effective audit organisation. The PSIAS replaced CIPFA's 'Code of Practice for Internal Audit in Local Government'. The PSIAS requires that areas of non-compliance with the PSIAS Definition of Internal Auditing and the Code of Ethics are reported in the Annual Audit report and that significant deviation requires inclusion in the Council's Annual Governance Statement. It should be noted that following the external validation in March 2018 and the self-assessment in May 2019, there are no deviations to report in the 2018/19 Annual Governance Statement.

### **Internal Control System**

In accordance with the Accounts and Audit Regulations 2015, Internal Audit is required to form an opinion on the adequacy and effectiveness of the council's internal control environment, which includes consideration of any significant risk or governance issues and control failures that have been identified throughout the year.

In providing an overall opinion on the council's system of internal control, it should be noted that assurance can never be absolute. Internal Audit can only provide reasonable assurance that there are no major weaknesses in the areas reviewed. In arriving at an opinion, consideration is given to;

- The findings from the audit work undertaken during the year;
- The amount of audit work undertaken in the year compared with work planned;
- The results of follow up action in respect of audit work;
- Whether or not any significant recommendations have not been accepted by management and the consequent risks; and
- The issues identified in the Annual Governance Statement.

The tables below show the total number of audits completed which contribute to the overall audit opinion. The table also shows the total number of audits still at the draft stage and where no reports have been issued following the preparation of a position statement.

<b>Assurance Level</b>	<b>Number of Audits</b>
Maximum	0
Substantial	11
Limited / Moderate	11
Minimal / None	0
Draft	2
Fieldwork	2
No report Issued / Position statement	4
Rolled to 2019/20 Audit Plan	6
<b>Total</b>	<b>36</b>

### **Internal Audit and Assurance Managers overall opinion on the council's internal control environment, risk management and governance arrangements**

Taking into account all the audit areas examined and the other work carried out during the year, it is my opinion that in respect of internal control, the council has in place satisfactory controls to be able to maintain an adequate and effective internal control environment. A number of audits have been given an overall assurance of 'limited'. However, follow-up reviews have been timetabled to ensure that agreed recommendations have been implemented.

It should be noted that at the time of publishing this audit opinion, two audit reviews (VAT and Insurance) had yet to be finalised. If at a later stage significant issues are identified that will ultimately change the overall opinion documented above, a further report to the Audit Committee will be completed.

### **Risk Management**

Work is currently underway to strengthen the Council's risk management processes across the organisation. Whilst the Risk Management Policy and Strategy has not been refreshed or approved by the Audit Committee since 2014, there are some good examples across the organisation, where it can be demonstrated that the Council has applied robust risk management processes into their decision making. In addition, the Executive Team have also recently drafted a Strategic risk register which was presented to the Audit Committee Team in February 2019. Recognising that there is still a considerable amount of work to ensure risk management is thoroughly embedded across the organisation, the Internal Audit and Assurance Manager will work with the Corporate Director over the next 12 months to identify a number of key activities which will be documented and monitored through the Corporate Services plan. It is also recommended that risk management is reported in the Annual Governance Statement as an area of significant concern.