

**Decision Maker:**      **AUDIT SUB-COMMITTEE**

**Date:**                   **Wednesday 25 June 2014**

**Decision Type:**      Non-Urgent                   Non-Executive                   Non-Key

**Title:**                   **ANNUAL AUDIT REPORT**

**Contact Officer:**      Luis Remedios, Head of Audit  
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**Chief Officer:**        Chief Executive

**Ward:**                   (All Wards);

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1.    Reason for report

The annual report of audit activity in 2013/14 is for Member information and is also intended to assist the Council in meeting the financial management and internal control requirements of the Accounts and Audit Regulations 2011. Part of the overall arrangements requires the Chief Executive and the Leader to sign an annual governance statement. Included in this report are highlights of the performance of the Internal Audit function, a summary of the audits undertaken and an opinion on the overall adequacy and effectiveness of the organisation's internal control environment based on this work and the Annual Governance Statement. Members should note that schools are now included within this report but there is an annual fraud report elsewhere on this agenda.

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2.    **RECOMMENDATION(S)**

**Members are asked to note the report and approve the Draft Annual Governance Statement.**

## Corporate Policy

1. Policy Status: Not Applicable:
  2. BBB Priority: Excellent Council:
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## Financial

1. Cost of proposal: Not Applicable:
  2. Ongoing costs: Not Applicable:
  3. Budget head/performance centre: Internal Audit
  4. Total current budget for this head: ££660K including £313K fraud partnership costs.
  5. Source of funding: General fund, Admin subsidy, Admin penalties, Legal cost recoveries, Provision of sold services to academies
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## Staff

1. Number of staff (current and additional): 6.5 FTE including 0.5 FTE risk officer
  2. If from existing staff resources, number of staff hours: 1,030 audit days were spent on the audit plan, fraud and investigations but excluding RB Greenwich investigators time.
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## Legal

1. Legal Requirement: Statutory Requirement:
  2. Call-in: Not Applicable:
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## Customer Impact

1. Estimated number of users/beneficiaries (current and projected): Approximately 150 including Chief Officers, Head Teachers and Governors
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## Ward Councillor Views

1. Have Ward Councillors been asked for comments? Not Applicable
2. Summary of Ward Councillors comments: Not Applicable

### 3. COMMENTARY

- 3.1 The annual report is for Member information and is also intended to assist the Council in meeting the financial management and internal control requirements of the Accounts and Audit Regulations 2011. Part of the overall arrangements requires the Chief Executive and the Leader to sign an annual governance statement. This will be put before Members as part of the statutory accounts. Included in this report are highlights of the performance and achievements of the Internal Audit Division, a summary of the audits undertaken and associated opinions along with a statement on the overall adequacy and effectiveness of the organisation's internal control environment based on this work.
- 3.2 Internal Audit's main objective remains as ' -assisting management and Members in minimising risks, maintaining high standards and continuously improving service delivery through independent appraisal, review and advice.' We have carried this out in 2013/14 by;
- **independently reviewing, appraising and providing assurance** on the systems of control throughout the Authority
  - ascertaining the **extent of compliance** with procedures, policies, regulations and legislation
  - facilitating good practice in **managing risks**
  - **working in partnership** with the external auditors and other external providers
  - **identifying fraud** and carrying out investigations
  - **running mandatory web training sessions for** officers in financial regulations, contract procedure rules and fraud awareness
- 3.3 Key aspects of our reviews looked at the controls in place and assess these and the associated risks if these controls are not in place or are not being fully followed. Essentially Internal Audit has ensured that the controls operate in an orderly and efficient manner, statutory and management requirements are complied with, assets are safeguarded, completeness and accuracy of records are secured and identified weaknesses are corrected when something has gone wrong. We have also considered the balance of controls against the cost of implementation and where the controls are regarded as over burdensome this will be acknowledged.
- 3.4 The purpose of the 2013/14 Internal Audit Plan was to:
- Optimise the use of audit resources available, given that these are significantly limited
  - Identify the key risks facing the Council in achieving its objectives and determine the corresponding level of audit resources
  - Ensure effective audit coverage and a mechanism to provide Members, and senior managers with an overall opinion on the auditable areas and the overall control environment
  - Add value and support senior management in providing effective control and identifying opportunities for improvement
  - Support the Director of Finance in fulfilling obligations as the Council's nominated Section 151 Officer
  - Deliver an Internal Audit service that meets the requirements of the Accounts & Audit Regulations and the Code of Practice.
  - Carry out major investigative work and adopt the lessons learnt by utilising these in other audits particularly in relation to cumulative spend
  - Provide adequate assurances on our work so that our external auditors can place reliance on our work thus saving on audit fees.

- 3.5 Internal Audit has striven to satisfy our customers through our business processes which make sure we have set challenging targets and standards for all audit staff through agreed objectives. We review and appraise the achievement of these objectives throughout the year. The overriding theme is the annual audit planning and work programme agreed each year. Although our aim has been to complete the 2013/14 plan, this has been subject to adjustment for unexpected levels of unplanned activity including fraud and investigative work where we have spent some 345 days. To redress some of the shortfall we bought in to the Internal Audit service of the London Borough of Wandsworth for the first time to carry out 6 audits from the audit plan totalling about 70 days. Our assessment is that quality and delivery of the service has been satisfactory.
- 3.6 Internal Audit work and outputs have been reviewed by External Audit who are able to conclude that Internal Audit were providing a satisfactory service and were able to place reliance on our work.
- 3.7 Internal Audit has 6.5 FTEs staff in post (including a 0.5 FTE officer solely responsible for risk) who are suitably experienced and qualified. In reality 5.5 FTEs auditors work on the plan or carry out investigations at any given time with about 0.5 FTE of the Head of Audit's time dedicated to servicing this committee and monitoring the fraud partnership.
- 3.8 Internal Audit have completed the high risk audit reviews scheduled in 2013/14 and received positive feedback from the client departments with an overall average of over 4 out of 5 for the audit satisfaction surveys. Overall, after allowing for a number of audits that were either postponed or cancelled due to management requests/ organisational change, we have completed over 90% of the plan against the annual performance indicator requirement of 90%. There remains 5 audits where work is in progress. The completion rate has been achieved despite the time spent on fraud and investigations of 345 days. Audits are completed within budgeted time unless major control issues are identified requiring additional testing. The summary of progress and other audit activity is shown in Appendix A.

### 3.9 Audit activity

Please refer to Appendix A

**Audit Activity key points in 2013/14**

**Planned audits-** please refer to appendix A for audits carried out in 2013/14. This constitutes our main area of activity.

**Risk Management –** The risk registers play a key part in the Annual Governance process - both corporate and departmental risk registers are maintained. The risks are reported through to the Audit Sub Committee and the corporate risks are reported through to the Risk Management Group and senior management.

**Customer Service –** We have received good customer feedback achieving an average score of over 4 out 5 in our audit surveys.

**Planning -** A key part of the audit planning process was consultation with senior officers, referral to previous audit reports and use of a risk methodology assessment form. This was completed for the 2013-14 plan.

**Sold Services –** the partnership with the Royal Borough of Greenwich for benefit fraud has continued to be highly effective both prosecuting and acting as a deterrent to public sector fraud. This is expanded upon in the Annual Fraud report elsewhere on this agenda. In 2013-14 we also carried out a number of responsible officer roles at academies that had generated about £24k with 14 academies using our services. This has resulted in a surplus of

about £8K.

**Partnership Working** – we continue to achieve closer links with other local authorities and public bodies to ensure our ability to work collaboratively. We also work with the London Audit Group and Kent Audit Group on developmental and training activities and have productive working relationships with the external auditor which helps to reduce the audit fee as they are able to place reliance on our work.

#### **Benefits Delivered**

**Effective Control** – our work continues to be instrumental in ensuring the Council has high standards of control and probity.

**Risk Management** – the Council has a robust framework for identification and management of risks, reducing likelihood of failure of service delivery. This is continually reviewed through the Risk Management Group and reported to Audit Sub Committee.

**Recommendations for Improvement**-Agreed actions for improvement are recognised and implemented. All priority one recommendations are reported to Members and followed up.

**Advice**- professional advice is given on new initiatives and ways of working. We have installed updated financial regulations and procedures as part of the managers' toolkit that has been approved by full council, undertaken web based training and awareness courses in financial regulations and contract procedure rules for over 600 officers.

**Assurances**-assurance provided to management by internal audit reviews. We also play a lead role in producing and coordinating the statutory Annual Governance Statement.

**Efficiencies**- our review activity enables us to offer advice to managers regarding opportunities to improve efficiency, examples include, data matching opportunities, identifying overpayments, identifying duplication and potential for better use of technology

**Audit Efficiency** – we will continue to streamline our own processes, for example, continue to use electronic working papers, continued use of self - assessment for schools.

**Fraud and Investigations**- we have provided substantial input into investigations into fraud and malpractice totalling 345 days.

Internal Audit has provided 1,030 audit days in 2013-14 including fraud and sold services (925 days for 2012-13) to the departments through reviews, investigations and financial support and advice. As well as mainstream audit activity, Internal Audit has spent time investigating fraud and irregularities, managing the fraud partnership, giving advice and guidance, development of the financial regulations that is elsewhere on this agenda and updated the raising concerns procedure, attendance at departmental and corporate working groups, representing the Council at external meetings, servicing this committee, and leading and participating in data matching exercises including the National Fraud Initiative.

#### **Summary of Audit Days provided to the departments.**

	<b>2012-13</b>	<b>2013-14</b>
<b>Departments</b>	<b>Audit days</b>	<b>Audit days</b>
Corporate Services	293	399
ECHS –Adults, Children & Public Health Services	331	303
Environment & Community	46	72
Fraud Work	128	153
Academies- sold services	77	103
RB Greenwich –sold services	50	0
	<b>925</b>	<b>1,030</b>

It should be noted that the departmental figures include 192 days spent on five major investigations against a total time of 345 days on fraud and investigations for 2013/14..

- 3.10 All audits arising from the approved plan have resulted in a formal report to management. Each audit has agreed terms of reference and is conducted according to the Public Sector Internal Audit Standards and Bromley’s standard audit documentation guidance. All final reports are agreed with the client prior to release and are followed up systematically in the following financial year unless there are priority one recommendations which are followed up within six months. In addition, all audit reports include an opinion based on our findings. Following a decision by Members, all audit reports suitably redacted, will be publicised on the internet unless exemption is sought.
- 3.11 Internal Audit have reported all priority one recommendations i.e. those where there are major weaknesses resulting in losses and therefore require urgent management attention. These reports are contained in the respective progress reports submitted to each cycle of this committee. The reason for the specific summary reports to Members are that all of these reports contain a recommendation which Internal Audit believe to be a risk to the service, system, function or establishment which needs to be addressed. The number of priority ones and the nature of any fundamental areas of weakness will determine the overall opinion given.
- 3.12 Over 2013/14 we issued 40 priority one recommendations –however 28 were in relation to three investigations that was reported in the November 2013 cycle of this committee. Outside of these investigations there were 12 priority one recommendations raised in respect of the Libraries investigation (2 of which 1 has been implemented), the Mobile phone investigation (1), Mental Health(1 that has been implemented), and Building Maintenance (1), Looked After Children (2), TCES audit (3), Main Accounting and Budgetary Control (1) and Creditors (1) . The current priority one list is attached to the Progress Report elsewhere on this agenda. There are two priority one recommendations brought forward from 2012/13 that are still considered to be outstanding –Emergency Accommodation & Rent Accounts specifically rent arrears that will be followed up in 2014/15 and Behaviour Services in respect of an unpaid an outstanding debt. See Appendix B for a summary of Priority 1 activity.
- 3.13 As in the previous year we have adopted a similar approach issuing assurances for our audits. Following an Internal Audit and after consultation with management, auditors form an overall opinion on the extent that actual controls in existence provide reasonable assurance that significant risks are being managed. They grade the control system accordingly. Full assurance is rare regarding internal control systems, because no matter how sophisticated they are, it will not be possible to prevent or detect all errors or irregularities. The opinions given are graded accordingly in the table below.

Assurance Level	Definition
Full Assurance	There is a sound system of control designed to achieve all the objectives tested.
Substantial Assurance	While there is a basically sound system and procedures in place, there are weaknesses, which put some of these objectives at risk. It is possible to give substantial assurance even in circumstances where there may be a priority one recommendation that is not considered to be a fundamental control system weakness. Fundamental control systems are considered to be crucial to the overall integrity of the system under review. Examples would include no regular bank reconciliation, non-compliance with legislation, substantial lack of documentation to support expenditure, inaccurate and untimely reporting to management, material income losses and material inaccurate data collection or recording.
Limited Assurance	Weaknesses in the system of controls and procedures are such as to put the objectives at risk. This opinion is given in circumstances where there are priority one recommendations considered to be fundamental control system weaknesses and/or several priority two recommendations relating to control and procedural weaknesses.
No Assurance	Control is generally weak leaving the systems and procedures open to significant error or abuse. There will be a number of fundamental control weaknesses highlighted.

- 3.14 Where Internal Audit have provided no assurance or there has been a significant number of priority one recommendations, based on the review and testing undertaken, a full management response and the audit report has been presented to the Audit Sub Committee e.g. Learning Disabilities, Insurance and Libraries. Responsible officers are called to account for the reasons for the weaknesses and give Members assurance of their management actions to implement audit recommendations. These actions are then followed up and reported within a six month timescale where it is reasonable to do so. It has been agreed that responsible officers will be required to attend the meetings where satisfactory action has not been taken.
- 3.15 Over the past year there have been five major investigations all reported to this committee- Learning Disabilities; Insurance; Misuse of the internet ; Libraries and a case of Financial abuse of a client. These investigations, other fraud work such National Fraud Initiative data matching and monitoring of the Greenwich partnership has taken a considerable amount of time some 345 days in 2013/14. These investigations had highlighted the need to promote officer awareness of financial regulations and the contract procedure rules. Over 600 officers have so far undertaken the web based training package.
- 3.16 The summary of audit work undertaken resulted in 86 reports including schools. Of the completed audits 30 were classified with substantial assurance, 9 with limited assurances and 1 nil assurance issued in the year. The remainder were follow up reports, investigation reports, pre academy school closure audits and work in progress audits where we do not give an opinion. Overall 230 improvement recommendations have been made in the year comprising of 40 priority ones, 166 priority twos and 24 priority threes. 21 recommendations are in respect of schools.

### **3.17 Schools**

- 3.18 Our volume of schools audits is influenced by our reduced staffing resources and the rate of schools converting to academy status. As a result the audit programme has been restricted to 17 schools, including one secondary school, two primary schools, follow up work at 3 schools and 11 closure audits of those schools converting to academy status.
- 3.19 The Internal Audit programme reviewed controls around processes categorised as Governance Arrangements, Financial Management Information, Primary Accounting Documentation (the tests in this area include, payments, income, payroll and school meals) and Assets.
- 3.20 The schedule in paragraph 3.30 gives a breakdown of type of recommendations made in respect of our school audits. The main recommendations for schools relate to primary accounting records which include non raising of orders, lack of evidence of quotes, recommendations in respect of banking arrangements, financial delegated responsibility limits, income including school meals, petty cash issues, outcomes from payroll testing, contracts register, cash flows and business continuity plans were also made.
- 3.21 Following the publication of a Department of Education Investigation report in May 2013 which described that the Accounting Officer at an Academy outside of Bromley was using Education Funding Agency monies for inappropriate purposes, management requested that Internal Audit undertake a review of purchase card transaction spend to ensure London Borough of Bromley funds are spent appropriately and in compliance with the Schools' Financial Regulations. This audit provided assurance to management in that no systematic purchase card spending abuse was identified and Internal Audit extended the audit testing in purchase card spending as part of the on-going School's programme.
- 3.22 Internal Audit has proactively sold services to Academies and during 2013/14 have been appointed to the role of Internal Auditor at a total of 14 schools (6 secondary and 8 primary

academies). This generates income of about £24K and a surplus of £7K for 2013/14 before recharges.

### **3.23 Annual Governance Statement**

- 3.24 The system of internal control is designed to manage risk to a reasonable level rather than to eliminate risk of failure to achieve policies, aims and objectives; it can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process which is designed to identify and prioritise the risks to the achievement of Bromley's policies, aims and objectives. It also evaluates the likelihood of those risks being realised and the impact should they be realised as well as managing them efficiently, effectively and economically. The main issues in 2012/13 related to breach of financial regulations and contract procedure rules; lack of supporting documents; no or outdated procedures; supervisory/monitoring issues; and primary accounting records. The main Internal Audit issues in 2013/14 related to supervisory/monitoring issues; no/obsolete procedures; and lack of supporting documents. The severity of each of these needs to be seen in the context of whether it was a priority one, two or three recommendation or not but it does give a broad picture of where improvements can be made. It should be noted that recommendations in respect of breach of financial regulations and contract procedure rules has decreased from 11% to 3% and probably reflects increased officer awareness of these regulations following the web based training undertaken by over 600 officers in 2013/14.
- 3.25 The scope of internal control spans the whole range of the Council's activities, encompassing policies, processes, tasks, behaviours and other aspects of the organisation. It is the means devised by management to promote, direct, restrain and check upon its various activities to ensure the Council is competently managed and its business is undertaken in an orderly manner in accordance with its objectives and policies. Each Chief Officer reviews the effectiveness of the system of internal control and risk management processes based on a list of key controls expected to be in place. Where measures are required to enhance the adequacy of existing internal controls actions are agreed. Because of the emphasis on risk within this process the individual departmental statements have been co-ordinated by the Risk Management Group that meets approximately every three months. In addition at the request of this committee, the Risk Management Group carried out an exercise to put in the financial impacts on the risks identified where possible. The outcome of this exercise has been reported to this Committee in March 2014.
- 3.26 In conclusion, the Head of Audit's overall opinion on the control environment based on the internal testing and reviews undertaken is that there is overall reliance on the internal controls identified and where there have been significant issues highlighted provide assurance that corrective management action has been or will be taken to mitigate the risks. Over the past year there have been investigations that highlighted a number of weakness in the areas of supervision/monitoring, document control and updated procedures but significantly a better understanding in officers' understanding/awareness of financial regulations and contract procedure rules. This has been due the mandatory web based training of over 600 officers involved in the finances of this authority. The Head of Audit can confirm that adequate action plans have been agreed for all areas of identified weakness and Internal Audit will continue to apply close scrutiny to ensure that all current priority control weaknesses are addressed by management. This assurance process constitutes part of the Annual Governance Statement which is attached to this report.
- 3.27. In summary the process (as adopted in the previous year) used for determining the annual governance statement follows proper practice as guided by CIPFA and is a combination of assurances derived from:

- The adequacy and effectiveness of the management review processes (Annual Governance Statement Checklist).
- Outcomes from the formal risk assessment and evaluation ( risk register)
- Relevant self-assessments of key service areas within the directorate
- Internal audit reports and results from follow ups regarding implementation of recommendations
- Outcomes from reviews of services by other bodies including Inspectorates, external auditors etc.

3.28 The Annual Governance Statement is attached as Appendix C.

### 3.29 Classification of Recommendations

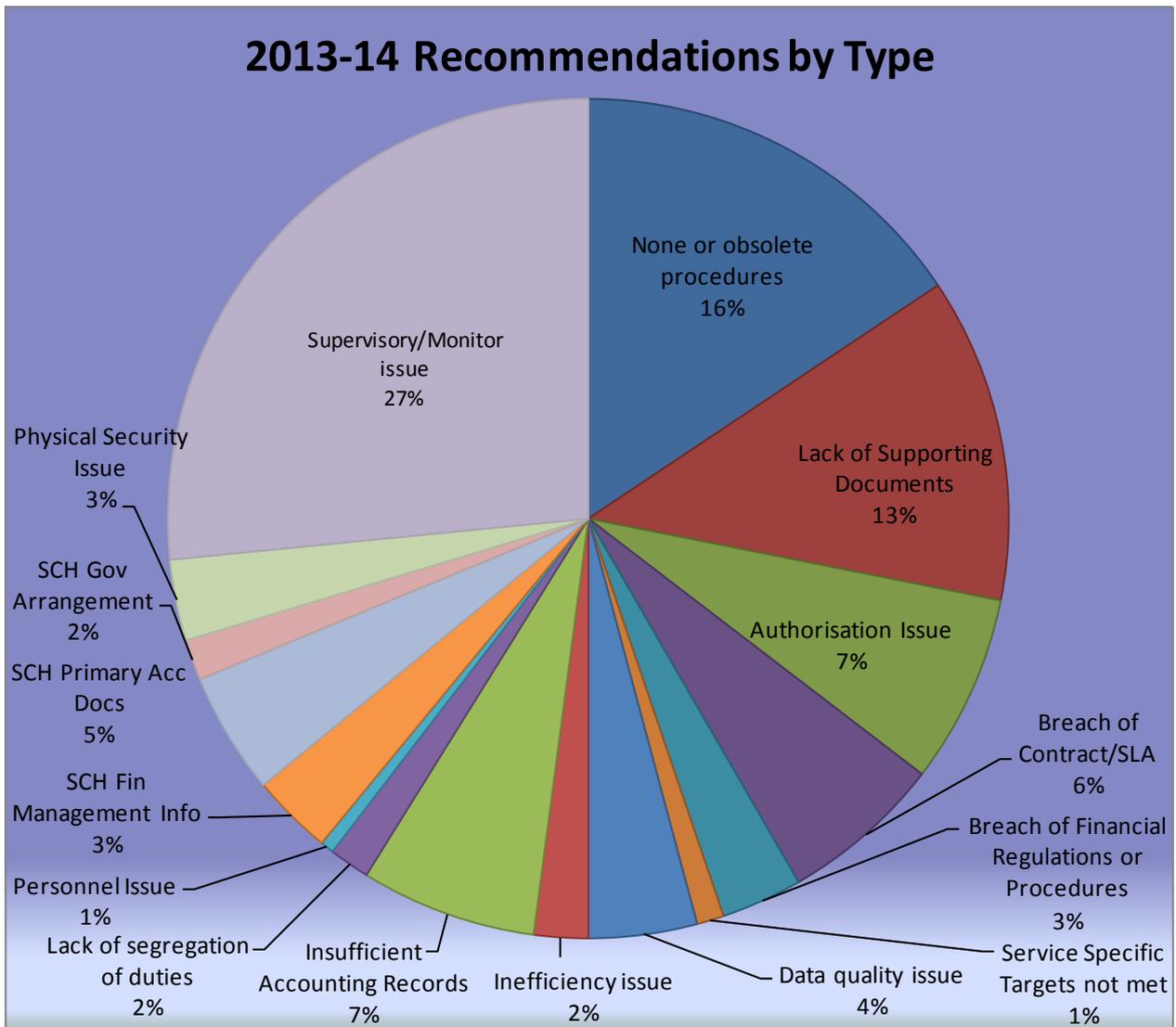
3.30 Typical control issues highlighted in the audit reports (as in previous years) fall under the following broad categories;

- Organisational – the controls that provide the framework under which the system of other controls can operate effectively and efficiently.
- Financial – the system of controls that ensures the accuracy and adequacy of financial records and also safeguards the organisation against possible financial loss due to fraud or error.
- Operational – the system of controls that ensures the efficiency and effectiveness of operations, ensures the organisation’s objectives are met (and services delivered) and also safeguards the organisation against any reputational damage or other loss.
- Compliance controls – the system of controls that ensure that the organisation complies with all relevant legislation, best practice guidance and internal policies with respect to the conduct of the business.

### 3.31 Recommendations by Category

Recommendation Category	% of all recommendations		
	2011-12	2012-13	2013-14
Access Control Issue	2%	2%	0%
Authorisation Issue	3%	1%	7%
Breach of Contract/SLA	2%	4%	6%
Breach of Financial Regulations or Procedures	7%	11%	3%
Data quality issue	5%	9%	4%
Inefficiency issue	5%	5%	2%
Insufficient Accounting Records	10%	9%	7%
Insufficient Resources Issue	1%	1%	0%
Lack of segregation of duties	1%	0%	2%
Lack of Supporting Documents	10%	10%	12%
None or obsolete procedures	4%	10%	16%
Personnel Issue	2%	1%	1%
Physical Security Issue	3%	2%	3%
Supervisory/Monitor issue	20%	12%	27%
Service Specific Targets not met	2%	2%	1%
SCH Asset Control	3%	3%	1%
SCH Fin Management Info	2%	1%	4%
SCH Governance Arrangements	3%	3%	1%
SCH Primary Acc Docs	16%	14%	3%

3.32 The above table is reflected as a pie chart below.



3.33 Insufficient accounting records –recommendations have been raised in a number of instances on a failure to raise orders that can result in commitments not being shown on budgets.

3.34 Supervisory/monitoring –the increase in the number of recommendations made for this category probably correlates to a reduction in staffing resources where there are fewer officers in post to fulfil these tasks.

**4. POLICY IMPLICATIONS**

None

**5. FINANCIAL IMPLICATIONS**

Some of the internal audit findings may have financial implications.

**6. LEGAL IMPLICATIONS**

Internal Audit is a statutory function under the requirements of the Accounts and Audit Regulations 2011.

**7. PERSONNEL IMPLICATIONS**

None

<b>Non-Applicable Sections:</b>	Policy & Personnel
Background Documents: (Access via Contact Officer)	None