

Decision Maker: **AUDIT SUB-COMMITTEE**

Date: **Wednesday 6 July 2016**

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

Title: **ANNUAL AUDIT REPORT**

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Chief Officer: Chief Executive

Ward: (All Wards);

1. Reason for report

The annual report of audit activity in 2015/16 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 2015. 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 those schools that are audited are now included within this report.

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: £469K including £174K fraud partnership costs
 5. Source of funding: General fund, Admin subsidy, Admin penalties, Legal cost recoveries
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Staff

1. Number of staff (current and additional): 5.5 FTE
 2. If from existing staff resources, number of staff hours: 2015-16 -872 audit days were spent on the audit plan, fraud and investigations – includes 110 days from LB Wandsworth but excludes RB Greenwich investigators time.
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Legal

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

1. Estimated number of users/beneficiaries (current and projected): Approximately 100 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 2015. 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 2015/16 by;

- **independently reviewing, appraising and providing assurance** on the systems of control throughout the Authority assisted in part by LB Wandsworth
- ascertaining the **extent of compliance** with procedures, policies, regulations and legislation
- facilitating good practice in **managing risks** working with our insurers
- **working in partnership** with the external auditors and other external providers
- **identifying fraud** and carrying out investigations working in partnership with RB Greenwich
- **continuing to host the interactive web training** for officers in Financial Regulations, Contract Procedure Rules and fraud awareness. We are developing a web based interactive training packages on audit controls on key audit findings and risk management.

3.3 Key aspects of our reviews looked at the controls in place and assessed these and the associated risks to ascertain if they are 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 2015/16 Internal Audit Plan was to:

- Optimise the use of audit resources available, given that these are significantly limited and utilise the audit services of the London Borough of Wandsworth.
- 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 to 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 2015 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.

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 2015/16 plan, this has been subject to adjustment for unexpected levels of unplanned activity including fraud and investigative work where we have spent some 311 days. To redress some of the shortfall we have again bought in to the Internal Audit service of the London Borough of Wandsworth to carry out 9 audits from the audit plan totalling 110 days. Our assessment is that quality and delivery of the service has continued to be satisfactory. However, the funding to commission them has been deleted with effect from April 2016.

3.6 We have met with our new external auditors and given them access to all our published reports that are on the web.

3.7 Internal Audit now has 5.5 FTEs staff in post who are suitably experienced and qualified. We had appointed to one principal auditor vacancy in May 2015 and deleted a 0.5 FTE principal auditor post as well as the 0.5FTE Risk Management Officer post with effect from April 2016. In reality 5 FTEs auditors work on the plan (augmented by resources bought in from LB Wandsworth) and carry out investigations (augmented by resources bought in from RB Greenwich), 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 2015/16 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 remain 6 audits where work is in progress. The completion rate has been achieved despite the time spent on fraud and investigations of 311 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 see Appendix A

Audit Activity key points in 2015/16

Planned audits- please refer to Appendix A for audits carried out in 2015/16. 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 corporate risks as well as high and significant risks are reported through to the Audit Sub Committee as well as to the Corporate 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 2015-16 Internal Audit plan.

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 outgoing and incoming external auditors.

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 Corporate 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, commissioning of services- health checks and on financial regulations, internal controls. We have continued to maintain the web based training and awareness courses in Financial Regulations, Contract Procedure Rules and the fraud toolkit.

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. Some of our findings have resulted in savings in costs and reclaiming of monies due.

Audit Efficiency – we will continue to streamline our own processes, for example, continue to use electronic working papers.

Fraud and Investigations- we have provided substantial input into investigations into fraud and malpractice totalling 311 days that have resulted in identifying losses, value for money issues, weaknesses in control and management shortcomings. We are also overseeing pro-active work resulting in identifying losses and making savings.

3.10 Internal Audit has provided 872 audit days in 2015-16 including fraud and investigation (963 days for 2014-15) 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, carrying out pre health checks on services outsourced, attendance at departmental and corporate working groups, representing the Council at external meetings, overseeing risk management, servicing this Committee, overseeing proactive exercise to identify fraud and wastage and leading and participating in data matching exercises including the National Fraud Initiative.

3.11 Below is a summary

Summary of Audit Days provided to the departments.

	2014-15	2015-16
Departments	Audit days	Audit days
Corporate Services	320	244
ECHS –Adults, Children & Public Health Services	301	219
Environment &	108	266

Community Services		
Fraud Work-General	166	143
Academies- sold services	68	0
	963	872

It should be noted that the departmental figures include 168 days spent on investigations against a total time of 301 days on fraud and investigations for 2015/16.

- 3.12 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. 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, are publicised on the internet unless exemption is sought. In 2015/16 we published 49 reports on the internet.
- 3.13 Internal Audit have reported all priority one recommendations i.e. those where there are major weaknesses resulting in losses and contract monitoring issues and therefore require urgent management attention. These reports are contained in the respective progress reports submitted to each cycle of this Committee. The number of priority ones and the nature of any fundamental areas of weakness will determine the overall opinion given.
- 3.14 Over 2015/16 we issued 28 new priority one recommendations – 22 were in relation to investigations of which 19 were reported in the part 2 November 2015 cycle of this Committee (10 were outstanding at June 2016 relating to contract monitoring matters). Outside of these investigations there were 6 new priority one recommendations raised in respect of: Domiciliary Care (2 priority one still outstanding at March 2016); Transition Team (1 priority one outstanding at June 2016); Extra Care Housing (1 priority one outstanding at June 2016); a primary school (1 priority one- the schools has converted to academy status and this recommendation may be followed up by the Schools Finance Team); and Penalty Charge Notices audit for 2015/16 (1 priority one recommendation which is currently being actioned for implementation). Finally there were 2 re-recommendations following full audits- creditors (1 priority one recommendation outstanding at June 2016); and Temporary Accommodation Rent Arrears (1 priority one recommendation outstanding at June 2016).
- 3.15 There are priority one recommendations brought forward from 2014/15 that are either considered to be outstanding or implemented: Family Placements (8 priority ones all implemented at March 2016); Review of Essential Car Users (3 priority one all implemented at March 2016); Leaving Care (9 priority ones all of which were implemented at June 2016); Creditors (1 priority one outstanding at March 2016); Insurance (1 priority one which was implemented at March 2016); Building Maintenance (1 priority one priority one which was implemented at March 2016); Fixed Penalty Notices (5 priority ones all of which were implemented at June 2016); Emergency Accommodation & Rent Accounts (1 priority one outstanding at March 2016); The current priority one list is attached to the Progress Report elsewhere on this agenda. See Appendix B for a summary of Priority 1 activity in 2015-16.
- 3.16 As in previous years we have adopted a similar approach issuing assurances for our audits. Following an Internal Audit review 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 of internal control systems is rare, because no matter how sophisticated or robust 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.

3.17 The summary of audit work undertaken resulted in 75 reports including schools; however some of these reports are in draft awaiting finalisation. Of the completed audits 43 were classified with substantial assurance, 12 with limited assurances and none with 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 286 improvement recommendations were made in the year comprising of 30 priority ones of which 28 were new and 2 were re-recommendations following audits, 211 priority twos and 44 priority threes. 59 recommendations are in respect of schools. See Appendix B for all 2015-16 audit activity that includes a summary of numbers of priority one, two and three recommendations on audit reports.

3.18 Schools

3.19 Internal Audit has visited 11 Bromley maintained schools in 2015-16, including 1 secondary school, 2 special schools and 8 primary schools. 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 Recommendations made at several schools this year, related to maintaining and reporting the contract register, completeness and certification of information held on the asset register, orders raised as expenditure is committed, expenditure and any variations to order to be adequately supported by documentation held at the school. A Priority 1 recommendation was raised for a primary school with regard to cash handling and management of the safe, accountability and security. There were also recommendations made for benchmarking, cash flow statements, lettings, scheme of delegation, purchase cards and declaration of interest forms. The schedule in paragraph 3.33 gives a breakdown of type of recommendations made in respect of our school audits.

3.21 There were follow up reviews for 4 schools that had been audited in 2014/15; of the 22 recommendations raised 21 were fully implemented and 1 partially implemented. For one

primary school, 6 new recommendations were raised when follow up testing identified issues relating to the IT contract; the award, monitoring, transparency, cumulative spend, disaster recovery and declaration of interest. Liberata had carried out an audit review in 2014/15, at the request of the Headteacher, identifying 11 areas of improvement. It was agreed that Internal Audit would carry out the follow up at this school, reporting that 7 of the 11 areas identified were considered outstanding and therefore raised as recommendations.

3.22 In addition to the planned school audits, Internal Audit have continued to support Bromley maintained schools, attending the finance officers' forum in October 2015, working with HR colleagues to issue HMRC guidance and responding to ad hoc requests for advice during the year.

3.23 Public Sector Internal Audit Standards -Peer review

3.24 We had previously reported to this Committee that the Public Sector Internal Audit Standards (PSIAS) which came in to effect in April 2013 requires an external assessment of the service every 5 years. Rather than employ a firm of accountants/auditors, the Society of London Treasurers felt that it would be more cost effective and useful if there was a London wide forum to undertake this task. Consequently we have joined a London wide external assessment group to undertake this assessment which was completed by the Head of Audit, Haringey in mid-March 2016 and the report received in April 2016. There are four possible outcomes from the review – 'Fully Conforms'; 'Generally Conforms'; 'Partially Conforms'; and 'Does not Conform'.

3.25 The outcome of the assessment is that we have been rated as 'Generally Conforms'. Generally Conforms means the reviewer has concluded that the relevant structures, policies, and procedures of the internal audit service, as well as the processes by which they are applied, at least comply with the requirements of the section in all material respects. For the sections and sub-sections, this means that there is general conformance to a majority of the individual statements of good practice, and at least partial conformance to the others, within the sub-section. As indicated above, general conformance does not require complete/perfect conformance.

3.26 The assessment covers four areas as indicated in Appendix C- Purpose and Positioning- does Internal Audit have the appropriate status, clarity of role and independence to fulfil its professional remit; Structure and Resources- does Internal Audit have the appropriate structure and resources to effectively deliver the internal audit remit; Audit Execution- does Internal Audit have the processes to deliver an effective and efficient internal audit service; and Impact of Internal Audit on the governance, risk and control environment of the organisation. A few recommendations have been made including a need to update the Internal Audit Charter which is elsewhere on this agenda.

3.27 Annual Governance Statement

3.28 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 Internal Audit issues in 2014/15 related to supervisory/monitoring issues; no/obsolete procedures; lack of supporting documents; and breach of Financial Regulations. The main Internal Audit issues in 2015/16 related to breach of contract /SLAs and Supervisory/Monitoring controls (26% of the total recommendations), none or obsolete procedures (8% of the total recommendations), lack of supporting documents (14% of the total recommendations) and Insufficient accounting records (17% of the total recommendations)

including schools). The severity of each of these needs to be seen in the context of whether it was a priority one, two or three recommendation but it does give a broad picture of where improvements can be made. However, given the high percentage of recommendations on breach of contract/SLA/supervisory/monitoring controls that is contract related, the Internal Audit plan for 2016/17 agreed by this Committee at the previous cycle does allocate more audit days to reviewing contract monitoring controls.

3.29 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. As part of the AGS process, 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. This exercise is coordinated by the Corporate Risk Management Group that meets three times a year prior to the meeting of this Committee.

3.30 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 audits and investigations that highlighted a number of weaknesses in the areas of supervision/monitoring, document control and updated procedures. Some of these weaknesses have resulted in priority one recommendations. The Head of Audit can confirm that adequate action plans have been agreed for all areas of identified weaknesses 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.

3.31 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);
- Signed assurance statements by senior management;
- Relevant self-assessments of key service areas within the directorate;
- Internal audit reports and results from follow ups regarding implementation of recommendations;
- Executive and Resources PDS Committee Annual Report;
- Outcomes from reviews of services by other bodies including Inspectorates, external auditors etc.

3.32 The Annual Governance Statement is attached as Appendix D.

3.33 **Classification of Recommendations**

3.34 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 data and safeguards the organisation against possible 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 ensures that the organisation complies with all relevant legislation, best practice guidance and internal policies with respect to the conduct of the business.

3.35 Recommendations by Category

Recommendation Category	% of all recommendations		
	2013-14	2014-15	2015-16
Access Control Issue	0%	0.5%	2%
Authorisation Issue	7%	6%	4%
Breach of Contract/SLA	6%	6%	9%
Breach of Financial Regulations or Procedures	3%	9%	5%
Data quality issue	4%	2%	1%
Inefficiency issue	2%	5%	4%
Insufficient Accounting Records	7%	6.5%	8%
Insufficient Resources Issue	0%	1%	1%
Lack of segregation of duties	2%	0%	0%
Lack of Supporting Documents	12%	9%	14%
None or obsolete procedures	16%	15%	8%
Personnel Issue	1%	1%	0%
Physical Security Issue	3%	2%	0%
Supervisory/Monitor issue	27%	24%	17%
Service Specific Targets not met	1%	2%	6%
SCH Asset Control	1%	1%	3%
SCH Fin Management Info	4%	4%	4%
SCH Governance Arrangements	1%	2%	5%
SCH Primary Accounting Docs	3%	4%	9%

3.36 The above table is reflected as a pie chart on the next page.

3.37 The main categories of the findings are expanded upon below:

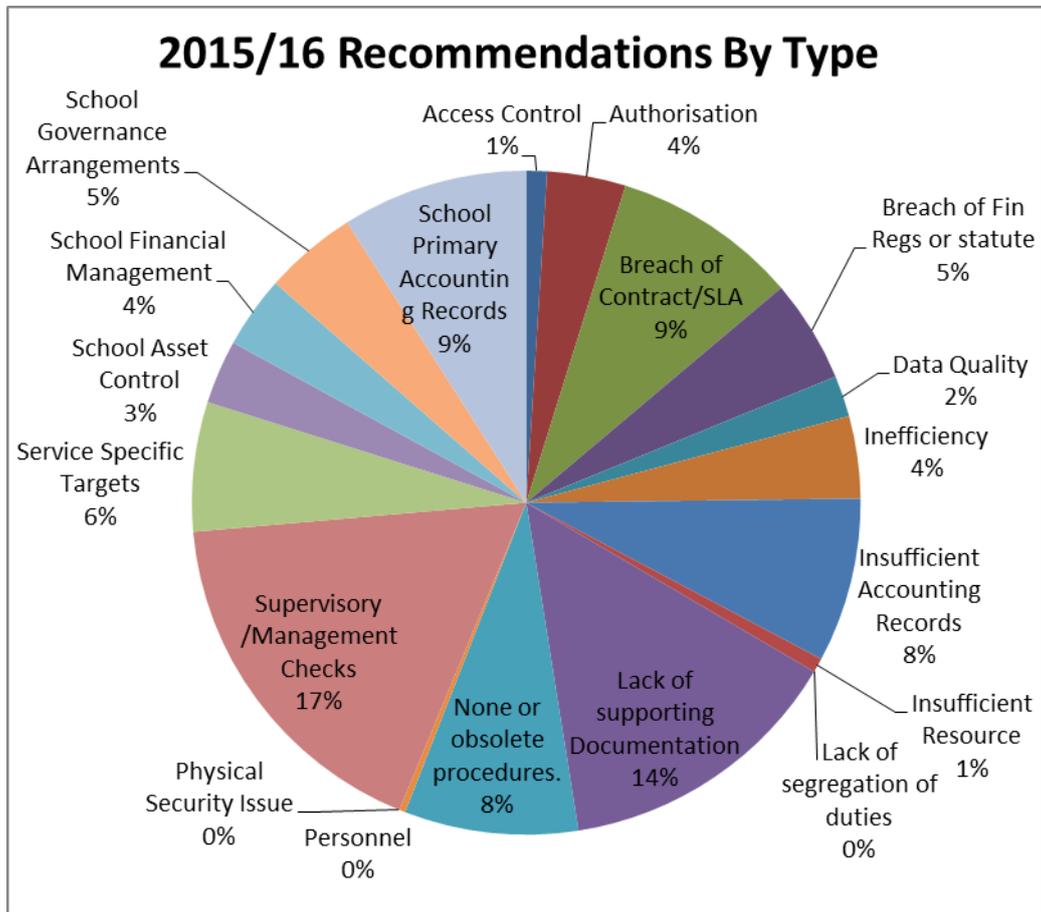
3.38 Insufficient accounting records –recommendations have been raised in a number of instances on a failure to raise orders that can result in commitments not being shown on budgets.

3.39 Lack of supporting documents –which is a breach of Financial Regulations or Contract Procedure Rules.

3.40 Breach of Contract/SLA/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. This is an increasing problem as more services are being commissioned and resources are decreasing.

3.41 None or obsolete procedures- this has could be caused by lack of resources to undertake updates as well as the changing nature of the organisation.

3.42 Lack of supporting documents- documents that were not available at the time of the audits. This could be caused by the physical movement of staff, lack of understanding on how long records should be kept and also documents that have been mislaid, misfiled or not filed.



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 2015.

7. PERSONNEL IMPLICATIONS

None

Non-Applicable Sections:	Policy; Personnel;
Background Documents: (Access via Contact Officer)	None