

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

**Date:**                    **Thursday 24 May 2018**

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

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

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**Chief Officer:**        Director of Finance

**Ward:**                    (All Wards);

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1. Reason for report

The report informs the Audit Sub Committee of Internal Audit activity in 2017/18. It assists the Council in meeting the financial management and internal control requirements of the Accounts and Audit Regulations 2015. In particular it includes:

- an overview of work undertaken and the levels of assurance;
- an analysis of the quality and effectiveness of Internal Audit confirming that the service conforms with the Public Sector Internal Audit Standards;
- the Head of Audit's opinion on the internal control environment.

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2. **RECOMMENDATION(S)**

**Members are asked to note the report and the Head of Audit's opinion on the soundness of the internal control environment within the London Borough of Bromley.**

### Impact on Vulnerable Adults and Children

1. Summary of Impact: Some of the audit findings could have an impact on adults and children.
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### 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: £560K
  5. Source of funding:
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### Personnel

1. Number of staff (current and additional): 6.5 FTE (currently one FTE vacant)
  2. If from existing staff resources, number of staff hours:
- 

### Legal

1. Legal Requirement: Statutory Requirement Non-Statutory - Government Guidance None:  
Further Details
  2. Call-in: Applicable Not Applicable: Further Details
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### Procurement

1. Summary of Procurement Implications:
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### Customer Impact

1. Estimated number of users/beneficiaries (current and projected):
- 

### Ward Councillor Views

1. Have Ward Councillors been asked for comments? Yes No Not Applicable
2. Summary of Ward Councillors comments:

### **3. COMMENTARY**

3.1 The annual report is for Member information and intended to assist the Council in meeting the requirements of the Accounts & Audit Regulations 2015. The regulations require the Council to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, and taking into account the Public Sector Internal Auditing Standards (PSIAS). The work forms the basis of the annual opinion of the Head of Audit and provides supporting evidence for the Annual Governance Statement, which also is considered on the agenda.

3.2 Internal Audit's objectives have been to assist management and Members in managing risks, maintaining good standards of control and continuously improving service delivery through independent appraisal, review and advice. We have carried this out in 2017/18 by:

- independently reviewing, appraising and providing assurance reports;
- ascertaining the extent of compliance with procedures, policies, regulations and legislation;
- reviewing client contract and monitoring arrangements;
- reviewing and refreshing the arrangements for Risk Management and departmental and corporate risk registers;
- identifying fraud and irregularity and working in partnership with RB Greenwich;
- hosting interactive web training for officers in Financial Regulations, Risk Management and Fraud Awareness.

3.3 Key aspects of our reviews examined controls in place and assessed these together with associated risks to ascertain if they are being followed. Internal audit has ensured that controls operate in an efficient and effective manner, statutory and management requirements are complied with, completeness and accuracy of records are secured and identified weaknesses are corrected.

#### **3.4 Analysis of 2017/18 activity and use of resources**

3.4.1 The 2017/18 Audit plan identified a total of 69 separate tasks including 3 schools. 19 audits were carried forward from 2016/17 and finalised in the year. By the end of the year work was either completed or in progress on a total of 51 further projects. 16 tasks were either cancelled or carried forward to 2018/19. Unplanned investigations were also carried out involving Internal Audit as opposed to the Anti-Fraud work separately completed by the Royal Borough of Greenwich Team.

3.4.2 Completion of the 2017/18 Internal Audit plan was been affected by several factors. Members were advised at the November meeting that the section had completed about 80% of the 2016/17 plan at the time of the Annual Report (June 2017) and therefore there was a significant amount of work brought forward into the year to finalise. Days lost to vacancy and sickness impacted on the 2017/18 plan, with 143 days lost during the year. Action was therefore required to risk-assess the current plan, bring in additional resources from the Croydon Framework and re-scope and prioritise tasks in the 2017/18 plan.

3.4.3 Members will be aware that since 2008 Croydon Council has held a single provider framework contract for the provision of Internal Audit services. The framework expired in March 2018 and a tender process has been undertaken. Whilst the incumbent supplier won the tender a number of staff who were assigned to Bromley projects, left for other work opportunities. The impact to

Bromley was slippage in the timing of the work assigned to them. However all outstanding allocated audits will be completed shortly.

3.4.4 Finally, as Members will be aware in prior years the Authority has been required to prepare draft financial statements by 30 June and final accounts by 30<sup>th</sup> September. From this year revised deadlines apply which require draft accounts by 31 May and final accounts by 31 July. These changes represent a significant change to the timetable that the Council has previously worked to. In order to support this, the Annual Governance Statement and the Annual report to support have been produced one month earlier than in previous years. As a result of these changes, combined with the issues above there is more work in progress and at draft stage than would otherwise be the case. Work in progress and draft reports will, when finalised, be reported to the next meeting of the Committee.

3.4.5 The days allocated to Departments is set out below with a comparison to 2016/17

**Table 1**

<b>Department</b>	<b>Actual Days 2016/17</b>	<b>Actual Days 17/18 including commissioned from the Croydon Framework (includes some yet to be delivered)</b>
<b>Chief Executive's</b>	303	321
<b>Education Care and Health Services including Public Health</b>	285	298
<b>Environment and Community Services</b>	183	124
<b>Sub Total</b>	<b>771</b>	<b>743</b>
<b>Anti-Fraud and Investigations</b>	91	81
<b>Total</b>	<b>862</b>	<b>824</b>

3.4.6 It should be noted that the 2016/17 departmental figures included 104 days spent on investigations in addition to the 91 shown in Anti-Fraud & Investigations row. Therefore 667 days (771 less 104) was spent on assurance work. In 2017/18, 743 have been spent on assurance work when the work commissioned from the Croydon Framework is completed. Therefore resources for 2017/18 have been adequate.

### **3.5 Summary of work undertaken and audit opinions**

3.5.1 Audits are conducted in accordance with prescribed standard. Not all tasks result in an opinion.

3.5.2 A summary of work undertaken follows in Table 2 overleaf.

**Table 2**

Planned tasks 2017/18	67
Deferred as already issued report on same issue this year/moved to next year or cancelled with management agreement	16
Completed tasks including reports at draft stage	36
Work in progress	15
Reports carried forward from 2016/17 and issued in 2017/18	19

3.5.3 Whilst there have been some variances and amendments to the plan, sufficient work has been undertaken to form the Head of Audit's opinion.

3.5.4 Further analysis is detailed in Appendix A

3.5.5 An Assurance rating was given in respect of 34 reviews at draft or final stage

**Table 3**

Full Assurance	0
Substantial Assurance	25
Limited Assurance	9
Nil Assurance	0

3.5.6 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 according to the criteria in Table 4 overleaf.

**Table 4**

<b>Assurance Level</b>	<b>Definition</b>
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.

3.5.7 Summaries of all individual reports have been reported to the Audit Sub-Committee following a formal report to management and it is not necessary to detail them again here. Each audit has agreed terms of reference and is conducted according to the Public Sector Internal Audit Standards. Final reports are agreed with the client prior to release. They are followed up systematically.

3.5.8 In June 2017, there were 35 priority 1 recommendations reported to Audit Sub Committee, brought forward from 2016-17. At the time of writing this report, 30 of these recommendations had been implemented. Fourteen new priority 1 recommendations were reported during 2017-18 of which 9 have been implemented prior to the May 2018 Committee. Ten priority 1 recommendations have been carried forward to 2018/19.

3.5.9 Following a decision by Members, all audit reports suitably redacted, are published on the internet unless exemption is sought. A summary of the key issues and challenges for the authority arising from our work is detailed in the Head of Audit's opinion in para 3.9 to 3.9.4.

### **3.6 Schools**

3.6.1 As at 1/4/17 there were 14 Bromley maintained schools; 1 secondary, 3 special schools and 10 primary schools. The 2017-18 audit plan included 20 days for school audits to be allocated during the year. The intention was to complete full audits at the secondary school and 2 primary schools and to complete the follow up of the

priority 1 recommendations at one primary school.

3.6.2 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. The programme was amended this year to also consider contract monitoring and authorisation procedures.

3.6.3 The follow up visit to the primary school in October 2017 satisfactorily evidenced implementation of the 5 priority 1 recommendations. The school had made significant progress to improve the financial management of the school and enhance the controls within the finance processes. The audit identified 4 new recommendations, all considered priority 2 and will be followed up during 2018-19.

3.6.4 The audit of the secondary school identified one priority 1 recommendation, 12 priority 2 recommendations and a priority 3 recommendation. The Internal Audit opinion was that limited assurance could be placed on the effectiveness of the overall controls. A follow up will be carried out in quarter 3 of 2018-19 and progress to implement the priority 1 will be reported to committee.

3.6.5 The significant findings at both schools resulted in a greater time spent at the schools, supporting officers. This reduced available time for the other Bromley schools. However of the 4 primary schools due for a full audit in 2017-18, 2 converted to Academy, 1 was audited in March and the other is booked for May. All schools which convert to Academy status are subject to a close down, pre academy conversion audit by the Schools Finance Team; 3 such visits were carried out this year.

3.6.6 As at 31/3/18 there are 9 Bromley maintained schools; 1 secondary, 2 special schools and 6 primary schools.

### **3.7 Risk Management**

3.7.1 Members were informed that we had commissioned Zurich, our insurers, to carry out a check and challenge process on the current risk registers to be undertaken for each of the three Directorates (Education, Care & Health Services (ECHS), Environment & Community Services (ECS) and Chief Executive Directorates). The aim of this process was to provide the Directorate Management Teams (DMTs) with an independent discussion on risk and one that challenged, refreshed and validated the current risk register content. The outputs from the exercise were updated departmental risk registers.

3.7.2 Zurich's findings and recommendations were discussed at the Corporate Risk Management Group and Zurich attended all the DMT's to discuss their findings and provide a challenge where necessary. Finally the findings were discussed at Corporate Leadership Team, where it was agreed to undertake the same challenge and scoring process for corporate risks.

3.7.3 Following further review and consideration by DMTs, the Corporate Leadership Team and the Corporate Risk Management Group, a summary of the latest iteration of the Departmental and Corporate Risk Registers appear elsewhere on the Agenda.

### **3.8 Public Sector Internal Audit Standards (PSIAS)**

3.8.1 Internal Audit engagements are subject to a thorough internal review of quality to ensure that its work meets the standards expected from its staff. For example an internal file quality review is carried out to confirm that:

- All work is undertaken in accordance with the PSIAS
- The work is planned and undertaken in accordance with risks associated with the areas under review
- The conclusions are fully supported by detailed work undertaken

3.8.2 Under the requirements of the Public Sector Internal Audit Standards (PSIAS) there is a need for an external quality assessment of the service every 5 years. A peer review was carried out in March 2016. The review concluded that the section generally conforms with the standards. A number of recommendations were made and actioned.

3.8.3 Internal Audit had been using a commercial software system since 2005-06. This was a fully integrated audit management, working papers, action tracking and reporting system. This was central to the working practices of the Audit Team; time recording, templates for standard audit documentation (terms of reference, satisfaction questionnaires, testing matrices), control matrices and risks, working papers and scanned evidence, draft and final reports and management information to monitor audit progress and outcomes, specifically recommendations classifications and implementation. The system had not been upgraded at Bromley for many years and therefore had become very slow and cumbersome and in many ways restricted efficient working practices.

3.8.4 Internal Audit were advised in July 2016 that the version used by the team would not be supported past June 2017, but the timescale for any decision to upgrade or replace was reduced when ISD confirmed that the system could not be migrated to the new servers as part of an urgent project planned for February 2017.

3.8.5 A quote of £9K was received to upgrade to the latest version including workshops, consultants support and changes to the software according to specific requirements. The Internal Audit Team attended two workshops in January and February 2017, confirming that there were significant changes between the versions which would be time intensive to adapt to a new system and its functionality. Although the new version satisfied some of the shortcomings of the current version it was designed for multi-site, hierarchical structure audit teams and was deemed too complicated for the team of 5 principal auditors and Head of Audit at Bromley.

3.8.6 The Internal Audit team reviewed current working practices and alternatives to the system. Given the change in Head of Audit with effect from May 2017, the incoming Head of Audit was invited to attend the team meeting to debate the strengths and weaknesses of changing or to develop bespoke systems using MS Word and Excel. A decision was made to develop processes in house. This will also help contribute to required savings. The newly developed systems have been successful although this has taken some time to develop with time required for the development of a suite of documentation for terms of reference, control matrices, report templates, review records, client questionnaires and time recording. Additionally monitoring spreadsheets for the audit plan, progress and outcomes to be monitored by the Head of Audit and reported to this committee were also written. There is a need to reflect on feedback on how they work in practice and ensure they are consistently applied. There is also a need to update the Internal Audit Manual to reflect these changes

3.8.7 All work is quality reviewed by the Head of Audit before reports are issued and it can be confirmed that the section still generally conforms to the PSIAS.

### 3.9 Head of Audit – Annual Opinion

3.9.1 The Annual assessment is based on the work reported between April 2017 and the date of this report. In formulating this opinion the assurance activity undertaken by the Council and other external assurance providers is taken into account along with the following:

- The Audit work undertaken including the assurance opinion ratings
- The follow up reviews determining how the authority responds to identified weaknesses and in particular priority 1 recommendations
- Its approach to risk management particularly the detailed refresh of the Council's Risk registers
- Internal Audit's review of the supporting evidence for the Annual governance Statement

3.9.2 The work completed to draft or final stage shows that 74% were classified as substantial assurance with 26% limited. In addition the results of follow up work, as outlined in paragraph 3.5.8, show that audit recommendations are consistently implemented. The concept of continuous improvement is applied in that even in the best performing authorities errors will occur or control failures may result despite good intentions. However the Council should learn from its past performance, rectify defects and not continue along a path when control failure is evident. The Corporate Leadership Team considers priority one recommendations on a regular basis and managers are held to account. Audit reports highlight those areas where internal control systems need to be improved and the Internal Audit Plan for 2018/19 has time allocated for undertaking follow up work. Internal Audit will pay particular attention to those areas where the Internal Audit opinion was limited and priority one recommendations have been raised.

3.9.3 The work reviewing the Annual Governance Statement also clearly demonstrates the range of organisational controls which serve to provide an effective level of governance.

3.9.4 **From the work undertaken during 2017/18, reasonable assurance can be provided that there is generally a sound system of internal control, designed to meet the Council's objectives and that controls are applied consistently.** Where weaknesses are identified, i.e. Limited Assurance reports and Priority One recommendations are made; these are tracked by the Corporate Leadership Team and the Audit Sub Committee until implemented or discharged. In giving this opinion it should be noted that assurance can never be absolute. Even sound systems of internal control can only provide reasonable and not absolute assurance and may not be proof against collusive fraud. Through our Internal Audit work we have noticed a trend that reduced resources has been quoted as a reason for a reduced level of a control or the reason why a recommendation is difficult to implement. This can also result in a lack of oversight where a post is removed and responsibility for that function is not assigned to another officer. As part of our work on risk management and identifying areas for inclusion in the Annual Governance Statement we have identified key areas for management attention over the next year as discussed in the paragraphs below.

### 3.10 Finance

3.10.1 The Council has identified the challenge in its capacity to make further budget savings and maintain frontline services. The Council has set a balanced budget for 2018/19 without a detrimental impact on key services. There are savings/income generating options required for 2019/20. However, there are significant challenges for 2020/21 and beyond. Work is ongoing

to explore options to address the future years' budget gap through the four year forward planning arrangements. This has therefore been raised as an issue for the Annual Governance Statement.

### **3.11 Contract Management**

3.11.1 Contract issues have been identified across the organisation in the last two years which have identified the need for strengthened control and management oversight. This had been most evident in management of the Waste Contract which had resulted in 15 Priority 1 Recommendations at the end of 2016/17. Progress in addressing these issues took time and therefore it was not until the end of the year that recommendations were fully implemented. However there have been other examples in the area of TCES and Adult Mental Health, which is at draft report stage. In these cases we have noticed a trend of posts being deleted to contribute to expenditure reductions but the oversight functions are not reassigned. There has also been a need identified to improve contract awareness and management skills. This has been monitored by the Contract Sub-Committee. As a result, a number of actions have taken place to strengthen arrangements across the Council. These include a Contract Database with an alert system for tendering/renewal. It also includes a Document Management System which holds all electronic contracts, minutes of meetings, Change Control Notices (CCN) and Waivers. Some of this will be fully implemented in August 2018 and Internal Audit is following up progress.

3.11.2 Training has been identified as a mandatory requirement for 'commissioners of services'. It consists of four modules (3 hours per module) with compulsory attendance on all four to complete the course.

- Module 1 – Commissioning
- Module 2 – Contracting process, engaging with the market (procurement)
- Module 3 – Tender & evaluation process
- Module 4 – Award (Governance)

3.11.3 In view of the importance of the Commissioning Agenda to the Council's strategic objectives this has therefore been raised as an issue for the Annual Governance Statement.

### **3.12 General Data Protection Regulations (GDPR)**

3.12.1 Significant changes are required to ensure that the Council is compliant with the General Data Protection Regulations 2016 (GDPR) when introduced from 25th May 2018. This includes interaction with customers, the way in which information is recorded, the way in which data processing activities are communicated and a number of other areas all relating to the Council's processing activities of personal information. It will have a significant impact on all directorates and contractual arrangements.

3.12.2 In preparation for this change, a detailed challenging independent review was undertaken by the Data Protection People (DPP), who were invited to carry out a data protection compliance review and gap analysis to compare current practices against the GDPR. Therefore this eliminated the need for Internal Audit to carry out its scheduled review. Reliance has been placed on this work, with Internal Audit providing advice to the project team at various stages.

3.12.3 The DPP review provided 51 recommendations that the Council needed to action to advance towards being compliant with GDPR. A High Level Project Plan was also provided to assist LBB in its efforts to be compliant by the go-live date of GDPR.

3.12.4 The 25<sup>th</sup> May 2018 is not a finish line and work is continuing on the project plan. However, when assessing progress in March, there was still a considerable amount of work to be done

to ensure compliance. This has therefore been raised as an issue for the Annual Governance Statement.

### **3.13 Corporate and other non-benefit Related Fraud**

3.13.1 Internal Audit works in partnership with the Royal Borough of Greenwich in respect of Fraud Investigations. In 2017/18 147 allegations of corporate related fraud were received. These are detailed in Appendix B of the Fraud Investigations and Internal Audit Exempt Items Report on the agenda. These investigations covered areas such as:

- Council Tax Discounts and Exemptions
- Blue Badge Fraud
- Fraudulent School Admission Applications
- Theft
- Conflicts of interest
- Freedom passes
- Housing related fraud
- False identity

3.13.2 Since last year's annual report, 168 allegations of corporate and other non-benefit related fraud were investigated, which included 21 cases brought forward from previous years. A total of 68 cases were successfully prosecuted in the year of which 66 cases related to Blue Badge misuse, one prosecution was for Council Tax fraud and one for a false re-housing application.

### **3.14 Freedom passes – Proactive Exercise**

3.14.1 Internal Audit and the Greenwich Fraud Team undertook a proactive data matching exercise in 2016-17 to identify Freedom Pass holders who potentially are no longer resident in the Borough. As previously reported, a total of 684 Freedom Passes were cancelled.

3.14.2 The proactive exercise also highlighted 20 cases where the council tax system identified a different occupant who was in receipt of single person discount. These cases were referred to Greenwich Fraud Team for further investigation. The outcome of further investigations into these cases is summarised in the Table 5 overleaf.

**Table 5**

ISSUE	ACTION TAKEN	NUMBER OF CASES	COMMENTS
Inappropriate claim of SPD by occupants	GFT visited the properties. Found both FP holder and CTP resident.	3	<p><b>Case 1:</b> SPD cancelled. Underpayment of £3,039.42 of Council tax is being recovered.</p> <p><b>Case 2:</b> SPD cancelled. Underpayment of £2,575.79 of Council tax is being recovered.</p> <p><b>Case 3:</b> Residency confirmed with landlord and SPD cancelled. Council tax payer prosecuted under Fraud Act for the underpayment of Council tax totalling £1,873.21. Additional overpayment of £3,233.43 HB and £205.37 CTB being recovered.</p>
Freedom pass holder not resident in Bromley	GFT visited the properties. Found FP no longer resident at the address	8	<p><b>Case 4, 5 and 6:</b> Moved abroad. FP cancelled.</p> <p><b>Case 7:</b> Moved out of London. FP cancelled.</p> <p><b>Case 8, 9:</b> Resident in another London borough.</p> <p><b>Case 10:</b> Previous resident with no forwarding address. FP cancelled.</p> <p><b>Case 11:</b> Business address used to obtain freedom pass. FP cancelled.</p>
No issue with FP entitlement.	Further investigation highlighted issues with other entitlements being claimed.	9	Seven cases referred to relevant departments for investigation. Data quality issue with the remaining two cases which have been resolved.

3.14.3 In addition to the previously reported potential savings of approximately £194K from cancelled Freedom passes, the proactive exercise has also identified underpayment of £7,488.42 Council Tax, overpayment of £3,233.43 Housing Benefit and £205.37 Council Tax Benefit.

### 3.14. National Fraud Initiative

3.14.1 The National Fraud initiative is carried out by the Cabinet Office every 2 years. However an annual match is made between the Council Tax database and the Register of Electors. After matching results were received in January 2017, Internal Audit and Counter Fraud staff ensure responsible officers carry out investigations into these matches which continue until the next exercise begins. The team also deal with enquiries from other public bodies.

**4. IMPACT ON VULNERABLE ADULTS AND CHILDREN**

The contents of this report have implications for both adults and children in respect of cost and care requirements.

**5. POLICY IMPLICATIONS**

None

**6. FINANCIAL IMPLICATIONS**

Some of the internal Audit findings have financial implications.

**7. PERSONNEL IMPLICATIONS**

Some investigations may result in disciplinary actions.

**8. LEGAL IMPLICATIONS**

Internal Audit is a statutory function under the Accounts & Audit Regulations 2015.

**9. PROCUREMENT IMPLICATIONS**

The contents of this report have implications for procurement relating to Contract Procedure Rules, Financial Regulations and VFM issues.

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