

**PART 1 - PUBLIC**

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Decision Maker: **Audit Sub Committee**

Date: **7<sup>th</sup> June 2011**

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

**TITLE: INTERNAL AUDIT ANNUAL REPORT 2010-11**

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Chief Officer: Chief Executive, Doug Patterson

Ward: Borough wide

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1. Reason for report

The annual report is for Member information and is also intended to assist the Council in meeting the accountability requirements of the Accounts and Audit Regulations. Part of the overall arrangements requires the Chief Executive and the Leader to sign an annual governance statement. This will be put before Members alongside the statutory accounts. 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 the Annual Schools Report and the fraud reports are considered by the Audit Sub-Committee separately.

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**2.RECOMMENDATIONS**

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

## Corporate Policy

Existing policy: Excellent Council

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## Financial

1. Estimated cost n/a
  2. Recurring cost
  3. Budget head Internal Audit<
  4. Total budget for this head £616,500 including the benefit fraud partnership costs
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## Staff

1. Number of staff (current and additional) – 10
  2. If from existing staff resources, number of staff hours – circa 2000 days
- 

## Legal

1. Statutory requirement: Accounts and Audit Regulations 2011
  2. Call-in is not applicable:
- 

## Customer Impact

Estimated number of users/beneficiaries (current and projected) - potentially all staff

Ward Councillor Views

not applicable

### 3. COMMENTARY

- 3.1 The annual report is for Member information and is also intended to assist the Council in meeting the accountability requirements of the Accounts and Audit Regulations. 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 carry this out by;
- **independently reviewing** and appraising systems of control throughout the Authority
  - ascertaining the **extent of compliance** with procedures, policies, regulations and legislation
  - **providing assurance** to management and Members that the areas subject to review are performing adequately and any control weaknesses are identified and rectified.
  - facilitating good practice in **managing risks**
  - **working in partnership** with the external auditors and other external providers
  - **identifying fraud** as a consequence of the reviews and **detering crime**.
- 3.3 A key aspect of all reviews is looking at the controls in place and making an assessment of these and the associated risks if these controls are not in place or are not being fully followed. Essentially the controls and actions ensure that the processing procedures 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. There is always the intention to consider the balance of controls against the cost of implementation and where the controls are regarded as over burdensome this will be acknowledged.

#### Performance

- 3.4 As a recap the purpose of the Internal Audit Plan was to:
- Optimise the use of audit resources available, given that these are limited
  - Identify the key risks facing the Council to 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
  - Supporting the Finance Director 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.

- 3.5 Internal Audit seeks 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 document used for measurement of our audit service is our business plan. Within this plan for each objective that is set we then present what we will do, how we will do it and who will monitor this. The overriding theme is the annual audit planning and work programme agreed each year. This plan will be subject to adjustment for unexpected levels of unplanned activity or shortfall in resources.
- 3.6 Internal Audit work and outputs have been reviewed by External Audit who was able to conclude that Internal Audit were providing a satisfactory service and were able to place reliance on our work. In addition, the use of resources assessment although now discontinued for official reporting purposes the fieldwork was undertaken and concluded positively on the elements relating to the work of Internal Audit.
- 3.7 Internal Audit have completed the high risk audit reviews scheduled in 2009-10 and received positive feedback from the client departments with an overall average of over 4.3 out of 5 for the audit satisfaction surveys. Overall 89% of the plan was completed against the annual performance indicator requirement of 90%.
- 3.8 In addition, 88% of the audits were completed within the allocated budgeted time allowed against a performance indicator requirement of 90%.
- 3.9 Unfortunately the performance indicator requiring 95% of audits to be completed within two months of commencement of fieldwork fell short of target for the second year running at 85%. Mitigating circumstances include vacancies, awaiting information from clients, extending the original scope where there are major audit findings and auditors being asked to carry out ad hoc work including investigations. However, this indicator will now be reviewed to see if it is still practical. One option being considered is streamlining the turnaround times at each stage of the process so that the total elapsed time is brought closer in line with the target. The importance of this target relates to impact of the audit finding especially if there is a material weaknesses revealed. Another option to alert management through an interim report outlining any specific areas before the full report is finalised.

### Audit Activity key points in 2010/11

**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 4.3 out of 5 in our audit surveys. A key part of the audit planning process is consultation with senior officers.

**Shared Service** – the partnership with L B Greenwich for benefit fraud has continued to be highly effective both prosecuting and acting as a deterrent to public sector fraud. In addition the partnership has been extended to include corporate anti fraud work. In 2010/11 we carried out three audits for LB Greenwich that generated £14K income. In 2011-12 we have agreed to undertake a number of audits for Greenwich under a partnership agreement which will generate income for Bromley.

**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.

**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 the new financial regulations and procedures as part of the managers' toolkit, undertaken training and awareness courses and had the revised Code of Corporate Governance adopted by the Council.

**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, though exploitation of the onebromley intranet, continue to use electronic working papers and use the functionality of the integrated database capturing audit and risk issues

3.10 Internal audit has provided 1,301 audit days (1,379 days for 2009-10) to the departments through reviews, investigations and financial support and advice. As well as mainstream audit activity internal audit has spent time on investigating fraud and irregularities, managing the fraud partnership, giving advice and guidance, development of regulations and codes of practice, attendance at departmental and corporate working groups, representing the Council at external meetings and leading and participating in data matching exercises including the National Fraud Initiative.

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

	2009-10	2010-11
Departments	Audit days	Audit days
Corporate Services	493	458
Children and Young People	498	493
Adult and Community services	241	198
Environment	97	60
Recreation and Renewal	50	92
	<b>1,379</b>	<b>1,301</b>

- 3.11 It is important to note that all audits arising from the approved plan result in a formal report to management. Each audit has an agreed terms of reference and is conducted according to the CIPFA audit code of practice and Bromley's standard audit documentation guidance. All final reports are agreed with the client prior to release and are followed up systematically. In addition, all final reports include an assessment of the risk of any control weakness identified.
- 3.12 Throughout the year Internal Audit have reported all priority one recommendations i.e. those that are significant and require urgent management attention. These reports are contained in the respective progress reports. 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 level of priority ones and the nature of any fundamental areas of weakness will determine the overall opinion given.
- 3.13 As a result of the Internal Audit work and in 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. Absolute 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.

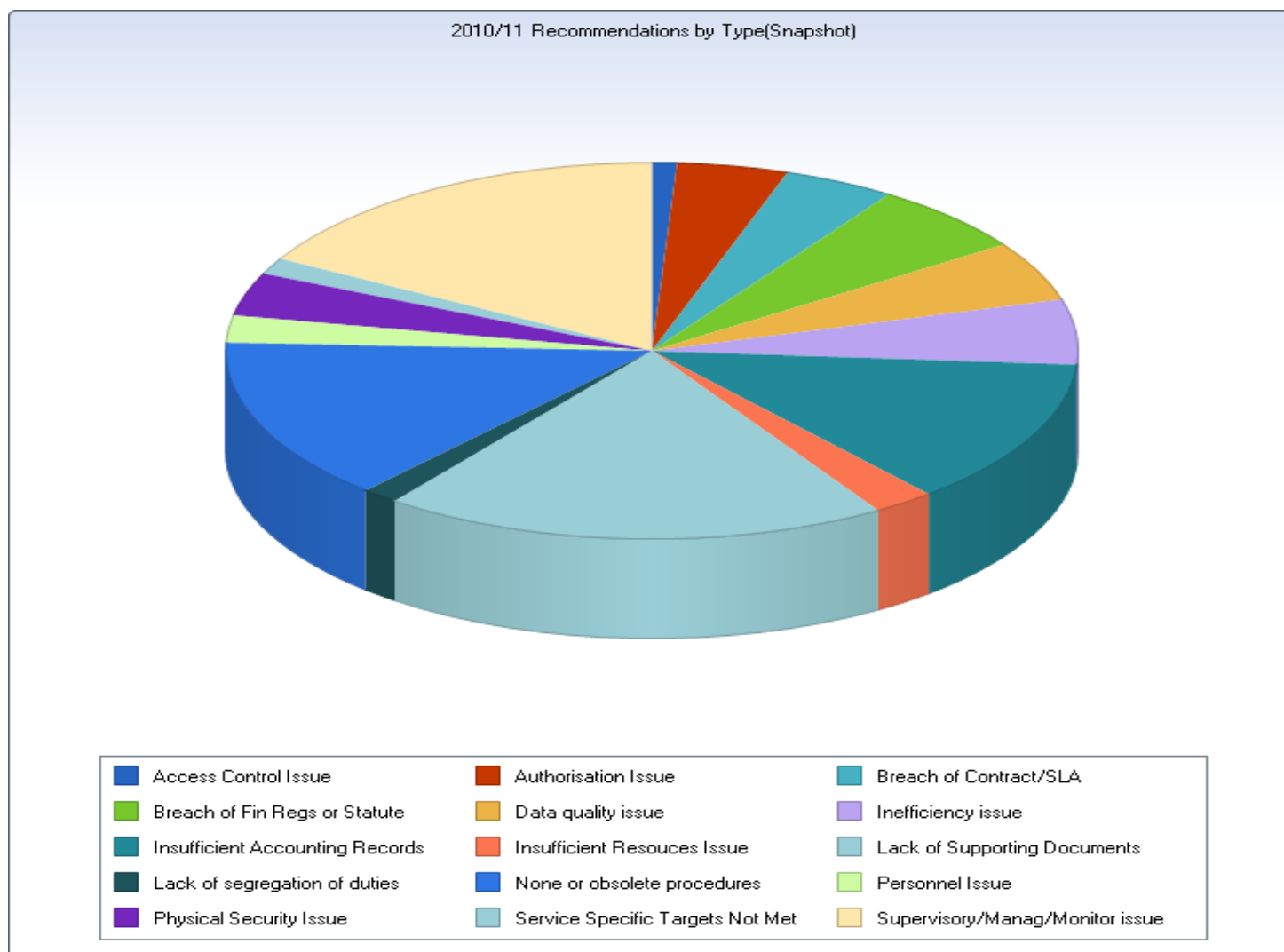
<b>Assurance Level</b>	<b>Definition</b>
Full Assurance	There is a sound system of control designed to achieve all the objectives tested.
Substantial Assurance	While there is a basically sound systems and procedures in place, there are weaknesses, which put some of these objectives at risk. It is possible 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 In any case where Internal Audit have been able to provide no assurance or there has been a significant number of priority one recommendations, based on the review and testing undertaken, a full management response has been presented at the Audit Sub Committee. In addition responsible officers are called to account for the reasons for the weaknesses and giving Members assurance of their management actions agreed with Internal Audit. These actions are then followed up and reported within a six month timescale. On other audits reviews with less material weaknesses but those still requiring urgent management action it has been agreed that responsible officers will be required to attend the meetings where satisfactory action has not been taken.
- 3.15 Appendix 1 lists the reports requiring special attention as a result of priority one recommendations both 2010/11 and previous years and reported to Members over the period

including progress on implementation. As reported in March 2011 to this committee, there were nine priority ones regarded as outstanding.

- 3.16 A listing of completed audits is given in appendix 2. The opinion details are given for each audit. Recommendations have been made in all reports and these are normally categorised as areas requiring immediate management attention as priority one, those that do not represent good practice as a priority two or finally suggestions for improvement at a priority three.
- 3.17 The summary of audit work undertaken resulted in 75 final reports excluding schools work. Of these 39 were classified with full or substantial assurance and 15 limited assurances were given with no nil assurances issued in the year. The remainder were follow up reports or investigation reports. Overall 207 improvement recommendations have been made in the year.
- 3.18 Typical control issues highlighted in the audit reports 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.

3.19 These control issues led to recommendations that were broadly categorised as follows;



Recommendation Category	% of all recommendations	
	2009-10	2010-11
Access Control Issue	1%	1%
Authorisation Issue	3%	4%
Breach of Contract/SLA	1%	4%
Breach of Financial Regulations or Procedures	13%	6%
Data quality issue	4%	5%
Inefficiency issue	4%	5%
Insufficient Accounting Records	11%	12%
Insufficient Resources Issue	1%	2%
Lack of segregation of duties	1%	1%
<b>Lack of Supporting Documents</b>	<b>24%</b>	<b>20%</b>
<b>None or obsolete procedures</b>	<b>13%</b>	<b>14%</b>
Personnel Issue	1%	2%
Physical Security Issue	2%	4%
<b>Supervisory/Monitor issue</b>	<b>21%</b>	<b>19%</b>
Service Specific Targets not met	N/A	1%



- 3.20 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 categorisation of recommendations into the above groups is a relatively new feature as this is the second year. The results of the first year demonstrated that the top three headings are lack of evidence, procedures and supervisory issues. These main heading types have been replicated in 2010/11. 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.
- 3.21 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.
- 3.22 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.
- 3.23 In conclusion, my overall opinion on the control environment based on the internal testing and reviews undertaken is that I am able to place 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 mitigated the risks. I can confirm that 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.
- 3.24 In summary the process 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
  - Outcomes from the formal risk assessment and evaluation ( risk register)
  - Relevant self-assessments of key service areas within the directorate
  - Relevant internal audit reports and results of follow ups regarding implementation of recommendations
  - Outcomes from reviews of services by other bodies including Inspectorates, external auditors etc.
- 3.25 For the full Statement please see Appendix 3.

#### **4 LEGAL IMPLICATIONS**

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

Non-Applicable Sections:	Finance, Policy, Personnel
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Background Documents: Access via Contact Officer)	Audit sub reports
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