

Agenda Item	6
Report No	AS/7/18

## HIGHLAND COUNCIL

**Committee:** Audit & Scrutiny Committee

**Date:** 14<sup>th</sup> June 2018

**Report Title:** **Internal Audit Annual Report 2017/18**

**Report By:** Corporate Audit Manager

### **1. Purpose/Executive Summary**

- 1.1 The attached report includes an assessment of the Council's framework of governance, risk management and control, and the associated opinion which provides information for the Council's Annual Governance Statement.

### **2. Recommendations**

- 2.1 The Committee is invited to note the content of the report, the audit opinion provided and to raise any relevant points with the Corporate Audit Manager.

### 3. Annual Report 2017/18

- 3.1 The Public Sector Internal Audit Standards requires that the Chief Audit Executive (the Corporate Audit Manager):

*“Delivers an annual internal audit opinion and report that can be used by the organisation to inform its governance statement.*

*The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and control.*

*The annual report must also include a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.”*

These requirements have been met by the report provided at **Appendix 1** with section 2 of the report used to inform the Council’s Annual Governance Statement.

- 3.2 The annual report also provides an overview of the Internal Audit Section’s activities and performance data for 2017/18.

### 4. Implications

- 4.1 There are no Resource, Legal, Community (Equality, Poverty and Rural), Climate Change/Carbon Clever, Risk or Gaelic implications. Any issues identified have already been addressed within previous reports to Committee.

Designation: Corporate Audit Manager

Date: 6<sup>th</sup> June 2018

Author: Donna Sutherland

Background Papers:



**The Highland Council**

**Internal Audit Annual Report 2017/18**

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## **1. INTRODUCTION**

- 1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1<sup>st</sup> April 2017 to 31<sup>st</sup> March 2018, and a report that can be used by the Highland Council to inform its Annual Governance Statement.
- 1.2 This report has been produced in accordance with the requirements of the Public Sector Internal Audit Standards (the Standards) which came into effect from 1<sup>st</sup> April 2013 and apply to all internal audit service providers. These Standards were developed in collaboration between the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors (CIIA).
- 1.3 Section 2450 of the Standards states that *“the annual Internal Audit opinion must conclude on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and control. In addition, the annual report must incorporate:*
  - *The opinion;*
  - *The summary of work that supports that opinion; and*
  - *A statement on conformance with the Standards and the results of the quality assurance and improvement programme”.*
- 1.4 This report also includes an overview of the Internal Audit Section’s activities for the financial year 2017/18.

## 2. ANNUAL GOVERNANCE STATEMENT

### 2.1 Internal Control

The Council's Financial Regulations require Service Directors to ensure the principles of internal control are incorporated in the working practices of their Services.

Internal control is defined as *"the whole system of checks and controls, financial or otherwise, established by management in order to provide reasonable assurance"* regarding the achievement of one or more of the following objectives:

- The reliability and integrity of information.
- Compliance with policies, plans, procedures, laws, regulations and contracts.
- The safeguarding of assets.
- The economical and efficient use of resources.
- The accomplishment of established objectives and goals for operations or plans.

Any system of control can only provide reasonable, and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud or breaches of laws and regulations. Accordingly the Council should seek continual improvement in the effectiveness of its systems of internal control.

### 2.2 Internal Audit

The Standards define internal auditing as *"an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes"*.

The work undertaken by Internal Audit is documented in an audit report and issued to management. Any areas of concern together with the management agreed actions and target dates for implementation are summarised in an Action Plan within the report. It is the responsibility of management to ensure that implementation of these actions takes place as agreed. The Internal Audit Section will undertake periodic follow-up reviews to ensure that the management agreed actions have been satisfactorily implemented and the results of this are reported to the Audit & Scrutiny Committee.

The Internal Audit Section operates in accordance with the Standards and as required, a risk based tactical audit plan is produced each year, and submitted for approval to the Audit & Scrutiny Committee. Organisational independence is demonstrated by the Corporate Audit Manager reporting in her own name to senior management, and having direct access to the Chief Executive, Audit & Scrutiny Committee, Pensions Committee, and/ or other Members as considered appropriate.

The Standards require that there is periodic self-assessment against the Standard's requirements and that an external assessment is conducted at least once every five years by a qualified, independent assessor from outside the organisation. The external assessment was undertaken last year and the report by the Audit & Risk Manager from West Dumbartonshire which concluded that the Internal Audit Service **Generally Conforms** with the Standards was reported to the Audit & Scrutiny Committee on 02/03/17. Where the assessment identified areas for improvement these were detailed in an action plan and a number of management actions were agreed. The last action to be completed is the amendment of the Internal Audit Charter. Therefore the self-assessment completed for 2017/18 now shows full compliance with the standards as summarised at Table 1 overleaf.

### Summary of conformance with the Standards

Table 1

Reference	Assessment Area	Fully Conforms 	Generally Conforms 	Partially Conforms 	Does Not Conform 
Section A	Definition of Internal Auditing				
Section B	Code of Ethics				
Section C	Attribute Standards				
1000	Purpose, Authority and Responsibility				
1100	Independence and Objectivity				
1200	Proficiency and Due Professional Care				
1300	Quality Assurance and Improvement Programme				
Section D	Performance Standards				
2000	Managing the internal Audit Activity				
2100	Nature of Work				

Reference	Assessment Area	Fully Conforms 	Generally Conforms 	Partially Conforms 	Does Not Conform 
2200	Engagement Planning				
2300	Performing the Engagement				
2400	Communicating Results				
2500	Monitoring Progress				
2600	Communicating the Acceptance of Risks				

### **2.3 Internal Audit work**

The 2017/18 audit plan was approved by the Audit & Scrutiny Committee on 02/03/17. All audit reports issued are provided as a standing agenda item to each Committee meeting together with progress against the Plan. Where the Plan has required to be adjusted during the course of the year all amendments have been set out in the progress report and have been approved by Members.

A summary of the audit reports issued together with the audit opinion and grades is provided at Section 3.2.

### **2.4 Areas of concern**

Any areas of concern identified from an audit review will result in an audit recommendation being made which is contained within an action plan. These recommendations are graded as high, medium or low; high defined as *“major issues that managers need to address as a matter of urgency”*.

During 2017/18, a total of 72 audit recommendations were made with 38 of these were classified as high grade. A full breakdown of the audit grades and the overall audit opinions can be found at Table 3 on pages 13 - 14. There are no particular themes or issues identified within the high graded recommendations.

The 2016/17 report referred to 3 high grade actions being addressed by management but were taking longer to implement than originally planned. Both actions relating to Inverness Old Town Arts and Inverness City Arts Group have now been closed following the advice of the Council's External Legal Advisors. The final action is in respect of Ben Wyvis Primary School and the rollout of tablets and software to area based Clerk of Works. This has been delayed due to the wider issue relating to the ICT rollout. As this particular action is not a significant governance issue it will not be reported in future years.

### **2.5 Action Tracking**

As part of the audit process, all audit recommendations these are action tracked to ensure that the agreed actions were implemented as agreed. The results of the action tracking, including delays in achieving the target dates are reported to the Audit & Scrutiny Committee on a six-monthly basis with reports provided on 16/06/17 and 23/11/17.

The action tracking process also allows for revision of the agreed action target dates. All actions were either satisfactorily implemented or revised target dates were agreed.

### **2.6 Assurances from Services**

As part of the Annual Accounts process, the Chief Executive and Service Directors are asked to provide assurance that the following statements are valid:

- That Financial Monitoring Statements are regularly reviewed at Service Management Meetings.
- That Staff have been made aware of Financial Regulations and Contract Standing Orders.
- That Staff have been made aware of the Code of Conduct, Information Systems Security, Fraud and Corruption and Whistle blowing policies.
- That the Service has a robust scheme of delegation and that Staff have been informed of their supervisory and accountability responsibilities and that their responsibilities are documented in a Job Description.
- That segregation of duties is an important control mechanism operation within the Service and where it has not been possible to operate such a control a suitable alternative is in place.
- That appropriate targets have been established within the Service to measure financial and other performance.
- That a formal system of project management, including project governance operates within the Service.

- That appropriate arrangements are in place to govern companies.

The necessary assurances have been provided and no issues have been highlighted which affects the Annual Governance Statement which forms part of the Council's Annual Accounts.

## **2.7 Governance arrangements**

The Council has a Local Code of Corporate Governance, which is consistent with the principles and reflects the requirements of the CIPFA/SOLACE Framework Note for Scottish Authorities – Delivering Good Governance in Local Government (2007). This framework has been updated with regard to the CIPFA Statement on the "*Role of the Chief Financial Officer (CFO) in Public Service Organisations*" and a supporting CIPFA/ SOLACE application note has been produced which shows that the Council complies with most of the additional governance requirements.

The Head of Corporate Governance is responsible for:

- Overseeing the implementation of the Local Code of Corporate Governance and monitoring its operation
- Reviewing the operation of the Local Code of Corporate Governance in practice
- Reporting annually to the Council on compliance with the Local Code and any changes required to maintain it and ensure its effectiveness.

The 2017/18 Code was approved by the Highland Council on 26/10/17.

The Council's corporate governance arrangements are subject to annual review by Internal Audit and the work undertaken in respect of the 2017/18 Local Code has not identified any control weaknesses in the Council's governance arrangements.

## **2.8 Risk Management**

Risk management is a key element of Corporate Governance. The Council has a risk management strategy which demonstrates its commitment to maintaining a structured approach to risk management and ensuring that it effectively manages its risks. This was recently updated in line with current best practice and approved by the Audit & Scrutiny Committee on 28/03/18.

The Corporate Risk Register is reviewed on a six-monthly basis and the results of these reviews were reported to the March and September meetings of the Audit & Scrutiny Committee.

## **2.9 Audit Opinion**

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's framework of governance, risk management and control for the year to 31<sup>st</sup> March 2018.

### 3. INTERNAL AUDIT GRADINGS AND OPINIONS

3.1 During the year, a total of 19 final reports were issued. Where the report contains an audit recommendation, this is given a grading of high, medium or low. In addition, the report contains an overall audit opinion which is used to inform the annual statement on internal control. With regard to the audit opinion, there are five levels of assurance which have the following definitions:

Level	Definition
<b>Full Assurance</b>	There is a sound system of control designed to achieve the system objectives and the controls are being consistently applied.
<b>Substantial Assurance</b>	While there is a generally a sound system, there are minor areas of weakness which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.
<b>Reasonable Assurance</b>	Whilst the system is broadly reliable, areas of weakness have been identified which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.
<b>Limited Assurance</b>	Weaknesses in the system of controls are such as to put the system objectives at risk, and/ or the level of non-compliance puts the system objectives at risk.
<b>No Assurance</b>	Control is generally weak, leaving the system open to significant error or abuse, and/ or significant non-compliance with basic controls leaves the system open to error or abuse.

3.2 Table 2 below, provides a summary of the audit reports issued together with the audit opinion, number of recommendations and a breakdown of the associated grades.

*Table 2*

Report Name	Report Date	Audit Opinion	No. of Recommendations	High	Medium	Low
Investigation into missing school meals income at a Primary School	06/04/17	Limited	5	2	3	0
Planning and Building Control Fees and Charges	27/04/17	Reasonable	5	2	2	1
Compliance with the Carbon Reduction Commitment Energy Efficiency Scheme 2015/16	31/05/17	Limited	5	3	2	0
Review of the arrangements for procurement & payment of Homeless Services	05/06/17	Limited	3	3	0	0
Review of Financial Procedures in Schools	15/06/17	Reasonable	7	4	2	1
Commissioned HLH Services	03/08/17	Substantial	3	0	3	0
Review of Burials and Cremations – Policy, Legislation and Processes	05/09/17	Limited	9	6	2	1
Inspection of Roads and Bridges	11/09/17	Substantial	3	1	1	1
Repairs and Maintenance - Care & Learning Properties	15/09/17	Limited	5	3	2	0

<b>Report Name</b>	<b>Report Date</b>	<b>Audit Opinion</b>	<b>No. of Recommendations</b>	<b>High</b>	<b>Medium</b>	<b>Low</b>
Secondary School Investigation – System Weaknesses	20/09/17	Limited	6	6	0	0
Renewable Heat Incentive Income Scheme - follow up	01/11/17	Full	0	0	0	0
Leader Programme 2016/17	13/11/17	Substantial	4	2	2	0
Cromarty Primary School - Review of Extension & Refurbishment Project	14/11/17	Limited	4	1	3	0
Out of Hours Social Work Service	21/11/17	Reasonable	4	1	2	1
European Maritime and Fisheries Fund 2016/17	21/11/17	Full	0	0	0	0
Investigation into missing school meals income at a Primary School	18/12/17	N/ A	0	0	0	0
Delivery of the Scottish Housing Quality Standard Programme within the HRA Capital Programme	19/12/17	Substantial	2	0	1	1
PPP Schools Contracts – Review of Value for Money Arrangements	07/02/18	Substantial	2	0	2	0
Review of the control of overtime within Community Services	20/03/18	Reasonable	5	4	1	0
<b>Totals</b>			<b>72</b>	<b>38</b>	<b>28</b>	<b>6</b>

#### 4. PERFORMANCE DATA

##### 4.1 Performance Data

In accordance with the Standards (PSIAS) a new Quality Assurance Improvement Programme (QAIP), which gives assurance over, and measures the Internal Audit activity, was introduced. This includes performance indicators which are reported to Committee on a quarterly basis. The information for the full year is set out in Table 3 below.

*Table 3*

Category	Performance Indicator	Target	2015/16	2016/17	2017/18	Within Target?
<b>Financial</b>						
Cost of Internal Audit	Actual net expenditure v budgeted net expenditure, expressed as a percentage	<100%	93%	92%	90%	✓
	Cost per £m net expenditure	Within lowest quartile (8 <sup>th</sup> or less) of CIPFA benchmarking comparators	N, 10th	Y, 5th	Not yet available	N/A
<b>Quality</b>						
Client Feedback	Percentage of satisfaction from individual audit engagements expressed through Client Audit Questionnaire	75%	85%	85%	85%	✓
	Percentage of Client Audit Questionnaires returned	70%	84%	90%	81%	✓
<b>Business Processes</b>						
Implementation of Recommendations	Percentage of recommendations accepted v number of recommendations made	95%	99%	99%	99%	✓
Timeliness of Final Report	Percentage of draft reports responded to by client within 20 days of issue	85%	68%	54%	64%	×
	Percentage of final reports issued within 10 days of receipt of management response	90%	92%	97%	100%	✓
Training & Development	Average number of training and development hours per employee	2 days or more	15 days	18.5 days	5.8 days	✓
Sickness Absence	Number of days absence per employee	Less than 5 days per annum	17 days	11 days	5.6 days	×

Comments on the performance data which is not within target:

Timeliness of final report

This is reported on a quarterly basis to Committee and significant improvements were made during the year. Therefore, it is expected that this will continue to improve and this target met during 2018/19.

Sickness absence

This is just short of the target and there were no issues with long-term sickness absence. However, the Section did have a lot of staff unwell over the winter period.