

# Report to Audit Committee

12<sup>th</sup> July 2018

By the Chief Internal Auditor



## INFORMATION REPORT

Not Exempt

### Internal Audit – Annual Report and Opinion 2017/18

#### Executive Summary

This report has been compiled to:

- Provide a statement on conformance with the Public Sector Internal Audit Standards.
- Summarise the effectiveness of internal audit work.
- Summarise the work undertaken by Internal Audit during 2017/18 and provide an overall opinion on the adequacy of the Council's governance arrangements, risk management systems and control environment.

#### Recommendations

- i) To note the summary of audit and project work undertaken since March 2018.
- ii) To note the statement of compliance with the Public Sector Internal Audit Standards.
- iii) To note the performance of internal audit against performance targets.
- iv) To note the opinion of the Chief Internal Auditor on the overall adequacy and effectiveness of the Council's internal control environment, governance and risk management systems.

#### Reasons for Recommendations

- i) To comply with the requirements set out in the Public Sector Internal Auditing Standards 2013 (amended 01/04/17).
- ii) The Audit Committee is responsible for reviewing the effectiveness of the Council's system of internal control.

**Background Papers:** (i) Internal Audit Reports (ii) Orbis Quality Assurance Improvement Programme - External Validation

**Consultation:** N/A

**Wards affected:** All

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# Background Information

## 1. Introduction and Background

### 1.1 Purpose of Report

The main purposes of the report are to:

- Provide a statement on conformance with the Public Sector Internal Audit Standards, and the results of the Orbis Self-Assessment with external independent validation.
- Provide feedback on the performance of the Internal Audit Section during the year.
- Summarise the work undertaken by the Council's Internal Audit Section and provide management and Members with an overall opinion on the adequacy and effectiveness of the Council's governance arrangements, risk management systems and internal control environment.

Internal audit work can provide 'reasonable', not 'absolute', assurance and it cannot guarantee that any system reviewed is free from material weakness. The opinion given on the overall system of internal control is based primarily on the audit work undertaken.

### 1.2 Quarterly Reports

The Audit Committee receives periodic reports on the work carried out by Internal Audit as part of the Council's governance arrangements. Please see Appendix 3 for the summary of work undertaken by Internal Audit since March 2018.

### 1.3 Strategic Audit Plan

The Internal Audit plan is a risk-based plan prepared by the Chief Internal Auditor in consultation with senior managers. Systems which are considered to be fundamental to the Council's operations, or that are considered to be high risk, are normally reviewed on an annual basis.

### 1.4 Staffing

During 2017/18, the audit team operated with 2.6 members of staff (two full time employees and one part-time employee). All auditors have the requisite experience to effectively fulfil their responsibilities, and all members of the team are professionally qualified.

## **2. Relevant Policy / Professional Standards**

### **2.1 Statutory Background**

The Accounts and Audit (England) Regulations 2015 state that “A relevant authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance.” This responsibility is discharged through the Council’s Internal Audit Section.

### **2.2 Relevant Professional Standards**

Internal Audit follows the standards set out in the Public Sector Internal Audit Standards 2013.

The Chief Internal Auditor is required to report on an annual basis to provide an opinion on the overall adequacy and effectiveness of the Council’s governance arrangements, risk management systems and internal control environment.

### **2.3 Relevant Council Policy**

The Council’s Constitution supports the statutory requirements outlined above. Financial Procedure Rule 4e 32 states that: “the Chief Finance Officer, as determined by the Council, will ensure that the Council has appropriate arrangements in place to maintain an adequate and effective internal audit”. The terms of reference for Internal Audit are detailed in the Council’s Internal Audit Charter which is approved and reviewed by the Audit Committee.

## **3. Compliance with the Public Sector Internal Audit Standards**

3.1 The Council’s Internal Audit Service is operated in accordance with the Public Sector Internal Audit Standards (PSIAS) which came into effect on 1st April 2013. The standards require that an external quality assessment is undertaken every five years by a qualified, independent assessor or assessment team from outside the organisation. The internal audit service at Horsham is now provided by the Orbis Partnership which has recently been externally reviewed by SWAP (the South West Audit Partnership).

3.2 The internal audit team joined the Orbis Partnership on 1<sup>st</sup> April 2018. The decision to join the Partnership was made in the previous financial year, and the last financial year 2017/18 has allowed a period of transition during which Orbis processes and ways of working have been adopted. It follows, therefore, that Horsham D.C is able to place reliance on the SWAP external assessment.

- 3.3 The results of the external review are the subject of a separate report. However, in summary, the independent external assessor's overall conclusion is that the service has achieved the highest level of conformance.
- 3.4 The Internal Audit Team has maintained its independence throughout 2017/18 in accordance with the Audit Charter.

## 4. Effectiveness of Internal Audit

### 4.1 Performance against the Annual Internal Audit Plan

The Internal Audit team uses a risk based approach when determining the annual audit plan and undertaking audit assignments. In order to respond to new risk areas identified during the year, the audit plan was sufficiently flexible to allow for additional audits to be undertaken.

During the year, 88% of audits on the 2017/18 audit plan were completed. Please see table below:

Performance	2017/18
Number of Audits Planned	24
Number of Audits Completed	21
Percentage Target	85%
Percentage Achieved	88%

#### Planned reviews not undertaken during 2017/18:

- Contract Management (included in the audit plan for 2018/19)
- Rural Car Parks (as reported to the Audit Committee in December 2017)
- Cloud Computing (as reported to the Audit Committee in December 2017)

#### Other amendments to the Audit Plan during 2017/18:

- As reported to the June 2017 Audit Committee meeting, Parking Enforcement was replaced by a review of the ANPR system. Parking Enforcement has been included in the audit plan for 2018/19.
- As reported to the June 2017 Audit Committee meeting, Mobile Devices was replaced by an initial review of cyber controls. Further audit work on cyber controls has been included in the audit plan for 2018/19.
- As reported to the December 2017 Audit Committee meeting, the audit follow up of building security was replaced by an audit follow up of bulky waste.

The following work was also undertaken:

- Special Investigation which led to the resignation of a member of staff.
- Orbis Integration – Project plan developed and implemented.
- Development of a Corporate Document Retention Policy.
- Training and support provided to senior officers and Members on the workings of the Housing Benefit Subsidy Grant.
- Audit of the Private Sector Housing Assistance Grant claim.
- Membership of the Corporate Governance Group.
- Membership of the Project Review Group.
- Membership of the GDPR Board.
- Anti-Fraud & Corruption Policy reviewed and updated.
- Support provided for risk management (including training to senior officers).
- Development of a risk management toolkit for projects.
- NFI (National Fraud Initiative) work.
- Input into the Annual Governance Statement.

#### 4.2 Implementation of agreed actions within the agreed timescale

The percentage of agreed action items implemented is one of the measures used to demonstrate the effectiveness of the audit team, although the actual implementation of agreed actions is a management responsibility.

From a review of 144 agreed actions for the previous financial year (2016/17), 139 have been implemented (97%) which is an improvement on the previous year.

Performance	2015/16	2016/17
No. of agreed actions for the year	135	144
No. of agreed actions implemented as at 31 <sup>st</sup> March	128	139
Percentage of Agreed Actions Implemented	95%	97%

Details continue to be reported to the Audit Committee which monitors progress on a quarterly basis.

#### 4.3 Reporting

“Draft” audit reports and working papers are subject to a quality review undertaken by the Chief Internal Auditor (CIA) before the final report is issued. There is a performance indicator which measures the percentage of audit reports issued within 15 days of the final audit meeting. The target for 2017/18 was set at 85%, and 92% has been achieved.

A target for issuing the “points arising” document within 15 days of receipt from the auditor was set, but due to a fundamental change in the process, this performance measure no longer applies.

#### 4.4 Management Feedback

On completion of each audit assignment, the Chief Internal Auditor consults management formally to obtain their opinion on the approach and value of the audit work. The target for “very good”, “good” and “satisfactory” performance was set at 95%. 100% has been achieved.

### 5. Opinion on the Control Environment

5.1 This section of the report draws attention to any issues the Chief Internal Auditor considers are particularly relevant to the preparation of the Annual Governance Statement and includes an opinion on the overall adequacy and effectiveness of the Council’s governance arrangements, risk management systems and internal control environment and discloses any qualifications to that opinion, together with the reasons for the qualification.

5.2 The overall opinion is that “**Satisfactory**” assurance can be given that there is generally a sound system of internal control designed to meet the Council’s objectives, and that the controls are generally being applied consistently. The opinion is based upon audit work undertaken during the year. The number of outstanding agreed action items from audit follow ups has also been taken into account.

<b>Assurance Areas:</b>	
Governance	<p>The Council is committed to the principles of good corporate governance, which are already demonstrated through many aspects of good practice.</p> <p>A number of improvements have been made in respect of the Council’s Governance Framework during 2017/18. In particular, a programme of regular governance training has been developed (e.g. health &amp; safety, anti-fraud, information and data security). This has been incorporated into the Council’s online appraisal system.</p>
Risk Management	<p>The Council’s risk management framework is now embedded into the culture of the authority. The Corporate Risk Register is formally reviewed quarterly by the Senior Leadership Team and Members of the Audit Committee. Every department maintains its own departmental risk register (including outsourced</p>

	functions), and an escalation process is in place. Project risks are considered, and a proportionate approach is taken depending upon the size and importance of the project.
Internal Control	The table of internal audit assurance opinions, in Appendix 1, shows the individual audit opinions from the audit assignments undertaken during 2017/18. Where significant control weaknesses have been identified, remedial action has either been implemented or is programmed to be implemented within three months in accordance with the Council's risk appetite.

### 5.3 **Qualification to the Opinion**

The audit opinion is based upon, but not limited to, the work performed by internal audit during the year. The opinion does not imply that Internal Audit has reviewed all risks and controls relating to the Council, but is based upon the range of individual opinions arising from risk based audit assignments completed during 2017/18. Opinions for individual audits are detailed in Appendix 1 of this report, and definitions of the opinions can be found in Appendix 2.

### 6. **Next Steps**

Not applicable.

### 7. **Outcome of Consultations**

Not applicable.

### 8. **Other Courses of Action Considered but Rejected**

Not applicable.

### 9. **Resource Consequences**

There are no direct staffing consequences.

### 10. **Legal Consequences**

There are no financial consequences. Where compliance issues are identified during audit fieldwork, the Head of Legal & Democratic Services (or relevant legal specialist) will be consulted.

## **11. Risk Assessment**

The Internal Audit function contributes to the effectiveness of the Council's risk management arrangements.

All Internal Audit work is undertaken using a risk based approach.

## **12. Other Considerations**

Internal Audit is a reporting function and there are no consequences in respect of Crime & Disorder; Human Rights; Equality & Diversity; or Sustainability. However these areas are considered where appropriate during audit fieldwork.

## Appendix 1

AUDITS	INTERNAL AUDIT ASSURANCE OPINIONS			
	SUBSTANTIAL	REASONABLE	PARTIAL	MINIMAL
HACKNEY & PRIVATE HIRE LICENCES		✓		
COMMERCIAL RENTS		✓		
USE OF CONSULTANTS		✓		
FORWARD PLAN		✓		
NEW FMS – DATA MIGRATION		✓		
COMMUNITY LINK ALARMS		✓		
CASUAL WORKERS		✓		
COUNCIL TAX	✓			
NNDR		✓		
BULKY WASTE (FOLLOW UP)		✓		
PAYROLL			✓	
CASH & BANK		✓		
ACCOUNTS PAYABLE		✓		
ACCOUNTS RECEIVABLE		✓		
TREASURY MANAGEMENT	✓			
HOUSING BENEFITS		✓		

*Note: The Horsham Internal Audit Team audited the Council Tax and NNDR systems on behalf of Horsham and Mid Sussex District Councils. The audit of Housing Benefits was undertaken by the Crawley Internal Audit team, and reliance has been placed on this work.*

## Appendix 2

### SUMMARY OF INTERNAL AUDIT ASSURANCE OPINIONS

Opinion	Definition
<b>Substantial Assurance</b>	Controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
<b>Reasonable Assurance</b>	Most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
<b>Partial Assurance</b>	There are weaknesses in the system of control and/or the level of non-compliance is such as to put the achievement of the system or service objectives at risk.
<b>Minimal Assurance</b>	Controls are generally weak or non-existent, leaving the system open to the risk of significant error or fraud. There is a high risk to the ability of the system/service to meet its objectives.

## Appendix 3

### Summary of audit work completed during Quarter 4

#### 1. Summary of Audit Findings

##### 1.1 Treasury Management

OVERALL AUDIT OPINION: **SUBSTANTIAL ASSURANCE** (↑)<sup>1</sup>

There is a sound system of control in place for Treasury Management and audit testing identified that expected controls are being consistently applied.

##### 1.2 Cash and Bank

OVERALL AUDIT OPINION: **REASONABLE ASSURANCE** (↑)

There is good separation of duties, and the Council maintains a daily cash flow forecast that ensures that bank account balances are monitored on a daily basis which ensures funds are deployed as efficiently as possible. A new and improved bank reconciliation process has been developed following the migration of the FMS to Technology 1 (T1), and this has facilitated more timely completion of the month end reconciliations. All timing differences and other outstanding items are reported and there are no unidentified differences on the reconciliations.

Some weaknesses in control have been identified, but none of these are considered to be high risk items. Actions have been agreed to:

- Improve the transparency of outstanding items when reconciling the income suspense account, and
- Ensure that '*number combinations*' that provide access to the Finance safe are changed when a member of staff (who knows the combination number) leaves the organisation.

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<sup>1</sup> The symbols in brackets indicate the movement in the level of assurance when the area was last audited.

(↑) = Improved.

(↔) = No change.

(↓) = Reduced.

If blank ~ No previous opinion

### 1.3 Housing Benefits

OVERALL AUDIT OPINION: **REASONABLE ASSURANCE** (↑)

The Horsham D.C subsidy grant was qualified by Ernst and Young (External Audit) during 2014/15 and 2015/16 which had resulted in significant financial clawbacks. This was largely due to data input errors spanning a number of years. A data cleansing exercise was commissioned at the beginning of 2017 which has improved the quality of data, and this improvement is reflected in the results of the subsidy grant audit for 2016/17.

The Housing Benefits internal audit for 2017/18 was undertaken by the Crawley Internal Audit team, and they concluded that there were no *new* significant weaknesses in control. The audit of the Housing Benefits system included a follow up of agreed actions from the previous audit, and most of these had been implemented. However, it was identified that one high priority item had not been implemented:

*“Quality Assurance information will be used to develop the annual training programme for individuals and general team needs”.*

This action has now been reassigned, and is scheduled to be completed by the end of June 2018.

### 1.4 Accounts Payable and Receivable

OVERALL AUDIT OPINION: **REASONABLE ASSURANCE** (↔)

The Council introduced the new ‘Technology One’ financial information system in September 2017. Because of the significant impact on the Finance Team, and in particular, the loss of their experienced Systems Accountant shortly after implementation, Internal Audit restricted its review of the accounts payable and accounts receivable systems to the identification and testing of ‘key system’ controls.

From the limited focus of this review, we did not identify any control weaknesses that could place system objectives at risk. It was noted, however, that no debts had been written off during 2017/18. It was agreed that these would be written off within the 2018/19 financial year once the recently appointed Systems Accountant has had an opportunity to understand the Technology One system.

## 1.5 Payroll

OVERALL AUDIT OPINION: **PARTIAL ASSURANCE** (↓)

Starter and leaver instructions have been correctly authorised by officers within the HR & OD Department, and there continues to be good separation of duties between the authorisation and processing of payroll amendments. There is an effective process in place to review and correct data input errors made by Capita<sup>2</sup>. Whilst control weaknesses have been identified exposing the Council to risk in some areas (see below), the auditor did not identify evidence of any incorrect payments from the sample testing undertaken.

The auditor identified that some of the monthly reconciliations between the General Ledger and SAP Systems had not been completed. Whilst the gross reconciliations were being undertaken and signed off by a senior officer, the net reconciliations were not being completed. Furthermore, some of the control accounts had not been reconciled since the beginning of 2017. The Payroll & Benefits Controller carried out the net reconciliation at the end of the financial year and 18 corrective journals were processed. Further corrective journals have also been processed for some of the control accounts. The corrective journals related to coding errors rather than payment errors (i.e. affecting the management accounts). One of the control account reconciliations revealed that an employee, who had left the Council's employment in the summer of 2017, had not fully repaid a staff loan due to a miscalculation. An invoice has now been raised for £54 to recover the outstanding amount.

The list of departmental authorised signatories for overtime and casual worker instructions is incomplete. Of particular concern is that instructions to make overtime payments to operatives at Hop Oast Depot have not been received from an authorised signatory. Appropriate remedial action has been agreed.

The annual reconciliation between the Staff Establishment and SAP System was not undertaken during 2017/18 to identify discrepancies between the two systems. This will be undertaken shortly, and will be repeated immediately prior to the implementation of the proposed new HR system next year.

## 2. Other Audit Work

2.1 Internal Audit has been involved in a number of activities since the last report to the Committee:

- Orbis Integration – final implementation of project plan.
- Further development of a retention schedule for the Council (in consultation with managers) in preparation for GDPR (General Data Protection Regulations).

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<sup>2</sup> Capita administers Payroll on behalf of West Sussex County Council (Horsham's service provider).

- Active involvement in the following groups:
  - Broadbridge Health Leisure Centre Project Board.
  - GDPR Board.
  - Corporate Governance Group.
  - Project Review Group.