

# Report

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| Report to:       | <b>Executive Committee</b>  |
| Date of Meeting: | <b>27 June 2018</b>   |
| Report by:       | <b>Audit and Compliance Manager (Finance and Corporate Resources)</b> |

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| Subject: | <b>Internal Audit Annual Assurance Report 2017/2018</b> |
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## 1. Purpose of Report

1.1 The purpose of the report is to:-

- ◆ report on the progress and performance of Internal Audit and to provide an independent audit opinion on the adequacy and effectiveness of the Council's governance, risk management and internal control systems based on audit work undertaken in 2017/2018

## 2. Recommendation(s)

2.1 The Committee is asked to approve the following recommendation(s):-

- (1) that the positive performance of Internal Audit be noted;
- (2) that the overall findings from internal audit work and that these findings have informed the Council's 2017/2018 governance statement be noted; and
- (3) that the level of assurance be noted.

## 3. Background

- 3.1 The internal audit service is delivered within South Lanarkshire Council (SLC) within the context of the Public Sector Internal Audit Standards (PSIAS) (revised 1 April 2017), compliance with which is mandatory under Section 95 of the Local Government (Scotland Act) 1973. This sets out a series of standards to ensure a professional, independent and objective internal audit service is delivered that supports good governance within SLC.
- 3.2 PSIAS requires that a Quality Assurance and Improvement Programme (QAIP) is developed to provide assurance that internal activity is conducted in accordance with an Internal Audit Charter, that it operates in an efficient and effective manner and that it is perceived to be adding value and improving operations. This programme includes periodic and ongoing internal assessments as well as an external inspection once in each five year period. An external review was undertaken in 2017/2018 and its conclusions supported the assertion in previous Internal Audit annual assurance reports that SLC's internal audit function generally conforms to the Public Sector Internal Audit Standards. A report on the outcome of this inspection was presented to the Risk and Audit Scrutiny Forum (RASf) on 21 March 2018.
- 3.3 Internal Audit has reported throughout the year to the RASf. Reports to the RASf have detailed the findings from each finalised assignment in conjunction with

information in relation to Internal Audit activity's purpose, authority, responsibility and performance relative to the 2017/2018 Audit Plan.

#### **4. Link to Council's Objectives and Top Risks**

- 4.1 As a function, Internal Audit seeks to link to the Council's Connect Ambition of 'achieve results through leadership, good governance and organisational effectiveness'. Specifically for Internal Audit this relates to the provision of assurance that the Council is well governed financially and operationally and has in place effective control and risk management arrangements. In areas where this is not the case, an action plan is developed and delivery tracked to demonstrate improvements are achieved.
- 4.2 In addition to Connect, assignments within the Audit Plan each year are linked to the Council's top risks to ensure that work is focused in areas of greatest risk and, where potentially, an independent review would add greatest value. The 2017/2018 Plan linked to seven of the Council's top ten risks (as identified in January 2017) with three areas not directly covered by the Plan; failure to develop a sustainable Council and communities, failure to demonstrate continuous improvement, limited strategic direction and a lack of cohesive change management and failure to manage increasing levels of adverse weather. Of these risks, the sustainability agenda was considered in the delivery of all audits within the Plan and change management covered by the programme of Service reviews underway. The remaining risk in relation to adverse weather was not included in the Plan as an audit was unlikely to add value.
- 4.3 PSIAS requires the audit plan to be kept under review as it progresses and this includes a comparison against the Council's top risks as these are reassessed during the year. The Council's top risks, revised in year, include the following three new top risks:
- potential liability arising from claims of historic abuse
  - failure to work with key partners to achieve outcomes of the Local Outcome Improvement Plan
  - implementation of Self Directed Support
- 4.4 In respect of the latter two risks, work was included in the 2017/2018 Plan. In respect of the first risk, Internal Audit forms part of the internal working group tasked with responding to this agenda.

#### **5. Internal Audit Workload – 2017/2018**

- 5.1 The actual number of audit days delivered in 2017/2018 was 1,318 days which was 15.8% above Plan. 97.4% of the Council Plan was delivered by 31 March 2018.
- 5.2 Each of the audits delivered in the year were conducted in conformance with PSIAS.

#### **6. Internal Audit Delivery – 2017/2018**

- 6.1 In terms of an overview of performance, Internal Audit has improved performance in 2017/2018 in relation to completing a greater percentage of the audit plan (97.4%; target 100%) and competing assignments within allocated days (82%; target 80%). Targets were met in relation to issuing draft reports on time (87%; target 80%) and productivity (86%; target 80%), albeit year-on-year performance has marginally declined.
- 6.2 As resources reduce, an increasing proportion of total time is being spent on external client work as well as responding to adhoc requests and participating in Council-wide

scrutiny and review groups. The presence on such groups provides an independent challenge to the work of the Group and ensures that emerging risks are known and addressed if required. Whilst not directly providing an audit opinion, knowledge of Council systems and processes are reviewed as part of the delivery of this role and does assist in the development of a more value-added role for the Service.

- 6.3 PSIAS requires the Council's internal audit function to demonstrate engagement with clients to ensure the Audit Plan is agreed at the outset of the year and continues to address known and emerging risks. Historically this had been achieved through client questionnaires and periodic meetings with Heads of Support Services. Moving forward, feedback will be gathered through annual questionnaires to Heads of Service within whose areas where there has been audit activity in the year and through annual meetings with Executive Directors.

## **7. Financial controls and findings**

- 7.1 The opinion in relation to financial controls has been formed based on two main areas of assurance, namely:

- ◆ a programme of financial audits included within the 2017/2018 Internal Audit Plan and
- ◆ the work of External Audit in relation to the Council's financial statements for the year ended 31 March 2017 (final) and 31 March 2018 (interim)

- 7.2 Interim audit work for 2017/2018 undertaken to date by the Council's External Auditor has been completed and no significant issues have been highlighted in the Interim Management Letter issued by Audit Scotland for the year ended 31 March 2018.

- 7.3 Overall there is a good level of assurance over financial control across the Council. Many significant financial controls are imbedded within systems and these have been tested throughout the year by a programme of internal and external audit testing.

- 7.4 In terms of the more significant financial audit assignments completed in the year, this included a joint audit of Accounts Payable/E-invoicing along with developing reports for Creditors to facilitate payment reviews and undertaking an assessment of PEF governance arrangements. Out with these specific assignments, the Continuous Controls Monitoring (CCM) project continued and has informed 'intelligent' sampling within both routine audits and specific investigations.

- 7.5 Financial investigative work in the year was not significant in terms of volume or value and not such to suggest any fundamental issues within routine financial control arrangements.

## **8. Operational controls and findings**

- 8.1 The opinion in relation to operational controls has been formed based on two main areas of assurance, namely:

- ◆ a programme of operational audits included within the 2017/2018 Internal Audit Plan and
- ◆ the work of external regulators and inspectors

- 8.2 Overall there is an adequate level of assurance over operational control across the Council. Although operational controls generally exist, on occasion, these lack

robust implementation. Controls such as adherence to proper processes and key controls rely on management checks and monitoring and, as operational controls are generally vested in people, this remains an area of higher inherent risk. Adherence to procedures remains key to ensuring a full audit trail is available to support all activity and demonstrate effective governance of Council funds.

8.3 In terms of the more significant operational audit assignments, a review of City Deal project management arrangements was undertaken in the year as well as an assessment of the level of implementation of the Community Empowerment Act. Audits in this area also sought to assess progress with the implementation of Self Directed Support and General Data Protection Regulations and covered Cyber Security and procurement arrangements.

8.4 Other than the specific assignments detailed above, investigative work was of low value and volume in operational areas during 2017/2018. Where appropriate, actions have been agreed or are being discussed with Resources.

## **9. Management of fraud risks**

9.1 There are four main routes for reporting fraud with the Council, whistle-blowing via letter, telephone call, verbal or email, through the CRM system, through local management or from the Police. Two-thirds of concerns reported during the year came through external whistle-blowing or through the CRM system. The remaining one-third of concerns were reported by local management. Irrespective of the source of alert, all notifications are risk assessed and, dependent on an initial evaluation of risk, either investigated by Internal Audit or the Personnel fact-finding team (with assistance from Resources if required) or, if relevant, passed to the Police. Fraud statistics are reported bi-annually to the RASF and a full report will be presented to the RASF detailing 2017/2018 statistics in September 2018.

9.2 The total value of fraud concerns reported to Internal Audit in 2017/2018 equated to £7.3k. The majority of this related to two separate investigations. Significant reputational risk can, of course, attach to frauds irrespective of the value. Audit recommendations are routinely made to address identified gaps in controls and standard fraud indicators are included in all audit programmes, the results of which are considered during the annual planning process.

9.3 In addition to the above investigative work, Internal Audit are responsible for co-ordinating investigation of National Fraud Initiative matches throughout the Council. 98.5% of all target investigations were completed by 31 March 2018. A report on the interim outcome of the NFI exercise was presented to the RASF in March 2018 and a final report on the exercise will be included in the annual Fraud Statistics report presented to the RASF later in the year. It is anticipated that no fraud will be identified by investigations although errors have been highlighted and a value attached to this.

9.4 A corporate fraud programme of work was also included in the 2017/2018 Annual Internal Audit Plan. Two more significant assignments within this programme was in relation to Tenancy Fraud and Abandoned Properties.

9.5 Internal Audit also monitors fraud alerts through internal and external sources and disseminates information as appropriate. In 2017/2018 the majority of the information shared with Council Resources related to fraudulent attempts to change bank details. A specific review of a sophisticated fraud that was perpetrated in another Local Authority is underway with a focus on areas where there is specific risk

of the same control gap within SLC. Appropriate action will be taken to address any identified risks to SLC.

## **10. Council wide Performance – Delivery of audit actions 2017/2018**

- 10.1 PSAIS places a responsibility for monitoring progress with the delivery of audit actions with the Chief Internal Auditor to ensure that recommendations are effectively implemented. Council-wide, 97% of internal audit actions were delivered on time (and 99% in total, with some only marginally late). Only one action remains outstanding as at 31 March 2018 and will now be followed up in 2018/2019. Individual Resource performance information in relation to audit actions is reported within IMPROVe.
- 10.2 The above performance data suggest that actions are being fully and timeously implemented. This is checked independently by a programme of formal follow-up reviews which are undertaken by Internal Audit each year. During 2017/2018, five formal follow-up audit assignments were completed. Of these assignments, all evidenced a degree of completion but there is a growing pattern of recommendations either not being implemented or only partially implemented. Where audit actions are particularly significant more extensive follow up work is now being programmed within audit plans.

## **11. Areas of external reliance**

- 11.1 On an annual basis, an assurance mapping process is undertaken in conjunction with the Good Governance Group to identify significant issues that could impact on the overall opinion expressed within this report. The audit opinion also considers significant partnerships. Assurances are sought in relation to governance arrangements annually by the Council during preparation of the Governance Statement. No issues have been identified that require specific note within this annual report. Internal Audit are represented on the Good Governance Group and through this, contribute to the preparation and development of the Governance Statement.
- 11.2 This includes the shared risk assessment, the output of a process each year that involves the Council and representatives of all scrutiny bodies who engage with the Council. The outcome (a Local Scrutiny Plan) from this in 2017/2018, identified no specific risk-based scrutiny risks for SLC although some areas of the Council's activity were to be the subject of ongoing monitoring and oversight by the Local Area Network during the year. In 2018/2019, a similar position has been identified and there are no scrutiny risks identified. Outwith this Local Area Network, the main area of external reliance is detailed in the paragraphs below.
- 11.3 External Audit undertook the 2016/2017 financial audit during 2017/2018 and provided an unqualified opinion in relation to the Council's financial statements. Interim audit work in relation to the year ended 31 March 2018 has been completed by External Audit and no significant issues identified in the Interim Management Letter that has subsequently been issued. Internal Audit have liaised with External Audit periodically throughout the year as required and have provided specific assistance around the provision of financial year-end data to Audit Scotland.
- 11.4 Audit Scotland also publish reports throughout the year in relation to a variety of areas. Where Resources consider it appropriate, these are reported to Committees covering the key messages and their application to SLC. In 2017/2018, relatively few reports were presented to Committees or Forums. The process for handling

Audit Scotland reports may benefit from a refresh to ensure that a more consistent approach is taken moving forward. Internal Audit will facilitate this review in 2018/2019.

## **12. Summary of overall assurance and audit opinion**

Adequate arrangements exist within SLC to escalate any concerns the Audit and Compliance Manager may have in relation to the level of risk accepted by management or SLC. Throughout the year there was no impairment in the scope of audit work or the ability of Internal Audit to express an independent opinion.

- 12.1 The objective of Internal Audit is to evaluate and improve the effectiveness of risk management, control and governance processes. The purpose of this report is to provide an independent audit opinion on the adequacy and effectiveness of the Council's internal controls based on audit work undertaken in 2017/2018 and by doing so to provide assurance around the overall adequacy and effectiveness of SLC's framework of governance, risk management and control arrangements.
- 12.2 Of the audit assignments completed to draft stage in 2017/2018 that provided an audit opinion, a material number concluded either good or adequate assurance as to the adequacy and effectiveness of controls. Overall, reasonable assurance can be placed on the adequacy and effectiveness of the Council's framework of governance, risk management and control arrangements for the year ending 31 March 2018.

Internal control remains, primarily, a management responsibility to ensure that the Council conducts its business in a manner that has due regard to the principles of good governance. The presence of an internal audit function does not negate the importance of effective internal controls. Internal Audit cannot be expected to give total assurance that control weaknesses or irregularities do not exist. The above financial and operational audit opinions are based upon the audit work undertaken during the year and knowledge of the Council's governance, risk management and control arrangements.

The Committee is asked to note the above findings and approve their inclusion in the Council's annual Governance Statement. An annual Internal Statement of Assurance is included at Appendix One based on the view of the Council's own internal audit function.

## **13. Employee implications**

- 13.1 The Internal Audit service in 2017/2018 was delivered by a team of thirteen. Of the team of thirteen, eleven are partly or fully qualified through either the Chartered Institute of Internal Auditors or one of the Consultative Committee of Accountancy Bodies.

## **14. Financial implications**

- 14.1 Audit and Compliance Services, during 2017/2018 spent £578,793 against a budget of £540,893 (to period 14). The over spend relates primarily to a surplus post that was awaiting redeployment in 2017/2018.

## **15. Other implications**

- 15.1 Each audit assignment seeks to identify efficiencies and report as a part of the audit opinion where appropriate. In practice this often translates into identifying audit recommendations that suggest a more efficient way in which to deliver services. Opportunities to identify 'cash' savings are becoming less frequent in an environment

of growing financial constraints. From Resources perspective, much of the 'value added' element of an internal audit service is linked to the function's ability to provide advice and guidance. In addition, there has been a growing focus on the content of action plans to ensure that these effect required improvements. This is particularly important in areas where issues are more significant.

15.2 Responding to Services' requests for assistance and participation in internal working groups is accommodated within the Plan and through contingency time. This aligns to the PSIAS requirement to deliver an effective internal audit service. The number of days allocated to contingency has been reduced in 2018/2019 to allow maximum audit coverage. This will remain under review during 2018/2019 and may require some revision particularly if a significant level of unplanned or ad hoc work materialises.

15.3 There are no sustainability issues in terms of the information contained in this report.

## **16. Equality impact assessments and consultation arrangements**

17.1 There is no requirement to carry out an impact assessment in terms of the information contained within this report.

17.2 Resource Heads of Service are consulted in advance of every planned audit assignment and following completion of fieldwork. Resources and elected members are also consulted during preparation of the annual audit plan.

**Yvonne Douglas**  
**Audit and Compliance Manager**

5 June 2018

### **Link(s) to Council Values/Ambitions/Objectives**

- ◆ Achieve results through leadership, good governance and organisational effectiveness

### **Previous References**

- ◆ 2017/2018 Quarter One Audit Plan (22 February 2017 RASF )
- ◆ 2017/2018 Quarters Two – Four Audit Plan (RASF 20 September 2017)
- ◆ 2016/2017 Internal Audit Annual Assurance Report (RASF 20 September 2017)
- ◆ 2018/2019 Internal Audit Plan (RASF 21 March 2018)

### **List of Background Papers**

- ◆ 2017/2018 progress reports to the Risk and Audit Scrutiny Forum
- ◆ Figtree statistical and assurance and time recording extracts
- ◆ Public Sector Internal Audit Standards (revised)
- ◆ Fraud statistics and NFI updates

### **Contact for Further Information**

If you would like to inspect the background papers or want further information, please contact:-

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**To the members of South Lanarkshire Council, the Chief Executive and Executive Directors**

As Audit and Compliance Manager of South Lanarkshire Council, I am pleased to present my annual statement and report on the adequacy and effectiveness of the governance, risk management and internal control systems of the Council for the year ended 31 March 2018.

**Respective responsibilities of management and internal auditors in relation to governance, risk management and internal control**

It is the responsibility of the Council's senior management to establish appropriate and sound systems of governance, risk management and internal control and to monitor the continuing effectiveness of these systems.

It is the responsibility of the Audit and Compliance Manager to provide an independent opinion on the adequacy and effectiveness of the governance, risk management and internal control systems of the Council. The Audit and Compliance Manager cannot be expected to give total assurance that control weaknesses or irregularities do not exist but can form an opinion based on work undertaken during the year and knowledge of control systems.

**The Council's framework of governance, risk management and internal controls**

South Lanarkshire Council has a responsibility to ensure its business is conducted in accordance with legislation and proper standards and adheres to and works within a framework of internal values and external principles and standards.

The governance framework comprises the systems and processes, culture and values by which the Council is directed and controlled and how it accounts to communities. It enables the Council to monitor the achievement of its strategic objectives and to consider whether those objectives have led to the delivery of appropriate services and value for money.

The system of internal control is a significant part of that framework and is designed to manage risk to a reasonable level. It cannot eliminate all risk of failure to achieve policies, aims and objectives and therefore only provides reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritise the risks that would prevent the achievement of South Lanarkshire Council's policies, aims and objectives, to evaluate the likelihood and potential impact of those risks being realised, and to manage them efficiently, effectively and economically.

**The work of Internal Audit**

Internal Audit is an independent and objective assurance function established by the Council to review its governance, risk management and internal control arrangements. It objectively examines, evaluates and reports on the adequacy of these arrangements as a contribution to general governance arrangements and more specifically the proper, economic, efficient and effective use of resources.

The Internal Audit Service operated in accordance with the Public Sector Internal Audit Standards (PSAIS) (revised 2017) throughout 2017/2018. An external assessment of the extent of compliance was undertaken in 2017/2018 as part of the Quality Assurance and Improvement Programme. This assessment concluded that the section generally conforms with the requirements set out in PSIAS with actions agreed to address areas of non-compliance identified by the review. These areas of non-compliance are not considered to impact upon the quality of the internal audit service delivered or the audit opinion expressed within this annual report.



The section undertakes an annual programme of work endorsed by the Risk and Audit Scrutiny Forum and approved by the Executive Committee. All plans are based on a formal risk evaluation process, which reflects agreed and emerging risks and changes within the Council and is subject to periodic review throughout the year.

All internal audit reports identifying risks, areas for improvement and/or non-compliance with expected controls are brought to the attention of management and include appropriate recommendations and agreed action plans. It is management's responsibility to ensure that proper consideration is given to internal audit reports and that appropriate action is taken to implement audit recommendations.

Internal Audit ensure that management has understood agreed actions or assumed the risk of not taking action. A programme of informal and formal follow-up audit assignments provides assurance around the complete and timeous implementation of audit recommendations. Significant matters arising from internal audit work are reported to the Executive Director Finance and Corporate Resources and the Council's Risk and Audit Scrutiny Forum.

#### **Basis of opinion**

My evaluation of the control environment relates only to South Lanarkshire Council and is informed by a number of sources but mainly by audit work undertaken during 2017/2018.

#### **Limitation of scope**

No individual audit assignments were specifically limited in scope at the outset but scopes were amended to reflect the output from the initial risk and control analysis undertaken at the start of each assignment and the resources available.

#### **Opinion**

It is my opinion, based on the above, that overall, reasonable assurance can be placed on the adequacy and effectiveness of the Council's framework of governance, risk management and control arrangements for the year ending 31 March 2018.

***Signature:-***

**Yvonne Douglas BA CA**

**26 April 2018**