

Internal Audit Service

2015/16 Opinion on the Framework of Governance, Risk Management and Control

May 2016



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Executive Summary

Overall, Internal Audit work performed in the financial year 2015/16 found that internal control systems in the areas audited were effective.

The majority of audited areas were awarded an audit opinion of 'moderate assurance' or higher. No 'critical priority' or 'high priority' recommendations were made by Internal Audit during the year, and no 'no assurance' audit opinions have been issued or are pending. This demonstrates that overall, a sound approach to governance and control is in place throughout the organisation.

As reported to Audit Committee, a number of areas of good practice were identified throughout the year. In other areas, improvement plans already in place by management, together with Internal Audit's recommendations, will continue to strengthen the organisation's framework of internal control.

The opinion of the Chief Internal Auditor is therefore that, at the time of preparing this report, the organisation's internal control systems in the areas audited are **satisfactory**. This is a positive assessment of the Authority's control environment and reflects favourably on the organisation's governance arrangements.

The control environment of the organisation has changed significantly in recent years, with a number of key services now delivered in partnership with a range of providers. Internal Audit will continue to monitor the impact of different service delivery methods on the framework of governance, risk management and control. The Authority should continue to monitor / manage authorisation and approval controls closely as partnership working progresses.

The organisation overall has a mature and business-focussed approach to its governance arrangements, and a culture where governance and risk management are embedded and given high organisational visibility.

Internal Audit Service

2015/16 Opinion on the Framework of Governance, Risk Management and Control

1 Purpose of Report

- 1.1 This report has been written to provide an annual Internal Audit opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

2 Governance, Risk Management and Control

- 2.1 Management's responsibility for the effectiveness of the internal control system is clearly set out in the Authority's Financial Regulations. The Regulations state¹:

- It is the responsibility of the Chief Finance Officer to assist the Authority to put in place an appropriate control environment and effective internal controls which provide reasonable assurance of effective and efficient operations, financial stewardship, probity and compliance with laws and regulations.
- It is the responsibility of Chief Officers to:
 - Manage processes to check that established controls are being adhered to and to evaluate their effectiveness, in order to be confident in the proper use of resources, achievement of objectives and management of risks.
 - Review existing controls in the light of changes affecting the Authority and to establish and implement new ones in line with guidance from the Chief Finance Officer and Internal Audit. Chief Officers should also be responsible for removing controls that are unnecessary or not cost or risk effective – for example, because of duplication.
 - Ensure staff have a clear understanding of the consequences of lack of control.

¹ Financial Regulations, Version 5a (September 2013), Regulations C.20-C.23

2.2 Appropriate controls will depend, amongst other factors, on:

- The nature, size and volume of transactions;
- The degree of control which management is able to exercise personally;
- The geographical distribution of the enterprise; and
- The cost of operation of the controls against the benefits expected from them.

2.3 There are eight main types of internal control, namely:

Preventative Controls

- (i) Segregation of duties (no one person should be responsible for processing and recording a complete transaction)
- (ii) Authorisation and approval (all financial transactions should require authorisation by an appropriate responsible official; the limits of authorisation should be specified)
- (iii) Physical (custody of / access to tangible assets should be secure and limited to authorised personnel)

Detective Controls

- (iv) Arithmetic & Accounting (controls within the recording function to check that transactions have been authorised, are included, are correctly recorded and are accurately processed)

Directive Controls

- (v) Organisation (responsibilities should be defined and allocated; reporting lines should be identified; delegation of authority should be clearly specified)
- (vi) Supervision (all actions by all levels of staff should be supervised; the responsibility for this supervision should be clearly laid down and communicated to the person being supervised)
- (vii) Personnel (procedures should exist to ensure that staff are competent to carry out the jobs assigned to them, including proper recruitment and performance management procedures, career prospects, training and pay policies)
- (viii) Management (controls exercised by management outside the day to day routine of the system, including supervision).

2.4 When auditing, Internal Audit assist management by testing to see whether the controls established for any given system are appropriate. It is important to stress that Internal Audit, while part of the Authority's overall assurance framework, is not a substitute for effective internal control within the Authority's systems.

3 Opinion on the Adequacy and Effectiveness of the Framework of Governance, Risk Management and Control

- 3.1 The Chief Internal Auditor is required under the Public Sector Internal Audit Standards (PSIAS), introduced in 2013 and revised March 2016, to provide an annual opinion, based on an objective assessment of the organisation's framework of governance, risk management and control. For the purpose of meeting this requirement, the Chief Internal Auditor provides one of two opinions:
- (a) That the organisation's framework of governance, risk management and control is **satisfactory** (i.e. that satisfactory assurance can be obtained from governance systems and procedures in place); or
 - (b) That the organisation's framework of governance, risk management and control is **not satisfactory** (i.e. that there is insufficient control in evidence within the organisation's governance systems to provide satisfactory assurance).
- 3.2 The opinion of the Chief Internal Auditor is that, at the time of preparing this report, the organisation's internal systems of governance, risk management and control were **satisfactory** overall during 2015/16. The Chief Internal Auditor has not needed to place reliance on the work of other bodies in forming her view, and there are no limitations in the scope of this opinion. There are no qualifications to this opinion.
- 3.3 This judgement is informed by the outcomes of Internal Audit work during 2015/16, which are reported to the Audit Committee in regular updates of key outcomes. These have demonstrated that the majority of audit opinions for work undertaken in this period have been 'moderate assurance' or higher, with a small number of 'limited assurance' and no 'no assurance' opinions. A full list of audits performed and opinions issued is included at **Annex A**.
- 3.4 As reported to the Audit Committee in the Key Outcomes reports, a number of areas of good practice were identified throughout Internal Audit's work during the year. In addition, evidence checking and follow up performed by Internal Audit has demonstrated effective management action in implementing Internal Audit's recommendations.
- 3.5 It is recommended that Internal Audit's satisfactory opinion on the framework of governance, risk management and control is considered as a source of assurance for the preparation of the Annual Governance Statement for 2015/16, and its subsequent approval by the Audit Committee.
- 3.6 This is a positive opinion, which means that the organisation has suitable internal control systems. This opinion is based solely on the areas reviewed, and the progress made by the organisation to action Internal Audit recommendations.

- 3.7 This opinion on the framework of governance, risk management and control has been prepared in accordance with the Public Sector Internal Audit Standards and the accompanying Local Government Application Note issued by the Chartered Institute of Public Finance and Accountancy as the 'relevant Internal Audit standard setter'.
- 3.8 Assurance can never be absolute, and neither can Internal Audit work be designed to identify all weaknesses that might exist. In accordance with its role, Internal Audit has agreed recommendations with management aimed at further strengthening the control environment in operation within the organisation.

4 Audit Work Performed During 2015/16

- 4.1 Internal Audit has provided an audit, advice, and financial consultancy / programme assurance service to the Authority in 2015/16.
- 4.2 The audit reports and briefing notes issued during 2015/16, and those related to this period which are currently being finalised with our audit clients, are set out at **Annex A**.
- 4.3 A framework of opinion classifications is used in Internal Audit reporting. The framework applies an overall assurance judgement to each system audited, as defined below.

Full Assurance	There is a sound system of control with key controls consistently applied.
Significant Assurance	There is a sound system of control, although there are some minor weaknesses in the system and/or occasional non-compliance with key controls.
Moderate Assurance	While there is a basically sound system of control, there are some weaknesses in the system and evidence of regular non-compliance with key controls.
Limited Assurance	The system of control is insufficient.
No Assurance	There is no system of control in place.

- 4.4 In addition to the overall opinion given on every internal audit, individual recommendations within each report are classified as critical, high, medium or low priority. This prioritisation is designed to assist management in assessing the importance of each recommendation. The definitions of these priority classifications are set out below:

Priority	Description
1* Critical / Catastrophic	Action considered imperative to ensure the organisation is not exposed to unacceptable risks.
1 High / Fundamental	Action that is considered urgent to ensure that the service area / establishment is not exposed to high risks.
2 Medium / Significant	Action that is considered necessary to avoid exposure to considerable risks.
3 Low / Less Significant	Action that is considered desirable or best practice and would result in enhanced control or better value for money.

- 4.5 The proportion of Internal Audit recommendations in the period April 2015 – March 2016 classified against each priority is as follows (data from the previous five years is also shown for comparison):

	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Critical Priority	Nil	Nil	Nil	Nil	Nil	Nil
High Priority	5 (%)	8 (1%)	17 (4%)	7 (3%)	7 (3%)	Nil
Medium Priority	185 (29%)	111 (20%)	108 (25%)	71 (27%)	101 (37%)	131 (41%)
Low Priority	458 (71%)	433 (78%)	311 (71%)	184 (70%)	163 (60%)	187 (59%)
TOTAL	648 (100%)	552 (100%)	436 (100%)	262 (100%)	271 (100%)	318 (100%)

Note: Percentages contain roundings

- 4.6 Prioritisation of Internal Audit recommendations is controlled through Internal Audit's quality control and file review processes. This is in accordance with the requirements of Public Sector Internal Audit Standards, which requires that a Quality Assurance and Improvement Programme is in place for Internal Audit's work.
- 4.7 In addition to performing internal audits of existing systems within the Authority and responding to queries on the operation of such systems, during 2015/16 Internal Audit has had a significant and increasing role in advising on new systems within the Authority. A full list of the programme assurance and project boards supported by Internal Audit is shown at Annex A. Whilst the time spent on such assurance work reduces the number of available audit days, it is considered an efficient use of Internal Audit's resource, in that assurance is obtained that effective controls are incorporated into new major systems from the outset. In turn, this minimises the risk of weaknesses in

systems and strengthens the control environment. This activity comprises 'consulting activity' under the Public Sector Internal Audit Standards, and is managed by the Chief Internal Auditor in the way prescribed by the Standards.

- 4.8 As in previous years, Internal Audit has undertaken the necessary assurance work and certified the Authority's compliance with the Public Services Network (PSN) Code of Connection requirements.

Audit Highlights 2015/16

- 4.9 This section of the report is designed to draw attention to significant audits and findings from Internal Audit in the 2015/16 year. It should be read in context of the overall positive 'satisfactory' audit opinion described above.
- 4.10 A number of audits attained a 'significant assurance' audit opinion. It is of comfort to the Authority that several of the organisation's fundamental financial systems, and high value / high volume transactional systems, were amongst those in this category. Council Tax, Debt and Non-Credit Income, Housing Benefit and Council Tax Support, National Non Domestic Rates, Rent Arrears and Former Tenants' Arrears all received a 'significant assurance' opinion. This provides assurance that these key systems bear appropriate levels of control.
- 4.11 In terms of those areas where 'limited assurance' opinions were determined, Internal Audit would draw attention to the audit of Information Governance. By way of context, in recent years there has been a national drive for large public bodies to better regulate this area. For all local authorities, it will be a challenge to manage the huge volumes of data which such bodies will understandably amass during the course of their operations. Although a 'limited assurance' audit opinion was issued with regard to the Authority's arrangements in this area, a raft of measures aimed at strengthening control around information governance are now in the process of being implemented. Internal Audit will continue to work with the relevant officers and afford this area a high priority in our planned audit coverage during 2016/17.
- 4.12 Internal Audit also examined a number of partnership arrangements, including the Authority's major strategic partnerships but also other partnerships during 2015/16. In respect of the Street Lighting Private Financing Initiative, Internal Audit's 'limited assurance' opinion confirmed management's assessment that arrangements should be put on a sounder footing. It will be important that performance data is appropriately challenged to ensure that North Tyneside's aspirations from this partnership are delivered. As partnership working is likely to continue to assume a greater role in local authority service delivery, it will be necessary to ensure that safeguards for North Tyneside's interests are built into regular monitoring and governance arrangements.

5 Schools' Financial Value Standard

- 5.1 Following the replacement of Financial Management Standard in Schools (FMSiS) by the Schools Financial Value Standard (SFVS) in 2013, time was included in the audit plan for 2015/16 to support and co-ordinate the work required by the Standard on behalf of the Authority.
- 5.2 The SFVS has been designed in conjunction with schools to assist them in managing their finances and to give assurance that they have secure financial management in place. Governing bodies have formal responsibility for the financial management of their schools, and so the standard is primarily aimed at governors; however the Authority's Chief Finance Officer is responsible for ensuring that submissions made by schools are in line with the judgements on these schools which have already been reached by Internal Audit.
- 5.3 On behalf of the Chief Finance Officer (Section 151 Officer), Internal Audit co-ordinated, received, reviewed and constructively challenged Schools' Financial Value Standard submissions, for all of the Authority's grant-maintained schools.

6 Special Investigations

- 6.1 In common with previous years, Internal Audit has performed a number of special investigations during 2015/16. These relate to issues which could not be foreseen in advance, and where (once investigated) irregularity may have been indicated. As such, it is important that the organisation can call upon Internal Audit resource to respond quickly to assess the extent of potential problems and to secure evidence if required. Internal Audit's work in this area has included responding to suspicions of theft of cash / cash discrepancies, potential inappropriate access / abuse of resources by employees, and requests for support from Northumbria Police which continued to require significant Internal Audit resource. Where irregularities were confirmed, swift action was taken by management (supported by Internal Audit) to cease the possibility of ongoing impropriety. Causes were then investigated and this, as is typically the case in this area of work, tended to highlight the need for enhanced directive control (see paragraph 2.3), in particular management and supervisory controls.

7 Counter Fraud and the National Fraud Initiative (NFI)

- 7.1 During 2015/16, two dedicated counter fraud posts, created on a self-funding basis, were appointed within the Internal Audit team. These counter fraud officers have undertaken a thorough review of the Authority's operations, from a counter fraud perspective, and developed a 'counter fraud blueprint' highlighting the areas of North Tyneside's operations where the risks of fraud are likely to be most prevalent. These risk areas were ranked, and work is now underway on reviewing Council Tax discount entitlement, which was identified as the first area for counter fraud review. This will help to ensure that discounts continue to be received by those entitled to them, whilst identifying and recovering discounts which have not been claimed appropriately.

- 7.2 North Tyneside Council is part of the Audit Commission's National Fraud Initiative and is thus legally obliged to provide relevant information under the requirements of the Audit Commission Act 1998. (NB. following the closure of the Audit Commission the powers to conduct the National Fraud Initiative passed to the Cabinet Office on 1 April 2015). Before this information can be provided, the Authority is required to ensure that appropriate steps have been taken to notify data subjects held in the organisation's relevant information systems that data may be used for the prevention and detection of fraud.
- 7.3 As in previous years, Internal Audit have acted as the lead within the Authority for the NFI. In addition to finalising work on the 2014/15 NFI exercise, which has taken significant time and resource, data from the Authority's systems was extracted and submitted to the Audit Commission in preparation for the 2015/16 exercise, focussing on data held in Council Tax and Electoral Registration systems. Details of data matches were received from the Audit Commission early in 2016 and work is underway on investigating potential matches.

8 Data Quality

- 8.1 During 2015/16, Internal Audit has performed an assessment of data quality issues as part of every audit undertaken. This has involved an assessment against the 6 characteristics / dimensions of data quality identified by the Audit Commission, which organisations can use to assess data quality and to manage its improvement. These are:
- (a) **Accuracy:** data should be accurate for its intended purpose and the need for accuracy balanced against the importance of the data attribute, in terms of its use and the cost or effort of collection.
 - (b) **Completeness:** data should be complete – should not contain invalid records or missing data.
 - (c) **Relevance:** data captured should be relevant to the purpose for which it is used.
 - (d) **Reliability:** data used should reflect stable and consistent data collection processes.
 - (e) **Timeliness:** data collection should be captured as quickly as possible after the event.
 - (f) **Validity:** data should be recorded in compliance with relevant rules and definitions.
- 8.2 The general trend from this work is that awareness of the importance of data quality is high within the organisation. The Authority recognises that there will be a need to continue this careful management moving forward. Where individual audits have identified scope for improvement in one of the characteristics shown, these have been highlighted to management as part of Internal Audit reporting.

9 Annual Governance Statement 2015/16

- 9.1 The Annual Report from the Chief Internal Auditor is one source of intelligence for the organisation when preparing the Annual Governance Statement (AGS). It is recommended that the Chief Internal Auditor's overall 'satisfactory' opinion on the organisation's framework of governance, risk management and control, is considered when preparing the Annual Governance Statement.

IA/AHM
May 2016

Annex A: Formal Audit Reports issued during 2015/16

<u>Audit:</u>	<u>Opinion:</u>
Business Continuity Planning	Moderate
Council Tax	Significant
Creditors & Procurement	Moderate
Debt & Non Credit Income	Significant
Environmental Controls & Disaster Recovery	Moderate
Housing Benefit & Council Tax Support	Significant
Information Governance	Limited
National Non Domestic Rates	Significant
Northgate Housing System Review	Moderate
Pre Employment Checks	Significant
Public Health Transition	Significant
Rent Arrears & Former Tenants' Arrears	Significant
Social Services Systems Review	Moderate
Streetlighting Private Financing Initiative (PFI)	Limited

Reports Pending from 2015/16 (draft report issued, awaiting issue as final report)

<u>Audit:</u>	<u>Indicative Opinion:</u>
Children's Safeguarding	Moderate
Corporate Health & Safety	Moderate
Creditors	Moderate
Payroll	Significant
Right to Buy	Significant
Schools Information Management System (SIMS)	Significant

Briefing Notes (Management Requests & Special Investigations)

Carbon Reduction Commitment Energy Efficiency Scheme
 DEFRA Flooding Grant Claim return
 European Court of Auditors' audit of ERDF Grant claim
 Local Transport Plan Capital Block Funding (Integrated Transport and Integrated Transport & Maintenance) Grant Claim returns
 Public Services Network Code of Connection compliance
 Tyne Port Health Authority Annual Return

Project Boards / Working Groups

Internal Audit has also supported the following Project Boards / Working Groups during 2015/16 in a programme assurance role:

Banking Services / Direct Banking
Cashless Projects
Customer Journey & Digital Strategy Delivery Board
Debtors System replacement
External Print Retender
ICT Performance & Prioritisation Board
Information Security Group
Petty Cash Process Review
Robotic Process Automation
Social Care Case Management System Replacement
Strategic Partnership Business and Technical
Troubled Families Stakeholder Group

Ad-hoc Queries / Requests for Advice

Internal Audit receives requests for ad-hoc advice and support throughout the year, in respect of which we may be required to extract prime data or produce analysis but where it is not always appropriate to issue a formal report. In 2015/16, **66** such requests requiring the application of Internal Audit resource were received and responded to.