



AUDIT COMMITTEE – 23RD APRIL 2019

SUBJECT: ANNUAL INTERNAL AUDIT REPORT 2018/19

REPORT BY: INTERNAL AUDIT SERVICES MANAGER

1. PURPOSE OF REPORT

The purpose of this report is to inform the Audit Committee of the Internal Audit Manager's overall opinion on the Authority's Internal Control Systems derived from the work undertaken by Internal Audit Services during the 2018/19 financial year.

2. SUMMARY

2.1 It is a requirement the Council's Financial Regulations, the Internal Audit Charter and the Public Sector Internal Audit Standards (PSIAS) that the Head of Internal Audit provides an annual report to support the Annual Governance Statement. The report should: -

- Include an opinion on the overall systems of internal controls.
- Present a summary of the audit work that has been undertaken on which this opinion is based.
- Draw attention to any issues which may impact on the level of assurance provided.

2.2 This audit opinion will inform the annual governance review process and be incorporated into the Annual Governance Statement which will be reviewed by the Audit Committee at its meeting in June 2019.

3 LINKS TO STRATEGY

3.1 Strong corporate governance arrangements are an essential element of ensuring that the Council's key priorities are effectively delivered and this in turn contributes to the following Well-being Goals within the Well-being of Future Generations Act (Wales) 2015: -

- A prosperous Wales.
- A resilient Wales.
- A healthier Wales.
- A more equal Wales.
- A Wales of cohesive communities.
- A Wales of vibrant culture and thriving Welsh Language.
- A globally responsible Wales.

4. THE REPORT

4.1 Both the Council's Financial Regulations and the Internal Audit Charter set out the reporting requirements for Internal Audit Services and the Public Sector Internal Audit Standards (PSIAS) introduced in 2013 have also reinforced the links with corporate governance and the assurance framework.

- 4.2 The purpose of this report is to provide Members of the Audit Committee with an opinion or view of the robustness and effectiveness of the internal control systems and procedures in place within the organisation during the 2018/19 financial year.
- 4.3 The opinion is a key element of the annual governance review process and forms part of the published Annual Governance Statement.
- 4.4 The approach adopted for reviewing and evaluating the internal controls and processes revolves around a flexible well constructed plan that considers several factors such as risk, impact, nature and history etc. Audits undertaken are evaluated against pre-set criteria to provide a ranking which is used to feed into the overall assessment.
- 4.5 Information used within the assessment process can also be obtained from other work undertaken such as grant certification work, system advice, participation on working groups and special investigations etc. all of which provide audit staff with intelligence which can both inform the audit planning function and inform the overall assurance provided by the audit opinion.
- 4.6 The prolonged sickness absence of the Internal Audit Manager during the year has impacted on both the day-to-day running of the Internal Audit Team as well as the completion of the improvement initiatives. Additionally, a number of large or complex pieces of work have taken resource away from previously planned areas; however, as previously discussed with the Audit Committee through having the ability to prioritise and reschedule the Team is able to respond to emerging or new risks.
- 4.7 The audits completed and used to generate the overall opinion are shown at Appendix 1 and Appendix 2 which also highlight the extent of the work completed and its diversity. Throughout the year some amendments to terminology and categorisations have been made but for clarity summaries of both appendices are included below.
- 4.8 During 2018/19 two investigations have been undertaken, one within a school and the other relating to operational activities within a service area. The school issue is an isolated incident relating to one member of staff and is not something that is common across our school estate. The service area investigation is ongoing and relates to contract administration/management and once the investigation is concluded any changes or system improvements identified will be reported on and an appropriate action plan agreed and implemented.
- 4.9 Systems audits have been carried out over a wide range of areas in order to gain an overall opinion of the effectiveness of the internal control system operating within the Council. These audits cover the key financial systems but may also address non-financial systems which are considered to be high risk or high impact. In the main systems or processes related to cash, income, payments or where high transaction volumes exist are covered in this way.
- 4.10 Some high risk areas traditionally covered by systems work received audit coverage via the evaluation and investigation of data matches identified from the National Fraud Initiative (NFI) exercise and this work was rolled over from the previous year.
- 4.11 System audits risk rate each individual finding which then informs an overall opinion on the adequacy of the system of controls and the compliance with the system in place (if transactional tests were performed).
- 4.12 Where findings are reported, recommendations are made to management, who are required to indicate the actions they are planning to take to address the findings noted. These form part of an action plan which are either followed up as a separate process or built into the planning of the next audit of that particular system.
- 4.13 In the main auditees and management accept recommendations made and an overall opinion is reported. Furthermore, in line with PSIAS, systems reports now also contain a "direction of travel" indicator to show whether there has been an improvement/ reduction in the nature or type of risks reported.

- 4.14 The following table summarises the opinions reported in respect of finalised audit assignments. Not all audits generate an opinion for example grants certification, and where no compliance testing is performed there is no opinion generated on this aspect.

Opinion	System (Nos)	Compliance (Nos)
Good/Effective	9	2
Satisfactory/Effective with room for improvement	11	4
In need of Improvement	3	4
Inadequate/unsatisfactory	1	
Total	24	10

- 4.15 Audit reports with at least one “in need of improvement” opinion noted above are as follows: -

NFI payroll.
 PCI compliance.
 WHQS data validation.
 Treasury Management.
 School transport – Taxis.
 Section 17 payments.

- 4.16 Those reports issued before October’s Audit Committee meeting would not have been reported due to the introduction of the 4 tier opinions from that point. Due to the timings of the reports, the Audit Committee cycle and other factors there may be a delay between the issue of the report and the reporting to the next Audit Committee.
- 4.17 Council operational establishments i.e. Schools etc. are audited on a rotational basis. The control systems and processes in establishments cover most of the administrative/financial operations carried out at the establishment, some of which feed into corporately managed systems which are audited centrally. In respect of establishment audits one overall opinion is given and as part of the audit process school governors are tasked with ensuring improvement takes place as agreed by the Head teacher and this is also followed up by audit staff.
- 4.18 While a formal action plan review process is not in place those establishments identified as being in need of improvement are required to complete an action plan and are subject to a follow up review to monitor progress of the implementation of the recommendations and an enhancement of the control processes in place.
- 4.19 Periodic visits to these sites may not only detect and correct poor practices, it may also give an opportunity to issue advice and guidance, correct poor or bad practice and enhance or set up a better control environment in situ. Regular visits may also act as a deterrent to any mal-practice.
- 4.20 Establishments visited included primary and secondary schools, a selection of libraries, social services establishments, a leisure facility and Blackwood Miners Institute.
- 4.21 When an irregularity is identified at an establishment it is normally contained within the individual establishment as a stand alone event which has no effect on the other establishments.

Opinion	Numbers
Good/effective	5
Satisfactory/effective with room for improvement	23

In need of Improvement	6
Unsatisfactory/inadequate	1
Total	35

- 4.22 Audit reports with an “in need of improvement” opinion noted above are as follows:- Llanfabon Infants, Park Primary, Risca Primary, White Rose Primary, YG Bro Allta, Gilfach Fargoed Primary and Islwyn High School. Those reports issued before October’s Audit Committee meeting would not have been reported due to the introduction of the 4 tier opinions. Due to the timings of the reports, the Audit Committee cycle and other factors such as school holidays there may be a delay between the issue of the report and the reporting to the next Audit Committee.
- 4.23 Other audit work undertaken during the period under review included regularity work, advisory work, supporting working parties and advising on best practise in relation to new systems and processes.
- 4.24 Grant certification - A number of Welsh Government grants are received by the Authority that are subjected to a review of accuracy and compliance with terms and conditions requiring a year-end certification. Significant revenue streams arise from these grants. 7 grant audits with a value of over £12 million were audited in 2018/19.
- 4.25 Audit staff supported the IT section in retaining the authority’s PCI (Payment Card Industry) accreditation. This required certain systems and processes to be in place and for these to be reviewed and checked at least annually. Failure to adhere to these Standards could result in the withdrawal of the facility to accept card income and the imposition of fines and penalties. In 2018/19 all locations that accept debit and credit card income were visited and reminders of best practice and any breaches noted were reported to site managers and a full report was issued to the PCI forum and IT security Officer. Recommended improvements were put in place and the Authority remains fully compliant with the Standard.
- 4.26 Audit staff had continued to provide advice and guidance to the Purchase Ledger Section in respect of best practices in administering and complying with the requirements of HMRC in paying contractors and limited companies and identifying instances of “deemed employment”. This is considered to be a high risk area as the regulations issued are recent and case law and practice is emerging in this area whilst fines and penalties imposed by HMRC for non-compliance have the potential to be major.
- 4.27 Primary school meal income amounts to over £1million per annum and issues relating to the administration and collection are a recurring theme in schools, and an audit review in 2017/18 had indicated this area was in need of improvement. Further ongoing advice and support has been provided to Catering Services and individual schools as the cashless primary school meals system was rolled out to a pilot of 5 schools and initial results are showing a reduction in cash handled in the pilot schools, with an associated reduction in risk of cash losses and arrears.
- 4.28 The Group Auditor was assigned as the Corporate Finance Information Governance Steward during 2017/18, a role that has continued into 2018/19. As Members are aware the General Data Protection Regulations (GDPR) came into force in May 2018 and this gives the Information Commissioner much greater powers in cases of breach and the value of fines has also increased. Recognising this as a risk a great deal of time was allocated to this role which included supporting the various sections within Corporate Finance in drafting Privacy Notices. This work has carried on into the current year. In addition, as part of this a significant one-off exercise was undertaken which involved reviewing all audit files and editing, archiving or destroying them to support the Section’s compliance with the Regulations.
- 4.29 The Internal Audit Manager is a member of the Corporate Governance Panel which met during the year. Corporate Governance Panel minutes were reported to the Audit Committee and the Panel informed the Annual Governance Statement process.

- 4.30 Internal Audit Services has continued to undertake final account reviews and other contract audit work with 63 contractors' final accounts being reviewed during the year (70 in 2017/18). These had a value of £23.5m (£9.5m 2017/18).
- 4.31 The Group Auditor is the primary contact for the NFI and uploads for the 2018/19 exercise were performed and coordinated by the Group Auditor in October 2018. Matches were released in January 2019 and work will be undertaken during 2019/20 to investigate these.
- 4.32 Anonymous letters, reports and complaints are received and assessed within Internal Audit to ensure that they are properly considered and if necessary they are then passed to appropriate Departments for further investigation or review. Resource demand for this process is difficult to forecast. During the year there were 59 letters logged (66 in 2017/18). These communications cover a range of possible issues and include highways, planning, anti-social behaviour, tipping, animal control, neighbour issues, child protection and safeguarding and possible other illegal activities. Each report is assessed individually and referred appropriately. Where allegations relate to criminal activities, benefit fraud, staff irregularities or safeguarding immediate referrals are made to relevant parties.
- 4.33 Internal Audit also log and record cheques returned to the Authority. These are scrutinised to ensure they do not relate to breakdowns in control processes. 61 were logged in 2018/19 (84 in 2017/18).
- 4.34 Compliance work was undertaken to assist with the IT security accreditation and 5 areas received coverage in 2018/19.
- 4.35 A member of the Internal Audit Team assisted the Corporate Accountancy Team following year-end 2017/18 in relation to closing down a number of grant claims. Another member of the Team has also been seconded to Caerphilly Homes since January 2019 to assist with addressing some of the recommendations contained in an audit report including data validation procedures following an audit of this area. This member of staff will continue with the project into the new financial year.
- 4.36 The Public Sector Internal Audit Standards (PSIAS) came into force on the 1st April 2013 and consist of the following: -
- Definition of internal audit.
 - Code of Ethics.
 - Standards for the Professional Practice of Internal Auditing.
- 4.37 The Standards aim to promote further improvement in the professionalism, quality and effectiveness of Internal Audit across the public sector. The Standards require that each public sector Internal Audit Service has in place robust arrangements for quality assurance and requires that Internal Audit is subject to an external assessment at least once every 5 years.
- 4.38 The results of an external assessment in 2017/18 were reported to the Audit Committee in January 2018. The assessment noted that there were no significant deviations from the Standards but a small number of recommendations to improve conformance were made and these are being progressed. The Internal Audit Service continued to conform to the Standards during 2018/19 and no significant deviations have been noted.

INTERNAL AUDIT MANAGERS OPINION

- 4.39 The Internal Audit Manager's opinion is that overall the Council's systems and control procedures are effective but there is need for improvement in some specific areas.
- 4.40 The investigation undertaken in respect of an education establishment is an isolated incident and does not reflect the position across all of the Council's establishments. Indications from

the ongoing departmental investigation are that there may be specific issues requiring attention that will need to be addressed moving forward.

5. WELL-BEING OF FUTURE GENERATIONS

5.1 Strong corporate governance arrangements are a key element in ensuring that the Well-being Goals within the Well-being of Future Generations Act (Wales) 2015 are met.

6. EQUALITIES IMPLICATIONS

6.1 There are no equalities implications.

7. FINANCIAL IMPLICATIONS

7.1 There are no financial implications.

8. PERSONNEL IMPLICATIONS

8.1 There are no personnel implications.

9. CONSULTATIONS

9.1 Any comments received have been reflected in the report.

10. RECOMMENDATIONS

10.1 To note the opinion expressed by the Internal Audit manager.

11. REASONS FOR THE RECOMMENDATIONS

11.1 To ensure that: -

- The Audit Committee is aware of the level of Internal Audit coverage and the overall opinion derived from undertaking this work.
- Adequate supporting information and evidence has been supplied to the Audit Committee to enable the Committee to meet its requirements under the Committee's terms of reference.
- Adequate assurance is provided to support the Annual Governance Statement process.

12. STATUTORY POWER

12.1 Local Government Act 2000

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