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## **INTERNAL AUDIT ANNUAL REPORT 2016/17**

**Report by Chief Officer Audit and Risk**

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### **AUDIT AND RISK COMMITTEE**

**28 March 2017**

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#### **1 PURPOSE AND SUMMARY**

- 1.1 The purpose of this report is to present to the Audit and Risk Committee the Internal Audit Annual Report for the year to 31 March 2017 which includes the Chief Officer Audit & Risk's independent assurance opinion on the adequacy of the Council's overall control environment.**
- 1.2 In support of the overall governance arrangements of the Council, as set out in the Local Code of Corporate Governance, and the Public Sector Internal Audit Standards (PSIAS) which require that the Chief Officer Audit & Risk provides an annual internal audit opinion and report to the Chief Executive on the adequacy and effectiveness of the Council's internal control and governance arrangements to support the preparation of the Annual Governance Statement.
- 1.3 The Remit of the Audit and Risk Committee indicates that it should ensure an adequate framework of internal control, risk management and governance throughout the Council.
- 1.4 The Internal Audit Annual Report 2016/17, at Appendix 1, includes the annual internal audit opinion regarding the adequacy and effectiveness of internal control within the Council, provides details of the Internal Audit activity and performance during the year to fulfil its role, and summarises the outcomes of assessments of the Internal Audit service against the Public Sector Internal Audit Standards (PSIAS).
- 1.5 The Chief Officer Audit & Risk's opinion is that, based on internal audit reviews, risk assessments and knowledge, the systems of internal control and governance arrangements within the Council are operating satisfactorily. Some improvements are required.
- 1.6 The Internal Audit Annual Report 2016/17 has been used to inform the Chief Executive's Annual Governance Statement 2016/17.

#### **2 RECOMMENDATIONS**

- 2.1 I recommend that the Audit and Risk Committee:**
- a) Considers the Internal Audit Annual Report 2016/17 and provides any commentary thereon.**
  - b) Agrees that the Internal Audit Annual Report 2016/17 be published on the Council's website.**

### **3 BACKGROUND**

3.1 The Public Sector Internal Audit Standards (PSIAS) that became effective for local authorities on 1 April 2013 requires that:

“The chief audit executive [SBC’s Chief Officer Audit & Risk] must deliver 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 incorporate:

- the opinion;
- a summary of the work that supports the opinion; and
- a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.”

3.2 The Remit and Terms of Reference of the Audit and Risk Committee indicate that it should:

- Ensure adequate framework of internal control, risk management and governance throughout the Council
- Encourage propriety and probity throughout the Council
- Assist in accountability to stakeholders

### **4 INTERNAL AUDIT ANNUAL REPORT 2016/17**

4.1 The Internal Audit Annual Report 2016/17, at Appendix 1, includes the Chief Officer Audit & Risk’s independent and objective opinion regarding the adequacy and effectiveness of internal control within the Council, provides details of the Internal Audit activity that supports the opinion and of the performance during the year to fulfil its role, and summarises the outcomes of assessments of the Internal Audit service against the Public Sector Internal Audit Standards (PSIAS).

4.2 The Chief Officer Audit & Risk’s opinion is that, based on Internal Audit reviews, risk assessments and knowledge, the systems of internal control and governance arrangements within the Council are operating satisfactorily.

4.3 Continuous improvements in internal controls and governance arrangements can be demonstrated through Management-initiated improvements complemented by the implementation of audit recommendations. Further improvements in internal control and governance have been agreed by Management as highlighted in Internal Audit reports and recommendations made during the year or outstanding from previous years.

4.4 The Internal Audit Annual Report 2016/17 provides assurances in relation to the Council’s corporate governance framework that is a key component in underpinning delivery of the corporate priorities within the Council’s Corporate Plan and has been used to inform the Chief Executive’s Annual Governance Statement 2016/17.

4.5 The annual internal self-assessment demonstrates sufficient evidence that the Council’s Internal Audit section complies with the Public Sector Internal Audit Standards (PSIAS) in all significant respects. An area of further improvement is shown in the Quality Assurance and Improvement Plan (QAIP) that is also included in the Internal Audit Annual Report 2016/17.

## **5 IMPLICATIONS**

### **5.1 Financial**

- (a) It is anticipated that efficiencies will arise either as a direct or indirect result of Management implementing the recommendations made by Internal Audit during 2016/17 through improved internal controls and governance arrangements.
- (b) The net cost (projected outturn at February 2016) of the Internal Audit service was £246k (2015/16 £250k). The majority of service expenditure relate to staff costs (99%) for resources comprising Chief Officer Audit & Risk (50% allocation), Internal Audit Manager (part year), three Senior Internal Auditors, and one Internal Auditor.

### **5.2 Risk and Mitigations**

- (a) Internal Audit provides assurance to Management and the Audit and Risk Committee on the adequacy and effectiveness of internal controls and governance within the Council, including risk management, and to highlight good practice and recommend improvements. Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and potential range and breadth of audit areas for inclusion within the plan.
- (b) Continuous improvements in internal controls and governance arrangements can be demonstrated through Management-initiated improvements complemented by the implementation of Audit recommendations.
- (c) It is anticipated that improvements in the management and mitigation of risks will arise as a direct result of Management implementing the Internal Audit recommendations made during the year or outstanding from previous years which will enable Management to demonstrate further improvement in internal controls and governance arrangements.
- (d) Delivery of the Internal Audit services in conformance with the PSIAS will enable the Council to meet the requirements of the Local Authority Accounts (Scotland) Regulations 2014 to consider the findings of assessments as part of the consideration of the system of internal control required by regulation 5.

### **5.3 Equalities**

It is anticipated there will be no adverse impact due to race, disability, gender, age, sexual orientation or religious/belief arising from the work contained in this report.

### **5.4 Acting Sustainably**

There are no direct economic, social or environmental issues with this report.

### **5.5 Carbon Management**

There are no direct carbon emissions impacts as a result of this report.

### **5.6 Rural Proofing**

This report does not relate to new or amended policy or strategy and as a result rural proofing is not an applicable consideration.

### **5.7 Changes to Scheme of Administration or Scheme of Delegation**

No changes to the Scheme of Administration or Scheme of Delegation are required as a result of this report.

## 6 CONSULTATION

- 6.1 As the Chief Officer Audit & Risk is required to give an independent opinion on the internal control and governance arrangements of the Council, consultation on Appendix 1 is not appropriate.
- 6.2 The Corporate Management Team has been advised to take into account the work of Internal Audit and independent opinion on the adequacy and effectiveness of the systems of internal control and governance when completing the annual self-evaluation and assurance process for the Council's Annual Governance Statement 2016/17.
- 6.3 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Chief Officer HR, and the Clerk to the Council have been consulted on the covering report and any comments received have been incorporated into the report.

### Approved by

**Jill Stacey, Chief Officer Audit and Risk Signature .....**

### Author(s)

Name	Designation and Contact Number
Jill Stacey	Chief Officer Audit and Risk Tel 01835 825036

**Background Papers:** Appropriate Internal Audit files

**Previous Minute Reference:** Audit and Risk Committee 29 March 2016

**Note** – You can get this document on tape, in Braille, large print and various computer formats by using the contact details below. Information on other language translations can also be given as well as provision of additional copies.

Contact us at Internal Audit [intaudit@scotborders.gov.uk](mailto:intaudit@scotborders.gov.uk)

**Chief Officer Audit & Risk's Annual Report and Opinion 2016/17****1 Introduction**

- 1.1 It is Management's responsibility to design and maintain proper risk management, governance and internal control processes and systems to ensure probity in systems and operations, including the prevention, detection and resolution of fraud and irregularities. Management is also responsible for checking that the arrangements and controls are operating effectively. These are known as the first and second lines of defence which are not fixed but evolve as the Council changes.
- 1.2 Internal Audit, as the third line of defence, is an independent appraisal function established for the review of the internal control system as a service to Scottish Borders Council. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources and the management of risk.
- 1.3 The Internal Audit activity adds value to the organisation (and its stakeholders) when it considers strategies, objectives, and risks; strives to offer ways to enhance governance, risk management and control processes; and objectively provides relevant assurance.
- 1.4 The Objectives of Internal Audit are set out in its Charter: "As part of Scottish Borders Council's system of corporate governance, Internal Audit's purpose is to support the Council in its activities designed to achieve its declared objectives and to do so:
- As a contribution to the Council's corporate management of risk.
  - As an aid to ensuring that the Council and its Members, managers and officers are operating within the law and relevant regulations.
  - In support of the Council's vision, values and priorities.
  - As a contribution towards establishing and maintaining a culture of honesty, integrity, openness, accountability and transparency throughout the Council in all its activities and transactions.
  - As a contribution towards ensuring that financial statements and other published information are accurate and reliable."
- 1.5 The Public Sector Internal Audit Standards (PSIAS) that became effective for local authorities on 1 April 2013 requires that:
- "The chief audit executive [SBC's Chief Officer Audit & Risk] must deliver 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 incorporate:
- the opinion;
  - a summary of the work that supports the opinion; and
  - a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme."
- 1.6 This Annual Report provides the annual internal audit opinion and summarises the work carried out by Internal Audit during the year to 31 March 2017 that underpins the opinion in accordance with the Internal Audit Charter, strategy and annual plan. The report also summarises the outcomes of assessments of the Internal Audit service against the Public Sector Internal Audit Standards (PSIAS).

## **2 Opinion on the systems of Internal Control and Governance**

- 2.1 My opinion is that, based on our reviews, risk assessments and knowledge, the systems of internal control and governance are operating satisfactorily.
- 2.2 Continuous improvements in internal controls and governance arrangements can be demonstrated through Management-initiated improvements complemented by the implementation of audit recommendations. Internal Audit reports during the year confirm improvements in internal controls and governance, internal financial control and risk management.
- 2.3 Reasonable assurance can be provided on the adequacy of the internal controls and governance arrangements in place. There is adequate awareness and observation of the Council's Local Code of Corporate Governance (approved May 2016; revised and awaiting approval) and key governance documents including Scheme of Administration (approved January 2015; amended January 2017), Procedural Standing Orders (approved March 2016), Scheme of Delegation (approved June 2014; amended March 2016), Financial Regulations (approved June 2016), and Codes of Conduct for Councillors and for Employees which can be demonstrated by way of the findings of Internal Audit reviews during 2016/17.
- 2.4 The Chief Officer Audit & Risk facilitates the annual review of the Council's governance arrangements against its Local Code of Corporate Governance (Local Code) carried out by a self-evaluation working group of officers from across the Council's services. This is part of the process to produce the Annual Governance Statement. The Local Code has been updated as part of the annual review process and it is anticipated to be presented to full Council for approval post May 2017. This is to ensure this key document continues to be relevant and complete to reflect the appropriate framework for effective governance of the Council's affairs and facilitate the exercise of its functions to deliver best value.
- 2.5 Further improvements in internal control and governance have been agreed by Management as highlighted in Internal Audit reports and recommendations made during the year or outstanding from previous years.

## **3 Internal Audit Annual Plan 2016/17 Delivery**

- 3.1 The following table shows the analysis of audit days and numbers by audit theme:

	<b>Plan days 2016/17</b>	<b>Actual days 2016/17</b>	<b>Plan Nos. 2016/17</b>	<b>Actual Nos. 2016/17</b>
<b>Corporate Governance</b>	<b>190</b>	<b>221</b>	<b>7</b>	<b>7</b>
<b>Financial Governance</b>	<b>180</b>	<b>166</b>	<b>7</b>	<b>7</b>
<b>IT Governance</b>	<b>60</b>	<b>34</b>	<b>4</b>	<b>4</b>
<b>Internal Controls</b>	<b>45</b>	<b>36</b>	<b>2</b>	<b>1</b>
<b>Asset Management</b>	<b>55</b>	<b>47</b>	<b>2</b>	<b>2</b>
<b>Legislative and other Compliance</b>	<b>50</b>	<b>50</b>	<b>4</b>	<b>4</b>
<b>Consultancy and Advice</b>	<b>90</b>	<b>93</b>		
<b>Other</b>	<b>69</b>	<b>42</b>		
<b>Non-SBC</b>	<b>70</b>	<b>96</b>		
<b>Total</b>	<b>809</b>	<b>785</b>	<b>26</b>	<b>25</b>

3.2 The level of Actual Audit days was broadly on plan (97%) despite the reduction of Internal Audit staff resources during the year, and all planned assurance Audits bar one were completed. The planned audit on Community Safety has been rescheduled to 2017/18 on request by the relevant Senior Management. This has not affected the assurance that Internal Audit is able to give.

3.3 The wide range of Internal Audit work performed during the year is listed below:

#### **Corporate Governance Audits**

3.4 To provide assurances in relation to the Council's corporate governance framework that is a key component in underpinning delivery of the corporate priorities within the Council's Corporate Plan, reviews included:

- Corporate Governance (Assessment of progress on implementation of Improvement action plans and Annual Evaluation against Local Code of Corporate Governance to ensure it complies with the CIPFA / SOLACE Revised Code 2016).
- Information Governance (Review of the framework including roles and responsibilities, policy development and implementation, and assess progress with implementation of improvement actions).
- Performance Management (Validation of performance indicators and benchmarking information that feeds the Performance Management reporting on the 8 Council Priorities and the submission for Local Government Benchmarking Framework to support self-assessment and continuous improvement).
- Workforce Planning (Review of approach to workforce development in alignment with business and financial planning processes to provide skills, knowledge and competency requirements for service delivery to meet objectives).
- Corporate Transformation (Review of governance and accountability arrangements including programme and project management, and of processes for benefit (financial and other) identification, tracking and realisation, to demonstrate value for money).
- Adult Social Care Services (Review governance and service arrangements being developed to effectively deliver integrated services commissioned by the Scottish Borders Health and Social Care Integration Joint Board (IJB)).
- Roads Services (Review governance arrangements being developed as part of proposals for alternative service delivery models for Roads services, and utilisation of best practice guidance and lessons learned).

#### **Financial Governance Audits**

3.5 To provide assurance on the internal financial controls in place and substantive testing of transactions to ensure completeness and accuracy of data in core financial systems, reviews included:

- Financial Policies and Procedures (Assess design of key processes and controls by Management and progress with review and update of Financial Regulations and associated procedures and guidelines as part of the Business World system project).
- Counter Fraud, Theft, Corruption & Crime (Review of fraud prevention controls and detection processes put in place by Management, assess progress with Improvement Plan actions, and provide intelligence via data sharing requests from Police Scotland).
- Income Charging, Billing & Collection (Follow-up the implementation of areas of improvements and assess key controls in Business World Sales to Cash workstream).
- VAT (Review of treatment of supplies and services made by the Council to customers).
- Procure to Pay Service (Review of payments processes at Service level including authorisation and assess key controls in Business World P2P workstream).

- Salaries (Review of controls at Service level including authorisation and assess key controls in Business World Payroll workstream).
- Revenues – Council Tax (Assess completeness and accuracy of Council Tax income associated with the new 2016/17 approved policy, and key controls introduced including application of discretionary exemptions).

#### **ICT Governance Audits**

3.6 To provide assurances that computer systems are secure, reliable and conform to nationally agreed standards, reviews included:

- ICT Change Programme including Security Controls and Operational Processes (Evaluate the ICT governance arrangements prior to transition to next phase of ICT Contract provision by CGI; assess the adequacy of proposed arrangements to manage the security of the Council's equipment, software and data; and review proposed change management and incident management controls).
- Public Sector Network (PSN) Compliance (Examine the Council's compliance with PSN requirements and progress with implementation of actions to achieve full compliance).

#### **Internal Controls Audits**

3.7 To provide assurances in relation to a range of the Council's internal controls in areas identified by Management, reviews included:

- Schools – Hawick High School, Galashiels Academy, Jedburgh Grammar, Kingsland PS, Reston PS and Parkside PS (Review of internal financial controls and business administrative procedures in place to ensure the efficient and effective use of resources in the school establishments, to complement the assurance received from Education Scotland arising from their inspection programme of schools).

#### **Asset Management Audits**

3.8 To provide assurances that Council assets are safeguarded and properly accounted for, and used economically, efficiently and effectively, reviews included:

- Asset Registers (Review of Property, Fleet, and IT asset registers and the reconciliations between the source computer-based systems and FIS, and assess key controls in Business World Record to Report workstream).
- Capital Investment (Review of Capital Planning basis against the priorities set by the Council; review of management systems in place to ensure that capital projects are being managed efficiently and effectively from inception to completion including post project evaluation; and assess progress with implementation of identified improvement actions to ensure compliance with established good practice).

#### **Legislative and Other Compliance Audits**

3.9 To test compliance with the terms of the funders' service level agreements or legislative requirements as part of the wider assurance framework, reviews included:

- Selkirk Conservation Area Regeneration Scheme (CARS) (Review as part of programme compliance and evaluation requirements of the external funders).
- EU LEADER Grants (Annual review of LEADER programme required by the Service Level Agreement (SLA) between Scottish Ministers (Managing Authority and the Paying Agency (RPID)) and Scottish Borders Council (Lead Partner for Scottish Borders Local Action Group (LAG)) to assess compliance by SBC with the terms of the SLA).
- European Maritime and Fisheries Fund (Annual audit under the terms of the SLA and legislative compliance including an assessment of compliance with the requirements of the SLA and the relevant EC Regulations).



- Carbon Reduction (Annual audit as part of the requirement under the Carbon Reduction Commitment Energy Efficiency Scheme prior to the Council's annual submission to Department of Energy and Climate Change).

### Other Work

- 3.10 Internal Audit responded to specific control issues highlighted by Managers during the year by incorporating those aspects within specific audit scopes or performing Contingency Audits approved by the Chief Officer Audit & Risk.
- 3.11 Resources were deployed in the delivery of the Follow-up work to check that recommendations have been implemented and to ensure that the new controls had the desired effect on improving internal control and governance. The following table highlights the current position (Source: Covalent as at 17 March 2017) with regards to Internal Audit recommendations arising from current and previous years:

Year identified	Total	Implemented	Not Yet Due	Overdue
2016/17	10	2	8	0
2015/16	21	19	1	1
2014/15	34	27	7	0

### Consultancy Work

- 3.12 The most significant piece of consultancy work related to full involvement in the design and implementation phases of the new Business World ERP system which will be used by the Council from April 2017 for HR, Payroll, Procurement and Finance management and administrative processes. The Chief Officer Audit & Risk is a member of the Business World ERP Project Board providing project assurance. Internal Audit has carried out testing to ensure that appropriate internal controls are in place and has performed the independent reconciliation and validation of extracted data from existing systems and of uploaded data into Business World system. Management expect improved internal financial controls via the Business World ERP System, it being a more modern system.
- 3.13 Internal Audit performed 'critical friend' role by undertaking in confidence an assessment of both current practice within the Council and the proposals under development against the key recommendations of the Accounts Commission Reports "Major capital investment in councils" and 'Good Practice Guide' (March 2013) and "Follow-Up" (January 2016). This adds value to the Council by influencing and offering ways to enhance the governance and internal control environment in alignment to the Council's strategic priorities.
- 3.14 Senior Internal Auditors continued to provide project assurance relating to the Welfare Reform Programme and Information Management Project, and the Chief Officer Audit & Risk is a member of the Information Governance Group providing support and advice.
- 3.15 Some independent challenge on governance arrangements and risk management has been provided through Internal Audit engagement in various forums as the Council continues to transform its services. For example, Alternative Service Delivery Models Board, Digital Customer Access Project, and Business Intelligence workshops.
- 3.16 Internal Audit contributed to the Council's Procurement PCIP assessment (specifically Internal Controls, Risk Management, and Fraud Prevention) whereby positive outcomes were noted with a final score of 71.9% into the highest possible scoring band of F1.
- 3.17 Opportunities were highlighted in connection with the Schools Internal Audit work to improve the effectiveness, efficiency and sustainability of the Primary Schools business support arrangements.
- 3.18 Internal Auditors responded to a number of requests for ad hoc advice and assistance on internal controls, risk management and governance.

#### **4 Public Sector Internal Audit Standards and Quality Assurance & Improvement Plan**

- 4.1 The professional standards as set out in Public Sector Internal Audit Standards (PSIAS) effective 1 April 2013 include:
- Definition of Internal Auditing;
  - Code of Ethics;
  - Attribute Standards (Purpose, Authority and Responsibility; Independence and Objectivity; Proficiency and Due Professional Care; Quality Assurance and Improvement Programme);
  - Performance Standards (Managing the Internal Audit Activity; Nature of Work; Engagement Planning; Performing the Engagement; Communicating Results; Monitoring Progress).
- 4.2 The Quality Assurance and Improvement Plan (QAIP) is designed to enable evaluation of Internal Audit's conformance with the Definition of Internal Auditing and the Standards, along with an evaluation of whether Internal Auditors apply the Code of Ethics, and an action plan to implement identified improvements.
- 4.3 The PSIAS includes the requirement to report the results of the QAIP to senior management and elected members. The following table provides Corporate Management Team and the Audit and Risk Committee with a summary overview and current status of not yet completed improvement actions arising from the External Quality Assessment (EQA) Peer Review by Renfrewshire Council carried out in October 2015 and the internal self-assessment 2015/16 against the PSIAS:

<b>Standard</b>	<b>Improvement Action</b>	<b>Target Date</b>	<b>Action Owner</b>
2000.6 Risk management	Continued improvement in identification and management of risk within the Council	March 2018	Chief Officer Audit & Risk

- 4.4 An internal self-assessment of Internal Audit practices against the Standards was carried out in 2016/17, as required by the PSIAS, taking into account the improvement actions implemented since the previous year's self-assessment. The 2016/17 self-assessment has indicated an improved level of conformance with both the Attribute Standards and Performance Standards and improved evidence of applying the Code of Ethics. The Summary of Conformance with the PSIAS indicates either 'Fully Conforms' or Generally Conforms' against the 13 Assessment Areas.

**Jill Stacey BA(Hons) ACMA CGMA**  
**Chief Officer Audit & Risk**  
**17 March 2017**