
INTERNAL AUDIT ANNUAL ASSURANCE REPORT 2017/18

Report by Chief Officer Audit & Risk

AUDIT AND SCRUTINY COMMITTEE

14 May 2018

1 PURPOSE AND SUMMARY

- 1.1 The purpose of this report is to present to the Audit and Scrutiny Committee the Internal Audit Annual Assurance Report for the year to 31 March 2018 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 on the adequacy and effectiveness of the Council's governance, risk management and internal controls to support the preparation of the Annual Governance Statement.
- 1.3 The Remit of the Audit and Scrutiny Committee indicates that it should ensure an adequate framework of internal control, risk management and governance throughout the Council.
- 1.4 To meet the requirements of the PSIAS the Internal Audit Annual Assurance Report 2017/18, at Appendix 1, includes the annual Internal Audit opinion, 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 PSIAS.
- 1.5 The Chief Officer Audit & Risk's opinion is that, based on Internal Audit reviews and knowledge, the systems of internal control, governance and risk management within the Council are operating satisfactorily.
- 1.6 The Internal Audit Annual Assurance Report 2017/18 has been used to inform the Chief Executive's Annual Governance Statement 2017/18.

2 RECOMMENDATIONS

- 2.1 I recommend that the Audit and Scrutiny Committee:**
- a) Considers the Internal Audit Annual Assurance Report 2017/18 (Appendix 1) and provides any commentary thereon.**
 - b) Agrees that the Internal Audit Annual Assurance Report 2017/18 be published on the Council's website.**

3 BACKGROUND

3.1 The Public Sector Internal Audit Standards (PSIAS) (2017) 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 Scrutiny 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 ASSURANCE REPORT 2017/18

4.1 The Internal Audit Annual Assurance Report 2017/18, at Appendix 1, includes the Chief Officer Audit & Risk’s independent and objective opinion regarding the adequacy and effectiveness of the Council’s governance, risk management and internal controls, 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 PSIAS.

4.2 The Chief Officer Audit & Risk’s opinion is that, based on Internal Audit reviews and knowledge, the systems of internal control, governance and risk management within the Council are operating satisfactorily. In respect of the most significant change for the Council relating to the implementation of the new Business World ERP system, there are system issues and delays in delivery of some functionality; the expected business benefits have not yet been realised and significant staff and consultant resources have been deployed to address issues and establish manual controls, where appropriate, in the interim.

4.3 Internal Audit reports during the year confirm improvements in internal controls, governance, and risk management through Management-initiated improvements complemented by the implementation of audit recommendations. Further improvements in internal controls, governance, and risk management 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 Assurance Report 2017/18 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 2017/18.

4.5 The annual internal self-assessment demonstrates sufficient evidence that the Council’s Internal Audit section conforms with the Definition of Internal Auditing and the Standards in the PSIAS.

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 2017/18 through improved internal controls and governance arrangements.
- (b) The net cost (projected outturn at February 2018) of the Internal Audit service was £234k (2016/17 £246k). The majority of service expenditure relates to staff costs (99%) for resources comprising Chief Officer Audit & Risk (50% allocation), Principal Internal Auditor, two Senior Internal Auditors, and two Internal Auditors.

5.2 Risk and Mitigations

- (a) Internal Audit provides assurance to Corporate Management and the Audit and Scrutiny Committee on the adequacy and effectiveness of internal controls, governance and risk management within the Council, highlights good practice and recommends improvements. Key components of the audit planning process include a clear understanding of the Council's functions, associated risks, and range and breadth of audit areas for inclusion within the plan. There is effective liaison between Internal Audit and the Corporate Risk Officer on an on-going basis to ensure that risk is considered in every audit and risk reviews take account of improvements arising from audit work.
- (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 Council's governance, risk management and internal controls, full 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 the independent opinion on the adequacy and effectiveness of the Council's governance, risk management and internal controls when completing the annual self-evaluation and assurance process for the Council's Annual Governance Statement 2017/18.
- 6.3 The Chief Financial Officer, the Monitoring Officer, the Chief Legal Officer, the Service Director HR, the Clerk to the Council, and Corporate Risk Officer have been consulted on the covering report and any comments received have been incorporated into the report.

Approved by

Jill Stacey, Chief Officer Audit & Risk **Signature**

Author(s)

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Background Papers: Appropriate Internal Audit files

Previous Minute Reference: Audit and Risk Committee 28 March 2017

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Contact us at Internal Audit intaudit@scotborders.gov.uk

Chief Officer Audit & Risk's Annual Report and Opinion 2017/18**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) (2017) 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 2018 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 and knowledge, the systems of internal control, governance and risk management within the Council are operating satisfactorily.
- 2.2 Internal Audit reports during the year confirm improvements in internal controls, governance, and risk management through Management-initiated improvements complemented by the implementation of audit recommendations.
- 2.3 The most significant change for the Council related to the implementation of the new Business World ERP system which went live from April 2017 for HR, Payroll, Procurement and Finance management and administrative processes. Due to system issues and delays in delivery of some functionality the expected business benefits have not yet been realised and significant staff and consultant resources have been deployed to address issues and establish manual controls, where appropriate, in the interim.
- 2.4 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 August 2017) and key governance documents including Scheme of Administration (approved November 2017), Procedural Standing Orders (approved June 2017), Scheme of Delegation (approved March 2018), Financial Regulations (approved June 2016), and Codes of Conduct for Councillors and for Employees. The Financial Regulations and associated policies, procedures and guidelines need to be reviewed, updated and developed, as appropriate, to reflect changes arising from the implementation of the Business World ERP system.
- 2.5 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.
- 2.6 Further improvements in internal controls, governance, and risk management 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 2017/18 Delivery

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

	Plan days 2017/18	Actual days 2017/18	Plan Nos. 2017/18	Actual Nos. 2017/18
Corporate Governance	140	110	6	6
Financial Governance	165	230	8	8
IT Governance	50	23	3	3
Internal Controls	60	85	3	4
Asset Management	65	47	4	3
Legislative and other Compliance	45	38	4	3
Consultancy and Advice	70	50		1
Other	52	70		
SBC Total	647	653	28	28
Non-SBC	65	86		
Total	712	739		

- 3.2 The level of Actual Audit days was slightly higher than plan (104%). This performance can be attributed to the greater direct audit productivity from the Internal Audit team than anticipated in the audit plan.
- 3.3 The allocation of audit plan days is not an exact science and some of the audit scopes have been carried out using less than planned days and some using more. The most significant variations are as follows:
- Financial Governance: A significant amount of additional audit assurance work related to the implementation of the new Business World ERP system which went live from April 2017 for HR, Payroll, Procurement and Finance management and administrative processes. This included Key Controls work, on which reliance will be placed by Audit Scotland (SBC's External Auditors), and review of Solution Design documents to understand system functionality. It should be noted that there has been significant learning and development on the new ERP system by Internal Audit which is expected to be beneficial for delivery of Internal Audit work in future years.
 - Internal Controls: an assurance audit on Registration Service was added to the Plan on request by Service Management.
 - Asset Management: The full scope of the planned assurance audit on Asset Registers has been deferred to 2018/19 to align to Business World development in agreement with Senior Management and External Auditors;
 - Legislative and Compliance: Selkirk Conservation Area Regeneration Scheme (Review as part of programme compliance and evaluation requirements of the external funders) has been rescheduled to 1st Quarter 2018/19 to align with the phasing of the return submission to Funder.
 - Non-SBC: More assurance work was performed for SB Cares and Scottish Borders Health and Social Care Integration Joint Board during the year and this has been reflected within the 2018/19 Annual Plan.
- 3.4 This has not affected the assurance that Internal Audit is able to give.
- 3.5 The wide range of Internal Audit work performed during the year is listed below:

Corporate Governance Audits

- 3.6 To provide assurances in relation to the Council's corporate governance framework that is a key component in underpinning delivery of the corporate objectives and priorities within the Council's Corporate Plan, reviews included:
- Corporate Governance (Assessment of progress on implementation of Improvement action plans, Annual Evaluation against Local Code of Corporate Governance, and involvement in the review of the Scheme of Delegation and Scheme of Administration, and associated Members Induction Training including Audit Committee).
 - Information Governance (Review of the framework including roles and responsibilities, policy development and implementation, and assess progress with implementation of improvement actions; Assess preparedness for the General Data Protection Regulations (GDPR) to come into force May 2018).
 - Performance Management (Validation of performance indicators and benchmarking information to support self-assessment and continuous improvement of the Council's services, specifically to ensure accuracy of data submitted for Local Government Benchmarking Framework and Corporate Priorities PIs).
 - Corporate Transformation Programme (Input to the planned review and refresh of the programme to influence the governance and accountability arrangements, including processes for benefit (financial and other) identification, tracking and realisation, and evaluation of outcomes and lessons learned).

- Complaints (Review and assess arrangements in place for both Corporate and Social Work complaints to provide assurance on whether the complaints process is being applied consistently to enable successful outcomes and realisation of the benefits associated with efficient resolution of complaints).
- Community Engagement (Evaluate systems and procedures to engage with and communicate to the community in setting, delivering and reporting on the Council's vision, priorities and plans. Assess Community Empowerment Act implications and extent to which the Council is complying with key elements of the legislation).

Financial Governance Audits

3.7 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 Policy Framework (Assess the Financial Policy Framework established as part of Business World implementation, review progress with update of Financial Regulations and associated policies, procedures and guidelines, and evaluate whether there is a comprehensive programme in place to review, update and develop relevant policies, procedures and guidelines; Carry out a specific assurance audit on Petty Cash Imprest and Emergency Funding to assess the processes and efficiency of the petty cash administration system (following on from our similar review in 2013) and provision of financial support to vulnerable people in emergency situations (on request from Chief Financial Officer following the Grenfell Tower incident in 2017)).
- Business World ERP System Key Controls incorporating Payroll, Sales to Cash, Procure to Pay, and Record to Report system process (Assess key controls of the new system for Payroll, Sales to Cash, and Procure to Pay processes and core General Ledger and Management Reporting (Record to Report), assess System Access, test sample of transactions from various data sets to determine if expected improved internal financial controls are being achieved, and perform the independent reconciliation and validation of extracted data from existing systems and of uploaded data into Business World ERP System).
- Contract Management (Assess governance and internal controls in place over contract monitoring arrangements with third parties including integrated sports and culture trust (Live Borders) and ALEO (SB Cares)).
- Revenues – Council Tax (Assess the application of the Council Tax increase in 2017/18 and the legislative changes to the 2017 Council tax multiplier affecting bands E – H; and Follow-up testing on completeness and accuracy of Council Tax income associated with the new 2016/17 approved policy on second homes, and key controls introduced including application of discretionary exemptions).
- Grants and Following the Public Pound (Follow-up on progress with implementation of previous Recommendations, including the update of the Following the Public Pound code of practice, and the Grants Review Project in support of securing best value).

ICT Governance Audits

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

- ICT Contract Management (Review of client relationship and contract management with CGI contract to assess compliance with Service Delivery and terms and conditions).
- ICT Security Controls (Assess the adequacy of the security arrangements including physical and environmental controls, disaster recovery, third party access, and operational controls – note: covered by PSN assurance work and input to the Council's

response to Scottish Government on the draft public sector action plan on cyber resilience, and consideration of cyber resilience essentials).

- Public Secure Network (PSN) Compliance (Examine the Council's compliance with PSN requirements and progress with implementation of actions required to achieve full compliance. Assess fulfilment of roles and responsibilities within the Council and CGI under contract).

Internal Controls Audits

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

- Schools – Peebles HS, Berwickshire HS, Selkirk HS, Morebattle PS, Duns PS and St Boswells 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, including evaluation of the systems in place to set and monitor budgets devolved to head teachers to ensure adherence to DSM standards and practices).
- Community Safety (Evaluate the partnership working within Community Safety to ensure responsibilities and accountabilities of partners are clearly defined and to ensure funds are used effectively and economically for the intended purpose to meet local priorities).
- Children & Young People Services Excursions (Assess what controls and processes are in place to ensure safety of children and young people on excursions).
- Registration Service – additional to the Plan on request by Service Management (Assess whether the Council is complying with the relevant legislation and has adequate controls are in place for registration fees and charges income).

Asset Management Audits

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

- Capital Investment (Assess progress with implementation of identified improvement actions to ensure compliance with established good practice by Accounts Commission "Major capital investment in councils" and 'Good Practice Guide' (March 2013) and "Follow-Up" (January 2016) - strategic asset management plans; governance of capital investment; capital planning; review, scrutiny and challenge; capital financial budget monitoring; delivery of the capital programme and capital plan projects).
- Industrial and Business Premises (Assess the corporate governance and financial governance arrangements linked to priorities within the Economic Strategy relating to Industrial and Business Premises and associated estate management including: strategy; development and implementation of infrastructure; demand analysis; estate management end to end processes from lease agreements, voids, and income management).
- Fleet Management (Evaluate controls in place to ensure fleet asset records are complete and accurate and fleet replacement decisions represent value for money. Review procurement practices for compliance and consider options for volume / value invoice processing. Consider repair and maintenance processes and supporting evidence associated with insurance claims).

Legislative and Other Compliance Audits

- 3.11 To test compliance with the terms of the funders' service level agreements or legislative requirements, reviews included:
- EU LEADER Grants (Annual review of LEADER programme required by the Service Level Agreement (SLA) between Scottish Ministers (Managing Authority and the Paying Agency) and Scottish Borders Council (Lead Partner for Scottish Borders Local Action Group) 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).

Consultancy Work

- 3.12 The most significant piece of consultancy work related to the implementation of the new Business World ERP system, with Internal Audit input provided at various workstream team meetings, workshops and the Project Board throughout the year.
- 3.13 In its 'critical friend' role, Internal Audit provided internal challenge on the planned programme of "How Good is Your Council" self-assessment and evidence completed by various Services to support self-evaluation and improvement as part of the Performance Management Framework.
- 3.14 A further piece of consultancy work was delivered on request from Passenger Transport Management. Internal Audit highlighted opportunities by way of a report to Management to improve the effectiveness, efficiency and sustainability of the arrangements for internal recharging of Passenger Transport Services provided to the Children and Young People Service and the Adult Social Care Service through innovation and change.
- 3.15 During the year Internal Audit responded to a number of requests for ad hoc advice and assistance on internal controls, risk management and governance, and considered and applied National Reports that give rise to introducing best practice arrangements or lessons learned from other local authorities or other public sector bodies. 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.

Other Work

- 3.16 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.
- 3.17 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: Pentana performance system as at 10 April 2018) with regards to Internal Audit recommendations arising from current and previous years:

Year identified	Total	Implemented	Not Yet Due	Overdue
2017/18	42	2	33	7
2016/17	10	8	0	2
2015/16	21	21	0	0
2014/15	34	30	4	0

- 3.18 In collaboration with the Corporate Fraud and Compliance Officer, Internal Audit provided intelligence via data sharing requests from Police Scotland, and submission of data sets and case management of data matches arising from the National Fraud Initiative (NFI) exercise as part of the wider assurance framework on counter fraud and crime controls.

Non SBC Work

- 3.19 The Council's Internal Audit service provided independent assurance on the overall risk management, internal control and corporate governance processes for SB Cares (the Council's adult social care ALEO), Scottish Borders Pension Fund, and Scottish Borders Health and Social Care Integration Joint Board. Separate annual audit assurance opinions are reported to their respective Senior Management and Boards, based on the work delivered in accordance with Annual Audit Plans that have been approved by their respective Senior Management and Boards.

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) (2017) 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 An internal self-assessment of Internal Audit practices against the Standards was carried out in 2017/18, as required by the PSIAS, taking into account the improvement actions implemented since the previous year's self-assessment and those arising from the External Quality Assessment Peer Review carried out by Renfrewshire Council in October 2015.
- 4.3 The 2017/18 self-assessment confirms completion of all remaining improvement actions in the Quality Assurance and Improvement Plan and 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. Internal Audit conforms with the Definition of Internal Auditing and the Standards.

Jill Stacey BA(Hons) ACMA CGMA
Chief Officer Audit & Risk
13 April 2018