

The Highland Council

Audit & Scrutiny Committee – 19th June 2014

Agenda Item	4
Report No	AS/8/14

Statement on Internal Control and Annual Report 2013/14

Report by Head of Internal Audit & Risk Management

Summary

The attached report includes an assessment of the adequacy, reliability and effectiveness of the Council's system of internal financial control and provides information for the Council's Corporate Governance Assurance Statement. This is contained within the Statement on Internal Control.

The annual report provides an overview of the Internal Audit Section's activities and performance data for 2013/14.

1. Statement on Internal Control

- 1.1 In order to comply with the requirements of the CIPFA Standards, a Statement on Internal Control must be produced. Section 2 of the attached report gives details relating to the Statement on Internal Control and the sources of information which inform the Statement.
- 1.2 On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control systems for the year to 31st March 2014.

2. Annual Report 2012/13

- 2.1 The report gives an overview of the Section's activities during 2013/14 and provides the first year's new performance data.

3. Implications

- 3.1 There are no Resource; Legal; Equalities; Climate Change/Carbon Clever; Risk and Gaelic and Rural implications arising from this report.

Recommendation

Members are invited to note the content of the attached report and the audit opinion provided, and to raise any relevant points with the Head of Internal Audit & Risk Management.

Designation: Head of Internal Audit & Risk Management

Date: 10th June 2014

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Background Papers:



The Highland Council

Statement on Internal Control and Annual
Report 2013/14

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1. INTRODUCTION

- 1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1st April 2013 to 31st March 2014, and a report that can be used by the Highland Council to inform its Governance Statement.
- 1.2 This report has been produced in accordance with the requirements of the Public Sector Internal Audit Standards (the Standards) which came into effect from 1st April 2013 and apply to all internal audit service providers. These Standards were developed in collaboration between the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors (CIIA).
- 1.3 Section 2450 of the Standards states that *“the annual Internal Audit opinion must conclude on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and control. In addition, the annual report must incorporate:*
 - *The opinion;*
 - *The summary of work that supports that opinion; and*
 - *A statement on conformance with the Standards and the results of the quality assurance and improvement programme”.*
- 1.4 This report also includes an overview of the Internal Audit Section’s activities for the financial year 2013/14.

2. STATEMENT ON INTERNAL CONTROL

2.1 Internal Control

The Council's Financial Regulations require Service Directors to ensure the principles of internal control are incorporated in the working practices of their Services.

Internal control is defined as *"the whole system of checks and controls, financial or otherwise, established by management in order to provide reasonable assurance"* regarding the achievement of one or more of the following objectives:

- The reliability and integrity of information.
- Compliance with policies, plans, procedures, laws, regulations and contracts.
- The safeguarding of assets.
- The economical and efficient use of resources.
- The accomplishment of established objectives and goals for operations or plans.

Any system of control can only provide reasonable, and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud or breaches of laws and regulations. Accordingly the Council should seek continual improvement in the effectiveness of its systems of internal control.

2.2 Internal Audit

The Standards define internal auditing as *"an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes"*.

The work undertaken by Internal Audit is documented in an audit report and issued to management. Any areas of concern together with the management agreed actions and target dates for implementation are summarised in an Action Plan within the report. It is the responsibility of management to ensure that implementation of these actions takes place as agreed. The Internal Audit Section will undertake periodic follow-up reviews to ensure that the management agreed actions have been satisfactorily implemented and the results of this are reported to the Audit & Scrutiny Committee.

The Internal Audit Section operates in accordance with the Standards and as required, a risk based tactical audit plan is produced each year, and submitted for approval to the Audit & Scrutiny Committee. Organisational independence is demonstrated by the Head of Internal Audit & Risk Management reporting in his own name to senior management, and having direct access to the Chief Executive, Audit & Scrutiny Committee, Pensions Committee, and/ or other Members as considered appropriate.

An internal assessment of compliance with the Standards has been undertaken using the CIPFA "Checklist for Assessing Conformance with the PSIAS and the Local Government Application Note". The detailed results of this assessment have been provided in a separate report to the Audit & Scrutiny Committee which shows:

- 76% full compliance;
- 14% partial compliance;
- 10% non-compliance with the various areas set out in the Standards.

The main area of non-compliance relates to the need for a Quality Assurance and Improvement Programme (QAIP) which covers all aspects of the internal audit activity and enables conformance with the Standards to be evaluated. There are various performance targets and measures in place to monitor Internal Audit's

activities (see performance data provided at section 5) but these have not been included within a QAIP document. This will be addressed shortly with an action plan prepared to address the areas of partial and non-compliance and will be considered by the Audit & Scrutiny Committee at their September meeting.

2.3 Internal Audit work

The 2013/14 audit plan was presented to the Audit & Scrutiny Committee on 27/03/14. A progress report and details of all audit reports are provided as a standing agenda item to each Committee meeting. A summary of the audit reports issued together with the audit opinion and grades is provided at Section 3.2.

The plan also includes a programme of work to support the Statement on Internal Control which includes:

- A high level review of the Council's system of internal control by way of an evidence-based checklist comprising of six key areas:
 - Control environment.
 - Identification and evaluation of risk and control objectives.
 - Information and reporting.
 - Control processes.
 - Monitoring and corrective action.
 - Assessment of whether the key controls have been applied during the year.
- Examination of the Council's main financial systems. Individual audits have been undertaken of the Councils budgetary control system and creditors system which examined the processes for the ordering and payment of goods and services. The other systems; Debtors, Payroll, General Ledger and Income have been subject to a review of the key controls including:
 - Financial procedures and guidance issued to staff;
 - Segregation of duties;
 - User access levels and appropriateness;
 - System backups.

A sample of transactions was also selected for detailed testing to verify that the controls were operating as expected and no control issues were identified.

At the time of writing this report the testing of payroll transactions had not been completed. With the exception of payroll, no control issues have been identified from this work which affects the audit opinion and the audit findings will be addressed in a separate report.

- Consideration of the Council's arrangements with regard to information management and security, corporate governance and risk management.

2.4 Areas of concern

Any areas of concern identified from an audit review will result in an audit recommendation being made which is contained within an action plan. These recommendations are graded as high, medium or low; high defined as *"major issues that managers need to address as a matter of urgency"*.

During 2013/14, a total of 134 audit recommendations were made. Of these, 14 were classified as high grade and details are provided in Table 1 overleaf. A full breakdown of the audit grades and the overall audit opinions can be found at Table 3 on pages 13 - 14.

Table 1

Area of Concern – High Grades	Update
<p><u>ICT Contract- Payment Process</u></p> <p>The supplier did not deliver an adequate Asset Register, and so Utility Charging had not commenced. As a result, the Council was paying for baseline monthly volumes of Core Services as opposed to actual volumes.</p> <p>In addition, ICT Services had to provide additional information to the supplier on the source information required to support Utility Charging as this contract did not clearly specify this.</p>	<p>Utility charging was due to be introduced by 31/08/13 and it was confirmed that this was implemented from 01/04/14. Reasons for the delay were reported to the FHR Committee in October 2013</p> <p>It was agreed that this will be addressed with future contracts which will include detailed source information requirements to validate/ evidence supplier's calculation of volumes.</p>
<p><u>Compliance with the Carbon Reduction Commitment Energy Efficiency Scheme 2010-11 and 2011-12</u></p> <p>CO₂ emissions relating to gas supplies were materially overstated in the 2010/11 Footprint Report. A number of other material errors were found in both years reported data which did not agree to the suppliers' annual emission statements.</p>	<p>This was followed up as part of the 2012-13 audit which showed that the agreed action had been undertaken. No material errors were found in this year's audit.</p>
<p><u>Schools – Financial Procedures</u></p> <p>There were a number of issues with School Lets Income in one School. Namely; income had been received by the School Fund rather than the Council; it could not be established if all income due had been received and banked; and there was no procedure for the recording of the float amount, the income sums received and reconciling this to receipts issued.</p>	<p>This action remains outstanding and has a revised target date of 28/08/14. This links with a report on School Lets which is to be provided to the next meeting of the Education, Children and Adult Services Committee.</p>
<p><u>Payments to Third Sector Organisations (Follow-up)</u></p> <p>The question contained within the Pre-Qualification Questionnaire regarding the provision of/ application for Council funding needs to be clearer as to the information requested in order to ensure that any possible duplicate funding can be identified.</p> <p>The information on SharePoint which should detail all grant applications received and their outcome was incomplete and inaccurate and could not be relied upon.</p>	<p>This action was due on 31/03/14 and an update is presently awaited.</p> <p>This agreed action has been implemented. New guidance was developed to support the Sharepoint system, and face to face training for key officers and business support was provided. In addition, online training will be developed by 30/11/14 to ensure that ongoing support is in place.</p>

Area of Concern – High Grades	Update
<p><u>Governance of Arms-Length External Organisations (ALEOs)</u></p> <p>(1) The Council does not maintain a central register of all organisations that fall within the definition of being ALEOs.</p> <p>(2) The role of the Leisure & Learning Client Manager in relation to High Life Highland is not operating effectively.</p> <p>(3) .There has been limited financial and performance information reported to the Council by Caledonia Community Leisure Ltd.</p> <p>The role of the Leisure & Learning Client Manager) in relation to Caledonia Community Leisure Ltd is not operating effectively.</p> <p>(4) There is no reporting to a Council Committee on the financial or governance issues of Eden Court.</p> <p>No financial or governance information is published and available to the public.</p> <p>The Learning and Leisure Client Officer is the Liaison officer within Highland Council but it is not clear that his remit includes Eden Court.</p> <p>(5) The Board of Directors of HOL is made up of 9 Directors, all of whom are Council Members. Unlike HLH and CCLL, there are no independent Directors. It is, therefore, important that the Members appointed have the necessary skills to perform their roles effectively</p> <p>(6) Caithness Horizons receives direct funding of £104,561 and rent free accommodation worth £61,000. No Memorandum & Articles or Liaison Council Officer could be identified.</p> <p>The funding is to continue for another 5 years and a robust reporting procedure implemented. At the time of the review it was agreed that ECS would take responsibility for the organisation.</p>	<p>This audit has not yet been followed up as the final action is not due to be implemented until 31/03/15. However, 2 target dates for (3) and (4) below were due on 31/03/14 but this was later revised to 30/06/14.</p>
<p><u>Children and Families Team – System Weaknesses report</u></p> <p>This report was prepared following an investigation into the fraudulent activities by a Team Manager in respect of Section 22 payments and travel claims.</p> <p>(1) Section 22 payment forms were not fully completed, and were not always evidenced that the client had received the payment. In addition, the payments considered to be fraudulent were not recorded on the Carefirst system.</p> <p>(2) Expenses claims were authorised for journeys that did not take place.</p>	<p>All of the management agreed actions have been implemented as agreed.</p>

Area of Concern – High Grades	Update
<p><u>Housing Benefit and Council Tax Benefit Payments 2012/13</u></p> <p>This parameter update report identifies the financial amount of every category of benefit in payment in any given year. It should be run, checked against the DWP guidance and signed off by an appropriate officer after benefits are updated for each new financial year.</p> <p>The report had not been run after the completion of the uprating exercise for the year 2013/14 until it was requested during the audit review.</p>	<p>This was addressed at the time of the audit when the report was produced and actioned.</p>
<p><u>Information Security</u></p> <p>There was a lack of staff awareness of Information Security. Only 19% of staff who were sent the Information Security Questionnaire had carried out the online training and other staff were unaware of basic information security practices.</p>	<p>In response, it was agreed that the low take up of Information Security Training will be raised with the Senior Management Team. This action is due on 30/06/14.</p>

2.5 Action Tracking

The areas of concern detailed in Table 1 have been addressed by audit recommendations agreed with Management who should take the necessary implementation action. As part of the audit process, these are action tracked to ensure that the agreed actions were implemented as agreed. The results of the action tracking, including delays in achieving the target dates are reported to the Audit & Scrutiny Committee on a regular basis and a report is provided as a separate agenda item.

5 follow-up reports (Payments to Nursery providers, School Meals Income and Collection Systems, Contractor's Framework Agreement for works up to £50,000, Business Continuity Planning Arrangements and Corporate Internet Use) were included within the 2013/14 audit plan as these had the audit opinion of "Limited Assurance" and/ or contained high grade recommendations. With regard to the follow-up of Corporate Internet Usage, there was dialogue with ICT Services round the high grade action to run regular monitoring reports. The audit was postponed in the knowledge that these reports were not yet available. Therefore the audit has been included within the 2014/15 audit plan in order to provide assurance over the revised reporting procedures which are now being introduced.

The 2013/14 annual report referred to a report to Committee on 28/03/13 which stated that a number of audit actions had not been implemented, despite assurances to the contrary for some of them. The Chair and Members of the Committee expressed their dissatisfaction regarding this at the meeting. In response, the former Chief Executive requested a report from the Head of Internal Audit & Risk Management which resulted in revised procedures being put in place from 15/04/13. However, the recent follow-up audits have identified that this process has not been complied with, and 6 high grade actions that were due to be implemented in 2013/14 have only been partially addressed. Details are provided in Table 2 overleaf.

In view of the above position, the Head of Internal Audit & Risk Management has written to all Directors and Service administrators of the Performance and Risk Management system (PRMS) and has reminded them of the following:

- Actions should only be signed off as complete by the responsible Head of Service.

- Where extensions of time are sought to implement agreed actions, requests must be made by the responsible Head of Service to the Head of Internal Audit & Risk Management.
- The monitoring of outstanding actions should form part of regular performance monitoring within each Service.

In addition to the above:

- Internal audit reports will, in future, be issued to the appropriate Service PRMS administrator in order that they can ensure that all reports are entered onto the system.
- Financial Regulations have been updated to reinforce the procedures regarding the audit actions.
- Compliance with the above processes will be reviewed during the course of this year and will be reported back to Committee.

Table 2

Area of Concern – High Grades	Update
<p><u>Corporate Internet Use</u></p> <p>Reports produced for Service monitoring were considered by Service Managers to be unreliable and not user friendly. In addition, there is no automated exception reporting alerts of suspected unauthorised corporate Internet use.</p>	<p>The revised monitoring reports which show high unauthorised internet use have not yet been implemented. Some of the reasons for this are as follows:</p> <ul style="list-style-type: none"> • The correct distribution of these reports is dependent on a Websense link to an out of date Council structure held within Active Directory network management software. Updating Active Directory is a large and complicated task which will need to be addressed, possibly during ICT re-provision. • The revised monitoring reports that were produced do not work on a new version of the Websense Software which has been implemented. <p>The current plan to overcome the above difficulties is to run Council wide reports which are not dependent on the Council's changed organisational structure. These will be run from June 2014.</p> <p>However, if a manager does suspect an individual of high unauthorised internet use, a report can be requested from ICT Services in accordance with the Acceptable Use Policy.</p>

Area of Concern – High Grades	Update
<p data-bbox="300 230 727 257"><u>Business Continuity Planning (BCP)</u></p> <p data-bbox="300 275 919 331">There are a total of 4 high grade actions which have not been fully implemented as agreed:</p> <p data-bbox="300 349 919 517">(1) There was no BCP for the Council to be used in any situation. It was agreed that a general Business Continuity Plan would be produced and approved by the Senior Management Team (SMT). The BCP would then be subject to annual review.</p> <p data-bbox="300 539 919 768">(2) It was identified that additional information should be included within the BCP as set out in best practice. There were Service specific issues which required addressing, and then inclusion within the BCP. It was also recommended that a Lead Service should assess which Council properties are useable and the facilities available in each building.</p> <p data-bbox="300 902 919 1077">(3) The recommendations from a report on flooding which resulted in a network outage, had not all been implemented. In particular, the Council's HQ was a single point of weakness in the Council's network and this required to be addressed.</p> <p data-bbox="347 1099 919 1267">It was agreed that the corrective actions would be addressed through an improved networks resiliency plan. In addition, it was intended to undertake a design review of the servers which were not included as part of the data centre migration.</p> <p data-bbox="300 1328 919 1469">(4) There are limitations with the back-up data centre which means that its use must be restricted to critical services. However, these had not been agreed between ICT Services and the Council's individual Services.</p>	<p data-bbox="946 349 1417 495">Whilst a Corporate BCP has been produced, it has not been approved by the SMT. In addition, it is incomplete and requires revision to reflect the new Council structure.</p> <p data-bbox="946 539 1417 887">It was agreed to establish Service-specific BCP working groups to create service-level response plans which would become an integral part of the BCP. The first stage of producing service level Business Impact Assessments (BIA) is nearly complete. Once this has been done they will be approved by the Executive Leadership Team and then the Services can write their Service level BCP.</p> <p data-bbox="946 909 1417 1312">This has been addressed except for the design review where a different approach was taken. The majority of issues have been resolved with the provision of two network routes, and the connections which can be used to divert traffic if any problems occur. The process for switching between networks still requires documenting. Also, any critical applications which are run on servers outside of the data centre should be identified during service reviews and addressed accordingly.</p> <p data-bbox="946 1335 1417 1581">It was agreed that critical services would be reviewed as part of the Data Recovery/ Business Continuity annual review and the operating procedure would be updated to reflect the prioritisation of systems. In addition, the limited capacity of the back-up data centre was to be identified and included in the corporate BCP.</p>

Area of Concern – High Grades	Update
<p data-bbox="295 230 919 286"><u>School Meals Income Collection and Monitoring Systems</u></p> <p data-bbox="295 304 919 533">It was recommended that the functionality of the school meals computer system (Saffron) should be enhanced so that a report of individual lodgements can be generated and individual lodgement amounts should be recorded on Saffron. Following this, monthly reconciliations should be completed on an individual lodgement basis to the general ledger.</p> <p data-bbox="295 551 919 692">This was accepted by management this has been requested, and would be addressed as part of a system upgrade, due for completion by end December 2012. Thereafter, income reconciliation will be carried out monthly</p>	<p data-bbox="941 304 1409 734">This has been partially addressed as an improved income reconciliation report was introduced and is in use. However, this did not provide the expected functionality with regard to the ability to record/ report meaningfully on individual lodgements and it was unclear if this would be feasible. Recent discussions with the supplier have suggested that this will be feasible, subject to the required data and format being obtained from Oracle. This is presently being addressed with the Finance Service.</p> <p data-bbox="941 752 1409 869">If this is not feasible, then other options will need to be explored in order to undertake monthly reconciliations.</p>

2.6 Assurance from Service Directors

As part of the Annual Accounts process, all Service Directors are asked to provide assurance that the following statements are valid:

- That Financial Monitoring Statements are regularly reviewed at Service Management Meetings.
- That Staff have been made aware of Financial Regulations and Contract Standing Orders.
- That Staff have been made aware of the Code of Conduct, Information Systems Security, Fraud and Corruption and Whistle blowing policies.
- That the Service has a robust scheme of delegation and that Staff have been informed of their supervisory and accountability responsibilities and that their responsibilities are documented in a Job Description.
- That segregation of duties is an important control mechanism operation within the Service and where it has not been possible to operate such a control a suitable alternative is in place.
- That appropriate targets have been established within the Service to measure financial and other performance.
- That a formal system of project management, including project governance operates within the Service.
- That appropriate arrangements are in place to govern companies.

The necessary assurances have been provided by all Service Directors and no issues have been highlighted which affects the Statement on Internal Financial Control.

2.7 Information Management and Security

The majority of the Council's information systems and services are currently provided by Fujitsu Services as part of a five year contract which commenced on 01/04/10 and has been partially extended for a further 18 months. The Council's ICT cost management framework and disaster recovery are also included within the Fujitsu contract. Performance of the contract and service delivery is monitored by the ICT Partnership Board and has been reported to the Finance, Housing and Resources (now Resources) Committee in April and October 2013. A dedicated ICT re-procurement team has been set up for re-provision beyond 2015 for some services, and beyond September 2016 for the majority of the contract

services. In August 2013 a notice was published in Public Contracts Scotland that it is likely a mixed economy approach for ICT Services re-procurement will be taken.

In addition to Fujitsu, the Council's other main ICT supplier, Vodafone (which acquired Cable & Wireless), provides managed data network services to Schools, Libraries and Council administration locations and had an extension to the Pathfinder North (PfN) contract from 2014 to March 2016. PfN contract performance is monitored by the Pathfinder North Partnership and is reported to the Resources Committee twice a year. The Partnership joined the Scottish Wide Area Network (SWAN) Vanguard Project to procure a single, network service for use by potentially all Scottish public service organisations and the Pathfinder North Project operating within Vanguard, has received a thorough External Project Assurance Review. This Review found that the re-procurement project was extremely well managed enjoying excellent project governance driven by a strong and genuine commitment to work in partnership. However, it was identified that the value of the benefits gained by the strong partnership and management will be eroded unless decisions are quickly taken to provide certainty on the future role of the partnership and the adequate resourcing of the management team. The Partnership agreed at a Project Board meeting in early 2014 to continue the Partnership for the foreseeable future and to actively look at developing this to include additional Partners (including baseline staffing requirements for the PfN Team). This is outlined in the 'Next Stage Plan – Transition and Partnership Development'.

The concurrent renewal of the Council's two major ICT service delivery contracts and the move to a mixed economy approach creates a challenging contract management environment for the Council's ICT Services.

The Council's compliance renewal date with authorisation to use the Cabinet Office's Public Sector Network for secure email communications between it and its government partners and applications such as DWP and Blue Badge, has been extended from September 2014 to 30/04/15.

The Council's latest organisation structure has still to be updated within its network management software Active Directory. This will be a substantial piece of work which will be implemented after the final structure is implemented by Services. In addition improvements in network audit logging and user access monitoring are under consideration.

The Council has an approved Information Security Management System in place as required by ISO 27001. In addition it has an Information Security Policy and Acceptable Use Policy. Operational Information Security management is managed by ICT Services and an ICT Security Group exists to support this through the review of security incidents and identifying and evaluating security risks. The Information Management Governance Board reviews high level information security risks referred from the ICT Security Group and other information security risks that relate to non-ICT issues. A formal review carried out in 2010 highlighted areas where the Council did not fully meet ISO 27001 compliance requirements at that time. However, a substantial amount of work has been carried out since that review and another formal review is due to be carried out in June 2014 as part of the Fujitsu ICT Contract Security Plan.

Third parties used to host Council systems and data may be required to hold an ISO 27001 certification and this will be considered in future procurement exercises. Fujitsu has ISO 27001 information security management certification for their Data Centre in Stevenage and their back up site in London until 04/12/15. During 2013/14, a member of Internal Audit visited the Stevenage Data Centre and controls were found to be as expected. In addition an Internal Audit review of physical and environmental security for other Inverness data sites,

not included in the Fujitsu certificate of assurance, was carried out. This review reported the audit opinion of "substantial assurance" for the areas covered.

ICT Projects carried out as part of the Fujitsu ICT contract are controlled through the PRINCE2 project management methodology and are overseen by a Projects Review Board. The Council has an approved ICT Strategy to support the Council's Corporate and Service Plans covering the period from 2012 – 17, and was last revised in October 2013.

The Information Management Governance Board also oversees the Information Management Strategy and its implementation across the Council, and this is supported by an Information Management Policy. Internal Audit reviewed the management of Council records by High Life Highland in the records repository at the Highland Archives and Registration Centre in Inverness. The review included observations of progress on records management in the Managing Information Project within the Corporate Improvement Programme and consideration of new legal requirements of the Public Records (Scotland) Act. The audit report provided an opinion of "substantial assurance" for the areas covered.

The Board also oversees data protection issues. The Council previously recognised that arrangements for data protection compliance with regard to governance and controls need to be strengthened and produced an action plan to introduce appropriate improvements which is predominantly complete. Actions are being monitored by the Information Management Governance Board.

2.8 Governance arrangements

The Council has a Local Code of Corporate Governance, which is consistent with the principles and reflects the requirements of the CIPFA/SOLACE Framework Note for Scottish Authorities – Delivering Good Governance in Local Government (2007). This framework has been updated with regard to the CIPFA Statement on the "*Role of the Chief Financial Officer (CFO) in Public Service Organisations*" and a supporting CIPFA/ SOLACE application note has been produced which shows that the Council complies with most of the additional governance requirements. Governance will be strengthened further when the Council's Financial Regulations are revised to clarify that the CFO, as well as the Head of Internal Audit & Risk Management, has direct access to the Audit & Scrutiny Committee. The revised Financial Regulations are due to be approved by the Audit & Scrutiny Committee on 19/06/14.

The Deputy Chief Executive/ Director of Corporate Development is responsible for:

- overseeing the implementation of the Local Code of Corporate Governance and monitoring its operation
- reviewing the operation of the Local Code of Corporate Governance in practice
- reporting annually to the Council on compliance with the Local Code and any changes required to maintain it and ensure its effectiveness.

This process is subject to annual audit and the 2013/14 review has not identified any control weaknesses in the Council's governance arrangements and the audit opinion of "substantial assurance" has been provided.

2.9 Risk Management

Risk management is a key element of Corporate Governance. The Council has a risk management strategy which demonstrates its commitment to maintaining a structured approach to risk management and ensuring that it effectively manages its risks. The strategy is subject to annual review and the last update was approved by the Audit & Scrutiny Committee on 20/06/13.

Review of the Corporate Risks, which should be undertaken on a six-monthly basis, was delayed due to the re-structuring of the Internal Audit & Risk

Management Section and then the subsequent re-structuring of Council Services. However, a review of the Corporate Risks with the new Executive Leadership Team took place in May 2014 and the result of this process is reported as a separate agenda item to Committee. A new approach has been taken which has resulted in:

- The risk information being clearly recorded which was not the case previously and this had been criticised by Audit Scotland in their Annual Plan for 2013/14;
- A fewer number of risks appearing on the register which accords with CIPFA's best practice which suggests that organisations should focus upon their "top ten" risks;
- Clear actions being recorded which address the identified risks and these have been assigned to appropriate officers with target dates set. This will allow progress to be monitored and reported upon to Members.

Further risk management training was provided to Members on 14/02/14 by a Risk Management Consultant from Zurich and the new Audit & Risk Manager. One of the agreed outcomes from this training was that better information would be provided to Members to enable them to properly scrutinise the process.

Following on from this, the Committee was informed at their meeting of 27/03/14 that a number of changes, including better report information, would be made to further enhance and improve upon the risk management arrangements and embed these throughout the Council. The new report format (see agenda item 7) has been agreed with the Chair of the Audit & Scrutiny Committee and is now in place. In addition, a plan has been agreed between the Head of Internal Audit & Risk Management and the Audit & Risk Manager as to the changes required over the forthcoming year and these consist of:

- A review of the Corporate and Cross Cutting Risk process by 30/06/14 (this has been completed).
- Establishing a Corporate Risk Management Group which will encompass all risks including ICT and major projects by 30/09/14.
- Revision of the Council's Risk Management Strategy by 31/12/14.
- Improving the robustness of the process for recording and monitoring Service risks, including ICT and project risks by 31/03/15.

2.10 Audit Opinion

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control systems for the year to 31st March 2014.

3. INTERNAL AUDIT GRADINGS AND OPINIONS

3.1 During the year, a total of 20 final reports were issued. Where the report contains an audit recommendation, this is given a grading of high, medium or low. In addition, the report contains an overall audit opinion which is used to inform the annual statement on internal control. With regard to the audit opinion, there are five levels of assurance which have the following definitions:

Level	Definition
Full Assurance	There is a sound system of control designed to achieve the system objectives and the controls are being consistently applied.
Substantial Assurance	While there is a generally a sound system, there are minor areas of weakness which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.
Reasonable Assurance	Whilst the system is broadly reliable, areas of weakness have been identified which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.
Limited Assurance	Weaknesses in the system of controls are such as to put the system objectives at risk, and/ or the level of non-compliance puts the system objectives at risk.
No Assurance	Control is generally weak, leaving the system open to significant error or abuse, and/ or significant non-compliance with basic controls leaves the system open to error or abuse.

3.2 Table 3 below, provides a summary of the audit reports issued together with the audit opinion, number of recommendations and a breakdown of the associated grades.

Table 3

Report Name	Report Date	Audit Opinion	No. of Recommendations	High	Medium	Low
ICT Contract – Payment Process	11/06/13	Substantial	14	1	13	0
Compliance with the Carbon Reduction Commitment Energy Efficiency Scheme 2010/11 and 2011/12	11/06/13	Limited	2	1	0	1
Schools – Financial Procedures	22/07/13	Limited	18	1	10	7
Housing Rents	16/09/13	Substantial	9	0	2	7
Housing Stores/ Repairs and Maintenance	16/09/13	Substantial	4	0	3	1
Curriculum Internet Use	06/11/13	Substantial	7	0	7	0
Corporate Governance Arrangements 2012/13	07/11/13	Reasonable	4	0	4	0
AXIS 4 - European Fisheries Funding Project	08/11/12	Reasonable	6	0	6	0
Payments to Third Sector Organisations (Follow-up)	11/11/13	Limited	4	1	3	0

Report Name	Report Date	Audit Opinion	No. of Recommendations	High	Medium	Low
Governance of Arms-Length External Organisations	12/11/13	Reasonable	9	6	3	0
Leader Programme 2012/13	17/12/13	Reasonable	5	0	5	0
Children and Families Team - System Weakness Report	19/02/14	Limited	2	2	0	0
Access and Authorisation Controls (Pecos and Accounts Payable)	19/02/14	Substantial	6	0	6	0
Debtors	10/03/14	Reasonable	7	0	4	3
Travel & Subsistence - Travel Desk Arrangements	14/03/14	Substantial	6	0	5	1
Housing Benefit and Council Tax Benefit Payments 2012/13	17/03/14	Substantial	4	1	2	1
Compliance with Carbon Reduction Energy Efficiency Scheme 2012/13	18/03/14	Full	1	0	0	1
Data Handling and Security	18/03/14	Substantial	8	0	7	1
Information Security	19/03/14	Substantial	5	1	4	0
Totals			121	14	84	36

4. OVERVIEW OF 2013/14

4.1 2013/14 Tactical Plan

The 2013/14 tactical plan was presented to the Audit & Scrutiny (A&S) Committee on 27/03/13. Progress against the plan is reported as a standing item at each Committee meeting as part of the internal audit reviews and progress report.

The audit reviews which could not be undertaken during the year, as originally planned, were discussed with Directors as part of the consultation process in producing the 2014/15 tactical plan.

4.2 Staffing Issues

The 2012/13 annual report made reference to the restructuring of the section which had been approved by the Finance, Housing & Resources Committee on 05/06/13. This resulted in the Insurance function being transferred to the Head of Accounting & Budgeting and Internal Audit and Risk Management remaining within the existing staff complement of 10 WTE (excluding the Head of Internal Audit & Risk Management).

In order to facilitate the restructuring 2 Auditor posts were held vacant and, in addition other vacancies arose during the course of the year which were reported to Committee as part of the standing item on the Progress report agenda. The vacancies concerned had a significant impact upon the ability to complete the audit plan and details of audits which had to be deleted were reported to the November 2013 and March 2014 meetings.

The new structure of the Internal Audit & Risk Management section comprises of a general audit team managed by the Audit & Risk Manager with 5 Auditor posts, 1 Assistant Auditor and 1 Trainee Auditor. The Computer Audit team is managed by the Computer Auditor who is supported by an Assistant Computer Auditor. Following the unsuccessful attempt to appoint an Auditor within the general team, the decision was made to advertise for an Assistant Auditor which had a very good response. The successful candidate took up post from 12/05/14 and this last appointment meant that the Section is now fully resourced.

4.3 Scrutiny Reviews

A scrutiny review of was undertaken using the Audit Scotland national report, *"Using Cost Information to Improve Performance: Are You Getting it Right?"* and the *"key points for action"* contained within it. A further Audit Scotland national report, *"Managing performance: are you getting it right?"* was published the following month and the Scrutiny Working Group recognised the overlap between both reports and decided that the review would consider both in order to establish whether further actions are required by the Council. This review has identified a number of areas for improvement and will be reported to the September meeting of the Audit & Scrutiny Committee.

Following completion of this exercise, it was recognised that the scrutiny review process requires improvement. To assist Members in undertaking effective scrutiny, further training was organised by the Corporate Development Section through CIPFA and this took place on 09/05/14.

In addition, the Head of Internal Audit & Risk Management met with the Chair and Vice-Chair of the Audit & Scrutiny Committee to discussion how to progress the work of the Scrutiny Working Group and the following has been agreed:

- Members should be drawn from Council as a whole (providing the membership of the Group reflects the Council's political balance) to ensure that they have the appropriate skills, experience, interest particular to the scrutiny topic concerned.

- At the start of each exercise we need to plan ahead the meetings required to complete the exercise so that the attendance of Members is better and there is greater continuity. We also need to provide within the plan the reporting timescales.
- Information provided at evidence gathering sessions needs to be supported by the relevant evidence. Where necessary, Internal Audit should undertake some subsequent analysis to support the reliability of this evidence. It may be necessary to then call back the Director to discuss that analysis.
- Scrutiny topics need to be risk-based and focussed.

4.4 Fraud and Irregularity Investigations

There were a total of 3 investigations undertaken, including 1 brought forward from the previous year:

- The brought forward investigation has been completed, and related to issues within a Children and Families Team. The individual at the centre of the investigation was dismissed following a disciplinary hearing. A system weaknesses report was later prepared and this was provided to the March 2014 meeting of the Audit & Scrutiny Committee. Recovery of the sum involved is being pursued through the individual's pension fund.
- An investigation into missing money from a School Fund has been undertaken. A report was prepared for management which resulted in an internal disciplinary investigation being instructed and this should be concluded shortly. In addition, a report has been made to the Police who are also investigating the matter.
- The final investigation also centres on a School and relates to concerns about the administration of the School Fund, and the appropriateness of both DSM and School Fund expenditure. Reports have been prepared for management who have instructed that a disciplinary investigation is undertaken.

Once the results of the last 2 investigations are known, including any action by the Police, any identified system weaknesses will be reported to the Audit & Scrutiny Committee.

5. PERFORMANCE DATA

5.1 Performance Data

A performance and quality assurance framework was previously introduced as a requirement of the CIPFA Code of Practice and a comprehensive set of targets to measure performance were implemented with effect from 01/04/12. These have been continued as the new Standards set out the need for a "quality assurance and improvement programme". There are various requirements within this programme which should include internal assessments including on-going monitoring of the performance of the internal audit activity. Table 4 below provides details of these measures and performance against target for the last 2 years. It is intended that this will be expanded upon and trends identified when data for 3 successive years is available.

Table 4

Category	Performance Indicator	Target	2012/13	2013/14	Within Target?
Completion of Audit Plan	Number of audits completed in the year v Number of audits in the Plan, expressed as a %	85%	24%	20%	X
Timeliness of Report	Number of draft reports issued within 15 days of Matters for Discussion meeting, expressed as a %	90%	0%	11%	X
Implementation of Recommendations	Number of recommendations accepted v number of recommendations made, expressed as a %	95%	99%	100%	√
Training & Development	Average number of training and development hours per employee	14 hours	36 hours	81.4 hours	√
Follow up reviews	Number of follow ups undertaken within due date, expressed as a %	95%	88%	33%	X
Sickness Absence	Number of days absence per employee	5 days per annum	2 days p.a.	1.7 days p.a.	√
Cost of Internal Audit	Actual net expenditure v budgeted net expenditure, expressed as a percentage	< 100%	83%	91.4%	√
Cost of Internal Audit	Cost per £m net expenditure	Within lowest quartile of CIPFA benchmarking comparators	Y, 30 th out of 32 authorities	Not yet available	n/a
Compliance with CIPFA Code of Practice/ Standards *1	Number of areas of compliance v best practice checklist, expressed as a %	95%	97%	N/A	√
		95%	N/A	76%	X

*1 From 01/04/13, the CIPFA Code was replaced by the Standards. It is now a requirement of the Standards that compliance is monitored and reported within the Annual Report.

Comments on the performance data:

Whilst there are a number of positive results in Table 4, there are 2 areas where performance was not within target:

Completion of the audit plan

This indicator measures the number of planned audits where the final report was issued by 31st March 2014 and does not take account of the fact that there were a number of planned audits that were still work in progress at the year end, including some where the draft report had been issued (note the Activity report to the Audit & Scrutiny Committee on 27/03/14 showed that 10 draft reports had been issued or were in progress). Other factors which contributed to the reported performance include the following:

- The Section had an unprecedented number of vacant posts and staff changes during the year. This accounts for the training hours being higher than expected and also impacts upon the ability to undertake audits as new staff will take longer to get up to speed with the processes. In addition, when a member of staff leaves the Section, their outstanding work must be taken forward and completed by another member of staff. During the year some staff have been thinly spread and competing demands have meant that some work is not completed as quickly as desired.
- The planned days for fraud investigations and provision of audit certificates have been fully utilised but has meant that the staff vacancies has impacted fully upon the planned audits. However, it was ensured that the audits undertaken were prioritised in order to support the Annual Statement on Internal Control.
- A number of the planned follow-ups have taken longer than expected. The budget for the follow-up reviews is based upon the assumption that the management agreed actions have been implemented and the failure to complete these means that the audit takes longer as time is spent agreeing new actions and writing a more detailed report.

Although the work of all staff is subject to weekly monitoring, it is evident that the Audit & Scrutiny Committee need to be better informed with regard to achievement of the Audit Plan. In this respect the Committee will, in future, receive a quarterly progress report at each meeting.

Follow ups

The delay in undertaking prompt follow-ups has resulted in the change in approach to obtaining the necessary information from the Council's Performance and Risk Management System (PRMS). Previously, once the last target date had been reached, a follow-up document would be issued to Services in order to confirm that the agreed actions had been implemented. This has now changed to obtaining this information from PRMS. However, delays with Services inputting internal audits recommendations and updating the corresponding actions that have been taken, means that this information cannot be followed up timeously.