The Highland Council

Audit & Scrutiny Committee – 16th June 2016

Statement on Internal Control and Annual Report 2015/16

Report by the Audit & Risk Manager

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 Annual Governance 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 2015/16.

1. Statement on Internal Control

1.1 In order to comply with the requirements of the Public Sector Internal Audit 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 2016.

2. Annual Report 2015/16

2.1 Sections 3 to 5 provides the information relating to the annual report; details of the audit report issued during the year, an overview of the Section's activities during the year and performance data for the past two years.

3. Implications

3.1 There are no Resource; Legal; Equalities; Climate Change/Carbon Clever; Risk, Gaelic and Rural implications as a direct result of this report.

Recommendation

The Committee is invited to note the content of the attached report and the audit opinion provided, and to raise any relevant points with the Audit & Risk Manager.

Designation: Audit & Risk Manager

Date: 6th June 2016

Author: Donna Sutherland, Audit & Risk Manager

Background Papers:

The Highland Council

Statement on Internal Control and Annual Report 2015/16

Contents

1. INTRODUCTION

1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1st April 2015 to 31st March 2016, and a report that can be used by the Highland Council to inform its Annual 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 2015/16.

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 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.

The Standards require that there is periodic self-assessment against the Standards and that the Head of Audit & Risk Management includes a statement of conformance within his annual report. This has been undertaken using the CIPFA *"Checklist for Assessing Conformance with the PSIAS and the Local Government Application Note".* Following on from the first assessment, an action plan was prepared to address the areas of partial and non-compliance and progress against the plan was reported to each Committee meeting. The last assessment was reported to Committee on 18/06/15 which showed that the Section had achieved 97% full, 2% partial and 1% non-compliance with the Standards.

One of the main areas of non-compliance relates to the requirement for an external assessment to be undertaken every 5 years or less. This will be

addressed in late 2016 when this assessment will be undertaken by West Dunbartonshire Council's Internal Audit Team.

2.3 Internal Audit work

The 2015/16 audit plan was approved by the Audit & Scrutiny Committee on 26/03/15. All audit reports issued are provided as a standing agenda item to each Committee meeting together with progress against the Plan. Where the Plan has required to be adjusted during the course of the year all amendments have been set out in the progress report and have been approved by Members.

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:
  o Control environment.
  o Identification and evaluation of risk and control objectives.
  o Information and reporting.
  o Control processes.
  o Monitoring and corrective action.
  o Assessment of whether the key controls have been applied during the year.

- Examination of the Council's main financial systems. This comprised of a full audit of the Council's Debtors system whilst the other systems; Payroll, General Ledger, Income, Budgetary Control and Creditors have been subject to a review of the key controls including:

  o Financial procedures and guidance issued to staff;
  o Segregation of duties;
  o User access levels and appropriateness;
  o 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. The audit findings will be addressed in a separate report.

- A review of the Council's corporate governance arrangements to ensure that these are robust and in accordance with best practice.

- Consideration of the Council's arrangements with regard to information management and security, risk management and managing the risk of fraud and corruption.

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 2015/16, a total of 164 audit recommendations were made. Of these, 40 were classified as high grade and further details are provided in Table 1 on pages 4 - 8. A full breakdown of the audit grades and the overall audit opinions can be found at Table 2 on pages 13 - 14. The number of high grades has increased significantly from previous years (19 in 2014/15) but 17 of the high grades come from 3 audit reports which highlighted particular issues with the governance of projects within the Council. These reports were in respect of the project to implement a new debt recovery system, the capital project for the building of the new Ben Wyvis Primary School and governance of Inverness Old Town Arts and

Inverness City Arts Group. All of these reports had the audit opinion of "Limited Assurance". Action plans were agreed to address the areas of concern identified by Internal Audit and these are followed up in the normal manner. Furthermore, to address audit concerns, a new Project Management Governance Policy was introduced and was fully adopted from 1 April 2016. The 2016/17 Internal Audit plan includes audits which will check that the new Governance Policy is complied with and this will include an examination of both ICT and capital projects.

Table 1

Area of Concern – High Grades	Agreed Action Completed/ Update (where not completed)
Scottish Welfare Fund payments (1) SWF application forms which held personal and sensitive data were not held securely on the system, contrary to the Data Protection Act. (2) Reconciliations between the SWF payment system and the financial ledger were not being performed due to a technical issue which meant that the payment analysis and history did not agree for some claimants.	All agreed actions have been completed.
Debt recovery system This report contained 4 high grade actions and was considered in private by the ASC on 18/06/15. As a result, the areas of concern are not detailed.	All agreed actions have been completed.
Investigation into Housing Revenue Account reconciliation process (1) The reconciliation process was not performed correctly as it did not reconcile the fully system information properly. (2) There was a lack of clarity between Services as to their respective roles and responsibilities. (3) As a result of the issues above, the present process is not working efficiently.	All agreed actions have been completed.
Community Payback Orders (1) The hours worked by Offenders has to be accurately recorded and monitored. One Team had a backlog of unrecorded unpaid work records and court disposals. (2) Across the Teams there had been a number of long term sickness absences which had a knock on effect on the administration of Community Payback Orders and the day to day organisation of Teams.	All agreed actions have been completed.

Area of Concern – High Grades	Agreed Action Completed/ Update
Mental Health Officer (MHO) Service (1) Due to increased service demands there was a waiting list of Adults with Incapacity referrals to be allocated to an MHO. At the time of the audit there were 32 cases on the waiting list (all within the Mid & South area) with the oldest dating back to 2012. (2) The CareFirst guidance did not cover all MHO procedures and as a result there were inconsistencies in how information was recorded on the system. Also a number of manual systems were in place that could be done more efficiently using the CareFirst system.	All agreed actions have been completed.
Capital Contracts - Ben Wyvis Primary School (1) Technical references, as required by Contract Standing Orders (CSOs) had not been requested. (2) The appointment of 2 Structural Engineers was not subject to formal tendering. Also the replacement Structural Engineer was provided by an associate of the main contractor. (3) Goods in excess of CSO limits were acquired from the main contractor without formal advertising. (4) There was a lack of communication concerning project roles and responsibilities. Also, there was no Project Execution Plan	An update report on progress in implementing the management agreed actions is provided as a separate agenda item. This shows that all high grade actions have been completed bar (5) below and revised target dates have been agreed as detailed.
(5) Monitoring by the Clerk of Works was insufficient and the level of information provided within reports was poor.	It was agreed that the Clerk of Works role would be reviewed to ensure that suitably qualified staff are allocated to projects and this was to be implemented by 30/11/15. These staff are now moving from D&I to Community Services and the transfer will not be completed until June 2016. Investigations are taking place into new software that will support the electronic reporting of project information and the target date for this action has changed from 31/03/16 to 30/09/16.
(6) The new school building was handed over on the planned date despite extensive snagging issues remaining. (7) The project reporting to Members was poor. Despite this being a requirement of Financial Regulations, no post-contract reviews were undertaken. (8) Again, contrary to financial Regulations, no risk register was maintained. Also project risks were not embedded within the Project Management procedures.	

Area of Concern – High Grades	Agreed Action Completed/ Update
(9) The recommendations from the Lessons Learned report on Lochardil Primary School had not been revisited to ensure that the appropriate actions had been taken and were working effectively.	
(10) The capital monitoring reports did provide the accumulated cost information for a project.	
Review of financial procedures operated in Schools	
(1) 3 of the schools visited did not maintain inventories.	This action has a revised target date of 31/12/16.
(2) A number of issues were identified in the Schools visited with regard to the administration of the School Fund contrary to the requirements of Financial Regulations.	This agreed action has been completed.
Governance of Inverness Old Town Arts and Inverness City Arts Group	
(1) The IOTA Project Manager submitted an invoice for the hours worked on a project for her own hours and the Administrative Assistant. The legitimacy of this questioned as both individuals were sub-contractors and submitted their own invoices. In addition, the Administrative Assistant submitted her own invoice for working on this project. On the basis of the information provided, it is appears that the Project Manager may have overbilled the Council for £4,500.	Records have been located which evidences the audit concern that overbilling occurred. However, this matter is still being pursued with the former Project Manager as is (2) below. Therefore, a revised target date of 30/09/16 has been set to resolve these matters.
(2) The IOTA brand name has continued to be used by the two sub-contractors despite this being the Council's intellectual property.	This matter is still being pursued with the former Project Manager.
(3) There was no formal agreement with the previous owner of the Hotel which meant that this could not be pursued when it was sold to a new owner.	Creative Scotland has agreed to consider a fresh application from the Council for this project. If this is pursued then it was agreed that a formal agreement would be reached with the Hotel owner before any costs were incurred.
Management of Housing Voids	
(1) Some properties had been classified as Performance Indicator Exempt (PIE) over a number of years. This included 4 properties in Caithness which had been surplus to requirements for a number of years but had not been disposed of and other properties which were refurbished but there were delays in recording that they were fit for re-let.	All agreed actions have been completed.
(2) There were significant delays in the issuing of invoices for rechargeable works.	

Area of Concern – High Grades	Agreed Action Completed/ Update
Review of the Council's arrangements for the charging for services It was agreed that a Member/ Officer working group would be established to consider and make recommendations to Committee on the full impact of phasing out free school lets (estimated lost income was £150k). However, this group had not been established but a savings target of £150k from the review of school lets had been set for 2016/17.	This action has a revised target date of 31/12/16.
Income Systems Officers still had access to the AXIS (income system) but their current job roles did not require this. Also, a review of AXIS users should be undertaken annually but this last occurred in 2013.	The agreed action has been completed.
Payroll Procedures A number of payroll forms (new starts, changes and leavers) had been completed by Business Support or Clerical staff rather than the appropriate Manager.	The agreed action has been completed.
Review of Pulteneytown People's Project (PPP) PPP received a significant amount of funding from the Council across 3 different Services. These are subject to different arrangements and the decision by one Service to cut/ reduce funding could impact upon the ability of PPP to provide other grant funded/ contractual services to another Council Service. Therefore it was recommended that consideration be given to the Council producing a single SLA with PPP for all services.	This was investigated but has proved to be impossible as the Employability Services tender is underway, the Housing Services tender process is being prepared and there is uncertainty over Deprived Area Funds in 2017/18.
School off-site excursions (follow-up) (1) Whilst the off-site excursion guidance was revised and all relevant Council and HLH staff were made aware of this, the guidance was not being consistently applied by staff when recording the planning stage of an excursion within the EVOLVE system.	The agreed action has been completed.
(2) It was agreed that the Council's minibus policy and associated guidance would be reviewed and updated by 31/03/15. However, this had not yet been completed.	It was agreed that the policy would be completed and taken to the ECAS Committee in March and the target date for completion was 30/04/16. This date has not been achieved but the Service has reported that considerable work has been undertaken on a new minibus use policy and guidance, with considerable engagement with schools, and the transport unit. This is now concluding and will see the revised minibus policy concluded in summer 2016.

Area of Concern – High Grades	*Agreed Action Completed/ Update*
Purchase Cards There were issues with recording the correct VAT type on transactions within Integra. A large number had been left blank, entered incorrectly or was not in agreement with the supporting documentation.	All agreed actions have been completed.
Community Challenge Fund - Governance Arrangements With regard to the monitoring of projects, it was found that: • One Service Level Agreement (SLA) did not clearly state who would undertake inspections and how performance standards would be verified. • A one-off contribution to a group did not state what the funds could be used for.	It has been agreed that the SLA will be updated and the guidance would be updated to address the various audit findings. This action is not yet due to be completed.
Drummuie Offices - Chimney Rebuild (1) Escalation of the issues should have happened earlier than it did.	This has been agreed and any issues will be discussed and revolved through the weekly Service Business Meeting.
(2) There is a wider need within the Service for clarity and understanding on conservation/ dangerous buildings legislation and regulation.	This has been identified as a training requirement and a course will be developed and rolled out to all responsible staff. This action is not due to be completed until December 2016.

As can be seen in the table above:
- 32 agreed actions have been completed as agreed
- 6 actions have revised target dates
- 2 actions are not yet due to be implemented.

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. This was reported on 17/11/15, and the next report will be provided on 16/06/16. Following a request from Committee for more regular reporting, it is intended that reports will be provided on a six-monthly basis to the June and November Committees.

The action tracking process also allows for revision of the agreed action target dates. All actions were either satisfactorily implemented or revised target dates were agreed. As reported in previous years, there have still been some issues with Services failing to timeously request time extensions. A new Internal Audit Reporting & Escalation Protocol was approved by the Executive Leadership Team and will come into effect from 30/05/16. The protocol is designed to ensure that all audit matters, including action tracking, are dealt with in a timely manner.

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 Annual Governance Statement which forms part of the Council's Annual Accounts.

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 was partially extended for a further 18 months up to 30/09/16. This extension covered all elements of the contract with the exception of network support services relating to Telephony and the Local Area Network (LAN). It also contains an agreed exit provision termination agreement to give the Council contractual cover until 31/03/17 in line with the ICT re-provision requirements.

The Telephony service successfully transferred to the Council on 01/04/15. On 01/03/16, a contract commenced with Capita (SWAN Value Added Service contract) for the LAN service.

Performance of the Fujitsu contract and service delivery is monitored by the ICT Partnership Board and reports are provided every 6 months to the Resources Committee. During 2015/16, Committee reports were presented on 27/05/15 for the period October 2014 to March 2015 and on 25/11/15 for the period April to September 2015.

The Council's contract with its other main ICT supplier, Vodafone, for managed data network services to Schools, Libraries and Council administration locations ended on 31/03/16. During March, the Wide Area Network (WAN) provision was transitioned from Vodafone to a new Capita Scottish Wide Area Network (SWAN) contract on a site by site basis. As at 31/03/16, two primary sites were connected to SWAN; Council Headquarters and an office in the Beechwood business park in Inverness. The first edge site transferred in the following month and transition will continue up to March 2017 for the remaining sites.

A new financial management information web-based system, Integra, supplied by Capita Integrated Business Solutions (Capita IBS) went live on 01/04/15.

The Council is authorised to use the Cabinet Office's Public Sector Network (PSN) for secure email communications between it and its government partners and applications such as DWP and Blue Badge. The Council has been re-accredited and this will cover the period 30/04/15 to 09/05/17.

The organisational structure in Active Directory does not accurately reflect the current structure of the Council. Active Directory (AD) is a database that keeps track of all the user accounts and passwords in the organisation and allows it to store user accounts and passwords in one protected location, improving security. It is used to allocate different access levels to different types of users who are accessing a network.

Consideration was given to making structural changes in AD during 2015/16 but this has not progressed primarily for two reasons:

- The Council structure has not yet reached a settled state so any changes made now would only be an interim position;

- An early project within the scope of the new ICT contract will provide for a re-structure and upgrade of AD.

Therefore any work carried out prior to the contract would not be good value for money. The implementation of AD is anticipated in April 2017 and will consider the requirements of Highlife Highland and Valuation Joint Board.

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. A new Project Management Governance Policy was approved by the Resources Committee on 25/11/15. One element of this policy was to provide Members with regular updates on the status of projects and the first report was provided to the Resources Committee on 24/02/16.

The Council has an approved Information Security Management System in place as required by ISO 27001. The Council's Information Management Strategy which covers the period 2013-2017 and this was last reviewed on 25/02/15. The Information Management Governance Board (IMGB) oversees and governs the delivery of the Strategy which is supported by a range of policies that make up the Information Management Policy Framework. The Framework includes the following policies: Information Management, Records Management, Records Retention & Disposal, Information Security and Data Protection which should be reviewed annually to ensure that these remain fit for purpose. In accordance with the Public Records (Scotland) Act 2011, the Council and the Highland Licencing Board submitted a Records Management Plan to the Keeper of the Records of Scotland which, following an assessment process, was approved on 31/03/16.

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 IMGB reviews high level information security risks referred from the ICT Security Group and other information security risks that relate to non-ICT issues.

The following third party assurances have been received:

- Fujitsu has ISO 27001 information security management certification for their Data Centre in Stevenage and their back up site in London until 04/12/18.

- For the SWAN contract Capita Business Services has ISO27001:2013 information security management certification for the period 26/01/15 to 26/01/18. Their Direct Network Service Provider (DNSP), Updata Infrastructure UK Ltd, has been assured as compliant with requirements to connect to the PSN as a DNSP. The Capita Updata connectivity and network framework has been assessed under CESG Assured Service and approved against Telecommunications from 23/03/15 to 22/03/18.

- In respect of Integra, Capita IBS has accreditations including ISO 9001:2008 – Quality Management System certification to 31/10/18 and ISO 27001:2013 – Information Security Management Systems Requirement certification to 15/06/18. The hosted system is managed in a UK data centre by Ark Data Centres Limited. Ark has certifications including ISO 27001:2013 – Information Security Management Systems Requirement for the provision of a distributed data centre environment valid from 28/07/13 to 27/07/16; ISO 9001:2008 – Quality Management System certification from 17/05/13 to 16/05/16 and certification for operating a Business Continuity Management System complying to the requirements of ISO22301:2012 from 18/05/13 to 17/05/16. To ensure the safety of the Council's network and comply with PSN requirements, penetration (PEN) testing was carried out in April 2016 and a report of findings followed in May 2016. This has highlighted a number of areas for improvement which have been classified in terms of the timescale in which these should be addressed as 1 critical, 10 high, 9 medium and 10 low. These are to be discussed with the contractor in order to agree the necessary actions required.

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.

The Depute 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.

The 2015/16 Code was approved by the Highland Council on 03/09/15 and was presented to the ASC for further scrutiny on 30/09/15.

The Council's corporate governance arrangements are subject to annual review by Internal Audit and the work undertaken in respect of the 2015/16 Local Code has not identified any control weaknesses in the Council's governance arrangements.

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 Corporate Risk Register is reviewed on a six-monthly basis and the results of these reviews were reported to the Audit & Scrutiny Committee on 18/06/15 and 24/03/16.

2.10 Managing the risk of fraud and corruption

CIPFA published the Code of Practice on managing the risk of fraud and corruption in 2014. The Code contains five key principles which are aimed at embedding effective standards for countering fraud and corruption in organisations in order to support good governance. These principles are to:

- Acknowledge the responsibility of the governing body for countering fraud and corruption

- Identify the fraud and corruption risks
- Develop an appropriate counter fraud and corruption strategy
- Provide resources to implement the strategy
- Take action in response to fraud and corruption.

A number of these standards are already in place such as the expected Human Resources and Information and Communication Technology policies, the Council's Anti-fraud and Anti-corruption policy. A review of compliance with the Code of Practice will be undertaken during 2016/17 and an action plan will be produced to address any improvements that can be made to further strengthen the Council's approach to managing the risk of fraud and corruption.

2.11 Integrated Care Arrangements

Integrated services for adult and children have been in place since 01/04/12. The arrangements were set out in a partnership agreement using the Lead Agency model where the Council and NHS Highland (NHSH) are jointly accountable for determining outcomes and the resources to be committed. The Council is the Lead Agency for children and NHSH for adults, and they are each responsible for all aspects of business delivery, strategy, internal governance, operational delivery or commission of services and fully accountable for the delivery of the agreed outcomes.

The Public Bodies (Joint Working) (Scotland) Bill 2014 came into effect on 01/04/15 and this required the development of an Integration Scheme. The Highland Partnership Integration Scheme was approved by the Scottish Government and is in place. Whilst this replaces the partnership agreement, the agreement is still used as detailed guidance.

During 2015/16, a review of the governance arrangements was undertaken and areas for improvement were identified. To address these, the Highland Partnership recommended a set of good governance principles namely:

- Each Lead Agency has a governance structure that reflects single governance, single budget and single management
- Each Lead Agency adopts a Strategic Commissioning approach to working with partners across the Public, Independent and third sectors to develop the Strategic Plan
- The Partnership is agreed on the functions of scrutiny and governance and where these responsibilities are discharged
- The Partnership has a Strategic Plan which is shared and equally owned
- The commissioning agency monitors the impact on outcomes.

The outcome of this review was reported to the Highland Council on 12/05/16 and the revised governance arrangements were agreed. The same report will also be presented to NHSH for agreement and it is intended that these will be implemented from April 2016.

2.12 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 2016.

3.   INTERNAL AUDIT GRADINGS AND OPINIONS

3.1   During the year, a total of 37 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 5 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 2 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 2

Report Name	Report Date	Audit Opinion	No. of Recommendations	High	Medium	Low
Scottish Welfare Fund payments	16/04/15	Reasonable	4	2	2	0
Debt Recovery System – Project Governance	12/05/15	Limited	7	4	3	0
Investigation into Housing Revenue Account reconciliation process	09/06/15	No	4	3	1	0
Community Payback Orders	10/06/15	Reasonable	8	2	3	3
Mental Health Officer Service	10/06/15	Limited	5	2	1	2
Non Domestic Rates - Billing and Collection	24/06/15	Substantial	4	0	4	0
General Ledger	13/07/15	Substantial	5	0	3	2
Verification of Performance Indicators 2013/14	18/08/15	Substantial	2	0	1	1
Records Management at Care and Learning Store, Nairn	20/08/15	Substantial	5	0	5	0
School Lets Arrangements	02/09/15	Limited	4	0	3	1
Council Tax - Billing and Collection	08/09/15	Substantial	1	0	1	0

Report Name	Report Date	Audit Opinion	No. of Recommendations	High	Medium	Low
Capital Contracts - Ben Wyvis Primary School	16/09/15	Limited	17	10	7	0
Review of financial procedures operated in Schools	16/09/15	Reasonable	5	2	3	0
Treasury Management	16/09/15	Substantial	2	0	1	1
Governance of Inverness Old Town Arts and Inverness City Arts Group	17/09/15	Limited	8	3	4	1
Housing Benefit Payments and Council Tax Reduction Scheme	18/09/15	Substantial	2	0	1	1
Matters Arising from the Highland Council's Statement of Internal Control 2014/15	21/09/15	Substantial	3	0	2	1
SEEMiS Integrated School Management System	21/09/15	Reasonable	5	0	5	0
Asset Management	22/09/15	Limited	5	0	5	0
Review of corporate control of overtime	22/09/15	Substantial	4	0	3	1
Online Payments review	22/09/15	Reasonable	5	0	5	0
Management of Housing Voids	22/09/15	Limited	3	2	1	0
Review of the Council's arrangements for the charging for services	05/11/15	Reasonable	4	1	2	1
Income Systems	05/11/15	Substantial	3	1	1	1
Payroll Procedures	06/11/15	Reasonable	4	1	2	1
Review of Pulteneytown People's Project	06/11/15	Substantial	5	1	3	1
LEADER Programme 2014/15	16/11/15	Substantial	2	0	2	0
EFF programme 2014/15	25/11/15	Full	0	0	0	0
School off-site excursions (follow-up)	08/12/15	Limited	3	2	0	1
Procurement - Review of Taxi and Private Hire Vehicle inspections contract	22/12/15	Substantial	2	0	2	0
Family Teams - Management of Staffing Establishment	06/01/16	Substantial	2	0	2	0
Data Protection	14/01/16	Reasonable	6	0	6	0
Purchase Cards	28/01/16	Reasonable	7	1	5	1
Corporate Property Asset Management System	09/03/16	Substantial	6	0	3	3
Community Challenge Fund - Governance Arrangements	04/03/16	Reasonable	4	1	3	0
Drummuie Offices - Chimney Rebuild	09/03/16	Not Applicable	3	2	1	0
Information Security in Schools	14/03/16	Reasonable	5	0	5	0
Totals			**164**	**40**	**101**	**23**

4. OVERVIEW OF 2015/16

4.1 2015/16 Tactical Plan

The 2015/16 tactical plan was approved by the Audit & Scrutiny (A&S) Committee on 26/03/15. 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 2015/16 tactical plan.

4.2 Staffing Issues

The structure at the beginning of the year consisted of a general audit team managed by the Audit & Risk Manager with 4 Auditors, 3 Assistant Auditors (1 full-time and 2 part-time) and 1 Trainee Auditor. The computer audit team was managed by the IT Auditor who was supported by an Assistant IT Auditor.

The Corporate Fraud team was established on 01/08/15 under the management of the Audit & Risk Manager. 1 of the Auditors transferred to this team together with a Senior Investigator and Investigator who were previously part of the Benefits Investigation team. On 11/12/15, the Auditor left for a promoted post with an NHS Trust and this post has since remained vacant as part of the Service's financial savings. Details of the work undertaken by the Corporate Fraud Team are detailed at section 4.4 below.

Sickness absence within the Section was unusually high during the year with a total of 207 working days lost. This was predominately due to the long-term absence of an Auditor, following a road traffic accident, during the period July 2015 to February 2016. Furthermore, there were several instances of short-term absences and 2 members of staff required hospital treatment.

Further staff changes will occur as a result of the Council's Voluntary Redundancy (VR) Scheme which resulted in a part-time Assistant Auditor leaving on 31/03/16 and the IT Auditor and Head of Audit & Risk Management leaving on 30/04/16.

4.3 Scrutiny Reviews

The Scrutiny Working Group undertook a review of the Council's arrangements for attendance management. The final report issued on 14/09/15 and was reported to the ASC on 30/09/15. This review identified a number of areas for improvement in relation to:

- The attendance management policy and guidance;
- Return to work interviews;
- Management of short and long term absences;
- Monitoring and reporting of sickness absence;
- Occupational Health arrangements.

An action plan was agreed with management to address the improvements required. A follow-up review will be undertaken by the Group during 2016/17.

4.4 Corporate Fraud Work

The remit of the new Corporate Fraud Team is the prevention, detection and investigation of all types of fraud within the Council. The Team also acts as the Single Point of Contact (SPOC) as part of the liaison arrangements with the Department of Work and Pensions.

From 01/08/15 – 31/03/16, a total of 59 referrals were made to the team. The types of fraud and the outcomes are detailed in Table 3 below.

Table 3

Fraud Type	No referrals	Results/ Current Status
Council Tax Reduction (CTR)	33	4 cases proven with £526 CT discount and £435 CTR. 20 have been closed. 9 are still in progress.
Tenancy Fraud	20	7 properties recovered to date with CTR of £894. 5 properties where no fraud was established. 7 investigations are still on-going including those where awaiting recovery of the property.
CTR/ Tenancy Fraud	3	1 case proven with £402 CTR. 2 have been closed.
Non-Domestic Rates	1	Investigation still on-going.
Employee Fraud	1	Investigation completed. Employee was interviewed under caution and a report has been sent to the Procurator Fiscal.
Blue Badge	1	Badge was issued by the Highland Council but the misuse occurred in an English Council area. Details have been provided to that Council to assist their case.
Total	**59**	

Addressing tenancy fraud has been one of the Team's main priorities for the year and this has been undertaken in close conjunction with Housing officers across the Council's areas. During the year, a total of 5 (2 in Ross-shire and 3 in Caithness) properties were recovered, 3 were pending (1 each in Caithness, Ross-shire and Lochaber) and another 8 (2 in Caithness, 2 in Ross-shire, 1 in Sutherland and 3 in the Inverness area) were being investigated. The updated position with regard to the referrals is shown in Table 3 above which shows that a further 2 properties have since been recovered. Audit Scotland previously reported that the cost of tenancy fraud was in the region of £18,000 p.a. per property, based upon the cost of housing a family in temporary accommodation for a year. Therefore, the sum involved for the 5 properties recovered would be £90,000 p.a.

5.   PERFORMANCE DATA

5.1   Performance Data

In accordance with the Standards (PSIAS) a new Quality Assurance Improvement Programme (QAIP), which gives assurance over, and measures the Internal Audit activity, was introduced. This contains a set of performance indicators which are reported to Committee on a quarterly basis. The information for the full year is set out in Table 4 below.

Table 4

Category	Performance Indicator	Target	2014/15	2015/16	Within Target?
Financial					
Cost of Internal Audit	Actual net expenditure v budgeted net expenditure, expressed as a percentage	<100%	97%	93%	√
	Cost per £m net expenditure	Within lowest quartile (8th or less) of CIPFA benchmarking comparators	Y, 5th (7th the previous year)	Not yet available	N/A
Quality					
Client Feedback	Percentage of satisfaction from individual audit engagements expressed through Client Audit Questionnaire	90%	92%	85%	×
	Percentage of Client Audit Questionnaires returned	70%	70%	84%	√
Compliance with CIPFA PSIAS	Percentage of areas of full compliance against the PSIAS	95%	97%	97%	√
Business Processes					
Implementation of Recommendations	Percentage of recommendations accepted v number of recommendations made	95%	99%	99%	√
Timeliness of Draft Report	Percentage of draft reports issued within 15 days of Matters for Discussion meeting	90%	14%	25%	×
Timeliness of Final Report	Percentage of draft reports responded to by client within 20 days of issue	85%	44%	68%	×
	Percentage of final reports issued within 10 days of receipt of management response	90%	87%	92%	√
Completion of Audit Plan	Percentage of audits completed in the year against audits in the Plan	85%	48%	56%	×
Follow up reviews	Percentage of follow ups undertaken within due date	95%	50%	61%	×

Category	Performance Indicator	Target	2014/15	2015/16	Within Target?
Staffing					
Training & Development	Average number of training and development hours per employee	2 days or more	24 days	15 days	√
Sickness Absence	Number of days absence per employee	Less than 5 days per annum	2.6 days	17 days	×

Comments on the performance data which is not within target:

Client Feedback

The questionnaire that is issued to the client officer was updated in quarter 2 and this initially saw a dip in the response rate during quarters 2 (80%) and 3 (83%). This has risen to 98% for quarter 4 so the quarterly trend has shown a continuing improvement.

Timeliness of draft report

Although there has been an improvement in performance, the completion of draft reports within the target timescale is still significantly below the target. One reason is the number of audits that each auditor is involved with at one time, each with varying priorities. There have also been problems during the year with obtaining responses to audit queries which has then affected the workload of staff, leading to bottlenecks at times. These factors have impacted upon work being completed within the original planned timescale.

Timeliness of final report

Problems in obtaining a timely response to draft reports had been an issue in the earlier part of the year. Although a number of responses have not been received within the 20 days target, when a reminder has been issued, a prompt response has been received.

In order to improve performance with regard to the timeliness of the draft and final reports, a new Internal Audit reporting and escalation protocol was agreed with the Executive Leadership Team and came into effect from 30/05/16.

Completion of the audit plan

This has been affected by the unexpectedly high levels of sickness absence (see section 4.2) and the fact that an Auditor's post was held vacant from mid-December onwards. As a result, a number of audits had to be deleted from the audit plan and details of these were provided to the Audit & Scrutiny Committee.

Also, this indicator 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.

<u>Follow ups</u>

Whilst there has been an improvement in the timely follow-up of audit recommendations, this is still short of the target. This was due to the fact that the Assistant Auditor who previously undertook the action tracking process left on 31/03/16. A total of 7 audits were due to be followed up after 01/04/16 and these fell short of the target by 1 day. If these had been undertaken within the target then the percentage would have increased to 91%. This has now been allocated to another member of staff who has been tasked with ensuring that all follow-ups are undertaken timeously.