

Internal Audit Service

2017/18 Opinion on the Framework of Governance, Risk Management and Control

May 2018



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Executive Summary

Overall, Internal Audit work performed in the financial year 2017/18 found that internal control systems in the areas audited were effective.

The majority of audited areas were awarded an audit opinion of 'significant assurance'. No 'critical priority' recommendations were made by Internal Audit during the year, and no 'no assurance' audit opinions have been issued or are pending. This demonstrates that overall, a sound approach to governance and control is in place throughout the organisation in the areas audited.

As reported to Audit Committee, a number of areas of good practice were identified throughout the year. In other areas, improvement plans already in place by management, together with Internal Audit's recommendations, will continue to strengthen the organisation's framework of internal control.

The opinion of the Chief Internal Auditor is therefore that, at the time of preparing this report, the organisation's internal control systems in the areas audited are **satisfactory**. This is a positive assessment of the Authority's control environment and reflects favourably on the organisation's governance arrangements.

As the risk environment within which local government operates continues to change, we will incorporate emerging risk areas within our future audit coverage. This will help to ensure that the annual opinion considers all material issues likely to affect the Chief Internal Auditor's judgement on governance, risk management and control.

1 Purpose of Report

- 1.1 This report has been written to provide an annual Internal Audit opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

2 Governance, Risk Management and Control

- 2.1 Management's responsibility for the effectiveness of the internal control system is clearly set out in the Authority's Financial Regulations. The Regulations state¹:

- It is the responsibility of the Chief Finance Officer to assist the Authority to put in place an appropriate control environment and effective internal controls which provide reasonable assurance of effective and efficient operations, financial stewardship, probity and compliance with laws and regulations.
- It is the responsibility of Chief Officers to:
 - Manage processes to check that established controls are being adhered to and to evaluate their effectiveness, in order to be confident in the proper use of resources, achievement of objectives and management of risks.
 - Review existing controls in the light of changes affecting the Authority and to establish and implement new ones in line with guidance from the Chief Finance Officer and Internal Audit. Chief Officers should also be responsible for removing controls that are unnecessary or not cost or risk effective – for example, because of duplication.
 - Ensure staff have a clear understanding of the consequences of lack of control.

- 2.2 Appropriate controls will depend, amongst other factors, on:

- The nature, size and volume of transactions;
- The degree of control which management is able to exercise personally;
- The geographical distribution of the enterprise; and
- The cost of operation of the controls against the benefits expected from them.

¹ Financial Regulations, Version 5a (September 2013), Regulations C.20-C.23

2.3 There are eight main types of internal control, namely:

Preventative Controls

- (i) Segregation of duties (no one person should be responsible for processing and recording a complete transaction)
- (ii) Authorisation and approval (all financial transactions should require authorisation by an appropriate responsible official; the limits of authorisation should be specified)
- (iii) Physical (custody of / access to tangible assets should be secure and limited to authorised personnel)

Detective Controls

- (iv) Arithmetic & Accounting (controls within the recording function to check that transactions have been authorised, are included, are correctly recorded and are accurately processed)

Directive Controls

- (v) Organisation (responsibilities should be defined and allocated; reporting lines should be identified; delegation of authority should be clearly specified)
- (vi) Supervision (all actions by all levels of staff should be supervised; the responsibility for this supervision should be clearly laid down and communicated to the person being supervised)
- (vii) Personnel (procedures should exist to ensure that staff are competent to carry out the jobs assigned to them, including proper recruitment and performance management procedures, career prospects, training and pay policies)
- (viii) Management (controls exercised by management outside the day to day routine of the system, including supervision).

2.4 When auditing, Internal Audit assist management by testing to see whether the controls established for any given system are appropriate. It is important to stress that Internal Audit, while part of the Authority's overall assurance framework, is not a substitute for effective internal control within the Authority's systems.

3 Opinion on the Adequacy and Effectiveness of the Framework of Governance, Risk Management and Control

- 3.1 The Chief Internal Auditor is required under the Public Sector Internal Audit Standards (PSIAS), introduced in 2013 and revised March 2016 and March 2017, to provide an annual opinion, based on an objective assessment of the organisation's framework of governance, risk management and control. For the purpose of meeting this requirement, the Chief Internal Auditor provides one of two opinions:
- (a) That the organisation's framework of governance, risk management and control is **satisfactory** (i.e. that satisfactory assurance can be obtained from governance systems and procedures in place); or
 - (b) That the organisation's framework of governance, risk management and control is **not satisfactory** (i.e. that there is insufficient control in evidence within the organisation's governance systems to provide satisfactory assurance).
- 3.2 The opinion of the Chief Internal Auditor is that, at the time of preparing this report, the organisation's internal systems of governance, risk management and control were **satisfactory** overall during 2017/18. The Chief Internal Auditor has not needed to place reliance on the work of other bodies in forming her view, and there are no limitations in the scope of this opinion. There are no qualifications to this opinion.
- 3.3 This judgement is informed by the outcomes of Internal Audit work during 2017/18, which are reported to the Audit Committee in regular updates of key outcomes. These have demonstrated that the majority of audit opinions for work undertaken in this period have been 'full assurance' or 'significant assurance', with a small number of 'limited assurance', and no 'no assurance' opinions. A full list of audits performed and opinions issued is included at **Annex A**.
- 3.4 A number of areas of good practice were identified throughout Internal Audit's work during the year. In addition, evidence checking and follow up performed by Internal Audit has demonstrated effective management action in implementing Internal Audit's recommendations.
- 3.5 It is recommended that Internal Audit's satisfactory opinion on the framework of governance, risk management and control is considered as a source of assurance for the preparation of the Annual Governance Statement for 2017/18, and its subsequent approval by the Audit Committee.
- 3.6 This is a positive opinion, which means that the organisation has suitable internal control systems. This opinion is based solely on the areas reviewed, and the progress made by the organisation to action Internal Audit recommendations.

- 3.7 This opinion on the framework of governance, risk management and control has been prepared in accordance with the Public Sector Internal Audit Standards and the accompanying Local Government Application Note issued by the Chartered Institute of Public Finance and Accountancy as the 'relevant Internal Audit standard setter'.
- 3.8 Assurance can never be absolute, and neither can Internal Audit work be designed to identify all weaknesses that might exist. In accordance with its role, Internal Audit has agreed recommendations with management aimed at further strengthening the control environment in operation within the organisation.

4 Audit Resourcing During 2017/18

- 4.1 The Regulations governing the operation of Internal Audit are the Public Sector Internal Audit Standards (PSIAS) 2017. In terms of resourcing, the PSIAS state that Internal Audit must be "appropriately positioned and adequately resourced". The PSIAS goes on to state that the Chief Internal Auditor must ensure that internal audit resources are appropriate, sufficient and effectively deployed to achieve the approved plan. Where the Chief Internal Auditor believes that the level of agreed resources will impact adversely on the provision of the annual internal audit opinion, the consequences must be brought to the attention of the board (in North Tyneside, the Audit Committee).
- 4.2 In 2017/18, as previously reported to Audit Committee in November 2017, Internal Audit's resourcing has been lower than planned, due to a number of factors. Against planned productive days of 854, 497 (58%) was achieved. The reasons for this in-year reduction in resourcing include:
- Delays encountered in appointing to vacant posts, following the 2016/17 reorganisation of the Internal Audit establishment, designed to ensure that there is an appropriate mix of knowledge, skills and other competencies needed to satisfy the authority's assurance needs going forward (198 days)
 - Deployment of an internal audit resource on a one-off item of non-audit work (187 days)
 - (28 day balance reflects 23 days of overachievement on expected productivity and a (net) 5 days of resource obtained from Northumberland County Council).
- 4.3 During 2017/18, 47 assignments were programmed. By April 2018, 31 assignments (66%) were complete, with a further 6 (13%) underway. The remaining 10 assignments (21%) have been risk assessed as part of Internal Audit's continuing rolling programme. 4 assignments have been reprogrammed and included in the 2018/19 Strategic Audit Plan. In respect of the remaining 6 assignments, Internal Audit's planned coverage has been changed following assurance mapping, to provide support to other assurance sources.
- 4.4 This means that the Chief Internal Auditor's opinion is based on a different assurance coverage than that originally planned. The issue of resourcing is

an important one for the organisation to be aware of and to monitor and manage going forward. The reasons for the downturn in resourcing during 2017/18 relate to a number of exceptional factors occurring concurrently. Recruitment to vacant posts created within the team is now complete which will be better able to provide the level and quality of assurance required during 2018/19 onwards.

5 Audit Work Performed During 2017/18

- 5.1 Internal Audit has provided an audit, advice, and financial consultancy / programme assurance service to the Authority in 2017/18.
- 5.2 The audit reports and briefing notes issued during 2017/18, and those related to this period which are currently being finalised with our audit clients, are set out at **Annex A**.
- 5.3 A framework of opinion classifications is used in Internal Audit reporting. The framework applies an overall assurance judgement to each system audited, as defined below.

Full Assurance	The system of internal control is designed to meet the organisation's objectives and controls are consistently applied in all the areas reviewed.
Significant Assurance	There is a generally sound system of control designed to meet the organisation's objectives. However, some weakness in the design or inconsistent application of controls put the achievement of particular objectives at risk in some of the areas reviewed.
Limited Assurance	Weaknesses in the design of, or regular non-compliance with, key controls put the achievement of the organisation's objectives at risk in some or all of the areas reviewed.
No Assurance	Significant weaknesses in the design of, or consistent non-compliance with, key controls could result (or have resulted) in failure to achieve the organisation's objectives in the areas reviewed.

Note: With effect from April 2017, use of an additional 'Moderate Assurance' opinion classification was discontinued.

- 5.4 In addition to the overall opinion given on every internal audit, individual recommendations within each report are classified as critical, high, medium or low priority. This prioritisation is designed to assist management in assessing the importance of each recommendation. The definitions of these priority classifications are set out below:

Priority	Description
1* Critical / Catastrophic	Action that is considered critical to ensure the organisation is not exposed to unacceptable risks.
1 High / Fundamental	Action that is considered urgent to ensure that the service area / establishment is not exposed to high risks.
2 Medium / Significant	Action that is considered necessary to avoid exposure to considerable risks.
3 Low / Less Significant	Action that is considered desirable or best practice and would result in enhanced control or better value for money.

- 5.5 The proportion of Internal Audit recommendations in the period April 2017 – March 2018 classified against each priority is as follows (data from the previous five years is also shown for comparison):

	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18
Critical Priority	Nil	Nil	Nil	Nil	Nil	Nil
High Priority	17 (4%)	7 (3%)	7 (3%)	Nil	3 (2%)	2 (1%)
Medium Priority	108 (25%)	71 (27%)	101 (37%)	131 (41%)	56 (36%)	51 (38%)
Low Priority	311 (71%)	184 (70%)	163 (60%)	187 (59%)	98 (62%)	82 (61%)
TOTAL	436 (100%)	262 (100%)	271 (100%)	318 (100%)	157 (100%)	135 (100%)

Note: Percentages contain roundings

- 5.6 Prioritisation of Internal Audit recommendations is controlled through Internal Audit's quality control and file review processes. This is in accordance with the requirements of Public Sector Internal Audit Standards, which requires that a Quality Assurance and Improvement Programme is in place for Internal Audit's work.
- 5.7 In addition to performing internal audits of existing systems within the Authority and responding to queries on the operation of such systems, during 2017/18 Internal Audit has had a significant and increasing role in advising on new systems within the Authority. A full list of the programme assurance and project boards supported by Internal Audit is shown at Annex A. Whilst the time spent on such assurance work reduces the number of available audit days, it is considered an efficient use of Internal Audit's resource, in that assurance is obtained that effective controls are incorporated into new major systems from the outset. In turn, this minimises the risk of weaknesses in systems and strengthens the control environment. This activity comprises

'consulting activity' under the Public Sector Internal Audit Standards, and is managed by the Chief Internal Auditor in the way prescribed by the Standards.

- 5.8 As in previous years, Internal Audit has undertaken the necessary assurance work and certified the Authority's compliance with the Public Services Network (PSN) Code of Connection requirements.

Audit Highlights 2017/18

- 5.9 This section of the report is designed to draw attention to significant audits and findings from Internal Audit in the 2017/18 year. It should be read in context of the overall positive 'satisfactory' audit opinion described above.
- 5.10 A number of audits attained a 'significant assurance' audit opinion. It is of comfort to the Authority that the majority of the organisation's fundamental financial systems, and high value / high volume transactional systems, were amongst those in this category. Business Rates and Housing Benefit and Council Tax Support both received a 'significant assurance' opinion. Whilst currently being finalised with clients, Creditor Payments, Council Tax and Payroll have all received an indicative 'significant assurance' opinion, and Rent Assessment and Collection a 'full assurance' opinion. This provides assurance to the Authority that these key systems bear appropriate levels of control.
- 5.11 In terms of the areas where a 'limited assurance' opinion was determined, Internal Audit would draw attention to the audits of Information Governance and School ICT Thematic Reviews. The focus of the audit of Information Governance was to review progress following the previous Information Governance audit report (issued February 2016) against an action plan in order to provide an up to date assessment of compliance. Additionally, the audit included a review of arrangements in place to prepare for the European Union's General Data Protection Regulation (EU GDPR) that comes into effect from 25 May 2018.
- 5.12 Whilst good progress had been made towards the implementation of a number of recommendations, further work was required to fully implement the action plan and mitigate all risks faced by the Authority. In respect of the Authority's preparedness for the implementation of the EU GDPR, the audit made five medium priority recommendations, but found that overall the Authority had good arrangements in place to prepare for the regulation's implementation.
- 5.13 The thematic ICT audit undertaken within schools involved a review of key ICT themes in a sample of the Borough's schools and identified a number of areas where controls could be strengthened to enhance the ICT control environment within schools. The sample of schools visited incorporated a mix of Primary, Middle and High schools, in addition to a mix of ICT Support providers and themes reviewed were:

- Malware Controls (controls over malicious software, including virus protection);
- Mobile Device Management (managing iPads, tablets, laptops);
- Network Security (passwords, access permissions);
- Data Security (encryption, data access permissions); and
- Disaster Recovery and Business Continuity Planning (backing up and restoring systems and data).

5.14 All schools visited as part of the sample have received individual feedback on all issues identified within that school. To help ensure that the findings within the thematic report were effectively communicated to all schools in the Borough, Internal Audit attended a Headteachers' briefing in January 2018 to explain findings and associated risks identified and to discuss how schools can best be supported to strengthen ICT controls in place.

6 Schools' Financial Value Standard

- 6.1 Time was included in the audit plan for 2017/18 to support and co-ordinate the work required by the Schools Financial Value Standard (SFVS) on behalf of the Authority.
- 6.2 The SFVS has been designed in conjunction with schools to assist them in managing their finances and to give assurance that they have secure financial management in place. Governing bodies have formal responsibility for the financial management of their schools, and so the standard is primarily aimed at governors; however the Authority's Chief Finance Officer is responsible for ensuring that submissions made by schools are in line with the judgements on these schools which have already been reached by Internal Audit.
- 6.3 On behalf of the Chief Finance Officer (Section 151 Officer), Internal Audit co-ordinated, received and reviewed Schools' Financial Value Standard submissions, for all of the Authority's grant-maintained schools. To reflect changes in resourcing within the Internal Audit team, in future years we will revise our approach to this strand of our work.

7 Special Investigations, Counter Fraud and the National Fraud Initiative (NFI)

- 7.1 In common with previous years, Internal Audit has performed 23 special investigations and management requests during 2017/18. These relate to issues which could not be foreseen in advance. As such, it is important that the organisation can call upon Internal Audit resource to respond quickly to assess the control and governance issues indicated and to secure evidence if required. Internal Audit's work in this area has included:
- potential cash discrepancies;
 - appropriateness of ICT access; and
 - interrogation of ICT systems and email records.
- 7.2 Where irregularities were confirmed, swift action was taken by management (supported by Internal Audit) to cease the possibility of ongoing impropriety.

Causes were then investigated and this, as is typically the case in this area of work, tended to highlight the need for enhanced directive control (see paragraph 2.3), in particular management and supervisory controls.

- 7.3 During 2015/16, dedicated counter fraud resource was appointed within the Internal Audit team. A thorough review of the Authority's operations has been undertaken, from a counter fraud perspective, and developed a 'counter fraud blueprint' highlighting the areas of North Tyneside's operations where the risks of fraud are likely to be most prevalent. These risk areas were ranked, and work prioritised on reviewing Council Tax Single Person Discount and Council Tax Exemption entitlements to help ensure that discounts continue to be received by those entitled to them, whilst identifying and recovering discounts which have not been claimed appropriately. As reported to Audit Committee in March 2018, counter fraud work undertaken realised £0.688m in directly cashable savings and £1.181m in indirectly cashable savings in the period to 30 September 2017.
- 7.4 North Tyneside Council is part of the Cabinet Office's National Fraud Initiative and is thus legally obliged to provide relevant information under the requirements of the Audit Commission Act 1998. (NB. following the closure of the Audit Commission the powers to conduct the National Fraud Initiative passed to the Cabinet Office on 1 April 2015). Before this information can be provided, the Authority is required to ensure that appropriate steps have been taken to notify data subjects held in the organisation's relevant information systems that data may be used for the prevention and detection of fraud.
- 7.5 As in previous years, Internal Audit have acted as the lead within the Authority for the NFI. In addition to finalising work on the 2016/17 NFI exercise, data from the Authority's systems was extracted and submitted to the Cabinet Office in preparation for the 2017/18 exercise, focussing on data held in Council Tax and Electoral Registration systems. Details of data matches were received from the Cabinet Office late 2017 and work is underway on investigating potential matches.

8 Data Quality

- 8.1 During 2017/18, Internal Audit has performed an assessment of data quality issues as part of every audit undertaken. This has involved an assessment against the 6 characteristics / dimensions of data quality identified by the Audit Commission, which organisations can use to assess data quality and to manage its improvement. These are:
- (a) **Accuracy:** data should be accurate for its intended purpose and the need for accuracy balanced against the importance of the data attribute, in terms of its use and the cost or effort of collection.
 - (b) **Completeness:** data should be complete – should not contain invalid records or missing data.
 - (c) **Relevance:** data captured should be relevant to the purpose for which it is used.
 - (d) **Reliability:** data used should reflect stable and consistent data collection processes.

- (e) **Timeliness:** data collection should be captured as quickly as possible after the event.
- (f) **Validity:** data should be recorded in compliance with relevant rules and definitions.

8.2 The general trend from this work is that awareness of the importance of data quality is high within the organisation. The Authority recognises that there will be a need to continue this careful management moving forward. Where individual audits have identified scope for improvement in one of the characteristics shown, these have been highlighted to management as part of Internal Audit reporting.

9 Clients' Views

9.1 For several years, Internal Audit has sought client feedback in respect of all audit reports issued, at the conclusion of each audit assignment.

9.2 The feedback received from respondents for 2017/18 remains very positive. Clients score the service from 1 to 4 against a number of criteria, with 1 being very satisfied and 4 being very dissatisfied. From all the returned feedback forms, clients' overall opinion was that audits are constructive and provide value to management. The overall average score of 1.25 compares to last year's score of 1.2; everyone responding at least satisfied but most clients are very satisfied. All responses to individual criteria were in the range of very satisfied to satisfied, however, Internal Audit seeks to continually improve and will be reviewing and implementing new processes through its quality assessment and improvement programme. The theme of comments added to the feedback is that audits are conducted in a professional manner and findings and recommendations will lead to system improvements.

9.3 The full results for 2017/18, along with comparative data from 2016/17, are shown at **Annex B**.

10 Annual Governance Statement 2017/18

10.1 The Annual Report from the Chief Internal Auditor is one source of intelligence for the organisation when preparing the Annual Governance Statement (AGS). It is recommended that the Chief Internal Auditor's overall 'satisfactory' opinion on the organisation's framework of governance, risk management and control, is considered when preparing the Annual Governance Statement.

IA/AHM
May 2018

Annex A: **Formal Audit Reports issued during 2017/18**

<u>Audit:</u>	<u>Opinion:</u>
Access Approvals	Moderate
Business Continuity Management	Significant
Business Rates	Significant
Hardware & Software Management	Significant
Housing Benefit and Council Tax Support	Significant
Information Governance	Limited
School ICT Thematic Reviews	Limited
Schools' Website Compliance with Department for Education	N/A

Reports Pending from 2017/18 (draft report issued, awaiting issue as final report)

<u>Audit:</u>	<u>Indicative Opinion:</u>
Creditors	Significant
Council Tax	Significant
Payroll	Significant
Rent Assessment & Collection	Full

Briefing Notes Completed

Carbon Reduction Commitment Energy Efficiency Scheme
 Local Transport Plan Capital Block Funding (Integrated Transport and Integrated Transport & Maintenance) Grant Claim returns
 Public Services Network Code of Connection compliance
 Tyne Port Health Authority Annual Return

Project Boards / Working Groups

Internal Audit has also supported the following Project Boards / Working Groups during 2017/18 in a programme assurance role:

Customer Journey & Digital Strategy Delivery Board
 Debtors System replacement
 ICT Performance & Prioritisation Board
 Information Security Working Group
 Office 365 & SharePoint (collaborative tooling solution)
 Oracle iSupplier
 Public Services Network
 Social Care Case Management System Replacement
 Troubled Families Stakeholder Group

Ad-hoc Queries / Requests for Advice

Internal Audit receives requests for ad-hoc advice and support throughout the year, in respect of which we may be required to extract prime data or produce analysis but where it is not always appropriate to issue a formal report.

Annex B: Overall Results from Client Feedback Forms 2017/18

Satisfaction score between 1 and 4 with 1 being very satisfied and 4 being very dissatisfied (scores from 2016/17 are shown in brackets):

	Average Score
AUDIT PLANNING/COVERAGE	
• With the advance notification for the audit	1.0 (1.0)
• With the areas covered by the audit	1.0 (1.0)
• That your requirements were reflected by the audit	1.25 (1.5)
AUDIT APPROACH	
• That the objectives of the audit were clearly explained and understandable to you	1.25 (1.2)
• With the knowledge and professionalism of the auditors	1.0 (1.0)
• With the attitude and politeness of the auditors	1.0 (1.0)
• With the auditors understanding of your operational requirements	1.25 (1.2)
• That there was adequate consultation on findings and recommendations	1.25 (1.2)
REPORTING ARRANGEMENTS	
• With the accuracy of the findings	1.25 (1.7)
• With the materiality of the findings	1.25 (1.7)
• That the report was clear and concise	1.25 (1.2)
• With the usefulness of the conclusions and recommendations	1.25 (1.2)
• With the arrangements for commenting on the draft report	1.25 (1.5)
• The time taken to produce the report following the audit visit	1.5 (1.5)
OVERALL OPINION	
• That the audit was constructive and provided value to management	1.25 (1.2)