Internal Audit Annual Report 2015/16

**CARDIFF
CAERDYDD**

MISSION STATEMENT

To provide a high quality service to existing and potential clients and to attain wide recognition as a lead provider of audit, risk and investigative services, based on achieving a high standard of professionalism and expertise in service delivery

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1. **INTRODUCTION**

The Annual Reporting Process

1.1. The annual report gives an overview of audit performance during 2015/16, seeks to provide an opinion on the adequacy of the control environment in the City of Cardiff Council, and report the incidence of any significant control weaknesses. This report is prepared by the Head of Finance who in the absence of the Audit Manager is responsible for the Internal Audit and Investigations Team. For ease of reference, the term Audit Manager will be used in this report in order to outline the responsibilities of the role.

1.2. As set out in the Public Sector Internal Audit Standards (PSIAS), a professional, independent and objective internal audit service is one of the key elements of good governance, and is defined as:

> *"an independent, objective assurance and consulting activity designed to*
> *add value and improve an organisation's operations."*

1.3. Management is responsible for the system of internal control and must set in place policies and procedures to ensure that the internal controls are functioning correctly. Internal Audit acts as an assurance function providing an independent and objective opinion on the Council's control environment by evaluating its effectiveness in achieving objectives.

Requirement for Internal Audit

1.4. The Council has a duty to maintain an adequate and effective system of internal audit of its accounting records and system of internal control.

1.5. The Audit Manager (the Chief Audit Executive – CAE - for the purpose of the Standard) must provide an annual internal audit opinion and report, timed to support the Annual Governance Statement. The PSIAS specifies 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 doing so the Audit & Risk manager undertakes an assessment of the adequacy of the controls in place to support the achievement of management and corporate objectives.

Report Preparation

1.6. This report has been prepared by the Head of Finance, based on the provision of the PSIAS. Assurance has been obtained from a number of sources including:

- *Internal Audit Assignments* – work undertaken as prioritised within the Annual Audit Plan. Each assignment is risk based to deliver added value and to maximise resources. Includes some unplanned audits, undertaken at the request of Senior Management.

- *Selected Value For Money studies and exercises on spend analysis* - selected from areas of budget spend.

- *Discussion with Senior Managers* – relationship manager meetings are held on a quarterly basis with Directors, and the Audit Manager holds regular meetings with the Corporate Director Resources / Section 151 Officer and the Chief Executive.

- *Consultancy* - advice and guidance offered generally or in specific matters, including the role of "critical friend" where new and innovative systems are being designed and developed.

- *Investigations into Suspected Frauds* – through prevention, detection and oversight of all internal investigations.

- *Risk & Governance Engagement* – work in co-ordinating the Corporate Risk Register, the Annual Governance Statement and associated documents.

- *Programme and Projects Assurance* – supporting the PQA framework and undertaking health checks around compliance.

Internal Audit Section Resources

1.7.   Until April 2015, the section was led by two Audit Managers, on a job share basis. At this point one of the Audit Managers retired and the arrangement continued throughout 2015/16 with the remaining Audit Manager carrying out his duties in a part –time role. With the retirement of the remaining Audit Manager on 31st March 2016, this delivered an opportunity to review the management responsibilities of Audit going forward.

1.8.   The Internal Audit team has 11 members of staff (10.0 FTE), made up of a Group Auditor, 2 Principal Auditors, 1 Senior Auditor, 7 Auditors (6.0FTE) and an Audit Assistant. Members of the team hold various qualifications, including CIPFA and AAT.

1.9.   In addition, the Investigations team comprised 3 members of staff (2.3 FTE) whilst the Risk, Governance and Programme Assurance role was carried out by 2 members of staff. These specialist areas had staff who were qualified in Corporate Governance and Programme and Project Management respectively.

1.10. The total budget for 2015-16 was £696,000 but, as a result of planned reduction of resources in some areas such as Programme Assurance, the actual net expenditure for the year was £630,000.

Independence and Objectivity

1.11.   Internal Auditors are required to undertake audits in line with the provision of the PSIAS and in accordance with the Codes of Ethics of any professional bodies. The importance of independence is communicated to auditors and care is taken to ensure that all audit work is undertaken in an independent and objective manner. The PSIAS (1100) stipulate that any conflicts of interest or impairment to independence or objectivity must be disclosed and each year all members of Internal Audit are required to complete a Staff Declaration Statement. This identifies any potential conflict of interest that any member of the Audit team may have, which is considered when assigning audits.

1.12.   The Audit Manager has direct reporting access to the Chief Executive, the Chair of Audit Committee and all elected Members as he considers appropriate.

Continuing Professional Development

1.13.   It is also specified in the PSIAS (1230) that Internal Audit staff have a personal responsibility to maintain and develop their competencies, so that they have the necessary skills and knowledge to undertake audits to a high standard. Members of staff are encouraged to attend courses provided by the South Wales Chief Internal Auditor group, and to identify other suitable CIPFA or IIA courses which are supported when budget restrictions allow. The provisions of the Council's Personal Performance and Development Review (PP&DR) process are fully supported in the section, and there are regular 1-2-1 meetings with the team members to discuss progress on assignments and identify improvement areas of working.

2.   REVIEW OF INTERNAL CONTROL AND OPINION

Opinion 2015/16

2.1   Based on the programme of audit and investigatory work undertaken and contributions to preparing some of the key governance documents e.g. the Corporate Risk Register and Annual Governance Statement, it is considered that the overall framework for financial control within the Council for 2015-16 remains satisfactory. This opinion is based on increasing pressure on resources in both demand and budgets. The counterpoint to this pressure is a robust performance culture which ensures high productivity across the whole section.

2.2   It is becoming increasingly difficult to provide a satisfactory opinion as, whilst the financial control framework remains robust, audits continue to highlight system weakness in some areas and / or compliance issues which identify further opportunities to enhance control. There is a huge pressure on budgets and inevitably there are significant cuts being made to posts, which puts additional pressure on those remaining resources combined with the loss of knowledgeable and experience as

officers leave the Council. This is happening at a time where demands are steady or increasing and there is an appetite for change which brings with it new challenges and risks that needs to be managed.

2.3   It is noted that there has been an increase in the % of audits completed where a "Limited or No assurance" opinion was provided, which it is felt reflects, to a degree, the pressure on resources across directorates to maintain a sound control environment while struggling to retain efficient and effective services and deliver the change agenda. This requires regular monitoring and reporting with key themes identified and targeted.

2.4   In addition to this general pressure on resources, areas of particular concern have been highlighted in quarterly progress reports presented to the Section 151 Officer and Audit Committee, and include:

- The Control Risk Self-Assessment approach has been a major step forward in gathering evidence to support sound governance, risk management and control arrangement and has been well received. In schools, it has provided an overview of key governance issues and in some individual schools follow up visits have identified some significant weaknesses in different aspects of governance and financial control. This continues to be closely monitored and the Group Auditor meets regularly with the Director of Education and now attends School Budget Forum. Audit also input to Head Teacher briefings.

- Work on contracts has identified concerns over contract management skills as new ways of operating are being explored. Some social service audits highlighted some contract related matters and how these need addressing given the significance of the contract sums.

- In some audits, it was evident that there was a lack of work instructions and process mapping to capture how procedures and systems operate. This was highlighted because of the potential impact with a number of experienced staff leaving, stressing the need for proper documentation to ensure remaining and any new staff consistently follow tried and tested systems which should comply with Council rules and policies.

2.5   On a positive note, the opportunity for Internal Audit to provide training on risk management and internal control as part of the Cardiff Manager Programme is seen as a major step forward in raising awareness with senior managers around these key areas of governance and has helped clarify and set out their responsibilities for leading on compliance.

3.   SUMMARY OF WORK PERFORMED

3.1   Internal Audit, as defined in the PSIAS, encompasses the whole internal control system and is not limited to financial controls. It is defined as helping *" … an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.*"

3.2   The range of functions provided throughout the year is as outlined in our Audit Charter, considered by the Audit Committee as part of the Audit Strategy at its meeting in March 2016.

3.3   Details of all audits and audit opinions, together with other tasks performed and key performance indicators, are reported quarterly to the Section 151 Officer and Audit Committee so they are regularly updated and aware of any matters arising from audit work.

3.4   Delivering the Audit Plan has been a challenge this year with a number of factors impacting on work undertaken. It has been difficult to identify a skill resource in Computer Audit and this is currently filled on a temporary basis whilst a permanent solution can be identified. A need for contract management specialist skills has also been identified and this will be a focus of skill development over the next twelve months.

Audit team

3.5   A summary of the final reports issued by Internal Audit during 2015/16 (and those at draft status at the year end) is attached as **Appendix A**. The overall level of audits reported is similar to the last two years (at around 100), although the makeup and complexity will be different.

3.6   Through constant monitoring and prioritisation, the focus remained on high risk audits and 23 of these were finalised or at draft report stage at year end, although there was some slippage and a need to prioritise some high risk audits in the Audit Plan for 2015/16. Of these, six were Limited Assurance where follow up audits are scheduled and further work is required to enhance controls and compliance in these areas.

3.7   A further 32 audit reports relating to Medium risk areas were issued, of which four were limited assurance (an additional two may result in limited assurance opinions, pending further discussion on the draft report), and eight grant audits completed, of which one raised some concerns.

3.8 Following up previous audits, where there was a "Limited" or "No" assurance opinion, has taken more time this year, with 26 being undertaken, of which 22 have seen satisfactory progress, leaving 4 requiring further review. This is considered to be a high profile area as it is key for Managers to react to audit recommendations to enhance control where gaps or compliance is flagged up as a concern.

3.9 It should be recognised that not all of the work undertaken by the Audit team results in an audit report or grant certificate. Work is undertaken in areas that provide assurance on risk management and internal control, including advice and guidance (both on current issues and on system development) and interpretation of Council Regulations. **Appendix B** provides a list of work areas where an audit report may not be the outcome.

3.10 In order to maximise audit resources, the approach using Control Risk Self Assessment (CRSA) has been extended over the past 12 months; a full programme is now in place for schools and this approach has been successfully used for a number of core financial systems. In schools, this has included a series of workshops to outline the process and get buy-in, and feedback has been very positive. There are plans to have completed CRSAs from all schools, and for 75% of all core financial systems by March 2016, with the remainder being completed by March 2017.

3.11 A key element of our role has continued to be as "critical friend", working with others when systems and processes are being redesigned and reconfigured to meet changing demands. Here our role in ensuring risks are properly identified, mapped and mitigated and controls adequately considered and prioritised and projects delivered to scope, time and budget is consider important, especially where the Council is undergoing such rapid change to deal with budgetary and other wide ranging pressures.

3.12 Regarding systems and processes, a significant amount of work has again been done reviewing our working practices across the Section over the past 12 months, building on previous work around lean auditing. A major service review was completed in the autumn which entailed a detailed examination of key activities and an assessment of where time was being spent, resulting in some areas for further development. A small Audit development team has been established to progress actions arising from the review and an opportunities log is being maintained and regularly discussed. Audit protocols and working methods have been updated and engagement with clients has continued to shape and enhance the service provided. Audit also volunteered to be a pilot site for the introduction of SharePoint, an electronic document management system and, in working towards implementation in May 2015, a huge amount of work was undertaken in streamlined filing systems and administrative processes which has helped with our push to having a paperless office.

3.13   The recommendations raised in audit reports are given a risk rating in line with the risk ratings in the Council's corporate risk strategy (i.e. red, red/amber and amber/green). The table below sets out the recommendations raised by the assurance level given:

Risk Rating	Recommendations Raised by Auditor	Recommendations Agreed by Client Manager	Percentage Agreed to Raised
Red	125	125	100%
Red/Amber	246	242	98%
Amber / Green	160	159	99%
TOTAL	**531**	**526**	**99%**

3.14   The number of green risk recommendations are no longer recorded as these are discussed with the client at the exit meeting when the draft report is discussed, in order that these matters do not disproportionately attract attention when the final report is issued.

3.15   The figures show that with 99% of audit recommendations agreed that managers welcome ideas as to how governance or controls can be enhanced and it provides a degree of assurance that the auditor understands the risks and is adding value through the fieldwork undertaken.

Recommendations Acted Upon

3.16   Important as it is that audit recommendations are agreed, change will only happen if the recommendations are implemented and so audit reports are monitored until all actions are closed. The database is regularly analysed and reports prepared every quarter of open actions. Each Directorate has a relationship manager who provides information on outstanding items in their regular meetings.

Investigation Team

3.17   **Appendix C** sets out a report which details the activities of the Investigation Team and **Appendix D** details ad-hoc investigations.

Risk and governance

3.18   In order to facilitate and challenge the review of the Corporate Risk Register (CRR), at intervals throughout the year Audit Management attended Senior Management Team to ensure collective "buy in" of the strategic risks facing the Council following updates by individual risk owners.

3.19   The Annual Governance Statement (AGS) 2014/15 was finalised in accordance with the accounting deadlines and presented to the Audit Committee in June 2015 and September 2015 as part of the Statement of Accounts. The drafting of the AGS 2015/16 commenced in quarter 4, with reports presented to Audit Committee in February 2016 and March 2016. Senior Management Assurance Statements were circulated to the Senior Management Team for completion at the year end position. A final draft of the AGS will be incorporated into the draft Statements of Accounts and presented to Audit Committee in June 2016.

3.20   The Risk & Governance team has supported the work of the Audit Committee by producing a number of reports relating to the Corporate Risk Register, the Annual Governance Statement and management assurance statements. Support has also been provided through updating of the Committee's Annual Self-Assessment and the drafting of the Committee's Annual Report.

4.   AUDIT PERFORMANCE AND ADDED VALUE

Quality Assurance

4.1   Internal Audit is committed to working to the highest professional standards, and to delivering a quality product that adds value to senior management. As such, performance is actively monitored and feedback from management is encouraged.

4.2   An Audit planning control database is maintained to effectively monitor work done in line with that planned. This is where the detail of the Audit Plan is kept. The database is used to allocate assignments and record work done in areas, to provide key performance information for management. Auditors are required to complete timesheets to record work undertaken on their assignments and tasks they are allocated (which are approved weekly by a senior auditor), so management can continually assess the Plan v Actual position for individual audits and across the overall Plan.

4.3   Each audit is subject to a qualitative review by a senior member of the team who ensure the focus on key risks is retained throughout the course of the assignment and time is used to best effect. The reviewer will undertake checks to ensure professional standards are maintained and no report is sent out without a review by a senior member of the team.   Any Limited Assurance report, or any with any significant issue to report, are reviewed by the Audit Manager.

4.4   Following the issue of a draft audit report a meeting is held with the Client Manager with an opportunity for them to challenge the audit findings and proposed recommended actions. This provides a degree of assurance that the final reported position is accurate and reflects the appropriate risk profile of the audit and any recommendations for improvement are considered.

Post Audit Assessment & Customer Feedback

4.5   As part of qualitative assurance, the Audit team uses a process known as "post audit assessment", which includes a client questionnaire.

4.6   The Post Audit Assessment sets out the core competencies required whilst undertaking an audit and the auditor for each assignment has to score their performance against each of these competencies. The assessment is useful in providing assurance that key competencies are evidenced throughout the audit process and as a useful means of identifying training needs. Analysing the assessments helps focus individual PPD reviews and provides audit management with an overview of performance at the different grades.

4.7   Following each audit Client Managers are contacted and asked to complete a Quality Assurance Questionnaire, recognising the value placed on the feedback they provide. These questions cover four categories, and the results are used to determine areas for improvement.

4.8   During the year, 39 questionnaires were issued. The results from the questionnaires are summarised in the table below:

	Excellent	Good	Satisfactory	Unsatisfactory	TOTAL
Communication	17	22	0	0	39
Auditor Advice	11	21	7	0	39
Report	8	26	5	0	39
Performance	18	19	2	0	39
	54	**88**	**14**	**0**	**156**

4.9   It can be seen that the feedback from the audit questionnaires is positive, which is encouraging as the nature and complexity of the assignments continues to change. The questionnaires also ask Managers to indicate whether they consider that the audit process added value and there were no negative responses. It can be seen that the majority of the auditees felt that the audits undertaken are constructive and add value.

Audit Recommendations

4.10   The extent to which audit recommendations are agreed by senior managers is used as a measure of auditor's performance as a high level suggests an understanding of the risks and controls within the area under review and adding value by proposing meaningful changes and cost effective changes. Details of these have already been provided above.

<u>Benchmarking</u>

4.11 The Audit team is both a member of the Welsh Chief Auditors and the CIPFA Internal Audit benchmarking group. In addition, preliminary work was undertaken with UK core cities but the results of this exercise will be received during 2016/17.

4.12 One key area that has been picked up is in respect of productivity which has fed into the team plan for 2016/17 to increase the proportion of productive time compared to non productive. This needs to be looked at in conjunction with quality of output to ensure that neither quality nor output are compromised.

<u>Self-Assessment and Peer Review</u>

4.13 Every year the Audit & Risk Manager completes the PSIAS self assessment evaluation and in doing so is able to confirm the work of the Audit team conforms to the standard. Again this year there are no significant non conformances considered worthy of reporting. This assessment is shared with the Wales Audit Office which looks to rely to a degree on the work of colleagues in Internal Audit.

4.14 In 2016/17 work has been programmed with neighbouring authorities for a full external assessment in the autumn, as required within the Standard.