

## REPORT TO THE AUDIT COMMITTEE – 24 MAY 2018

### INTERNAL AUDIT ANNUAL REPORT AND INTERNAL FINANCIAL CONTROL STATEMENT 2017/18

#### 1. Recommendations

The Committee is requested to:

**1.1 Note the Internal Financial Control Statement for 2017/18;**

**1.2 Note that the Chief Internal Auditor has confirmed the organisational independence of Internal Audit;**

**1.3 Note that there has been no limitation to the scope of Internal Audit work during 2017/18; and**

**1.4 Note that a draft report has been received from Dundee City Council's Internal Audit Section relating to the required External Quality Assessment and the outcome of that will be reported to Committee in July, 2018.**

#### 2. Discussion

2.1 It is one of the functions of the Audit Committee to review the activities of the Internal Audit function, including its annual work programme. Internal Audit reports interim progress in December each year and provides a full year report following the end of the financial year.

2.2 The Internal Audit plan for 2017/18 was agreed by the Audit Committee on 29 March, 2017. Each of the audits contained in the plan was allocated a number of days determined by the perceived complexity of the work, level of testing envisaged and expected outcome of the audit. The plan also included an allocation of time for dealing with additional work requests, providing advice to Services, and for investigations into suspected financial irregularities. The allocation of time to planned audits included an allowance for those 2016/17 audits that had yet to be completed.

2.3 Appendices A and B to this report detail the position with those audits that were carried forward from 2016/17, along with details of the position relating to audits contained in the original 2017/18 plan. As can be seen from the appendix, work from one year routinely rolls over into the following year. It is also the case that work detailed in the plan can be deferred to future years.

2.4 All of the residual 2016/17 work carried forward has been completed. Progress with the 2017/18 planned work was well progressed, although some audits have taken longer than anticipated to complete due to issues identified during testing and the availability of resources during the year.

2.5 The 2017/18 Internal Audit plan was based on the Internal Audit Section

being fully staffed during the year. However, the Section was operating at less than full establishment during the year due to: higher than usual sickness absence; the resignations of three Assistant Auditors, all of whom were replaced on temporary contracts to 31 March, 2018. The Section ended the year at full establishment. It is estimated that around 10% of the Section's capacity during the year was lost for these staffing reasons.

- 2.6 During 2017/18, a large number of recommendations were accepted which, if taken to full implementation, will improve the Council's internal control environment and, in some cases, result in more efficient and effective processes, and financial savings for the Council. Difficulties continue to be experienced by Services in achieving implementation dates and more work than planned was spent following up on these issues. Failures to implement the more significant recommendations can have an impact on the overall Internal Audit opinion expressed in the annual Internal Financial Control Statement and the level of assurance that can be provided to those charged with governance.
- 2.7 It is considered that sufficient work was completed during the year, or was sufficiently advanced by the year-end, on which to base the conclusion drawn in the annual Internal Financial Control Statement. This is attached as Appendix C, and concludes that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's internal control system in the year to 31 March, 2018.
- 2.8 However, as with previous years, Internal Audit has highlighted some significant concerns throughout the year relating to compliance with Council policies and procedures, and with regard to delays in the implementation of recommendations agreed in Internal Audit reports. The number of recommendations made by Internal Audit has increased when compared to the previous year and the number of reports containing recommendations graded as "major" remained the same.
- 2.9 The Public Sector Internal Audit Standards (PSIAS) require that the Chief Internal Auditor reports to Senior Management and the Board (the Audit Committee) on the outcome of Internal Audit's Quality Assurance and Improvement Plan (QAIP).
- 2.10 A checklist developed by the Scottish Local Authorities Chief Internal Auditors' Group for undertaking external peer reviews has previously been used to undertake the required self-assessment in assessing conformance with the PSIAS and the associated Local Government Application Note. The checklist is a lengthy document, comprising a range of detailed questions, which leads to an assessment of 13 key areas of the PSIAS. Following completion of the self-assessment, the previous outcome, was that Internal Audit either Fully or Generally Complied with all areas examined. Where General Compliance was recorded, actions were determined, with the intention of moving these areas to 'Fully Complies'.
- 2.11 There is a requirement that an External Quality Assessment be undertaken of a Council's Internal Audit arrangements at least once every five years. During 2017/18, Dundee City Council's Internal Audit undertook an External Quality Assessment of Aberdeenshire Council's Internal Audit arrangements. The draft report resulting from that review has recently been received and responded to. The final outcome will be reported to the

Audit Committee in July, 2018.

- 2.12 As part of reporting on the QAIP, there is a requirement to provide the Board with performance data. As has been reported previously, this has been a matter of debate amongst practitioners in Scotland, with little consensus reached on what should be measured. Internal Audit's performance data, as it stands, is attached as Appendix D for discussion.
- 2.13 The Standards also require that Internal Audit confirms to the Board, at least annually, that it is organisationally independent. The organisational independence of Internal Audit is established through Financial Regulations (approved by the Policy and Resources Committee) and the Internal Audit Charter (approved by the Audit Committee). Other factors which help ensure Internal Audit's independence are that: the Internal Audit plan is approved by the Audit Committee; Internal Audit reports its outputs to Committee in the name of the Chief Internal Auditor; the Chief Executive and the Chair of the Audit Committee are invited to contribute to the Chief Internal Auditor's annual review; and, the outcome of the review is referred to the Chief Executive by the Director of Business Services.
- 2.14 There is also a requirement to report any instances where the scope of Internal Audit's work has been limited. During 2017/18, there was no such limitation.
- 2.15 The Head of Finance and Monitoring Officer within Business Services have been consulted in the preparation of this report. Any comments made have been incorporated within the report and they are satisfied that the report complies with the Scheme of Governance and relevant legislation.

### **3. Scheme of Governance**

- 3.1 The Committee is able to discuss this item in terms of Sections G.1.1.d and G.1.4 of the List of Committee Powers in Part 2A of the Scheme of Governance, as the Committee is responsible for Internal Audit matters and reviewing the activities of Internal Audit.

### **4. Equalities, Staffing and Financial Implications**

- 4.1 An equality impact assessment is not required because the reason for this report is for Committee to discuss and comment on Internal Audit's annual report, performance measures and Internal Financial Control Statement, none of which has a differential impact, as a result of this report, on people with protected characteristics.
- 4.2 There are no staffing or financial implications arising directly from this report.

### **CHIEF INTERNAL AUDITOR**

Report prepared by David Hughes, Chief Internal Auditor. 9 May, 2018.

**APPENDIX A**

**2016/17 Audit Work carried forward into 2017/18:**

<b>Service</b>	<b>Audit Topic</b>	<b>Position as at 31 March 2018</b>
Business Services	Social Media	Complete August 2017
	Fixed Asset Register	Complete May 2017
	CRM System	Complete September 2017
	Treasury Management	Complete May 2017
	Budget Monitoring	Complete July 2017
	Debtors System	Complete May 2017
	Benefits	Complete June 2017
	Payroll System	Complete October 2017
	Payroll Processes	Complete October 2017
	Health and Safety	Complete May 2017
	Deployment of Microsoft Technology	Complete June 2017
Halls	Complete July 2017	
Education and Children's Services	Children's Homes	Complete June 2017
	Sports Facilities	Complete May 2017
Aberdeenshire Health & SC Part	Criminal Justice Service	Complete September 2017
Infrastructure Services	Transportation Purchasing and Creditors	Complete July 2017
	School and Supported Local Bus Services Tendering	Complete April 2017
	Building Maintenance Establishment Visits	Complete August 2017
	Car Park Income	Complete March 2018

**APPENDIX B - 2017/18 Audit Work:**

Service	Audit Topic	Position as at 31 March 2018
Corporate / Cross Service	Timesheets & Allowances	Complete June 2017
	Business Continuity Planning	Complete September 2017
	New Governance Arrangements	Complete October 2017
	Compliance with Procurement Related Legislation and Council Regulations	Complete October 2017
	Overtime	Complete October 2017
	Climate Change Action Plan	Complete November 2017
	Attendance Management	Draft Report issued April 2018
	Partnerships and Joint Working	Complete April 2018
	Changes in Government Policy, Legislation and Regulation	Complete May 2018
Business Services	Payroll Reconciliations	Complete August 2017
	Procurement of ICT hardware, software, etc outwith ICT	Complete December 2017
	Purchase Cards	Complete January 2018
	Training for Councillors	Complete January 2018
	Pensions	Complete January 2018
	Balance Sheet Codes	Draft Report issued March 2018
	Benefits	Complete December 2017
	Mobile Telephony	Complete May 2018
	Leavers' Procedures	Complete May 2018
	Budget Setting Process	Draft Report issued March 2018
	Change Management (ICT)	Draft Report issued February 2018
	System Recovery	Draft Report issued April 2018
	City Region Deal	Work in Progress
	Fixed Asset Register	Work in Progress
Centralisation of Payments Function	Cancelled as progress with project not sufficiently advanced.	

**APPENDIX B - 2017/18 Audit Work (continued):**

<b>Service</b>	<b>Audit Topic</b>	<b>Position as at 31 March 2018</b>
Business Services (cont)	Councillors Code of Conduct	Work in Progress
	Estates Rationalisation	Work in Progress
	Hard FM Contract	Work in Progress
	Business Rates	Move to 2018/19 as agreed by Audit Committee on 14 December 2017
Education and Children's Services	Primary Schools	Complete August 2017
	Libraries	Complete September 2017
	Education Maintenance Allowances	Complete October 2017
	PFI / PPP Charges	Complete November 2017
	Proposed Sport and Culture Trust	Complete November 2017
	Procurement	Complete November 2017
	Health and Safety (SSERC)	Complete January 2018
	Academies	Complete February 2018
	Community Centres	Complete May 2018
	Catering Procurement	Complete May 2018
	Out-of-Authority Placements	Move to 2019/20 at request of Service
	Raising Attainment and Closing the Gap	Draft Report issued April 2018
	Teachers Payroll	Move to 2018/19 as agreed by Audit Committee on 14 December 2017
Aberdeenshire Health and Social Care Partnership	Day Care Establishment Visits	Complete September 2017
	Social Work Tendering	Complete November 2017
	Joint OT Store	Draft Report issued April 2018

**APPENDIX B - 2017/18 Audit Work (continued):**

Service	Audit Topic	Position as at 31 March 2018
Infrastructure Services	MOT and Taxi Licensing	Complete September 2017
	EAFRD Grant Claim	Complete October 2017
	Gas Servicing	Complete October 2017
	Vehicle Usage	Complete November 2017
	Homeless Persons Budget	Complete December 2017
	Recycling	Complete January 2018
	Quarries	Draft Report issued April 2018
	Housing Tendering Procedures	Work in Progress
	Roads Procurement and Tendering	Work in Progress
	Regeneration	Work in Progress
	Bus Service Operators Grant	Complete – No reporting to Committee
	Interreg Projects	Complete – No reporting to Committee

## Appendix C

### **Internal Audit Statement relating to Aberdeenshire Council's Internal Control System for the year ended 31 March 2018**

As Chief Internal Auditor of Aberdeenshire Council, I am pleased to present my annual statement on the adequacy and effectiveness of the internal control system of the Council for the year ended 31 March 2018. The purpose of this statement is to assist the Head of Finance in forming his opinion in relation to the required annual Governance Statement to be included in the Annual Accounts.

#### **Opinion**

It is my opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Council's framework of governance, risk management and control in the year to 31 March 2018.

However, as in previous years, some significant concerns have been identified throughout the year. Recommendations graded as "major" have been made in 7 reports in 2017/18 (10 in 2016/17 and 10 in 2015/16): Health and Safety, Payroll System, Timesheets and Allowances, Compliance with Procurement Related Legislation and Financial Regulations, Proposed Sport and Culture Trust, Gas Servicing Procedures, and Education Procurement. The outcome of these audits, along with others, and concerns regarding the implementation of previously agreed recommendations have been reported to the Audit Committee throughout the year.

Recommendations made regarding the issues identified have been agreed with management and Internal Audit will be ascertaining progress with implementing these during 2018/19. Progress made by Services will help inform Internal Audit's annual opinion for 2018/19.

In addition to the above, areas of good practice, improvement, and procedural compliance have been identified and these have been detailed in individual assignment reports.

#### **Basis of Opinion**

My evaluation of the control environment is informed by a number of sources:

- The audit work completed by Internal Audit during the year to 31 March 2018;
- Progress made by Services with implementing agreed Internal Audit recommendations;
- The assessment of risk completed during the updating of the audit plan;
- Reports issued by the Council's external auditors; and
- Internal Audit's knowledge of the Council's governance, risk management and performance monitoring arrangements.

## **Respective responsibilities of management and internal auditors in relation to internal control**

It is the responsibility of the Council's senior management to establish an appropriate and sound system of internal control and to monitor the continuing effectiveness of that system. It is the responsibility of the Chief Internal Auditor to provide an annual overall assessment of the robustness of the internal control system.

### **Sound internal controls**

The main objectives of the Council's internal control systems are to:

- ensure adherence to management policies and directives in order to achieve the organisation's objectives;
- safeguard assets;
- ensure the relevance, reliability and integrity of information, so ensuring as far as possible the completeness and accuracy of records; and
- ensure compliance with statutory requirements.

Any system of control can only ever 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 or regulations. Accordingly, the Council is continually seeking to improve the effectiveness of its systems of internal control.

### **The Work of Internal Audit**

Internal Audit is an independent appraisal function established by the Council for the review of the internal control system as a service to the organisation. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources.

The section undertakes an annual programme of work agreed with Service Directors and the Audit Committee. The audit plan is based on a risk assessment process which is revised on an ongoing basis to reflect evolving risks and changes within the Council.

All Internal Audit reports identifying system weaknesses, non-compliance with expected controls, and / or assurance of satisfactory operation are brought to the attention of management and include appropriate recommendations and agreed action plans. It is management's responsibility to ensure that proper consideration is given to Internal Audit reports and that appropriate action is taken on audit recommendations. The Internal Auditor is required to ensure that appropriate arrangements are made to determine whether action has been taken on internal audit recommendations or that management has understood and assumed the risk of not taking action.

**David Hughes**  
**Chief Internal Auditor**  
**Aberdeenshire Council. 23 April 2018**

**Appendix D**

**INTERNAL AUDIT PERFORMANCE MEASURES**

PI	Description	Target	Actual 2016/17	Actual 2016/17
1	Percentage of planned audits commenced where the Service was given advance notice of commencement of field work.	100%	100.00%	100.00%
2	Percentage of current year audits (as adjusted through consideration of subsequent year's plan, see Note (1)) where draft report issued by deadline.	90%	56.82%	62.79%
3	Percentage of current year audits (as adjusted) completed by end of current year.	65%	55.56%	60.00%
4	Percentage of previous year audits (as adjusted) completed by end of current year.	100%	100.00%	100.00%
5	Percentage of current year audits (as adjusted) that were completed in the year within 110% of planned time allocated.	90%	66.67%	50.00%
6	Percentage of previous year audits (as adjusted) that were completed within 110% of planned time allocated.	90%	60.53%	63.00%
7	Percentage of planned time taken for current year audits that were completed in the year.	90 - 110%	100.21%	121.08%
8	Percentage of planned time taken for all previous year audits completed by end of current year.	90 - 110%	123.05%	106.63%

PI	Description	Target	Actual 2017/18	Actual 2016/17
9	Percentage of recommendations accepted by management (See Note (2)).	95%	98.46%	98.49%
10	Where management has not agreed recommendation, percentage who accept risk.	100%	100.00%	100.00%

Notes:

- (1) The adjusted number of audits in the plan for 2016/17 was 50, and for 2017/18 was 54.
- (2) The number of recommendations made by Internal Audit in 2016/17 was 464, and for 2017/18 was 521.

Commentary

The level of performance in most areas is comparable between 2017/18 and 2016/17, although improvements have been made in the amount of time spent on reviews when compared to that planned. This was identified as an issue in the 2016/17 annual report and action has been taken to make improvements, although there are still some areas where improvements can be made.