

**INTERNAL AUDIT ANNUAL REPORT 2016-17**

**1 Purpose**

- 1.1 The Head of Internal Audit (Corporate Governance Manager) is required to provide a written annual report to those charged with governance, timed to support the Annual Governance Statement. This report should be presented to Members and considered separately from the Annual Governance Statement and formal accounts.
- 1.2 The report summaries the work of Internal Audit for the period 1 April 2016 to 31 March 2017, identifying the areas upon which the audit opinion is based.

**2 Recommendations/for decision**

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|-----|---|
| 2.1 | The Committee is requested to note the contents of the Internal Audit Annual Report for the financial year 2016-17. |
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**3 Supporting information**

- 3.1 The Audit Committee's terms of reference include dealing with internal and external audit issues. This report allows formal recognition of the Annual Internal Audit report by a committee of the Council.
- 3.2 The Council is required to issue a statement of accounts each year. Included in the accounts is a statutory Annual Governance Statement to be signed by the Leader and Chief Executive. This statement gives assurance that matters relating to the Council's operations are being properly managed and controlled.
- 3.3 The Annual Governance Statement draws upon the management and internal control framework of the Council, especially the work of internal audit and the Council's risk management framework. In particular the independent report of the Council's Head of Internal Audit is a significant factor in determining the position to be reported.
- 3.4 The attached report includes the Head of Internal Audit's opinion on the adequacy and effectiveness of the Council's systems of governance, risk management and control.
- 3.5 In forming this opinion the Head of Internal Audit can confirm that internal audit activity throughout 2016-17 has been independent from the rest of the organisation and has not been subject to interference in the level or scope of the audit work completed.

**4 Options considered**

- 4.1 None - The Internal Audit Annual report is a statutory requirement.

**5 Resource implications**

- 5.1 None

Contact Officer

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Background Documents

None



# **Internal Audit Annual Report**

**APRIL 2016 – MARCH 2017**

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## Contents

<b>1. Introduction</b> .....	2
<b>2. Head of Internal Audit Opinion</b> .....	3
<b>3. Summary of Internal Audit Activity</b> .....	4
Overview .....	4
Direction of control travel.....	5
Significant control weaknesses .....	5
Other internal audit work .....	6
Follow up work / outstanding recommendations .....	6
<b>4. Review of Effectiveness</b> .....	6
<b>Appendix 1: Opinion types</b> .....	7
<b>Appendix 2: Internal audit classifications</b> .....	8

# 1. *Introduction*

Internal Audit is a statutory requirement for local authorities under the Accounts and Audit Regulations (2015), which states that a local authority must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance.

The Public Sector Internal Audit Standards (PSIAS) require the Head of Internal Audit (Corporate Governance Manager) to deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement. The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control (i.e. the Council's system of internal control). The annual report must incorporate:

- the opinion;
- a summary of the work that supports the opinion; and
- a statement on conformance with the Public Sector Internal Audit Standards.

This is achieved through the completion of a risk-based plan of work, agreed with management and approved by the Audit Committee, which is designed to provide a reasonable level of assurance. The opinion does not imply that Internal Audit has reviewed all risks relating to the organisation.

## 2. *Head of Internal Audit Opinion*

In giving this opinion, it should be noted that assurance can never be absolute. The work of internal audit can only provide reasonable assurance that there are no major weaknesses in the processes and controls reviewed.

In assessing the level of assurance to be given, I have based my opinion on:

- the results of assurance reviews and consultancy/advisory work undertaken during the year;
- the results of follow-up action taken in respect of assurance reviews, including those from previous years;
- whether or not any limitations have been placed on the scope of internal audit;
- the extent of resources available to deliver the internal audit work;
- the proportion of the Council's assurance needs that have been covered within the period; and
- the quality and performance of the internal audit service and the extent of compliance with the Standards.

I am satisfied that sufficient assurance work has been carried out to allow me to form an opinion on the adequacy and effectiveness of Aylesbury Vale District Council's systems of governance, risk management and control.

My opinion is as follows:

### **Generally satisfactory with some improvements required to specific systems and processes**

Governance, risk management and control in relation to business critical areas is generally satisfactory. However, there are some weaknesses in the framework of governance, risk management and control which potentially put the achievement of the Council's objectives at risk.

Some improvements are required in those areas to enhance the adequacy and effectiveness of governance, risk management and control.

**Kate Mulhearn**  
**Corporate Governance Manager**  
**July 2017**

The key factors that contributed to my opinion are summarised as follows:

- Overall the weaknesses in control design and operating effectiveness identified were medium or low risk. Improvements have been made during the year in some key financial systems (Accounts Payable, General Ledger, Budget Management) to strengthen the overall control environment.
- Improvements are still required in a number of areas. High risk reports were issued for Accounts Receivable and Housing Benefits.
- A number of internal audit reports highlighted inadequacies in the level of management information, both at a corporate and service level to enable effective monitoring and oversight of both financial and non-financial performance.

Please see further detail in Section 3.

### 3. Summary of Internal Audit Activity

#### Overview

A total of 13 assurance reviews were completed in 2016/17 of which 2 were classified as “high” risk, 6 were given “medium” and 5 were given “low” risk classifications. This resulted in the identification of 6 high, 21 medium and 25 low risk findings relating to weaknesses in the design and operating effectiveness of controls.





In the previous financial year 13 assurance reviews were completed resulting in 6 high, 22 medium and 9 low priority recommendations for improvement. Due to the different mix and focus of reviews the overall results cannot directly be compared from year to year.

The table below sets out the results of the internal audit work.

Review	Report risk rating*	Number of findings			
		Critical	High	Medium	Low
General Ledger	Medium	-	-	3	3
Payroll	Low	-	-	1	3
Accounts Receivable	High	-	2	2	2
Accounts Payable	Low	-	-	-	3
Treasury Management	Medium	-	-	2	2
Fixed Assets	Medium	-	-	2	4
Contract Management	Medium	-	-	3	-
Budget Management	Low	-	-	1	3
Safeguarding	Medium	-	1	1	1
Housing benefits	High	-	3	3	-
Council Tax & Business Rates	Low	-	-	1	2
Commercial Property – Service Charges	<i>Medium (draft)</i>	-	-	2	1
Vale Lottery	Low	-	-	-	1
Company Governance – Aylesbury Vale Broadband	N/A – Advisory review	-	-	-	-
<b>Total</b>		-	<b>6</b>	<b>21</b>	<b>25</b>

\*A definition of the risk classifications is attached at Appendix 2.

## Direction of control travel

Finding rating	Trend between current and prior year	Number of findings	
		2016/17	2015/16
Critical	-	-	-
High		6	6
Medium		21	22
Low		25	9
<b>Total</b>		52	37

The results may not be directly comparable year on year due to the different mix of reviews performed. In addition, in 2016/17 there was a new Head of Internal Audit and new team delivering the reviews. By starting to provide trend information now we should be able to build a picture over the coming years.

## Significant control weaknesses

A number of weaknesses were identified that should be reported in the Annual Governance Statement. These relate to the “high risk” reports issued for Accounts Receivable and Housing Benefits and a general theme about lack of management information:

### *Accounts Receivable*

There has been a lack of corporate and local oversight of the debt held in each service area and irregular monitoring of the age profile of debt. There are no corporate performance indicators to identify areas which are performing less well in their debt management to allow more effective corrective action to be taken.

There is also a lack of clarity over the roles and responsibilities of the Income Team and service areas regarding which team is responsible for debt management. The Council recognises these challenges and in November 2016 set up a Corporate Debt Project to address the issues and improve debt management processes.

Through the work of the Debt Project, issues have been identified between the system interfaces and manual processes that ensure information on housing benefit overpayment debt is consistent and reconciled between the finance system (TechOne) and benefits system (Northgate). During June/July 2017 the project team has been working to reconcile the two systems and clear any discrepancies. At the time of concluding this report all electronic matching and sorting has been completed on the data from both systems. The task in process is to work through manually each unmatched item and investigate both systems to correct the difference. At this stage we understand that it will not result in a material adjustment to the reported debt figures. Work is also progressing with the software providers to address the underlying issue around the interface between TechOne and Northgate. In the mean time, dedicated resource has been identified to ensure manual processes will operate effectively to maintain ongoing updates and accuracy.

### *Housing Benefits*

The structure of the benefits administration team changed significantly as a result of the Commercial AVDC business review. We reported inadequacies in both the current structure and the knowledge and experience of the staff.

Quality checks have been performed inconsistently and there has been inadequate follow-up of outcomes from quality checks during the year. In addition, there has been a lack of performance monitoring and reporting of key housing benefit metrics.

#### *Management information*

A number of internal audit reports have highlighted inadequacies in the level of management information, both at a corporate and service level to enable effective monitoring and oversight of both financial and non-financial performance, and inform decisions. This issue has been highlighted on the corporate risk register. The restructure has created two new posts to support enhanced Business Intelligence across the Council and investment has been made in software to enable data extraction and reporting across all the systems. This is an area of focus during 2017/18.

### **Other internal audit work**

#### *Risk Management*

The risk management arrangements form a key part of the Council's overall internal control framework. Internal audit has not provided any specific assurance over this process during the year but the Corporate Governance Manager has facilitated the regular review of the corporate risk register by Commercial Board, Audit Committee and Cabinet.

### **Follow up work / outstanding recommendations**

Agreed actions arising from audit reports are kept under review by Internal Audit and regular reports on overdue actions are provided to the Audit Committee.

Audit recommendations raised during 2015/16 internal audit reviews relating the financial systems have been followed up as part of current year testing. To the extent that issues have not been satisfactorily addressed they have been re-raised in the current year reports.

There are no significant issues to report regarding the follow up of any audit recommendations.

## **4. Review of Effectiveness**

The Council's internal audit function has been restructured during 2016/17 as part of the Commercial AVDC transformation programme. Since September 2016, the Head of Internal Audit role has been fulfilled by the Corporate Governance Manager and work has been performed by an external service provider under a co-source arrangement.

A self-assessment against the requirements of the Public Sector Internal Audit Standards (PSIAS) was conducted in 2013 and the gap analysis and action plan was last updated in July 2015. I have considered the requirements of PSIAS and there are no areas of concern to indicate that the current arrangements are not fully compliant with the Standards.

During 2017/18 a new co-source contract will be procured and compliance with PSIAS will be considered as part of the service specification.



## Appendix 1: Opinion types

At the end of the year, the Head of Internal Audit provides an annual assurance opinion based on the work performed, which is used to inform the Council's Annual Governance Statement. The table below sets out the four types of opinion along with an indication of the types of findings that may determine the opinion given. The Head of Internal Audit will apply his/her judgement when determining the appropriate opinion so the guide given below is indicative rather than definitive.

Type of opinion	Indication of when this type of opinion may be given
<b>Satisfactory</b>	<ul style="list-style-type: none"> <li>• A limited number of medium risk rated weaknesses may have been identified, but generally only low risk rated weaknesses have been found in individual assignments; and</li> <li>• None of the individual assignment reports have an overall report classification of either high or critical risk.</li> </ul>
<b>Generally satisfactory with some improvements required</b>	<ul style="list-style-type: none"> <li>• Medium risk rated weaknesses identified in individual assignments that are <i>not significant in aggregate</i> to the system of internal control; and/or</li> <li>• High risk rated weaknesses identified in individual assignments that are <i>isolated</i> to specific systems or processes; and</li> <li>• None of the individual assignment reports have an overall classification of critical risk.</li> </ul>
<b>Major improvement required</b>	<ul style="list-style-type: none"> <li>• Medium risk rated weaknesses identified in individual assignments that are <i>significant in aggregate but discrete parts</i> of the system of internal control remain unaffected; and/or</li> <li>• High risk rated weaknesses identified in individual assignments that are <i>significant in aggregate but discrete parts</i> of the system of internal control remain unaffected; and/or</li> <li>• Critical risk rated weaknesses identified in individual assignments that are <i>not pervasive</i> to the system of internal control; and</li> <li>• A <i>minority</i> of the individual assignment reports may have an overall report classification of either high or critical risk.</li> </ul>
<b>Unsatisfactory</b>	<ul style="list-style-type: none"> <li>• High risk rated weaknesses identified in individual assignments that <i>in aggregate are pervasive</i> to the system of internal control; and/or</li> <li>• Critical risk rated weaknesses identified in individual assignments that are <i>pervasive</i> to the system of internal control; and/or</li> <li>• <i>More than a minority</i> of the individual assignment reports have an overall report classification of either high or critical risk.</li> </ul>
<b>Disclaimer opinion</b>	<ul style="list-style-type: none"> <li>• An opinion cannot be issued because insufficient internal audit work has been completed. This may be due to either: <ul style="list-style-type: none"> <li>○ Restrictions in the audit programme agreed with the Audit Committee, which meant that our planned work would not allow us to gather sufficient evidence to conclude on the adequacy and effectiveness of governance, risk management and control; or</li> <li>○ We were unable to complete enough reviews and gather sufficient information to conclude on the adequacy and effectiveness of arrangements for governance, risk management and control.</li> </ul> </li> </ul>

## Appendix 2: Internal audit classifications

### Report classifications

The overall report classification is determined by allocating points to each of the individual findings included in the report.

Findings rating	Points
Critical	40 points per finding
High	10 points per finding
Medium	3 points per finding
Low	1 point per finding

Report classification		Points
●	Critical risk	40 points and over
●	High risk	16– 39 points
●	Medium risk	7– 15 points
●	Low risk	6 points or less

*Individual finding ratings*

Individual findings are considered against a number of criteria and given a risk rating based on the following:

Finding rating	Assessment rationale
<b>Critical</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Critical</b> impact on operational performance; or</li> <li>• <b>Critical</b> monetary or financial statement impact [quantify if possible = materiality]; or</li> <li>• <b>Critical</b> breach in laws and regulations that could result in material fines or consequences; or</li> <li>• <b>Critical</b> impact on the reputation or brand of the organisation which could threaten its future viability.</li> </ul>
<b>High</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Significant</b> impact on operational performance; or</li> <li>• <b>Significant</b> monetary or financial statement impact [quantify if possible]; or</li> <li>• <b>Significant</b> breach in laws and regulations resulting in significant fines and consequences; or</li> <li>• <b>Significant</b> impact on the reputation or brand of the organisation.</li> </ul>
<b>Medium</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Moderate</b> impact on operational performance; or</li> <li>• <b>Moderate</b> monetary or financial statement impact [quantify if possible]; or</li> <li>• <b>Moderate</b> breach in laws and regulations resulting in fines and consequences; or</li> <li>• <b>Moderate</b> impact on the reputation or brand of the organisation.</li> </ul>
<b>Low</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Minor</b> impact on the organisation's operational performance; or</li> <li>• <b>Minor</b> monetary or financial statement impact [quantify if possible]; or</li> <li>• <b>Minor</b> breach in laws and regulations with limited consequences; or</li> <li>• <b>Minor</b> impact on the reputation of the organisation.</li> </ul>
<b>Advisory</b>	<p>A finding that does not have a risk impact but has been raised to highlight areas of inefficiencies or good practice.</p>