

Report to: **Audit, Best Value and Community Services Scrutiny Committee**

Date: **12 March 2014**

By: **Chief Operating Officer**

Title of report: **Internal Audit Progress Report – Quarter 3 (01/10/13 – 31/12/13)**

Purpose of report: **To provide Members with a summary of the key audit findings, progress on delivery of the audit plan and the performance of the internal audit service during Quarter 3**

RECOMMENDATIONS:

- 1. Members are recommended to consider and agree any action that should be taken in response to the issues raised in any of the audits carried out during Quarter 3;**
 - 2. Identify any new or emerging risks for consideration for inclusion in the internal audit plan.**
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1. Financial Appraisal

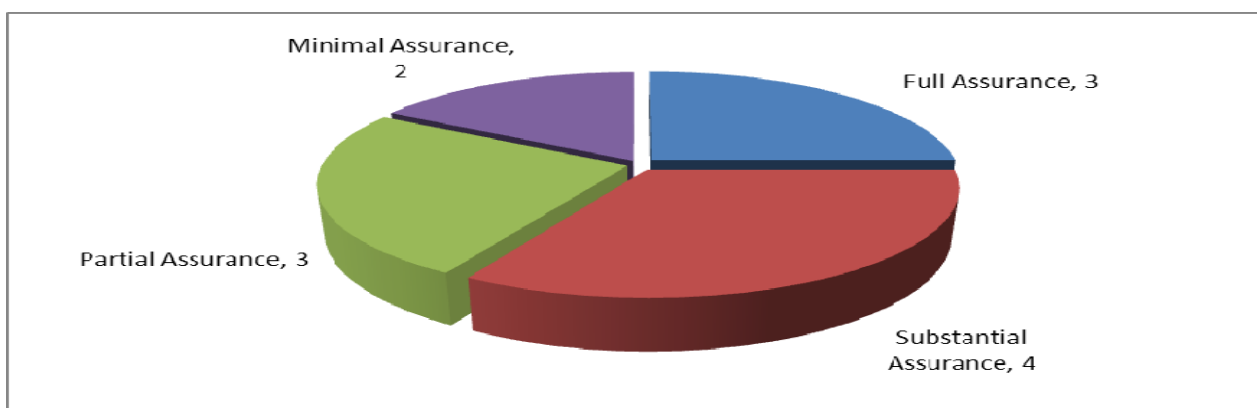
1.1 There are no direct financial implications arising from the recommendations in this report.

2. Supporting Information

2.1 The current annual plan for internal audit is contained within the Internal Audit Strategy and Annual Plan 2013-14. This was prepared after consulting Chief Officers and senior managers and was endorsed by Audit, Best Value and Community Services Scrutiny Committee (24 June 2013) and Cabinet (23 July 2013). This progress report covers work completed between 1 October 2013 and 31 December 2013.

3. Summary and Key Audit Findings

3.1 Key audit findings from final reports issued during Quarter 3 are summarised in Appendix A.



3.2 Overall, of the 12 formal audits completed, 3 resulted in a 'full assurance' opinion, 4 received 'substantial assurance', 3 received 'partial assurance' (1 of which was a school) and 2 audits received 'minimal assurance' (both of which were schools).

3.3 Whilst the same range of internal audit opinions are issued for all audit assignments, it is necessary to also consider the level of risk associated with each area under review when drawing an opinion on the Council's overall control environment. **Taking into account these considerations, the Head of Assurance continues to be able to provide reasonable assurance that the Council has in place an effective framework of governance, risk management and internal control.**

3.4 This overall conclusion has been drawn based on all audit work completed in the year to date and takes into account the management response to recommendations raised and the level of progress in subsequent implementation.

3.5 During the quarter, we have continued to identify a pattern of control weaknesses within schools and as reported previously, action is being taken in an attempt to address this through the formation of a new Schools Risk Review Group, the first meeting of which took place in November 2013. With the exception of schools, the results from our work in quarter 3 have been generally positive, with seven of the remaining nine audits receiving either full or substantial assurance.

3.6 Formal follow up reviews continue to be carried out for all audits where either 'minimal' or 'no assurance' opinions have been given and for all higher risk areas receiving 'partial' assurance. In addition, arrangements are in place to monitor implementation of all individual high risk recommendations and at the time of writing this report, all recommendations had been implemented with the exception of three which have been partially implemented. Further details of these recommendations are provided in Appendix B.

3.7 Members will recall that flexibility was built into the audit plan to allow resources to be directed to any new and emerging risks. We continue to liaise with departments to identify these but would also welcome input from Members. Details of those reviews added and removed from the plan so far this year are set out at the end of Appendix A.

4 Performance against targets

4.1 Progress against agreed performance targets (focussing on quality / customer satisfaction, compliance with professional standards, and cost / coverage) can be found in Appendix C. The majority of targets have been assessed as on target (Green), with the exception of delivery of 90% of the annual audit plan by 31 March 2014. Performance against this measure has fallen slightly as a result of needing to divert staff resources to major unplanned investigation activity during the quarter, some of which has been summarised within Appendix A. A number of audits were, however, nearing completion at the time of writing this report and we anticipate that, in the absence of any further investigation activity, the plan delivery target will be met by the end of the financial year.

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Local Members: All

Background Documents: Internal Audit Strategy and Annual Plan 2013-14

Summary of key audit findings

Supporting People System (SPOCC)

SPOCC is the Supporting People IT system used by Adult Social Care through which payments of £12.149 million were made in 2012/13. Payments are made to 41 providers ranging from four-weekly payments of between £100 and £360,000.

The key control objectives of this audit were to ensure that:

- access to the system is secure and data held is protected against loss or damage;
- only authorised staff may commit the organisation to expenditure;
- payments are made correctly, within agreed timescales and only for services received;
- there is adequate segregation of duties between the contracting and payment functions;
- data from SPOCC is transferred completely and accurately to SAP; and
- all expenditure incurred is accurately and completely recorded.

Based on the audit work undertaken during this review and our follow up of previous audit recommendations, we have been able to provide **substantial assurance** that there is a sound system of controls in place.

We found that payments are made correctly, within agreed timescales and only for services received. The main areas for improvement related to updating policy and procedural documentation and ensuring appropriate verification checks are always undertaken. All recommendations were agreed with management.

Trapeze System

Trapeze is an IT system used by the Passenger Transport Services within the Communities, Economy and Transport Department to manage the entire Passenger Transport 'procure to pay' process. This includes the transfer of data into SAP, via an interface, to enable the processing of annual payments of approximately £13m.

There are four different types of financial transactions which pass through the interface:

- Home to school transport invoices;
- Parental mileage claims;
- Public transport operator statements for contracted bus services;
- Freedom Pass statements.

A total of 2,977 financial transactions were processed through the interface and transferred onto SAP between 1st April 2013 and the 31st July 2013, involving 219 operators/claimants for a total value of £5,780,000.

In addition to covering the following key control objectives, this review sought to confirm that the recommendations made in the reviews of Home to School Transport System (January 2011) and Trapeze Application Audit (October 2012) have been implemented:

- Access to the system is secure and data held is protected against loss or damage;
- Payments are made correctly, within agreed timescales and only for services received;
- There is adequate segregation of duties between the contracting and payment functions;
- All expenditure incurred is accurately and completely recorded.

Overall, based on the audit work carried out, we have been able to provide **substantial assurance** over the control environment, with sufficient progress made on implementing previous recommendations and only a small number of further improvements being identified. These related primarily to improving system and data security, none of which were considered to be high risk in nature.

Pension Fund Investments

As part of its role as the administering authority for the East Sussex Pension Fund, ESCC is responsible, through the Pension Fund Investment Panel, for setting the investment policy and reviewing the performance of the Fund's external investment managers. Day to day management of the investments has been delegated to the external fund managers. The specialist provider of custodian services, Northern Trust, continues to be engaged by the Fund. The value of the Fund's assets, as stated in the final accounts for the year ending 31st March 2013, was £2.34 billion.

This review of Pension Fund Investments was conducted in accordance with our Pension Fund Internal Audit Strategy and covered the following key control objectives:

- All pension fund investments are completely, accurately and correctly recorded in the general ledger, including the proper segregation of ESCC and ESPF assets;
- Pension fund and fund manager performance is monitored, with appropriate action taken in the event of under- performance;
- Cash/short-term investments held by ESCC on behalf of the fund are accurately apportioned, with all income from interest and dividends received promptly and completely;
- All risks to the availability, integrity and security of data are adequately managed.

Based on the audit work and testing undertaken as part of the review, it is pleasing to report that we have been able to provide **full assurance** over the control framework with only a small number of low risk recommendations being made.

Pension Fund Governance and Strategy

This review of the Council's Pension Fund Governance and Strategy arrangements was conducted in accordance with our Pension Fund Internal Audit Strategy and covered the following key control objectives:

- There is a statement of objectives for the Fund which is linked to measurable targets and performance indicators;
- There are comprehensive risk management arrangements in place for the Pension Fund;
- The investment strategy is appropriate and strategy decisions are implemented correctly and in a timely manner;
- Management information systems provide assurance that Fund assets are invested in accordance with the investment strategy;
- Adequate reporting and monitoring arrangements are in place to monitor the performance of external advisors and service provider;
- All accounting records and statements are in accordance with the prevailing accounting standards and good practice;
- The Fund is administered in accordance with best practice and legislative requirements;
- The Fund Administrators communicate effectively and promptly with all stakeholders.

Overall, we have been able to establish, based on the testing carried out, that robust governance arrangements are in place and are therefore able to provide **full assurance** over the control environment. As with the Pension Fund Investments review, only a small number of low risk recommendations have been made, all of which were agreed with management.

Notification of Payroll Changes

During quarter 3, Personnel and Training (PAT) developed proposals to revise the arrangements by which they are notified of payroll changes by managers and by schools. The proposals focussed on streamlining and automating procedures to make them more efficient whilst still ensuring the required outcomes are achieved.

In view of the importance of ensuring payroll transactions are processed in a controlled manner, it was agreed with management that we would review the new system proposals covering the following control objectives:

- Adequate controls exist within the new “notification of changes to payroll” processes to ensure that all changes are complete, accurate, authorised, genuine, and processed correctly;
- The new system is subject to sufficient testing prior to implementation.
- All data is transferred completely and accurately into SAP;
- Access to the new processing system and associated data within it is strictly controlled and restricted to authorised individuals;
- Back-up procedures have been established and are adequate in the event of a system failure or disaster;
- Support arrangements for the new process are in place.

Overall, we did not identify any significant issues that would prevent the ‘changes to the notification and processing of contractual changes’ being rolled out across the authority and were therefore able to provide an opinion of **substantial assurance**. Only two areas for improvement were identified and agreed with management, relating to further strengthening security over personal data and producing clear documentation and guidance notes for users.

Treasury Management

The main purpose of this review, which is conducted annually, was to provide an opinion on the effectiveness of key controls in the Treasury Management system. As well as testing transactions from the current financial year, we also followed-up recommendations arising from our 2012/13 review. The control objectives of the audit were to ensure that:

- All Treasury Management transactions are authorised properly, in accordance with ESCC’s Treasury Management Policy, and are in accordance with best practice;
- All Treasury Management transactions are recorded accurately in the accounts, supporting documentation is retained for all transactions, and all transactions are recorded on a timely basis;
- All lending and borrowing decisions are based upon robust cash flow forecasting over the short, medium and long term;
- Monies are transferred only in accordance with approved policy and there is satisfactory internal control in the money transfer systems.

Based on the audit work undertaken, we have once again been able to provide **full assurance** over the control environment in this area, with only two recommendations for improvement identified, neither of which were considered to be high risk.

Appointeeships/Deputyships

When an individual loses the mental capacity to manage their own financial affairs, the Department for Works and Pensions can appoint a person to collect and administer the state benefits and pensions on the individual’s behalf. Where there is no one else to manage a client’s finances, the Council may apply for ‘corporate appointeeship’.

If a client has savings, a private bank account and a private pension or other capital, the Council also has to apply to the Court of Protection for a Deputyship Court Order. This enables the Council's Client Affairs Team to administer and manage all of the client's finances and accounts. The Appointee and Deputyship service is not a statutory Council function and cases are only taken on where the Council is the last resort and there is no-one else to help the client manage their finances.

Our audit of these arrangements has been completed as part of the agreed annual audit plan for 2013/14, the main purpose of which was to ensure that, where the Council assumes the role of corporate appointee, adequate controls are in place to effectively and efficiently manage all appointee and deputyship client accounts.

From the audit work completed, we have been able to provide **partial assurance** that there is a sound system of controls in place. The review found no evidence indicating that inappropriate decisions are being made in relation to the management and use of clients' monies. Some areas were, however, identified where the overall control framework could be strengthened further and these included:

- Ensuring that the Council has in place a clear set of policy and procedure documents that set out our specific roles and responsibilities when we assume the role of appointee or deputy for a client;
- Reviewing and evaluating alternative investment policies covering client balances over a certain financial threshold, taking into account the level of return to be obtained, the level of risk and the administrative implications;
- Strengthening controls over the submission and processing returns received from care providers;
- Exploiting opportunities to streamline working practices and avoid duplication.

All recommendations arising from our work were agreed with management and in many cases; these had already been incorporated within a formal action plan developed by the Client Affairs Team.

Families with Multiple Problems Programme

The Government's 3-year Troubled Families Programme offers attachment fees and payments to local authorities who can demonstrate that they have improved the wellbeing of families in which members are involved in crime and anti-social behaviour, are unemployed and/or missing education.

Family keywork in East Sussex (part of the 'Thrive' programme) is a multi-agency approach to improving outcomes for families identified as at risk of requiring repeated interventions or sanctions. It aims to provide earlier, coordinated and more effective support to families whilst reducing the long-term costs to local services.

In order to access the government funding, payable for both engaging with families and subsequently achieving positive results, the Council is required to submit results data quarterly to the Department for Communities and Local Government (DCLG), with the first of these being made at the end of July 2013.

Since the commencement of the programme, we have provided advice and support to Children's Services in developing appropriate mechanisms for inviting, assessing and approving applications from organisations that provide enhanced support to troubled families with funding from the Troubled Families Grant.

We also assisted the department in liaising with the DCLG to confirm the required monitoring data that local authorities should provide in order to enable the programme to be monitored and evaluated on a national level.

The main scope of this most recent review was to ensure that robust controls are in place to ensure that all data reported to the DCLG in support of the grant application is correct, and is supported by appropriate documentation.

Overall we found that adequate guidance and procedures had been developed to manage the Troubled Families Programme with our sample testing confirming that the key controls within the system are being complied with. We have therefore been able to provide **substantial assurance** over the control environment.

The main areas identified for improvement related to further strengthening data validation arrangements, covering both ESCC and partner organisations.

Oracle Database Follow Up

Internal Audit carried out a review of the adequacy and effectiveness of controls applied to the Oracle Database as part of the agreed audit plan for 2012/13. Due to the control improvements required and the partial assurance audit opinion given at that time, a follow-up review has been undertaken as part of the agreed audit plan for 2013/14.

The follow up established that two medium risk recommendations remained outstanding, relating to the application of security patches and the development of appropriate risk based performance indicators. Until such time as these issues are addressed, the audit opinion remains at **partial assurance**. Management within ICT Services have, however, committed to ensuring that both recommendations will be fully implemented by the end of January 2014.

School Audits

During the quarter, we have continued to conduct visits to schools in the County, with the individual schools selected in conjunction with the Children's Services Department on the basis of risk. In all cases, recommendations arising from our work have been formally agreed with school management.

Etchingham CE Primary School (Minimal Assurance) – Our review identified a number of key weaknesses within the school that, when combined, impacted the control environment and increased the risk of errors, fraud and loss. We found control weaknesses within the school's processes for payroll, expenditure and the operation of the School Fund.

In terms of additional hours by staff, these had not been formally approved in advance of them being worked and claim forms did not adequately specify on what basis the claims were made, increasing the risk of inappropriate claims and financial loss. We also found that funds owing to the school's official budget share had been incorrectly paid into the School Fund, and that a number of School Fund transactions were not supported by receipts or invoices.

Bodiam CE Primary School (Minimal Assurance) – As well as having concerns in relation to the resourcing of the Finance function in the school and the health and wellbeing of staff where long hours were being worked, we also identified weaknesses in relation to payroll, staff reimbursement for expenses, purchasing and associated payment authorisation controls. In addition, we found instances of budget share monies being paid into the School Fund which could lead to inaccurate financial reporting and understatement of the school's financial position.

Hazel Court Special School (Partial Assurance) – Our review found weaknesses in relation to the expenditure and payroll process, the administration of the School Fund and the security of assets, resulting in an opinion of partial assurance. Specifically, there was a need to introduce a separation of duties within payroll and School Fund operations, and also to ensure that all payroll claim forms are formally authorised prior to being processed.

Investigations

During the quarter, we were contacted by staff within Adult Social care regarding concerns over a service user who was in receipt of a direct payment to which they may not have been entitled. The individual concerned was receiving substantial funding from both ESCC and the Independent Living Fund (part of the Department of Work and Pensions) in order to procure their own care. This care was required as a result of the individual claiming to suffer from severe levels of physical incapacity.

Following preliminary enquiries, involving an analysis of all available documentation and interviews with potential witnesses, a Magistrates Court approval was obtained to conduct directed surveillance under the Regulation of Investigatory Powers Act. This was subsequently undertaken using specialist consultants and resulted in clear evidence to show that the individual was not entitled to the level of funding being provided and was not receiving the levels of care which they claimed were being provided. As a result, all of our evidence was handed over to Sussex Police, who have arrested both service user and the alleged carer. Both have been bailed whilst the criminal investigation continues. As with any case of this kind, we will work with both the Police and Legal Services in an attempt to recover all financial losses to the authority.

Additional Audit Reviews

Through discussions with management, the following reviews have been added to the audit plan during the course of the year on the basis of risk (see 3.7 above):

- Milton Grange Care Home
- Phoenix Arts Centre, William Parker Sports College
- Deceased Client Notifications
- SAP Interfaces
- Oracle Database Follow Up
- Conflicts of Interest Administration
- Waste – Income Generation from the Energy Recovery Facility (ERF)
- Nursery Income Follow-Up
- EXOR Follow-Up

The following audits, originally scheduled for 2013/14, have been deferred to 2014/15, primarily in order to allow resources to be focussed on emerging higher risk areas and unplanned investigations. In all cases, these have been agreed with both the Chief Finance Officer and senior departmental managers:

- Capital Programme Project Management
- Children's Centres – Governance and Financial Management

High risk recommendations where implementation is overdue / unconfirmed

Action has been taken against all of the high risk recommendations due to be implemented, with the majority of these now fully in place.

Two recommendations arising from the audit of the Administration of Looked After Children (LAC) Funds have been partially implemented. We understand from management that staff have researched and devised an appropriate system to support the recommendations relating to the adoption of amendments to existing procedures and the maintenance of a central record of savings held by LAC. As reported on in quarter 2, these are due to be fully embedded during February 2014.

The final overdue recommendation relates to Ringmer Primary School where there had been a significant delay on producing and auditing school fund accounts. We understand that the accounts have now been produced and are in the process of being audited. They are due to be signed off by the governing body in February 2014.

Internal Audit Performance Indicators

Measure	Source of Information	Frequency	Specific Measure / Indicator	RAG Score	Actual Performance
Client Satisfaction					
Chief Officer/DMT	Consultation / Survey	Annual	Confirmation of satisfaction with service quality and coverage and feedback on areas of improvement.	G	Confirmed as part of audit planning process and on-going liaison. Improvement actions built into business plan.
Client Managers	Satisfaction Questionnaires	Each Audit	>89%	G	100%
Section 151 Officer and other Client Assistant Directors	Liaison Meetings	Quarterly	Satisfied with service quality, adequacy of audit resources and audit coverage.	G	Confirmed through on-going liaison.
ABV&CSSC	Chairs Briefing and Formal Meetings	Quarterly / Annual	Confirmation of satisfaction with service quality and coverage and feedback on areas of improvement.	G	Confirmed through annual review of effectiveness and feedback from committee as part of quarterly reporting.
Cost/Coverage					
CIPFA Benchmarking	Benchmarking Report and Supporting Analysis Tools	Annual	1. Cost per Audit Day; 2. Cost per £m Turnover; equal to or below all authority benchmark average	G	1. £316 against average of £325 2. £559 against average of £1,004
Local and National Audit Liaison Groups	Feedback and Points of Practice	Quarterly	Identification and application of best practice.	G	Ongoing via attendance at CCAN, HCCIAG and SAG.
Delivery of the Annual Audit Plan	Audits Completed	Quarterly	90% of audit plan completed.	A	63.9% against a Q3 target of 67.5%. This is mainly due to a large proportion of time spent on investigation activity within the quarter. A number of reviews were also close to completion at the end of the quarter.

Measure	Source of Information	Frequency	Specific Measure / Indicator	RAG Score	Actual Performance
Professional Standards					
Compliance with professional standards	Self-Assessment against new Public Sector Internal Audit Standards	Annual	Completed and implementation of any actions arising.	G	Self assessment completed and action plan for improvement currently being developed.
External Audit Reliance	Fundamental Accounting Systems Internal Audit Activity	Annual	Reliance confirmed	G	Confirmed in the Annual Audit Letter November 2013.