

Report to: **Audit, Best Value and Community Services Scrutiny Committee**
Date: **17 March 2015**
By: **Chief Operating Officer, Business Services Department**
Title of report: **Internal Audit Progress Report – Quarter 3 (01/10/14 – 31/12/14)**
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. Background

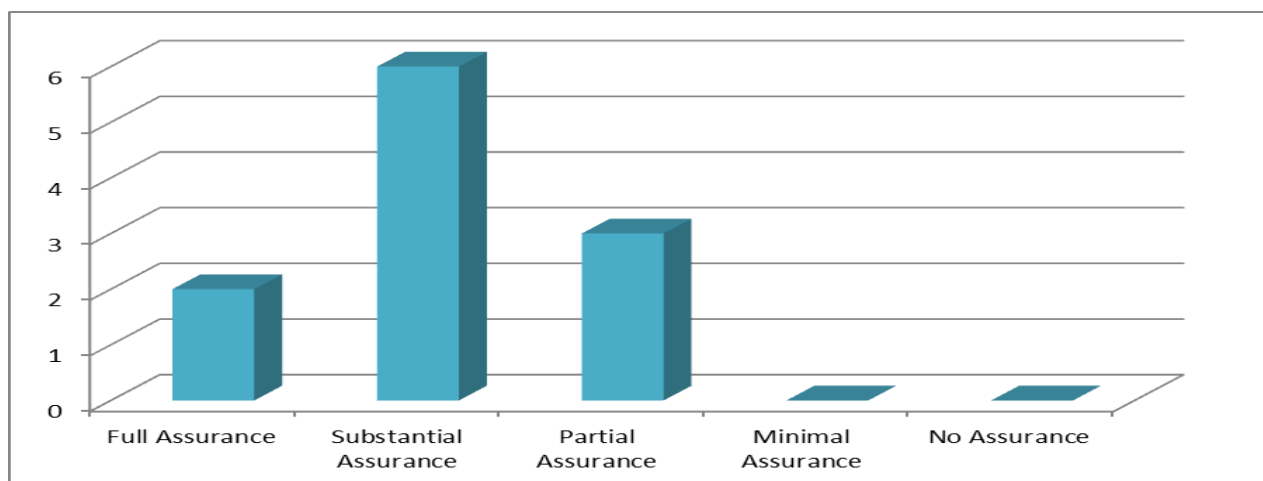
1.1 This progress report covers work completed between 1 October 2014 and 31 December 2014 and follows previous update reports relating to quarters 1 and 2 of 2014/15.

2. Supporting Information

2.1 The current annual plan for internal audit is contained within the Internal Audit Strategy and Annual Plan 2014-15. This was prepared after consulting Chief Officers and senior managers and was endorsed by Audit, Best Value and Community Services Scrutiny Committee (10 June 2014) and Cabinet (01 July 2014).

3. Conclusion and Reasons for Recommendation

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



3.2 Overall, of the 11 formal audits completed, 2 received a 'full assurance' opinion, 6 received 'substantial assurance' (2 of which related to schools) and 3 received 'partial assurance'. It is pleasing to report that none of the reviews completed during this most recent period have resulted in audit opinions of 'minimal' or 'no' assurance. In the three instances of partial assurance being given (SAP Security and Administration, ICT Change Control, Patch and

Release Management and School Funds), we have obtained a commitment from management to address the required actions as a priority and will be undertaking further follow-ups in due course to ensure that this takes place.

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 The 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 Since our previous report to this committee, further action has been agreed in order to strengthen the financial governance in schools. Specifically, one off funding has been secured in order to develop and deliver a comprehensive training programme for governors, headteachers and school business managers. This training will be developed jointly between BSD Finance, Internal Audit and Children's Services and will be supplemented with an extended programme of school audits. The audit programme will be based on a random sample of schools across the County with the objective of assessing the current standards of financial governance, which can then be followed by a similar exercise, once the training has been rolled out, in order to assess its impact and effectiveness.

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 due had been implemented.

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 this committee. Details of those reviews added and removed from the plan so far this year are set out at the end of Appendix A.

3.8 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 2015. Whilst this is the case, it is important to highlight that at the time of writing this report, a total of eleven audit reports had been produced in draft and were with clients awaiting imminent finalisation. These have not been taken in account when producing the results for quarter 3 so we remain confident of achieving the 90% plan completion target by 31 March 2015.

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BACKGROUND DOCUMENTS: Internal Audit Strategy and Annual Plan 2014-15

Summary of Key Audit Findings

Treasury Management

The purpose of this audit was to review and assess controls employed by management to ensure the effective management of risk to the County Council's financial assets (cash). This included a review of controls around the use of Natwest Bankline for the online movement of funds.

Overall, we found that Treasury Management controls continue to be robust and we were able to provide a **full assurance** opinion. Two minor issues arose during the audit regarding the maintaining of appropriate segregation of duties (especially as the Council moves towards Agile working arrangements) and security controls around the cash flow spreadsheet. The recommendations relating to these areas are due to be implemented in full by January 2015.

Pension Fund Governance and Strategy

ESCC has a statutory responsibility to administer and manage the East Sussex Pension Fund. The scheme provides retirement benefits for County Council employees and also for employees of Brighton & Hove City Council, the five borough and district councils in East Sussex, together with various other scheduled and admitted bodies. Responsibility for the overall direction of the Fund's investment policy lies with the Pension Fund Investment Panel (PFIP). Day to day management of the investments has been delegated to external fund managers, who report to the PFIP quarterly on their activities.

The introduction of the Public Service Pensions Act 2013 is resulting in a number of changes to local government pensions' governance arrangements. From April 2015, a Local Pensions Board will have to be in place, supported by a Pensions Committee. These will replace the Pension Fund Investment Panel and the role carried out by the Governance Committee. A timetable has been drawn up to make these changes, including the appointment of Pension Board members.

Overall, we were able to provide an opinion of **full assurance** in relation to the system of internal control for pension fund governance and strategy. Whilst this is the case, we have found it necessary to repeat a small number of recommendations arising from our previous audit which had still to be implemented in full. In doing so, we acknowledge that these are of a low risk nature and that management attention has been focussed on preparing for the upcoming changes referred to above.

SAP Security and Administration

SAP is the Council's main accounting and financial system and it is therefore essential that the risks in relation to security and administration are managed effectively. A failure to properly control access rights and security could result in financial loss and unauthorised access to sensitive data. Inadequate control could also lead to reputational damage and potential fines/litigation where there is non-compliance with data protection laws.

Overall, our work identified a number of opportunities for improvement which would help to reduce the risk exposure to the Council. An audit opinion of **partial assurance** was therefore provided, with the main areas for improvement relating to:

- enhancing overall governance of the SAP security and administration control environment, which was found to be somewhat diluted due to a fragmentation of responsibilities between different teams;
- ensuring that appropriate mechanisms are in place to manage and monitor the allocation and use of the many SAP roles and transactions that exist and the division of duty conflicts that can occur within these;
- reviewing SAP workflow levels and approval responsibilities to ensure their continued appropriateness to the business;
- ensuring that the audit trail policy around key data items and retention periods is adequate and properly implemented.

Recommendations relating to these and other areas were agreed in full with management. In all cases, these are due to be implemented by 31 March 2015 and will be followed up by Internal Audit as part of our 2015/16 annual audit plan. It should be noted that, in the case of the overall governance weaknesses referred to above, an alignment of SAP teams has already taken place which has served to address the issues raised.

ICT Change Control, Patch and Release Management

Change, patch and release management processes and procedures are key areas within any ICT division and affect the efficient and effective running of ICT services. Such procedures are designed to preserve the integrity and stability of information systems and incorporate processes to identify, assess, improve and implement changes to these.

This audit reviewed the controls in place in relation to change, patch and release management, with specific focus on how well the Council is performing compared to the Information Technology Infrastructure Library (ITIL) best practice approach to ICT service management. This is a widely accepted framework to help organisations assess, improve and develop ICT service management.

Overall, and despite a number of areas of good practice being identified, a **partial assurance** audit opinion was provided due to improvement in various areas being required. In summary, these relate to:

- developing and documenting formal operational procedures for defining, designing, building and rolling out releases to the Council;
- establishing clear roles and responsibilities for release management;
- establishing operational procedures for software release and distribution;
- assessing, documenting and approving back-out plans (the processes required to restore a system to its original or earlier state in the event of a failed or aborted implementation), test plans and acceptance criteria for all release management activities;
- ensuring there is a defined process to collate information regarding software licences, where there is currently a risk that unlicensed software may not be identified.

The review also highlighted the need to review and update the change management policy on an annual basis to ensure it is up-to-date, relevant and fit-for-purpose, and also to ensure that all changes are properly scheduled so that the business is not unduly disrupted.

All of the recommendations made as part of this review were agreed with management. In relation to the specific issues around release management, management have confirmed that with immediate effect, all releases will be subject to the formal change management process until such a time that release management has been formally differentiated from the change management process. In terms of this and also the need for closer alignment with the ITIL framework, ICT Services are going through a period of review and envisage new processes and improved compliance with best practice will be achieved during the course of 2015/16.

Purchasing Cards

Purchasing cards (P-Cards) are used at the County Council to allow employees more flexibility when purchasing goods and services via the internet or from local suppliers. They can also enable more efficient and better value purchasing. As of September 2014, there were approximately 530 P-Card holders across the Council, including schools.

The purpose of this audit was to provide assurance that P-Cards are only issued to appropriately authorised and trained staff and are used only to purchase goods and services that are wholly, exclusively and necessary for the use of the Council, and offer best value. The scope of our work incorporated transactions carried out between April 2013 and September 2014, during which over 31,000 P-card transactions took place, amounting to expenditure of £2.7m.

Overall, we found the P-Card control framework to be robust, particularly in relation to the issuing of cards and the provision of appropriate training. We were, therefore, able to provide an opinion of **substantial assurance**.

However, we also identified opportunities to strengthen the P-Card monitoring and review process, specifically in relation to ensuring that purchases are only made in accordance with policy. Detailed transaction testing identified a number of instances where transactions were potentially in breach of policy and have therefore been referred back to departments for clarification as to the specific nature of the purchases and the basis on which they were subsequently approved. This work is ongoing, but in the meantime, all P-Card users and reviewing managers have been reminded of the need to ensure all purchases comply with Council policies and procedures.

THRIVE Programme

Thrive is a three-year programme to improve the system of support for vulnerable children and young people in East Sussex, running from 2012 to 2015. The long term aim of the programme is to ensure that the Council has a financially sustainable children's safeguarding system which acts in a proportionate, timely and effective way to reduce children's and young people's needs.

As part of the phased development of THRIVE, we have provided support, advice and assurance that new systems and working practices are introduced in a controlled manner. The scope of this particular audit was to ensure that, as THRIVE draws to a close in March 2015, adequate transition arrangements are in place to ensure that risks are managed effectively.

Overall, we were able to provide an opinion of **substantial assurance**, noting that adequate steps have been taken to manage the process of concluding the project and identifying areas where support will be needed to meet continuing demand. It was pleasing to note that:

- an exit strategy had been developed to manage risk as the THRIVE project comes to an end and this is being monitored by management;
- a post project review to evaluate the effectiveness of THRIVE is being prepared and will be finalised in June 2015;
- recommendations made in the previous audit report have been implemented in full.

We did, however, make some minor recommendations relating to:

- the need to continue to hold Executive Board and Programme Team meetings until the end of the project to help ensure the effective implementation of transition arrangements and the mitigation of risks;
- ensuring that the internal budget monitoring of THRIVE includes actuals derived from the Council's main financial system, SAP, so that THRIVE investment and pressure expenditure is correctly reported within the post project review.

Contract Management Follow-Up – Apetito

A contract management review on the Apetito contract was completed in March 2014 as part of a wider corporate review of contract management arrangements within the Council. At the time, we were only able to give a minimal assurance audit opinion on the overall effectiveness of controls and identified a number of areas of concern where improvements were necessary.

A follow-up review was therefore completed to provide assurance that the recommendations made previously and agreed with management had been adequately implemented.

We found that significant progress had been made in implementing the recommendations, specifically in relation to improving governance arrangements, including the development and implementation of a contract management plan with clearly defined roles and responsibilities, decision-making protocols and performance and financial management arrangements. As a result, we have now been able to provide an opinion of **substantial assurance**.

Some opportunities for further improvement were found to exist; the most important of which were to ensure that agreed performance indicators are sufficient to enable effective monitoring of the contract and that performance against these is measured on a regular basis to enable appropriate remedial action to be taken where necessary. Opportunities to improve risk management were also identified. In all cases, the recommendations have been agreed with management and are due to be implemented before the end of March 2015.

Cultural Compliance Review – The Customer Services Group

The 2014/15 internal audit plan includes specific reviews of individual service areas' compliance with a range of key Council policies and procedures, including obtaining assurance that each service area has robust management and supervisory arrangements in place. The areas covered include management and control of:

- Annual leave;
- Staff travel and expenses;
- Timesheets and claim forms;
- Council equipment and other resources;
- Gifts and hospitality;
- Conflicts of interests.

An individual report is produced for each service area reviewed and, once these have all been completed, an overall report will be produced identifying key themes.

The first of these reviews has been completed within the ESCC Customer Services Group within the Economy, Transport and Environment Department. This team provides one of the first points of contact for many of the people who wish to talk to the Council, via the contact centre in Ringmer, including responding to queries, fault reports and complaints from the public relating to a range of services.

Based on the audit work carried out, we found that staff work in compliance with Council policies and procedures and we were able to provide an opinion of **substantial assurance** as a result. Some minor opportunities for improvement were, however, identified. These related to ensuring all staff complete an annual declaration of interests and that, where positive declarations are made, appropriate safeguards are considered and implemented where necessary. These actions were agreed in full with management.

School Funds

In addition to their Budget Shares, most schools operate private (or voluntary) funds, which they manage themselves. These funds, known as School Funds, are separate from the Budget Share and have separate bank accounts, but are operated by school staff as part of their normal duties.

Recent school audits have highlighted instances of poor practice in some schools in relation to School Funds; in particular, we have found examples of inappropriate expenditure (including cash payments to staff), a failure to report School Fund accounts to governors and of excessively high School Fund balances.

The main purpose of this audit was to ascertain whether these issues are representative of schools as a whole. A sample of ten schools (two secondary, six primary and two special) was selected, including some that were pending academy conversion.

From the work carried out, we have provided an audit opinion of **partial assurance**. Whilst this opinion was based on the sample of schools chosen, instances of poor practice found in other audits serve to further highlight the risks associated with the operation of school funds, which are often not subject to the same level of control as official Budget Share funds. There is potential for reputational damage to schools or the Council where School Fund money is used inappropriately and/or not for the benefit of pupils.

Areas for improvement included the need for each school to:

- define the purpose and objectives of having a School Fund;
- establish guidance over the administration of the School Fund;
- ensure School Fund monies are used appropriately and for the benefit of the pupils;
- ensure there is a process in place to approve the payment of School Fund invoices;
- improve the receipting process for School Fund income, so that income received can be reconciled to income banked;
- ensure an appropriate segregation of duties is in place;
- present audited accounts to school governing bodies within the defined timeframes, and for governors to challenge where this doesn't happen;
- ensure School Fund balances are not excessive.

A formal action plan covering the above areas has been agreed in full with management, most of which relates to strengthening and re-issuing guidance to all schools.

Individual School Audits

During the quarter, we have continued to conduct visits to schools in the County, with the individual schools selected through the Schools Risk Review Group (made up of representatives from Internal Audit, Personnel and Training, Finance and the Standards and Learning Effectiveness Service) on the basis of risk. Follow-up reviews have also been completed where appropriate. In all cases, recommendations arising from our work have been formally agreed with school management, with copies of all audit reports now sent directly to all members of each school's governing body. We also prepare a summary of the report for the relevant local Member where the audit opinion is below partial assurance. This is in addition to the quarterly bulletins we provide to governors which highlight common themes and issues arising from our work which we recommend they seek assurance on within their own schools.

The following school audits have been completed in the quarter.

School	Opinion	Key Findings
Uckfield Community Technical College – Follow-Up Review	Substantial Assurance	<p>Significant improvement on the previous opinion of minimal assurance. Some areas for further improvement remain, including the need to ensure:</p> <ul style="list-style-type: none"> • invoices are approved in accordance with School Financial Regulations; • claims for reimbursement are properly approved in line with the school’s Scheme of Delegation; • an up-to-date lettings policy is in place and that all lettings are properly approved; • an up-to-date asset register is maintained which is checked and certified correct on an annual basis.
Etchingham CE Primary School Follow-Up	Substantial Assurance	<p>We found that the school has made significant progress in implementing the recommendations made previously. Only a few areas for further improvement remained, including the need to:</p> <ul style="list-style-type: none"> • review and approve the Staffing Committee’s terms of reference; • ensure all payments are certified in accordance with the school’s Scheme of Delegation; • raise official orders for all goods, works and services required by the school at the time these are ordered with the supplier.

Investigations

Mileage Overclaims

Following a referral from Personnel and Training, an internal audit investigation was undertaken in relation to the submission and payment of potentially over-inflated and/or false mileage claims by a member of staff in Adult Social Care. In reviewing the staff member’s mileage over a period of approximately four years, it was confirmed that inflated mileage had been claimed and paid, resulting in an overpayment of approximately £1,000 during this period.

The individual concerned is no longer employed by the County Council and work is underway to recover the amounts overpaid.

Other Investigations

In addition to the case referred to above, work has been taking place on a number of other investigations during the quarter. Whilst we have completed our work on some of these, due to ongoing disciplinary processes and court action, we are unable to report further details at this stage.

It is important to note that at the conclusion of all formal investigations, a determination is made by management, in conjunction with Personnel and Training, Internal Audit and Legal Services where appropriate, as to what action should be taken in response. This determination takes into account a range of factors, including the seriousness of the case, the financial values involved and the standard of evidence available.

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):

- Lease Cars;
- Chyngton Primary School ICT Services;
- Annual Governance Statement;
- Bus Services Operators Grant;
- Procurement Cards;
- E-Recruitment iGrasp Replacement.

In agreement with management, the following audits have been removed from the 2014/15 audit plan and will be considered for inclusion in the 2015/16 plan as part of the overall risk assessment completed during the planning process.

- Procurement Shared Services;
- Procurement Standing Orders;
- Integrated Waste Management Services Contract.

High risk recommendations where implementation is overdue / unconfirmed

Action has been taken against all of the high risk recommendations due to be implemented.

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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 through Chief Officer consultations in February / March 2014, where high levels of satisfaction confirmed.
Client Managers	Satisfaction Questionnaires	Each Audit	>89%	G	100%
Section 151 Officer	Liaison Meetings	Quarterly	Satisfied with service quality, adequacy of audit resources and audit coverage.	G	Confirmed through ongoing liaison throughout the year and via approval of audit strategy and plan.
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 (to be reviewed for 2015/16)	Annual	1. Cost per Audit Day; 2. Cost per £m Turnover; equal to or below all authority benchmark average	G	Opportunities to improve benchmarking being explored. Last results available are for 2012, these show: 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	On-going via attendance at County Chief Auditors Network, Home Counties Audit Group and Sussex Audit Group.
Delivery of the Annual Audit Plan	Audits Completed	Quarterly	90% of audit plan completed.	A	62.2%.

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, improvement plan in place and being actioned.
External Audit Reliance	Fundamental Accounting Systems Internal Audit Activity	Annual	Reliance confirmed	G	Confirmed as part of BDO Annual Governance Report.