Title of paper:	**INTERNAL AUDIT ANNUAL REPORT 2016/17**	
Director(s)/ Corporate Director(s):	Geoff Walker Director of Strategic Finance	**Wards affected: All**
Report author(s) and contact details:	Shail Shah Head of Audit and Risk 0115 8764245 shail.shah@nottinghamcity.gov.uk	
Other colleagues who have provided input:		
Recommendation(s):		
1	Note the audit work completed during the year. .	
2	Note the Head of Audit and Risk's Annual Opinion.	
3	Select up to two audits from Appendix 3 for examination at the November meeting and enquire and receive any assurance from the Head of Internal Audit regarding the limitation of scope and resources	

1   REASON FOR RECOMMENDATIONS

1.1   This report outlines the work of the Internal Audit (IA) service at the end of the fourth quarter 2016/17. The report includes the Head of Audit and Risk's (HoIA) annual opinion on the effectiveness of the internal control systems operating within the City Council and its significant partnerships.

1.2   The Accounts and Audit Regulations 2015 state that local authorities 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 (PSIAS) or guidance.

1.3   The Audit Committee's Terms of Reference include receiving an annual report on the work of IA.

1.4   The Public Sector Internal Audit Standards (PSIAS) require the responsibility for the management of Internal Audit to be set with the Board. In practical terms, this Board responsibility is vested in the Audit Committee and Section 151 Officer who exercise their Board responsibility via the Constitution and the associated policies and procedures of the City council.

1.5   The PSIAS require the HoIA to deliver an annual audit opinion and report that can be used to inform the Annual Governance Statement. The annual report should include a summary of the work supporting the opinion.

2 BACKGROUND

2.1 The IA service impacts on corporate objectives by bringing a systematic disciplined approach to improve the effectiveness of risk management control and governance processes and is an important part of the Council's governance and control framework.

2.2 The coverage set out in the 2016/17 Audit Plan has been substantially achieved and the associated Performance Indicator targets have been met.

2.3 The assurance gained from this activity, together with that gained from a review of other control and assurance mechanisms, has enabled the HoIA to give a reasonable assurance that the internal control systems are operating effectively within the Council and its significant partnerships.

3 REVIEW OF THE YEAR

3.1 Reports to the Audit Committee

An important part of the IA service is to inform the Audit Committee about the adequacy of the Council's governance and internal control systems and an important role of the Committee is to oversee the performance of the IA service. Table 1 summarises the information the Committee has received from the HoIA during the last year.

TABLE 1: REPORTS FROM HEAD OF AUDIT AND RISK	
Report	**Purpose**
Annual Governance Statement	Informed councillors about the overall control environment.
Internal Audit Quarterly Reports	Allowed the Committee to review the performance of the service.
Internal Audit Reports Selected for Examination	Allowed councillors to gain a detailed view of some of the services reviewed and gain a clear insight into how and why work was undertaken.
Role of Audit Committee and Work Programme	Helped the Committee to determine a work programme aligned to its Terms of Reference.
Internal Audit Charter	Informed the Committee of the rationale underpinning the service, the standards it would meet, and the way it interfaced with the City Council and its partners.
Internal Audit Annual Plan	Informed councillors of the impending work programmes and how this and future work impacted on the Council Plan.
Internal Audit Annual Report	Gave the Committee an overview of the work undertaken by IA and gave the HoIA's opinion in respect of the Council's overall control environment.
East Midlands Shared Services (EMSS) Annual Report and HoIA Assurance	Informed councillors of the work East Midlands Shared Services (EMSS) operations and the associated governance arrangements.
Committee Member training	Overview for the Committees regarding the committee governance framework in place performance and the Council's associated assurance arrangements

4 ORGANISATIONAL INDEPENDENCE

4.1 The PSIAS require that the Head of Internal Audit must confirm to the Audit Committee at least annually, the organisational independence of internal audit activity. The Internal Audit Charter and the council's Financial Regulations re-inforce this requirement. The Internal Audit Charter has been revised as a consequence of the PSIAS external assessment and is submitted to this committee for approval.

4.2 The Charter specifies that the Head of Internal Audit must report to a level within the council that allows internal audit to fulfil its responsibilities. Appropriate reporting and management arrangements are in place within NCC that preserve the independence and objectivity of the Head of Internal Audit.

4.3 The reporting and management arrangements in place are appropriate to ensure the organisational independence of the internal audit activity. Robust arrangements are in place to ensure that any threats to objectivity are managed at the individual auditor, engagement, functional and organisational levels. Nothing has occurred during the year that has impaired my personal independence or objectivity nor has there been any inappropriate scope or resource limitations.

5 SERVICE QUALITY AND COMPLIANCE WITH PSIAS

5.1 The service works to a charter endorsed by the Audit Committee. This charter governs the work undertaken by the service, the standards it adopts and the way it interfaces with the Council. IA colleagues are required to adhere to the code of ethics, standards and guidelines of their relevant professional institutes and the relevant professional auditing standards.

5.2 The Public Sector Internal Audit Standards (PSIAS) introduced a mandatory requirement for an external assessment of an organisation's internal audit function, which has to be completed once every five years by a qualified, independent reviewer from outside of the organisation. We completed a detailed self-assessment against the requirements of the standards, after which Birmingham City Council completed an external assessment in March 2017 and concluded that the section "mostly conforms to the requirements of the PSIAS."

5.3 The report produced by the team from Birmingham City Council was finalised with an agreed action plan. The recommendations from this report, along with improvements highlighted by our own self-assessment have been combined into an Improvement Plan. Copies of the Improvement Plan will be provided to members and will be available upon request. To date, good progress has been made in implementing the agreed improvements and we will continue to work on the outstanding issues throughout 2017.

5.4 The highlighted improvements include the need for an Assurance Framework to be developed by the Council and reported to the Audit Committee. We will report to this committee as this work progresses throughout the year.

5.5 It is a requirement of the PSIAS that the Chief Audit Executive (Head of Internal Audit) must develop and maintain a quality assurance and improvement programme (QAIP) that covers all aspects of the internal audit activity (Appendix 1).

5.6 The service has met the requirements of the Accounts and Audit Regulations 2015 and associated regulations in respect of the provision of an IA service. The service has internal quality procedures and is ISO9001:2008 accredited.

6 INTERNAL AUDIT ACTIVITY

The following outlines the IA work completed in 2016/17.

6.1 Local Performance Indicators

Table 2 illustrates how the service has met its key quality and output objectives as reflected in its Charter and agreed by the Committee.

TABLE 2: PERFORMANCE OUTTURN				
Indicator		**Target**	**Actual Year**	**Comments**
1.	% of all recommendations accepted	95%	98%	Above Target
2.	% of high recommendations accepted	100%	99%	Reasons known, in tolerance
3.	Average number of working days from draft agreed to the issue of the final report assurance	8 days	2 days	Above Target
4.	Number of key / high risk systems reviewed	11	11	
5.	% of colleagues receiving at least three days training per year	100%	100%	
6.	% of customer feedback indicating good or excellent service	85%	99%	Above Target

6.2 Resources Used

Colleagues in post are professionally qualified and/or have extensive practical experience in the public sector. All colleagues participated in personal development reviews and most received at least three days training according to business needs. The predicted outturn after adjustments for 2016/17 is in accordance with the budget. The 2016/17 internal audit plan contained 1990 days and I am satisfied that there were adequate staffing resources available to me to deliver the plan.

6.3 Audit Plan

6.3.1 The Audit Plan and quarterly monitoring reports were presented to the Committee throughout the year, detailing progress against the Plan.

Table 3: Plan Outturn		
Total Planned Days	**Actual End of Year**	**Comments**
1990	**2072**	

6.3.2 The final outturn for 2016/17 is given in **Table 3** above and the audit coverage across departments and other service areas is shown in **Diagram 1** and **Appendix 4** gives a

summary of the outturn against planned resources .This diagram illustrates that there was no significant variation from plans endorsed by the Committee.

Diagram1 Internal Audit Plan against Actual 2016/17

6.3.3 Appendix 2 and Appendix 3 give details of the reports issued in the final quarter of the year. These appendices are the final reports in the quarterly IA performance monitoring cycle undertaken by the committee. They contain details of the recommendations made and levels of assurance given. Appendix 5 provides details of all final reports issued in 2016/17

6.3.4 Actual planned days have been sufficient to substantially complete the Audit Plan. Appendix 4 contains the summarised plan and outturn. In accordance with normal practice, the plan was flexed during the year and changes were reported to the Committee.

6.4 **Recommendations analysis by risk**

Table 4 shows the total of all recommendations made in the period. Overall recommendations performance is above the IA target of 95%.

TABLE 4: RECOMMENDATIONS ACCEPTED DURING 01/01/2017 TO 31/03/2017				
	2016/17		**Jan- Mar**	
	All	**High**	**All**	**High**
Total recommendations made	286	90	48	13
Rejected	7	1	0	0
Total recommendations accepted	279	89	48	13
Percentage accepted	98%	99%	100%	100%

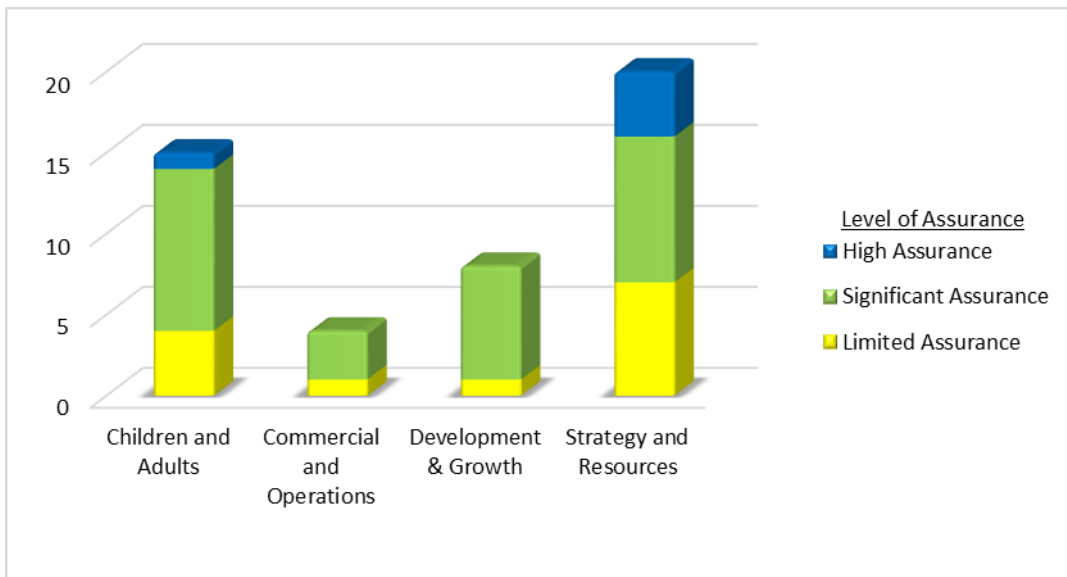6.5 **Level of Assurance Given in Audit Reports**

6.5.1 The committee sees a list of all audit reports, level of assurance and the associated high risk recommendations as part of its annual work programme. Below is a summary of the work reported in the year.

6.5.2 The level of assurance given is derived from the findings based on the following definitions:

TABLE 5 : DEFINITIONS OF ASSURANCES GIVEN IN IA REPORTS	
Level of Assurance	**Definition**
High	High assurance that the system of internal control is designed to meet the organisation's objectives and controls are consistently applied in all the areas reviewed. Our work found some low impact control weaknesses which, if addressed, would improve overall control. These weaknesses are unlikely to impair the achievement of the objectives of the system.
Significant	Significant assurance that there is a generally sound system of control designed to meet the organisation's objectives and that controls are generally being applied consistently in the areas reviewed. However, some weakness in the design or inconsistent application of controls put the achievement of particular objectives at risk.
Limited	Limited assurance as weaknesses in the design or inconsistent application of controls put the achievement of the organisation's objectives at risk in the areas reviewed.
No	No assurance as weaknesses in control, or consistent non-compliance with key controls, could result in failure to achieve the organisation's objectives in the areas reviewed.

6.5.3 Diagram 2 illustrates the assurance given to Corporate Directors during the year.

Diagram 2: IA assurances given by department 2016/17

6.5.4 A level of assurance was given in all the reports issued and no report was issued with "no assurance". The diagram reveals a consistent picture of assurance across the directorates. The assurance given informs Corporate Directors' opinion of their corporate governance arrangements and ultimately helps them give assurance for the Annual Governance Statement. For those areas receiving significant and limited assurances, recommendations were made to address the issues and risks identified. The HoIA judges that the action taken to date to address these issues has been proportionate and timely enough to mitigate the risks involved.
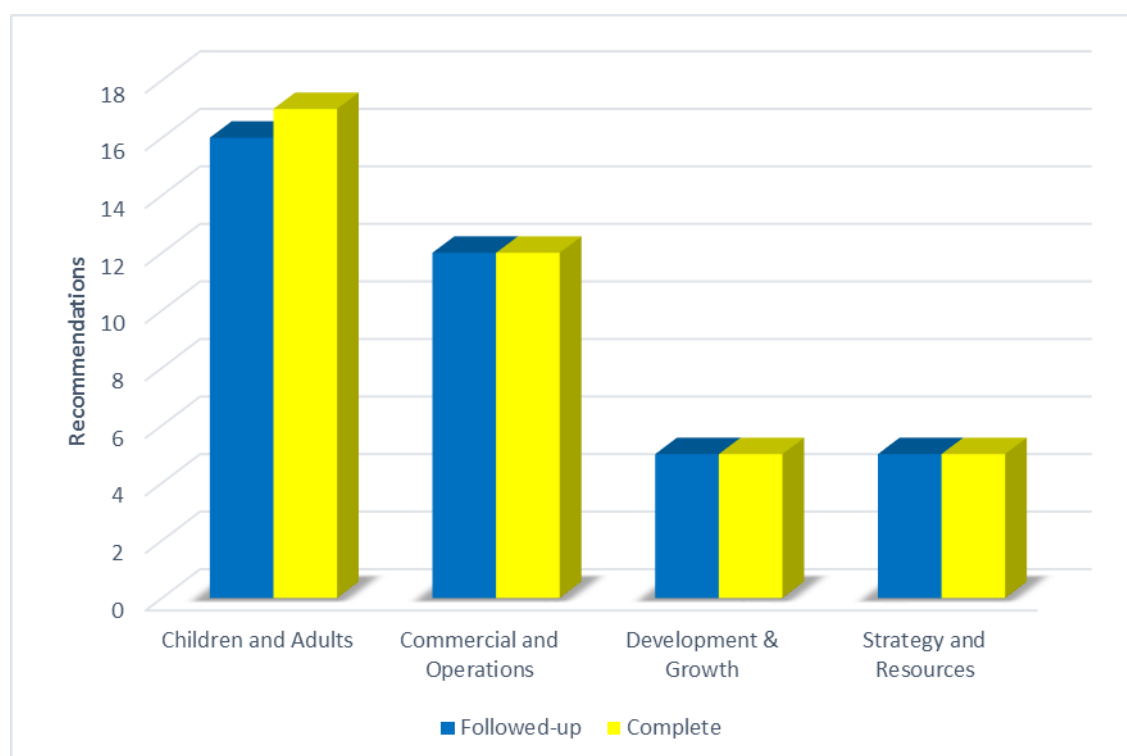
6.6 **Recommendations made**

6.6.1 Recommendations are prioritised according to their risk rating in accordance with the definitions in the table below.

| TABLE 5 : DEFINITIONS OF RISK PRIOTIES USED IN IA REPORTS	
Priority	**Definition**
High	A fundamental weakness which presents material risk to the audited body and requires urgent attention by management.
Medium	A significant weakness whose impact or frequency presents an unacceptable risk to the audited body that should be addressed by management.
Low	The audited body is not exposed to any significant risk, but the recommendation merits attention.

6.6.2 IA monitors the progress made by clients by undertaking follow up audits which assess the success in implementing the recommendations made. The position for the year, based upon the follow up audits completed, is summarised in Diagram 3.

Diagram 3: Results of Follow Up Audits

6.6.3 Diagram 4 illustrates the position on high risk recommendations made, analysed by client directorate. The Committee sees all reports issued and the associated high risk recommendations as part of its quarterly review of IA performance. Systems are in place to monitor these recommendations, and those outstanding beyond their target date are reported to the responsible colleague nominated in the agreed action plans for their follow up.

Diagram 4: Progress on High Risk Recommendations
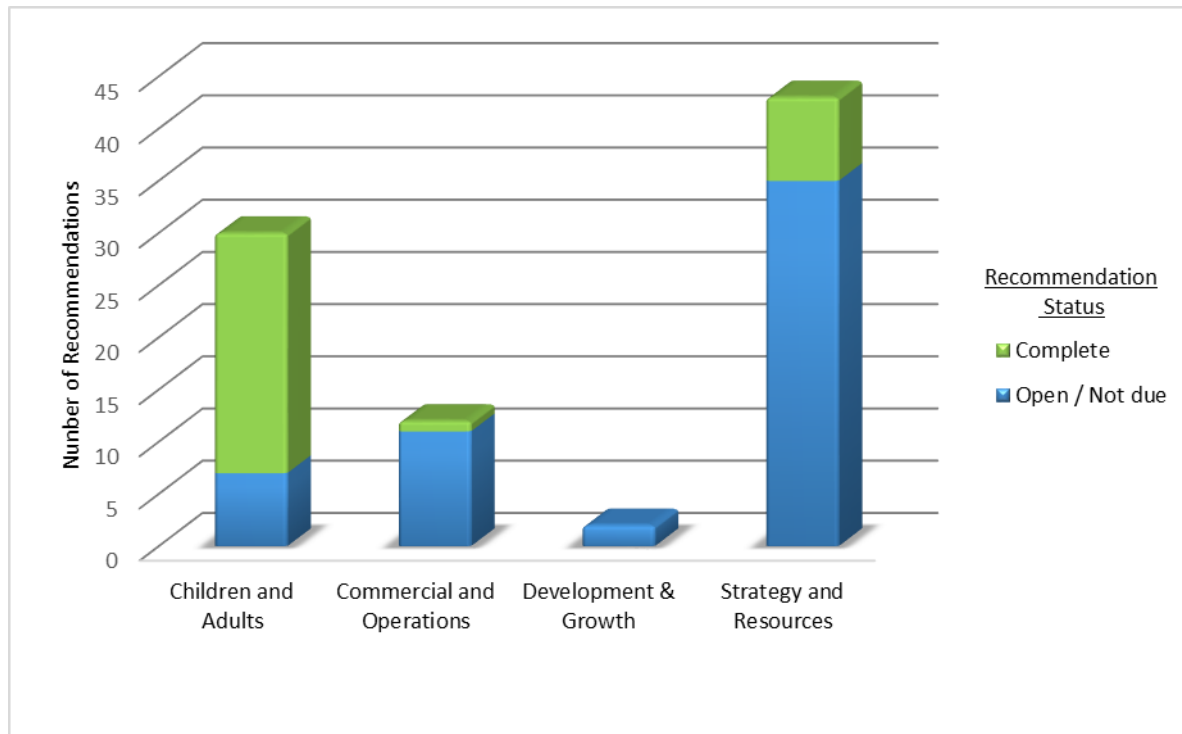
6.6.4 The HoIA has constantly reviewed the progress made on these high risk recommendations and has concluded that Corporate Directors have acted appropriately to address the recommendations reported to them.

6.7 Risk Themes

6.7.1 IA recommendations are categorised into themes to reflect the main element of the weaknesses they are trying to address.

6.7.2 Diagram 5 illustrates the distribution of the main themes of the recommendations made. The diagram shows that a similar pattern exists across departments, the main themes pertaining to the financial loss and the operation of internal controls.

6.7.3 The recommendations made to address the issues underpinning the themes strengthen the control environment and help the Council use its resources in the most appropriate way to achieve its objectives.

Diagram 5: Risk Themes
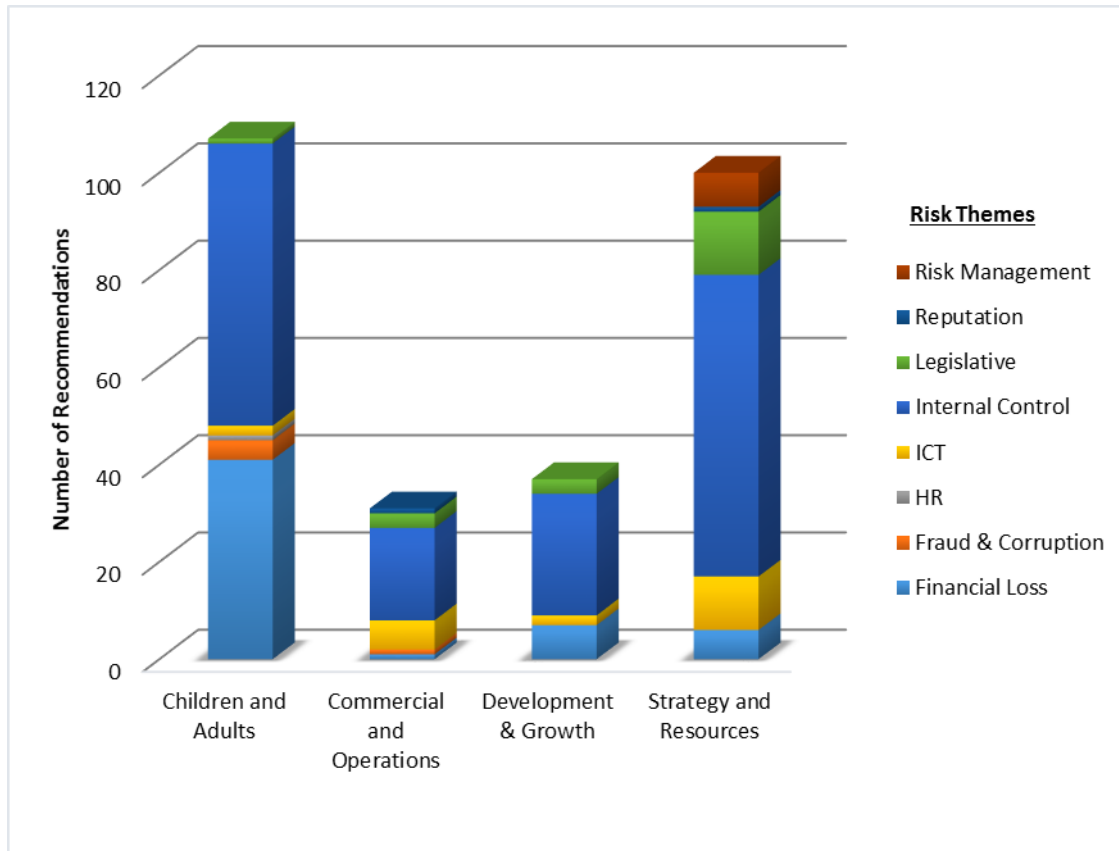
6.8 Corporate Fraud Team

The Corporate Fraud Team is responsible for the investigation of irregularities and is also tasked with the proactive review of areas at risk of fraud / error with a view to identifying income and savings. The priority for 2016/17 was to identify £400,000 of cashable income; the final figure recorded as £687,000 plus savings of £502,000.

6.9 Head of Audit's Annual Opinion 2016/17

6.9.1 The PSIAS require the HoIA to give an opinion and report to support the City Council's Annual Governance Statement. Corporate Directors are responsible for ensuring that proper standards of internal control operate within their directorates. IA reviews these controls and gives an opinion in respect of the systems and processes put in place. The audit work concludes with a report detailing the findings and giving an overall level of assurance.

6.9.2 The IA service works to a risk based Audit Plan agreed with Corporate Directors and agreed by the Committee. The 2016/17 Audit Plan has been completed in accordance with the PSIAS and other professional standards applicable to the service. The IA service has undertaken reviews of the internal control procedures in respect of the key systems and processes of the Council and its partners, where appropriate. The service has operated within professional standards as PSIAS.

6.9.3 Planned work has been supplemented by ad hoc reviews in respect of irregularities and other work commissioned by Corporate Directors or the partners of the City Council and the work undertaken by external review agencies. Reports in respect of all reviews have been issued to the responsible colleagues, together with recommendations and agreed action plans. Further, each quarter a list of reports has been sent to the Committee for consideration.

6.9.4 Throughout 2016/17 the HoIA has continuously reviewed the significant challenges and risks associated with the Council's operations and has allocated the necessary resources, via the audit plan, to form his opinion on the Council's governance arrangements. In forming his opinion the HoIA has reviewed all the IA reports issued in 2016/17 which has included ICT work and drawn upon available external sources of assurance from independent review bodies and internal assurance mechanisms to help him identify and assess the key control risks to the Council's objectives. Other sources of assurance has included the AGS Statement, Ombudsman Report, KPMG the Council's external auditor, and the partnership health check review

6.9.5 The HoIA has concluded that although no systems of control can provide absolute assurance, nor can IA give that assurance, he is satisfied that, on the basis of the audit work undertaken during the 2016/17 financial year, there have been no significant issues (as defined in the CIPFA Code of Practice) reported by IA. Furthermore, on the basis of the audit work undertaken during the 2016/17 financial year, covering financial systems, risk and governance, the HoIA is able to conclude that a reasonable level of assurance can be given that internal control systems are operating effectively within the Council, its significant partners and associated groups.

7 BACKGROUND PAPERS OTHER THAN PUBLISHED WORKS OR THOSE DISCLOSING EXEMPT OR CONFIDENTIAL INFORMATION

None

8 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

- Accounts and Audit Regulations 2015
- Audit Plan 2016/17
- CIPFA SOLACE Delivering Good Governance in Local Government
- Public Sector Internal Audit Standards 2013

List of Appendices

Appendix 1   Quality Assurance and Improvement Programme (QAIP)

Appendix 2   List of all reports issued during 1st January 2017 to 31 March 2017 with High Priority Recommendations

Appendix 3   List of final Audit reports issued 1st January 2017 to 31 March 2017

Appendix 4   Summary Internal Audit Plan / Outturn 2016/17

Appendix 5   List of all final reports issued in 2016/17