



Northumberland
County Council

Shared Internal Audit and Risk Management Service

2018/19 Opinion on the Adequacy and Effectiveness of the Framework of Governance, Risk Management and Control

May 2019

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Executive Summary

Overall, Internal Audit's work performed during 2018/19 found that the County Council's internal systems of governance, risk management and control are satisfactory overall. This is a positive assessment of the Council's control environment and reflects favourably on the organisation's governance arrangements.

This 'satisfactory' overall judgement is informed by the outcomes of Internal Audit work during 2018/19. This work demonstrates that the majority of audit opinions issued in the period have been categorised as 'significant assurance'. No 'critical priority' recommendations were made by Internal Audit during the year, and no 'no assurance' audit opinions have been issued or are pending.

The Chief Internal Auditor draws attention to a change in entities within the County Council's accounting group boundary, whereby the wholly owned Arch Group of Companies was wound up during 2018/19 and replaced by a new company, Advance Northumberland. Significant efforts have been made by interim finance staff to establish sound financial systems within the new entity. It must be recognised that due to concerns identified in the predecessor organisation, which have been separately reported to Audit Committee, and the relatively recent creation of Advance Northumberland, systems within the new company are yet to fully embed. As such, this should continue to be a focus of the County Council's attention when undertaking its own assessment of governance and control

The opinion of the Chief Internal Auditor (known as the 'chief audit executive' under the Public Sector Internal Audit Standards) is, at the time of preparing this report, that the organisation's internal control systems in the areas audited are **satisfactory**.

1 Purpose of Report

- 1.1 This report has been written by the Chief Internal Auditor to provide an annual opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control, taking into account the expectations of the Council's Leadership Team, Audit Committee and other key stakeholders.

2 Governance, Risk Management and Control

- 2.1 Management's responsibility for the effectiveness of the internal control system is clearly set out in the Council's Finance and Contract Rules which state:

- The Chief Finance Officer is responsible for advising on effective systems of internal control. These arrangements need to ensure compliance with all applicable statutes and regulations, and other relevant statements of best practice. They should ensure that public funds are properly safeguarded and used economically, efficiently, and in accordance with the statutory and other authorities that govern their use;
- It is the responsibility of Directors to ensure that effective systems of internal control are in place, to ensure compliance with Financial Regulations and Financial Procedures and to establish sound arrangements for planning, appraising, authorising and controlling their operations in order to achieve continuous improvement, economy, efficiency and effectiveness and for achieving their financial performance targets.

- 2.2 When auditing, Internal Audit assist management by testing to see whether the controls established for any given system are appropriate. It is important to stress that Internal Audit, while part of the Authority's overall assurance framework, is not a substitute for effective internal control within the Authority's systems.

- 2.3 Effective controls will depend, amongst other factors, on:

- The nature, size and volume of transactions;
- The degree of control which management is able to exercise personally;
- The geographical distribution of the enterprise; and
- The cost of operation of the controls against the benefits expected from them.

- 2.4 There are eight main types of internal control, namely:

Preventative Controls

- (i) Segregation of duties (no one person should be responsible for processing and recording a complete transaction).
- (ii) Authorisation and approval (all financial transactions should require authorisation by an appropriate responsible official; the limits of authorisation should be specified).
- (iii) Physical (custody of / access to tangible assets should be secure and limited to authorised personnel).

Detective Controls

- (iv) Arithmetic & Accounting (controls within the recording function to check that transactions have been authorised, are included, are correctly recorded and are accurately processed).

Directive Controls

- (v) Organisation (responsibilities should be defined and allocated; reporting lines should be identified; delegation of authority should be clearly specified).
- (vi) Supervision (all actions by all levels of staff should be supervised; the responsibility for this supervision should be clearly laid down and communicated to the person being supervised).
- (vii) Personnel (procedures should exist to ensure that staff are competent to carry out the jobs assigned to them, including proper recruitment and performance management procedures, career prospects, training and pay policies).
- (viii) Management (controls exercised by management outside the day to day routine of the system, including supervision).

3 Opinion on the Adequacy and Effectiveness of the Framework of Governance, Risk Management and Control

- 3.1 The Chief Internal Auditor is required under the Public Sector Internal Audit Standards (PSIAS), introduced in April 2013 and revised April 2017, to provide an annual opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control. For the purpose of meeting this requirement, the Chief Internal Auditor provides one of two opinions:
 - (a) That the organisation's framework of governance, risk management and control is **satisfactory** (i.e. satisfactory assurance can be obtained from governance systems and procedures in place); or
 - (b) That the organisation's framework of governance, risk management and control is **not satisfactory** (i.e. there is insufficient control in evidence within the organisation's governance systems to provide satisfactory assurance).
- 3.2 The opinion of the Chief Internal Auditor is that, at the time of preparing this report, the County Council's internal systems of governance, risk management and control were **satisfactory** overall, during 2018/19.
- 3.3 At the time that the 2017/18 Annual Audit Opinion was prepared, the Chief Internal Auditor drew attention to significant emerging risks in a wholly owned group of companies (Arch Corporate Holdings Ltd.). During 2017/18, a number of governance matters were identified in this group of companies, with issues of potential criminality referred to Northumbria Police. Since that time, Arch Corporate Holdings Ltd. has ceased to operate and a new company, Advance Northumberland Ltd., has been created. Substantial efforts have been made within the new company to address weaknesses in systems of governance and control which existed in the predecessor organisation. However, it is likely to take some time for these systems (and indeed the entire framework of directive control) to become fully

embedded. Consequently, this opinion recognises the evolving nature of arrangements around the Advance Northumberland entity and the impact that this entity may potentially have on the County Council's framework of governance, risk management and control. This should continue to be an area of focus for the County Council when reviewing its internal control arrangements.

- 3.4 The Chief Internal Auditor has not needed to place reliance on the work of other bodies in forming this view, and there are no limitations in the scope of the opinion.
- 3.5 Assurance can never be absolute, and neither can Internal Audit work be designed to identify all weaknesses that might exist. This judgement is informed by the well-established framework of core financial systems which are in place within the County Council, and the outcomes of Internal Audit work during 2018/19, which is reported to the Audit Committee in regular Key Outcomes reports. These have demonstrated that the majority of audit opinions issued in the period have been 'significant assurance'. A full list of audits performed and opinions issued is included at **Annex A**.
- 3.6 In accordance with its role, Internal Audit has agreed recommendations with management aimed at further strengthening the control environment in operation within the organisation. It is management's responsibility to implement agreed recommendations. As part of 2019/20 planned service improvements, Internal Audit will be reviewing the approach to evidence checking the extent to which agreed recommendations have been implemented. In doing so, Internal Audit must balance the value to be gained from revisiting previous recommendations, management's own responsibility for their implementation and the respective value to be gained by reviewing new areas of emerging risk.
- 3.7 The opinion of the Chief Internal Auditor on the framework of governance, risk management and control is a positive opinion. This opinion is based solely on the areas reviewed.
- 3.8 It is recommended that Internal Audit's overall satisfactory opinion on the framework of governance, risk management and control is considered as a source of assurance for the preparation of the Annual Governance Statement for 2018/19, and its subsequent approval by the Audit Committee.

4 Audit Work Performed During 2018/19

- 4.1 Internal Audit has provided an audit, advice and programme assurance service to the Council in 2018/19. The work of Internal Audit is governed by the PSIAS and the accompanying Local Government Application Note issued by the Chartered Institute of Public Finance & Accountancy as the 'relevant Internal Audit standard setter'.
- 4.2 The audit reports issued during 2018/19, and those related to this period which are currently being finalised with our audit clients, are set out **Annex A**. During 2018/19 Internal Audit undertook a high volume of work in response to emerging assurance issues, particularly around Arch, and accordingly it was necessary to switch resource from some scheduled audit and assurance activity. As a result, and in

accordance with professional auditing guidelines, the Chief Internal Auditor re-assessed and reviewed the overall Plan to ensure audit resources were directed to areas of maximum benefit.

- 4.3 A framework of opinion classifications is used in Internal Audit reporting. The framework applies an overall assurance judgement to each system audited, as defined below:

Assurance Level	Description
Full Assurance	The system of internal control is designed to meet the organisation's objectives and controls are consistently applied in all the areas reviewed.
Significant Assurance	There is a generally sound system of control designed to meet the organisation's objectives. However, some weakness in the design of, or occasional non-compliance with, key controls put the achievement of the organisation's objectives at risk in some of the areas reviewed.
Limited Assurance	Weaknesses in the design of, or regular non-compliance with, key controls put the achievement of the organisation's objectives at risk in some or all of the areas reviewed.
No Assurance	Significant weaknesses in the design of, or consistent non-compliance with, key controls could result (have resulted) in failure to achieve the organisation's objectives in the areas reviewed.

- 4.4 The opinions given to audits issued during 2018/19 are also shown in **Annex A**.

- 4.5 In addition to the overall opinion given on every audit assignment, individual recommendations within each report are classified as critical, high, medium or low priority. This prioritisation is designed to assist management in assessing the importance of each recommendation. The definitions of these priority classifications are set out below:

Priority	Classification	Description
1*	Critical / Catastrophic	Action that is considered critical to ensure the organisation is not exposed to unacceptable risks.
1	High / Fundamental	Action that is considered urgent to ensure that the service area / establishment is not exposed to high risks.
2	Medium / Significant	Action that is considered necessary to avoid exposure to considerable risks.
3	Low / Less Significant	Action that is considered desirable or best practice and would result in enhanced control or better value for money.

- 4.6 The number of Internal Audit recommendations agreed with management during the 2018/19 audit year, classified against each priority, is provided in the table below (data from the previous four years is also shown for comparative purposes).

Priority Level	2014/15	2015/16	2016/17	2017/18	2018/19
Critical Priority	Nil	Nil	Nil	Nil	Nil
High Priority	18 (5%)	7 (2%)	11 (4%)	3 (3%)	Nil
Medium Priority	130 (39%)	181 (59%)	119 (49%)	47 (53%)	54 (39%)
Low Priority	187 (56%)	118 (39%)	115 (47%)	39 (44%)	86 (61%)
TOTAL	335 (100%)	306 (100%)	245 (100%)	89 (100%)	140 (100%)

- 4.7 There is a trend reflected within the table above of a reducing number of recommendations. This is partly because of the amount of additional work performed within Arch Corporate Holdings Ltd. (wholly owned company within the County Council's accounting group boundary), in 2017/18 and 2018/19. Internal Audit resourcing has also been affected by some long-term sickness absence, and vacancies, during 2018/19. Resourcing continues to be closely monitored and additional resources have been sought to increase assurance capacity. Management of existing resources continues to be undertaken under the County Council's prevailing policies.
- 4.8 Prioritisation of Internal Audit recommendations is controlled through Internal Audit's quality control and file review processes. This is in accordance with the requirements of Public Sector Internal Audit Standards, which requires that a Quality Assurance and Improvement Programme is in place for Internal Audit's work.

Audit Highlights 2018/19

- 4.9 This section of the report is designed to draw attention to significant audits and findings from Internal Audit in the 2018/19 year. It should be read in context of the overall positive 'satisfactory' audit opinion described above.
- 4.10 It is of comfort to the Authority that the fundamental financial systems, and high value / high volume transactional systems achieved assurance of 'significant'. These systems comprise the main processes by which the organisation makes payments or receives income.
- 4.11 Attention is also drawn to the 'significant assurance' opinions reached in respect of Children's Safeguarding Improvement Plan and Part III Accounts. These aspects of the Authority's operations focus on the Authority's stewardship and fiduciary duties,

often for very vulnerable service users. 'Significant assurance' opinions in respect of such sensitive aspects of the Authority's operations are to be welcomed.

- 4.12 Regarding Information Technology arrangements, there are aspects of the systems in place which are of concern. For example, the Authority's preparedness for General Data Protection Regulation (GDPR), Payment Card Industry Data Security Standards (PCIDSS), ICT Business Continuity / Disaster Recovery and BACS System Review all received a 'Limited Assurance' audit opinion. This highlights key areas of risk which should be a focus of management attention, especially given the importance of computerised systems for the effective delivery of so many of the Authority's services. The Authority's arrangements for Business Continuity Management similarly received a 'limited assurance' opinion. However, arrangements around administration of the Internet were found to be more soundly based, resulting in a 'significant assurance' opinion for that audit.
- 4.13 Internal Audit's work involving the Arch Group of Companies (which was wound down during 2018/19 and replaced with a new company, Advance Northumberland) is referenced above at paragraph 3.3. This work has continued to be a focus for the Internal Audit team in 2018/19, given the nature of risks identified within Arch during 2017/18. Internal Audit's 2017/18 report regarding Arch was presented to an extraordinary meeting of the County Council's Audit Committee on 22 March 2019 and highlighted a range of deficiencies in the Arch Group of Companies identified in 2017. This is material to the County Council's framework of governance, risk management and control and hence is referenced in this report.
- 4.14 In addition to performing internal audits of existing systems within the Council and responding to queries on the operation of such systems, during 2018/19 Internal Audit continued to have an increasing role in advising on new systems and processes within the Council. A full list of the programme assurance work and project groups supported by Internal Audit is shown at **Annex A**. Whilst the time spent on such assurance work reduces the number of available audit days, it is considered an efficient use of Internal Audit's resource, in that assurance is obtained that effective controls are incorporated into new systems and processes from the outset. In turn, this minimises the risk of weaknesses in systems and strengthens the control environment. It is expected that this type of audit work will continue in future years. Key highlights from Internal Audit's programme assurance work during 2018/19 include:
- a) **Digital Northumberland Board** - Internal Audit's role on the Digital Northumberland Board was to provide an independent assurance role and as such provide an audit comment on any issues presented at Board meetings. While the Board was active Internal Audit used it as a vehicle to share good practice/lessons learned from similar assurance work performed elsewhere by the shared Internal Audit team. Internal Audit reviewed specific projects overseen by the Board including the roll out of superfast broadband across the county, NCC's participation in Gov.UK Verify projects and reviewed multiple policies for which the Board was the approval body.
 - b) **Oracle Cloud Project** - In the early stages of the project Internal Audit provided comment to the project sponsor on the quality of project

management and the timeliness and completeness of documentation presented to the Board. After several delays the majority of business modules, with the exception of Payroll, were implemented in late 2018. Due to a number of issues Payroll is not yet implemented in Oracle Cloud. As a result NCC will need to extend its use of and support for Oracle R12 on which Payroll is currently hosted. Responsibility for extended support costs is the subject of discussion between NCC, Oracle and Evosys (NCC's Oracle Cloud implementation partner).

- 4.15 As a general comment, recent projects have identified areas that would have benefitted from more in-depth assurance at an earlier juncture.
- 4.16 There are a number of funding organisations that require an Internal Audit review prior to final grant claim submission. This area of our activity is also shown at **Annex A** and involved the certification of £33.2m grant funding in 2018/19.

5 Schools' Financial Value Standard

- 5.1 Time was included in the audit plan for 2018/19 to support and co-ordinate the work required by the Schools Financial Value Standard (SFVS) on behalf of the Authority.
- 5.2 The SFVS has been designed in conjunction with schools to assist them in managing their finances and to give assurance that they have secure financial management in place. Governing bodies have formal responsibility for the financial management of their schools, and so the standard is primarily aimed at governors; however the Authority's Chief Finance Officer is responsible for ensuring that submissions made by schools are in line with the judgements on these schools which have already been reached by Internal Audit.
- 5.3 On behalf of the Chief Finance Officer (Section 151 Officer), Internal Audit co-ordinated, received and reviewed SFVS submissions for all of the Council's grant-maintained schools. All schools submitted their self-assessments by the deadline of 31 March 2019.

6 Special Investigations

- 6.1 During 2018/19, the Service undertook a high volume of work in response to emerging governance issues arising in year, most notably around Arch. These relate to issues which could not be foreseen, and where irregularity may have been indicated. As such, it is important that the organisation can call upon Internal Audit resource to respond quickly to assess the extent of potential problems. Issues around Arch are highlighted earlier in this report (see para. 3.3 above).

7 The National Fraud Initiative (NFI)

- 7.1 Northumberland County Council is part of the Cabinet Office's National Fraud Initiative (NFI) and is required to provide particular sets of data to the Minister for the Cabinet Office for matching for each exercise. Before this information can be provided, the Council is required to ensure that appropriate steps have been taken

to notify data subjects held in the organisation's relevant information systems that data may be used for the prevention and detection of fraud.

- 7.2 As in previous years, Internal Audit have acted as the lead within the Council for the NFI data-matching exercise. Data was extracted from the relevant Council systems and submitted to NFI, additionally fair processing notices were issued to notify all data subjects that data may be used for the prevention and detection of fraud. The NFI 2018/19 results have been released and Internal Audit and appropriate officers within departments are currently investigating the matches and updating the NFI system with outcomes.

8 Ad-hoc Queries / Requests for Advice

- 8.1 Internal Audit receives requests for ad-hoc advice and support throughout the year, in respect of which we may be required to extract prime data or produce analysis but where it is not usually appropriate to issue a formal report.

9 Clients' Views

- 9.1 For several years, Internal Audit has sought client feedback in respect of all audit reports issued, at the conclusion of each audit assignment.
- 9.2 The feedback received from respondents for 2018/19 remains very positive. Clients score the service from 1 to 4 against a number of criteria, with 1 being very satisfied and 4 being very dissatisfied. From all the returned feedback forms, clients' overall opinion was that audits are constructive and provide value to management. The overall average score in 2018/19 was 1.0 (the highest that can be achieved).
- 9.3 Internal Audit seeks to continually improve and will be reviewing and implementing new processes through its quality assessment and improvement programme. The theme of comments added to the feedback is that audits are conducted in a professional manner and findings and recommendations will lead to system improvements.
- 9.4 The full results for 2018/19, along with comparative data from 2017/18, are shown at **Annex B**.

10 Annual Governance Statement 2018/19

- 10.1 The Annual Report from the Chief Internal Auditor is one source of intelligence for the organisation when preparing the Annual Governance Statement. Internal Audit has continued to target its assurance activity at areas of risk in its 2018/19 coverage in line with the agreed audit plan. Regular reports have been presented to Audit Committee during the year to allow the Audit Committee to develop awareness of the application of the Council's governance structure.
- 10.2 It is suggested that the following issues are considered for inclusion in the Annual Governance Statement:

Overall Opinion on the organisation's internal systems of governance, risk management and control:

The overall opinion of the Chief Internal Auditor on the organisation's internal systems of governance, risk management and control, was found to be satisfactory (ref. point 3.2).

In determining the overall 'satisfactory' opinion, the Chief Internal Auditor has had regard to the established framework of core financial systems in place within the Authority, which when audited during 2018/19 were found to bear appropriate internal controls and to be operating satisfactorily.

Attention is drawn to a number of audits undertaken regarding the County Council's Information Technology arrangements, a number of which received a 'limited assurance' audit opinion during 2018/19. As the public services, including Northumberland County Council, continue to embrace channel shift which is likely to see an increasing reliance on computerised systems and 'self-service' by stakeholders, it is essential that all ICT systems are fit for purpose. This will be a continued area of focus within the Authority.

A number of audits of Council services where safeguarding and stewardship responsibilities are paramount (for example Children's Safeguarding Improvement Plan and Part III Accounts) have demonstrated effective systems in place.

During 2018/19, the County Council's former wholly owned group of companies (Arch Corporate Holdings Ltd.) began to be wound down and a new company (Advance Northumberland Ltd.) was created. As a company wholly owned by the County Council, any such entity must have an impact (favourably or adversely) on the overall framework of governance, risk management and control within the County Council. Substantial efforts to implement effective systems within Advance Northumberland have been made by interim finance officers. This will continue to be an area of Internal Audit's focus as systems become embedded.

Annex A: Formal Audit Reports issued during 2018/19

Audit	Opinion
BACS System Review	Limited
Business Continuity Management	Limited
Children's Safeguarding Improvement Plan	Significant
Council Tax	Significant
Creditor Payments	Significant
ICT Business Continuity / Disaster Recovery	Limited
Internet	Significant
Part III Accounts	Significant
Payment Card Industry Data Security Standard(s)	Limited
Payroll	Significant
Preparation for General Data Protection Regulation (GDPR)	Limited
Public Services Network (PSN) Code of Connection Briefing Note	N/A
Rent Assessment & Collection	Significant
Stores Partnership – Post Contract Implementation	Significant

Reports Pending from 2018/19 (draft report issued, awaiting issue as final report)

Audit
Google Applications

Grant Claim certification

Broadband Delivery UK Grant
Carbon Reduction Commitment
Pothole Action Fund
Disabled Facilities Grant
Local Authority Bus Subsidy Ring-Fenced (Revenue) Grant
Local Transport Plan Grant
Troubled Families Grant

Programme Assurance / Projects Groups

Digital Northumberland Strategy Board
Oracle Cloud Project
Troubled Families Partnership

Annex B: Overall Results from Client Feedback Forms 2018/19

Satisfaction score between 1 and 4 with 1 being very satisfied and 4 being very dissatisfied (scores from 2017/18 are shown in brackets):

	Average Score
AUDIT PLANNING/COVERAGE	
• With the advance notification for the audit	1.0 (1.0)
• With the areas covered by the audit	1.0 (1.0)
• That your requirements were reflected by the audit	1.0 (1.25)
AUDIT APPROACH	
• That the objectives of the audit were clearly explained and understandable to you	1.0 (1.25)
• With the knowledge and professionalism of the auditors	1.0 (1.0)
• With the attitude and politeness of the auditors	1.0 (1.0)
• With the auditors understanding of your operational requirements	1.0 (1.25)
• That there was adequate consultation on findings and recommendations	1.0 (1.25)
REPORTING ARRANGEMENTS	
• With the accuracy of the findings	1.0 (1.25)
• With the materiality of the findings	1.0 (1.25)
• That the report was clear and concise	1.0 (1.25)
• With the usefulness of the conclusions and recommendations	1.0 (1.25)
• With the arrangements for commenting on the draft report	1.0 (1.25)
• The time taken to produce the report following the audit visit	1.0 (1.5)
OVERALL OPINION	
• That the audit was constructive and provided value to management	1.0 (1.25)