

# **LONDON BOROUGH OF MERTON**

## **INTERNAL AUDIT ANNUAL REPORT YEAR ENDING 31<sup>ST</sup> MARCH 2017**

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## **1. Head of Audit Assurance Opinion**

- 1.1 Internal Audit has reviewed the effectiveness of the Council's systems of internal control for 2016/17 and has taken into account appropriate assurances obtained from other relevant internal and external sources. The opinion, based on this work, is that the Council's systems of internal control are generally sound and effective although the expected high standards of control have not been achieved in a limited number of council activities (detailed below). There is therefore a requirement to improve in these areas.
- 1.2 Appropriate action plans are in place in response to internal audit actions where necessary. It is important that departments ensure that audit actions are implemented in a timely manner to ensure effective controls are in place.

## **2 The Internal Audit Assurance Framework**

- 2.1. A key responsibility of Internal Audit is to give the organisation assurances about the levels of internal control being exercised in the areas of risk and in particular where there are transactions that are considered "material" to the Council.
- 2.2. Internal Audit seeks to ensure that Merton's systems adhere to recognised standards and that public accountability can be demonstrated and is transparent.
- 2.3 Overall, whilst issues have been identified and resolved, the systems of control within the Council are such that reliance can be placed upon them.
- 2.4. In order to give such an assurance, a balanced programme of Internal Audit reviews is constructed each year. This Annual Internal Audit Plan contains elements of all the Council's activities selected using a "Risk Based" approach. There are many tools used to achieve a balanced plan including undertaking systems reviews, regularity audits (e.g. schools), contract and computer audit, fraud and misappropriation reviews and an annual review of major financial systems such as Council Tax, cash and bank and Housing Benefits.
- 2.5. In order to contribute to the Annual Governance Statement, all Internal Audit reports give an audit assurance. These assurances were changed in 2016/17 to have a consistent 5-borough audit partnership assurance rating, these changes are as follows:
  - a) Substantial Assurance – changed to Full Assurance
  - b) Satisfactory Assurance – changed to Substantial Assurance
  - c) Limited Assurance- still Limited (no change)
  - d) No Assurance – still No Assurance (no change)
- 2.6. In addition, each recommendation emanating from the audit review is given a high, medium or low risk priority for implementation. All recommendations are followed up by Internal Audit to ensure that they have been implemented.
- 2.7. The audit plan for 2016/17 covered those area of high fraud risk, as identified through the councils own assessments and through information from CIPFA, the Audit Commission and other sources, where fraud risks are highlighted. Examples of these are procurement cards, business rates, direct payments.

- 2.8 These audits reviewed the controls in place, although no fraud was identified in any of these reviews, a number of recommendations were made to improve the controls.
- 2.9 In addition to the agreed audit plan, additional audits and reviews at the request of Management have been completed. These have ranged from full audits to focused audit investigations. Examples of these additional pieces of work included:
- Safeguarding adults
  - Affordable housing grant agreement
  - Apprenticeships
  - Facilities procurement
  - Memorandum of Understanding
  - Parking permit income
  - Procurement/interims
- 2.10 Internal Audit has also undertaken substantial testing on the new financial E5 system as well as ongoing advice on the new social care system, Corelogic.
- 2.11 These referrals to Internal Audit help to demonstrate the continued good engagement from departments and their awareness of the role of Internal Audit and the work that they can undertake to support their service. The Council's risk profile is constantly changing. Therefore, Internal Audit and the internal audit plan needs to be flexible to be able to respond to these changing and emerging risks.
- 2.12 The Internal Audit function is conscious of the significant pressure on resources that the Council is facing and has continued to identify where we can support management through looking to identify potential efficiencies and making recommendations for possibly fewer but better controls wherever possible.

### **3. 2016/17 Internal Audit Assurances**

- 3.1. During 2016/17 there were 47 Internal Audit reviews completed providing an assurance rating. (A further 12 areas were reviewed as either advisory or signing off accounts).
- 3.2 A full list of the assurances can be found in Appendix A. A summary of all limited assurance audits for 2016/17 are included in Appendix B. Action Plans for improvements are in place for all audits. Discussions are being held with Departments and action plans are still to be finalised in some instances.

3.3 The following tables summarise the results by audit type:

**Table 1 Internal Audit Assurances by Audit Type 2016/17**

Assurance	assurance	Limited	Totals
Procurement	2	2	4
Establishments	6	3	9
Financial Systems	7	1	8
IT	4	0	4
Service Specific	14	7	21
Corp Gov/grants	1	0	1
<b>Totals</b>	<b>34</b>	<b>13</b>	<b>47</b>

3.4 Table 2 summarises results for the last three financial years in the form of number of reviews and % for satisfactory and limited assurance.

**Table 2 Internal Audit Assurances 2014/15- 2016/17**

	Assurance			Limited Assurance		
	2014/15	2015/16	2016/17	2014/15	2015/16	2016/17
<b>C&amp;H</b>	5 (63%)	5 (56%)	<b>2 (67%)</b>	3 (37%)	4 (44%)	<b>1 (33%)</b>
<b>CS</b>	24(86%)	21 (81%)	<b>19(76%)</b>	4 (14%)	5 (19%)	<b>6 (24%)</b>
<b>E&amp;R</b>	10(83%)	4 (57%)	<b>3 (60%)</b>	2 (17%)	4 43%	<b>2 (40%)</b>
<b>CSF</b>	8 (89%)	9 69%)	<b>9 (69%)</b>	1 (11%)	4 31%	<b>4 (31%)</b>
<b>All depts.</b>	3 (75%)	0	<b>1</b>	1 (25%)	0	<b>0</b>
<b>Total</b>	50(82%)	41(71%)	<b>34(72%)</b>	11(18%)	17(29%)	<b>13(28%)</b>

3.5. The percentage of audit assurances achieving a satisfactory/substantial or above rating has increased slightly since year. In all cases action plans are in place for agreed areas of improvement. Management summaries for each limited report were regularly submitted to the Standards and General Purposes Committee.

3.6. When analysing these statistics between years the following factors need to be taken into account:

- The same areas are not audited every year hence a like for like comparison cannot be made. Individual audits differ considerably in terms of scope and objectives.
- The numbers of audits carried out in the year (small numbers in an area can give misleading results in % terms.)
- There have been changes in the departmental responsibilities over the three-year period.

**Key Areas for 2016/17**

3.7 Internal Audit has continued to improve their level of engagement with all levels of management. This has been achieved by attending regular DMT's to discuss audit progress, meeting with key stakeholders prior to the start of the audit to agree the audit brief.

- 3.8 When the audit plan is set, discussions are held with all key people for input, this engagement has enabled the Internal Audit team to focus on the key areas of risk as well as work closely with management to formulate actions to address areas where improvement is required.
- 3.9 As set out in the above section we have identified areas of good practice and an effective control environment across the majority of the systems, processes and establishments reviewed. This includes the Council's key financial systems as set out below.
- 3.10 However there are a number of areas where further improvements are required to strengthen the control environment and we have summarised the key themes identified below.

#### Procurement

- 3.11 A sample of four areas reviewed found that 2 areas received a limited assurance as their procurement arrangements needed improvement, Contract Compliance and e-tendering where recommendations for improvement are currently in progress. A Corporate Procurement audit is due to be undertaken in 2017/18.

#### Financial systems

- 3.12 Of the 6 main financial systems reviewed this year, they all received a satisfactory/substantial assurance. The Pension Investment limited assurance audit final report for 2015/16 was issued in 2016/17, a follow up review is currently in progress.

**Table 3 Financial systems audit assurance for last 3 years**

Financial System	Assurance 2016/17	Assurance 2015/16	Assurance 2014/15
Cash and bank	satisfactory	satisfactory	Not audited
Payroll (iTrent)	satisfactory	satisfactory	Limited
Accounts Payable	Not audited	Not audited	Satisfactory
Fixed Assets	Not audited	Not audited	Satisfactory
Debtors	satisfactory	Not audited	Not audited
Housing benefits	satisfactory	Limited	Not audited
Treasury management/pension investment	Not audited	Limited	Limited
Council Tax	satisfactory	Not audited	Satisfactory
National Non-Domestic Rates (NNDR)	Not audited	satisfactory	Satisfactory
General Ledger	satisfactory	satisfactory	Not audited
Budgetary Control	Not audited	Not audited	Satisfactory

- 3.13 The Payroll (iTrent) audit has been carried out as part of a joint review for London Borough's:-Sutton, Merton, and Kingston undertaken by Mazars.

## IT audits

There were 3 Information Technology audits this year on Firewall & Network security, Internet Payments and IT laptops & mobile devices, all received a substantial assurance. These audits were undertaken by Mazars.

## Service Specific

- 3.14 There were 21 service specific audits carried out, of these 7 received a limited assurance (33%) where staff did not follow a proper process in financial arrangements leading to weak controls. These limited reviews were in a range of service reviews, Fuel Bunker and cards, No recourse to public funds, Agency and temporary Staff, Civic Regalia, Prepaid cards, Market Street traders, DBS follow up.
- 3.15 During 2016/17 the Head of Internal Audit worked closely with other elements of the Corporate Governance Division including leading on the working group for the 2016/17 Annual Governance Statement. Internal Audit have been involved with a number of governance reviews which have identified areas for improvement across the Council.

## Schools

- 3.16 There were 9 school audits carried out this year, 3 of which have resulted in a limited assurance (33%). A follow up audit will be undertaken at these schools to ensure that the recommendations have been implemented. Internal Audit work closely with finance throughout the year to be aware of any concerns at schools in relation to budget deficits and late returns. Where concerns are raised, these are taken into account in the audit planning for each year.

## **4. Follow up's**

- 4.1 During 2016/17 Internal Audit made a total of 389 recommended improvement actions, at the time of this report 281 actions (72%) were fully implemented. 108 actions have yet to be implemented, of these 18 actions are overdue.
- 4.2 For those outstanding actions, an expected implementation date is provided by the manager. Monthly reports are sent out to all managers for actions due, where these are over two months overdue, the Head of Service also receives a copy. If an action is more than 3 months overdue, then the appropriate Director is informed. Any overdue outstanding audit actions are then reported to Standards /General Purposes committee.
- 4.3 Where reports are given a limited assurance and therefore have a number of recommendations a full follow up audit is usually carried out in the subsequent year to gain assurance that these recommendations have been actioned.

## **5 Anti-Fraud**

- 5.1 The council Anti-Fraud and Corruption strategy, to sets out the council's approach to detecting, preventing and investigating fraud and corruption This strategy is supported by the councils whistleblowing policy, which was reviewed and

updated in 2016 and by the council's code of conduct. The Internal Audit section has a key role in implementing this strategy and to ensure that the internal controls in place are robust to prevent fraud occurring or to tighten controls where fraud has occurred.

## 6 Fraud Partnership

6.1 The South West London Fraud Partnership cases for Merton are: -

2016/17	Open Cases b/fwd	New Cases in Year	Total Cases	Closed No Sanction	Closed With Sanction	Open Cases c/fwd
Tenancy Fraud	55	109	164	120	10	34
Housing Applications	0	23	23	2	16	5
Right to Buy	1	29	30	8	4	18
Blue Badge Fraud	0	7	7	5	0	2
Corporate – Internal	3	11	14	3	5	6
Council tax Reduction	5	14	19	9	2	8
<b>Totals</b>	64	193	257	147	37	73

### Housing Fraud

- 6.2 Ten properties were recovered in 2016/17. This allows for those on the councils waiting list to be provided with the opportunity for a housing tenancy. Work is ongoing, including 3 cases with legal for consideration of legal action.
- 6.3 Right to buy applicants are passed to the Fraud partnership and the application checked to Housing Benefit, four applications have been cancelled as a result of incorrect information provided.

### Corporate Fraud

- 6.4 The corporate fraud cases involved employees for 2016/17, resulted in: -
- 2 resignations (1 of which may have further action taken),
  - 3 disciplinary hearing- (1 dismissed, 1 final warning and 1 written warning)
  - 2 Prosecutions in progress
  - 1 No Further action - recommended improved controls
  - 3 in progress



## National Fraud Initiative (NFI)

- 6.5 The NFI matches are: - Creditors, Market Traders, Personal Alcohol Licences, Parking, Payroll, Pensions, Personal Budgets, Residential Care, Council Tax & Electoral Registration. This data is matched between councils and within Merton.

NFI 2016/17 – 5,890 matches have been received for review. Further matches may be released as they refresh data from other sources.

- 6.6 SWLFP are undertaking initial checks on reports considered high risk (such as Payroll to Payroll matches across boroughs) and will be arranging meetings to discuss with service areas which reports they will action.

At the 31<sup>st</sup> March 2017;

- 86 matches have been completed and closed;
- 11 matches are in progress (had some action taken on them)
- 1 matches had been closed as fraud; and
- 0 matches identified as errors.

NFI 2014/15 – 9,058 were received, of which 1,917 were shown as recommended matches.

At the 31<sup>st</sup> March 2017;

- 624 matches had been completed and closed;
- 726 matches were in progress (had some action taken on them)
- 4 matches had been closed as fraud; and
- 9 matches identified as errors.

In total £31,810.39 has been identified as overpaid/incorrectly paid as a result of the NFI. The council will seek to recover this money.

## **7. Review of the Effectiveness of the System of Internal Audit**

- 7.1 The Annual Audit Plan for 2016/17 was agreed by Standard/General Purposes Committee Members at the start of the year. At the year-end 100% of the audit planned days were achieved and 90% of audit actions implemented by the agreed date.

- 7.2 Internal audit has contributed to the overall corporate governance of the council's activities by:

- Completion of the audit plan
- Member of the corporate risk strategy group.
- Chair of AGS working group

- Providing advice/training on corporate policies and procedures and control issues

7.3 The Public Sector Internal Audit Standards defines the level of effective audit service expected for all public sector audit services. There is a requirement to undertake an annual internal review of compliance to the standard, an internal review of the standard to confirm conformity has been carried out in 2016/17. A small number of changes are required to reflect the new audit partnership. These include updating the customer survey, reviewing retention policy and carrying out a training needs analysis. Based upon our ongoing assignment and review processes, together with the results of our Customer Surveys, we believe that we are substantially compliant with those Performance Standards

7.4 The standard also requires an independent external assessment to be carried out every 5 years. This was undertaken as part of a peer review in March 2014, and resulted in a conclusion that Merton internal Audit service is compliant with the standard. The next external assessment will be on the audit partnership in 2018/19.

#### Quality assurance

7.5 Internal Audit operates a Quality Assurance system for its internal audits. This includes; -

- Preparation of a detailed audit plan which is reviewed by the Director of Corporate Services and the Shared Service Board prior to submission to the Standards and General Purposes Committee for approval;
- Regular review of progress against the plan to ensure we are delivering the work we have promised. Quarterly reports are made to the Shared Service Board
- A tailored audit approach using a defined methodology and assignment control documentation which is subject to a review protocol;
- The use of qualified, highly trained and experienced staff;
- Monitoring of performance against targets.
- The review of all reports by the Head of Audit.