

Internal Audit Work to February 2020 Report by Chief Internal Auditor

1. Purpose of the Report

The purpose of this report is to provide members of the Audit Committee with details of the recent work carried out by Internal Audit and the findings and recommended audit actions agreed by Management to improve internal controls and governance arrangements.

2. Progress Report

- 2.1 The Internal Audit Annual Plan 2019/20 was approved by the Audit Committee on 12 March 2019. Internal Audit has carried out the following work in the period from 1 January to 20 February 2020 associated with the delivery of the Plan to meet its objective of providing an opinion on the efficacy of the Council's risk management, internal control and governance.
- 2.2 The MLC Internal Audit function conforms to the professional standards as set out in Public Sector Internal Audit Standards (PSIAS) (2017) including the production of this report to communicate the results of the reviews.
- 2.3 Internal Audit issued final assurance reports on the following subjects:
- Procurement and Management of Contracts
 - Change and Transformation Programme
 - Business Planning, Budget Setting and Monitoring
- 2.4 An Executive Summary of the final Internal Audit assurance report issued, including audit objective, findings, good practice and recommendations (where appropriate), and the Chief Internal Auditor's independent and objective opinion on the adequacy of the control environment and governance arrangements within each audit area, is shown in Appendix 1.

The definitions for Internal Audit assurance categories are as follows:

Level	Definition
Comprehensive assurance	Sound risk, control, and governance systems are in place. These should be effective in mitigating risks to the achievement of objectives. Some improvements in a few, relatively minor, areas may be required.
Substantial assurance	Largely satisfactory risk, control, and governance systems are in place. There is, however, some scope for improvement as current arrangements could undermine the achievement of objectives or leave them vulnerable to error or misuse.
Limited assurance	Risk, control, and governance systems have some satisfactory aspects. There are, however, some significant weaknesses likely to undermine the achievement of objectives and leave them vulnerable to an unacceptable risk of error or misuse.
No assurance	The systems for risk, control, and governance are ineffectively designed and operated. Objectives are not being achieved and the risk of serious error or misuse is unacceptable. Significant improvements are required.

Current Internal Audit Assurance Work in Progress

2.5 Internal Audit assurance work in progress to deliver the Internal Audit Annual Plan 2019/20 consists of the following:

Audit Area	Audit Stage
Leisure Management Booking System	Drafting the Report
Community Engagement	Drafting the Report
ICT Operational Processes	Drafting the Report
Capital Investment	Testing underway
Workforce Planning	Testing underway
Information Governance (Records Management)	Testing underway
Automated Invoice Payments	Planning underway

Internal Audit Consultancy and Other Work

- 2.6 Internal Audit staff have been involved in the following for the Council to meet its aims and objectives, and its roles and responsibilities in accordance with the approved Internal Audit Charter and Strategy:
- In its critical friend role provided an independent view and challenge at various forums including Business Transformation Board, Capital Plan and Asset Management Board, Learning Estate Strategy Board, and Information Management Group.
 - Monitored publication of Audit Scotland reports and co-ordinated submission by Management of Audit Scotland Reports to the Audit Committee or other Committee as relevant.
 - Attended and provided support for the Serious and Organised Crime Group (Principal Internal Auditor).
 - Consultation on development of Audit Plan 2020/21.

Recommendations

2.6 Recommendations in reports are suggested changes to existing procedures or processes to improve the controls or to introduce controls where none exist. The grading of each recommendation reflects the risk assessment of non-implementation, being the product of the likelihood of the risk materialising and its impact:

High: Significant weaknesses in existing controls, leaving the Council or Service open to error, fraud, financial loss or reputational damage, where the risk is sufficiently high to require immediate action within one month of formally raising the issue. Added to the relevant Risk Register and included in the relevant Assurance Statement.
Medium: Substantial weaknesses in existing controls, leaving the Council or Service open to medium risk of error, fraud, financial loss or reputational damage requiring reasonably urgent action within three months of formally raising the issue.
Low: Moderate weaknesses in existing controls, leaving the Council or Service open to low risk of error, fraud, financial loss or reputational damage requiring action within six months of formally raising the issue to improve efficiency, effectiveness and economy of operations or which otherwise require to be brought to attention of senior management.
Outwith the report, Internal Audit informs operational managers about other matters as part of continuous improvement.

2.7 The table below summarises the number of Internal Audit recommendations made during 2019/20:

	2019/20 Number of Recs
High	9
Medium	6
Low	0
Sub-total reported this period	15
Previously reported	33
Total	48
Recommendations agreed with action plan	48
Not agreed; risk accepted	0
Total	48

3. Report Implications

3.1 Resource

Resource implications of implementing Internal Audit recommendations are considered as part of the audit process to ensure these are reasonable and proportionate to the risks.

3.2 Risk

The PSIAS require Internal Audit to evaluate the effectiveness of the Council's Risk Management arrangements and contribute to improvements in the process. At the start of each audit engagement, to capture potential areas of risk and uncertainty more fully, key stakeholders have been consulted and risk registers have been considered. During each audit engagement the management of risk has been tested.

It is anticipated that improvements in the management and mitigation of risks will arise as a direct result of Management implementing the Internal Audit recommendations made. If audit recommendations are not implemented, there is a greater risk of financial loss and/or reduced operational efficiency and effectiveness, and Management may not be able to demonstrate improvement in internal control and governance arrangements, and effective management of risks.

3.3 Single Midlothian Plan

Themes addressed in this report:

- Community safety
- Adult health, care and housing
- Getting it right for every Midlothian child
- Improving opportunities in Midlothian
- Sustainable growth
- Business transformation and Best Value
- None of the above

3.4 Key Priorities within the Single Midlothian Plan

Midlothian Council and its Community Planning Partners include the following areas as key priorities under the Single Midlothian Plan:

- Reducing the gap in learning outcomes
- Reducing the gap in health outcomes
- Reducing the gap in economic circumstances

3.5 Impact on Performance and Outcomes

The Findings and Recommendations from Internal Audit work during the year assists the Council in improving its performance and outcomes.

3.6 Adopting a Preventative Approach

Internal Audit assurance work includes assessments on when a preventative approach can be adopted.

3.7 Involving Communities and Other Stakeholders

This report has been presented to the Corporate Management Team (comprising Chief Executive, Executive Directors and Chief Officers) to outline the key messages of assurance and areas of improvement. Directors, Chief Officers, Heads of Service and Managers relevant to the area audited have agreed the final Internal Audit reports as set out in the relevant Executive Summary within Appendix 1.

3.8 Ensuring Equalities

There are no equalities issues with regard to this report.

3.9 Supporting Sustainable Development

There are no sustainability issues with regard to this report.

3.10 IT Issues

There are no IT issues with regard to this report.

4. Recommendations

The Audit Committee is asked to:

- a) Note the final assurance reports issued in the period from 1 January to 20 February 2020 associated with the delivery of the approved Internal Audit Annual Plan 2019/20; and
- b) Acknowledge the assurance provided on internal controls and governance arrangements in place for the areas covered by this Internal Audit work.

Date: 20 February 2020
Report Authors: Jill Stacey, Chief Internal Auditor
E-Mail: Jill.Stacey@midlothian.gov.uk

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
<p>Subject: Procurement and Management of Contracts</p> <p>Category: Assurance - Risk</p> <p>Date issued: 3 December 2019 Draft; 06 February 2020 Final</p> <p>Level of Assurance: Limited</p>	<p>The purpose of this assurance audit was to review the high level controls and governance arrangements surrounding the Procurement and Management of Contracts.</p> <p>Midlothian Council's Procurement Strategy for 2018 to 2023 states that: as a procuring / contracting authority Midlothian has five strategic themes: Economic Benefits, Social Benefits, Environmental Benefits, Commercial Efficiency, and Contract and Supplier Management. It outlines the central role of the Procurement function in supporting the Council to achieve its strategic priorities within a constrained financial envelope. Midlothian Council delivers contracts in excess of £100m every year, therefore it is important that robust processes and procedures are in place to protect the Council and public against criminal activity.</p> <p>The Council's Procurement team is centralised within Corporate Solutions (formerly FISS) and is managed in the interim by the Legal Services Manager. The Construction team within Property & Facilities Management undertake their own procurement exercises.</p> <p>Internal Audit considers that the level of assurance we are able to give is Limited Assurance. The Procurement team has undergone a significant turnover of staff over the past year and lacks the capacity and resilience to deliver its strategic priorities. There are a number of contracts that have expired and have not been retendered, there are delays undertaking tender exercises, and there is a lack of oversight of other areas undertaking tender exercises. There is no system in place to manage contracts from cradle to grave and no dedicated contract monitoring resource. There is a lack of formal reporting of any contract monitoring undertaken by Services and the Procurement team does not have oversight of this.</p> <p>Any issues arising have been communicated directly to relevant Service Management as they were identified. However some of these are still ongoing as part of the Corporate Fraud activity on contract management compliance.</p>	3	3	0	<p>Management have agreed the factual accuracy of the report, accepted the report findings, and agreed the implementation of the Internal Audit recommendations.</p> <p>CMT has discussed the report and supported the recommended improvements, encouraging their implementation as a matter of urgency.</p>

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
Subject: Procurement and Management of Contracts (cont'd)	<p>We made the following recommendations:</p> <ul style="list-style-type: none"> Plans for the future delivery of the Procurement function should be urgently implemented to ensure there is sufficient capacity to deliver an effective and efficient service. This should include suitable resource to oversee all procurement and contract management activities undertaken across the Council. (High) Contracts that have expired should be urgently retendered to ensure that the Council is obtaining best value. (High) Regular meetings with Procurement to discuss service delivery strategy, new areas of spend, contracts that have / are due to expire, current service provision including any off contract spend and supplier performance (mirroring the Commissioning and Contracts meetings held by the Health and Social Care Directorate) should be held by all Directorates. (High) Contract and supplier management processes require to be strengthened across the Council. This should include ensuring that there is a contracts management system to manage contracts from cradle to grave, ensuring there is dedicated resource to monitor and manage contractors and ensuring that there are sufficient performance measures built into every contract to allow for adequate monitoring. (Medium) The improvement actions arising from the Scotland Excel PCIP assessments, the Council's self-evaluation, and audit recommendations should be progressed. (Medium) A Quality Assurance arrangement should be developed and implemented as a matter of urgency to ensure the necessary improvement actions are being implemented and to continuously improve this service area. (Medium) 				<p>Progress has already been made on their implementation, as set out below:</p> <p>Discussions have been held with other Councils to engage suitable resource to oversee current procurement activity through shared services or other routes.</p> <p>Work is underway to identify and re-tender expired contracts which includes the use of Non-Competitive Action authorisations in the short-term.</p> <p>Regular meetings between Services and Procurement are being held.</p>

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
<p>Subject: Change and Transformation Programme</p> <p>Category: Assurance - Risk</p> <p>Date issued: 09 January 2020 Draft; 12 February 2020 Final</p> <p>Level of Assurance: Limited</p>	<p>The purpose of this assurance audit was to review progress made with the implementation of improvements to ensure that the governance and accountability arrangements for transformation are effective.</p> <p>Since our previous report considerable work has been undertaken to improve processes for delivering the transformation programme, though this will take time to embed before benefits are fully realised.</p> <p>The Chief Executive, supported by Senior Officers, is providing the impetus for change in order for the Council to deliver quality services on a financially sustainable basis. The Medium Term Financial Strategy (MTFS) is an important step but is yet to fully address budget gaps in later years.</p> <p>Governance arrangements are in place to monitor the delivery of the various initiatives within the transformation programme, but their efficiency and effectiveness could be further improved.</p> <p>Neither the Business Transformation Board (BTB) nor Business Transformation Steering Group (BTSG) have been adequately sighted on the planning behind the delivery of all savings. The quality of planning is variable; the majority ranging from no implementation plan in place to outline plans requiring further work. Some Service areas have fully engaged with Finance allowing for their much closer involvement; others have not and consequently the financial efficacy of those plans is unclear.</p> <p>For the 2019/20 year further progress is being made but concerns exist over delivering all savings and in particular efficiency savings. Savings are not sufficiently ambitious and are not suitably cross cutting.</p> <p>At present savings are listed as proposals in multiple programmes, including the old Delivering Excellence Programme, the Resource Allocation Programme, and MTFS, which incorporate a large number of predominantly low value, single service cost cutting proposals partly due to carry forward of non-delivery of prior year savings.</p> <p>The approach to consolidating the various programmes for monitoring and reporting purposes by Directorate is known as the Dashboard which is evolving. Dashboards are aligned to the quarterly budget monitoring and do not present information in a sufficiently concise format.</p> <p>The four recommendations made in our previous report are shown as 100% complete based upon the development and approval of the MTFS.</p>	5	1	0	<p>Management have agreed the factual accuracy of the report, accepted the report findings and agreed the implementation of the Internal Audit recommendations.</p> <p>CMT have discussed the report and supported the recommended improvements.</p>

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
Subject: Change and Transformation Programme (cont'd)	<p>Internal Audit is able to give Limited assurance (Risk, control, and governance systems have some satisfactory aspects; however, there are some significant issues likely to undermine the achievement of objectives). Subsequent to the completion of audit fieldwork, action has been taken to improve further governance, scrutiny, focus and reporting arrangements. We consider that action taken to date together with prompt and full implementation of the recommendations set out below will significantly improve the effectiveness of governance and accountability arrangements:</p> <ul style="list-style-type: none"> • Governance structures for the Change and Transformation Programme should be fully defined. The roles and responsibilities of both the BTB and BTSG require clear definition through up to date terms of reference which set out the relationship between the BTB and BTSG. (Medium) • Governance exercised by BTSG should be more strategic and provide better political steer. It should also provide greater challenge when approving proposals for delivering transformation for onward approval by Council. (High) • BTB and BTSG should now concentrate on the programme for later years and manage the programme for the current year as far as possible on an exception basis. (High) • Service areas should place greater emphasis on developing truly ambitious initiatives which will transform the way that services are delivered. As transformational changes may have long lead times this work should be undertaken at the earliest opportunity. Each Directorate should have a change Board to develop savings proposals and implementation plans, and monitor their delivery (High) • BTB should call in underlying plans for existing higher value proposals and assess how robust/realistic those plans are in terms of delivery. Where Finance have already completed an assessment BTB should have due regard to their findings and undertake further enquiry where appropriate. In future where a proposal has significant financial implications BTB should review the planning documentation and satisfy themselves as to the viability of the initiative before allowing admission to the programme. (High) • All savings should be consolidated within a single programme under the Medium Term Financial Strategy by Service by Directorate. (High) 				<p>Progress has already been made on their implementation, as set out below:</p> <p>Revised terms of reference will be presented to BTB and BTSG in February 2020.</p> <p>Focus on future year's implementation plans is underway.</p> <p>Building on the areas where positive transformation has taken place.</p> <p>Work has already commenced on consolidating this into one programme.</p>

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
<p>Subject: Business Planning, Budget Setting and Monitoring</p> <p>Category: Assurance - Risk</p> <p>Date issued: 09 January 2020 Draft; 20 February 2020 Final</p> <p>Level of Assurance: Limited</p>	<p>The purpose of this assurance audit was to evaluate the implementation of improvements to ensure that budgets set for 2019/20 are sustainable and based on realistic plans which are subjected to appropriate scrutiny and challenge.</p> <p>Since our previous report work is ongoing to improve processes for budgetary control, though this will take time to embed before benefits are fully realised. Action has been taken to attempt to stabilise the Council's financial position; driven by the Chief Executive supported by Senior Officers and the Financial Services team. Positive steps taken include:</p> <ul style="list-style-type: none"> • setting a balanced budget for 2019/20 and beyond which does not further deplete the General Fund Balance; • provision of clarity on budget holders' accountability and responsibility to manage within set budgets and not overspend as part of good financial discipline; • improved scrutiny of quarterly financial outcomes for directorates through meetings between the Directors, Heads of Service and the Chief Executive; • development of a Medium Term Financial Strategy and Reserves Strategy; and • five of the seven recommendations made in our previous report have been implemented whilst two remain incomplete. <p>Some improvements have been made to Budget monitoring and reporting processes. There is evidence of improved engagement between the Financial Services team and Budget Holders. Work is underway to address the issues associated with feeder systems and business processes which impact on the completeness of the information available on which to prepare projections.</p> <p>We completed our audit fieldwork in November 2019 and our report reflects our findings at that time. Internal Audit considers that the level of assurance we are able to give is Limited Assurance relating to budgets set for 2019/20 and associated monitoring and reporting processes. Risk, control, and governance systems have some satisfactory aspects. Some improvements have been made in the last 9 months as noted above though further improvements are required.</p>	1	2	0	<p>Management have agreed the factual accuracy of the report, accepted the report findings and agreed the implementation of the Internal Audit recommendations.</p> <p>CMT have discussed the report and supported the recommended improvements.</p> <p>The proposed Internal Audit planned for 2020/21 on Business Planning, Budget Setting and Monitoring will be scheduled early in the year to cover business and financial planning processes for 2020/21 which will be used by Management to inform the processes for 2021/22.</p>

Report	Summary of key findings and recommendations	Recommendations			Status
		H	M	L	
Subject: Business Planning, Budget Setting and Monitoring (cont'd)	<p>Concurrent with and subsequent to audit fieldwork relating to budget sets for 2019/20, further work is ongoing by Management to improve budgetary control through the financial planning process for 2020/21. We consider that ongoing work together with prompt and full implementation of the two remaining previous recommendations and the further three recommendations set out below will improve the effectiveness of budget setting, budget monitoring and reporting processes:</p> <ul style="list-style-type: none"> • A risk assessment should be carried out in conjunction with the review of the Reserves Strategy of elements that could potentially call on uncommitted reserves. (High) • The Financial Services team should review budget monitoring reporting at other local authorities of a similar size to Midlothian. Opportunities exist to present reports in more detail and with greater clarity for users than are currently produced; a fuller explanation of the reasons and implications of revisions to budgets during the year would be helpful to aid all stakeholders in their understanding of the budget position. (Medium) • As the position with savings will need to be assessed as part of the quarterly budget monitoring, reporting progress with the achievement of savings targets should be integrated into the budget monitoring reports and then reused for reporting to BTB and BTSG. (Medium) 				<p>Progress has already been made on their implementation, as set out below:</p> <p>In finalising the 2020/21 budget a risk adjustment of £0.4m (approx. 10% of savings) has been included to partly mitigate any shortfall in savings impacting directly on the reserves position.</p> <p>An examination of other authorities' reports is being undertaken with the aim to incorporate any improvements in 2020/21 Q1 report.</p> <p>A refreshed approach to BTB dashboards is currently being rolled out with information fully integrated to reflect the budgeted savings and be consistent with information reported in financial monitoring reports.</p>