

WEST MERCIA ENERGY INTERNAL AUDIT ANNUAL REPORT 2014/15

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1. Summary

This annual report provides members with details of the work undertaken by Internal Audit for the year ended 31 March 2015. It reports on progress against the annual audit plan. It also provides the Head of Audit's (Audit Service Manager's) opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and internal controls, as required by the Public Sector Internal Audit Standards, which in turn contributes to the review of the effectiveness of the systems of internal control as required by the Accounts and Audit Regulations 2011 4(2).

Final performance has been good with 100% of the revised plan being delivered.

Four good and three reasonable assurances were made in 2014/15, together with one limited assurance in respect of Risk Management. The significant issues in respect of the Risk Management Audit have been reviewed by management in the financial year and an updated Risk Management Policy was agreed by the Joint Committee in February 2015.

A total of 22 recommendations have been made in the eight audit reports issued in the year. No fundamental recommendations have been made during 2014/15.

On the basis of the work undertaken and management responses received; the organisation's governance, risk management and internal control processes are sound and working effectively and the Audit Service Manager is able to deliver a positive year end opinion on West Mercia Energy's internal control environment for 2014/15.

2. Recommendations

The Committee are asked to note;

- a) Performance against the Audit Plan for the year ended 31 March 2015.
- b) That the system of governance, risk management and internal control is operating effectively and can be relied upon when considering the Annual Governance Statement for 2014/15.
- c) The Audit Service Manager's positive year end opinion on West Mercia Energy's governance, risk management and internal control environment for 2014/15 on the basis of the work undertaken and management responses received.

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 The delivery of a risk based Internal Audit Plan is an essential part of ensuring probity and soundness of the organisation's financial, governance and risk management systems and procedures and is closely aligned to the West Mercia Energy risk register. The Plan is delivered in an effective manner; where Internal Audit independently and objectively examines, evaluates and reports on the adequacy of its customers control environments as a contribution to the proper, economic, efficient and effective use of resources. It provides assurances on the internal control systems, by identifying areas for improvement or potential weaknesses and engaging with management to address these in respect of current systems and during system design. Failure to maintain robust internal controls create an environment where poor performance, fraud, irregularity and inefficiency can go undetected leading to financial loss and reputational damage.
- 3.2 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998 and the Accounts and Audit Regulations 2011.
- 3.3 There are no direct environmental, equalities or climate change consequences of this proposal.
- 3.4 Internal Audit customers are consulted on the service that they receive, feedback from which is included in this report and continues to be positive.

4. Financial Implications

- 4.1 The Internal Audit plan is delivered within approved budgets; the work of Internal Audit contributes to improving the efficiency, effectiveness and economic management of the organisation.

5. Background

- 5.1 This report is the culmination of the work of the Internal Audit team during 2014/15 and seeks to:

- Provide an opinion on the adequacy of the risk management, control and governance arrangements;
 - Inform the annual review of the effectiveness of its system of internal control that informs the Annual Governance Statement by commenting on the nature and extent of significant risks; and
 - Inform the review of an effective Internal Audit by providing performance data against the plan.
- 5.2 The requirement for Internal Audit derives from local government legislation, including section 151 of the Local Government Act 1972 which requires the Authority to make arrangements for the proper administration of its financial affairs. Proper administration includes Internal Audit. More specific requirements are detailed in the Accounts and Audit Regulations 2011, in that “a relevant body must undertake an adequate and effective internal audit of its accounting records and systems of internal control in accordance with the proper practices in relation to internal control”.
- 5.3 The Accounts and Audit Regulations 2015 have been issued and apply from the start of the financial year 2015/16. The existing requirement, to have internal audit undertake an effective internal audit of accounting records and systems of internal control in accordance with proper practices, has been updated to: ‘evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance’. There are some changes to the access rights of internal audit requiring the organisation to supply any documents, records and information and explanations as are considered necessary by the internal auditors. In addition, organisations are no longer required to undertake an annual review of effectiveness, although audit committees should note the requirements of the Public Sector Internal Audit Standards to maintain an ongoing programme of quality assessment and improvement.
- 5.4 The Public Sector Internal Audit Standards (PSIAS) define the scope of the annual report on internal audit activity. The annual report must incorporate an annual internal audit opinion on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and internal control. This annual report provides information to support that assessment and that an effective Internal Audit is established for West Mercia Energy, in accordance with the requirements of the 2011 Accounts and Audit Regulations. The Internal Audit Service is provided by Shropshire Council. In June 2015, a paper is to be presented to Shropshire Council’s Audit Committee which provides assurance on the effectiveness of the Internal Audit service against the PSIAS. West Mercia Energy can take assurance from this report.
- 5.5 Internal Audit operates a strategic risk based plan. The plan is reviewed each year to ensure that suitable audit time and resources are devoted to reviewing the more significant areas of risk, this results in a comprehensive range of audits undertaken in the year, to support the overall opinion on the control environment. The plan contains a small provision for contingency provision;

any unforeseen work demands that may arise, i.e. special investigations, are delivered in addition to the planned work in agreement with the Director.

Annual Internal Audit Opinion from Internal Audit Work undertaken during 2014/15

- 5.6 It is the responsibility of West Mercia Energy to develop and maintain the internal control framework. In undertaking its work, Internal Audit has a responsibility under the Public Sector Internal Audit Standards to deliver an annual internal audit opinion and report. The annual internal audit opinion will conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and internal control. This opinion plays a key part in informing West Mercia Energy's Annual Governance Statement.
- 5.7 The results of individual audits, when combined, form the basis for the overall opinion on the adequacy of the organisation's internal control systems. No system of internal control can provide absolute assurance against material misstatement or loss, nor can Internal Audit give that absolute assurance. The work of Internal Audit is intended only to provide reasonable assurance on controls on the basis of the work undertaken. In assessing the level of assurance to be given, I have taken into account:
- The work undertaken on the fundamental financial systems. Whilst revealing a small number of areas of weakness and identifying areas for improvement, there are no significant material weaknesses that could result in a material misstatement in the accounts and reliance can be placed upon them. Plans have been adopted to manage outstanding concerns.
 - The work undertaken in respect of risk management highlighted two significant weaknesses in respect of the categorisation and reporting of risk to the Joint Committee. The report was accepted by management and a revised risk management policy and update provided to the Joint Committee in February 2015. The review also highlighted gaps in documentation and management processes. Management have provided full assurance to address the improvements noted.
- 5.8 These assurances are provided on the basis that management carry out the actions they have agreed in respect of the recommendations made to address any weakness identified and improvements suggested.

On the basis of the work undertaken and management responses received; the organisation's governance, risk management and internal control processes are sound and working effectively and the Audit Service Manager is able to deliver a positive year end opinion on West Mercia Energy's internal control environment for 2014/15.

Key Assurances provided during 2014/15

5.9 Audit assurance opinions are awarded on completion of audit reviews reflecting the efficiency and effectiveness of the controls in place, opinions are graded as follows:

Good	Evaluation and testing of the controls that are in place confirmed that, in the areas examined, there is a sound system of control in place which is designed to address relevant risks, with controls being consistently applied.
Reasonable	Evaluation and testing of the controls that are in place confirmed that, in the areas examined, there is generally a sound system of control but there is evidence of non-compliance with some of the controls.
Limited	Evaluation and testing of the controls that are in place performed in the areas examined identified that, whilst there is basically a sound system of control, there are weaknesses in the system that leaves some risks not addressed and there is evidence of non-compliance with some key control.
Unsatisfactory	Evaluation and testing of the controls that are in place identified that the system of control is weak and there is evidence of non-compliance with the controls that do exist. This exposes the organisation to high risks that should have been managed.

Audit assurance opinions delivered in 2014/15

Audit	Good	Reasonable	Limited	Unsatisfactory
Corporate Governance		✓		
Risk Management			✓	
Creditors	✓			
Procurement		✓		
Finance	✓			
Debtors	✓			
Payroll	✓			
General IT Controls		✓		
Total for year				
➤ numbers	4	3	1	0
➤ percentage	50%	37.5%	12.5%	0%

5.10 Four good, three reasonable and one limited assurance were issued during the financial year. Positive responses to recommendations have been received by management and will be followed up next year to determine whether satisfactory improvements have been made.

5.11 The Internal Audit team has achieved 100% of the plan which is in line with its target.

5.12 Audit recommendations are also an indicator of the effectiveness of the internal control environment and are rated according to their priority:

Best Practice (BP)	Proposed improvement, rather than addressing a risk.
Requires Attention (RA)	Addressing a minor control weakness or housekeeping issue.
Significant (S)	Addressing a significant control weakness where the system may be working but errors may go undetected.
Fundamental (F)	Immediate action required to address major control weakness that, if not addressed, could lead to material loss.

5.13 Recommendations are rated in relation to the audit area rather than the organisation's control environment, for example, a control weakness deemed serious in one area which results in a significant or fundamental recommendation may not affect the overall control environment. Similarly, a number of significant recommendations in a small number of areas would not result in a limited opinion if the majority of areas examined were sound, consequently, the number of significant recommendations in the table below will not necessarily correlate directly with the number of limited assurance opinions issued in above. Any significant or fundamental recommendations resulting from a control weakness in West Mercia Energy's control environment would be reported in detail to the Joint Committee.

5.14 A total of 22 recommendations have been made in the eight audit reports issued in the year; these are broken down by audit area in the table below.

Audit opinion and recommendations made on 2014/15 audits

Audit	Level of Assurance Given	Number of Recommendations made				Total
		BP	RA	S	F	
Corporate Governance	Reasonable		5	1		6
Risk Management	Limited		4	2		6
Creditors	Good		3			3
Procurement	Reasonable			1		1
Finance	Good		1			1
Debtors	Good		1			1
Payroll	Good		1			1
General IT Controls	Reasonable		1	2		3
Total for year						
➤ numbers		0	16	6	0	22
➤ percentage		0%	72.7%	27.3%	0%	100%

- 5.15 It is management's responsibility to ensure that accepted audit recommendations are implemented within an agreed timescale. With the exception of annual audits where recommendations are revisited as a matter of course; remaining recommendations are followed up annually by obtaining an update from management on progress made and performing sample testing. No recommendations have been rejected in the year by management.

Audit Performance

- 5.16 Audit Performance is demonstrated by measuring achievement against the plan, ensuring compliance against the Public Sector Internal Audit Standards, and evaluating improvements made over the last twelve months. The effectiveness of Internal Audit is further reviewed through the Audit Committee's delivery of its responsibilities and direct from customers as they provided responses to surveys sent out after each audit.

Reporting

- 5.17 All Internal Audit work is reviewed by a senior auditor to ensure it complies with Internal Audit's standards and that the recommendations made are supported by the work undertaken before any audit reports are issued. This is seen as a fundamental part of ensuring audit quality and that clients receive reports which are both informative, useful and add value to their work processes and procedures.
- 5.18 All audit assignments are subject to formal feedback to management. Draft reports are issued to the managers responsible for the area under review for agreement to the factual accuracy of findings and recommendations. After agreement, a formal implementation plan containing management's agreed actions and comments is issued to relevant officers. Follow up reviews capture evidence of implementation of recommendations.

Quality Assurance/Customer Feedback Survey

- 5.19 A customer feedback survey form is sent out with the all audits completed. These provide key feedback on the quality of audit service in relation to a number of areas, including:
- Pre auditing arrangements;
 - Post audit briefings;
 - Audit coverage/scope of the audit;
 - Timeliness of production of report;
 - Accuracy and clarity of the report;
 - Practicality of recommendations;
 - Professionalism of approach;
 - Communication skills and
 - Timeliness of audit to your business.
- 5.20 The surveys are a key part of ensuring the work meets our client expectations and that the quality of audit work is maintained. The results have been analysed over the last year and the percentage of responses are identified in the table below:

Customer Feedback Survey Forms - percentage of excellent and good responses

Item Being Scored	2014/15
Pre-audit arrangements	100%
Post-audit briefing	100%
Audit coverage/scope of the audit	100%
Timeliness of production of report	100%
Accuracy and clarity of report	100%
Practicality of recommendations	100%
Professionalism of approach	100%
Communication skills	100%
Timeliness of audit to your business	100%
Number of forms returned	6

5.21 Overall the results are pleasing, showing services delivered consistently at a high level. The information is used both to improve techniques overall within the team and at annual performance appraisals to identify future development focus relating to individual skills or competences.

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

- Proposed 2012/13 to 2015/16 Internal Audit Programme - Audit Committee on 25 February 2013.
- Public Sector Internal Audit Standards.
- Accounts and Audit Regulations 2011 and 2015