BUSINESS ASSURANCE
Final Internal Audit Assurance Report 2016/17

Effectiveness of Audit Committee

18th November 2016

Overall IA Assurance Opinion:
REASONABLE

Recommendation Overview:

High Risk	0
Medium Risk	4
Low Risk	3
Notable Practice	0

Review Sponsor:

Fran Beasley	Chief Executive and Corporate Director of Administration

Report Distribution:

Audit Committee	All Audit Committee Members (including the Independent Chairman and substitute Audit Committee Members)
Lloyd White	Head of Democratic Services
Khalid Ahmed	Democratic Services Manager
Muir Laurie	Head of Business Assurance

Ownership of all final Internal Audit assurance reports rests with the relevant Audit Sponsor. However, we will disclose final Internal Audit assurance reports to the Audit Committee upon their specific request.

1. Introduction

1.1 This risk based Internal Audit (IA) assurance review forms part of the 2016/17 Quarter 2 IA Operational Plan, presented to Audit Committee on 12th July 2016. **The purpose of this review is to provide assurance to the Corporate Management Team (CMT) and the Audit Committee over the key risks in relation to the Effectiveness of the Audit Committee, as follows:**

- The scope of work to be performed by the Audit Committee is not suitably defined in the Terms of Reference and therefore it may not encompass all the assurance needs of the Council and the Cabinet. As a result there is an increased risk that the Audit Committee is not performing its role and responsibilities in line with best practice guidelines;

- The Audit Committee members are not suitably independent and objective, resulting in potential biased and ineffective decisions being made. Members may not have a good understanding of the Council's objectives, priorities, risks and strategies and therefore decision making by the Audit Committee may not be suitably aligned;

- The Audit Committee does not contain or have at its disposal an appropriate mix of skills or its Members may not have been adequately trained. Consequently, there is a risk that Members may not be able to perform their duties effectively and fulfil the requirements of their role, which may result in reputational damage for the council;

- The Audit Committee does not effectively support the Council by reviewing and scrutinising the completeness of key documentation to satisfy their needs, and by reviewing the reliability and integrity of documentation. As a result, the Council may be in breach of their statutory obligations which could cause reputational damage or financial loss for the Council;

- The Audit Committee does not engage effectively with financial and performance reporting issues, and with the work of key stakeholders, primarily IA and External Audit; Furthermore, the Audit Committee may not communicate effectively with the Council's CMT, Cabinet and other stakeholders. This may result in a loss of public money resulting in adverse public reaction and reputational loss; and

- The Audit Committee's reputational image amongst other local authorities audit committee's is considered weak and ineffective in its role, scrutiny, decision making and therefore may result in further adverse reputational damage for the Council.

1.2 This report is produced on an exception basis, highlighting the key aspects from the IA assurance review to management. Further detailed findings are available upon specific request.

2. Background

2.1 An effective and independent Audit Committee (AC) is a key component of the Council's corporate governance and risk management framework. The purpose of an AC is to provide those charged with governance independent assurance on the adequacy of the risk management framework, the internal control environment and the integrity of the financial reporting and annual governance processes.

2.2 An effective AC leads to improved internal control, risk management and financial reporting. It provides a forum for discussing key issues raised by IA and External Audit, working independently to provide assurance to the Council.

2.3 CIPFA best practice guidance states that in order for the AC to be fully effective and therefore able to provide meaningful advice to the Council, its Members need to be independent, diligent, knowledgeable, and receive relevant, timely and reliable information. This guidance also indicates that AC Members must be in a position to challenge Directors and the Cabinet and draw attention to any governance weaknesses.

2.4 Best practice guidance also states the AC should have clear reporting lines and unrestricted rights of access to other Council committees and senior managers (as required). In addition, the AC will have sufficient administrative support and access to all relevant and timely information.

2.5 The AC currently comprises of five members including an independent Chair. The remainder of the Committee, in accordance with best practice, is representative of the political make up of the Council which helps to ensure that no political agenda is given priority at meetings with decisions made by the Committee are free from political influence.

3. Executive Summary

3.1 Overall, the IA opinion is that we are able to give **REASONABLE** assurance over the key risks to the achievement of objectives for Effectiveness of the AC. Definitions of the IA assurance levels and IA risk ratings are included at **Appendix C**.

3.2 We were pleased to confirm that the AC's Terms of Reference (located within the Council's Constitution) is appropriately made available to its users in addition to being presented within each meeting agenda. It was however identified that the Terms of Reference has not been subject to review since May 2013.

3.3 In addition, AC report packs are issued to members six working days in advance of a meeting, which is in line with best practice and provides sufficient time to allow AC members to review reports ahead of meetings. Furthermore, it was confirmed through our bench-marking exercise against nine other local authorities that relevant and appropriate documentation is provided to the AC for review.

3.4 It was confirmed that the composition of the committee is in line with the Constitutional requirements, with four elected Councillors and an independent Chairman and the Vice-Chair from the majority group. However, a bench-marking exercise, assessing LBH against nine other local authorities, identified that an average committee membership consisted of six Members. With quorate currently requiring four members, there is an increased likelihood of AC meetings being delayed or cancelled. Assessment of Member's attendance to the first AC meeting of 2016/17 (12th July 2016) was the lowest with only two Members present and therefore requiring two substitutes to meet quorum requirements.

3.5 We undertook a review of the last six meetings of the AC and noted that, due to unforeseen circumstances, two Members, including the Independent Chairman, were unable to attend two of the last six AC meetings. We are aware that the Council's Constitution (Section 2.05b) places responsibilities on Members and co-opted Members for meeting attendance. Further, upon discussion of this issue with Democratic Services, we were advised that no role description is in place for the Independent Chairman, outlining their role, responsibilities and the Council's expectations.

3.6 Declarations of interests are initially completed by members following election via the "Register of Interest Form", which we were able to confirm evidence of for all four elected committee members. It was however noted that the Independent Chairman's latest declaration was completed in November 2014. In addition, any conflicts of interests arising through meeting agenda items are required to be declared at the commencement of the AC meeting and recorded within meeting minutes. Review of the last six committee minutes identified one instance where there was no record within the meeting minutes that the agenda item "Declaration of Interests" was discussed.

3.7 During the assurance review, we concluded that, whilst AC Members inherently possess key attributes required of committee Members, there is still a requirement to understand relevant service areas across the Council where further specific AC related training is necessary. AC Members had previously been consulted on a Skills Matrix developed by the Head of Business Assurance (HBA).

3.8   Whilst there was some appetite from Committee Members for this, we note this has not been progressed further by Democratic Services. The Skills Matrix would help in the identification of specific AC training requirements and help inform a tailored Training and Development Plan (T&DP) for AC Members. This gap, coupled with the limited induction process upon appointment, may impact the effectiveness of the Audit Committee.

3.9   As recorded within the AC's ToR, an Annual Report is required to be submitted to Full Council on the activities of the AC. It was confirmed that this was last completed and submitted to AC in 2013/14, although was not subsequently presented to Full Council for consideration. In addition, no annual report has been produced by the AC and reported to Council for 2014/15 or 2015/16.

3.10   It was also identified that a formal assurance mapping exercise to identify the sources of assurance from across the Council is currently not in place. This was also raised within the IA 15/16 Assurance Review of the Effectiveness of the AC and the recent IA 16/17 Assurance Review of the Effectiveness of IA. As a result we will not be re-raising this recommendation within this assurance review.

3.11   The detailed findings and conclusions of our testing which underpin the above IA opinion have been discussed at the exit meeting with the Head of Democratic Services and the Democratic Services Manager and are available to management upon specific request. The key findings and IA recommendations raised in respect of the risk and control issues identified are set out in the Management Action Plan included at **Appendix A**. Good practice suggestions and notable practices are set out in **Appendix B** of the report.
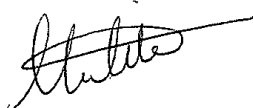
4. Acknowledgement

4.1   Business Assurance would like to formally thank all of the officers contacted during the course of this review for their co-operation and assistance. In particular the Democratic Services Manager, whose advice and help were gratefully appreciated.

5. Business Assurance Contact Details

This audit was led by: Priyanka Mittal
                                Senior Internal Auditor

This audit was reviewed by: Elaine Polton CPFA
                                Assistant Internal Audit Manager

Thank you,

Martyn White, CIA
Senior Internal Audit Manager

Management Action Plan

No.	Key Finding
1	It was confirmed through reviewing Council meeting minutes that the Audit Committee's (AC) Terms of Reference (ToR) was last reviewed on the 9th May 2013. Examination of the AC ToR identified the following inconsistencies: • Item 2 of the ToR states that the AC will *"Make recommendations to the Leader of the Council and Cabinet Member for Finance, Property and Business Services on any changes to the Council's Internal Audit Strategy"*. However, it was confirmed that this does not accurately reflect current practice undertaken by the AC; • Item 5 of the ToR states that the AC will *"Following a request to the Corporate Director of Finance, and subject to the approval of the Leader of the Council and Cabinet Member for Finance, Property and Business Services, to commission work from Internal Audit"*. Once again this does not reflect current practices undertaken by the AC in regards to the Council's Internal Audit function; • Item 16 of the ToR states that the AC will *"Review and monitor Council policies on 'Raising Concerns at Work' and anti-fraud and anti-corruption strategy and the Council's complaints process, making any recommendations on changed to the Leader of the Council and the Deputy Chief Executive and Corporate Director of Resident Services"*. We were unable to evidence that the AC considered aspects of review and monitoring of the Raising Concerns at Work policy or the complaints process within the last 3 years; and • Item 17 of the ToR states that the AC is required to *"Oversee the production of the authority's Statement of Internal Control and recommend its adoption"*. However this terminology is incorrect as Statement of Internal Control ceased to exist in 2008 and was subsequently replaced by the Annual Governance Statement. In addition, assessment of the AC ToR against best practice guidance developed by CIPFA (Practical Guidance for Local Authorities & Police, December 2013) and HM Treasury (Audit and Risk assurance Committee Handbook, March 2016), identified the following missing information: • Rights of AC Members; • Access rights of the Head of Internal Audit & External Audit representative to the Chair of the Committee; • Meeting requirements (frequency & quorum); and • Information Requirements to be provided to AC for review, e.g. External Audit report; Internal Audit report; Corporate Risk Register; Statement of Accounts; Governance Statement; and Risk Management Strategy. Whilst we confirmed that some of the above information (i.e. Committee Members & quorum) is recorded within the Council's Constitution, this is not specifically within the AC's ToR. This issue was raised within the 2015/16 review and we note this has not been implemented.

Management Action Plan

Risk	Recommendation	Management Action Proposed	Risk Owner & Implementation date
Where the AC's ToR is not subject to an annual review there is an increased risk that the content does not accurately represent the required roles and responsibilities of members in line with best practice guidance. *Where the content of the ToR excludes key specific information identified, there is a risk that it does not provide sufficient information for its users.*	The AC ToR should be reviewed with consideration given to including suggested changes from relevant key officers, External Audit and AC Members. All changes proposed following the review should be formally approved with an annual review of the ToR incorporated as part of the AC Forward Plan.	Accepted; a review of the AC ToR is currently underway. Once complete, the Head of Democratic Services will discuss the outcome with the Leader of the Council with a view to a report on the proposed changes to the ToR being submitted to the December meeting of the AC. There will also be an annual item on the AC Forward Plan for a review of the AC ToR.	Lloyd White, Head of Democratic Services 31st December 2016
Risk Rating		**Risk Response***	
MEDIUM ●		**TREAT**	

Please refer to **Appendix C for Risk Response definitions.*

Management Action Plan

No.	Key Finding
2	Whilst we were informed that new Council Members receive an induction pack following an election, it was confirmed that there is no formal induction programme specifically provided to new appointments to the AC.

Risk	Recommendation	Management Action Proposed	Risk Owner & Implementation date
Where new members appointed to the AC do not receive a formal induction programme there is an increased risk that members may not have an appropriate understanding of the Council's; objectives, priorities, risks, strategies and key stakeholders. As a result, members may be unable to effectively scrutinise and fulfil their roles and responsibilities as an AC.	A formal induction programme should be provided to all new members (incl. substitutes) to the AC. This should encompass but not be limited to the following: An induction pack capturing the following information: • The AC ToR; • Internal & External Audit Plans; • Corporate Risk Register; • Council's Strategy; and • Latest relevant financial reports. Meetings with: • AC Chair & AC Members; • Internal Audit; • External Audit; and • Other relevant senior managers.	Agreed; an induction programme for all AC Members will be introduced by Democratic Services, which will include a pack prepared for Members of the AC.	Lloyd White, Head of Democratic Services 31st December 2016
Risk Rating		**Risk Response***	
MEDIUM ●		**TREAT**	

*Please refer to **Appendix C** for Risk Response definitions.

Management Action Plan

No.	Key Finding
3	AC Members had previously been consulted on a 'Skills Matrix' developed by the Head of Business Assurance (HBA) in February 2014. Whilst there was some appetite from Committee Members for this, we noted that it has not been progressed further by Democratic Services to identify specific training needs of the AC. In addition, we confirmed that within the AC's Forward Plan a training item is identified stating the training to be provided at the start of the meeting to members. However, this Forward Plan does not identify all training to be provided during the year as there is no Training and Development Plan as such in place.

Risk	Recommendation	Management Action Proposed	Risk Owner & Implementation date
Where a skills matrix assessment is not undertaken there is a risk that potential skill gaps are not promptly identified of AC members and therefore training cannot be targeted to address these. *Where a formal Training and Development Plan is not in place there is an increased risk that Members may not have sufficient skills and knowledge required to effectively carry out their roles and responsibilities as an AC Member. Further, there is likelihood that where this occurs, the Council may face financial and reputational damage.*	Democratic Services should consider developing a skills matrix for AC Members including substitute AC Members. Outcomes of the skills matrix assessment should help inform/ determine the contents of the AC Training and Development Plan. The Plan should be developed in consultation with AC Members on an annual basis as part of the skills matrix exercise and be formally approved by the AC. Linked to this, Democratic Services should consider introducing formal training sessions to all AC Members (including AC Substitutes) on a quarterly basis as a minimum. Where feasible, training should be delivered either prior to AC meetings for a minimum of 30 minutes or delivered on separate occasions to AC meetings.	Democratic Services will review the proposed skills matrix with the Head of Business Assurance and establish the key training needs to be delivered. Need to establish if delivery of training at AC meetings is the most effective way of targeting all the AC Members, including substitutes. Also need to clarify if quarterly is the correct timescale. Once key training for all AC Members has been delivered, Democratic Services will consider wider Member training as and when required.	Lloyd White, Head of Democratic Services 31st March 2017
Risk Rating **MEDIUM** 🟡		**Risk Response*** **TREAT**	

Please refer to **Appendix C for Risk Response definitions.*

Management Action Plan

No.	Key Finding
4	As per the AC's Terms of Reference, the AC is required to report to Full Council on an annual basis via the submission of the Annual Report, outlining their activities during the financial year. However, it was identified that this report was last produced for 2013/14, initially submitted to AC on 30th July 2014, however no evidence was available to support that this was subsequently presented to full Council. Furthermore, it was confirmed that no Annual Report was produced for 2014/15 and 2015/16.

Risk	Recommendation	Management Action Proposed	Risk Owner & Implementation date
Where the Annual Report is not produced and submitted to Council on an annual basis, in line with the AC's ToR and best practice guidance, there is an increased risk that appropriate governance is not in place. Where the activities of the AC are not reported there is an increased likelihood that the Council may face reputational damage.	The AC Annual Report should be produced on an annual basis by the Chairman of the AC, in consultation with AC Members & Democratic Services. This report should be promptly submitted to full Council on an annual basis for review and approval.	Accepted; An annual AC report will in future be produced by Democratic Services in liaison with relevant officers. This will also be added to the AC Forward Plan.	Lloyd White, Head of Democratic Services 31st March 2017
Risk Rating		**Risk Response***	
MEDIUM ●		**TREAT**	

*Please refer to **Appendix C** for Risk Response definitions.

Good Practice Suggestions

No.	Key Finding	Observation / Suggestion	Risk / Rationale	Risk Rating
5	It was confirmed that the composition of the committee is in line with the Constitutional requirements of four elected Councillors and an independent Chairman, with the Vice-Chair coming from the majority group. However, a bench-marking exercise undertaken assessed LBH against nine other local authorities and identified that on average Audit Committee membership consisted of six Members. Furthermore, Members' attendance to the first meeting of financial year 2016/17 (12th July 2016) had only two members in attendance and therefore required two substitutes to ensure this was quorate.	Consideration should be given to increasing AC membership to reduce the risk of AC meetings being delayed or cancelled because they do not meet the quorum requirements of four members.	*If there are only five AC Members and regular reliance on the substitutions process, there is an increased risk that AC meetings may not be effective or have to be delayed or cancelled as they cannot go ahead if they do not meet the quorum requirement of four Members. Any AC meetings cancelled at short notice would increase the Council's administrative costs and may cause statutory deadlines not to be met/ potential reputational damage.*	**LOW** ●

Good Practice Suggestions

No.	Key Finding	Observation / Suggestion	Risk / Rationale	Risk Rating
6	On commencement of AC Meetings, Members are given the opportunity to declare any conflicts of interests they may have with agenda items. This is recorded within the meeting minutes by the Clerk to the AC. Of the last six committee meetings we confirmed a declaration of interests was not recorded in one meeting: • Meeting 2nd July 2015: No record within meeting minutes that Agenda Item 2 "Declaration of Interest" was discussed prior to the commencement of the committee meeting.	When preparing meeting minutes following AC meetings; accurate and complete information should be presented to address the outcomes of all agenda items. Where no declarations of interests are declared, this should also be recorded within minutes to ensure evidence of agenda items being discussed.	*Where the outcome of an agenda item (declaration of interests) is not recorded within the meeting minutes, there is a risk that its users are unable to confirm whether these have been appropriately declared. Where this occurs, there is a risk the Council may face reputational damage.*	**LOW** ●

Good Practice Suggestions

No.	Key Finding	Observation / Suggestion	Risk / Rationale	Risk Rating
7	Section 2.05b of the Council's Constitution states *"If Members (including co-opted member) fail to attend any meeting of the committee or advisory group to which they are appointed/co-opted throughout a period of six consecutive months, they will cease to be a member of that committee or group unless their absence is due to a reason which has been previously approved"*. Analysis of meeting attendance over the last 18 months identified that: • The Independent Chairman has been unable to attend 2 of the last 6 AC meetings (March & July 2016); and • Councillor O'Brien has been unable to attend to attend 2 of the last 6 AC meetings (July and September 2016). Furthermore, it was confirmed by the Head of Democratic Services that the Chairman to the AC does not have a formal Job Description in place outlining his roles and responsibilities.	Attendance to all AC meetings should be made in line with Constitutional requirements. Management should consider implementing a defined role description for the AC chair, including minimum attendance requirements.	*Where consistent membership of the AC is not maintained there is an increased risk that an appropriate and consistent level of independent review may not be undertaken reducing the effectiveness of the Audit Committee. Where this occurs, accurate assurance needs cannot be provided to the Council and could result in financial and reputational damage.*	LOW ●

INTERNAL AUDIT ASSURANCE LEVELS AND DEFINITIONS

ASSURANCE LEVEL	DEFINITION
SUBSTANTIAL	There is a **good level of assurance** over the management of the key risks to the Council objectives. The control environment is robust with no major weaknesses in design or operation. There is **positive assurance** that objectives will be achieved.
REASONABLE	There is a **reasonable level of assurance** over the management of the key risks to the Council objectives. The control environment is in need of some improvement in either design or operation. There is a misalignment of the level of residual risk to the objectives and the designated risk appetite. There remains **some risk** that objectives will not be achieved.
LIMITED	There is a **limited level of assurance** over the management of the key risks to the Council objectives. The control environment has significant weaknesses in either design and/or operation. The level of residual risk to the objectives is not aligned to the relevant risk appetite. There is a **significant risk** that objectives will not be achieved.
NO	There is **no assurance** to be derived from the management of key risks to the Council objectives. There is an absence of several key elements of the control environment in design and/or operation. There are extensive improvements to be made. There is a substantial variance between the risk appetite and the residual risk to objectives. There is a **high risk** that objectives will not be achieved.

1. **Control Environment:** The control environment comprises the systems of governance, risk management and internal control. The key elements of the control environment include:

   - establishing and monitoring the achievement of the authority's objectives;

   - the facilitation of policy and decision-making;

   - ensuring compliance with established policies, procedures, laws and regulations – including how risk management is embedded in the activity of the authority, how leadership is given to the risk management process, and how staff are trained or equipped to manage risk in a way appropriate to their authority and duties;

   - ensuring the economical, effective and efficient use of resources, and for securing continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness;

   - the financial management of the authority and the reporting of financial management; and

   - the performance management of the authority and the reporting of performance management.

2. **Risk Appetite:** The amount of risk that the Council is prepared to accept, tolerate, or be exposed to at any point in time.

3. **Residual Risk:** The risk remaining after management takes action to reduce the impact and likelihood of an adverse event, including control activities in responding to a risk.

RISK RESPONSE DEFINITIONS

RISK RESPONSE	DEFINITION
TREAT	The probability and / or impact of the risk are reduced to an acceptable level through the proposal of positive management action.
TOLERATE	The risk is accepted by management and no further action is proposed.
TRANSFER	Moving the impact and responsibility (but not the accountability) of the risk to a third party.
TERMINATE	The activity / project from which the risk originates from are no longer undertaken.

INTERNAL AUDIT RECOMMENDATION RISK RATINGS AND DEFINITIONS

RISK	DEFINITION
HIGH ●	The recommendation relates to **a significant threat** or opportunity that impacts the Council's corporate objectives. The action required is to mitigate a substantial risk to the Council. In particular it has an impact on the Council's reputation, statutory compliance, finances or key corporate objectives. **The risk requires senior management attention**.
MEDIUM ●	The recommendation relates to **a potentially significant threat** or opportunity that impacts on either corporate or operational objectives. The action required is to mitigate a moderate level of risk to the Council. In particular an adverse impact on the Department's reputation, adherence to Council policy, the departmental budget or service plan objectives. **The risk requires management attention**.
LOW ●	The recommendation relates to **a minor threat or opportunity** that impacts on operational objectives. The action required is to mitigate a minor risk to the Council as a whole. This may be compliance with best practice or minimal impacts on the Service's reputation, adherence to local procedures, local budget or Section objectives. **The risk may be tolerable in the medium term**.
NOTABLE PRACTICE ●	The activity **reflects current best management practice** or is an innovative response to the management of risk within the Council. **The practice should be shared with others**.