

## **AUDIT COMMITTEE ANNUAL REPORT 2015/16**

### **Introduction by the Chair of Audit Committee**

This report provides an overview of the Audit Committee's activity during the financial year 2015/16.

I am pleased to report that the Audit Committee continued to focus its efforts on effectively discharging its functions and responsibilities in accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) guidance of 2004 entitled "Audit Committee principles in local authorities in Scotland: a guidance note".

The Audit Committee met quarterly throughout the financial year i.e. March, June, September, and December; the meetings were attended by representatives of the Head of Governance and Law, the Head of Strategic Finance, the Chief Internal Auditor, Audit Scotland along with other Council Officers as and when requested to attend.

In 2015/16, the following Councillors served on the Audit Committee at various points during the year; Gordon Blair, Maurice Corry, Iain MacDonald, Iain S MacLean, Richard Trail and Michael Breslin. In respect of the Chair and Vice Chair posts, I, Martin Caldwell continued in the role of Chair with Sheila Hill as Vice Chair and I am pleased to advise the our term has been extended to 31 October 2017.

In looking forward to 2016/17 and beyond, given the significant financial pressures challenges facing the Council and the implementation of major initiatives such as of Health and Social Care integration, the importance of an effective Audit Committee remains critical. Along with my fellow members I look forward to meeting the challenges ahead and continuing to add value to the Council's governance framework.

Martin Caldwell  
Chairperson

Sheila Hill  
Vice Chairperson

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## **1. Terms of Reference**

- 1.1 The Committee's Terms of Reference are to promote good internal control, financial and risk management, governance and performance management. This provides substantial assurance of effective and efficient operation, and compliance with laws and regulations, including the Council's Financial and Security Regulations, Contract Standing Orders and accounting codes of practice.
- 1.2 The specific Terms of Reference are as follows –

### **Constitution**

- The Council has established a Committee to be known as the Audit Committee.

### **Key Activities**

- Agree the Internal Audit strategic plan, oversee and review action taken on Internal Audit recommendations;
- Consider the annual report, opinion, and summary of Internal Audit activity including the level of assurance it can give over the Council's corporate governance arrangements, internal control and risk management system, and to consider other specific Internal Audit reports.
- Consider the External Auditor's Annual Audit Plan, Annual Letter, relevant reports, and the report to those charged with governance and other specific External Audit reports;
- Comment on the scope and depth of External Audit work and to ensure it gives value for money;
- Commission work from Internal Audit, External Audit and third parties where appropriate;
- Consider the performance of Internal and External Audit;
- Facilitate training to support the role of Audit Committee Members;
- Develop a culture of compliance within the Council to ensure the highest standards of probity and public accountability;
- Support best practice in the financial administration of the Council;
- Review the Council's financial performance as contained in the Annual Report, and to report annually to the Council on the internal control environment;
- There should be a least one meeting a year, or part thereof, where the Audit Committee meets the Internal and External Auditors separately from management;
- The Committee will prepare an annual work plan setting out meeting dates for the financial year and anticipated Internal Audit, external audit and management reports expected to be covered at each meeting; and
- The Committee shall prepare an annual report to the Council covering its activities and key findings each year. This report will be considered at the Council meeting that agrees the External Auditor's annual audit letter; and in addition, the Committee will submit highlight reports to the Council as appropriate.

## **Regulatory Framework**

- Maintain an overview of the Council's Constitution in respect of contract procedure rules, and financial regulations;
- Monitor and seek assurance with regard to risk control measures through the review of the effectiveness of risk management systems and corporate governance in the Council;
- Monitor the Anti-fraud and corruption strategy and the Council's arrangements for dealing with any allegations of fraud or similar improper behaviour; and to consider the Council's compliance with its own and other published standards and controls; and
- Monitor the Council's compliance with the Public Interest Disclosure Act and the Bribery Act in the discharge of its functions.

## **Financial Accounts and Governance**

- Examine the activities and accounts of the Council and exercise a governance role over management efforts to ensure that:
  - (a) The expenditure approved by the Council has been incurred for the purposes intended;
  - (b) Services are being provided efficiently and effectively;
  - (c) Value for money is being obtained, all in accordance with Best Value requirements; and
  - (d) The Council has appropriate information and advice available to them to make decisions.
- Review the annual statement of accounts, specifically to consider whether appropriate accounting policies have been followed and whether there are concerns arising from the financial statements or from the audit that need to be brought to the attention of the Council;
- Oversee the production of the Council's Governance and Internal Control Statement; and
- Consider the External Auditor's report to those charged with governance on issues arising from the audit of the accounts.

## **Other Monitoring**

- Assess the effectiveness of the Council's Performance Management System;
- Consider performance and inspection reports from Internal Audit, external audit and other relevant scrutiny bodies;
- Commission specific reviews to be carried out where necessary;
- Review Best Value arrangements and outcomes, with consideration of both external and internal Best Value reports, strategy/plans and outcomes from Best Value reviews;

- Review the impact of national performance reports from external bodies such as Audit Scotland and consider their impact on future audit plans in terms of audit work to be undertaken by both external and Internal Audit; and
- The Chief Executive will attend one meeting per annum to report on how the Council is addressing its key strategic risks and other matters of interest.

## **2. Audit Committee's Effectiveness and Impact**

2.1 The Audit Committee's role is to ensure that the Council's internal control framework and governance arrangements are operating effectively. The Audit Committee receives and reviews reports covering:

- External and Internal Audit Annual Plans and Audit Reports;
- Quarterly Progress Reports on Internal Audit Activity;
- Audit Recommendation Follow up Reports;
- Risk Management Reports;
- Corporate Performance Audit Report;
- Council's Assurance & Improvement Plan;
- Financial Statements;
- Treasury Management Assurance Report;
- Where appropriate Audit Scotland National Reports;
- National Fraud Initiative Reports; and
- Performance Management Annual review /assurance report.

2.2 The Audit Committee has the right to request updates after reviewing submitted reports. This approach afforded the Audit Committee the opportunity to ask directly key questions and receive assurances. In addition, the Audit Committee can routinely challenge management when agreed audit recommendations implementation dates were missed.

2.3 Audit Scotland in March 2016 presented their Annual Audit Plan setting out their approach to the audit of the Council, reflecting their statutory duties and risk based approach. The Audit Plan was considered by the Audit Committee and accepted. Internal audit also presented their annual audit plan for 2016/17 which was approved.

2.4 It is disappointing to note that Member attendance at quarterly meetings has seen an adverse movement from previous years. It is essential that members of the committee engage in the process in order to ensure the Audit Committee builds on its effectiveness and maintains a positive impact and high profile within the Council.

A number of changes to the membership of the Committee took place during the year which has had an impact on continuity and development plans. Councillors Corry, MacDonald and Blair are no longer members of the Committee. There are currently two vacancies on the Committee.

2.5 In its ongoing development the Audit Committee introduced a number of changes resulting in additional assurance and improved effectiveness and these continue to mature. These are:

- Securing an Assurance Mapping report for the Council
- Developing communication protocols between Internal and External Audit

- Developing a link between Audit and Performance Review & Scrutiny Committees
- Securing an Annual Audit and Risk report from the Chief Executive.
- Strengthening the process of annual audit plan preparation by requesting draft version for early discussion.
- Undertaking Effectiveness self -evaluation using CIPFA guidance documentation
- Introduction of informal Effectiveness / development sessions prior to Audit Committee meetings.

2.6 Increased management attendance at Committee meetings has allowed members to challenge officers actively in relation to findings and recommendations within reports. It is intended that where reports are of limited assurance level then relevant management /officer representation will be available as matter of course.

### **3. Assurances**

#### **3.1 Internal Audit Assurance**

3.1.1 Internal Audit is a key source of assurance for both members and management on the effectiveness of the control environment. The Committee has a responsibility for ensuring that Internal Audit is effective in the provision of this assurance. The Committee is pleased to note the Internal Audit team has been appropriately resourced throughout the year allowing the timely completion of the annual audit plan.

3.1.2 The Committee has received regular reports and information from the Chief Internal Auditor including:

- Internal Audit's risk based planning methodology and annual audit plan;
- Regular progress reports;
- An Annual report from the Chief Internal Auditor in line with best practice in the CIPFA code for Internal Audit in Local Government which provided an opinion on the control environment and the effectiveness Internal Audit activity.

3.1.3 Control weaknesses are effectively dealt with via a follow-up process which is reporting quarterly to the Committees emphasising the importance of fully implementing Internal Audit recommendations.

3.1.4 At the March 2016 meeting, the committee noted a change to Assurance opinions with main change being the introduction of Reasonable Assurance which sits between existing Substantial and Limited opinions. This change will be effective from April 1<sup>st</sup> 2016.

#### **3.2 External Audit Assurance**

3.2.1 External Audit is an essential part of the process of accountability and assurance for public funds, providing an independent opinion on the financial statements, and reviewing aspects of governance and financial management. Working closely with Internal Audit, the External Audit programme ensures that statutory responsibilities are delivered, without the duplication of audit work. Both programmes are submitted to the Audit Committee for scrutiny.

3.2.2 Assurance was received from external auditors, Audit Scotland, for 2014/15 financial statements as follows:

- They presented a true and fair view in accordance with applicable law;
- The accounts prepared properly in accordance with IFRS; and
- The accounts prepared properly in accordance with Local Government Act (Scotland) 1973.

3.2.3 External Audit is required to report by exception on a number of areas in relation to their audit, namely accounting records, statement of governance and control, availability of information and explanation and failure to achieve a prescribed financial objective. External Audit reported no exceptions in respect of these matters for 2014/15.

3.2.4 The external auditor's 2014/15 Annual Audit Report on the council (September 2015) highlights that operational governance arrangements are generally sound, with key financial controls operating effectively. In their 14/15 report, External Audit included a review of internal audit and concluded that overall the internal audit service operates in accordance with Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place.

### **3.3 Systems of Risk Management**

3.3.1 It is the role of the Audit Committee to gain assurance on the adequacy of the system of internal controls and on the adequacy of the system of risk management. The role of the Audit Committee is to test the adequacy of the arrangements in place to manage risk. The Audit Committee in 2015/16 received risk management reports and these showed continued progress by the Council in the development and regular review of risk management systems. The Audit Committee has agreed to maintain its focus on seeking assurance on the development of adequate systems of risk management. The Audit Committee continue to receive an Assurance Mapping report prepared by Grant Thornton, Internal Audit Strategic partners. The Chief Executive also submitted a report to the committee on Audit and Risk arrangements.

### **3.4 Governance & Internal Control**

3.4.1 In accordance with the CIPFA/SOLACE guidance note for Scottish Local Authorities, issued in May 2009, the completed Local Code of Governance 2013/14, together with an Action plan was presented and reviewed at the June 2015 Audit Committee meeting. The draft Statement of Governance & Internal Control was also reviewed and noted for inclusion in the Annual Accounts, subject to External Audit feedback. A final version was submitted to the PRS committee for formal approval.

3.4.2 The draft Statement of Governance & Internal Control was informed by the:

- Work of officers within the Council;
- Work of External and Internal Audit;
- Statements of governance or internal control provided by external bodies;
- External review and inspection reports and
- Recommendations from the Audit Committee.

The content of the Governance Statement and the process for preparing the Governance Statement has been reviewed for 2015-16 financial year-end.

#### **4. Independence**

- 4.1 To assist in preserving the Committee's independence and provide a clear distinction between the Audit Committee and the Performance Review and Scrutiny Committee measures are in place including:
- The appointment of an independent chair and vice chair; and
  - Clear terms of reference for both Committees
- 4.2 There are areas where Audit and Scrutiny naturally combine and a basic protocol for joined up working or areas of collaboration is in place. The Chief Internal Auditor, although having no direct operational responsibility, will have an overview of Scrutiny support arrangements and will liaise with the respective chairpersons.

#### **5. Training and Development**

- 5.1 The Council continues with its Internal Audit partnership approach with Grant Thornton which has proved very beneficial in terms of PSIAS compliance, strategic support and specialist discreet areas of work. Looking forward Grant Thornton will undertake a piece of work in relation to preparing an IT Risk Assurance MAP which will be used to inform future year Audit Plans.
- 5.2 Audit Committee Effectiveness sessions have taken place throughout the year, aimed at addressing themes arising from analysis of the CIPFA self-assessment exercise. It is anticipated that these will continue throughout 16/17, albeit in a different format and frequency. Any specific training requirements or requests will be addressed as and when they arise.

#### **6. Looking Forward**

- 6.1 Argyll and Bute Council was previously incurring an External Audit fee at the higher level as a result of increased correspondence from members of the public. In my last report I noted it was the desire of the Audit Committee in carrying out its activities to endeavour to add additional assurance in respect of governance, risk and control processes which would hopefully contribute to a possible reduction in external audit fees. I am pleased to note that the Audit Fee has now reduced and hope that the work of the committee contributed, in some part, to the overall reduction.
- 6.2 The Committee is committed to self-evaluation and continuous improvement. Due to current vacancies and change in membership, effectiveness sessions will be postponed in the short term and replaced with a development day for new and existing members. I would like to thank members for their attendance and contributions to these sessions. Our focus will continue to be on the role of the Audit Committee, developing skillset and expertise to allow effective challenge together with the ongoing interaction with the work of the Scrutiny committee and as such it is essential that the vacancies on the committee are filled as early as possible and that new members of the committee are fully signed up to continuous improvement.



## **7. Conclusion**

- 7.1 Based on the reports received and reviewed by the Committee and the follow up work requested, it is the opinion of the Audit Committee that an overall substantial assurance opinion can be placed upon the adequacy and effectiveness of the Council's internal control system in 2015/16. It is noted that 4 reports did have limited assurance with unacceptable residual risk and weaknesses identified however this is mitigated by active monitoring and follow up of recommendations together with timely management action. This follow up process will be further enhanced by the inclusion of supplementary further testing within the continuous monitoring programme.
- 7.2 Throughout 2015/16 the Audit Committee evolved and continues to evolve with an agreed framework of reporting and agenda management which allows it to undertake appropriate assessment of the Council's progress in addressing identified issues covering risk, governance and internal control. With a solid base established in this regard, the Committee continues to adopt a pro-active posture on the Council's operations.

Audit Committee performance has been aided through the expertise and contribution from its Members during 2015/16.