

TRANSPORT FOR LONDON

AUDIT COMMITTEE

SUBJECT: INTERNAL AUDIT ANNUAL REPORT 2009/10

DATE: 15 JUNE 2010

1 PURPOSE AND DECISION REQUIRED

1.1 The purpose of this paper is to summarise Internal Audit activity for the year ended 31 March 2010, to account for the use of resources and provide an opinion on the internal controls as required by the CIPFA Code of Practice for Internal Audit in Local Government.

2 AUDIT OPINION

2.1 Based on the work the Department has completed during the course of the year, which is set out in more detail below, and taking into account other sources of assurance including:

- (a) external expert reviews as part of the project approval process;
- (b) the work of other management assurance teams;
- (c) the result of the Use of Resources assessment by the external auditors;
- (d) a review of the Control Risk Self Assurance exercises within TfL; and
- (e) a review of the Statements of Control completed by London Underground,

we have concluded that TfL's control environment is adequate for its business needs and operates in an effective manner.

2.2 There have been no matters arising from any of the work we have completed that require to be brought to the attention of the Audit Committee.

2.3 There have been no restrictions imposed on the scope of the internal audit function.

2.4 In addition, using assurance gained from our audit work on governance matters and the specific review carried out on the preparation of the Statement of Governance, we can conclude that TfL's code of governance, including internal control, is adequate and effective.

3 WORK DONE

Introduction

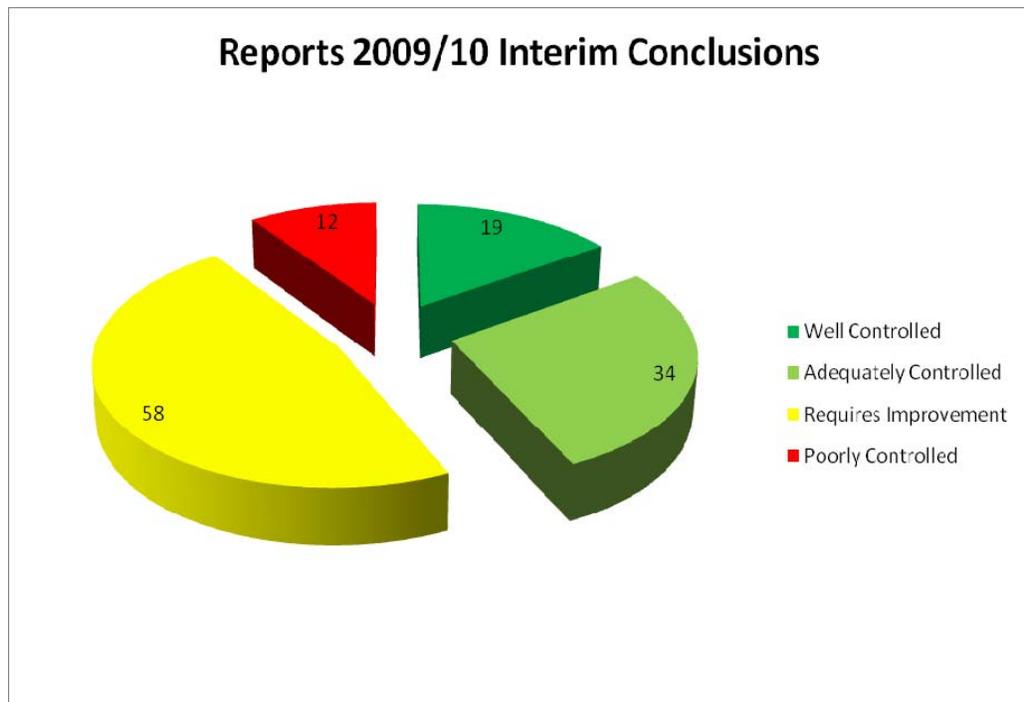
- 3.1 Internal Audit work falls into two main areas namely audit assurance as set out in the Audit Plan, and Fraud Awareness, Prevention, Detection and Investigation. In addition, we provide advice on controls and processes both via reviews and by attendance at working groups. The sections below explain the work that has been done in these areas in the past year.

Audit assurance

- 3.2 In any year, our Audit Plan can change significantly as projects and procurements are cancelled or deferred and new or changing risks take priority. For this reason, we use a “rolling” plan which means we confirm our audit schedule on a quarterly basis, although we have a view as to the work we aim to complete during the next twelve months.
- 3.3 The proportion of time spent by business unit was:

	Actual 2009/10 (%)	Plan 2009/10 (%)
Group Wide	10.2	14.3
Finance	28.2	24.0
General Counsel	3.2	2.9
Group Mktg and Comms	2.6	3.3
Surface Transport	16.1	14.5
London Underground	23.4	28.2
London Rail	6.7	6.2
Crossrail	9.6	6.6
	<u>100</u>	<u>100</u>

- 3.4 The actual time analysed above includes time spent on audits brought forward from the 2008/09 plan. In particular, the higher than planned proportion of Crossrail work reflects a number of audits from the 2008/09 plan that were not carried out until 2009/10.
- 3.5 A number of audits in the 2009/10 Audit Plan were still in progress at 31 March. We also completed some audits carried forward from the 2008/09 Audit Plan during the year. Our interim conclusions on work completed during the year are set out in the chart below.



- 3.6 Follow up audits and resulting final reports indicate that management action plans agreed as part of the audit process are being completed effectively and on a timely basis.

Other Work

- 3.7 In addition to the planned audit work above, we have also continued to be involved in Programme Boards and Steering Groups for major projects and other governance bodies, and have been represented on the following during the year:
- (a) PRG Meeting
 - (b) LU ERP IP Programme Board
 - (c) LU Risk Management Meeting
 - (d) SAP Real Estate Programme Board
 - (e) One London Project Board
 - (f) IM Steering Committee
 - (g) YourIM Business Sponsor Group (BSG)
 - (h) IM Security Peer Review Group
 - (i) Heads of Procurement Meeting
 - (j) United Kingdom Border Agency/TfL Liaison Meeting
 - (k) Efficiencies Delivery Board (formerly OCR Programme Board)
 - (l) Accommodation Strategy Programme Board
 - (m) Project Compass Programme Leadership & Direction (PL&D)
 - (n) Crossrail Independent Assurance Framework Group

- 3.8 This involvement enables us to provide input on risk management and control matters at an early stage in major projects as well as allowing observation of project and other governance processes.

Control Risk Self Assurance (CRSA)

- 3.9 CRSA is a process that enables management to assure themselves that key controls are operating across a whole process. It can reduce, but not eliminate, the need for internal audit. The CRSA returns are reviewed by Senior Audit Managers to ensure they are in line with audit findings during the year and to ensure the assurance gained is taken into account for the internal audit opinion. Any differences are discussed and resolved. LU also has a 'Statements of Internal Control' process which complements CRSA and is similarly subject to Internal Audit review.

Fraud Prevention, Detection and Investigation

- 3.10 During the year, a total of 32 fraud awareness sessions, including two identity documentation verification training sessions, were delivered to a total of 492 members of staff. A further 277 people successfully completed the online fraud awareness training package, Fraud-i. We also held the second TfL Fraud Awareness Week in December, which included publicity with posters and static stands at head office buildings and also articles placed in internal publications. During the week, we distributed approximately 3,000 leaflets to TfL staff advising them about protecting the organisation, and themselves.
- 3.11 Our forensic data analysis capability continues to be enhanced and we are now using new tools for the searching of TfL databases for fraud and our analysts have provided high quality evidence for both internal and police investigations.
- 3.12 We have worked closely with Crossrail senior management and, as well as producing a counter fraud plan, we have developed an action plan including fraud awareness workshops and the establishment of a Fraud Risk Assurance Group and have also identified areas for proactive fraud detection work.
- 3.13 There were 71 new cases reported during 2009/10, added to the 39 cases brought forward from 2008/09. There were no significant trends identified from our investigations but we continue to investigate cases of identity theft and fraud or thefts of pensions.
- 3.14 The investigations of note were:
- (a) Cloned credit cards used to purchase Oyster PAYG. Cloned American Express (Amex) credit cards were used at various LU stations to purchase unregistered PAYG and weekly travel Oyster cards to the approximate value of £5,000 during November and December 2009. The fraud spend continued and increased on a daily basis and eventually was estimated to be £1,000 per day (approximate total loss was estimated at £35,000). In January 2010 a joint TfL/LU Revenue/BTP operation resulted in a female passenger being

arrested by the BTP for possession of articles intended for use in fraud. Our investigations continued to identify further fraudulent transactions and in February 2010, in a joint operation with TfL, the BTP Organised and Financial Crime Unit arrested two prolific offenders and also found two 'credit card factories'. The BTP recovered hundreds of cloned and counterfeit credit cards and the computers/software/hardware used to make the cloned cards. In February 2010, two further arrests took place.

- (b) Allegation of Fraudulent Refund Payments In March 2009 the Oyster Help Desk discovered that there were a number of refund payments that appeared suspicious and our investigation identified that a manager had regularly entered the refund system and authorised payments from previously closed files onto a number of credit or Oyster cards of his choice. The total amount stolen was in the region of £4,500. On 24 March 2009 the manager was arrested and admitted the fraud. He later appeared at court where he pleaded guilty to two charges of Fraud by Abuse of Position of Trust and one charge of Theft. He was given a 12 months' suspended sentence, a two year Supervision Order, 260 hours unpaid work and ordered to pay TfL compensation of £4,500. The manager has also been dismissed by TfL. Group Customer Services have addressed the risk issues connected with this case.
- (c) Alleged Theft at a Travel Information Centre (TIC) during Oyster card Sales. An allegation was received that an employee was allegedly stealing the £3 deposit paid by customers during an Oyster card transaction. An investigation was undertaken including test purchases. The employee was subsequently arrested by the BTP and admitted stealing £2,000 over a two month period. In June 2009, he appeared at the City of Westminster Magistrates' Court and was given a four month custodial sentence (suspended for two years) and a two year Supervision Order. He has since been dismissed from TfL for Gross Misconduct. Measures have been put in place to prevent this type of crime from happening again.
- (d) Allegation of False Representation regarding failed oyster cards. An individual made a series of claims stating each time that his weekly Oyster card was defective and had been loaded with PAYG and weekly travel cards. The cards were renewed and all value reinstated, but in reality the Oyster value had been spent or had not been loaded in the first place and therefore all claims were false. Our investigation identified the culprit and evidence was handed to the BTP. In October 2009, a man was arrested and subsequently charged with eight specimen offences of fraud by false representation. In January 2010, the suspect appeared at City of Westminster Magistrates Court and pleaded guilty. He was fined £300, ordered to pay court costs of £85, a victim supplement of £15 and compensation to LU of £348.60, the total value of the specimen charges.

- (e) Identity Theft Cases. We continue to investigate cases of suspected identity theft, many of which are reported under the National Fraud Initiative (NFI). This is a growing and prevalent crime and one that affects most industries, and our cases included a LU employee who had applied for four UK passports claiming that his passports had been either lost or stolen. Following a joint investigation, the employee was found guilty and received two sentences of four months imprisonment, to run concurrently. The employee was also dismissed from LU. We also had two cases of LU employees who had used duplicate employments both of whom received police cautions for fraud by false representation and have been dealt with under LU disciplinary processes.
- (f) Pension Investigations. We also continue to work with the TfL Pension Fund (TfLPPF) to investigate fraud and theft of pensions. We have assisted in the recovery of over £28k this year and calculate that, as a result of our investigations, we have prevented further losses amounting to £88k. Examples of our investigations include an overpayment of £4,200 which resulted in the arrest of a deceased pensioner's daughter in law. She denied stealing the full overpayment but was cautioned for theft and agreed to repay the amount at £50 per month. In another case, the NFI data matching exercise identified that a pension of £5,900 had been paid to a pensioner who had died. It was believed this may have been stolen by the deceased's daughter who was interviewed and agreed to repay the amount in full but denied any criminal liability.

3.15 The disposal of cases throughout the past year (previous year's totals in brackets) is as follows:

	Investigations	
In Progress at 1 April 2009		39 (54)
New since 1 April 2009		71 (64)
	No Crime/ Offence established	48 (50)
	Disciplinary Action Taken	11 (8)
	Police/ Judicial Action Taken	19 (21)
Closed since 1 April 2009	Sub Total	78 (79)
In Progress at 31 March 2010		32 (39)

3.16 The 71 new investigations consist of 36 (43) fraud cases, 26 (13) reports of theft and 9 (8) 'other' types of cases.

3.17 Reports were received from the following sources:

Source	2009/10	2008/09
Internal Audit	2	0
Internal Control	13	12
Staff Member	26	29
Member of Public	9	5
Law Enforcement Agency	5	4
Anonymous	3	5
National Fraud Initiative	13	9
Totals	71	64

4 RESOURCES

Audit assurance

- 4.1 The Director of Internal Audit left TfL in the course of the year, with the vacancy being filled on an interim basis by the Senior Audit Manager – Business Processes following a recruitment process. The consequential SAM vacancy has also been filled internally on an interim basis.
- 4.2 Otherwise, staffing has been relatively stable through 2009/10. The six former Metronet auditors for whom we have had management responsibility since the middle of 2008/09 transferred to TfL during the year. The SAM-Crossrail joined the department in April, and we also took on three extra auditors to enable us to handle the growing volume of work associated with Crossrail. The costs of this resource are recharged to Crossrail.
- 4.3 One audit manager vacancy arose during the year, which we filled through an internal promotion.
- 4.4 We have also had two auditors who have taken up secondments to other TfL departments and another auditor who has left in the course of the year. Whenever vacancies arise, it is our usual practice to review carefully whether or not they need to be filled. In these cases, one of the vacancies due to secondment was filled by a temporary member of staff, but the other two vacant positions have been left open. This reflects our efforts to deliver assurance more efficiently, particularly through changes to the focus of our project audit work and through greater involvement of our managers in high-level reviews and project governance meetings rather than solely relying on traditional audits.

Fraud Awareness, Prevention, Detection and Investigation

- 4.5 There were no resource changes in this area during the year.

Staff training and development

- 4.6 Our training strategy sets out the standards we require for all staff to both maintain their existing professional qualifications and to ensure they receive sufficient continuous training in internal audit and fraud investigation (as appropriate) to keep them up to date with best practice. All of our joiners into audit positions who do not have previous audit experience must complete the IIA's Certificate of Internal Audit during their first year in the department, and several members of the department have now achieved this qualification. In addition, three members of the department are now studying for the IIA's Diploma, which is the next level of professional qualification.
- 4.7 We have continued to take advantage of free seminars provided by professional bodies and discounted places offered at conferences where we are providing a speaker. We also have an ongoing arrangement with an external trainer in Audit and Risk methodologies to provide in house courses at lower cost than external ones.
- 4.8 We continually monitor training to ensure all staff are achieving the requisite standard and also to monitor costs. Our training budget was reduced last year, but through judicious selection of courses, including our use of free or discounted courses, we have again underspent the training budget. We have, therefore, made a further permanent reduction in the budget going forward, but remain confident that the training provision is sufficient for us to maintain our high standard of professionalism.

Co-sourcing

- 4.9 We have continued to use Ernst & Young (EY) to supplement our resources under our existing contact. However, our use of EY staff has again reduced, and they have principally been used to support us on the SAP implementation work in Crossrail and LU. This has resulted in an underspend against budget. We anticipate further reductions in the use of EY resource in 2010/11 as we enhance our in-house SAP audit capabilities.
- 4.10 The co-sourcing contract was due to expire in March 2010 but was extended to October 2010 with the aim of allowing the new Director of Internal Audit to have input into the re-let of the contract. It is likely that a further extension will be required to enable the new contract to take account of the findings from the forthcoming strategic review of Internal Audit.

5 INTERNAL AUDIT PROCESSES

- 5.1 During the year, we carried out an internal Quality Assurance review of our audit processes to ensure that our audits are being carried out in accordance with the requirements of our audit manual and with best practice. The review identified some areas where our documentation of audits could be improved. These have been communicated to staff and have led, in some cases, to amendments to our Audit Manual to ensure clarity.

5.2 Our Contract Audit Toolkit is now being sold through CIPFA, and we received our first royalty cheque for £2,000 during the course of the year. We have also received invitations to speak about the Toolkit at conferences and to the internal audit functions of other organisations.

6 BENCHMARKING AND NETWORKING

6.1 To ensure that TfL’s Internal Audit department remains up to date and understands best practice, it is important that we meet and work with other Internal Auditors and Fraud Investigators as well as attending and speaking at conferences relevant to our professional and business needs. The department has memberships of the Institute of Internal Auditors, CIPFA and the Association of Certified Fraud Examiners among others, which means we receive copies of publications, newsletters and updates from these bodies which assist in ensuring that we are up to date.

6.2 Members of the team also belong to the CIPFA Procurement and Contract Audit Forum; the London Audit Group; the Working Group of the IIA Technical Committee; the Association for Project Management (APM) Specific Interest Group on Project & Programme Assurance; the APM Audit and Performance Review Committee; the Institute of Risk Management, the Institute of Occupational Safety and Health; the Security Institute; the London Fraud Forum; the National Federation of Fraud Forums and the Fraud Advisory Panel.

7 CUSTOMER FEEDBACK

7.1 At the end of every audit we send out a customer feedback form to the principal auditee(s) requesting their view on the audit process and the report. The form is questionnaire based so it can be completed easily and quickly. A copy of the questionnaire is included in Appendix 1.

7.2 Our return rate for feedback forms has increased to 60 per cent from 55 per cent in the last year. The majority of respondents are satisfied with the way we carry out our work with the commonest criticisms being around understanding the scope of the audit and the length of time it can take to complete the fieldwork and issue the draft report for discussion. The summary of scores for 2009/10 and prior years is set out in the table below.

	Strongly Agree %	Agree %	Disagree %	Strongly Disagree %
2005/06	56	40	4	0
2006/07	38	54	7	1
2007/08	35	56	7	2
2008/09	32	56	10	2
2009/10	40	51	8	1

7.3 A more detailed analysis is attached in Appendix 1.

7.4 We received only seven 'Strongly disagreed' scores across 75 forms returned. All feedback which is less than satisfactory is followed up by the Director of Internal Audit to ensure the concern is understood, discussed with the audit team and lessons learned where appropriate.

8 RECOMMENDATION

8.1 The Audit Committee is recommended to NOTE this report.

9 CONTACT

9.1 Contact: Clive Walker, Interim Director of Internal Audit
Number: 020 7126 3022
Email: CliveWalker@tfl.gov.uk

CFF sent (period 1 – 13): 133
CFF returned (period 1 – 13): 75

**Customer Feedback Form – SUMMARY OF RESPONSES FOR
2009/10**

Understanding our customers' needs and expectations and ensuring we are meeting them, is an important part of the continuous improvement we strive for in Internal Audit. We have recently worked with you on an audit project and would be grateful if you would take a few moments to give us feedback on our performance – after all, we have just given you feedback on yours!

Scale (please tick one):

1 = Strongly agree, 2 = Agree, 3 = Disagree, 4 = Strongly disagree

	Question	1	2	3	4	No mark given
1	Communication prior to the audit work was appropriate and I was aware of visit dates and objectives before the work started	37	36	2	0	0
2	Throughout the audit process I was kept informed of the work being done and issues arising	24	40	11	0	0
3	Internal audit staff demonstrated a good understanding of the business and associated risks (or took the time to develop such understanding during the audit process)	20	49	4	2	0
4	Internal audit staff demonstrated a pragmatic and commercial approach to developing solutions to issues identified during the audit	21	42	7	2	3
5	The audit report was issued in a timely fashion and was a fair summary of audit findings and management responses	28	35	10	2	0
6	Internal audit staff acted in a professional manner throughout the assignment	49	25	0	1	0

7. What did we do best?

“The team gave a professional view on the process undertaken and at times gave advice on how the process was going (good or bad) and advised what was required at each milestone so we could ensure we were ready.”

“Process was open and consultative and audit team were keen to listen and learn. This encouraged a level of openness on our side and the report probably benefitted from this. “

“Developed good professional relationships with the team members.”

“Demonstrated a good understanding of the business.”

“Understand our business and offer pragmatic suggestions for improvement.”

“Constant feedback throughout and helping me to address concerns and issues during the audit. “

“Gave me guidance and clarity where it was needed and consideration given the projects profile and the extreme conditions /pressure that us in the project were under at the time...A true reflection on how audit and the projects team work together to achieve the goals. ”

8. What could we have done better?

“Kept the principal auditee better informed.”

“I feel quite strongly that the final tone and wording of the executive summary was not fair....The summary is inflammatory and may give the reader far greater concern than is necessary...The general perception prior to the issue of the report was that things could be better, but nothing too serious. However, the final wording does not portray this at all.”

“Communicated better on the reasons for the delay in getting the report out. Also explained what timeframes were being worked towards once it was known that there would be a delay in getting the report out.”

“....the review could have been completed within slightly more aggressive timescales as it would have been beneficial to the project to have the review findings earlier.”

“Provided the feedback over a shorter time frame. I consider it went on far too long.”

“It is a tribute to the quality of the auditors work that nobody has thought of any aspect that could have been done better.”