



# MIDDLESBROUGH COUNCIL

STRATEGIC FINANCE  
SERVICE

ANNUAL INTERNAL AUDIT  
REPORT 2006/2007

1. INTRODUCTION
2. INTERNAL AUDIT ASSURANCE
3. SUMMARY OF INTERNAL AUDIT ACTIVITY 2006/2007
4. AUDIT PERFORMANCE

#### APPENDICIES

- A. OUTTURN SUMMARY
- B. DEFINITIONS OF AUDIT ASSURANCE

## Section 1

---

# INTRODUCTION

---

### *Annual Reporting*

The annual report of Internal Audit presents Members of the Audit Committee with a summary of:

- Work undertaken to formulate an opinion of the overall adequacy and effectiveness of the internal control environment and any qualifications to that opinion
- Key findings
- Issues of concern
- Action in hand as a result of audit work undertaken during the period
- Internal audit activity, showing internal audit's performance and progress for the year ended 31<sup>st</sup> March 2007.

A key part of the Audit Committee's role is to form an overall opinion on the internal control environment and the quality of internal audit coverage.

## Section 2

---

# INTERNAL AUDIT ASSURANCE

---

### ***Internal Control and the role of Internal Audit***

The Council's key financial systems are managed and delivered on its behalf by HBS. One of HBS's objectives is to improve internal processes and thereby deliver 'fit for purpose' systems that support frontline services and achieve productivity gains. As a result of continuous change in processes and procedures risks facing the Council are constantly evolving. Regular review and evaluation of these risks is therefore essential to maintain a robust and sound system of internal control. The importance of internal control is to manage risks that could have a significant affect on the Council's ability to fulfil its objectives.

It is the role of management to design, operate and monitor an appropriate system of internal control that contributes to the delivery of the Council's objectives. All employees have some responsibility for internal control as part of their accountability for achieving objectives.

Internal Audit provides independent, objective advice and assurance that the systems of control and risk management are adequate and effective.

A sound system of internal control should provide reasonable but not absolute assurance that the Council will not be prevented from achieving its objectives, or the

orderly and legitimate delivery of services, by circumstances that may reasonably have been foreseen.

The Accounts and Audit (Amendment) (England) Regulations 2006 paragraph 4 (2) require the Council to review, at least once a year the effectiveness of its systems of internal control and include a statement on internal control, prepared in accordance with proper practice in its annual accounts. The work of Internal Audit described in this report and the opinion based on that work contributes to the production of that statement.

### ***Opinion 2006/2007***

No assurance can ever be absolute, however this opinion seeks to provide a reasonable assurance that there are no significant weaknesses in the Council's whole system of internal controls.

***On the basis of the audit work completed, the Council has in place a satisfactory framework of internal control, which provides a reasonable assurance regarding the efficient and effective achievement of its objectives. No significant weaknesses have been identified.***

The level of assurance given takes into account:

- All audit work completed in 2006/2007
- Follow up actions from previous years audits
- Management's responses to findings and recommendations
- Effects of significant changes in the Council's systems
- The extent of resources available to deliver the audit plan
- Quality of the internal audit service's performance
- The extent to which resource constraints may limit the ability to meet the full audit needs of the Council
- Any limitations that may have been placed on the scope of Internal Audit.

All audit reports produced have included a management action plan where recommendations have been made which will enhance the level of control, together with an opinion of the systems reviewed. Timescales for the implementation of recommendations have been agreed with managers responsible for each area audited.

### ***The Statement of Internal Control for 2006/07***

CIPFA guidance sets mandatory proper practice for the basic content of the required annual Statement of Internal Control and its approval and publication represent the end result of the annual review of internal control. The Corporate Affairs Committee is responsible for approving the Council's Statement for signing by the Chief Executive and Mayor prior to its publication with the Council's accounts.

Internal control is operating effectively and the main area for continuing action included within the Statement on Internal Control relate to:

- Regeneration Works employment schemes. Internal Audit identified significant issues in the processes and procedures being followed in these regeneration schemes

In response all project officers now undergo basic project management training and detailed training in procurement would be undertaken on an ongoing basis. Other training involved Project Officer in relation to the monitoring and information requirements of grant providers to ensure that only eligible expenditure was included in claims. Stronger management controls and checking procedures would be implemented and continue to be monitored.

### Section 3

---

## **SUMMARY OF INTERNAL AUDIT ACTIVITY 2006/2007**

---

Audits completed in 2006/2007 covered all aspects of the Authority. The total time delivered on audit work (2,413 days) exceeded the original plan (2,159 days). Of the 2,413 days delivered on audit work, 266.5 days related to audits carried forward from the previous year. The percentage of total available time spent on audit work was 93% compared to 85% in the previous year.

An analysis of time spent carrying out audits for different Services is shown in Appendix A.

In total 77 audits were completed during the year and the accounts audited for 26 Community Councils, 9 Youth and Community Centres and 4 Community Centres. Each audit report contains an opinion on the financial controls and procedures in operation categorised as shown in Appendix B.

The following table analyses the opinions given on each of the reports:

Analysis of Audit Opinions 2006/2007

| Service                              | Opinion        |                       |                   |              | Total     |
|--------------------------------------|----------------|-----------------------|-------------------|--------------|-----------|
|                                      | Full Assurance | Substantial Assurance | Limited Assurance | No Assurance |           |
| Key Financial Systems                | 3              | 5                     | 3                 | 0            | 11        |
| Children Families & Learning         |                | 3                     | 3                 | 1            | 7         |
| Schools                              | 4              | 9                     | 10                | 0            | 23        |
| Environment & Neighbourhood Services | 0              | 9                     | 9                 | 0            | 18        |
| Regeneration                         | 0              | 3                     | 5                 | 3            | 11        |
| Social Care                          | 0              | 4                     | 1                 | 1            | 6         |
| Corporate Services                   | 0              | 4                     | 3                 | 0            | 7         |
| <b>TOTALS</b>                        | <b>7</b>       | <b>37</b>             | <b>34</b>         | <b>5</b>     | <b>83</b> |

Where a 'no assurance' opinion was expressed management took immediate action to improve controls.

### *Financial Control*

More reviews of financial systems in schools and other establishments were completed in the year. In most cases the systems in place were assessed as having adequate controls or being capable of bringing about improvements to controls if the recommendations made following audits, were implemented.

The audit programme for schools was updated during the year to ensure that Schools demonstrated the financial competencies demanded by the DfES's Financial Standards in Schools. The revised audit programme was followed at both Secondary and Primary Schools. During the year external assessors assessed Secondary Schools against the Standard. The results of the assessments available to Internal Audit indicate that all Schools achieved the required standard.

During the year Internal Audit carried out a number of surprise audits at Leisure Centres and the Municipal Golf Club which are open outside office hours to cash up and verify banking procedures. No significant errors were detected. In addition Internal Audit interviewed individuals using the Municipal Golf Course between the hours of 7.00am and 9.00am to ensure that they were in possession of a either a valid membership card or had a receipt showing that they had paid the appropriate fee.

An audit and value for money study was conducted at the nautical studies centre based on the river Tees.

### *Performance Indicators*

Significant resources were targeted at reviewing systems that generate data to produce Best Value Performance' and 'CPA' indicators. The data was evaluated for accuracy, validity and relevance. Discrepancies were discussed with management and appropriate actions taken to address system weaknesses and incorrect data.

### *Employment Initiatives*

At the request of Director, Internal Audit conducted audits of three employment initiatives. The audits identified significant weaknesses in procedures and processes such that assurance could not be given that all resources could be accounted for, had been used for their intended purpose and they had been used efficiently.

### *Breaches of Contract Standing Orders*

During the year Internal Audit investigated a number of suspected breaches of the Council's Standing Orders with respect to Contracts. Where a breach was found to have occurred the matter was referred to the appropriate Head of Services for consideration. The amount of time spent investigating breaches of procurement rules increased during the year.

## *Social Care Commissioning*

A review was undertaken into arrangements for the commissioning, procurement of services and monitoring of contracts. The audit made a number of recommendations to improve the procurement process.

## *Anti-Fraud and Corruption*

Financial regulations require managers to report all suspected irregularities to Internal Audit. In financial year 2006/2007, 11 instances of irregular activity were reported and investigated either wholly or in part by Internal Audit. A small number of suspected incidents of financial irregularity reported to Internal Audit were found, on investigation to be unsupported by the evidence.

| Type of Incident Reported                              | Number |
|--|--------|
| Allegations of financial mismanagement or misconduct   | 4      |
| Theft of equipment / assets                            | 5      |
| Misuse of asset  | 0      |
| Time recording   | 0      |
| Theft misappropriation of Middlesbrough Council monies | 2      |
| Total  | 11     |

The number of reported cases shows only a slight increase on the total reported in 2005/2006.

During the year one case reported to the police for further investigation in 2005/2006 reached the courts. The case was successfully prosecuted resulting in an individual receiving a suspended custodial sentence and community service.

Recommendations to improve control of risks identified through Internal Audit activity were discussed, with and accepted by, relevant managers and will be followed up by Internal Audit.

## *Section 4*

---

## **AUDIT PERFORMANCE**

---

The audit plan for 2006/2007 was acknowledged to be challenging. Two members of staff left to take up posts in the NHS and two others were absent on maternity leave for a substantial part of the year. Fortunately the Internal Audit Section was able to recruit to both vacant posts and retain an experienced auditor on a temporary contract to cover for one of the two Auditors on maternity leave.

Targets for delivery of the audit plan and achieving audits within budgets have not been met although performance continues to improve. Delivery of planned audits was not assisted by the fact that between November 2006 and March 2007 175 days were spent auditing employment initiative schemes. Approximately 38 days was met

from the contingency provision, which meant that the remaining 137 days had to be sourced by deferring planned audits. In addition the complexity of the audits was such that the work had to be undertaken by a skilled auditor with many years experience.

However, there was a discernible improvement in the performance of Internal Audit, particularly:

- Internal Audit contributed to increasing the internal control CPA performance score to a 3 from a 2
- All the key financial audits were either completed or had commenced prior to the end of the financial year with the exception of Payroll and Pensions Administration
- Time taken to audit the accounts of Community Councils and Community Centres was reduced by 10 days despite a request to audit the books of an additional Community Centre
- The average time taken to audit a primary school only increased by 1 day from 12 to 13 despite additional work to identify those areas where the school did not reach the Financial Management Standard.

Performance indicators to facilitate monitoring the Internal Audit Section's efficiency and effectiveness are reported below.

|   | 2005/2006 | 2006/2007 |
|---|-----------|-----------|
| Chargeable days per FTE employee (Audit Commission benchmark = 175) | 185       | 172       |
| No. of Recommendations made   | 760       | 1180      |
| No. of Audits commenced   | 138       | 131       |
| Completion of annual plan   | 64%       | 75%       |
| No. of days spent on audits carried forward from previous year      | 455       | 266.5     |

Middlesbrough is a member of the CIPFA/IPF Audit Benchmarking Club. Through this, information about our costs and productivity is compared against other unitary authorities. The figures for 2006/2007 have only just been received from IPF. The average figures quoted are estimates and subject to change but are given here for the purpose of comparison.

|                            | Middlesbrough |        | Average |        |
|----------------------------|---------------|--------|---------|--------|
|                            | 05/06         | 06/07  | 05/06   | 06/07  |
|                            | £             | £      | £       | £      |
| Cost per £m gross turnover | 1,432         | 1,248  | 1,130   | 1,127  |
| Cost per auditor           | 46,437        | 48,000 | 47,710  | 49,805 |
| Cost per audit day         | 224           | 240    | 276     | 295    |
| Audit days per auditor     | 166           | 172    | 170     | 170    |



Middlesbrough spends more per £m gross turnover on its audit service than other, unitary councils. The below average cost per auditor and per audit day are the result of lower than average salaries and overhead costs. The number of audit days per auditor has increased and is now slightly above average.

*Key issues for the next year*

Internal Audit continues to carry vacant posts and relies upon agency staff to deliver the audit plan. Efforts will continue to recruit suitably qualified and experienced staff to deliver the audit plan,

Internal Audit makes a significant contribution to the internal control 'key line of enquiry' part of the 'use of resources' category of the Council's Comprehensive Performance Assessment (CPA). The challenge is to improve the overall score. The implementation of internal control is not the responsibility of Internal Audit, as this would impact upon its independence; however it can promote improvements in controls through audit raising awareness and assurance work.

A new Code of Practice for Internal Audit in Local Government in the United Kingdom was published towards the end of 2006. The new code incorporates Ethics for Internal Auditors as a Standard, promotes a risk-focused approach to auditing and strengthens the requirements for monitoring the performance and effectiveness of Internal Audit. This recognises the amendments to the Accounts and Audit Regulations 2003, which require an Authority to conduct an annual review of how effective its internal audit systems are and for the findings of the review to be considered by a committee or the Authority itself.

---

## OUTTURN SUMMARY

---

The following table summarises the internal audit coverage across all Council Services during 2005/2006

| Service                               | 2005/2006 |             | 2006/2007 |             |
|---------------------------------------|-----------|-------------|-----------|-------------|
|                                       | Plan Days | Actual Days | Plan Days | Actual Days |
| Children, Families and Learning       |           |             |           |             |
| Life Long Learning                    | 37        | 75          | 94        | 179         |
| Standards                             | 5         | 0           | 0         | 0           |
| Inclusion                             | 30        | 17          | 68        | 29          |
| Planning & Information                | 22        | 13          | 43        | 33          |
| Vulnerable Children                   | 35        | 0           | 86        | 134         |
| Schools                               | 314       | 360         | 272       | 305         |
| Environment & Neighbourhood           |           |             |           |             |
| Transport                             | 7         | 25          | 25        | 1           |
| Street Scene                          | 52        | 13          | 63        | 87          |
| Community Protection                  | 53        | 14          | 92        | 122         |
| Horticulture, Parks & Leisure Centres | 42        | 69          | 62        | 165         |
| Regeneration                          |           |             |           |             |
| Middlesbrough Town Centre Company     | 0         | 0           | 0         | 0           |
| Museums & Galleries                   | 13        | 0           | 20        | 42          |
| Library & Information                 | 20        | 27          | 13        | 27          |
| Cultural Services                     | 18        | 21          | 0         | 47          |
| Economic & Community Regeneration     | 40        | 85          | 45        | 32          |
| Planning & Regeneration               | 25        | 61          | 103       | 208         |
| Social Care                           | 176       | 92          | 200       | 68          |
| Corporate Centre                      |           |             |           |             |
| Finance                               | 37        | 18          | 30        | 22          |
| Legal services                        | 15        | 0           | 36        | 32          |
| Chief Executives Office               | 0         | 0           | 0         | 0           |
| Members Office                        | 0         | 3           | 3         | 0           |
| Performance & Policy                  | 55        | 75          | 55        | 41          |
| Corporate Systems                     | 795       | 894         | 449       | 543         |
| Contract Audit                        | 80        | 6           | 83        | 19          |
| IT Audit                              | 95        | 2           | 80        | 48          |
| Advice                                | 33        | 63          | 65        | 49          |
| Contingency                           | 100       | 257         | 135       | 149         |
| Non Audit Work                        | 36        | 24          | 37        | 31          |
| Total Audit Days                      | 2135      | 2214        | 2159      | 2413        |

---

**DEFINITIONS OF AUDIT ASSURANCE**


---

| Assurance Level | Summary Description  | Detailed Definition   |
|-----------------|--|---|
| Full            | Effective controls in operation and evidence of full compliance          | No exposure to predictable risks, as key controls in place, applied consistently and effectively. No significant or fundamental recommendations made  |
| Substantial     | Controls in operation but enhancements beneficial or full compliance     | Probability of some risks of error, loss, fraud impropriety or damage to reputation, which can be prevented by improvements in the control environment. Key or compensating controls present but not fully applied. Small number of significant but no fundamental recommendations made.  |
| Limited         | Enhancement of controls or the application of controls required          | Authority / Service open to risks that potentially could result in the non achievement of objectives or result in error, loss, fraud, impropriety or damage to reputation. Some gaps in key controls or compensating controls or significant evidence that controls are not applied consistently or effectively. Small number of fundamental and also limited number of significant recommendations |
| Little / No     | Enhancement of controls critical or the application of controls required | The Authority / Service is vulnerable to a significant risk that could lead to failure to achieve key objectives / major loss due to error, fraud or impropriety / damage to reputation. Evidence of significant failure in application of key controls. Large number of both fundamental and significant recommendations made.   |