

ANNUAL REPORT

2002/03

BY

AUDIT MANAGER

CONTENTS

Section

1. INTRODUCTION
2. INTERNAL CONTROL STATEMENT
3. OVERVIEW OF 2002/2003
4. THE FUTURE
5. CONCLUSION

Appendices

1. Comparison of Actual Input against Budget
2. Productive Days against Planned, for each Service.

1. INTRODUCTION

- 1.1 It is considered important that, the Resources and Audit Scrutiny Panel should receive an annual report from the Audit Manager. This is the first annual report to elected members detailing the work of Internal Audit. It includes an assessment of the adequacy, reliability and effectiveness of the internal control system of the Council, a comparison of actual audit activity with that planned and highlights major findings where action appears desirable but has not been taken. This report forms the conclusion of the work undertaken by Internal Audit during the period 1st April 2002 to 31st March 2003.
- 1.2 The 2002 Code of Practice for Local Authority Accounting introduced the requirement from 2002/2003 for local authorities to include a statement of systems of internal financial control within their financial statements. Such a statement requires certain information to be addressed, including information on internal audit standards and reporting arrangements and the effectiveness of the system of internal financial control.
- 1.3 The purpose of this report is therefore twofold: the first being to provide this control opinion, while the second is to provide Members with an overview of the Internal Audit Section's activities and achievements over the year 2002/03.

2. INTERNAL CONTROL STATEMENT

- 2.1 It is the responsibility of management to develop and maintain the internal control framework and to ensure that an organisation's resources are properly applied in the manner and on the activities intended. The main objectives of internal control, financial and otherwise, are:
 - To ensure adherence to management policies and directives in order to achieve the organisation's objectives
 - To safeguard assets
 - To secure the relevance, reliability and integrity of information, so ensuring as far as possible the completeness and accuracy of records, and
 - To ensure compliance with statutory requirements.
- 2.2 Any system of control can only ever provide reasonable and not absolute assurance that control weaknesses or irregularities do not exist or that there is no risk of material errors, losses, fraud, or breaches of laws or regulations. Internal control should not be regarded as static. It should be flexible to change so that it is not in conflict, but consistent with the Council's vision, goals and strategies.

2.3 For 2002/03 the Code of Practice on Local Authority Accounting in the UK requires the Director of Resources to sign a statement on the system of internal financial control as a note to the published accounts. To enable him to do this I am required to provide an independent opinion on the adequacy and effectiveness of the system of internal financial control operating in the Council.

2.4 **In my opinion, based on the findings of work undertaken by Internal Audit, there are sound systems of internal financial control in place. A number of areas for improvement have been identified and will be implemented on an agreed phased basis subject to the level of risk.**

3. OVERVIEW OF 2002/03

Performance Overview

3.1 The audit plan for financial year 2002/03 was developed from the strategic plan covering financial years 2001/02 to 2003/04. The strategic plan was prepared after identifying all systems that require review and carrying out an assessment of risk, based on the information available to Internal Audit. A summary of the audit days delivered during 2002/03 is provided in Table 1.

Table 1. Summary of audit days delivered 2002/03

	BUDGETED DAYS	ACTUAL DAYS	UNPLANNED DAYS
Direct Audit Activity	1989	2042	53
Non Productive Days	1131	1078	(53)
Total	3120	3120	0

The actual total input from staff of 2,042 audit days was 53 days greater than the budgeted figure of 1,989 days.

3.2 Included within the non productive time are 77 days utilised on corporate duties, the bulk of which relate to:

- The production of an Internal Audit Manual
- Maintenance of the time planning and recording system
- Implementing changes to ensure the Internal Audit Service meets professional standards

3.3 A planned contingency of 160 days was set aside at the beginning of the year to cover special investigations and other requests from Services for audit assistance. Calls from Services for additional audit input met from the contingency allocation totalled 134 days.

3.4 The reasons for the large volume of unplanned activity, for the full year , can be explained as follows:

- Priority changes
- Unfamiliarity of new systems
- Excessive activity in review process
- Material findings encountered as part of review.

3.5 As a result of the above, the number of audits planned to be delivered in the year was not achieved. Planned activities, as included in the annual plan for the year 2002/03, and those activities actually undertaken are included with this report at Appendix 1. Similarly the number of audits provided to each Service is summarised as Appendix 2.

Audit Approach

3.6 Internal Audit examined systems operated by Services to provide assurance that they were achieving the objectives set by management. At the conclusion of each audit, a report is prepared to bring to managers' attention areas of non-compliance with expected controls together with recommendations for improvements to the system. An agreed action plan is included in the final report. It is the responsibility of managers to ensure that proper consideration is given to Internal Audit reports and that appropriate action is taken on audit recommendations or that management has understood and assumed the risk of not taking action.

3.7 In its coverage of the Council's main financial systems, Internal Audit made 117 recommendations of which 90 were implemented in full and a further 8 in part during the year. The remaining 19 recommendations which related to efficiency issues have proved to be impractical to implement after discussions with managers.

3.8 An implicit part of our systems based audit approach is an evaluation of the controls in place to prevent and detect fraud; sufficient audit testing is undertaken to confirm that controls are working in practice.

Fraud and Special Investigations

3.9 Financial Regulations require that whenever any matters arise that involve, or are thought to involve, irregularities concerning finance, assets or property in the exercise of the function of the Council, the Head of Service will immediately notify the Director of Resources and Audit Manager.

3.10 In total 48 days (unplanned) were spent on this activity, covering a total of 13 different events. This input includes both the time spent on undertaking the investigation and in making recommendations to management to secure improved controls. Two cases involving the fraudulent manipulation of cheques issued by the Council were reported to the Police. In both cases the receiving Banks reimbursed the Council for any loss.

- 3.11 In 2002 Middlesbrough Council continued its involvement in the National Fraud Initiative in accordance with an Audit Commission national requirement. This initiative detects potential frauds by matching data held by all participating Councils. For 2002, Middlesbrough submitted housing benefit, payroll, student awards and pensions data to the Audit Commission for matching purposes.
- 3.12 Middlesbrough Council is also a member of the National Anti-Fraud Network. The network aims to prevent fraud in a co-ordinated manner by circulating details of known fraudsters within the network.
- 3.13 In addition, Middlesbrough Council is also a member of the North East Fraud Forum and IPF's Better Governance Forum which concentrates on three themes: risk management, ethical standards and countering fraud.

SAP Implementation

- 3.14 The implementation of the SAP system will continue to have a significant impact on the development and operation of the key financial systems.
- 3.15 Although this has led to some areas of control weakness in the transitional arrangements for processing the payroll and recording financial transactions, Internal Audit is satisfied that there are sufficient compensating controls (in particular service budget management) in place to prevent these weaknesses from having material consequences.

Relationship between Internal and External Audit

- 3.16 As part of External Audit's programme of audit and inspection, they review the work performed by Internal Audit, examining audit resource, audit planning, execution of the plan and audit reporting. In the Audit Commission's 2002/03 Audit Letter, the External Auditor confirmed that financial controls were strengthened through Internal Audit's coverage of all main financial systems annually. Internal Audit was stated to have continued to develop and met most of the CIPFA standards during 2002/03. Control and delivery of work was identified as a continuing problem with a backlog of work of over 19% at the year-end.

Staffing

- 3.17 Although the Section had a full complement of staff for the financial year significant resources were lost through two members of staff on maternity leave. In addition, the audit section had to review its working arrangements when two members of staff in different job groups successfully applied for job share.
- 3.18 Two members of staff were successful in passing examinations leading to the qualification of the Association of Cost and Certified Accountants. The trainee

auditor successfully completed the foundation stage of the Association of Accounting Technicians examinations.

4. THE FUTURE

- 4.1 A tactical audit plan was prepared for the year 2003/04, the third from the strategic audit plan 2001/02 to 2003/04. However, it was considered that in view of the changes within the Council, both structural and technological that the strategic planning process needed to be redrafted.
- 4.2 At the end of the year, work was proceeding to identify all the systems that required review. Once this process was completed, discussions were to be held with Directors and Heads of Service to risk assess these identified tasks into a strategic plan for the current and following two years.
- 4.3 The preparation of a strategic plan for the years 2003/04 to 2006/07, based on a revised audit environment, and in conjunction with the related risk assessment, must be an immediate priority for the Section. It is intended that such a plan will be presented to the Performance, Policy and Resources Scrutiny Panel in 2003.
- 4.4 The revised plan will assist in bringing about improvements in the monitoring and controlling of individual audits.

5. CONCLUSION

- 5.1 Internal Audit is an independent appraisal function established by the Council for the review of its systems of internal control. It aids management by helping to ensure that adequate systems of internal control are in place and complied with. Fulfilling this latter role depends very much on the co-operation and support of staff in all Services and, I would like to extend my thanks to colleagues for the continued assistance given to Internal Audit staff during the year.

APPENDIX 1

Service	System	Planned Days	Actual Days	Unplanned Days	Planned Days Not Worked
Corporate Activity	Policies & Procedures, S Os, Financial Regs, Codes of Conduct etc. Standing Orders	35	4	0	31
Corporate Activity	Gifts & Hospitality	11	0	0	11
Corporate Activity	Fraud Awareness	15	2	0	13
Corporate Activity	National Fraud Initiative	15	9	0	6
Corporate Activity	CCTV	5	1	0	4
Corporate Activity	RIPA	0	3	3	
Corporate Activity	Public Service Agreements	5	0	0	5
Corporate Activity	Local Strategic Partnerships	5	0	0	5
Corporate Activity	Insurance & Risk Management	20	5	0	15
Corporate Activity	Exemptions to Contract Standing Orders	10	13	3	0
Corporate Activity	Contract Registers	0	25	25	0
Corporate Activity	Travel & Subsistence	10	40	30	0
Corporate Activity	Car Allowances	6	0	0	6
Corporate Activity	Cheque Control	24	14	0	10
Corporate Activity	Electoral Registration	5	0	0	5
Corporate Activity	Local Land Charges	5	12	7	0
Computer Audit	SAP Payroll / Financials	10	79	69	0
Computer Audit	Networks & Communication	15	0	0	15
Computer Audit	Contingency Planning	10	0	0	10
Computer Audit	Application Reviews	41	4	0	37
Corporate Strategy	Performance Indicators, Targets	22	21	0	1
Corporate Strategy	Best Value Reviews	60	0	0	60
Corporate Strategy	Procurement	20	0	0	20
Corporate Strategy	Members Allowances	5	1	0	4
Neighbourhood Renewal	Single Regeneration Bids	10	1	0	9
Neighbourhood Renewal	Financial Management & Budgetary Control	5	0	0	5
Central Systems	Banking & Income	43	33	0	10
Central Systems	Capital Finance	20	0	0	20
Central Systems	Council Tax	16	14	0	2
Central Systems	Non Domestic Rates	16	47	31	0
Central Systems	Asset Register	10	25	15	0
Central Systems	General Ledger	16	1	0	15
Central Systems	Creditors	20	99	79	0
Central Systems	Debtors & Cash Income	50	98	48	0
Central Systems	Payroll & Human Resources	40	19	0	21
Central Systems	Loans & Investment	13	22	9	0
Central Systems	Treasury management	10	22	12	0
Central Systems	Leasing	0	33	33	0
Central Systems	Pension Administration	20	32	12	0
Central Systems	VAT	0	23	23	
Corporate Strategy	Property	30	0	0	30
Central Home Office Services	Magistrates Court	3	0	0	3
Education	Primary Schools	91	207	116	0
Education	Secondary Schools	44	93	49	0
Education	Voluntary Schools	10	0	0	10
Education	Special Schools	22	24	2	0
Education	Catering	76	34	0	42

Service	System	Planned Days	Actual Days	Unplanned Days	Planned Days Not Worked
Education	LEA Central Systems	27	21	0	6
Life Long Learning	Youth & Community Centres	33	64	31	0
Life Long Learning	Community Councils, Partnerschaft	16.5	59	42.5	0
Life Long Learning	Community Centres	9	25	16	0
Life Long Learning	Nautical Studies	5	0	0	5
Life Long Learning	Surestart	5	0	0	5
Public Protection	Community Protection	18	27	9	0
Public Protection	Consumer Services	2.5	10	7.5	0
Public Protection	Environmental Health	31	27	0	4
Public Protection	Building Control	10	19	9	0
Public Protection	Development Control	10	19	9	0
Public Protection	Financial Management & Budgetary Control	4	0	0	4
Housing General Fund	Caravan Site	5	0	0	5
Housing General Fund	Renovation Grants	0	28	28	0
Housing General Fund	Homelessness	5	1	0	4
Housing General Fund	Staying Put Agency	3	0	0	3
Housing General Fund	Asylum Seekers	5	1	0	4
Housing General Fund	Housing Benefits	20	24	4	0
Housing General Fund	Housing Benefits – Client Service	10	21	11	0
Housing General Fund	Housing Advances	5	18	13	0
Housing Revenue Account	Rents	30	36	6	0
Housing Revenue Account	Minor Works	10	0	0	10
Housing Revenue Account	Other Income	10	0	0	10
Housing Revenue Account	Area Offices	12	1	0	11
Housing Revenue Account	Other Communal Services	5	0	0	5
Housing Revenue Account	Sheltered Accommodation	5	0	0	5
Housing Revenue Account	Repairs & Maintenance	15	5	0	10
Housing Revenue Account	Financial Management & Budgetary Control	2.5	0	0	2.5
Leisure Services	Golf Centre	0	18	18	0
Leisure Services	Landscape & Countryside	11	0	0	11
Leisure Services	Parks	44	15	0	29
Leisure Services	Leisure Facilities	19	31	12	0
Leisure Services	Leisure Management Contract	5	10	5	0
Leisure Services	Rents Other Than Housing	5	0	0	5
Leisure Services	Sports Development	14	1	0	13
Leisure Services	Middlesbrough Golf Club Accounts	3	4	1	0
Cultural Services	Middlesbrough Theatre	0	2	2	0
Cultural Services	Entertainment	0	1	1	0
Cultural Services	Ice Magic	0	7	7	0
Libraries	Libraries	9	0	0	9
Museums & Galleries	Museums	10	1	0	9
Social Services	Children Looked After	28	12	0	16
Social Services	Surestart	10	0	0	10
Social Services	Youth Justice	0	22	22	0
Social Services	Other Children's Services	13	6	0	7

Service	System	Planned Days	Actual Days	Unplanned Days	Planned Days Not Worked
Social Services	Children's Services	10	0	0	10
Social Services	Adults Under 65 Physical Disabilities	10	0	0	10
Social Services	Older People	74	73	0	1
Social Services	Equipment & Adaptations	5	0	0	5
Social Services	Sensory Agency	5	0	0	5
Social Services	Occupational Therapy Team	2	0	0	2
Social Services	Other Adult Services	6	0	0	6
Social Services	Home Care	7	0	0	7
Social Services	Adults Under 65 Learning Disabilities	0	1	1	0
Social Services	Voluntary Services	0	8	8	0
Social Services	Estates	0	87	87	0
Social Services	Hospital/Social work	3	0	0	3
Social Services	Elderly Mental Infirm	3	0	0	3
Social Services	Learning Disability Team	2	0	0	2
Social Services	Mental Health & Learning	2	0	0	2
Social Services	Emergency Duty Team	0	2	2	0
Social Services	Duty Team	0	18	18	0
Social Services	Assessment Care Management	0	30	30	0
Social Services	Administration	0	7	7	0
Social Services	Appliance Service	0	11	11	0
Social Services	Residential Care Home Placement Agency	8	0	0	8
Social Services	Health Action Zone	10	0	0	10
Social Services	Financial Management & Budgetary Control	7.5	0	0	7.5
Transport & Design	Car Parking	0	1	1	0
Transport & Design	Public Transport	5	0	0	5
Transport & Design	Highways Maintenance	0	17	17	
Transport & Design	Custodian Properties	5	0	0	5
Transport & Design	Technical Services & General Transportation	25	0	0	25
Transport & Design	Financial Management & Budgetary Control	4	0	0	4
Streetscene	Highways Responsive Maintenance	10	14	4	0
Streetscene	Refuse Collection Domestic	10	0	0	10
Streetscene	Building Cleaning	5	1	0	4
Streetscene	Nurseries	10	0	0	10
Streetscene	Ground Maintenance	10	1	0	9
Streetscene	Stores	10	42	32	0
Streetscene	Financial Management & Budgetary Control	7	0	0	7
Contract Audit	Pre Contract	30	21	0	9
Contract Audit	Current Contract	50	67	17	0
Contract Audit	Post Contract	40	14	0	26
Contract Audit	Partnership Agreements	10	18	8	0
Contract Audit	Revenue Contracts	28	0	0	28
Allowances	Contingency	160	0	0	160
Cleveland Police	Computer Audit	12	13	1	0
	TOTAL	1989	2042	1047	1011

Service	System	Planned Days	Actual Days	Unplanned Days	Planned Days Not Worked
Overhead	Annual Leave	328	328	0	0
	Public Holidays	108	108	0	0
	Sickness	50	92	42	0
	Other Absence	44	238	194	0
	Vacancy	30	16	0	14
	Study / Exam Leave	45	39	0	6
	Training	78	35	0	43
	Administration	175	156	0	19
	Audit management	136	50	0	86
	Meetings	137	16	0	121
	TOTAL		1131	1078	236
	GRAND TOTAL	3120	3120		

APPENDIX 2

ANALYSIS OF AUDITS BY SERVICE

SERVICE	FINANCIAL YEAR 2002/03
ENVIRONMENT	
Transport & Design	10
Public Protection & Planning	6
Streetscene Services	2
EDUCATION	
Primary Schools	9
Secondary Schools	2
Special Schools	1
Other Education Audits	4
REGENERATION, HOUSING & CULTURE	
Economic Regeneration	0
Housing General Fund	1
Housing Revenue Account	1
Museums & Galleries	0
Libraries	0
Cultural Services	0
Sport & Leisure	37
Neighbourhood Renewal	0
New Deal for Communities	0
SOCIAL SERVICES	
Social Services	10
CORPORATE CENTRE	
Finance	0
Legal Services	0
Members Office	0
Cabinet Office	0
Strategic Partnering	0
PPP / HBS Contract	0
Corporate Strategy	1
CENTRAL	
Home Office Services & Registrars	0
Central Systems	13
Corporate Activity	2
Police Authority	1
Partnerschaft	1
Middlesbrough Golf Club	1