



**MELTON BOROUGH COUNCIL**  
**ANNUAL REPORT OF INTERNAL AUDIT**  
**2012 -13**

**Date:** 24<sup>th</sup> June 2013

## ***Background***

1. The work of internal audit is governed by the Accounts and Audit Regulations 2011; the CIPFA Code of Practice for Internal Audit in Local Government (2006) and associated Standards; and, since 1<sup>st</sup> April 2013, by the Public Sector Internal Audit Standards. The Code of Practice requires the “Head of Internal Audit” to report to those charged with governance the findings of audit work; provide an annual opinion on the effectiveness of the Council’s internal control environment and identify any issues relevant to the preparation of the Annual Governance Statement.

## ***Internal Audit Work Carried Out 2012/13***

2. During 2012/13 planned internal audit work was undertaken to provide assurance about all aspects of the Council’s activities, specifically
  - Key Financial Systems
  - Other Financial Systems
  - ICT
  - Counter-Fraud Arrangements
  - Governance & Performance
  - Customer-Facing Services
3. Appendix 2 provides a summary of planned work undertaken and the audit opinion associated with each completed audit.

## ***Effectiveness of Internal Audit***

4. The Accounts and Audit Regulations require that the Council undertakes an annual review of the effectiveness of internal audit and the CIPFA Code of Conduct identifies 11 criteria against which effectiveness can be assessed. The detailed results of a self-assessment undertaken for 2012/13 are set out in Appendix 3. In summary, although the Consortium has met all of the requirements of the CIPFA Code in terms of the formal adoption of the policies and procedures specified, actual performance did not satisfy the criteria relating to five of those criteria relating to:
  - Staffing, Training & Development;
  - Undertaking Audit Work;
  - Due Professional Care;
  - Reporting; and
  - Performance.

The self-assessment also acknowledged that insufficient work has been done on developing the capacity of the Committee to allow full compliance to be claimed on the Audit Committee criterion.

5. The high level of staff vacancies experienced by the Consortium during 2011/12 and 2012/13 – which were reported to Governance Committee during the year – were judged to be a significant contributory factor the identified non-compliance with the Code of Practice. The post of Audit Manager (the Head of Consortium's deputy) was vacant from June 2011 to January 2013; between June 2011 and August 2012 the only established management post filled was that of the Head of Consortium; and between April and November 2012 vacancy level ranged from 40% to 50% of establishment. While it proved possible to engage suitable audit contractors to mitigate, in part, these staff shortages, the total number of audit days delivered in 2012/13 was 320 against a planned figure of 370. The direct and indirect impacts of resourcing issues recognised at the time included:
  - A reduction in the number of planned audits delivered (with the agreement of relevant clients)
  - A reduction in the number of days applied to some audits (with a consequent – and agreed – narrowing of scope)
  - Disruptions in the planned schedule of work as audit management attempted to match audits commissioned to the skills and experience of the auditors and audit contractors available
  - Time available for oversight and development of newly recruited and relatively inexperienced Auditors.
6. Rutland County Council, as employing body for the Consortium, has now commissioned an external review of internal audit. The results of that review, when available, will be reported to the Committee.

### ***Internal Audit Opinion and Assurance Statement***

7. It is the Head of Consortium's Opinion that the overall Assurance Level provided by the Council's internal control framework is **Sound**. That Opinion reflects the fact that levels of assurance for individual audit assignments were in the Good/Sound range for:
  - Key Financial Systems;
  - Other Financial systems
  - ICT; and
  - Counter-Fraud Arrangements

The Unsatisfactory assurance rating for the audit of Environmental Management and the Marginal ratings for the audits of the Cemetery and Inventories do not relate to any strategic weaknesses in the control framework.

## ***Appendix 1: Limitations and Responsibilities***

### ***Limitations inherent to the internal auditor's work***

The Consortium has prepared the Annual Report of Internal Audit and undertaken a programme of work agreed by the Council's senior managers and approved by the Audit and Risk Committee subject to the limitations outlined below.

### ***Opinion***

The Opinion is based, primarily, on work undertaken as part of the agreed 2012/13 Audit Plan. Each audit assignment undertaken addressed the control objectives agreed with the relevant, responsible managers.

There might be weaknesses in the system of internal control that we are not aware of because they did not form part of our programme of work; were excluded from the scope of individual internal assignments; or were not brought to our attention. As a consequence, the Audit and Risk Committee should be aware that the Opinion might have differed if our programme of work, or the scope of individual assignments was extended or other relevant matters were brought to our attention

### ***Internal Control***

Internal control systems, no matter how well designed and operated, are affected by inherent limitations. These include the possibility of poor judgement in decision making; human error; control processes being deliberately circumvented by employees and others; management overriding controls; and unforeseeable circumstances.

### ***Future Periods***

Our assessment of the Council's control framework is for the year ended 31<sup>st</sup> March 2013. This historic evaluation of effectiveness may not be relevant to future periods due to the risk that:

- The design of controls may become inadequate because of changes in operating environment, law, regulatory requirements or other factors; or
- The degree of compliance with policies and procedures may deteriorate.





### ***Responsibilities of management and internal auditors***


It is management's responsibility to develop and maintain sound systems of risk management; internal control and governance; and for the prevention or detection of irregularities and fraud. Internal audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.

The Consortium endeavours to plan its work so that there is a reasonable expectation that significant control weaknesses will be detected. If weaknesses are detected additional work is undertaken to identify any consequent fraud or irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected, and our work should not be relied upon to disclose all fraud or other irregularities that might exist.

## Appendix 2: Summary of Internal Audit Work Undertaken for 2012/13

Audit Assignment	Assurance Rating	Area Reviewed	Date of Reporting	Comments	Direction of Travel
<b>Fundamental Financial Systems</b>					
Benefits	Sound	Full system audit covering controls relating to: assessment of claims; dealing with changes in circumstances; identification and recovery of overpayments; and secure payment to clients.	April 2013	<b>Strengths</b> Appropriate and effective framework of controls. <b>Areas for Improvement</b> None identified	↑
Budgeting & Budgetary Control	Good	Full system audit covering controls relating to: development and approval of annual budgets; and arrangements to monitor budgets in-year and deal with budget variances	February 2013	<b>Strengths</b> Appropriate arrangements to align budgets to corporate priorities; effective Member engagement. <b>Areas for Improvement</b> None identified	↔
Creditors	Sound	Full system audit covering controls relating to: approval of orders and authorisation of invoices received from creditors.	DRAFT	<b>Strengths</b> Appropriate and effective framework of controls based upon electronic ordering. <b>Areas for Improvement</b> Scope to reduce the number of transactions for which electronic orders are not used.	↓
Debtors	Good	Full system audit covering controls relating to: accurate identification of debts due; timely billing and effective pursuit of debts; accounting for income received; and write off of irrecoverable debts.	April 2013	<b>Strengths</b> Appropriate and effective framework of controls; regular monitoring by Management Team of performance in collecting money owed. <b>Areas for Improvement</b> None identified	↔

Housing Rents	Sound	Full system audit covering controls relating to rent setting; billing and collection; accounting for income received; and arrears management.	April 2013	<p><b>Strengths</b> Appropriate and effective framework of controls; regular monitoring by Management Team of performance in collecting rent due and managing rent arrears.</p> <p><b>Areas for Improvement</b> It would be desirable to improve effectiveness of recovery of current and former tenants' arrears</p>	
Local Taxes	Good	Full system audit covering controls relating to: billing and collection of taxes; and reliefs and discounts sought and granted.	April 2013	<p><b>Strengths</b> Appropriate and effective framework of controls; regular monitoring by Management Team of performance in collecting taxes due.</p> <p><b>Areas for Improvement</b> Complete update to Business Recovery Plan.</p>	
Main Accounting System (included Fixed Assets & Cash & Banking)	Good	Full system audit covering controls relating to: receipt and accurate recording of income received; accurate recording of all transactions in the General Ledger and the Accounts; maintenance of the Asset Register and the correct valuation of assets.	April 2013	<p><b>Strengths</b> Appropriate and effective framework of controls, particularly an effective schedule of reconciliations.</p> <p><b>Areas for Improvement</b> None identified</p>	
Payroll & Employee Benefits	Good	Full system audit covering controls relating to: accuracy and legitimacy of payments; accuracy of accounting; and proper treatment data.	April 2013	<p><b>Strengths</b> Appropriate and effective framework of controls</p> <p><b>Areas for Improvement</b> None identified</p>	

Treasury Management	Good	Full system audit covering controls relating to: the Council's Treasury Management Policy; the conduct and recording of all transactions; the engagement of specialist advisors; and the treatment of data.	January 2013	<p><b>Strengths</b> Appropriate and effective framework of controls operated by a highly experienced officer.</p> <p><b>Areas for Improvement</b> The Treasury Management Strategy is to be updated to address investment in banks within combined banking groups.</p>	
<b>Other Financial Systems</b>					
Medium Term Financial Planning	Sound	Audit of controls to ensure that, over the medium term, the Council has a level of financial resources consistent with its service delivery plans	January 2013	<p><b>Strengths</b> Effective integration of financial and service planning.</p> <p><b>Areas for Improvement</b> None identified</p>	N/A
Accounting for Tax	Good	Audit of controls to ensure that the Council complies fully with HMRC requirements.	March 2013	<p><b>Strengths</b> Appropriate and effective framework of controls operated by officers who have received appropriate training.</p> <p><b>Areas for Improvement</b> None identified</p>	N/A
<b>ICT</b>					
Security of Financial Data	Sound	Audit to confirm that key financial data is held securely and that its use is consistent with the Data Protection legislation.	May 2013	<p><b>Strengths</b> Effective arrangements to back up and secure data. Up to date provisions to restore services in the event of a major incident. Approved uses of personal data registered with Information Commissioner</p> <p><b>Areas for Improvement</b> None identified</p>	

NTA Penetration Testing On Site Security	Sound	Audits undertaken by ICT specialist contractor to provide assurance that the Council's software controls meet Government standards and provide appropriate protection against "hacking". The two exercises look at on site vulnerability (i.e. abuse by employees) and vulnerability to external hackers.	April 2013	<b>Strengths</b> Positive attitude towards issue remediation and a proactive approach to security in general <b>Areas for Improvement</b> Adopt stricter patching policy and more complex passwords.	
NTA Penetration Testing Internet Security	Sound		April 2013	<b>Strengths</b> Established processes and protocols to mitigate risks <b>Areas for Improvement</b> Adopt stricter patching policy and more complex passwords	
<b>Counter-Fraud Arrangements</b>					
Counter-Fraud Arrangements	Sound	Audit undertaken to establish how well the Council's existing counter-fraud arrangements match the new expectations set out in the Government's Local Government Counter Fraud Strategy.	May 2013	<b>Strengths</b> Proactive use of data matching to detect fraud and protect income due from local taxes. <b>Areas for Improvement</b> Action to improve awareness of the Council's fraud risks.	N/A
<b>Governance &amp; Performance</b>					
Corporate Governance Arrangements	Good	The audit included an examination of the key controls giving assurance that the Council: promotes and demonstrates the values of good governance; has the capacity for informed, transparent decision making; provides for clear accountability for decisions taken and outcomes delivered; and manages its risks	May 2013	<b>Strengths</b> Well integrated performance management framework. <b>Areas for Improvement</b> A higher take up by Members of available risk management training.	N/A



Inventories	Marginal	Compliance exercise to give assurance that appropriate policies are in place and being followed to give appropriate and reliable inventory records	DRAFT	<p><b>Strengths</b> Work is in hand to create centralised inventory records</p> <p><b>Areas for Improvement</b> Action is required to provide comprehensive central records.</p>	N/A
<b>Customer Facing Services</b>					
Environmental Maintenance	Unsatisfactory	Audit undertaken to provide assurance of compliance with relevant corporate policies and procedures.	DRAFT	<p><b>Strengths</b> Building blocks for effective management and control systems are in place</p> <p><b>Areas for Improvement</b> Action to make use of the potentially effective control framework.</p>	N/A
Use of Planning Processes	Good	Audit examined arrangements to ensure that S106 monies were received and applied in line with agreements negotiated	May 2013	<p><b>Strengths</b> Clear policies and procedures including effective monitoring arrangements.</p> <p><b>Areas for Improvement</b> None identified</p>	N/A
Cemetery	Marginal	Audit examined arrangements for proper record keeping; to comply with H&S requirements; to collect and account for income; and to provide appropriate information to the public	December 2012	<p><b>Strengths</b> Appropriate policies and procedures including arrangements to minimise disruption when undertaking routine maintenance.</p> <p><b>Areas for Improvement</b> Quality of statutory record keeping</p>	N/A
Commercial Landlord	Sound	Audit covered negotiation and management of leases and arrangements to maintain the property portfolio.	June 2013	<p><b>Strengths</b> Clearly defined processes for lease negotiation supported by use of standard lease templates; clear strategy of maintenance of the portfolio; regular performance reporting</p> <p><b>Areas for Improvement</b> Ongoing work to improve management of information.</p>	N/A

## NOTES

### Assurance Ratings

The range of assurance ratings available in 2012/13 were:

Good;  
Sound;  
Marginal;  
Unsatisfactory; and  
Unsound

Assurance ratings in the range Good-Sound indicate that an acceptable level of internal control has been identified.

### Direction of Travel

Where it is possible to compare an audit undertaken in 2012/13 to a comparable audit in previous years, Direction of Travel arrows have been used to indicate whether the controls identified and tested give:

better assurance



;

worse assurance



; or

an unchanged level of assurance



### Areas for Improvement

The issues identified have been addressed through audit recommendations.

### **Appendix 3: CIPFA Code of Practice – Internal Audit Self-Assessment**

The CIPFA Code of Practice prescribed the standards of organisation and operation for Internal Audit in local government during 2012/13 and represents the appropriate basis for evaluating the Consortium’s organisational and operational arrangements.

<b>Standard</b>	<b>Significance of Standard</b>	<b>Complies ?</b>	<b>Evidence</b>	<b>Issues and Areas for Development</b>
Scope	Relates to arrangements to ensure that all stakeholders have a common and correct understanding of the purpose and responsibilities of Internal Audit.	Mostly	<p>Role &amp; Responsibility Statement approved by Committee. The Statement provides a definition of Internal Audit; sets out Terms of Reference for the Consortium and defines the respective responsibilities of Head of Consortium; the Section 151 Officer and other managers.</p> <p>Statement is supplemented by Statement on Responsibilities for Fraud &amp; Corruption and a Policy on Consultancy Work</p>	<p>Little work was done to ensure that the Governance Committee had an appropriate understanding either of its role or that of Internal Audit.</p> <p>Training for the Audit &amp; Risk Committee in 2013/14 is planned</p>
Independence	Relates to arrangements to demonstrate that the work of Internal Audit is not subject to undue influence by senior management or compromised by day to day involvement in the management of control systems or by personal interests	Yes	<p>Audit Charter approved by Committee sets out arrangements to demonstrate independence.</p> <p>The Head of Consortium reports to the Welland Board on the operations and performance matters – including budgetary requirements.</p> <p>Individual Auditors make annual Declarations of Interest.</p> <p>The Consortium has no responsibilities for management of the Council’s systems. Rutland County Council is the employing body for the Consortium.</p>	<p>The new PSIAS will require that the Governance Committee adopts a “gatekeeper” role that will enhance the independent status of Internal Audit. Planned training will give the Committee the skill sets needed to discharge that role.</p>

Standard	Significance of Standard	Complies ?	Evidence	Issues and Areas for Development
Ethics	Relates to arrangements to ensure that Auditors behave in a manner that gives clients confidence that work is undertaken competently; that reporting is objective; and that confidentiality is respected.	Yes	Code of Ethics is in place which sets standards for Integrity, Objectivity, Competence and Confidentiality consistent with CIPFA/IIA requirements.  Team briefings used to reinforce understanding of relevant issues.  Declarations of Interest	As part of the programme of development for new and inexperienced Auditors the Code will be revisited in Team Briefings.
Audit Committee	Relates to arrangements to allow the Audit & Risk Committee to operate as an independent provider of assurance for the Council and to support the independence and effectiveness of the Consortium.	Partly	The role and responsibilities of the Audit & Risk Committee set out in the Constitution are consistent with CIPFA Standards.  The Committee approves the Annual Audit Plan; receives regular reports on the performance of Internal Audit; and considers the Annual Report  Following the publication of the Public Sector Internal Audit Standards the Committee received reports and briefings advising that it would be required to undertake a more challenging role in future years.	Little work was done to ensure that the Governance Committee had the capacity to discharge its responsibilities.  Training is planned for 2013/14 to ensure that the Committee can operate in conformity with the PSIAS.
Relationships	Relates to arrangements to ensure effective engagement with clients – to ensure that the Annual Plan focuses on key risks for which assurance is required; that individual audit assignments focus on key issues; and that agreed recommendations are implemented promptly. Relates also to management of the relationship with External Audit so that the Council obtains all the assurance required without duplication of work.	Yes	Audit Manual contains a Policy of Managing Relationships  Regular One to One Meetings with Section 151 Officer (key client)  CSQ data used to manage and evidence levels of client satisfaction  Agreement in place with PwC covering reliance on work of Internal Audit.	It will be necessary to develop a new protocol to cover liaison with External Audit to deliver shared assurance about Key Financial Systems that specifies precise testing parameters and gives the Consortium early notice of the key controls for which assurance is required..

Standard	Significance of Standard	Complies ?	Evidence	Issues and Areas for Development
<p style="text-align: center;">Staffing, Training and Development</p>	<p>Relates to arrangements to define the skills and experiences that Auditors and Audit Managers require to do their jobs; to appraise individuals against those requirements; and to deliver necessary training, coaching and other development work.</p>	<p style="text-align: center;">Partly</p>	<p>Current Job Descriptions and Competency Matrices exist for all posts and regular appraisals are undertaken in line with corporate policy.</p> <p>Welland Board has approved a policy on professional training for Auditors and an adequate budget to support training.</p> <p>The Head of Consortium and the two Audit Managers hold full professional qualifications; engage in CPD; and have a minimum of 6 years experience of internal audit in local government.</p> <p>The last four recruitment exercises for Auditor posts (April 2007 to September 2012) have not attracted any suitable candidates with relevant audit experience. The Consortium has, instead, recruited graduates with a view to undertaking a development programme that has previously given good results</p> <p>The post of Audit Manager (the Head of Consortium's deputy) was vacant from June 2011 to January 2013: between 1<sup>st</sup> April 2012 and 1<sup>st</sup> November 2012 vacancy levels were 40% of establishment, rising to 50% in September and October.</p>	<p>During 2012/13 vacant management posts and the recruitment of new and inexperienced Auditors made it difficult to deliver appropriate levels of supervision and employee development.)</p> <p>During 2013/14 the Head of Consortium, supported by the Audit Managers, will carry out a structured review of each Auditor's development needs and ensure that training, supervision and allocation of assignments is delivered in a coherent manner to develop each Auditor's competencies</p>

Standard	Significance of Standard	Complies ?	Evidence	Issues and Areas for Development
Strategy and Planning	Relates to arrangements to ensure that the Annual Audit Plan is aligned with the Council's Aims and Objectives and that the Consortium has sufficient, appropriate resources to meet clients' needs and expectations.	Yes	<p>Audit &amp; Risk Committee endorsed the use of the Stamford Model as the basis for developing the 2012/13 Audit Plan. Committee has also been advised that the new PSIAS will require a change to the planning approach.</p> <p>The Welland Board has approved changes to the Consortium's delivery model and resource base so that greater use can be made of Audit Contractors to deliver specialist skills that are not deliverable by the in-house team (e.g. ICT auditing) and to allow for a flexible response to unforeseen client requirements.</p>	<p>It will be necessary to update the Strategy in 2013/14 to reflect the requirements of the PSIAS.</p> <p>It will also be necessary to develop formal protocols for engagement of audit contractors that conform with the revised Contract Procedural Rules for Rutland County Council (as employing body).</p>
Undertaking Audit Work	Relates to arrangements to ensure that audits focus on the things that matter to the clients; that assurance is delivered about key risks; and that the Auditor records sufficient relevant evidence to support audit opinions and recommendations.	Partly	<p>Risk and Control Evaluation Meetings allow for the identification and recording of clients' requirements. Terms of Reference are agreed for all assignments.</p> <p>Galileo Audit Software provides a framework for consistent recording and presentation of evidence</p> <p>For the Council's Key Financial Systems audit programmes have been designed, explicitly, to meet declared requirements of External Audit. As a result financial risk that do not meet External Audit's materiality requirements may be overlooked</p>	<p>The Audit Plan for 2013/14 provides for a specific assignment to meet External Audit requirements</p> <p>It will be necessary to update the Audit Manual in 2013/14 to reflect the requirements of the PSIAS</p> <p>As part of that update, the Head of Consortium will revise the audit planning processes to ensure that key risks are identified</p> <p>The way in which systems evaluation is undertaken is being reviewed</p>

Standard	Significance of Standard	Complies ?	Evidence	Issues and Areas for Development
Due Professional Care	Relates to arrangements to ensure that Auditors are doing work that is within their levels of competence and are demonstrating due care and diligence. The Standard also refers to the need to be alert for indicators of fraud or corruption; and to whistleblowing arrangements.	Partly	The Audit Manual includes a Statement of Personal Responsibility; guidance on Indicators of Fraud & Corruption; and guidance on whistleblowing.	<p>During 2012/13 staffing issues made it difficult to match available auditors to commissioned audits consistent with their skills and experience.</p> <p>See Staff Training &amp; Development. The Audit Plan for 2013/14 contains assignments consistent with a new-entrant Auditor under supervisions; and Auditors at different levels of professional development. In planning assignments the Head of Consortium and the Audit Managers will ensure that all work is appropriately allocated and supervised.</p>
Reporting	Relates to arrangements to ensure that appropriate sufficient and timely information is provided to clients and stakeholders; and that information is not subject to inappropriate influence.	Mostly	<p>Reporting lines to clients have been agreed and recorded. There are provisions for closing meetings with clients to confirm accuracy of reports and drafts of reports are circulated to interested parties in line with agreed reporting arrangements</p> <p>Galileo ensures a consistently structured reporting format is followed. Specific guidance has been issued on form and content of recommendations.</p> <p>When Terms of Reference are drafted, planned dates for delivery of work are agree.</p>	<p>During 2012/13 staffing issues made it impossible to meet agreed delivery dates and a significant proportion of assignments were not finalised until April/May 2013. In 2013/14 the PI "Audits on Time" will be used to ensure timely reporting</p> <p>During 2013/14 Galileo Report Templates will be revised to address specific issues of compliance with PSIAS</p>

Standard	Significance of Standard	Complies ?	Evidence	Issues and Areas for Development
Performance	Relates to arrangements to ensure that the Consortium can deliver, consistently, the quantity and quality of work required to deliver the assurance required by clients.	Mostly	<p>Audit Manual defines quality assurance processes.</p> <p>Galileo evidences quality assurance by tracking review points raised and cleared</p> <p>Targets for days delivered, auditor productivity and levels of customer satisfaction are set, monitored and reported to Governance Committee</p>	<p>During 2012/13 there was a 20% shortfall of resources which inevitable impacted on ability to satisfy clients' requirements. Every effort was made to mitigate the impact of the shortfall by open communication with clients as a way of identifying and meeting acceptable standards and levels of delivery. Successful recruitment exercises and the development of more formal relationships with suitable audit contactors should make the Consortium more robust.</p> <p>The PSIAS require the Consortium to develop further its quality assurance process by establishing a Quality Assurance &amp; Improvement Programme</p>