

APPENDIX A

REPORTING OFFICER:	Melanie Dexter – Audit Manager
DATE:	9 th June 2016
SUBJECT:	Merseyside Fire and Rescue Service - Annual Internal Audit Report 2015/16

1 Purpose

- 1.1 This report summarises the work that Internal Audit has undertaken across Merseyside Fire & Rescue Service (the 'Service') during the 2015/16 financial year; the service for which is provided by Liverpool City Council, Internal Audit Service.
- 1.2 The purpose of the Annual Internal Audit Report is to meet the Chief Internal Auditor (CIA) annual reporting requirements set out in the Public Sector Internal Audit Standards (PSIAS). It sets out the requirement for the CIA to report to senior officers and the 'Board' (for the service this is the Audit Sub-Committee) to help inform their opinions on the effectiveness of the framework of governance, risk and control in operation within the Authority. The PSIAS requirements are that the report must incorporate:
- An annual internal audit opinion on the overall adequacy and effectiveness of the organisation's governance, risk and control framework (the control environment);
 - a summary of the audit work that supports the opinion; and
 - a statement on conformance with the PSIAS and the results of the quality assurance and improvement programme.
- 1.3 The audit work has been carried out in accordance with the 2015/16 risk-based audit plan. The plan is designed to give reasonable assurance that controls are in place and working effectively. Opinions are formed in respect of each individual audit and the audit opinion is separated between control environment (the controls in place) and compliance (whether or not the controls have been adhered to) so it is easier to identify where corrective action is needed. We have retained the corporate impact opinion which is a measure of the significance of the findings to the organisation as a whole. An explanation of the level of assurance and corporate impact ratings are detailed within this report.
- 1.4 We have liaised with senior management throughout the year to ensure that internal audit work undertaken continues to focus on the high risk areas and in the light of new and ongoing developments in the service; to help ensure the most appropriate use of our resources.
- 1.5 As a result of this liaison some changes were agreed to the plan during the year and were brought to the 28th January Audit Sub-Committee Meeting. Specifically 3 internal audits were deleted from the plan, but an additional 4 audits were added to the plan. The total number of audits actually undertaken in 2015/16 is 12 compared to 14 in the prior year.

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- 1.6 A summary of the performance of Internal Audit against its performance measures is also included in this report.
- 1.7 The Annual Internal Audit Report is an important source of evidence for the Annual Governance Statement, and this report is timed to support the preparation of this Statement for the 2015/16 year.
- 1.8 We would like to thank those officers throughout the Authority who provided their assistance and cooperation in the course of our work throughout the year.

2 Opinion on the overall control environment

- 2.1 Internal Audit works to a risk based audit plan. The plan is designed to give reasonable assurance that controls are in place and working effectively. From the Internal Audit work undertaken in compliance with the PSIAS in 2015/16, it is our opinion that we can provide **Substantial Assurance** that the system of internal control in place at Merseyside Fire & Rescue Service for the year ended 31st March 2016 accords with proper practice.
- 2.2 The 2015/16 fundamental systems audits have shown a substantial level of compliance and none of the audits have identified weaknesses that have required a corporate impact assessment of major or moderate. Based on the audit work carried out in 2015/16 we are not aware of any significant control weaknesses within the Service which impact on the Annual Governance Statement.
- 2.3 We undertake individual internal audits with the overall objective of providing members, the Chief Fire Officer, the Treasurer and other officers with reasonable, but not absolute, assurance against material misstatement or loss and, accordingly, this opinion does not provide such an absolute assurance.
- 2.4 Internal Audit uses an overall opinion grading for audits and certain responsive work which is based on the ratings of the audit recommendations being made and is explained in more detail in section 5. The table below summarises the opinions given on internal audit work in 2015/16.

Fig 1 Summary of Opinions from the 2015/16 audit plan

Assurance Level	Control Environment	Compliance
Substantial	8	8
Good	1	1
Acceptable	0	0
Limited	0	0
None	0	0
Sub-total	9	9
Audits not yet reported	3	3

Assurance Level	Control Environment	Compliance
Total Audits Completed	12	12
Audits started not yet completed	1	1
Audits Deferred	2	2
Total	15	15

3 Summary of findings arising from Internal Audits in 2015/16

- 3.1 The opinion of the Chief Internal Auditor is informed significantly by the results of audits of the Authority's fundamental systems. These are the major systems which underpin the system of internal control and financial reporting. A summary of the outcomes of the audits for these systems for the year is set out below in Fig 2.

Fig 2 Completed fundamental systems audits from the 2015/16 audit plan

Audit Title	Control Environment	Compliance	Corporate Impact
Payroll	Substantial	Substantial	Minor
Budgetary Control	Substantial	Substantial	Minor
General Ledger	Substantial	Substantial	Minor
Treasury Management	Substantial	Substantial	Minor
Medium Term Financial Plan	Substantial	Substantial	Minor
Creditors	Substantial	Substantial	Minor
Debt Management	Substantial	Substantial	Minor
Ethical Governance*	<i>Review stage</i>	<i>Review stage</i>	<i>Review stage</i>
Procurement	<i>Planning stage</i>	<i>Planning stage</i>	<i>Planning stage</i>

* Report issued in draft

Payroll

- 3.2 The objective of the audit was to review the effectiveness of the key controls in place within the payroll system to form an opinion as to whether they are operating effectively to manage the relevant risks. The scope of the audit reviewed and tested the effectiveness of system controls, including those controls that ensure that employee records are created and terminated correctly; payroll expenditure is accurately recorded within the financial system; and monitoring arrangements are sufficient to prevent and detect payroll errors. The audit scope also included a review of the quality of data held on the system. Computer Assisted Audit Techniques (CAATs) were used to analyse payroll data over the selected period for specific tests such as potential duplicate employees and completeness of employee records.

Budgetary Control

- 3.3 The scope of the review was to examine the budget monitoring arrangements for the 2015/16 financial year to enable us to provide an overall opinion as to whether controls were adequate and effective. The audit included a review of key controls including the confirmation that procedures are in place to effectively control revenue expenditure and commitments and to ensure that these are reflected in the budget; that the frequency and adequacy of budget monitoring reports provided to cost centre managers is appropriate; that procedures are in place to ensure that significant variances are promptly identified, reported on and appropriate corrective action is taken; that the procedure for amending budgets is appropriate; and that there is regular reporting of the financial position to the Authority throughout the year.

General Ledger

- 3.4 The objectives of this audit were to review the effectiveness of the controls in place within the general ledger system for the 2015/16 financial year and to form an opinion as to whether they are operating effectively to manage the relevant risks. The main controls reviewed were the accuracy and completeness of financial data held on the system; controls covering unauthorised or inappropriate access to the system; the authorisation of journals; monitoring of the use of suspense accounts; and the bank reconciliation process. Where appropriate Computer Assisted Auditing Techniques (CAATs) were used in order to obtain greater coverage in the audit testing.

Treasury Management

- 3.5 The aims of this audit were to review the key controls in place within the Treasury Management system to form an opinion on whether they are operating effectively to ensure that associated risks are adequately mitigated. The main areas reviewed encompassed ensuring that reporting of Treasury activities was in line with the CIPFA Code of Practice; ensuring appropriate rationale behind investment decision making (including reviewing cash flow balances); the selection of institutions for investments is in line with the Authority's investment strategy and that the procedures for the authorisation of investments and loans are appropriate and were adhered to.

Medium Term Financial Plan

- 3.6 The purpose of this audit was to review the key controls in place with regards to the Medium Term Financial Plan and to form an opinion on whether they are operating effectively to ensure that associated risks are adequately mitigated. The main areas reviewed were ensuring that assumptions made are suitably robust; that the overall figures set out in the Plan are achievable; that the Plan allows the Service's key operational and financial aims and priorities to be met; and that the MTFP is reviewed and updated appropriately to take into account material changes.

Creditors

3.7 The audit examined the effectiveness of the key controls in place within the creditor system to form an opinion as to whether they are operating effectively to manage the relevant risks. To assist in this the review tested key controls in place that are designed to ensure all invoices are processed and paid on time; ensure all creditor details are correct and no duplicate accounts exist; ensure all payments are authorised prior to being processed; ensure the Authority is not overcharged for goods and services and ensure that the orders are not placed that exceed the budget limit. Where appropriate the use of CAATs testing was utilised to obtain a detailed level of analysis of the data.

Debtors

3.9 The scope of the audit involved reviewing the controls in place for the collection of sundry debts owed to MFRS. In particular the review focused on the following key controls: invoices are only raised when there is evidence of a debt owed and clearly show what the debt is for and who the payment should be made to. The procedures in place governing the recovery of debts owed were reviewed and assurance was sought to ensure debts are written off once recovery action has been exhausted.

Ethical Governance

3.10 The audit has been scoped to both examine the risks to the Authority and to review the key controls in respect to governance arrangements. The areas tested in the review included the arrangements for ensuring Members and Officers' are aware of the Code of Conduct; the arrangements for ensuring Members are aware of and comply with the correct procedure in respect of claiming for allowances; ensuring Members and Officers comply with the Code of Conduct in respect of gifts and hospitality and declarations of interest; and the maintenance of the policies and procedures for Members and Officers. The report is currently being reviewed by officers

3.11 A summary of all other audits completed during 2015/16 are shown in Fig 3 with a brief explanation for all audits. Assurance can also be taken when undertaking advisory work due to gaining an understanding of the relevant systems and how they operate.

Fig 3 Other Strategic/Client directed/Ad hoc audits completed from the 2015/16 audit plan

Audit Title	Control Environment	Compliance	Corporate Impact
Consultation / Equalities	Substantial	Substantial	Minor
Facilities Management Contract Management &	Good	Good	Minor

Audit Title	Control Environment	Compliance	Corporate Impact
Performance monitoring process			
Property & ICT Asset Management	<i>Review stage</i>	<i>Review stage</i>	<i>Review stage</i>
Ancillary Fleet & Vehicle Asset Management Plan	<i>Review stage</i>	<i>Review stage</i>	<i>Review stage</i>
IT applications	Deferred	Deferred	Deferred
Joint Working / Devolution Agenda	Deferred	Deferred	Deferred

Consultation / Equalities

- 3.12 The audit review examined the processes and procedures followed in the station merger / closure consultation exercises in order to provide assurance to the Authority that the consultation process took account of the views and opinions of all interested parties. In order to do this the procedures followed for consulting with interested parties over the planned closure / mergers of various fire stations to confirm the effectiveness of the process were reviewed.

Facilities Management Contract Management & Performance monitoring process

- 3.13 The overall objective of this work was to review contract management and performance monitoring arrangements operating for the new Facilities Management contract to ensure that they are at the level and standard expected. The scope covered the examination of the processes and procedures in place in order to give assurance to the Authority that they are effective and sufficient to ensure best value from the contract and the service provided.

Property & ICT Asset Management

- 3.14 The objective of this review is to ensure that there are adequate controls in place to safeguard property & ICT assets. The working papers are currently in review so it would be inappropriate to include an overall opinion at this stage.

Ancillary Fleet & Vehicle Asset Management Plan

- 3.15 The objective of this review is to ensure that there are adequate controls in place to safeguard assets owned, specifically that accurate records are maintained and that all vehicles and fleet, including ancillary fleet is utilised and managed effectively and efficiently. The working papers are currently in review so it would be inappropriate to include an overall opinion at this stage.

- 3.16 It is our intention to report the opinions for both these asset management audits to the next scheduled audit sub-committee meeting.

Contingency/Responsive/Advice and Assistance

- 3.17 No contingency/responsive time was allocated this financial year; this time is frequently used for grant certifications or to provide ad-hoc advice & assistance but it has not been required on this occasion.
- 3.18 The following two audits were not undertaken as it was considered in both instances that the time would be better spent in the forthcoming year when both areas were sufficiently developed, they will therefore be carried forward to the 2016/17 audit plan:

Fig 4 Audits deleted from the 2015/16 audit plan

Audit Title	Notes
ICT Applications	These audits will be rolled forward into 2016/17
Joint Working / Devolution Agenda	

Follow Up

- 3.19 It is our policy to follow up all recommendations that are given either a three star (essential/strategic) or a two star (high) priority rating. All recommendations made in 2014/15 were followed up within 6 months of the agreed implementation date and were found to have been implemented, with the exception of two recommendations for contract management as the report was only issued in late March. These will be followed up when due and will be reported accordingly.

4 Internal Audit service delivery

- 4.1 The key performance indicators for Internal Audit are set out in the table below, together with the outturn at the year end compared to target and those achieved in 2014/15.

Fig 5 Internal Audit Performance

Performance Measure	Target 2015/16	Actual 2015/16	Actual 2014/15
Completion of audit exercises consistent with the audit plan	90%	80% (92%)	88% (100%)
% of audit reports issued within time target	80%	67%	64%
Average score out of 5 for overall value added by IA work based on returned satisfaction questionnaires.	4.5	4.5	4.7

- 4.2 Actual performance for performance measure one (completion of audit exercises consistent to audit plan) appears poor compared to the previous year but this is because two planned audits were dropped from the agreed plan at the request of Service management. If these audits are excluded actual performance achieved is 92%, in line with the target.
- 4.3 Measure two (% of audits issued within time target) continues to require improvement; we may need to consider extending timescales for reporting as public sector teams tend to have fewer staff and larger workloads and hence time is spread more thinly.

Quality Assurance and Improvement Programme

- 4.4 The Public Sector Internal Audit Standards (PSIAS) require each Chief Internal Auditor to assess the Internal Audit service and ascertain any improvements that are required to be made. Whilst this requirement is new that activity has always been undertaken on a continuous basis using our corporate approach and therefore we have not changed the format.

Compliance with the PSIAS

- 4.5 Internal Audit has been assessed internally by the Chief Internal Auditor against the PSIAS and has concluded that Internal Audit complies with the PSIAS in all material respects. An external peer review will be carried out in line with the requirements of the PSIAS, during the forthcoming financial year as reported separately to the 28th January Audit Sub-Committee meeting.
- 4.6 The table below summarises budgeted and actual audit days for information, based on an agreed 112 days’ work. Actual time is less than planned time as two of the audits have not taken place. It is our intention that the contracted 112 days per year are fulfilled over the two years if required.

Fig 6 Actual v Budgeted Days

Audit Title	Planned	Actual
Fundamentals	40	50
Strategic reviews/client directed/ad-hoc reviews	55	40
Contingency	4	0
Follow Up	5	1
Audit management	8	8
Total	112	99

5 Definitions of audit assurance

- 5.1 Internal Audit uses an overall opinion grading for audits and some responsive work. Where no issues surrounding the control environment are found, a substantial level of assurance will be given on the controls tested.

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However where weaknesses with controls have been identified, depending on the potential impact of those weaknesses, a lower graded assurance level will be given.

- 5.2 The grades, which are summarised in the table below, are based on the ratings of the audit recommendations being made. The corporate impact rating sets the audit findings in context based on the overall risk to the Service.

Control Environment Assurance – Opinion on the design and suitability of the current internal controls.	
Level	Definition
Substantial	There are minimal control weaknesses that present very low risk to the control environment
Good	There are minor control weaknesses that present low risk to the control environment
Acceptable	There are some control weaknesses that present a medium risk to the control environment
Limited	There are significant control weaknesses that present a high risk to the control environment
None	There are fundamental control weaknesses that present unacceptable level of risk to the control environment
Compliance Assurance – Opinion on the level of compliance with current internal controls.	
Level	Definition
Substantial	The control environment has substantially operated as intended.
Good	The control environment has largely operated as intended although some minor errors have been detected
Acceptable	The control environment has mainly operated as intended although errors have been detected
Limited	The control environment has not operated as intended. Significant errors have been detected
None	The control environment has fundamentally broken down and is open to significant error or abuse
Organisational impact – The potential impact on the organisation if the recommendations are not implemented.	
Level	Definition
Major	The weaknesses identified during the review have left the Council open to significant risk. If the risk materialises it would have a major impact upon the organisation as a whole.
Moderate	The weaknesses identified during the review have left the Council open to moderate risk. If the risk materialises it would have a moderate impact upon the organisation as a whole.
Minor	The weaknesses identified during the review have left the Council open to a low level of risk. If the risk materialises it would have a minor impact on the organisation as a whole.