

**AGENDA ITEM:**

<b>REPORT TO:</b>	<b>MERSEYSIDE FIRE &amp; RESCUE AUTHORITY</b>
<b>DATE:</b>	<b>17 MAY 2012</b>
<b>REPORT NO.</b>	<b>CFO/080/12</b>
<b>REPORTING OFFICER:</b>	<b>DEPUTY CHIEF EXECUTIVE</b>
<b>CONTACT OFFICER:</b>	<b>IAN CUMMINS, HEAD OF FINANCE, EXTN. 4244</b>
<b>OFFICERS CONSULTED:</b>	
<b>SUBJECT:</b>	<b>ANNUAL REVIEW OF INTERNAL AUDIT</b>

**APPENDIX A TITLE Annual Internal Audit Report 2011/12 – Merseyside Fire & Rescue Service**

**Hard copy attached**

Purpose of Report

1. To review the work of Internal Audit in 2011/12.

Recommendation

2. The report to be noted.

Introduction & Background

3. Internal Audit is an independent appraisal function established by the management of an organisation for the review of the internal control system as a service to the organisation. It objectively examines, evaluates and reports on the adequacy of internal control as a contribution to the proper, economic, efficient and effective use of resources. (Source: Code of Practice for Internal Audit In Local Government).
4. The Authority has a statutory duty to ensure that it maintains an adequate and effective system of Internal Audit of its accounting records and control systems. (Accounts and Audit (England) Regulations 2011).
5. In order to fulfil these functions the Authority has carried out a competitive tendering exercise in 2004,2008 and 2011 in which each of the five Merseyside District Councils and others, were invited to bid to provide Internal Audit services for the Authority. The contract was awarded to Liverpool City Council's Internal Audit Service on all occasions. The current contract is for a three year period, with effect from 1<sup>st</sup> April 2011, with an option for a one year extension.

6. Each year Internal Audit submit a plan for their work following consultation with the Deputy Chief Executive and other key officers. This plan is set based upon an assessment of risks, previous findings and the relationship with External Audit work. The 2011/12 plan was considered by the Audit & Value For Money Scrutiny Panel on 8<sup>th</sup> September, 2011 (CFO/095/11).
7. The Internal Audit outturn report for 2011/12 is attached as Appendix A. On the basis of the reviews undertaken Internal Audit have concluded that ***“the Authority’s internal control environment is adequate and generally effective, bearing in mind that any control system can provide only reasonable assurance and not absolute assurance”....”Based on the audit work carried out in 2011/12 we are not aware of any significant control weaknesses within MFRS which impact on the Annual Governance Statement”***
8. Appendix A provides a brief overview of the key findings of each audit. Details of audit work and copies of the audit reports are reported on a regular basis to members via the quarterly financial monitors to the Audit & Value For Money Scrutiny Committee. Unless Internal Audit finds major system faults in any area, full audit reports are not normally presented to the Authority.
9. During 2011/12 Internal Audit have completed 11 reviews of major systems and with a further 2 currently being finalised. 8 out of the 11 audit reviews found high or significant assurance in the current system of control and governance. In 2 audit reviews the opinion was that moderate or limited assurance could be given as some weaknesses or non-compliance with procedures had been identified. Officers have considered the recommendations made by Internal Audit to resolve the system control or governance weaknesses and have agreed actions with Internal Audit to resolve these issues. Officers have in all cases implemented the required changes in 2011/12 or they are planned to be in place in 2012/13.

#### Equality & Diversity Implications

10. None arising from this report.

#### Staff Implications

11. There are no staff implications arising from this report.

#### Legal Implications

12. The Authority has a statutory duty to ensure that it maintains an adequate and effective system of Internal Audit of its accounting records and control systems. (Accounts and Audit (England) Regulations 2011).

#### Financial Implications & Value for Money

13. The cost of the Internal Audit Service from Liverpool City Council in 2011/12 was some £35,500. The Authority had made adequate budget provision in 2011/12 to pay for these audit services.

## Risk Management, Health & Safety and Environmental Implications

14. None arising from this report.

## Contribution to Our Mission – To Achieve: Safer Stronger Communities – Safe Effective Firefighters

15. The Authority is committed to ensuring strong internal control processes are in place to ensure all information and services delivered are transparent and fair and all audit requirements are adhered to. The Authority continues to strive to maintain the highest level of standards and commitment to the community it serves.

## **BACKGROUND PAPERS**

- Account and Audit (England) Regulations 2011
- Code of Practice for Internal Audit in Local Government, CIPFA 2003

## APPENDIX A

<b>REPORTING OFFICER:</b>	Melanie Dexter – Audit Manager
<b>DATE:</b>	17 May 2012
<b>SUBJECT:</b>	Annual Internal Audit Report 2011/12 - Merseyside Fire and Rescue Service

### 1 Purpose

- 1.1 The purpose of this report is to provide a summary of the work performed on behalf of MFRS and to inform the Authority on the audit opinions, and key issues raised by Internal Audit during 2011/12.
- 1.2 The work has been carried out in accordance with the 2011/12 risk based audit plan and the agreed audit days have been delivered. The plan is designed to give reasonable assurance that controls are in place and working effectively. All of our planned work has been performed for 2011/12, with the exception of the treasury management and performance management reviews which are yet to be finalised.
- 1.3 Section 10.4 (Annual Reporting and Presentation of Audit Opinion) of the CIPFA Code of Practice for Internal Audit in Local Government requires the Head of Internal Audit to provide a report annually, this report should include:
  - An opinion on the effectiveness of the overall control environment based on Internal Audit work carried out in 2011/12;
  - A summary of the main issues arising from Internal Audit work during 2011/12;
  - A summary of the performance of Internal Audit against its performance measures.
- 1.4 The Annual Internal Audit Report is also an important source of evidence for the Annual Governance Statement. This report is timed to support the preparation of this Statement for the 2011/12 year.
- 1.5 This report does not include individual audit recommendations made as individual audit reports are provided during the year and presented to Committee as and when completed.

### Acknowledgements

- 1.6 We would like to thank those officers throughout MFRS 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. On the basis of audit reviews carried out in 2011/12, Internal Audit concluded that the Authority's ***internal control environment is adequate and effective, bearing in mind that any control system can provide only reasonable assurance and not absolute assurance.***
- 2.2 Based on the audit work carried out in 2011/12 we are not aware of any significant control weaknesses within MFRS which impact on the Annual Governance Statement.
- 2.3 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 4. The table below summarises the opinions given on internal audit work in 2011/12 compared to 2010/11.
- 2.4 Please note: the 2010/11 opinion descriptions have been restated to match the opinion terminology adopted for 2011/12 onwards.

Assurance Level	No. of audits 2011/12	% of total	No. of audits 2010/11	% of total
High	5	50	12	86
Significant	3	30	0	0
Moderate	1	10	2	14
Limited	1	10	0	0
Total	10*	100	14**	100

\* of the 14 items on the plan, two are incomplete (performance management & treasury management), one was not performed (Control Centre Efficiency, due to the cancelled regional control centre project) and one did not result in an opinion (responsive work).

\*\*of the 15 items on the plan, 1 did not result in an opinion (consultation work on PFI arrangements).

### 3 **Summary of main issues arising from Internal Audits in 2011/12**

#### **Fundamental Systems**

- 3.1 The areas covered comprised: payroll, non-pay expenditure (procurement), budgetary control, general ledger, debtors and treasury management. The payroll and general ledger audits involved the use of Computer Assisted Audit Techniques (CAATs) to perform a series of tests to validate specific data. By using CAATs we were able to consider the whole of the data population testing for certain criteria and enhance the assurance we are able to provide over the effective operation of the system.
- 3.2 The opinion of the Head of Internal Audit is informed significantly by the results of audits of the fundamental systems. The results of these audits show a solid level of assurance with the majority of the opinions showing high assurance levels and relatively low corporate impacts.
- 3.3 Two star recommendations were made following only one of the reviews: the procurement review was performed to provide assurance on the effectiveness of contract management procedures within the Authority. The main finding was in relation to the ongoing monitoring of existing contracts; although the procurement team's contract managers are well trained and knowledgeable there is little in the way of formal review of the service provided by contractors. It has been noted that a more structured performance monitoring procedure has recently been adopted for all north-west collaborative contracts and the Authority is keen to use this as an appropriate standard to apply to new contracts going forward.
- 3.4 We have not completed the fieldwork for the treasury management review so it would be inappropriate to include an overall opinion at this stage.

#### **Strategic reviews/Client directed/Ad hoc reviews**

- 3.5 The areas covered here comprised: workforce planning, income generation, PFI, information security policies, ethical governance & performance. The control environment and systems are operating effectively to ensure that the majority of relevant risks are well managed.

#### ***Workforce Planning***

- 3.6 The audit included a review of the workforce planning strategies and plans put in place within the Authority to effectively address the reduction in government funding, and the arrangements in place for maintaining appropriate skilled and experienced staff.

- 3.7 Based upon the audit testing, we were able to perform at this time, we can provide assurance that adequate controls are in place, and that the key risks are being effectively managed. However, we found that the process is in the early stages, and a number of the documents and plans are still to be developed. As a consequence, a subsequent brief audit overview in late 2012/13 is planned to identify progress to date, and confirm the current position.

#### ***Income Generation***

- 3.8 The objective of this review was to assess the work that the Authority has undertaken in relation to income generation, in response to the significant public sector budget cuts. The Authority carried out a review of their main controllable income lines to identify any areas where income could be potentially increased. Our work provided assurance that MFRS have taken appropriate steps to review their controllable income in order to explore potential options that may contribute towards minimising the impact of the budget cuts.

#### ***PFI***

- 3.9 The overall objective of the audit was to review the contract management framework for the project, and review the controls in place to ensure that robust procedures are operating for monitoring the performance of the contractor. As the project build is still in its relative infancy, elements of our testing were limited. However, based on the audit testing, we were able to perform at this time we can provide significant assurance that the controls are operating effectively. Further Internal Audit work will be performed in 2012/13.

#### ***Information Security Policy***

- 3.10 The aim of this audit was to establish whether the Authority's information security policy was in line with best practice, and appropriate to the needs of the organisation. The Authority has put in place a robust set of procedures to protect the information it both holds and produces. These practices are largely supported by a comprehensive set of policies and guidance documents although there were instances where although an appropriate action was taking place, it was not specifically detailed in a policy or procedure note as a requirement. We can provide assurance that the control environment is operating effectively to ensure that the majority of relevant risks are managed.

#### ***Ethical Governance***

- 3.11 This audit set out to review the governance arrangements in place relating to both Members and Officers gifts and hospitality and Members allowances. The Gifts and Hospitality Registers were reviewed along with other relevant policies and procedures.
- 3.12 Based on the audit testing we were only able to provide limited assurance that the controls are operating effectively due to the weaknesses found in relation to the Officer's register of gifts and hospitality. Our audit opinion was based on the manner in which gifts and hospitality were recorded and the fact that the records did not contain sufficient information to allow effective public scrutiny.

- 3.13 Senior officers are currently looking into specific concerns raised and are due to provide a formal response in the near future. Work is also already in progress to implement a revised Officer Code of Conduct, and it is currently out for consultation. Guidance has also been drafted to assist in practical implementation alongside the revised Code of Conduct and training is planned for officers. We therefore have a degree of assurance that because of the changes already planned to date the corporate impact is assessed as low.

#### ***Performance Management***

- 3.14 This review is focused upon the reporting of performance data to identify whether key stakeholders are supplied with the appropriate information regarding performance management in relation to key areas, and to establish whether appropriate action is being taken to address any performance issues. The fieldwork is still in progress.

#### **Responsive Work**

- 3.15 A review was undertaken following concerns that a small grant payment payable to MFRS was erroneously paid into the personal bank account of an MFRS employee. The review examined the arrangements within MFRS for claiming grants and the reasons why the payment was made in this way. The review confirmed that there is a clear procedure for claiming grants from outside organisations but in this instance the correct procedures were not followed. However, there was no evidence to suggest fraudulent intentions. Appropriate action has been taken to ensure relevant procedures are clearly communicated and refresher training has been provided.

#### **Follow Up**

- 3.16 It is our policy to follow up all recommendations that are given either a three star (essential/strategic) or a two star (substantial) priority rating. All but one set of recommendations made in 2010/11 were followed up within 6 months of the agreed implementation date. All were found to have been implemented. The follow up of a petty cash review (responsive work) is due to take place next month.

### **4 Summary of audit opinions**

- 4.1 Internal Audit uses an overall opinion grading for audits and some responsive work. Where no issues surrounding the control environment are found, a high level of assurance will be given on the controls tested. However where weaknesses with controls have been identified, depending on the potential impact of those weaknesses, a lower graded assurance level will be given.



4.2 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 Authority.

<b>Audit Opinion</b>	<b>Explanation</b>
High	There is a sound system of control and governance in place to achieve the system objectives, controls are being consistently applied and the relevant risks to the service are well managed
Significant	The control environment / systems are operating effectively to ensure that the majority of relevant risks are managed. Slight improvements need to be made in order to provide substantial assurance that all of the objectives of the system are met.
Moderate	Weaknesses and / or non-compliance with procedures are placing system objectives at risk.
Limited	There are control weaknesses and/or non-compliance with basic controls that are so significant the relevant risks are not being managed at all. The system is open to significant error or abuse.
<b>Corporate Impact</b>	<b>Description of Risk</b>
High	<ul style="list-style-type: none"> <li>• Total service loss for a significant period</li> <li>• Fatality of employee/service user/other person</li> <li>• Adverse national media coverage</li> <li>• Severe stakeholder concerns</li> <li>• Mass complaints</li> <li>• Financial loss in excess of £1 million</li> </ul>
Medium	<ul style="list-style-type: none"> <li>• Significant service disruption</li> <li>• Major disabling injury</li> <li>• National media coverage</li> <li>• Significant service user complaints</li> <li>• Financial loss in excess of £100,000</li> </ul>
Low	<ul style="list-style-type: none"> <li>• Limited service disruption</li> <li>• Adverse local media coverage</li> <li>• Some service user complaints</li> <li>• Stakeholder concerns</li> <li>• Financial loss in excess of £10,000</li> <li>•</li> </ul>
Negligible	Short term inconvenience Negligible injury Local media coverage Isolated service user complaints Financial loss less than £10,000

The audit opinions given against work carried out in 2011/12 are shown against each of the completed pieces of work in the table below:

<b>Audit Subject</b>	<b>Audit Opinion</b>	<b>Corporate Impact</b>
<b>Fundamental Systems</b>		
Payroll	High	Negligible
Budgetary Control	High	Negligible
General Ledger	High	Negligible
Debt Management	High	Negligible
Non-pay expenditure	Moderate	Low
Treasury Management	WIP	WIP
<b>Strategic Reviews/Client Directed /ad-hoc Reviews</b>		
Workforce Planning	High	Negligible
Income Generation	Significant	Low
PFI	Significant	Low
Information Security Policy	Significant	Low
Ethical Governance	Limited	Low
Control Centre Efficiency	n/a	n/a
Performance Management	WIP	WIP
<b>Responsive</b>		
Grant Payment	n/a	n/a

## 5 Internal Audit service delivery

5.1 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 2011/12. The percentage of audit reports issued within time target has slipped it will therefore be a priority in 2012/13 for us to ensure we meet these targets.

<b>Performance Measure</b>	<b>Target 2011/12</b>	<b>Actual 2011/12</b>	<b>Actual 2010/11</b>
Completion of audit exercises consistent with the audit plan	90%	85%	93%
% of audit reports issued within time target	80%	67%	79%

<b>Performance Measure</b>	<b>Target 2011/12</b>	<b>Actual 2011/12</b>	<b>Actual 2010/11</b>
Average score out of 5 for overall value added by Internal Audit work based on returned customer survey questionnaires.	4.5	<b>4.4</b>	<b>4.3</b>

### **Audit Plan**

- 5.2 The table below summarises budgeted and actual audit days and number of audits. 10 of the planned audits were completed by the year end, with the treasury management and performance audits due to be reported on in May 2012. The audit of the Regional Control Centre was dropped from the non-financial systems element of the plan and an additional piece of work was completed from the contingency-responsive budget.

	<b>11/12 Audit Plan</b>		<b>Actual Results for 11/12</b>	
	Total No.days	No of audits	Total No.Days	No of audits completed
Fundamentals	45	6	<b>39</b>	<b>5</b>
Strategic reviews/client directed/ad-hoc reviews	66	7	<b>68</b>	<b>5</b>
Contingency	5	-	<b>17</b>	<b>1</b>
Follow Up	5	-	<b>0</b>	-
Audit management	9	-	<b>13</b>	-
<b>Total</b>	130	13	<b>137</b>	<b>11</b>