

**REPORT TO:** Audit and Governance Committee

**MEETING DATE:** 19 June 2012

**BY:** Executive Director (Support Services)

**SUBJECT:** Internal Audit Annual Report 2011/12

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## **1 PURPOSE**

- 1.1 To inform the Audit and Governance Committee of Internal Audit work carried out during the period from April 2011 to March 2012.

## **2 RECOMMENDATION**

- 2.1 That the Audit and Governance Committee note the contents of the Internal Audit Annual Report 2011/12.

## **3 BACKGROUND**

- 3.1 The CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom requires that the Internal Audit Manager should prepare an annual report which details the audit work undertaken.
- 3.2 The work of Internal Audit plays a key role in providing assurance to Management on the adequacy and effectiveness of internal controls.
- 3.3 The audit work undertaken in 2011/12 identified a number of areas with scope for improvement – the main areas are outlined in Appendix A.
- 3.4 Internal Audit also undertook a range of other work including assisting in the improvement of existing systems and the implementation of new systems, providing advice and consultancy on a range of internal control issues, the auditing of annual accounts of Management Committees, investigating the circumstances surrounding returned cheques, analysing financial information in respect of external organisations, attendance at year-end stocktakes and advice and support to Community Councils.

## **Key Measures of Performance**

### **3.5 Percentage of audit recommendations accepted by Management – 99%**

In 2011/12 Internal Audit made 154 recommendations to Management. Management have responded positively to both the findings and recommendations and have agreed to take action to address the areas with scope for improvement.

### **3.6 Percentage of audit staff with CCAB accounting qualifications – 80%**

The Internal Audit Unit operates with a complement of 5 staff members, four qualified auditors and one part-qualified senior audit assistant.

### **3.7 Completion of the audit plan**

The audit plan for 2011/12 was approved by the Audit and Governance Committee in September 2011 and covered the period from October 2011 to September 2012. However, to meet the requirements of the Council's new external auditors the audit plan was re-aligned in March 2012 to reflect the Council's financial year and a revised audit plan for 2012/13 was approved by the Audit and Governance Committee covering the period from April 2012 to March 2013.

The work undertaken in financial year 2011/12 forms the basis of this report and the findings from our audits have informed our Controls Assurance Statement for 2011/12.

## **4 POLICY IMPLICATIONS**

### **4.1 None**

## **5 EQUALITIES IMPACT ASSESSMENT**

### **5.1 This report is not applicable to the well being of equalities groups and Equality Impact Assessment is not required.**

## **6 RESOURCE IMPLICATIONS**

### **6.1 Financial – None**

### **6.2 Personnel – None**

### **6.3 Other – None**

## **7 BACKGROUND PAPERS**

- 7.1 CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom.
- 7.2 Audit and Governance Committee, 28 September 2010 – Audit Plan 2010/11.
- 7.3 Audit and Governance Committee, 27 September 2011 – Audit Plan 2011/12.

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## Appendix A

### Audit work undertaken – April 2011 to March 2012

Audit	Key Findings	Number of Recommendations
<b>Debtors</b>	<p>The main objective of the audit was to ensure that sundry income due to the Council was properly identified, collected and accounted for.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"><li>• At present, the Council has no formal procedures in place to provide detailed guidance on its main financial processes, including income collection and the sundry accounts process. <i>Risk – errors and irregularities may occur.</i></li><li>• There is a lack of segregation of duties in respect of raising invoices, collection of income and the write-off of debts. <i>Risk – errors and irregularities may remain undetected.</i></li><li>• The systems in place for raising invoices were considered inadequate – in a number of areas examined, invoices had not been raised promptly. <i>Risk – loss of income to the Council.</i></li><li>• The existing practice of using the debtors system to raise invoices for income received in advance requires review. <i>Risk – failure to properly account for income received.</i></li><li>• Regular reconciliations are not being undertaken between the debtors' ledger and the debtors control account in the general ledger. <i>Risk – errors and irregularities may remain undetected.</i></li><li>• There was a failure to properly account for capital and interest payments received in respect of common repairs. <i>Risk – failure to correctly allocate income received.</i></li><li>• No systems are in place to ensure that credit balances are monitored on a regular basis – credit balances on the debtors' ledger at 1 March 2011 were approximately £282,000. <i>Risk – errors and irregularities may remain undetected.</i></li><li>• There is a lack of regular reviews of cancelled invoices, credit notes issued, suppressed accounts and bad debts written off. <i>Risk – errors and irregularities may remain undetected.</i></li></ul>	21

Audit	Key Findings	Number of Recommendations
<b>Bank Reconciliations</b>	<p>The main objective of the audit was to ensure that the arrangements in place for undertaking bank reconciliations were adequate.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The Council's Financial Regulations specify that Statements of Current Working Method will be maintained for each of the Council's main financial processes – Statements of Current Working Method have yet to be developed for cash and banking. <i>Risk – lack of clear guidance.</i></li> <li>• The approach currently adopted for preparing bank reconciliations requires review – bank reconciliations for the general account do not compare the balance between the bank statement and the cashbook as at the same date. <i>Risk – failure to identify if differences relate to genuine month end timing differences rather than to error.</i></li> <li>• For the general account, there were significant delays in the monthly bank reconciliations being carried out. <i>Risk – failure to promptly identify anomalies or items requiring further investigation.</i></li> </ul>	7
<b>Non-Domestic Rates (Valuation &amp; Billing)</b>	<p>The main objective of the audit was to ensure that internal controls surrounding the administration of Non-Domestic Rates Valuation and Billing were adequate.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• There is a lack of clear separation of duties – members of staff involved in the raising of Non-Domestic Rates bills are also responsible for carrying out amendments to the system, the suppression of accounts, the collection of income and the recovery of debt. <i>Risk – errors and irregularities may remain undetected.</i></li> </ul>	3

Audit	Key Findings	Number of Recommendations
	<ul style="list-style-type: none"> <li>• There is a lack of a clear audit trail for suppressed accounts – the date the recovery hold is placed on the account is not being entered on the Capita system. <i>Risk – lack of an audit trail.</i></li> <li>• For composite properties i.e. properties which have both commercial and residential uses, no procedures are in place for reconciling the total number of properties between the Non-Domestic Rates system and the Council Tax system. <i>Risk – information held may be inaccurate.</i></li> </ul>	
<b>Non-Domestic Rates (Liability)</b>	<p>The main objective of the audit was to ensure that internal controls surrounding the administration of Non-Domestic Rates Liability were adequate.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The procedures in place for the award of discretionary rates relief require review. <i>Risk – inconsistencies may occur in the award of discretionary reliefs.</i></li> <li>• There was a lack of documentary evidence to support the award of unoccupied property relief. <i>Risk – lack of a clear audit trail.</i></li> <li>• No planned programme of visits is currently undertaken for properties receiving unoccupied property relief. <i>Risk – reliefs and exemptions awarded may not be valid.</i></li> <li>• The monitoring arrangements for the award of Small Business Bonus Scheme relief require review. <i>Risk – failure to apply the relief scheme accurately.</i></li> <li>• The rural settlement list currently held is not updated on an annual basis and made available for public inspection. <i>Risk – failure to comply with legislation.</i></li> </ul>	6

Audit	Key Findings	Number of Recommendations
<b>Council Tax Refunds</b>	<p>The main objective of our audit was to ensure that all refunds are valid and that an adequate audit trail exists for all refunds made.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The existing arrangements in place for reconciling refunds between the Council Tax system and the Council's General Ledger require review. <i>Risk – errors and irregularities may occur and remain undetected.</i></li> <li>• The approved authorised signatory list was incomplete and failed to properly record all members of staff authorising refunds. <i>Risk – inappropriate refunds may be made.</i></li> <li>• There is a lack of checking procedures in place to ensure that all transfers between Council Tax accounts are valid. <i>Risk – errors and irregularities may occur and remain undetected.</i></li> <li>• There was a failure to review all refunds that may result in a debit balance on the taxpayer's account. <i>Risk – inappropriate refunds may be made.</i></li> <li>• No reviews are currently undertaken of Council Tax accounts with credit balances. <i>Risk – errors and anomalies may remain undetected.</i></li> </ul>	13
<b>Benefits</b>	Detailed testing was carried out on a sample of 30 benefit cases as part of a joint audit with Audit Scotland.	Results were passed to Audit Scotland

Audit	Key Findings	Number of Recommendations
<p><b>Procurement</b></p>	<p>The main objective of the audit was to ensure that the procurement of goods, services and works was in accordance with the Council's Standing Orders and Corporate Procurement Procedures.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• In some instances there was a lack of evidence to demonstrate that contractors invited to submit quotes had been selected on a fair and equitable basis. <i>Risk – favouritism and bias may occur.</i></li> <li>• In one instance we found that a tender received late had been considered as part of the evaluation process and the contractor was subsequently awarded the contract. <i>Risk – the integrity of the tender process may be compromised.</i></li> <li>• Departures from Corporate Procurement Procedures had not been properly approved by relevant Council Officers as required by the Council's Standing Orders – in 2 cases reports submitted to Cabinet stated that appropriate authorisation had been received from the Chief Executive and the Head of Law and Licensing, although no prior approval had been given. <i>Risk – information provided to Members may be inaccurate.</i></li> <li>• For contracts in excess of £250,000 we found instances where a performance bond had not been obtained from the contractor. <i>Risk – inability to recover costs for non-completion of contracts.</i></li> <li>• The contracts register in place was found to be incomplete – in a number of instances departments had entered into a contract with suppliers, but had failed to complete appropriate documentation to enable the Corporate Procurement Team to update the contracts register. <i>Risk – information may be incomplete.</i></li> <li>• The Council's website contains inaccurate information – the website states that the Council has an approved list of suppliers for construction works below £1.2 million, however no such list exists. <i>Risk – information may be misleading.</i></li> </ul>	<p>9</p>



Audit	Key Findings	Number of Recommendations
<p><b>Homelessness Bed &amp; Breakfast</b></p>	<p>The main objective of the audit was to ensure that internal controls surrounding the administration of Homelessness Bed &amp; Breakfast were adequate.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• There was a lack of supporting documentation to confirm that tenders had been properly evaluated in accordance with the agreed evaluation criteria. <i>Risk – B &amp; B providers may not meet the key requirements and standards expected by the Council.</i></li> <li>• In one case, a B &amp; B provider used by the Council was not part of the approved Framework Agreement and did not have a formal contract in place. <i>Risk – failure to comply with the Council's terms and conditions.</i></li> <li>• Payments for B &amp; B services made to one provider were at rates in excess of the agreed contracted rates. <i>Risk – irregularities may occur.</i></li> <li>• Information provided to homeless applicants in respect of the timescales for the submission of appeals was inconsistent with legislation. <i>Risk – non-compliance with legislation.</i></li> <li>• The arrangements in place to ensure that homeless applicants complete and return their Housing Benefit application form require review. <i>Risk – failure to recover all amounts due to the Council.</i></li> <li>• There was a lack of monitoring arrangements in place to ensure that discounts offered by B &amp; B providers had been correctly deducted from supplier invoices. <i>Risk – excess costs may be incurred by the Council.</i></li> <li>• The Homelessness Section made a payment of £6,300 to a B &amp; B provider, despite being advised that the Council had no liability for these costs. <i>Risk – inappropriate payments may be made by the Council.</i></li> <li>• The number of homeless applicants placed in certain B &amp; B establishments by the Council resulted in the B &amp; B providers breaching legislation relating to multiple occupancy. <i>Risk – breaches in legislation may occur.</i></li> </ul>	<p>24</p>

Audit	Key Findings	Number of Recommendations
<p><b>Framework Agreement – Tender Evaluation</b></p>	<p>The main objective of the audit was to review key aspects of the tendering exercise.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• There was a lack of documentation in place to demonstrate why a Framework Agreement had been selected as the most appropriate procurement route. <i>Risk – lack of an audit trail to confirm that all procurement options had been considered.</i></li> <li>• There was a lack of evidence to confirm that tender documentation had been properly checked for accuracy and completeness prior to issue – the annual budget figure quoted in the tender documentation was found to be incorrect. <i>Risk – errors and omissions may remain undetected.</i></li> <li>• The pricing element of the tender was based on a Schedule of Rates rather than a Bill of Quantities – the total price submitted by contractors and used in the tender evaluation bore no relationship to the actual overall costs that would be incurred by the Council over the period of the Framework Agreement. <i>Risk – inappropriate award decisions may be made.</i></li> <li>• There was a lack of adequate arrangements in place to ensure that all aspects of tender preparation had been properly reviewed and supervised – there was a failure to ensure that appropriate consideration had been given to the planned programme of work to be undertaken, the product specifications required and the measurements that contractors were asked to price for. <i>Risk – inaccuracies and omissions may remain undetected.</i></li> <li>• The existing procedures in place for the evaluation of tenders require review including the criteria used in the selection and award stages, the weightings split between price (25%) and quality (75%) and the scoring of quality criteria. <i>Risk – failure to achieve best value for the Council.</i></li> <li>• The arrangements in place for obtaining and evaluating references were considered unsatisfactory. <i>Risk – lack of robust procedures may adversely impact on the evaluation and selection of contractors.</i></li> </ul>	<p>14</p>

Audit	Key Findings	Number of Recommendations
<p><b>Tyne Esk LEADER Programme</b></p>	<p>The main objective of the audit was to ensure that adequate systems and processes were in place for administering the Tyne Esk LEADER Programme.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The procedures in place for the processing of LEADER applications and the payment of LEADER grant claims require review. <i>Risk – failure to comply with relevant regulations and guidance.</i></li> <li>• There was a lack of evidence to confirm that proper consideration had been given to the total amount of LEADER funding available for applications assessed and approved by the Local Action Group (LAG). <i>Risk – over commitment of project funds.</i></li> <li>• The existing monitoring arrangements failed to incorporate the revised technical guidance issued in July 2011 in respect of both on-the-spot checks and ex-post checks. <i>Risk – failure to comply with relevant regulations and guidance.</i></li> <li>• There was insufficient information on the project files to enable an assessment to be made of the legitimacy and accuracy of processing. <i>Risk – lack of an audit trail.</i></li> <li>• Where payments made in respect of grant claims differed from the invoice amounts, there was a lack of adequate information on file to explain the reasons for the differences. <i>Risk – lack of an audit trail.</i></li> <li>• The arrangements in place for the recording and reporting of overpayments and irregularities require review. <i>Risk – failure to comply with relevant regulations and guidance.</i></li> </ul>	<p>6</p>

Audit	Key Findings	Number of Recommendations
<p><b>Adult Social Care – Direct Payments</b></p>	<p>The main objective of the audit was to ensure that internal controls in place for Direct Payments were adequate.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The monitoring arrangements in place for Direct Payments are considered inadequate – there was a failure to ensure that clients completed and returned Financial Statements of Expenditure on a four-weekly basis. <i>Risk – errors and irregularities may remain undetected.</i></li> <li>• There was a lack of checks being undertaken on financial information provided by clients. <i>Risk – Direct Payments may not be used for their intended purpose.</i></li> <li>• The Frameworki system is not currently being used to its full potential – although the system has the facility to automatically process Direct Payments, payments are currently being manually calculated and recorded on a spreadsheet. <i>Risk – errors and irregularities may occur.</i></li> <li>• There is a lack of checking procedures in place to ensure that Direct Payments made to clients are accurate and complete – in a number of cases examined payments were incorrectly calculated following changes to care packages. <i>Risk – errors and irregularities may occur and remain undetected.</i></li> <li>• The Council does not have a formal policy in place covering the management and administration of Direct Payments. <i>Risk – failure to achieve desired outcomes.</i></li> <li>• The separation of duties in place for administering the financial aspects of Direct Payments are insufficiently clear with a number of key activities being undertaken by the same member of staff. <i>Risk – errors and irregularities may remain undetected.</i></li> </ul>	<p>9</p>

Audit	Key Findings	Number of Recommendations
<b>Residential Home – Young People</b>	<p>The main objective of the audit was to review the financial and budgetary controls operating within Pathway Residential Unit for Young People.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The procedures in place for the use of purchase cards require review. <i>Risk – lack of effective procedures may lead to misuse of purchase cards.</i></li> <li>• There was a lack of monitoring by Management to ensure that all purchase card transactions were valid. In certain cases we found that purchase cards had been used for personal purchases. <i>Risk – inappropriate expenditure may occur.</i></li> <li>• Purchase cards were being used to purchase goods, where the Council already had contracted suppliers in place. <i>Risk – failure to comply with purchase card procedures.</i></li> <li>• In a number of cases, breaches in purchase card security were found – cardholders were sharing their purchase cards and pin numbers with other members of staff. <i>Risk – irregularities and misuse may occur.</i></li> <li>• There was a lack of clear audit trail to support purchase card and petty cash transactions – in some instances no receipts had been provided for the purchases made. <i>Risk – errors or irregularities may occur.</i></li> <li>• An up to date asset register was not maintained – details of additions and disposals of assets were not being recorded. <i>Risk – assets may be misappropriated.</i></li> <li>• There was a lack of adequate segregation of duties – the member of staff responsible for operating the petty cash imprest account was also a cheque signatory. <i>Risk – errors or irregularities may occur.</i></li> <li>• We found that some items of equipment, which had been purchased for significant sums, were not being utilised by the Unit. <i>Risk – inefficient use of resources.</i></li> </ul>	<p>16</p>

Audit	Key Findings	Number of Recommendations
<p><b>Free School Meals and Clothing Grants</b></p>	<p>The main objective of the audit was to review the internal controls surrounding the administration of free school meals and clothing grants.</p> <p><b>Areas with Scope for Improvement</b></p> <ul style="list-style-type: none"> <li>• The Council's free school meals and clothing grants application form requires review to ensure that it accurately reflects legislation and that the declaration completed by applicants is comprehensive. <i>Risk – non-compliance with legislation.</i></li> <li>• Information provided on the Council's website in respect of free school meals and clothing grants is out of date. <i>Risk – information provided may be inaccurate.</i></li> <li>• There was a lack of segregation of duties in respect of the processing and authorising of manual BACS payments for clothing grants. <i>Risk – errors and irregularities may occur and remain undetected.</i></li> <li>• The arrangements in place for the award of discretionary clothing grants require review. <i>Risk – inappropriate payments may be made.</i></li> <li>• Regular reconciliations were not being undertaken between the Council's General Ledger and the SEEMIS system used by Education for administering free school meals and clothing grants. <i>Risk – errors and irregularities may occur and remain undetected.</i></li> </ul>	<p>10</p>
<p><b>Review of Previous Years' Work</b></p>	<p>The outcome of previous years' work was reviewed to ensure that recommendations had been actioned as agreed by Management. Follow-up audits were carried out on:</p> <p>PPP Contract Monitoring  Software Licensing  Payroll Overtime  Community Care – Charging for Services Provided</p>	<p>N/A</p>

Audit	Key Findings	Number of Recommendations
<p><b>How Good Is Our Council (HGIOC)</b></p>	<p>We reviewed the Council's self-evaluation framework 'How Good is Our Council' (HGIOC), which was introduced to promote performance improvement across all services.</p> <p><b>Areas with Scope for Improvement</b></p> <p>Our review identified areas with scope for improvement including the failure by one Service area to undertake the self-evaluation exercise, a lack of consistency in the level at which self-evaluation was undertaken, delays in completing self-evaluation templates, the failure to involve a cross section of staff in gathering evidence and providing judgements, a lack of sufficient evidence in some areas to support the robustness of the evaluation process and the failure to fully complete the self-evaluation template.</p>	<p>16</p>
<p><b>Miscellaneous Grants</b></p>	<p>For grants awarded to the Council, a statement of compliance with grant conditions was provided to the Scottish Government.</p>	<p>N/A</p>
<p><b>National Fraud Initiative (NFI)</b></p>	<p>Internal Audit participates in the National Fraud Initiative, which is organised by the Audit Commission and coordinated for Scottish Local Authorities by Audit Scotland. The initiative seeks to identify potential frauds or overpayments by matching data held both within the Council and that held by other bodies.</p> <p>The NFI work carried out by Internal Audit in 2011/12 resulted in the recovery of over £16,000 of overpayments.</p>	<p>N/A</p>
<p><b>Investigations</b></p>	<p>As part of the audit plan work was also undertaken in respect of fraud and irregularity investigations.</p>	<p>N/A</p>