



CHIEF INTERNAL AUDITOR'S ANNUAL REPORT AND OPINION 2010 - 2011

Prepared by:	Neil Pitman, Chief Internal Auditor
Date:	31 st May 2011

1. INTERNAL CONTROL AND THE ROLE OF INTERNAL AUDIT

- 1.1. Under the Accounts and Audit (Amendment) (England) Regulations 2006¹, the Council was required to 'maintain an adequate and effective system of internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control'. The standards for 'proper practices' for internal audit are laid down in the Chartered Institute of Public Finance and Accountancy's *Code of practice for internal audit in Local Government in the United Kingdom (2006)* ["CIPFA Code"].
- 1.2. Internal audit is an assurance function that provides an independent and objective opinion to the Council on the control environment, comprising risk management, internal control and governance, by evaluating its effectiveness in achieving the Council's objectives.
- 1.3. It is a management responsibility to establish and maintain internal control systems and to ensure that resources are properly applied, risk is appropriately managed and outcomes achieved.

2. INTERNAL AUDIT OPINION

- 2.1. The purpose of this report is to give my opinion as Chief Internal Auditor for Southampton City Council on the adequacy and effectiveness of the Council's framework of risk management, internal control and governance from the work internal audit have carried out for the year ending 31st March 2011.
- 2.2. The report and opinion provides as a key contributor to the Annual Governance Statement, however, remains only one element of the wider assurance process.
- 2.3. In giving this opinion, it should be noted that assurance can never be absolute and therefore, only reasonable assurance can be provided that there are no major weaknesses in the processes reviewed. In assessing the level of assurance to be given, I have based my opinion on:
 - written reports on all internal audit work completed during the course of the year;
 - results of any follow up exercises undertaken in respect of previous years' internal audit work;
 - the results of work of other review bodies where appropriate;
 - the extent of resources available to deliver the internal audit work;
 - the quality and performance of the internal audit service and the extent of compliance with the CIPFA Code;
 - any limitations which may have been placed on the scope or operation of internal audit; and
 - the proportion of Southampton City Council's audit need that has been covered within the period.

¹ Accounts and Audit (England) Regulations 2011 effective 31 March 2011 state 'a relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control'

Opinion

I am satisfied that sufficient assurance work has been carried out to allow me to form a reasonable conclusion on the adequacy and effectiveness of Southampton City Council's internal control environment.

In my opinion, Southampton City Council's framework of governance, risk management and management control is basically sound, however, some weaknesses have been identified through our work or we have found evidence that the framework may not be consistently applied. Where weaknesses have been identified through internal audit review, we have worked with management to agree appropriate corrective actions and a timescale for improvement.

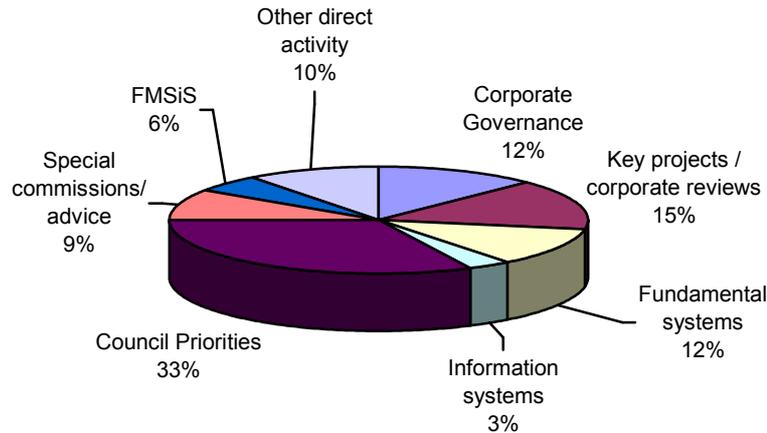
The system of internal control will be strengthened by the work that is being carried out to improve and embed general compliance with corporate policy, strengthened operation of the heating charges account and the transfer of Thornhill Plus You to Plus You Limited.

This overall audit opinion should be read in conjunction with the key issues set out in the following paragraphs.

3. INTERNAL AUDIT COVERAGE AND OUTPUT

- 3.1. The *Strategic internal audit plan* details a rolling, three-year programme of audits, designed to support preparation of the *Annual governance statement* and encompasses the following core principles:
- focus on the Council's defined purpose and outcomes;
 - effective performance in clearly defined functions and roles;
 - promoting values that underpin good governance through upholding high standards of conduct and behaviour;
 - taking informed and transparent decisions within a framework of controls and managing risk;
 - developing the capacity and capability of members and officers to be effective; and
 - engaging stakeholders to ensure robust public accountability.
- 3.2. The 2010 -11 internal audit plan, approved by the Audit Committee 18 March 2010 (revised 3 February 2011) was informed by the corporate risk register and performance framework, supplemented with internal audit's own assessment of risk and materiality.
- 3.3. Internal audit delivered 1215 audit days across 79 review areas over the course of the year ending 31st March 2011.

Analysis of audit days by review type



3.4. The revised 2010-11 internal audit plan has been delivered with the following exceptions:

- At the time of this report, the following reviews are work in progress:
 - Contract management
 - Procurement
 - Cash collection and banking
 - Joint Commissioning Standards

I do not consider these exceptions to have an adverse impact on the delivery of my overall opinion for the period.

3.5. We have published an opinion in final or draft reports (where we are concluding discussions with management in the agreement of action plans) in respect of 55 reviews completed during the year².

3.6. Where our work identified risks that we considered fell outside the parameters acceptable to the Council, we agreed appropriate corrective actions and a timescale for improvement with the responsible managers.

3.7. We actively monitor progress against the agreed action plans until we receive confirmation from management that all agreed actions have been completed or as happens in time of significant change, superseded.

² 20 reviews did not culminate in a formal opinion, these include grant certification work, walkthrough tests, National Fraud Initiative, fraud and irregularity advice

3.8. The opinion assigned to each internal audit review on issue of the report is defined as follows:

Opinion	Framework of governance, risk management and management control	Number of published opinions in this category (2010-11)	Number of open audits with opinions in category at year end
Substantial assurance	A sound framework in place that is operating effectively. Some immaterial evidence of inconsistent application.	29	10
Adequate assurance	Basically a sound framework in place but with repeated evidence of inconsistent application.	16	3
Limited assurance	Critical weakness (es) identified within the framework or significant evidence of inconsistent application.	7	3
No assurance	Fundamental weaknesses have been identified or the framework is ineffective or absent.	3	-

4. SIGNIFICANT ISSUES ARISING

4.1. Heating Charges – No assurance

In response to local government elector queries raised with the District Auditor, internal audit have supported the Audit Commission in reviewing the way the Council operates its heating charges account

Review highlighted some significant weakness in internal control. Testing carried out identified inadequate controls in place to govern changes made to the record of electricity meters. Additionally the Council had poorly managed commissioned surveys of electricity meters and failed to set up an accurate meter record.

A number of actions have since been addressed or are being developed to rectify key control weaknesses identified:

- Review of the record of electricity meters and implementation of a more effective database and system of control;
- Confirmation of the designation of electricity meters; and
- Establishment of the extent of the errors in meter records and assessment of the impact on past charges to tenants and leaseholders.

4.2. Compliance with corporate policy – No assurance (x2)

Following a succession of internal audit reviews during 2010–11, commonalities in control weaknesses were identified exposing both individual service areas and the Council to the risk of loss and / or failure to comply with corporate policy

Common failings were identified with regard compliance with:

- Contract procedure rules;
- Declarations of interest; and
- Financial procedure rules

In response internal audit have compiled a 'health check' for completion by all relevant service managers to enable a self assessment to be carried out against the recurring areas of concern.

The checklist is intended as a self-assessment to assist service departments evaluate local levels of internal control and should represent an honest critique of arrangements in place.

On completion internal audit will review completed assessments to ensure appropriate actions are in place to mitigate potential control weaknesses.

4.3. Thornhill Plus You – Limited assurance³

An internal audit review of Thornhill Plus You (TPY) highlighted a high level of risk in respect of grant monies being recouped by the Department for Communities and Local Government (CLG) as a result of unallocated funds and project underspends. Concerns were also raised with regard the lack of transparency in the authorisation and movement of funds between projects exposing a further risk of claw back from the CLG.

The TPY programme ended in March 2011. To continue the improvements identified during the life of the programme a charitable company was created, by TPY members, 'Plus You Limited' (PYL) to deliver the future needs of the area. PYL will take over the ownership of TPY assets and will generate income to re-invest into projects when the funding ceases.

At the time of the audit there was no action plan in respect of close down procedures for TPY to hand over to PYL or clear distinction between assets belonging to PYL or the Council. Additionally the succession strategy was pending approval both locally and by the CLG.

A significant resource has since been invested in ensuring an effective succession strategy is in place and a further internal audit review will be undertaken during 2011/12 to assess residual accountabilities for the Council following transfer to PYL.

³ Highlighted as a significant issue due to potential corporate connotations. The remaining 'Limited' assurance reviews relate primarily to establishment visits with key issues mirroring those detailed in section 4.2

5. ADVICE TO MANAGEMENT

- 5.1. During the year internal audit has worked with management on a consultancy/advisory basis on a number of projects, including:
- Putting People First (In Control)
 - Partnership governance and reviews
 - Investigations into fraud, corruption and improper practice

6. ANTI FRAUD AND CORRUPTION

- 6.1. Within the year we have conformed to the National Fraud Initiative (NFI) timetable to submit datasets relevant for the period and received 11,348 data matches which are currently under review.
- 6.2. In addition, we have assessed and where appropriate, advised, investigated or supported the investigation of a number of allegations of fraud, corruption or improper practice. A number of these cases were allegations made under the Duty to Act (“Whistleblowing”) Policy. Evidence, advice and guidance have been passed to management to pursue internal disciplinary processes or to the Police to pursue criminal investigation where appropriate.

7. INTERNAL AUDIT PERFORMANCE

<i>Annual performance indicators 2010-11</i>		
Aspect of service	Target output or performance measure	Actual output or performance
Cost and quality of input	Service costs are within budget	Outturn report showed under spend resulting from efficiency proposals
	Direct audit days account for 65% of total time available	Direct audit days accounted for 73% of total time available
Productivity and process efficiency	A minimum of 90% of the annual plan is delivered	95% of the revised annual plan has been delivered
	100% of high risk audits are delivered	100% of high risk audits have been delivered.
	Draft reports are issued within 10 days of completion of fieldwork	83 % of draft reports are issued within 10 days of completion of fieldwork

Annual performance indicators 2010-11		
Aspect of service	Aspect of service	Aspect of service
Productivity and process efficiency	Client response received to draft audit reports within 10 days of issue	*Estimated 70% of client responses are received to draft audit reports within 10 days of issue
	Final reports are issued within 10 days after agreement with client	75% of final reports are issued within 10 days after agreement with client
Quality of output	80% of clients are satisfied with the service delivered	A quality survey conducted during 2010 reported that 83.3% of respondents rated the internal audit service as good, very good or excellent.
	External audit place reliance on work of internal audit	External audit placed reliance on the work of internal audit during 2010/11
Compliance with professional standards	CIPFA Code of practice for internal audit in local government (2006) is complied with	Compliant
Outcomes and degree of influence	90% of agreed high priority actions are implemented within agreed timescale	*Estimated 75% of agreed high priority actions are implemented within agreed timescale

* Currently configuring audit management software to provide accurate measures in this performance area.

7.2 Internal Audit Resources

The resource profile has changed significantly during 2010 -11. On 1 November 2010 Southampton City Council and Hampshire County Council agreed to a collaborative approach for the provision of a shared internal audit service. The agreement introduces a shared Chief Internal Auditor role across both authorities

This initiative provides further scope to develop the shared service approach to best utilise areas of expertise across both authorities and generate economies of scale through training and development.

The service operated at a 15% shortfall in planned FTE staff over a six month period. Supplementary resources were bought in from South Coast Audit for the delivery of IT reviews within the 2010-11 internal audit plan.

7.3 Quality control

Our aim is to provide a service that remains responsive to the needs of the Council and maintains consistently high standards. This was achieved in 2010-11 through the following internal processes:

- Compliance with CIPFA Code of practice for internal audit in local government (2006);
- ongoing liaison and communication with the management to ascertain the risk management, control and governance arrangements, key to corporate success;
- ongoing development of a constructive working relationship with the Audit Commission to ensure development of a cooperative assurance approach;
- a tailored audit approach using a defined methodology and assignment control documentation;
- the review and quality control of all internal audit work by professional qualified senior staff members.

8. ACKNOWLEDGEMENT

- 8.1. I would like to take this opportunity to thank all those staff throughout Southampton City Council with whom we have made contact in the year. Our relationship has been positive and management were responsive to the comments we made both informally and through our formal reporting.

Neil Pitman
Chief Internal Auditor
31st May 2011