

Agenda Item No: 8 **Report No:** 81/17

Report Title: Annual Report on the Council's Systems of Internal Control 2016/17

Report To: Audit and Standards Committee **Date:** 19 June 2017

Ward(s) Affected: All

Report By: Head of Audit and Counter Fraud

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Purpose of Report:

To inform Councillors on the adequacy and effectiveness of the Council's systems of internal control for 2016/17.

Officers Recommendation(s):

- 1** To receive the annual report by the Head of Audit and Counter Fraud (HACF, previously HAFP).
 - 2** To note that the overall standards of internal control were satisfactory during 2016/17 (as shown in Section 3).
 - 3** To note that the satisfactory opinion on internal control is taken forward into the draft Annual Governance Statement (AGS) 2017 that is presented separately to this meeting of the Committee. The approved AGS is to be included with the Statement of Accounts 2016/17 that will be published in September 2017 (see Section 7).
 - 4** To report to the Cabinet on the Council's systems of internal control.
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Reasons for Recommendations

- 1** The remit of the Audit and Standards Committee includes a duty to keep under review the probity and effectiveness of internal controls, both financial and operational, including the Council's arrangements for identifying and managing risk. There is a further duty to consider the annual report by the HACF, and to report annually to the Cabinet on the adequacy and effectiveness of internal controls within the Council.

2 Background

- 2.1** The Chartered Institute of Public Finance and Accountancy (CIPFA) has, with the other governing bodies that set auditing standards for the various parts of the public sector, adopted a common set of Public Sector Internal Audit Standards (PSIAS) that were applied from 1 April 2013. The PSIAS have been updated, with new standards published in April 2016. The impact of the new standards was reported to the September 2016 meeting of the Committee.
- 2.2** The requirements of the PSIAS overlap with those of the Accounts and Audit Regulations, which require that there be an annual report on the internal control environment. This requirement has been met by an internal study carried out by HACF, with the results independently reviewed by the Deputy Chief Executive and now reported to the Audit and Standards Committee.

3 Opinion of the Head of Audit and Counter Fraud on the Internal Control Environment at Lewes District Council for the year ended 31 March 2017

- 3.1** The overall standards of internal control are satisfactory. This opinion is based on the work of Internal Audit, other internal reviews and external assurance bodies, and the Council's work on risk management. The risk management process has identified that most risks are mitigated by the effective operation of controls or other measures. Whilst recommendations have been made to improve procedures and controls in some areas, there were no instances in which internal control problems created significant risks for Council activities or services. In most cases managers have addressed the control issues since the respective audits, and within those recommendations not yet implemented there are no issues that create significant risks for the Council.
- 3.2** This report outlines the work on which the above opinion is based, including high level summaries of the external review processes and their results.

4 Internal Audit Work 2016/17

- 4.1** The work carried out by Internal Audit has been sufficient to enable HACF to issue an unqualified opinion on the overall adequacy and effectiveness of the Council's control environment. The work carried out by Internal Audit is summarised in the Annual Report on Internal Audit Performance and Effectiveness 2016/17 that is presented separately to this meeting of the Committee.

5 Risk Management

- 5.1** Cabinet approved the Risk Management Strategy in September 2003. Since then risk management at the Council has been developed via a series of action plans, with the result that all the elements of the risk management framework set out in the strategy are in place and are maintained at best practice standards.
- 5.2** The Annual Report on Risk Management was presented to the June 2016 of the Committee, and subsequently to the Cabinet. The Committee receives updates on risk management at every meeting. The reports during 2016/17 have noted that most risks are mitigated by the effective operation of controls or other

measures. However, there are some risks that are beyond its control, for example a major incident, a 'flu' pandemic, a downturn in the national economy or a major change in government policy or legislation. The Council has sound planning and response measures to mitigate the effects of such events, and continues to monitor risks and the effectiveness of controls.

- 5.3** In response to reductions in Government funding for local authorities, the Council has been making significant savings each year in its General Fund budget (which covers all services except the management and maintenance of Council owned homes) since 2011/12.
- 5.4** The General Fund budget for 2016/17 included a savings target of £0.685m including £0.4m to be generated from the JTP with EBC, of which Phase One (creating a single team of leaders and managers across LDC, EBC and Eastbourne Homes) is the main driver. This target is expected to be achieved, although because the new JTP Phase One management restructure will not be fully completed until June 2017, some of the savings will be deferred into 2017/18.
- 5.5** General Fund savings continue to be required over the next four years, with net expenditure to reduce by £2.2m from £13.2m to £11.0m by 2020/21 - £0.9m is to be generated from the remaining elements of the JTP. In 2017/18, the JTP is required to deliver General Fund savings of £0.3m.
- 5.6** There are also pressures to reduce spending on the management and maintenance of Council owned (HRA) housing. Starting in 2016/17, the Government has required all housing authorities to reduce tenants' rents by a 1% in cash terms in each of the four years through to 2019/20. As a result, by 2019/20, total annual rent income will have fallen by £0.6m to £14.4m. This means that savings of £2.2m will be needed to offset the expected impact of inflation on expenditure budgets over that period. A share of the JTP savings will pass through to the HRA.
- 5.7** The system of management assurance (see Section 6) has confirmed the operation of controls and the absence of significant control issues during the period of the savings programme so far. HACF will monitor the impact on the control environment of the JTP, and will liaise with managers who are working to ensure that the control environment keeps pace with these changes. This comment is reflected in the draft Annual Governance Statement (AGS) 2017.
- 5.8** The overall satisfactory situation in respect of risk management has helped to inform the opinion on the internal control environment.

6 System of Management Assurance

- 6.1** The Council operates a management assurance framework. The framework has enabled senior officers to confirm the proper operation of internal controls, including compliance with the Constitution, in those services for which they were responsible in 2016/17. As part of this process all members of the Corporate Management Team (CMT) are required to consider whether there were any significant governance issues during 2016/17. At its meeting on 30

May 2017 CMT confirmed that there were no significant governance issues to report.

7 Corporate Governance

- 7.1** In March 2016 the HACF in consultation with key officers, reviewed the Council's Local Code of Corporate Governance, and concluded that the arrangements remain satisfactory and fit for purpose. These results were reported to the March 2016 meeting of the Committee.
- 7.2** The Council is required to produce an Annual Governance Statement (AGS), which outlines the main elements of the Council's governance arrangements and the results of the annual review of the governance framework including the system of internal control. The draft AGS for 2017 is reported separately to this meeting of the Committee.

8 External assurance

- 8.1** The Government relies on external auditors to periodically review the work of the Council to make sure it is meeting its statutory obligations and performing well in its services. The results of these external reviews have helped inform the opinion on the internal control environment. The recent results are summarised below.
- 8.2** Annual Audit Letter for 2015/16 (October 2016) – This report summarised the key issues from the work carried out by BDO during the year, and was presented to the November 2016 meeting of the Committee. The key issues were:
- BDO issued an unqualified true and fair opinion on the financial statements for the period ended 31 March 2016.
 - BDO identified a number of misstatements on the Cash Flow Statement and in the classification of short term investments. These were corrected before completion of the financial statements.
 - BDO were satisfied that the Narrative Report, which local authorities include in the Statement of Accounts to offer interested parties guidance on the most significant matters, was consistent with the financial statements.
 - BDO did not identify any significant deficiencies in the Council's framework of internal controls, but did report on areas where improvements in controls could be made including declarations of related party transactions, the documentation of Council Tax discounts, and access to some IT systems.
 - BDO were satisfied that the Annual Governance Statement (AGS) was not misleading or inconsistent with other information they were aware of from their audit work.
 - BDO issued an unqualified conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources.
 - BDO found that the Council has adequate arrangements for budget setting and budget monitoring, and the Council has identified sufficient savings over the next four years to balance its budget.

- BDO noted that many of the savings will arise from the Joint Transformation Programme with EBC, and BDO were satisfied that there are effective governance arrangements in place to oversee delivery of the project.
- BDO noted that the Council's Whole of Government Accounts (WGA) submission is below the threshold for further work other than to submit the WGA Assurance Statement. This was submitted on 7 October 2016 ahead of national deadline.
- BDO reported that the review of grant claims and returns for 2015/16 is in progress, and the results will be reported on completion.
- BDO reviewed the governance arrangements for Council's New Homes Project, and made a number of recommendations for improvement that should be applied to future projects.

8.3 Grant Claims and Returns Certification for year ended 31 March 2015 (April 2016). The report was presented to the June 2016 meeting of the Committee. The key points were:

- The audit identified a high level of errors within the cases tested, which required a significant amount of extra testing by BDO and the Council. No amendments were made to the final claim submitted to DWP.
- The main errors were in the administration of benefits involving non-HRA rent rebates and rent allowances. There were a small number of cases of incorrect classification of expenditure as non-HRA, when the expenditure should have been classified as HRA rent rebates.
- The audit identified deficiencies in the Council's systems and controls around the identification of prior year uncashed payments, resulting in an under claim of £556.
- As a result of the errors found in administering benefits, BDO qualified the claim across all benefit expenditure types. The additional work required to be completed by the Council and BDO meant that the audited claim was submitted to DWP in March 2016, four months after the deadline date.
- The certification of the returns for the Pooling of Housing Capital Receipts was completed satisfactorily without amendment of certification. The main reported issue was the need for the Council to have in place appropriate plans to use retained receipts by certain milestone dates, otherwise the receipts must be paid to DCLG.

8.4 As was reported to the June 2016 meeting of the Committee, DWP made a marginal adjustment to the submitted claim which was agreed at a total value of approximately £35.8m.

8.5 The results of these external reviews have helped inform the opinion on the internal control environment.

9 Financial Appraisal

9.1 There are no additional financial implications arising from this report.

10 Sustainability Implications

- 10.1** I have not completed the Sustainability Implications Questionnaire as this report is exempt from the requirement because it is an internal monitoring report.

11 Risk Management Implications

- 11.1** The risk assessment shows that if the Audit and Standards Committee does not ensure proper oversight of the adequacy and effectiveness of the Council's systems of internal control there is a risk that a key aspect of the Council's control arrangements will not comply fully with best practice.

12 Equality Screening

- 12.1** I have given due regard to equalities issues and, as this is an internal monitoring report with no key decisions, screening for equalities is not required.

13 Background Papers

None.

14 Appendices

Appendix 1: Table of abbreviations.

APPENDIX A1

Table of abbreviations

AGS – Annual Governance Statement

BDO – BDO, the Council's external auditors. Formerly BDO Stoy Hayward

CIPFA – Chartered institute of Public Finance and Accounting

CMT – Corporate Management Team

EBC – Eastbourne Borough Council

HACF – Head of Audit and Counter Fraud

HAFP – Head of Audit, Fraud and Procurement

HRA – Housing Revenue Account. Refers to Council owned housing

ISO – International Organisation for Standardisation

IT – Information Technology

JTP – Joint Transformation Project

LDC – Lewes District Council

PSIAS – Public Sector Internal Audit Standards

WGA – Whole of Government Accounts