

Agenda Item No: 6 **Report No:** 47/14

Report Title: Interim Report on the Council's Systems of Internal Control 2013/14

Report To: Audit and Standards Committee **Date:** 17 March 2014

Ward(s) Affected: All

Report By: Head of Audit and Performance

Contact Officer

Name: David Heath

Post Title: Head of Audit and Performance

E-mail: David.Heath@lewes.gov.uk

Tel no: 01273 484157

Purpose of Report:

To inform Councillors on the adequacy and effectiveness of the Council's systems of internal control during the first eleven months of 2013/14, and to summarise the work on which this opinion is based.

Officers Recommendation(s):

- 1 To note that the overall standards of internal control were satisfactory during the first eleven months of 2013/14 (as shown in Section 3).

Reasons for Recommendations

- 1 The remit of the Audit and Standards Committee includes the duties to agree an Annual Audit Plan and keep it under review, and 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.

Information

2 Background

- 2.1 The Internal Audit function at Lewes previously operated in accordance with the Code of Practice for Internal Audit published by the Chartered Institute of Public Finance and Accountancy (CIPFA). 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 apply from 1 April 2013. The Head of Audit and Performance (HAP) advised the Audit and Standards Committee of the effect of the new standards at its March 2013 meeting.
- 2.2 The PSIAS 2013 specify the requirements for the reporting to the Audit and Standards Committee and senior management by HAP. These requirements are met via a series of reports, which include interim reports to each meeting of the

Committee. Each interim report includes a review of the work undertaken by Internal Audit compared to the annual programme, an opinion of HAP on the internal control, risk management and governance environment at the Council, together with any significant risk exposures and control issues, in the period since the beginning of the financial year. Each interim report contains an appendix that includes an outline of each of the final audit reports issued since the previous meeting of the Committee, and an appendix that outlines any significant recommendations that have not yet been implemented.

3 Internal Control Environment at Lewes District Council

3.1 The Annual Report on the Council's Systems of Internal Control for 2012/13 included the opinion of HAP that the overall standards of internal control are satisfactory. This opinion was based on the work of Internal Audit and the Council's external auditors, BDO, and the Council's work on risk management. In the eleven months since the start of the financial year there has been nothing to cause that opinion to change and there have been no instances in which internal control issues created significant risks for Council activities or services.

4 Internal Audit work 2013/14

4.1 This section of the report summarises the work undertaken by Internal Audit during the first eleven months of the year, compared to the annual plan that was agreed by the Audit and Standards Committee in March 2013.

4.2 Table 1 shows that a total of 686 audit days have been undertaken compared to 709 planned. The variance of 23 days is largely because of time spent by a team member in supporting the team's move to the Council's new IT systems and the departure of a part time member of the Internal Audit team. The team member has taken voluntary severance as part of the ongoing Council scheme and left on 6 February 2014. It is unlikely that audit days will be close to plan by the year end. The team member will not be replaced, and the Strategic Audit Plan for the period 2014/17 (reported separately to this Committee) is based on future staffing of the Internal Audit team being 3.2 FTE (compared to 3.8 FTE currently).

Table 1: Plan audit days compared to actual audit days for April to February 2014

Audit Area	Actual audit days for the year 2012/13	Plan audit days for the year 2013/14	Actual audit days to date	Pro rata plan audit days to date
Main Systems	289	245	232	
Central Systems	54	90	29	
Departmental Systems	128	155	175	
Performance and Management Scrutiny	68	74	39	
Computer Audit	20	60	7	
Environmental Audit	42	33	65	
Management Responsibilities/Unplanned Audits	128	117	139	
Total	729	774	686	709

Note: The 'Pro rata plan audit days to date' provides a broad guide to the resources required to carry out planned audits. The actual timing of the individual audits will depend on a variety of factors, including the workloads and other commitments in the departments to be audited.

4.3 *Main Systems:* The initial work was on completing the testing of the key financial systems in order to gain assurance on the adequacy of internal controls for the Annual Governance Statement (AGS) and to inform BDO's work on the Council's

accounts for 2012/13. The audit did not identify any significant control issues that would have an impact on the Council's main accounts, although it was necessary to highlight a recurring issue in the authorisation of purchase orders and invoices. A summary report was finally issued. The corresponding audit on the key financial systems for 2013/14 is underway. In a recent development agreed with BDO, this work now includes testing of the Fixed Assets and Council Tax Reduction Scheme systems for the first time.

- 4.4** The priority work with BDO to test the Council's subsidy claims for Benefits and NDR for 2012/13 is completed. The NDR claim was signed off and submitted by BDO without qualification.
- 4.5** The Internal Audit work on the Benefits subsidy claim identified errors in the processing of claims and, at the request of BDO, has again required significant additional testing to determine the extent and impact of the issues noted. The need for additional work on the subsidy claim has had an effect on the progress that has been possible on the audits within Central Systems and Computer Audit. The work on the subsidy claim was completed by the due date, and the claim was signed off and submitted by BDO.
- 4.6** BDO issued a letter of qualification that was supported by statements of the claim adjustments that would be required. The Head of Revenues and Benefits queried the outcome of the BDO audit and the DWP interpretation of the audit findings. The query was on the grounds that the extrapolations used by BDO to estimate the adjustments to the claim appeared, in some cases, incorrect. DWP and BDO have agreed the results of the re-assessment, and this has been confirmed in a written statement. A report on the Benefits subsidy claim work by Internal Audit has been finally issued.
- 4.7** *Central Systems:* Final reports were issued for the audits of Insurance and Electoral Registration and Elections. An audit of Communications is underway.
- 4.8** *Departmental Systems:* Final reports have been issued for the audits of Waste and Recycling, the Planning User Group, and Housing Management. Audits of Planning and Development Control and Cemeteries are at the draft report stage.
- 4.9** *Performance and Management Scrutiny:* Internal Audit has been represented on the Management Boards for the Agile Working and Food Waste projects to advise on internal control and quality assurance. The Agile Working and Food Waste projects have been completed and Internal Audit contributed to the end of project reviews. From May 2013, Internal Audit has been performing a quality assurance role on the joint Regeneration and Enterprise Project Board that is managing four regeneration projects. Information obtained from the audit of Economic Development (Departmental Systems) has been used to help with quality improvements in the four projects, and no separate audit report was issued. From January 2014 Internal Audit has been performing a quality assurance role on the project to develop the North Street Quarter of Lewes.
- 4.10** *Computer Audit:* Internal Audit completed the IT aspects of the testing of the main financial systems, and a report on the audit of IT Change Control was finally issued. Two unplanned audits on IT issues are summarised at 4.14.
- 4.11** *Environmental Audit:* During June 2013, Internal Audit examined the Council's annual EMAS statement prior to its submission to Lloyd's Register Quality Assurance (LRQA) verifier as part of the assessment process. The verifier

concluded that, with no significant issues to report, the Council continues to meet the requirements of the published standards and it was recommended that the Council's EMAS registration be confirmed. A final report was issued for the 2012/13 audit of EMAS: Waste and Recycling. The 2013/14 programme of EMAS audits has been completed, with final reports issued for the audits of EMAS: Management and Control, EMAS: Pollution Prevention and Control, and EMAS: Legal Compliance.

- 4.12** *Management Responsibilities/Unplanned Audits:* This category provides resources for the support for the Audit and Standards Committee, liaison with BDO, managing the Follow Up procedures, as well as for special projects or investigations.
- 4.13** Internal Audit has been coordinating the Council's work for the 2012/13 NFI data matching exercise which is run by the Audit Commission. The base data was forwarded to the Audit Commission in October 2012, and the results were returned to the Council in February 2013 for the investigation of reported matches. This investigation work is ongoing.
- 4.14** Internal Audit has reviewed the Health and Safety function at the Council at the request of the Chief Executive, and a final report has been issued. The completion of a review of the interfaces between key systems has been delayed in order to take account of the restructuring of the Council and a planned study to make business processes more efficient. A final report has been issued following an examination of the links between the Council and the Bank Automated Clearing System (BACS).
- 4.15** Internal Audit has completed the cyclical Equality Analysis report on the service. Some aspects of the planning and conduct of audits were reviewed for possible improvements, and this work was completed by the end of January 2014.

Follow up of Audit Recommendations

- 4.16** All audit recommendations are followed up to determine whether control issues noted by the original audits have been resolved. The early focus for follow up in 2013/14 was on confirming the implementation of the recommendations that were agreed in the previous year. The results of this work were reported to the June 2013 meeting of the Committee. There are no significant recommendations that are currently outstanding.

Quality Reviews/Customer Satisfaction Surveys/Performance Indicators (PIs)

- 4.17** The results of the Internal Audit quality reviews, customer satisfaction surveys and PIs for 2012/13 were reported to the June 2013 meeting of the Committee. The results enabled the HAP to report that the Internal Audit service at Lewes is fully effective, is subject to satisfactory management oversight, achieves its aims, and objectives, and operates in accordance with the Internal Audit Strategy as approved by the Committee.
- 4.18** Proposals for a revised set of PIs for Internal Audit were agreed at the September 2013 meeting of the Committee, and the new PIs formed the framework for the report on Internal Audit Benchmarking that was presented to the December 2013 meeting of the Committee.

Combatting Fraud and Corruption

National reporting

- 4.19** The Annual Report on the Council's work to combat Fraud and Corruption 2012/13 was presented to the September 2013 meeting of the Committee. The report advised that the numbers and values of the fraud cases at LDC had been submitted to the Audit Commission as part of the fraud and corruption survey that all Local Authorities are required to complete. The results of the national survey have been published in an Audit Commission annual report on fraud and corruption in local government called 'Protecting the Public Purse.'
- 4.20** The Audit Commission report 'Protecting the Public Purse' compares performance by differences types of local authority across a range of fraud types. The Head of Audit and Performance is examining the report to determine the scope for possible additional controls or preventative measures where these would be justified by the results of risk assessments.

Recent events

- 4.21** In December 2011, the Chair of the Audit and Standards Committee asked Internal Audit to confirm the correct operation of the controls over additions and amendments to suppliers' details in Agresso. From the audit work carried out Internal Audit obtained substantial assurance that the Council operated sufficient controls to prevent unauthorised amendments to suppliers' details being used to create improper payments. Nevertheless, additional controls were introduced including telephone calls to suppliers to confirm the validity of all requested changes.
- 4.22** In late November 2013, the Council's Payments Team received a written request to change the bank account details for one of the Council's key suppliers. The standard telephone call to the supplier confirmed that the requested change was invalid and represented an attempted fraud. No payments were made to the bogus bank account, and details of the attempted fraud were passed to the bank's Fraud Notification Team for investigation.

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 risk management process has identified 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. The overall satisfactory situation for risk management has helped to inform the opinion on the internal control environment.
- 5.3** In response to the Government's national deficit reduction plan, the Corporate Management Team (CMT) put in place a phased programme to make savings in the Council's budgets. The programme commenced in 2011/12 and has achieved each

of its annual savings targets including that for the current year 2013/14. The savings target for the next two years is £1.146m, with £596,000 in 2014/15 and £550,000 in the year after. The source of savings from this point forward will continue to come from structural change rather than incremental change. The savings target for 2014/15 will mainly derive from efficiencies in procurement and the new Agile Working environment. The HAP has reviewed with CMT the impact on the control environment of the savings achieved so far, and has obtained assurance that there has been no adverse effect on the operation of controls. This exercise will be ongoing while the programme of savings continues.

- 5.4** The Annual Report on Risk Management was presented to Cabinet at its July 2013 meeting. This report confirmed the strategic risks identified by CMT and the action plan for risk management for the year ahead.

6 System of management assurance

- 6.1** The Council operates a management assurance system, which 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 2012/13. A joint statement by the Chief Finance Officer (Section 151) and Monitoring Officer confirmed that there were no significant governance issues for the Council in 2012/13. Nothing has arisen in the first eleven months of the financial year to change these assessments.

7 Corporate governance

- 7.1** In June 2013, the HAP 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 June 2013 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 AGS for 2012/13 was reported to the September 2013 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. In February 2013, the Council external auditors PKF announced their merger with BDO and the operation of the new merged entity under the BDO brand. The results of the reviews by BDO have helped inform the opinion on the internal control environment. The recent results are summarised below.
- 8.2** Annual Audit Letter for 2012/13 (October 2013) – This report outlined the key findings from BDO's audit of 2012/13. The letter confirmed that:

- BDO issued an unqualified true and fair opinion on the financial statements for 2012/13.
- BDO identified one material misstatement in relation to the accounting for the value of additions to HRA Council dwellings. Appropriate amendments were made to the financial statements.
- Working with Internal Audit, BDO found one deficiency in internal controls involving the authorisation of purchase order requisitions and invoices.

Management has agreed to strengthen relevant internal controls and processes within the creditor payments system.

- BDO were satisfied that, in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources and therefore issued an unqualified value for money conclusion.
- BDO were satisfied that the Annual Governance Statement (AGS) was not inconsistent or misleading with other information they were aware of from the audit of the financial statements and complies with '*Delivering Good Governance in Local Government*' (CIPFA/Solace).
- BDO reported on the outcome of the audit of one grant claim and three government returns for the period ended 31 March 2012. The Housing and Council Tax Benefit subsidy claim (total value £41 million) was amended to correct errors, the overall effect being a reduction in subsidy of £902. BDO were unable to fully quantify other errors identified and included the facts in a qualification letter to the Government department (DWP).
- BDO completed a short form assurance review of the Council's Whole of Government Accounts (WGA) because the Council's WGA is below the threshold for a full assurance review. The review confirmed that the 'net funded pension balance' was consistent with the audited financial statements and the 'property, plant and equipment carrying amount at 31 March 2013' was not consistent with the audited financial statements because of the material audit adjustment.
- The Council's financial governance arrangements have continued to enable strong leadership on financial matters from the top of the organisation through the work of the Cabinet and Corporate Management Team.
- The process of financial planning is embedded across the Council through the annual budget setting process, and is supported by the medium term financial strategy which covers a three year period and is updated annually. The Council's revenue budget for 2013/14 requires additional savings of £757,000 and a contribution from the General Fund balance of £484,000 due to further reductions in the Council's grant settlement and spending pressures.

8.3 Grant Claims and Returns Certification for 2012/13 (February 2014) – This report is presented separately to this meeting of the Committee.

9 Financial Appraisal

9.1 There are no additional financial implications 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 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 key aspects of the Council's control arrangements may not comply with best practice.

12 Legal Implications

12.1 There are no legal implications arising from this report.

13 Equality Screening

13.1 This report is for information only and involves no key decisions. Therefore, screening for equality impacts is not required.

14 Background Papers

14.1 Annual Audit Plan 2013/14 that was presented to the Audit and Standards Committee on 18 March 2013. This can be found at :
<http://cmis.lewes.gov.uk/CmisWebPublic/Binary.ashx?Document=6156>

15 Appendices

15.1 Appendix A - Statement of Internal Audit work and key issues

15.2 There is no Log of Significant Outstanding Recommendations (normally Appendix B) for this report.

APPENDIX A

Statement of Internal Audit work and key issues

Audit report: EMAS: Legal Compliance

Date of final issue: 17 February 2014

Overall opinion:

From the work carried out for this review, Internal Audit has obtained partial assurance that there is a sound system for monitoring compliance with environmental legislation. Monitoring processes were put in place following the previous audit in 2011, but changes in the staffing and organisation of EMAS have meant that it has not been possible to maintain these arrangements as an effective monitoring system. This does not mean that the Council is not complying with environmental legislation, simply that there is not a straightforward process for confirming compliance. There are no recommendations

Main points:

- The detailed work on the updating of the legal registers was part of the EMAS administration, development and coordination role of the Environment and Energy Officer (EEO). The EEO left the Council in June 2012, and since then there has been no single person working in that role. At the November 2012 meeting of the Environmental Steering Group (ESG), it was decided that the responsibilities of the EEO post would be dispersed throughout the Council to departmental managers with the related activities included in the respective departmental Service Plans.
- From the work on this and other recent audits it would appear that the dispersal of roles and responsibilities has not been entirely effective. In particular, the dispersal made it difficult for the Council to be assured that environmental management activities were being adequately coordinated. One issue has been the lack of clarity as to who would be responsible for maintaining the legal registers and arranging for departmental managers to check compliance. As a result, there has been no one carrying out these tasks.
- The Council is to decide on the makeup of the new environmental management system and how it will be operated. It is not clear that a detailed monitoring system will be necessary in future, but Internal Audit will ensure that the issue of monitoring compliance with environmental legislation will be considered as part of these developments.

Audit report: Electoral Registration and Elections

Date of final issue: 20 February 2014

Overall opinion:

From the audit work carried out during this review Internal Audit has obtained full assurance that there is sound system of internal control covering electoral registration and elections. Controls are in place and compliance with the controls is good. The satisfactory situation means that there are no improvements that need to be made within the scope and objectives of the audit.

Main points:

- Registers of electors are compiled as required under the Representation of Peoples Acts, full and edited copies of the register are held in the appropriate

public places and are correctly circulated. Canvas forms were sent out in October 2013 and have been followed up, and can be matched with the electoral register.

- European and overseas citizens who are entitled to vote are recorded correctly, and effective measures have been introduced to encourage postal voting. Electoral expenses are paid and accounted for correctly. The May 2013 County Council Elections for the Lewes Electoral Division was managed without any problems or adverse comment by the Electoral Commission.
- The Council is prepared to implement the Government's initiative to change to individual voter registration in July 2014 which means identities can be cross referred with other government agencies for verification purposes.
- Issues outstanding from the last audit (September 2010) have been addressed. The Electoral Commissions report emanating from the May 2010 Parliamentary Elections regarding planning for elections has been considered and the Council has decided to maintain its established practices for the operation of polling stations. Appropriate training has been carried out for polling station staff.

Audit report: HB Subsidy Claim 2012/13

Date of final issue: 3 March 2014

Overall opinion:

From the audit work carried out during this review Internal Audit has obtained substantial assurance that there is a sound system of internal control covering the processing of benefit applications and the accounting for benefit payments. Controls are in place and, on the whole, compliance with controls is reasonable. The errors noted in the processing of applications indicate that there is scope to strengthen the way some procedures and controls are operated, but the values of the errors are mainly very low. The report includes one recommendation.

Main points:

- The value of the subsidy claim is approximately £43 million.
- The standards set by DWP and the Audit Commission for the conduct of testing and the interpretation of errors are very strict. Despite the low value of the errors noted, the incidence of errors in the initial and additional testing required BDO to issue a qualification letter on 29 November 2013. The BDO qualification letter was supported by statements of the test results and error rates for the different classes of benefit claims, from which were estimated the claim adjustments that would be required.
- The Head of Revenues and Benefits undertook a detailed re-appraisal of the BDO results. The re-appraisal queried the BDO calculation of the adjustments to the claim on the grounds that the use of the error rates from the test samples in extrapolating the outcome for whole populations of claims appeared, in some cases, incorrect. After consideration, the DWP and BDO have accepted the detailed case presented by the Head of Revenues and Benefits, and have agreed the revised adjustments. The final outcome is that the subsidy claim is to be adjusted by approximately £4,000.

Audit report: BACS Payments and Receipts

Date of final issue: 3 March 2014

Overall opinion:

The Head of IT Services had contacted Internal Audit to request a review of an issue that had become apparent during the winter holiday that spanned December 2012/January 2013. The issue had the potential to delay the processing of priority BACS transactions at the beginning of the month, but it had been resolved in time.

The review has provided Internal Audit with substantial assurance that there is a sound system of internal control covering BACS Payments and Receipts. Procedures and controls are in place, and there is satisfactory compliance. There are no recommendations in the report.

Main points:

- The issue had arisen from an upgrade in the Albany BACS system and changes in system permissions that were needed to reflect staff changes within IT Services – these two sets of changes were not processed fully, and prevented the LDC link to the BACS system working correctly. The issue was investigated and resolved as an emergency by IT Services, and the direct debit transactions due at the beginning of January 2013 were collected on the correct date.
- Further scheduled upgrades to the system have been managed successfully, and there has been no repeat of the processing problems that triggered the investigation.