

**Agenda Item No:** 6 **Report No:** 11/15

**Report Title:** Interim Report on the Council's Systems of Internal Control 2014/15

**Report To:** Audit and Standards Committee **Date:** 26 January 2015

**Ward(s) Affected:** All

**Report By:** Head of Audit and Performance

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### **Purpose of Report:**

To inform Councillors on the adequacy and effectiveness of the Council's systems of internal control during the first nine months of 2014/15, 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 nine months of 2014/15 (see Section 3).
  - 2 To note the results of the planned review of the Audit Plan 2014/15 (see Section 7).
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### **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 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 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, including 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 will contain 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 2013/14 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 nine 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 2014/15

4.1 This section of the report summarises the work undertaken by Internal Audit during the first nine months of the year, compared to the annual plan that was agreed by the Audit and Standards Committee in March 2014. Further information on each of the audits completed since the previous meeting of the Committee is given at Appendix A.

4.2 Table 1 shows that a total of 523 audit days have been undertaken compared to 491 planned. The variance of 32 days is largely due to the investigation carried out by the HAP (see paragraph 4.13) that was not planned at the start of the year. It is estimated that the audit days will be closer to plan by the year end.

4.3 As was anticipated when the Audit Plan 2014/15 was prepared, the ongoing restructuring of the Council has necessitated a review of the plan. The significant additional work required for the Benefits subsidy claim (see 4.5) is another factor in the need to review the plan and reallocate resources. The results of this review are given at Section 7.

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

Audit Area	Actual audit days for the year 2013/14	Plan audit days for the year 2014/15	Actual audit days to date	Pro rata plan audit days to date
Main Systems	260	285	259	
Central Systems	31	65	21	
Departmental Systems	178	100	42	
Performance and Management Scrutiny	64	40	38	
Computer Audit	11	65	27	
Environmental Audit	65	-	-	
Management Responsibilities/Unplanned Audits	132	98	136	
Total	741	653	523	491

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.

4.4 *Main Systems:* The initial work was on completing the testing of the major 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 2013/14. The audit did not identify any significant control issues that

would have an impact on the Council's main accounts. A summary report has been finally issued.

- 4.5** The initial work on behalf of BDO to test the Council's subsidy claims for Benefits for 2013/14 was completed to plan. The work identified errors in the processing of claims and, at the request of BDO, this required additional testing to determine the extent and impact of the issues noted. During October 2014, BDO checks identified further issues that required additional testing, and this process of further check and testing has been ongoing. As a result, it was not possible to submit the claim by the due date of 31 November 2014. After further quality tests by BDO, the claim is expected to be signed off and submitted by the end of January 2015. As a result of the issues noted, BDO are likely to issue a letter of qualification. A summary report by Internal Audit on the Benefits subsidy claim work is at the draft stage.
- 4.6** It has not been necessary to carry out the anticipated work to verify the Council's subsidy claim for NDR. This follows a decision by DCLG and the Audit Commission that there need not be verification of the NDR claim return for 2013/14.
- 4.7** *Central Systems:* An initial outline study for the audit of Business Continuity Planning resulted in a summary report being issued to the Director of Corporate Services; an updated Business Continuity Plan for the Council's services was issued in December 2014. A final report has been issued for the audit of Safeguarding.
- 4.8** *Departmental Systems:* Final reports have been issued for the audits of Cemeteries and Planning and Development Control, and an audit of Building Control is at the draft report stage. An audit of Housing Management is at the planning stage. Internal Audit is reviewing selected aspects of the procedures for the maintenance and repair of Council housing.
- 4.9** *Performance and Management Scrutiny:* A final report was issued for the audit of Ethics. Internal Audit has been performing a quality assurance role for the Regeneration and Enterprise Project Board that is managing four regeneration projects, and for the project to develop the North Street Quarter of Lewes. Internal Audit is examining the internal control aspects of the project to develop new processes for the delivery of Council services.
- 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 Security has been finally issued.
- 4.11** *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.
- 4.12** Internal Audit has been coordinating the Council's preparations for the 2014/15 NFI data matching exercise which is run by the Audit Commission. The base data was forwarded to the Audit Commission in October 2014 and the investigation of any matches will begin in February 2015.
- 4.13** At the request of the Chief Executive, Internal Audit has investigated the relationship between the Council and Seaford and District Constitutional Club in respect of possible development opportunities at the site. A final summary report has been issued and was presented to the December 2014 meeting of the Committee.

## **5 Follow up of Audit Recommendations**

**5.1** 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 2014/15 was on confirming the implementation of the recommendations that had been agreed in the previous year. The results of this work were reported to the June 2014 meeting of the Committee.

## **6 Quality Reviews/Customer Satisfaction Surveys/Performance Indicators (PIs)**

**6.1** The results of the Internal Audit quality reviews, customer satisfaction surveys and PIs for 2013/14 were reported to the June 2014 meeting of the Audit and Standards 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 Audit and Standards Committee.

**6.2** Proposals for a revised set of PIs for Internal Audit were agreed at the September 2013 meeting of the Committee. The new PIs formed the framework for the report on Internal Audit Benchmarking that was presented to the December 2013 meeting of the Committee, and the corresponding results for 2013/14 were reported to the September 2014 meeting of the Committee.

## **7 Review of 2014/15 Audit Plan**

**7.1** As part of the report to the March 2014 meeting of the Committee that detailed the Strategic Audit Plan, the HAP advised that there would be a six month review of the Audit Plan for 2014/15 to assess whether any significant changes are necessary in response to the ongoing restructuring of the Council.

**7.2** That review has taken place at the nine month stage, and the results of the review are now presented to the Committee. The review was held back to take account of a range of issues, in particular the ongoing restructuring and the impact of the significant extra work on the Benefits subsidy claim with BDO. The HAP plans the following adaptations to the programme of work in the Audit Plan for 2014/15.

- The issue of the updated Business Continuity Plan in December 2014 means that further audit work is not necessary during 2014/15. The next audit of this subject will be scheduled for a future date in the audit cycle.
- The audit of Communications that was begun in 2013/14 was halted in agreement with the Director of Business Strategy and Development in recognition of the major restructuring that was taking place in the department. The restructuring has been ongoing during 2014/15 and further audit work is not yet appropriate. The next audit of this subject will be scheduled for a future date in the audit cycle.
- The audit of Estates Management was halted to enable resources to be directed to the investigation requested by the Chief Executive. A summary of key conclusions on Estates Management is being prepared to inform the ongoing restructuring of the Facilities function. No further work is planned in 2014/15 and the next audit of this subject will be scheduled for a future date in the audit cycle.
- The audit of Trade Waste reached the fieldwork stage before being suspended because resources had to be re-assigned to the completion of the work on the HB subsidy claim. There is now no time to reschedule this audit in 2014/15 because of higher priority work on the key financial systems, and the audit of Trade Waste will be a priority task in the programme of audits for early 2015/16.

- The planned audit of Internet/Intranet has been postponed because of the ongoing work on the redesign of the Council's website. The next audit of this subject will be scheduled for a future date in the audit cycle.

Other audits in the programme for 2014/15 that are planned or underway will continue to a normal conclusion.

## **8 Combatting Fraud and Corruption**

### **National reporting**

- 8.1** The Annual Report on the Council's work to combat Fraud and Corruption 2013/14 was presented to the September 2014 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 will be published in an Audit Commission annual report on fraud and corruption in local government called 'Protecting the Public Purse.'
- 8.2** The Audit Commission report 'Protecting the Public Purse' for 2012/13 compared performance by differences types of local authority across a range of fraud types. The HAP has been examining the report to determine the scope for possible additional controls or preventative measures where these would be justified. The major outcomes of this study are outlined below.

### **Local developments**

- 8.3** As part of the Council's response to the Audit Commission report 'Protecting the Public Purse' for 2012/13, Internal Audit and Housing Services are now represented on the Sussex Tenancy Fraud Forum (TFF). TFF is a body that enables information sharing and joint initiatives with neighbouring authorities in both East and West Sussex to combat the various aspects of tenancy fraud.
- 8.4** There had been some uncertainty over the future of the Benefit Fraud Investigations Team. CMT agreed a business case for the Investigations Team to work as part of Internal Audit from 1 November 2014. The team is now working on the prevention and detection of fraud across additional areas of Council services including tenancy fraud and business rates (NDR) fraud. The team will maintain its membership of the East Sussex Fraud Officers Group (ESFOG), a body that enables information sharing and joint initiatives with neighbouring authorities on a wide range of counter fraud work.
- 8.5** In response to offers of funding from DCLG for counter fraud initiatives, a sub group of six authorities within ESFOG submitted a successful funding bid. DCLG award the group £365,000 for the development of a 'Hub' approach to coordinating new anti-fraud initiatives across East Sussex. The Hub will be managed by officers at Eastbourne BC with input from ESFOG partners, and the initial stages will see a programme of standardised training and planning, and the introduction of a case management system. Work on cases in the separate authorities will take priority until there is a fully coordinated Hub joint exercise.

### **Investigations Team**

- 8.6** As was advised to the December 2014 meeting of the Committee, reports on the Council's Systems of Internal Control will include a new section dealing with the work of the Investigations Team. This is the first of these sections.

- 8.7** Since 1 November 2014, the work on developing the team's approach to counter tenancy fraud has included attendance at the national Tenancy Fraud Conference and obtaining best practice guidance on tenancy fraud from other authorities and private sector organisations. Six suspected cases of tenancy fraud have been referred to the team and are being investigated.
- 8.8** The team has continued to receive referrals of suspected fraud in respect of the CT Reduction Scheme (CTRS), and investigation of 25 cases is underway. NDR is the next priority area for the team, based upon some initial research and a small pilot study. Training in counter fraud work for NDR will be coordinated with the Hub.
- 8.9** Internal Audit has in place an agreement with DWP for the future management of cases of HB fraud. The major work on each case will be the responsibility of the national Single Fraud Investigation Service (SFIS) but LDC retains a role in referring cases of suspected HB fraud to SFIS and handling requests for information. A total of 40 cases have been passed to SFIS and 12 information requests have been actioned.

## **9 Risk Management**

- 9.1** 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.
- 9.2** 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.
- 9.3** 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. The savings target for 2014/15 is £596,000 and this has been achieved, primarily from the first phase of the restructuring programme. The savings target is kept under review (so that it can reflect the latest projections of Government funding, inflation forecasts, etc.) and reported regularly to Cabinet.
- 9.4** The most recent report to Cabinet was in November 2014, and the report indicated a total savings target for the period 2015/16 to 2019/20 of £2,604,000. Of this, £550,000 is to be delivered next year, with £520,000 already identified. The source of savings will continue to come from structural change rather than incremental change. A further review of the savings target will take place at the February 2015 Cabinet meeting. The Head of Audit and Performance 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.
- 9.5** 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. The next report will be presented to the Cabinet in March 2015.

## **10 System of management assurance**

**10.1** 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 2013/14. 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 2013/14. Nothing has arisen in the first nine months of the financial year to change these assessments.

## **11 Corporate governance**

**11.1** 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. The Code has been reviewed and the results are presented separately to this meeting of the Committee.

**11.2** 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 2013/14 was reported to the September 2014 meeting of the Committee.

## **12 External assurance**

**12.1** 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.

**12.2** Annual Audit Letter for 2013/14 (October 2014) – This report summarises the key issues from the work carried out by BDO during the year. The letter confirms that:

- BDO issued an unqualified true and fair opinion on the financial statements for 2013/14.
- BDO identified three misstatements in relation to revaluations of land and buildings and the accounting for the value of additions to HRA Council dwellings. Appropriate amendments were made to the financial statements. As these corrections relate to capital transactions and valuations there was no impact on the General Fund or HRA balance.
- BDO did not identify any significant deficiencies in internal controls but, working with Internal Audit, BDO observed instances where purchase orders were either in excess of the officer's formal authorisation limits or were placed by officers not on the authorised signatory list. Management has agreed to review and strengthen this control.
- BDO were satisfied that the Council has robust systems and processes to manage financial risks and opportunities effectively and to secure a stable financial position that enables it to continue to operate for the foreseeable future, and BDO therefore issued an unqualified value for money conclusion.
- BDO noted that the Council maintains healthy levels of earmarked reserves and balances, and Members have agreed a policy to use reserves to fund investments and non-recurring expenditure.
- 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 noted that the Council's Whole of Government Accounts (WGA) submission is below the threshold for audit and they were required only to review the total amounts in the Data Collection Tool for property, plant and equipment and for the net pension liability. BDO reported that the values in the Data Collection Tool were consistent with the audited financial statements.
- The Medium Term Financial Strategy was updated during the year and Members continue to consider options for achieving additional savings, with these likely to arise from the continued organisational development process and Programme Nexus.
- BDO have completed their review of the Housing Pooled Capital Receipts 2013/14 and have no matters to report.
- BDO reported on the results of the most recent grant claims and returns certification report that covered three returns for 2012/13 amounting to £67 million. The Housing Pooled Capital Receipts return and National Non Domestic Rates returns were certified without amendment or qualification. The BDO audit of the Housing and Council Tax Benefits subsidy claim for 2012/13 found a number of errors in processing. Following further discussion and the provision of additional supporting information by the Council, DWP amended its assessment of the impact on the claim and made a deduction of approximately £4,000 from the final settlement.
- When the Annual Audit Letter was issued (late October 2014) the BDO work on the Housing Benefits subsidy claim for 2013/14 was still in progress. The results from this work will be reported to the Committee at the first meeting after submission of the claim.

### **13 Financial Appraisal**

13.1 There are no additional financial implications from this report.

### **14 Sustainability Implications**

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

### **15 Risk Management Implications**

15.1 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.

### **16 Legal Implications**

16.1 There are no legal implications arising from this report.

### **17 Equality Screening**

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



## **18 Background Papers**

**18.1** [Annual Audit Plan 2014/15 that was presented to the Audit and Standards Committee on 17 March 2014.](#)

## **19 Appendices**

**19.1** Appendix A - Statement of Internal Audit work and key issues.

**19.2** 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: IT Security – Compliance with Public Sector Network (PSN) standards**

**Date of final issue: 23 January 2015**

#### **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 IT security arrangements that are necessary to achieve PSN compliance. On the whole, compliance is soundly based, with issues from the previous verification process and penetration tests having been addressed, and PSN considerations are taken into account for new IT developments.

However, there are a small number of issues that indicate there is scope to strengthen the ways in which the PSN submission is prepared and checked. Internal Audit believes that the need to focus time and resources on the major project to update the Council's IT infrastructure is likely to have impacted on compiling the PSN submission. There is also the point that PSN standards and controls are very exacting, and may not be entirely necessary for all the uses made of PSN by the Council. The report contains five recommendations.

#### **Main points:**

- The Council's PSN submission for 2104 achieved Compliance Certification, without which the Council would not have been able to connect to the secure government network. The audit has noted instances where the answers and explanations given in the Council's submission were not entirely accurate or might not stand up to a more rigorous compliance review by the PSNA. The areas of non-compliance are not necessarily significant but they could place the Council's PSN certification at risk if noted by the PSNA. The Council may decide that this risk is not sufficient to justify some of the additional controls that would be necessary to meet full compliance with PSN standards.
- Not all the 46 Council officers who currently have access to PSN services will have been subject to the necessary security vetting checks as required by PSN, and there is no standing arrangement for new PSN users to be vetted to the required standard. To achieve this standard would require the use of Disclosure Scotland for most staff using the PSN network, and this could prove an onerous and expensive task. The Council could take a pragmatic approach and put in place controls that ensure the required vetting is applied to PSN users over time.
- The Council has met one of the key conditions in respect of Information Risk Management – the identification of a named responsible officer. However, it is not clear that the roles, responsibilities and supporting framework that would represent a security governance structure that is fully PSN compliant are present at the Council. The Council is undergoing a fundamental restructuring against a backdrop of challenging savings requirements. As a result, it is unlikely the Council will be in a position to assign all the roles and responsibilities required by PSN in the short term.