

Agenda Item No: 7 **Report No:** 59/17

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

Report To: Audit and Standards Committee **Date:** 20 March 2017

Ward(s) Affected: All

Report By: Head of Audit, Fraud and Procurement

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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 ten months of 2016/17, 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 ten months of 2016/17 (as shown in Section 3).
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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 were applied from 1 April 2013. The Head of Audit, Fraud and Procurement (HAFP) advised the Audit and Standards Committee of the effect of the standards at its March 2013 meeting.
- 2.2** 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.

- 2.3** The PSIAS 2016 continue to specify the requirements for the reporting to the Audit and Standards Committee and senior management by HAFP. These requirements are met via a series of reports, including interim reports to each meeting of the Committee.
- 2.4** Each interim report includes a review of the work undertaken by Internal Audit compared to the annual programme, an opinion of HAFP 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 2015/16 included the opinion of HAFP 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 ten 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. Prompt corrective action was taken to address issues noted during an internal audit of the Council's Right to Buy (RTB) processes (see also 4.9).

4 Internal Audit work 2016/17

- 4.1** This section of the report summarises the work undertaken by Internal Audit during the first ten months of the year, compared to the annual plan that was presented to the Audit and Standards Committee in March 2016. 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 554 audit days have been undertaken compared to 528 planned.

Table 1: Plan audit days compared to actual audit days for April 2016 to January 2017

Audit Area	Actual audit days for the year 2015/16	Plan audit days for the year 2016/17	Actual audit days to date	Pro rata plan audit days to date
Main Systems	360	290	287	
Central Systems	57	70	82	
Departmental Systems	68	70	86	
Performance and Management Scrutiny	27	45	8	
Computer Audit	2	45	-	
Management Responsibilities/Unplanned Audits	88	116	91	
Total	602	636	554	528

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 The variance of 26 days has largely been due to HAFP being involved in more direct audit work at this stage of the year than was originally envisaged. It is estimated that the audit days will be closer to plan by the year end, partly because of the staff change outlined below.
- 4.4 One of the Senior Auditors at LDC retired in January 2017. The intention is for the vacancy to be filled at Auditor level - the recruitment process will commence shortly and there will be a reduction in the days available for audit work in the latter months of 2016/17. The Audit Manager at EBC has carried out audit work at LDC during the year, but this arrangement is no longer in place.
- 4.5 **Main Systems:** The initial work was on 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 2015/16. A final report was issued. The corresponding work for 2016/17 is underway.
- 4.6 The work on behalf of BDO to test the Council's subsidy claim for Housing Benefits (HB) for 2015/16 has been completed. BDO's initial planning for this work had set out the standard testing requirements and identified the likely need for significant additional testing to address the issues noted in the previous year's claim. The standard testing was completed, and the test samples for the additional testing were confirmed in late October. The timetabled date for BDO to have signed off and submitted the audited claim was at the end of November 2016, but that date was not met because of the extra work that has been required. The claim is expected to have been submitted the time of the Committee meeting.
- 4.7 **Central Systems:** Some outstanding issues from the audit of Electoral Registration and Elections were being examined prior to confirmation of the draft report – that work is complete and the draft report has been issued. Final reports have been issued for the audit of Ethics, Newhaven Business Centre, Insurance, and for the priority audit of Business Continuity Planning (BCP). The results of the joint review of the EBC/LDC Leisure Trusts have been discussed with CMT, and a draft report has been issued. The current audit of Ethics is underway.
- 4.8 **Departmental Systems:** The final reports from the audits of Right to Buy (RTB), Private Sector Housing and Cemeteries have been issued. The audit of Estates Management, incorporating work on the corresponding function at EBC, began in January 2017.
- 4.9 The final report from the audit of RTB included an estimate of the impact of the discounting errors in completed and ongoing RTB sales in the period 2012/13 – 2015/16. The estimated loss to LDC was approximately £100,000. Immediate action was taken to correct the prices of ongoing sales, as was reported to the September 2016 meeting of the Committee. The effect is that the loss to LDC has been reduced to £88,000.
- 4.10 **Performance and Management Scrutiny:** The main work in this category has been in reviewing the data that supported the Annual Governance Statement (AGS), and specific tasks related to the Internal Audit aspects of the Council's Joint Transformation Programme (JTP).
- 4.11 **Computer Audit:** Internal Audit has examined the IT aspects of the main financial systems (see 4.5 above).

4.12 Management Responsibilities/Unplanned Audits: This category provides resources for activities such as support for the Audit and Standards Committee, managing the Fraud Investigations Team, liaison with BDO, and meeting requests for unplanned work.

4.13 There has been one unplanned audit that has been completed - a small scale exercise to review cash handling procedures at the Lewes Tourist Information Centre, and there were no significant outcomes.

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 2016/17 was on confirming the implementation of the recommendations that had been agreed in the previous year. The results of this work were reported separately to the June 2016 meeting of the Committee. The work to follow up the recommendations made during 2016/17 is underway.

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 2015/16, and the targets for 2016/17, were reported to the June 2016 meeting of the Committee. The results enabled the HAFP 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.

7 Review of 2016/17 Audit Plan

7.1 As part of the report to the March 2016 meeting of the Committee that detailed the Annual Audit Plan, HAFP advised that there would be a nine month review of the Audit Plan for 2016/17 to assess whether any significant changes are necessary.

7.2 That review has taken place and the results of the review are now presented to the Committee. The review takes account of a range of issues, in particular the Joint Transformation Programme, the impact of the significant extra work on the Benefits subsidy claim with BDO, the retirement of the Senior Auditor and the extra audit days worked by HAFP. There has been little overall impact on the number of days available to complete the audit programme for 2016/17, but there has been a need to re-assign some tasks.

7.3 HAFP advises that all significant aspects of the annual audit plan will be covered. The exceptions are:

- As previously reported, the planned audit of IT Security and Networks will not be possible because of the retirement of the Senior Auditor who was the specialist computer auditor. The audit will be scheduled for a future date in the audit cycle.
- The planned audit of Members Allowances and Expenses is scheduled into the Annual Plan for 2017/18 that is presented separately to the Committee.

Other audits in the programme for 2016/17 that are planned or underway will continue to a normal conclusion.

8 Combatting Fraud and Corruption

- 8.1** The Annual Report on the Council's work to combat Fraud and Corruption 2015/16 was presented to the June 2016 meeting of the Committee. That report was a detailed statement of the strategies and structures that in place to counter fraud and corruption, and the information within the report is still accurate and relevant. Below are updates that outline the main developments since the start of 2016/17.

Local developments

- 8.2** The Investigation Team maintains 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. A sub group of seven authorities within ESFOG are working together in a 'Hub' approach to coordinate new counter fraud initiatives across East Sussex and Brighton.
- 8.3** The Hub has funded training, the implementation of a shared case management system, a housing support system that uses tenancy data to help improve tenancy management and highlight fraud risks, and a programme of counter fraud publicity work by the private sector company PRG.

LDC Investigations Team

- 8.4** The Council has in place an agreement with DWP for the management of cases of HB fraud, and officers work with local DWP teams to help ensure efficient operation of the processes covered by the agreement. The major work on each case is the responsibility of the national Single Fraud Investigation Service (SFIS) within DWP. The Council retains a role in referring cases of suspected HB fraud to SFIS and handling requests for information. In an agreement with the Investigation Team at EBC a member of that team has, since mid-August 2016, taken over the Council's SFIS liaison work. Since 1 April 2016, 110 HB cases have been passed to SFIS, and 64 information requests have been actioned.
- 8.5** The LDC Investigations Team retains responsibility for dealing with the cases of suspected Council Tax Reduction Scheme (CTRS) fraud that are often linked to HB cases, and administering the penalties for cases that are not subject to prosecution. Nine cases are currently under review and one case is being investigated.
- 8.6** The main focus of the team's work in 2016/17 has been in continuing to address tenancy issues. The team's approach has included obtaining best practice guidance from other authorities, and maintaining effective referral arrangements with officers in LDC Housing Services. Four properties have been returned to the Council's housing stock, and a number of cases have been closed. Seven suspected cases of abandonment or subletting are being investigated or are undergoing pre-investigation review.
- 8.7** Since July 2016, the Investigation Team has been operating a new regime of checks on Right to Buy (RTB) applications to prevent and detect fraud, and protect the Council against money laundering. To date, 24 RTB applications have been withdrawn after intervention by the Investigations Team. Two cases of suspected RTB fraud are being investigated – one involves an ongoing application, and the other involves one of the withdrawn applications. The team is assessing a number

of the other withdrawn RTB applications because the cases could indicate potential fraud.

National Fraud Initiative (NFI)

- 8.8** Internal Audit continues to coordinate the Council's work on NFI data matching exercises. Council services submitted the various data ranges in mid-October 2016 and have dealt with a number of queries since then.
- 8.9** Internal Audit, the Investigations Team and service managers have been preparing for the receipt of the reported matches, which arrived in late January 2017. There are 1,838 matches detailed across 81 reports. Each report sets out different types of potential frauds among benefit claimants, housing tenants, and anyone receiving payments or discounts from the Council. Council departments have nominated officers to investigate matches in their service areas. The exercise involves analysis of the matches to weed out those that are the result of error or coincidence, and then the examination of the remaining matches to assess the likelihood of fraud.
- 8.10** The major work will be in examining 930 reported matches involving HB. The staff in Revenues and Benefits will seek to recover benefits that have been incorrectly claimed, with more significant cases of suspected HB fraud being passed to SFIS for investigation in the normal way (see 8.4 above). A further priority is the examination of a new series of matches involving entries on the Housing Register.

9 Risk Management

- 9.1** Cabinet approved the Risk Management Strategy in September 2003. Since then risk management at the Council has been the subject of ongoing development, 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.
- 10** 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.
- 11** 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.
- 12** 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.

- 13** 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.

14 System of management assurance

- 14.1** 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 are responsible. 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 2015/16. At its meeting on 3 May 2016 CMT confirmed that there were no significant governance issues to report. There has been nothing in the first ten months of the financial year to change these assessments.

15 Corporate governance

- 15.1** In March 2016, HAFP 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. The corresponding review for 2017 is underway and the results will be presented to the June 2017 meeting of the Committee.

- 15.2** 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 2016 was presented to the June 2016 meeting of the Committee, and the final version of the AGS was presented to the September 2016 meeting of the Committee with the Statement of Accounts for 2015/16. The draft AGS for 2017 will be presented to the June 2017 meeting of the Committee.

16 External assurance

- 16.1** 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.

- 16.2** 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.

16.3 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.

16.4 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.

17 Financial Appraisal

17.1 There are no additional financial implications from this report.

18 Sustainability Implications

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

19 Risk Management Implications

19.1 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.

20 Legal Implications

20.1 There are no legal implications arising from this report.

21 Equality Screening

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

22 Background Papers

22.1 [Annual Audit Plan 2016/17](#)

23 Appendices

23.1 There is no Statement of Internal Audit work and key issues (normally Appendix A1) for this report.

23.2 Appendix A2: Table of abbreviations.

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

APPENDIX A1

Statement of Internal Audit work and key issues

No statement for this report.

Appendix A2

Table of abbreviations

AGS – Annual Governance Statement
BCP – Business Continuity Planning
BDO – BDO, the Council's external auditors. Formerly BDO Stoy Hayward
CIPFA – Chartered institute of Public Finance and Accounting
CMT – Corporate Management Team
CTRS – Council Tax Reduction Scheme
DCLG – Department for Communities and Local Government
DFGs – Disabled Facilities Grants
DWP – Department of Work and Pensions
EBC – Eastbourne Borough Council
ESFOG – East Sussex Fraud Officers Group
HAFP – Head of Audit, Fraud and Procurement
HB – Housing Benefit
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
NFI – National Fraud Initiative
PIs – Performance Indicators
PSIAS – Public Sector Internal Audit Standards
QAIP – Quality Assurance and Improvement Programme
RTB – Right to Buy
SFIS – Single Fraud Investigation Service
WGA – Whole of Government Accounts