

<b>Report To:</b>	<b>Audit and Standards Committee</b>
<b>Date:</b>	<b>16 July 2019</b>
<b>Title:</b>	<b>Annual Report on the Council's Systems of Internal Control 2018/19</b>
<b>Report of:</b>	<b>Chief Internal Auditor</b>
<b>Ward(s):</b>	<b>All</b>
<b>Purpose of report:</b>	<b>To provide a summary of the activities of Internal Audit and Counter Fraud for the year 1<sup>st</sup> April 2018 to 31<sup>st</sup> March 2019.</b>
<b>Officer recommendation(s):</b>	<b>To note that the overall standards of internal control were generally satisfactory during the financial year 2018/19</b>
<b>Reasons for recommendations:</b>	<b>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.</b>
<b>Contact Officer(s)</b>	<b>Name: Jackie Humphrey Post title: Chief Internal Auditor E mail: jackie.humphrey@lewes-eastbourne.gov.uk Telephone number: 01323 415925</b>

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## **1 Introduction**

- 1.1** 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 first applied from 1 April 2013. The PSIAS were updated in March 2017. The updated standards are not materially different from the previous version, and so have not been separately reported to the Committee.
- 1.2** The PSIAS 2017 continue to specify the requirements for the reporting to the Audit and Standards Committee and senior management by the Chief Internal Auditor. These requirements are met via a series of reports, including interim reports to each meeting of the Committee.
- 1.3** Each interim report includes a review of the work undertaken by Internal Audit compared to the annual programme, an opinion of the Chief Internal Auditor 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. .
- 1.4** In September 2015, Cabinet approved a strategy for the development of shared services between Lewes District Council (LDC) and Eastbourne Borough Council (EBC) based on the integration of the majority of council services via a Joint

Transformation Programme (JTP). The formal integration of the Internal Audit and Counter Fraud Teams in both councils took place on 1 July 2017.

- 1.5** Together with a number of other corporate services, the third and final phase of the JTP process has included Audit and Counter Fraud. The results of the consultation process were confirmed in mid-February 2019. The post of Head of Audit and Counter Fraud has been replaced by the post of Chief Internal Auditor which has now been filled. The Audit Manager post has been backfilled and, at the time of writing one interviews had taken place for the one audit vacancy and CMT were being asked for permission to fill the second vacant Auditor post which had been caused by the appointment of the Audit Manager.

## **2 Internal Control Environment at Lewes District Council**

- 2.1** The Annual Report on the Council's Systems of Internal Control for 2017/18 was presented to the July 2018 meeting of the Committee. The report included the opinion of Head of Audit and Counter Fraud (HACF) that the overall standards of internal control are generally satisfactory. This opinion was based on the work of Internal Audit, the internal assurance framework, external reviews, and the Council's work on risk management. In the period 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.

## **3 Internal Audit work 2018/19**

- 3.1** This section of the report summarises the work undertaken by Internal Audit, compared to the annual plan that was presented to the Audit and Standards Committee in March 2018.
- 3.2** Table 1 shows that a total of 669 audit days have been undertaken compared to 673 days planned for the year.

Table 1: Plan audit days compared to actual audit days for April 2018 to end March 2019

Audit Area	Actual audit days for the year 2017/18	Plan audit days for the year 2018/19	Actual audit days to date
Main Systems	347	308	450
Central Systems	67	65	65
Departmental Systems	3	87	29
Performance and Management Scrutiny	34	30	11
Computer Audit	5	25	13
Management Responsibilities/Unplanned Audits	101	158	101
Total	557	673	669

- 3.3 Main Systems:** The key work has been 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 2017/18. The testing was completed and a final report issued. The results contributed to the overall opinion given by HACF (see Section 2 above). The corresponding work for 2018/19 is currently being undertaken.

- 3.4** The work on behalf of BDO to test the Council's HB subsidy claim 2016/17 has been the other main priority and is now complete. BDO had identified the need for significant additional testing to address the issues noted in the 2015/16 claim and other errors noted in the current claim. The timetabled date for BDO to sign off and submit the audited claim was the end of November 2017 but, because of the significant extra work required and BDO's other commitments, the claim was submitted in the last week of September 2018.
- 3.5** The corresponding exercise to test the Council's HB subsidy claim 2017/18 is now the main priority and the work has been underway for some months. The results from the initial sample testing have helped to inform BDO's work on the Council's 2017/18 accounts. BDO identified the need for significant additional testing to address the issues noted in the 2016/17 claim. The timetabled date for BDO to sign off and submit the audited claim was the end of November 2018 but, because of the late start to the exercise and the significant extra work required the claim is still being tested. BDO have stated that they will have no capacity to fully check the work until August 2019 though testing is being passed to them when completed.
- 3.6 *Central Systems:*** An audit of Safeguarding at both councils has been completed by audit personnel in Eastbourne, and a final report has been issued. A final report has been issued for the annual audit of Ethics. The review of joint ventures and Council owned companies has been completed and a draft report has been issued.
- 3.7 *Departmental Systems:*** The audit of Estates Management, incorporating work on the corresponding function at EBC, began in 2017 but was put on hold to free resources for the work on the HB subsidy claim and the testing of the main financial systems - the audit has been completed by audit personnel in Eastbourne and a final report has been issued. An audit of the Licensing of Houses in Multiple Occupation (HMO) has been carried out by personnel in Eastbourne, and a final report has been issued. An audit of the other aspects of Licensing is underway.
- 3.8 *Performance and Management Scrutiny:*** The initial work in this category was the review of the data that supports the Annual Governance Statement (AGS) for 2018, with the main task being the examination of the revised Strategic Risk Register.
- 3.9 *Computer Audit:*** Internal Audit has examined the IT aspects of the main financial systems, and is examining the controls over the implementation of the CX Housing Management system. An audit of Cyber Security is at the planning stage.
- 3.10 *Management Responsibilities/Unplanned Audits:*** This category provides resources for activities such as support for the Audit and Standards Committee, managing the Counter Fraud Team, liaison with BDO, managing the Follow Up procedures, as well as for special projects or investigations.
- 3.11** CMT requested Internal Audit to carry out an assurance review to support the establishment of the newly configured Health and Safety (H&S) service. The review includes site visits to two key service areas – the Eastbourne Crematorium and the Waste and Recycling (W&R) service for LDC. A final interim report was issued on the W&R aspects of the review, and the results of the H&S review of the crematorium have been included in a draft report that also covers other aspects of the Bereavement Services at the location. Internal Audit has also carried out a review of the management of statutory building compliance at both councils; an interim report was issued in June 2018, with a final report issued during October

2018. HACF is currently engaged in a series of governance and risk management reviews with the Chief Finance Officer.

#### **4 Peer Review**

- 4.1** The External Peer Review of LDC Internal Audit has been completed. The review was carried out by the Principal Auditor at Chichester District Council and the results were reported to the September 2018 meeting of the Committee. The overall results of the review were that the LDC Internal Audit service generally conforms to the standards set by PSIAS 2017.
- 4.2** The Peer Review examined the service in four key sections – Purpose and positioning; Structure and resources; Audit execution; Impacts – comparing service activities to the statements of good practice contained within the PSIAS. The review also took account of the results from the client questionnaires sent to CMT, Heads of Service and the Chair of the Audit and Standards Committee.
- 4.3** The review found that the Internal Audit service fully complies with 43% of the statements of good practice and, for the remainder, complies with the PSIAS requirements in all material respects. The exceptions were in areas such as annual appraisals, succession planning, and the rotation and technical development of audit staff who are not professionally qualified. No remedial action is planned because the service complies with Council policies in these areas, but these do not meet PSIAS requirements in all respects.
- 4.4** Where the service is planning remedial action is in completing the audit manual which is in the processing of being re-worked following the merger with Eastbourne Borough Council. The work is underway, and includes the procurement of the Pentana audit management system, but no target date for completion has been set.

#### **5 Review of 2018/19 Audit Plan**

- 5.1** As part of the report to the March 2018 meeting of the Committee that detailed the Annual Audit Plan, HACF advised that there would be a nine month review of the Audit Plan for 2018/19 to assess whether any significant changes are necessary.
- 5.2** That review has taken place and the results of the review were presented to the January 2019 meeting of the Committee. The review took account of a range of issues including the significant extra work on the HB subsidy claim, the loss of audit days due to sickness, and the extra days worked by HACF. There has been a significant impact on the number of days available to complete the audit programme for 2018/19, and there has been a need to re-assign some tasks.
- 5.3** HACF advised that the significant aspects of the annual audit plan would be covered, but with a small number of audits scheduled into the Annual Plan for 2019/20. Other audits in the programme for 2018/19 that are planned or underway will continue to a normal conclusion. A number of these audits may run on into the early months of 2019/20.

## **6 Combatting Fraud and Corruption**

### **National initiatives**

- 6.1** The 2018 National Fraud Initiative (NFI) exercise is underway, with the Counter Fraud Investigations Manager in Eastbourne taking the coordination role for both councils. The matches were received in February 2019, with 1654 matches for LDC across 55 reports. Each report sets out different types of potential fraud among benefit claimants, housing tenants, and anyone receiving payments or discounts from the Council. There is a targeted approach to the examination of matches to identify those that indicate the greatest likelihood of fraud or significant error. So far, 333 matches have been closed with no errors or frauds identified. A further 42 matches are currently being examined.

### **Local initiatives**

- 6.2** The Investigation Team is a member 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. Since 2014/15, a sub group of authorities within ESFOG, including LDC and EBC, have been working as a 'Hub' to coordinate new counter fraud initiatives across East Sussex.
- 6.3** The Hub has been administered by officers at Eastbourne, with input from ESFOG partners as appropriate. Lewes and Eastbourne Counter Fraud activities have benefitted from Hub funding in the provision of training, the introduction of a shared case management system, a shared approach to publicity for Hub activities, and the set-up of an on-line system to allow the public to report suspected frauds.
- 6.4** Hub funds have been set aside to cover known future commitments, with the balance divided among members to fund local Counter Fraud initiatives. The Hub still meets quarterly or as and when required.

### **Counter Fraud Team**

- 6.5** At present, countering housing tenancy fraud and abandonment, and preventing RTB fraud, are the main operational priorities for the Counter Fraud Team at Lewes because of the evidence of this being a high risk area for the Council. There are 23 cases of suspected abandonment and/or subletting under investigation, plus three of suspected housing application fraud. Six properties have been returned to stock after joint action by officers in Housing, Legal Services and Counter Fraud to address cases of abandonment or anti-social behaviour. Further property returns are anticipated in current cases where evidence gives a strong indication that the tenant no longer lives at the property. One case of abandonment has been referred to Legal Services for preparation for court action.
- 6.6** Since April 2018, 31 new RTB applications have been received for checking to prevent fraud and protect the Council against money laundering. In the same period, 25 RTB applications have been approved and passed for processing. In the same period, nine RTB applications have been withdrawn or closed after intervention by the team. The team will assess these applications to determine whether the cases indicate potential fraud. Two cases of suspected RTB fraud are under investigation, and one of these cases has been referred to Legal Services for preparation for court action.

- 6.7** Audit and Counter Fraud has in place an agreement with DWP for the management of cases of HB fraud. The major work on each HB case is the responsibility of the national Single Fraud Investigation Service (SFIS) within DWP. LDC retains a role in referring cases of suspected HB fraud to SFIS and handling requests for information. A member of that Eastbourne Counter Fraud team and a member of the HB team share the DWP liaison work for LDC, and this arrangement allows the Lewes Counter Fraud team to focus on case work in other areas. In the period since April 2018, there have been 15 referrals to SFIS, and 37 information requests have been actioned.

## **7 Risk Management**

- 7.1** 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.
- 7.2** The Annual Report on Risk Management and the Strategic Risk Register was presented to the March 2018 meeting of the Committee. The report recommended a change to the circulation of the report, with the Committee becoming the principal recipient of the Strategic Risk Register. 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 the Council's 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.
- 7.3** CMT has reviewed the Strategic Risk Register, and the results of the review were reported to the September 2018 meeting of the Committee.
- 7.4** The December 2018 Cabinet meeting received the draft budget proposals for 2019/20. In summary, the wider economic picture remains challenging and there is no end in sight to austerity for local government. The budget report contained a detailed risk analysis that highlighted a range of financial risks, potential outcomes and possible mitigations in areas such as pay and price inflation, and changes in government legislation. The risks assessed as having a 'High' likelihood and the most significant impact were probable increases in interest rates and their effect on borrowing costs, and the government reductions to retained business rates.
- 7.5** The February 2019 Cabinet meeting received updated reports on the Council's financial performance and, following wide consultation on the draft budget, the formal budget proposals for 2019/20. The budget report included the conclusion that 'The Council is reasonably placed financially to meet the demands on its services as well as the reductions in Government support. However, the challenge over the medium term is profound and more change is necessary to move to a sustainable position. The Council is more dependent on commercial activity than it has ever been and this requires a high level of monitoring and risk management.'

## **8 System of management assurance**

- 8.1** 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 senior managers are required to consider whether there were any significant governance issues during 2017/18. None were reported and, at its meeting on 26 June 2018, CMT confirmed that there were no significant governance issues to report.

## **9 Corporate governance**

- 9.1** 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 2018-19 is presented as a separate report to this meeting of the Audit and Standards committee.

## **10 External assurance**

- 10.1** 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 Council's external auditors are from April 2018 for a period of five years. No reports have yet been received from Deloitte. Below the reports of BDO for the year financial year 2017-18, which were issued in the financial year 2018-19, have been summarised.

- 10.2** Audit Completion Report (September 2018) – This report summarised the key issues from work carried out by BDO during the year ended 31 March 2018. When the report was published it represented an interim position because BDO were in the process of completing the audit – the Council had not prepared the draft and final Statement of Accounts in accordance with the new statutory deadlines. The interim key issues highlighted in the report overview section were:

- BDO had not identified any significant audit risks since the presentation of their Audit Plan in February 2018, and there were no significant changes to the planned audit approach.
- BDO had not identified any material misstatements, although the audit was still in progress and could result in audit differences.
- BDO were satisfied that, despite the recognised funding gap in the Medium Term Financial Strategy (MTFS), the Council has appropriate arrangements to remain financially sustainable over the period of the MTFS. All the required savings for 2018/19 had been identified.
- BDO anticipated issuing an unmodified opinion on the arrangements to secure economy, efficiency and effectiveness in the use of resources.
- Subject to successful completion of outstanding work, BDO anticipated issuing an unmodified opinion on the Council's financial statements, and on the consistency of other information in the Statement of Accounts with the financial statements.

**10.3 Grant Claims and Returns Certification for year ended 31 March 2017 (November 2018). The key points were:**

- The audit of the HB subsidy claim identified a high level of errors within the cases tested. This situation, together with the prior year issues identified in the previous audit, required a significant amount of extra testing comprising ten samples of 40 cases, and 100% testing of 129 non-HRA cases.
- The additional work required to be completed by BDO and the Council meant that the audit was completed and a qualified certification issued on 28 September 2018, significantly later than the national deadline of 30 November 2017.
- The claim was valued at £35,127k. The audit identified the need for five different types of amendments to the claim totalling £49k. Because the total level of errors was below the allowed threshold, this did not result in further changes to the total amount of subsidy claimed. A final adjustment of the claim resulted in an increase of £678.
- The review of the returns for the Pooling of Housing Capital Receipts was completed satisfactorily without amendment or qualification. Total receipts were recorded as £1,964k, of which £408k was payable to DCLG.

**11 Managing the Risk of Fraud and Corruption**

**11.1** Cipfa suggests it is good practice to make a statement on the adequacy of an authority's counter fraud arrangements in the annual governance report. Cipfa has published a Code of Practice on Managing the Risk of Fraud and Corruption which contains five principles:

- Acknowledge responsibility
  - Identify risks
  - Develop a strategy
  - Provide resources
  - Take action

**11.2** Having considered all the principles the Chief Internal Auditor is satisfied that the Council meets these by having fully resourced Counter-Fraud and Audit teams who review the risks across the authority and direct their work as appropriate. It is therefore considered that the organisation has adopted a response that is appropriate for its fraud and corruption risks and commits to maintain its vigilance to tackle fraud and uphold its zero tolerance policy.

**12 Annual Governance Statement and Opinion of the Chief Internal Auditor.**

**12.1** The work of the Internal Audit and Counter-Fraud teams referred to in this report has been used as the basis for the opinion of the overall effectiveness and adequacy of the internal control environment along with other ad hoc work undertaken by auditors.

**12.2** Considering the findings it is the opinion of the Internal Chief Internal Auditor that internal controls in processes and IT systems across the authority were generally found to be sound.



- 12.3** There is an exception to this opinion in respect of the new Housing Management software. This is specifically dealt with in the Annual Governance Statement report.
- 12.4** This opinion feeds into the Annual Governance Statement which is reported separately to this committee.

### **13 Conforming with the Public Sector Internal Audit Standards**

- 13.1** The Public Sector Internal Audit Standards (PSIAS) came into effect from 1<sup>st</sup> April 2013. The work of the Internal Audit section is annually assessed for compliance against the standards. This is an internal self-assessment.
- 13.2** A checklist for compliance has been completed and it is found that the Internal Audit function is “generally conforming” to the standards. Conformance remains at about 99% of the points listed in the standards.
- 13.3** The variances are in minor areas such as appraisals where Council procedures differ slightly from the standards.
- 13.4** It is therefore the opinion of the Chief Internal Auditor that the Council’s Internal Audit Service generally conforms with the standards.
- 13.5** The standards require an external review to be carried out at least every five years. This review was carried out by Chichester District Council and the results reported to the Audit and Standards Committee at the September 2018 meeting. The overall results were that the Internal Audit service at Lewes District Council generally conforms to the standards set out in the PSIAS.
- 13.6** The Internal Audit team has maintained its independence throughout 2018/19 in accordance with the Audit Charter.

### **14 Financial Appraisal**

- 14.1** There are no financial implications arising from the recommendations in this report other than those already contained within existing budgets.

### **15 Legal Implications**

- 15.1** This report demonstrates compliance with regulations 3 and 5 of The Accounts and Audit Regulations 2015.
- 15.2** Regulation 3 requires the Council to ensure that it has a sound system of internal control which—
- (a) facilitates the effective exercise of its functions and the achievement of its aims and objectives;
  - (b) ensures that the financial and operational management of the authority is effective; and
  - (c) includes effective arrangements for the management of risk.

- 15.3** Regulation 5 requires the Council to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance.

*Lawyer consulted 13.06.19*

*Legal ref: 008346-LDC-OD*

## **16 Risk Management Implications**

- 16.1** If the Council does not have an effective risk management framework that is subject to proper oversight by Councillors it will not be able to demonstrate that it has in place adequate means to safeguard Council assets and services, and it could be subject to criticism from the Council's external auditor or the public.

## **17 Equality analysis**

- 17.1** An equalities impact assessment is not considered necessary because the report is for information only and involves no key decisions.

## **18 Appendices**

None

## **19 Background Papers**

Audit reports issued throughout the year.