

Committee	Audit Panel	Item No.	8
Report Title	Head of Audit & Risk Annual Assurance Report for 2010/11		
Contributors	Interim Head of Audit and Risk		
Class	Open	Date	22 June 2011

1. Reasons for lateness

- 1.1 It was not quite possible to finalise all the details of this report in time for dispatch on 14 June 2011 as work on the annual governance statement (which was dispatched on time) was also required to be completed. Nevertheless it is essential that the report is considered at this meeting, in the context of the annual governance statement and draft accounts.

2. Purpose

- 2.1. The purpose of this report is to present members of the Audit Panel with the Head of Internal Audit & Risk's annual assurance opinion and statement on the effectiveness of the Council's system of internal control.

3. Recommendation

- 3.1. Members are asked to note the report.

4. Introduction

- 4.1. The new Accounts and Audit (England) Regulations 2011 statutory instrument, requires the Council to "undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control". And the Council, "must at least once in each year, conduct a review of the effectiveness of its internal audit".
- 4.2. The proper practices for internal audit are set out in the Chartered Institute for Public Finance and Accountancy's Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 (the CIPFA Code). The CIPFA code is informed by standards from other professional institutes, including the Institute of Internal Auditors (IIA) and the Government Internal Audit Standards (GIAS) issued by HM Treasury.
- 4.3. This report provides the Head of Internal Audit and Risk's assurance opinion on the adequacy and effectiveness of the London Borough of Lewisham's internal control arrangements for the year April 2010 to March 2011.
- 4.4. The annual assurance statement accompanying this opinion contributes to the annual review of internal control required by the Accounts and Audit (England) Regulations 2011 for the completion of the Annual Governance Statement.
- 4.5. The timing of this report is scheduled to allow it to be considered as part of the Council's annual review of governance and internal control.

5. Background

- 5.1. The CIPFA code sets out a number of elements to be included in the annual opinion and statement of the Head of Internal Audit. These are:

- Include an opinion on the overall adequacy and effectiveness of the organisation's control environment
- Disclose any qualifications to that opinion, together with the reasons for the qualification
- Present a summary of the audit work from which the opinion is derived, including reliance on work by other assurance bodies
- Draw attention to any issues the Head of Internal Audit judges particularly relevant to the Annual Governance Statement
- Compare the work actually undertaken with the work that was planned and summarise the performance of the internal audit function against its performance measures and targets, and
- Comment on the compliance with these standards and communicate the results of the internal audit quality assurance programme.

6. Opinion

6.1. The Head of Internal Audit's opinion on the overall adequacy and effectiveness of the Council's risk management systems and internal control environment, including any qualifications to that opinion, is as follows:

6.2. *I have considered all of the work undertaken and reported on by the Internal Audit Service and Anti-Fraud and Corruption Team during the year ended 31 March 2011 and work undertaken post year end. In my opinion, **satisfactory assurance** can be placed on the adequacy and effectiveness of internal controls in place in those areas reviewed. Where weaknesses have been identified these have been reported on and are being addressed by management.*

6.3. *I have also considered the risk management processes in operation throughout the organisation. The Council's risk management arrangements have also been assessed by the Internal Audit Service contractor – RSM Tenon – maintaining its position as 'Risk Managed'. I'm satisfied that the Council has an established risk management process in operation at the Corporate and Directorate levels, which it continues to challenge and enhance at the operational level.*

6.4. *I was part of the Annual Governance Statement working party through 2010/11, a group of senior officers responsible for preparing and reviewing the Council's Annual Governance Statement. I am satisfied that the content of the statement is accurate and its completion has complied with the relevant CIPFA guidance. Issues which I have judged relevant to the preparation of the Annual Governance Statement have been included.*

7. Qualifications to the opinion

7.1. Overall a lot of good practices were identified as in place and operating effectively in the Council's governance, risk and control arrangements. However, one key system was not reviewed and three areas that will benefit from continued management attention and control improvements were noted. They were; information governance, contract monitoring, compliance with procedures, and the fixed asset system.

7.2. The fixed asset system is a key financial system used for the monitoring and reporting of the Council's property, plant and equipment. During 2010/11 the Council implemented a new system to improve the quality and ease of monitoring its fixed assets, in part to facilitate meeting the new requirements for reporting under IFRS. However, the system implementation, uploading of records and cleansing of data was not completed in time for the planned internal audit review. As a key system for

the preparation of the financial statements it was therefore agreed, with management and the Council's external auditors, the Audit Commission, that this review will be conducted by the Audit Commission as part of their year end work.

- 7.3. From over 100 internal audits completed in the year 266 high and medium recommendations were made. Of these identified over 70% were in respect of the application of controls, rather than the design of the controls. Monitoring compliance with agreed policies and procedures is an important part of management assurance, mitigating risk and over time reducing the level of independent assurance needed. The internal audit service is continuing the practice of following up all high and medium recommendations to ensure their implementation and reinforce the messages with managers around the importance of complying with agreed controls.
- 7.4. Review of the Council's procurement arrangements has generally found the controls in place to be good. However, once services are procured there is the risk of managing contractors, both in terms of quality of service delivery and how they use and maintain the Council's assets. This risk is increasing as the Council shares or outsources more services to other private, public or third sector organisations, with different models for resourcing and supporting the delivery of core services. A significant proportion of the 2011/12 audit plan will be focused on this area of risk.
- 7.5. Information governance includes the arrangements for the management of sensitive and confidential information and data in all its forms across the Council's activities. Audit and Risk work in 2010/11 identified the need to better align the Council's policies and procedures to meet legislative and good practice requirements, raise awareness of the risk and monitor compliance with internal controls. The actions to achieve this improvement have been included in the Annual Governance Statement.

8. Internal audit

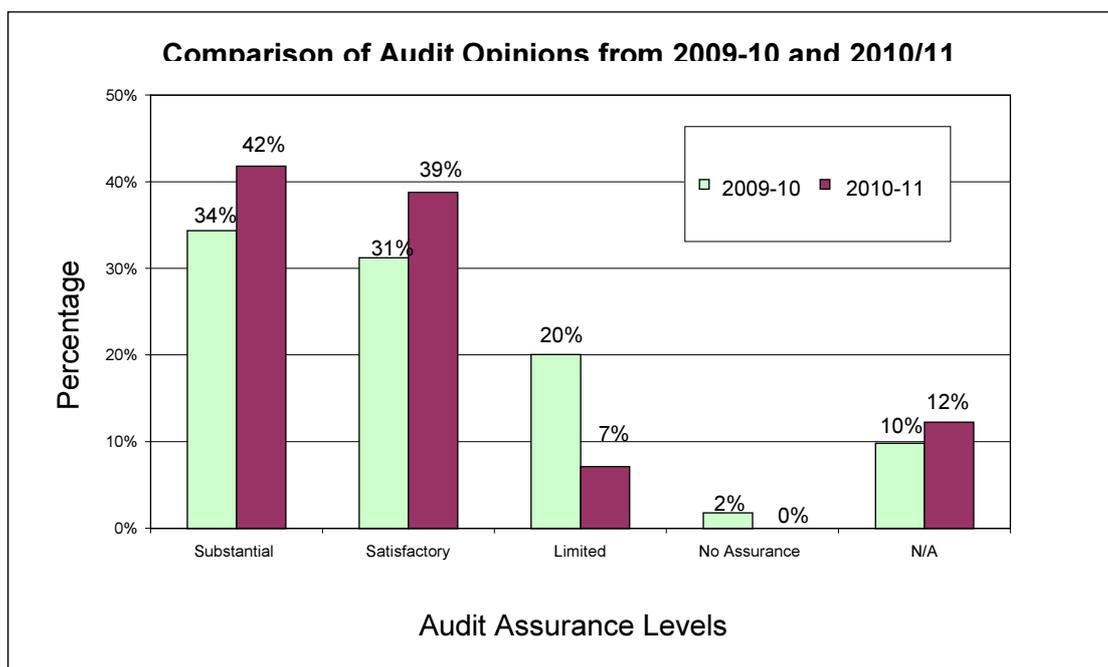
- 8.1. The internal audit plan for 2010/11, approved by the Audit Panel in March 2010, included 100 audits, requiring 1,175 days of audit work (excluding follow-up reviews and contingency). Through the year in response to circumstances and emerging risks 22 additional audits were added and 12 removed from the plan. Of the revised full year plan 95% was completed to draft report stage by the 31 March.
- 8.2. The Council's staff monitor and manage the delivery of the internal audit service by its appointed contractor – RSM Tenon – via an agreed set of performance indicators reviewed monthly. Over the year the contractor has performed, including addressing concerns raised about slippage in the plan, to deliver 95% of the plan by year end.
- 8.3. The full year performance figures for the five key performance indicators are set out in the table below:

Performance Indicators to Q4 (for 2010/11)	Target	Actual	Variance (+/-)
1. Percentage of draft audit reports issued within 15 working days of the exit meeting	90%	83%	(7)%
2. Percentage of final reports issued within 10 working days of agreed draft report	95%	96%	1%
3. Percentage of final reports issued within 30 working days from issue of original draft report	100%	90%	(10)%
4. The average level of client satisfaction to be achieved (out of 5)	4	4.2	0.2
5. Percentage of recommendations agreed with management	100%	100%	-

• High recommendations	90%	98%	8%
• Medium recommendations			
• Low recommendations	80%	100%	20%

8.4. Three of the five targets were exceeded. The reasons behind the two targets were missed have been reviewed and understood. Arrangements to ensure continuity of work to meet deadlines when a key member of the team is away have been strengthened and the targets adjusted to remain challenging but not unrealistic.

8.5. A comparison of internal audit opinions in the finalised audit reports for 2010/11 (91% of the plan) compared to the prior year is presented below. (N/A = those reports that were advisory, grant work, FMSiS or other non-audit assurance work). There were no 'No Assurance' reports issued in 2010/11.



8.6. As part of this work, where recommendations are made to enhance controls or address specific issues these are classified according to their significance – High, Medium or Low. For 2010/11 266 high and medium recommendations were made. This represents 63% of the total compared to 60% for the prior year. A slight decline. Of the recommendations made in 2010/11 70% were in respect of the application of controls (compliance), rather than the design of the controls.

8.7. Internal audit met regularly throughout the year with the external auditors, the Audit Commission. The external auditors review the quality of internal audit's work when deciding whether to place reliance on it to support their financial statements work.

8.8. Key financial systems

8.8.1. The key financial systems are fundamental to the operation of the Council, so it is important that these systems have robust internal control mechanisms and operate effectively. For these reasons internal audit allocates over 20% of the internal audit resource and reviews these systems every year, irrespective of previous assurance opinions.

8.8.2. A total of twelve key financial systems audits were completed from a planned thirteen in the 2010/11 audit plan. The exception being fixed assets. The fixed asset system audit for 2010/11 has been transferred to the external auditors as the system implementation, uploading of records and cleansing of data was not completed in time for the planned internal audit review. The other twelve system audits all received a positive (i.e. substantial or satisfactory) audit opinion. All except two received the same or improved levels of assurance.

8.8.3. A summary of this year's outcomes, with prior year comparisons, is presented below:

Key Audit	2008/09 Opinion	2009/10 Opinion	2010/11 Opinion	2010/11 Direction of Travel
Payroll	Limited	Satisfactory	Substantial	▲
Budget setting & control	Satisfactory	Substantial	Substantial	◀▶
Main accounting / general ledger	Substantial	Substantial	Substantial	◀▶
Council tax	Substantial	Substantial	Substantial	◀▶
Treasury management	Substantial	Substantial	Substantial	◀▶
Housing benefits	Substantial	Substantial	Substantial	◀▶
Pensions	Substantial	Substantial	Substantial	◀▶
Capital programme & expenditure	Satisfactory	Satisfactory	Satisfactory	◀▶
Cash collection & banking	Substantial	Substantial	Satisfactory	▼
NNDR (business rates)	Substantial	Substantial	Satisfactory	▼
Creditors (accounts payable)	Limited	Satisfactory	Satisfactory	◀▶
Debtors (accounts receivable)	Substantial	Satisfactory	Substantial	▲
Fixed assets	Satisfactory	Satisfactory	Deferred	see commentary

8.9. Risk based work

8.9.1. Aside the key financial system work, the majority of the audit plan is guided to assessing the effective governance, risk and control arrangements in operation around identified areas of risk to the Council's objectives. Internal audit supports this objective through a mix of audit and advisory pieces of work.

8.9.2. In 2010/11 internal audit completed 55 audits, ten advisory reports, and four grant claims. These figures exclude the information technology and schools audit conclusion reported separately below. For the 55 reviews resulting in an internal

audit opinion, 52 (95%) received a positive (substantial or satisfactory) level of assurance. This compares to 70% for the prior year.

8.9.3. In addition, internal audit are regularly invited to sit on project boards to advise on possible areas of risk and control for management to consider in the design and implementation of new systems and processes. This work is important to managing the risk of control weaknesses being identified post-implementation when they will be harder and more expensive to correct.

8.10. Information technology

8.10.1. As part of the internal audit contract, the Council retains the services of Information Technology (IT) experts to assist on specialist audits of the Council's IT systems. These experts supported the work of internal audit throughout the year by regularly attending internal audit and IT project meetings and led on eight IT focused internal audit and advisory pieces of work. Of these five received a positive (substantial or satisfactory) level of assurance.

8.10.2. A significant area identified for control improvements was that of information governance. The control risks relate to behaviours and processes as much as the systems themselves. This has been acknowledged by management and incorporated in the Annual Governance Statement.

8.11. Schools

8.11.1. The schools are audited using a three year rolling plan, adjusted for emerging risks and changes to school circumstances (for example, creation of an Academy). During the course of 2010/11 the Department for Education withdrew the FMSiS and related audit requirements. Improving the standard of internal control in schools has been a priority in previous years and strong improvements have been achieved.

8.11.2. From the internal audit conclusions in 2010/11 these improvements have continued. Last year 23 of Lewisham's 80 schools were audited, with all but one (95%) receiving a positive (substantial or satisfactory) level of assurance. This compares to 2009/10 when 80% of schools audited received a positive assurance opinion. From these audits, all high and medium recommendations are followed-up to evidence implementation of agreed control improvements.

9. Anti-fraud and corruption

9.1. In addition to internal audit services, Audit & Risk is responsible for managing fraud investigations across the Council. This work is conducted by the Anti-Fraud and Corruption Team (A-FACT).

9.2. The anti-fraud work in the Council arises from the need for it to ensure confidence in the administration of public funds. As part of which, it must be recognised that the undermining of public confidence that can result from the discovery of a fraudulent or corrupt act can inflict a much greater damage than the act itself.

9.3. To put this risk in context, the level of fraud against the London Borough of Lewisham can be estimated at £33m based on National Fraud Association figures for Local Government. The work of A-FACT is split into four areas the activities for which are summarised below.

9.4. Benefits investigations

9.4.1. During the year to March 2011 the Benefit Investigation Team has secured 181 sanctions against an annual target of 180. The total value of fraudulent benefit overpayments identified was £846,022.

9.4.2. The Benefit Investigation Section also investigate allegations of non-receipt of Housing Benefit cheques. When a Benefit claimant reports the non-receipt of a cheque which has been cashed the team investigates the circumstances of the encashment prior to reissuing payment. In the last year the team has taken action in the seven.

9.4.3. On recovery these amounts represents a saving to the public purse. As the table below shows the team's productivity continues to improve

Year	No of referrals received	No. of closed cases	No. of o/s cases at year end	No. of Sanctions	No of sanctions per officer	Value of fraudulent over payment
2006/07	711	434	568	149	16	£359,404
2007/08	469	483	554	164	18	£455,773
2008/09	561	761	354	159	23	£450,569
2009/10	548	486	416	143	20	£651,827
2010/11	591	626	381	181	25.8	£846,022

9.4.4. The sanctions figure is made up of 23 Administrative Penalties, 137 Cautions and 21 Prosecutions. In the case of the Administrative Penalties a financial penalty of 30% of the overpaid benefit must be paid by the claimant. The total amount of the Administrative Penalties levied in 2010/11 was £32,923.

9.5. Housing investigations

9.5.1. The team's Housing Investigation Practitioner investigates allegations of Housing and Homelessness Application Fraud and Cash Incentive Scheme payments against the London Borough of Lewisham. The investigation of tenancy fraud has been the responsibility of Lewisham Homes since October 2008.

9.5.2. During the year to the end of March 2011 60 cases were passed for investigation, a similar amount to last year. The officer dealing with these cases completed 47 cases compared to 35 cases last year. There are currently 72 cases under investigation.

9.5.3. Of the 47 cases that were completed 16 resulted in successful outcomes ranging from false Homelessness applications being cancelled, through Housing Register application being withdrawn, to sub-let tenancies being recovered.

9.6. Special investigations

9.6.1. During the year to March 2011 the Special Investigations section received 250 new allegations or enquiries relating to fraud and/or irregularity.

2010/2011 Special Investigations Cases				
Year	Balance	New	Closed	Balance
2007/08	98	92	89	101
2008/09	101	88	109	80
2009/10	80	187	168	97
2010/11	97	250	213	134

9.6.2. During this period the section completed 213 cases/enquiries. A further 134 cases are still in progress. These figures include Lewisham Homes cases but exclude pre-employment checks undertaken.

9.6.3. By far the biggest area of work this year has been with employee related fraud. Within the Council 41 employee related cases were investigated involving 44 people. Of these twenty have concluded with action being taken ranging from disciplinary action up to and including dismissal.

- 9.6.4. A-FACT has been undertaking a significant amount of work for Lewisham Homes under our SLA in the past year. We have concluded 24 investigations, including probity checks on staff and members of the board. A number of complex investigations are still ongoing and will be reported as they are concluded.
- 9.6.5. A-FACT supports Human Resources by undertaking a part of the recruitment checks. Each potential employee of the Council is required to complete a pre-employment form which focuses on any issues relating to benefits, council tax, rent and personal business interests which may put the individuals integrity in doubt. In the year to March 2011 279 checks on staff were undertaken. This compares to 443 in the previous year. These checks identified one case where the applicant was not eligible to work in the UK and twelve cases where arrangements were made to pay off rent or council tax arrears.
- 9.6.6. Other successful activities in the year include eight out of ten Blue Badge fraud investigations, support and information on four attempted cheque and bank account frauds, use of the Proceeds of Crime Act powers to support our own work and that of another London Borough to recover assets, and a range of other alleged frauds ranging from referrals from other organisations to corporate credit card fraud.
- 9.6.7. The team also has a Detective Constable on secondment from the Metropolitan Police who contributes and enhances the work of A-FACT by providing advice, assistance and applying Police powers where appropriate. His access to Police systems and intelligence has proved invaluable. He is currently working on a number of complex cases and was key to four of the prosecutions undertaken this year.

9.7. Fraud prevention

- 9.7.1. A-FACT supports internal audit in promoting a strong internal control environment with clear controls and procedures, manages a fraud hotline (important as the majority of referrals come from tip-offs), works with Legal to maintain the fraud and whistle blowing policies and reporting lines, and undertakes data matching, training and promotion of anti-fraud successes.
- 9.7.2. A-FACT responded to 34 requests for information from other agencies to assist with fraud enquiries under the Data Protection Act. In addition the team's Intelligence Officer responded to 1,287 requests for information. These requests were primarily from the Police, Department for Work and Pension, other local authorities and Central Government departments such as UK Borders Agency and HM Revenue & Customs. This is up slightly in the number of requests conducted last year.
- 9.7.3. A-FACT has continued to publicise successful cases in the local press and has also received national television coverage on two episodes of the BBC programme Saints and Scroungers. Feedback from all coverage has been positive. We are also undertaking work with Trading Standards in connection with counterfeiting offences.
- 9.7.4. During the year A-FACT provided training focussing on frontline staff, especially in the area of document verification. This has been aimed at Human Resources, the Housing Options Centre, and Lewisham Homes staff. General fraud awareness training has also been provided to the Lewisham Homes Board of Directors.

10. **Risk management**

- 10.1. The Council has a risk management strategy and policy in place. It defines the roles and responsibilities of individuals, directorates and groups, and sets out how the risk management process will be embedded. The strategy and policy were revised in 2010/11 and approved by the Internal Control Board and Audit Panel.

- 10.2. The Mayor and Cabinet and Members are appraised on risk management monthly via the monthly management report. The monthly management report clearly maps risks to the Council's priorities and provides a narrative on changes to existing or emerging key (red) risks.
- 10.3. During 2010/11 the Council's internal audit service undertook their annual risk maturity review of the arrangements in place and their operation. This confirmed that Lewisham has maintained its rating of 'Risk Managed'. This is the second highest level on the Institute of Internal Auditors five point scale.
- 10.4. The Council continues to build on its approach to risk management, improving the quality of reporting on risks to the Executive Management Team and Internal Control Board. While arrangements are strong at the Corporate and Directorate levels a review of operational risk registers identified that practices were not always consistent at the operational level. This is an area for training and improvement.
- 10.5. Evidence for the effective mitigation of identified risks and related focus on strengthening the organisation's internal controls comes from a number of sources. In addition to the work of internal audit these include:
 - reports on the Council's services by other inspectorates (such as the Audit Commission, Care Quality Commission, OFSTED),
 - pieces of commissioned consultancy support (for example, review of preparedness of carbon reduction plans, procurement experts on the Leisure contract), and
 - management assurances (using specialist skills such as those of the counter-fraud, health & safety and insurance teams as well as performance management and exception reporting on core activities).

11. Compliance with the code

- 11.1. The Chartered Institute for Public Finance and Accountancy's Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 (the CIPFA Code) is a non-statutory code. However, the new Accounts and Audit (England) Regulations 2011 statutory instrument, requires the Council to "undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control". Internal audit is therefore required to comply with the CIPFA Code.
- 11.2. The internal audit service is overseen by the Head of Internal Audit & Risk supported by a contract manager. The service is provided by an external contractor, RSM Tenon. They are a regulated firm approved to provide audit and accounting services. As such they adhere to the industry good practice standards and have a good quality control mechanism. This involves an internal quality review of all audit reports, including comprehensive working papers, and ongoing supervision, training and appraisal of staff.
- 11.3. The Accounts and Audit (England) Regulations 2011 further require that the Council, "must at least once in each year, conduct a review of the effectiveness of its internal audit". In 2009/10 this requirement was met in three ways; self-assessment, peer review and an external review. All three reviews confirmed that internal audit complies with the requirements of the code.
- 11.4. For 2010/11 the internal audit arrangements were reviewed by the Head of Audit & Risk. No significant changes have been made to the working practices and delivery of internal audit services. The work of the internal audit team continues to be subject regular monitoring meetings with the contractor – RSM Tenon – and the Council's

external auditors, and results of their work and progress with the implementation of recommendations reported to the Internal Control Board and Audit Panel quarterly.

12. Legal Implications

12.1. There are no legal implications arising directly from this report.

13. Financial Implications

13.1. There are no financial implications arising directly from this report.

14. Equalities Implication

14.1. There are no specific equalities implications arising directly from this report

15. Crime and Disorder Implications

15.1. There are no specific Crime and Disorder implications arising directly from this report

16. Environmental Implications

16.1. There are no specific environmental implications arising directly from this report

17. Background Papers

17.1. Internal audit and A-FACT papers to the Audit Panel through 2010/11

If there are any queries on this report please contact the Head of Audit & Risk on 020 8314 9114.