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| Title of meeting: | Governance & Audit & Standards Committee |
| Date of meeting: | 1 st July 2016 |
| Subject: | Annual Internal Audit Report for the 2015/16 Financial Year |
| Report by: | Chief Internal Auditor |
| Wards affected: | All |
| Key decision: | No |
| Full Council decision: | No |

1. Summary

- 1.1 In 2015/16 Internal Audit raised 1 Critical Risk exception, which has since been resolved. A further 4 audits have been given no assurance since the last meeting and are detailed in Section 6. This brings a total of 11 no assurance audit opinions for 15/16.
- 1.2 The final audit plan contained 78 full audits and 39 follow up audits. 100% of the revised 2015/16 Audit Plan has been completed.
- 1.3 In addition to the planned audits there are 11 areas of on-going work and 4 continuous audits which contribute to risk assurance.
- 1.4 Areas of Assurance are shown in Appendix A.
- 1.5 During 2015/16 Audit carried out 120 days for external clients across four client groups.
- 1.6 A total of £351,006 has been raised in overpayments relating to Housing and Council Tax Benefit and Council Tax Support frauds following 192 investigations and 60 implemented sanctions. Further details are provided in section 9

2. Purpose of report

- 2.1 This report is to give the Annual Audit Opinion on the effectiveness of the control framework, based on the Internal Audit findings for 2015/16 and highlight areas of concern.
- 2.2 To advise Members of the Audit Plan for 2016/17.
- 2.3 To provide a summary of the Counter Fraud cases investigated and sanction results.

3. Recommendations

- 3.1 That Members note the Audit and Counter Fraud Performance for 2015/16.
- 3.2 That Members note the highlighted areas of control weakness from the 2015/16 Audit Plan
- 3.3 Members note the Annual Audit Opinion on the effectiveness of the system of internal control for 2015/16.
- 3.4 Members endorse the Audit Plan for 2016/17
- 3.5 Consider any additional actions to be taken in response to matters raised within this report relating to the reviews undertaken.

4. Background

- 4.1 The Annual Audit Plan for 2016/17 has been drawn up in accordance with the agreed Audit Strategy approved by this Committee on 29th January 2016 following consultation with Directors and the previous Chair of this Committee. The Plan will be revised quarterly to take account of any changes in risks/ priorities, in accordance with the Strategy.
- 4.2 From the 1st April 2015 officers within PCC's Benefit Counter Fraud Team moved across to Internal Audit, pending the transfer of Housing Benefit cases only to the Department of Works & Pensions (DWP) as part of the Governments 'Single Fraud Investigation Service' initiative.
- 4.3 This transfer occurred on 1st September 2015, however existing joint DWP cases were still progressed until PCC's statutory powers under Social Security Administration Act 1992 to investigate were removed on 31st March 2016.
- 4.4 Nominated PCC staff within Audit and Counter Fraud still hold specific powers in order to investigate Sub-Letting and Council Tax Support Fraud. These include Social Housing Fraud Act 2013 and Council Tax Reduction Schemes (Detection of Fraud & Enforcement) Regulations 2013 / Local Government Finance Act 1992.

5. Audit Plan Status 2015/16

Percentage of the approved plan completed

- 5.1 100% of the annual audit plan has been completed. Appendix A shows the completed audits for 2015/16. Appendix B shows the completed follow up audits for 2015/16

The overall percentage figure is made up as follows:

- 78 (67%) new reviews where the report has been issued.

- 39 (33%) planned follow ups where the report has been issued

5.2 As requested by Members of the Committee a breakdown of the assurance levels on completed audits since the last meeting is contained in Appendix A. Where specific parts of the control framework have not been tested on an area (because it has been assessed as low risk for example) it is recorded as NAT (No Areas Tested) within the Appendix.

Reactive Work

- 5.3 Reactive Work undertaken by Internal Audit in 2015/16 includes:
- 21 special investigations (excludes Benefit and Council Tax Support cases)
 - 69 items of advice, (where the advice exceeds an hours work)

As well as the following unplanned reviews

- Channel Shift Programme
- Disposal of goods found within abandoned garages
- Community Capacity Grant
- City Deal grant
- Contract Procedure Rules update
- Cash Handling Instructions update
- External marketing and presentations
- Contract Issues Adult Social Care

Exceptions

- 5.4 Of the 2015/16 full audits either completed or at the draft report stage the number of exceptions within each category have been:
- 1 Critical Risk
 - 102 High Risk
 - 34 Medium Risk
 - 10 Low Risk (Improvements)

5.5 The table below is a comparison of the audit status figures for this financial year and the previous two years

| | 2013/14 | 2014/15 | 2015/16 |
|---|----------------|----------------|----------------|
| % of the audit plan completed | 99% | 100% | 100% |
| No. of Audits Completed for the year | 143 | 150 | 116 |
| No. of Critical exceptions* | 18 | 11 | 1 |
| No. of High risk exceptions | 215 | 186 | 103 |

5.6 In order to provide a more meaningful comparison the table below reflects the audit figures excluding schools and follow up audits. Due to the nature of the

testing conducted during school audits they can result in a high number of exceptions being raised. The average number of high risk exceptions per audit is in brackets

| | 2013/14 | 2014/15 | 2015/16 |
|--|----------------|---------------|---------------|
| No. of Full Audits Completed for the year | 120 | 85 | 76 |
| No. of Critical exceptions | 9 | 11 | 1 |
| No. of High risk exceptions | 129 (1.075) | 91 (1.071) | 98 (1.289) |

Whilst there has been a decrease in the number of critical risk exceptions raised in 2015/16 the number of high risk exceptions per full audit has increased over the previous two years.

Ongoing Areas

- 5.7 The following 11 areas are on-going areas of work carried out by Internal Audit;
- Regulation of Investigatory Powers Act (RIPA)- authorisations
 - Anti-Money Laundering monitoring and reporting
 - Investigations
 - Financial Rules Waivers
 - National Fraud Initiative (NFI) to facilitate national data matching carried out by the Cabinet Office
 - National Anti-Fraud Network (NAFN) bulletins and intelligence follow up
 - Counter Fraud Programme
 - Policy Hub project to ensure that all Council policies are held in one place and staff are notified of the policies relevant to them
 - G&A&S Committee reporting and attendance and Governance,
 - Audit Planning and Consultation
 - Risk Management

Continuous Audit Areas

- 5.8 The following 4 areas are subject to continuous audit (i.e. regular check to controls) and feed into overall assurance;
- Legionella Management
 - Asbestos Management
 - Key risks management in services
 - Performance Management

6. Areas of Concern

Updates

- 6.1 **Security & Reception Arrangements - Resolved**

- 6.1.1 The original audit resulted in a critical risk exception being raised as during observations in the ground floor area 5 confidential conversations were conducted in a public area. This presented a risk of non-compliance with the Data Protection Act which could have resulted in a fine and reputational damage for the Authority.
- 6.1.2 An action was agreed whereby a corporate communication was sent to all staff reminding them of the risks associated with conducting confidential conversations in a public area.
- 6.1.3 Follow up testing was conducted confirming that the communication had been sent out as agreed. Further observations were undertaken and it was noted that staff seeing visitors for ad-hoc appointments were using meeting rooms where available and taking their visitors away from earshot to conduct the appointment. As a result the exception has been closed.

6.2 **Domiciliary Care - Unresolved (Risk Accepted)**

- 6.2.1 The 2014/15 audit of this area was given a no assurance rating as testing found that there was no mechanism in place to identify if providers were over invoicing for the care provided and were not being challenged where the actual time spent with clients was less than the planned and billed time. This presented a financial risk and an operational risk that clients are not receiving the full care they need.
- 6.2.2 An action was agreed to send a letter to all providers to advise them that sample checking will require them to investigate and provide assurance that care needs have been met. 5% checks on invoices were also set to continue.
- 6.2.3 Follow up testing was undertaken on Quarter 1 returns which showed that out of 10 providers 4 were 77 hours under the contracted amount. Using the 5% checks undertaken during October - December 2015 the projected overspend in this area was £10,043
- 6.2.4 Adult Social Care and the Integrated Commissioning Unit are due to work together to implement a partnership approach to commissioning and managing domiciliary care providers based on active monitoring. This is still in an embryonic stage and until it is implemented the risk has been accepted by management.

6.3 **Mainland Marketing Distributions Shipping Ltd (MMD) - Invoicing for Terminal Services - Part Resolved**

- 6.3.1 The 2014/15 audit in this area highlighted 4 high risk exceptions and was given a no assurance rating.
- 6.3.2 The 4 high risk exceptions related to:
- Too much reliance on one member of staff for the invoicing process
 - Incorrect charges being raised
 - Additional charges allowable by under the contract were not being raised

- Discrepancies between ships manifests and the shed list

These exceptions all presented a financial risk that MMD was not maximising its income which directly affects the profitability of the company.

6.3.3 Follow up testing confirmed that the exceptions relating to the incorrect charges and discrepancies between the manifests and shed lists have been closed. Progress has been made with regard to the invoicing process with the final actions due to have been completed in May 2016. MMD have brought in software that will allow them to start charging for container storage, it is hoped this will be implemented in June 2016. Charges for pallet storage should be implemented from October 2016.

6.4 **Management of Markets - Unresolved**

6.4.1 The 2014/15 audit of this area highlighted 4 high risk exceptions and was given a no assurance rating.

6.4.2 The 4 high risk exceptions related to:

- Lack of documented strategy for the management of markets. Without a strategy the Authority may not be maximising income in this area.
- Failure to complete adequate checks on stall holders were compliant with their contractual obligations in relation to fire and electrical safety. This presents a reputational and legal risk should any accidents or issues arise
- Poor record keeping over which traders had been allocated pitches. This could result in a financial loss if fees are not allocated correctly.
- Failure to monitor the collection of pitch fees. This presents a risk of fraud as pitch fees could be stolen by the market inspectors.

6.4.3 Follow up testing found that all 4 exceptions were still open. There is currently a wider review being undertaken as to how markets are managed within the city. The City Centre Management team is also in the process of being restructured. Once the new structure has been confirmed work will begin immediately to resolve the outstanding issues highlighted by the audit. This is expected to be carried out by 31st August 2016.

6.5 **Events (Part of the 16/17 planned work) - Unresolved**

6.5.1 The 2015/16 audit of this area highlighted 7 high risk exceptions and was given a no assurance rating. A follow up audit was carried out in May 2016.

6.5.2 The 7 high risk exceptions related to:

- Lack of clear procedures for processing event applications. Without these there is a risk to the authority that health and safety requirements may be overlooked and potential risks may not be included in assessments and insurance requirements
- Inconsistency in the event application process and information provided. This could lead to health and safety oversights which may damage the Authority's reputation and see a reduction of number of events subsequently held in the city

- A lack of clear audit trail regarding fees and charges. This could result in a financial loss to the authority if fees are being undercharged.
- Risk assessments not being carried out or being undertaken after the event. Failure to undertake adequate risk assessments could lead to people attending the event being put at risk of injury. This could result in significant reputational damage for the Authority
- Failure to comply with insurance requirements. Testing was unable to evidence that the £5m public liability cover required, was in place for 13 of 25 events sampled. As a result the Authority would be liable for any injury or claim that occurred at these events.
- Security arrangements, testing found that the same company was being used without a corporate contract or waiver being in place. This is a breach of PCC's contract procedure rules and risks the Authority not receiving value for money on the service.
- Lack of monitoring at events for example confirming food stalls hold a valid hygiene certificate or inflatables comply with the relevant standards. Failure to undertake these checks could put members of the public at risk of injury.

6.5.3 Following up testing found that 5 of the 7 agreed actions had been completed. The 2 areas where the risk remains are:

- Applications - The Events Team are moving to an online application system which at the time of the follow up was in the testing phase. It is expected that the system will go live from July 2016
- Monitoring - spot checks are still being undertaken at Events to ensure they are being held in line with their applications. The new online application process will allow the Events Team to get a better overview of the event and deal with any concerns or queries.

6.5.4 A new audit opinion of "reasonable assurance" was given as a result of the follow up. No further follow ups are planned in this area

New Areas of Concern

6.6 Through Care Team

6.6.1 The audit of the Through Care Team was given no assurance as 5 high risk exceptions were raised.

6.6.2 The exceptions related to the following areas:

- Failure to have the required Pathway Plan in place for relevant young people
- The late completion of young people's Leaving Care Assessments of Needs
- Care leaver's grants being overpaid or issued twice
- Inadequate record keeping in relation to care leaver grant logs
- Transaction logs maintained by the Through Care Team not reconciling with Finance records.

These represent financial risks if funds are not being properly managed and accounted for. There are also operational risks surrounding the young people and the support they are receiving.

- 6.6.3 The following actions were agreed to mitigate these risks:
- The Pathway Plan template and process has been reviewed. Monthly reports will now be produced
 - The Leaving Care Assessment has been replaced with a single assessment for all 16 to 18 year olds
 - The Through Care Team are working with Finance to introduce pre-paid cards for the care leavers to improve the record keeping and control over the Authorities funds.

6.6.4 These will be followed up as part of the 2016/17 audit of this area.

6.7 **Accounts Receivable**

6.7.1 For the past 3 financial years an exception has been raised as part of the Accounts Receivable audit regarding the lack of controls over the authorisation of credit notes. Testing during the 2015/16 audit confirmed that the risk had yet to be mitigated and as such has been given no assurance. Without proper authorisation controls there is the risk that credit notes could be raised fraudulently resulting in a financial loss to the Authority.

6.7.2 The current reporting function of Oracle E-Business Suite does not produce an adequate report in order for credit notes to be monitored. In the interim the Income and Payments Manager will undertake spot checks on a random sample of credit notes to mitigate the risk.

6.7.3 This will be followed up in the 2016/17 audit of Accounts Receivable.

6.8 **Mainland Marketing Distributions Shipping Ltd (MMD) Main Accounting**

6.8.1 The audit of MMD Main Accounting was given no assurance as testing confirmed that there is currently no mechanism in place to monitor user access levels and privileges within the Navision accounting system. This was originally raised during the 2012/13 audit of MMD Accounts Receivable. The risk of fraud is high as functionality within Navision includes the ability to amend payee details. Staff may also be able to circumvent segregation controls with multiple access rights.

6.8.2 A further audit of MMD Accounts Receivable forms part of the 2016/17 Audit Plan. The risk will be followed up as part of that review with a view to using data analytics software to gain greater understanding of the risk exposure.

7. Annual Audit Opinion

- 7.1 Due to the number of critical and high risk exceptions raised against the work carried out the Audit opinion for 2015 /16 is that only limited assurance on the effectiveness of the control framework can be given.
- 7.2 There are now four audit opinion levels as agreed in the 2016/17 Audit and Counter Fraud Strategy and these are: no assurance, limited assurance, reasonable assurance and full assurance. Where there are mainly medium or low risk exceptions the annual audit opinion would be reasonable or full assurance.
- 7.3 The Audit opinion for last year was also limited assurance due to the level of critical and high risk exceptions. There is still a significant level of high risk exceptions raised this year and in addition to this there has been an increase in the number of investigations that have involved staff.
- 7.4 Internal Audit is concerned that the overall effectiveness of the control framework position has declined/not improved in recent years, which is not adequately reflected in the 'limited assurance' and will continue to work with Directors, the Deputy Chief Executive and the Chief Executive to improve on specific areas of control and risk management weaknesses.
- 7.5 Any significant corporate weaknesses and agreed actions will be reflected in the Annual Governance Statement. The impact of the Internal Audit work for 2015/16 may affect that year's work for External Audit. It may also inform their work for 2016/17 and where they consider there are weaknesses in control that could materially affect the accounts they may need to carry out further work to gain the necessary audit assurance required for a true and fair view of the financial position and compliance with professional codes of practice.
- 7.6 Internal Audit has carried out a self-assessment and confirms that they are compliant with the Public Sector Internal Audit Standards (PSIAS).

8. 2016/17 Audit Plan

- 8.1 The Audit Plan planned coverage for 2016/17 has been drawn up using the Strategy approved by Members of this Committee at their 29th January 2016 meeting.
- 8.2 Meetings have been held with all Directors and the Chief Executive and the previous Chair of the Governance & Audit & Standards Committee who have all been consulted on the areas planned and the overall Audit Plan.
- 8.3 The 2016/17 Audit Plan is attached as Appendix C to this report. There are currently 111 Audits & 27 Follow up Audits identified although this will increase once preliminary audit work commences on areas such as contracts and grants which are currently undetermined. In addition to this a quarterly review will be

carried out to take account of changing risks & priorities, all of which will be reported back to this Committee.

8.4 As at the 6th June 2016 242 days have been purchased by external clients for Internal Audit work, this is an increase of 122 days from the previous year.

9. Counter Fraud Performance

9.1 Below is a table summarising the work completed by the Corporate Counter Fraud Team during 2015/16

| Case Type | Number Cautioned | Number Prosecuted | Admin Penalty | Sanctioned Fraud Overpayment | Total Overpayment Raised |
|---------------------|------------------|-------------------|---------------|------------------------------|--------------------------|
| Housing Benefit | 26 | 17 | 5 | £182,333.64 | £304,164.13 |
| Council Tax Support | 22 | 10 | 2 | £26,123.46 | £41,389.36 |
| Council Tax Benefit | 0 | 0 | 0 | £2359.95 | £5453.10 |

9.2 A caution is a warning given in certain circumstances as an alternative to prosecution to a person who has committed an offence. A caution can only be considered when there is sufficient evidence to justify instituting criminal proceedings and the person has admitted the offence during an Interview under Caution.

9.3 An administrative penalty: is an alternative to prosecution and only applies where it appears to the Secretary of State and/or a local authority that the making of an overpayment was attributable to an act or omission by the claimant and that there are grounds for instituting proceedings for an offence.

9.4 The administrative penalty is payable in addition to any recoverable overpayment. The Department for Work and Pensions are now responsible for issuing Administrative penalties relation to Housing Benefit.

9.5 A Caution and Administrative penalty can only be offered where the Local Authority has established sufficient evidence to prosecute. These sanctions are offered as an alternative to prosecution but the claimant is not obliged to accept and may decide to proceed to court.

9.6 A sanctioned overpayment relates to cases that have either been cautioned, prosecuted or have had an administrative penalty applied, i.e. an offence was

identified. The total overpayment contains an element of cases where no offence has been identified.

9.7 The total value of the 7 administrative penalties was £6638.53. Investigations into sub-letting also resulted in 6 properties being recovered.

9.8 Overall 246 cases were referred to the Counter Fraud Team during 2015/16 of which 192 (78%) were investigated following a risk assessment on the intelligence received. This resulted in 60 sanctioned cases (31%). The breakdown of the sanctioned cases is as follows:

- 21 prosecutions
- 32 cautions
- 7 administrative penalties

10. Equality impact assessment (EIA)

10.1 The contents of this report do not have any relevant equalities impact and therefore an equalities assessment is not required.

11. Legal Implications

11.1 The City Solicitor has considered the report and is satisfied that the recommendations are in accordance with the Council's legal requirements and the Council is fully empowered to make the decisions in this matter.

11.2 Where system weaknesses have been identified he is satisfied that the appropriate steps are being taken to have these addressed.

12. Finance Comments

12.1 There are no financial implications arising from the recommendations set out in this report.

12.2 The S151 Officer is content that the progress against the Annual Audit Plan and the agreed actions are sufficient to comply with his statutory obligations to ensure that the Authority maintains an adequate and effective system of internal audit of its accounting records and its system of internal control.

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Signed by: Elizabeth Goodwin, Chief Internal Auditor

Appendices:

Appendix A – Completed audits from 2015/16 Audit Plan

Appendix A - Municipal Year 201516

Appendix B - Completed follow up audits from 2015/16 Plan

Appendix C - 2016/17 Audit Plan

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

| Title of document | Location |
|---|---|
| 1 Accounts and Audit Regulations | http://www.legislation.gov.uk/uksi/2011/817/contents/made |
| 2 Previous Audit Performance Status and other Audit Reports | Refer to Governance and Audit and Standard meetings – reports published online http://democracy.portsmouth.gov.uk/ieListMeetings.aspx?Committeeld=148 |

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by on

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Signed by: