

<b>Report to</b>	Audit committee 23 July 2013	<b>Item</b>
<b>Report of</b>	Head of internal audit and risk management, LGSS	<b>9</b>
<b>Subject</b>	Annual audit report on internal audit and fraud 2012-13	

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## **Purpose**

To inform members of the head of internal audit's annual audit opinion for 2012-13 and the work of internal audit and the fraud team which supports the opinion. The report forms part of the evidence to support the council's annual governance statement.

## **Recommendation**

To receive the annual audit opinion and note the work of internal audit and the fraud team for 2012-13.

## **Corporate and service priorities**

The report helps to meet the corporate priority Value for money services

Ward/s: All wards

Cabinet member: Councillor Waters – Deputy leader and resources

## **Contact officers**

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## **Background documents**

# Report

## Background

1. *“Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes”* (Public Sector Internal Audit Standards).
2. Under the Accounts and Audit Regulations 2011, the council must 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.
3. The guidance accompanying the regulations states that proper internal audit practices are those contained within the *CIPFA Code of Practice for Internal Audit in Local Government in the UK 2006*.
4. In 2012 the relevant internal audit standard setters adopted a common set of standards across the public sector – the *Public Sector Internal Audit Standards* (PSIAS), which came into effect on 1 April 2013.
5. Both old and new codes require the head of internal audit to deliver the annual internal audit report and opinion which is timed to support the council’s annual governance statement.
6. This annual report being presented to members incorporates:
  - The overall opinion
  - A summary of the work that supports the opinion
  - Conformance with the relevant internal audit standards
  - The work of the fraud team in 2012-13

## Audit assurance work

7. From the 2012-13 audit plan 22 audits either had final reports issued or the audit involvement is complete. Another nine are at draft report stage or nearing completion. Three have been slipped into 2013-14.
8. The following is a summary of audit assurance work undertaken in 2012-13. It shows the assurance levels, or other description where an assurance opinion was not appropriate, of all audits undertaken in 2012-13, including those at draft report stage and 2011-12 reports completed in 2012-13:
9. Full assurance:
  - Payroll
10. Good assurance (or equivalent):
  - National non-domestic rates (NNDR)
  - Homelessness

- Housing voids
- Members expenses – the system for paying members' allowances and expenses works well.
- Performance management - the framework for measuring and reporting performance works well

11. Moderate assurance (or equivalent):

- Housing rents / arrears
- Treasury management
- Housing and council tax benefits
- Council tax
- Planning income
- Off-street parking
- Sports facilities
- Oracle purchasing
- Care and repair contract
- HR starters and leavers
- Business continuity management – score of 63% against the standard, a slight improvement since the previous audit
- Academy IT system (housing)
- Oracle IT system (financial)
- Disaster recovery

12. Limited assurance:

- Accounts receivable. Delays in receiving a response to the draft report have been referred to in the draft annual governance statement
- Provision market

13. Unsatisfactory assurance

- Contract management procedures – citywide services
- Investment property portfolio

14. Further details of the significant findings from completed audits with less than 'good' assurance are as follows:

15. **Housing rents/arrears:**

Reconciliation of housing system to general ledger – variances had not been investigated.

Writing off debts – not all had been authorised at the appropriate level.

Recommendations agreed – some in place, remainder due for implementation by September 2013.

#### **16. Treasury management:**

There were some gaps with compliance to the code of practice, eg treasury management strategy and practices.

Reconciliations to the general ledger were not completed on a timely basis.

Procedure notes need updating.

Recommendations agreed – some in place, remainder due for implementation by December 2013.

#### **17. Housing and council tax benefits:**

Long delays between receipt of change of circumstances information and the information being processed, resulting in overpayments.

Writing off debts – not all had been authorised at the appropriate level.

Recommendations agreed and due for implementation by June 2013.

#### **18. Council tax:**

Some council tax discounts did not have end dates on the system.

Inconsistent handling of account amendments, depending on how the information is received.

Outstanding debt was remaining static due to resourcing issues.

There were no regular reviews of the suspense account.

Reporting of critical data relied on one key member of staff and would be at risk in their absence.

Recommendations agreed and due for implementation by July 2013.

#### **19. Planning income:**

There is no formal policy covering the refunding of fees.

Inconsistent use of income codes leading to possible miscoding.

No reconciliation between income received via the planning portal and the amount appearing on the general ledger.

Recommendations agreed and due for implementation by December 2013.

#### **20. Off-street parking**

The cash collection contract needed to be reviewed and retendered, also to include cash from other areas of the council.

The reconciliation of raw data from the pay and display machines needed improvement in terms of the audit trail.

Recommendations agreed – some in place, remainder due for implementation by July 2013.

#### **21. Sports facilities**

Improvement needed to method of recording data on use of facilities.

Review needed on the policy of selling season tickets.

There were no written policies or procedures.

Recommendations agreed and due for implementation by March 2013.

## **22. Oracle purchasing**

Training and guidance for users and authorisers could be improved.

Access levels and system facilities for procurement staff required reviewing.

Automatic creation of purchase order numbers had not been switched on.

Recommendations agreed – some in place, remainder due for implementation by March 2013. One recommendation is dependent on the planned upgrade of Oracle.

## **23. Care and repair contract**

The original contract needed to be retendered.

The contractor had been paid to register a number of decent homes loans with the land registry. No information on the decent home loans registered had been requested or received by the council.

Recommendations agreed and in hand - in fact the service has now been brought back in house from 1 July. (At the time of the audit follow up the information on loans registered had not been received, therefore this has been referred to in the draft annual governance statement.)

## **24. HR starter and leavers**

Evidence of qualification checks not held on files.

Induction process was being inconsistently applied by managers.

Inconsistencies regarding access to systems when someone goes on maternity leave.

No evidence that performance against the agency worker contract was being monitored.

Recommendations agreed – some in place, remainder due for implementation by April 2013.

## **25. Provision market**

Weaknesses in control processes relating to lack of strategic policy, lack of detailed procedures, public liability insurance, content of leases, rental basis.

The action plan resulting from the audit is substantially complete, with the remaining two actions in progress (see annex 1).

## **26. Contract management procedures – citywide services**

There was a lack of an effective control system for the contract manager to manage large value contracts.

No training linked to Oracle purchasing which would improve control over payments.

No formal contract procedures or database to help control large value contracts.

Recommendations agreed and due for implementation by March 2013.

## **27. Investment property portfolio**

Significant weaknesses in control processes relating to procedures, lettings and IT systems.

Function has since been transferred to NPS. A new management structure is in place and the action plan resulting from the audit is complete (see annex 1).

## **Audit opinion on individual audits**

28. The following describes the opinions that can be given for an audit:

29. Full assurance - There is a sound system of control designed to address the relevant risks with controls being consistently applied.

30. Good assurance - There is a sound system of control, designed to address the relevant risks, but there is evidence of non-compliance with some of the controls.

31. Moderate assurance - Whilst there is a basically a sound system of control, designed to address the relevant risks, there are weaknesses in the system, that leave some risks not addressed and there is evidence of non-compliance with some of the controls.

32. Limited assurance - The system of control is weak and there is evidence of non compliance with the controls that do exist which may result in the relevant risks not being managed.

33. Unsatisfactory assurance - Control processes are generally weak leaving the processes/systems open to significant error or abuse.

## **Follow ups**

34. The following audits have been followed up:

- Previous accounts receivable audit by KPMG – satisfactory progress on main recommendations
- National non-domestic rates 2011-12 - satisfactory progress on main recommendations
- Licensing – approximately half of the recommendations have been implemented. The remainder are dependent on completion of the licensing ‘green book’ policy review, which has been delayed.
- Investment property portfolio – since the audit the function has transferred to NPS Property Consultants. The estates director at NPS has provided a detailed update on progress against the action plan, which shows that all of the action points have been addressed.

## **Progress on action plan from 2011-12 AGS**

35. Members receive regular progress reports on actions taken to address significant audit findings, which were included in the annual governance statement 2011-12.

36. The issues, responses and progress to date are shown in **annex 1**.

37. As all the actions are either complete or being addressed no further updates are felt to be necessary.

## **Special investigations**

38. The team had an input into the following special investigations:

- Inappropriate access by a member of staff and others in the team to computer records of a family member. Dealt with via the disciplinary process. The investigation was the result of a whistleblowing allegation (the only allegation logged in 2012-13).
- Unauthorised disclosure of personal data (an email circulation list) caused by human error. A reminder was sent to all staff about how to minimise the chances of this happening again.
- The theft of cash from one of the council's leisure facilities. The employee was dismissed.
- The temporary loss of a package containing personal data whilst in transit. The package was retrieved unopened; following the incident guidance was circulated to all staff and procedures have been improved to prevent a recurrence.

## **Internal audit key performance indicators**

39. The following shows the key performance indicators in the service specification and the results for 2012-13:

- Internal audit plan to be endorsed by CLT and audit committee by 30th June each year - achieved. Plan for 2012-13 was endorsed by audit committee in March 2012 and the plan for 2013-14 was endorsed in March 2013.
- % of internal audit plan delivered – target 100%. Actual 91%. All but three audits had been scoped and started, with eight audits nearing completion, including at draft report stage.
- % of productive time achieved by the division against the total resource days available – target 85%. Actual productive time was 82% - this was affected by the team's accommodation move in 2012.
- Draft IA reports issued within 15 days of receipt of agreed management comments – achieved.
- Final reports issued within 10 days of receipt of management comments – achieved.
- Progress reports to audit committee 6 monthly - achieved. Progress reports are usually presented to every audit committee

## **Conformance with relevant internal audit standards**

40. The relevant standard for 2012-13 was the *Code of Practice for Internal Audit in Local Government in the UK 2006*.

41. An initial assessment against the code shows substantial conformance, with the main areas for improvement identified as training and development needs for individual team members, and further development of the quality assurance programme.
42. An assessment will be made against the new *Public Sector Internal Audit Standards* (PSIAS) to ensure that any areas needing improvement are identified and addressed in order to ensure that the standard is fully met.

## **Other areas of non-assurance work**

43. Other areas of non-assurance and consultancy work which were carried out in 2012-13 are as follows:
  - National fraud initiative (see below). The audit manager (Norwich) is the key contact for the exercise, and ensures that all data is correctly submitted and co-ordinates the proper investigation of the subsequent matches.
  - Preparation of the annual governance statement and supporting evidence.
  - Completion of the Audit Commission's annual fraud survey.
  - Maintaining, and reporting on, the corporate risk register. Delivered awareness training for managers on the updated risk management strategy.
  - Contractor financial appraisals.

## **National fraud initiative (NFI) 2011-12**

44. This is the council tax single person discount exercise which occurs in alternate years to the main NFI exercise (see below).
45. The results were made available in February 2012 and as with previous years Norfolk County Council agreed to the council's request to provide a temporary member of staff to assist with investigating approximately 1600 matches. There is no assumption of fraud just because a match appears in the results.
46. The exercise was completed in December 2012, and as a result of the actions taken discounts of over £93k were removed from 340 accounts.
47. In view of this successful outcome, Norfolk County Council agreed to provide the temporary member of staff to the end of March 2013 in order to review a sample of all single person discounts claimed, not just those identified by NFI. As a result of this review a further £12k of discounts were removed.

## **NFI 2012-13**

48. This is the main data matching exercise which occurs every two years. The results were received at the end of January 2013.
49. There are 72 reports, mainly covering benefits and housing, and 2,669 matches, of which the Audit Commission recommended 554 as a priority for investigation. The majority of matches relate to housing benefit. Staff in various departments have made good progress in reviewing matches to identify any further action that needs to be taken – to date 65% of reports and matches have been closed.



50. So far the exercise has uncovered one housing fraud which led to the recovery of a council property; and identified one duplicate payment for £2,474 made in error – however, this had already been picked up by the supplier and refunded.

## **Fraud team and counter fraud activity 2012-13**

51. The following sections summarise the counter fraud activity in the year 2012-13 by the fraud team, in conjunction with other council staff and staff from other organisations.

### **Continuing counter fraud initiatives**

52. In 2012-13 the council employed a temporary visiting officer to investigate unlawful subletting. Experience shared by another authority found that this was a good way to verify circumstances of people on the common housing register. A number were removed from the register where their circumstances had changed and they had failed to notify the council. This post has been so successful that the council has now made it a permanent position.

### **Liaison and joint working**

53. On a day by day basis the team works in partnership with the fraud section of the Department for Work and Pensions (DWP) on cases where there is a similar interest. This contributed to about 45% of the team's successful outcomes, which is consistent with the previous years return. However, due to a change in direction by the DWP (focussing on prosecutions over non-criminal sanctions) the majority of these cases were prosecution.
54. The team also works with other government departments to combat the threat of fraud, including the police, HM Revenue and Customs, UK Border Agency, the Security Industry Authority and other local authorities.

### **Training**

55. One fraud officer is also an accredited financial investigator under the Proceeds of Crime Act 2002. This has included successful cases within the fraud team, cases with private sector housing and also work for another Norfolk authority.
56. Fraud awareness training was provided to various sections of the council dealing with front-line and back of house services. As a result of these sessions, some staff asked for, and received, one-to-one fraud shadowing to give a more detailed understanding of the team's activities and to ensure better quality referrals.

### **Fraud team performance**

57. Proven fraud (for benefit purposes) is measured by the number of (non-criminal) sanctions and prosecutions achieved in a year. Sanctions are defined as simple cautions (a warning where an offence has occurred, but is less serious and court is not the first option) or an administrative penalty (similar to a 'caution', but the customer accepts a fine of either 30% or 50% (depending on the start date of the offence) of the overpaid benefit).

58. There were 641 benefit referrals in 2012-13 (771 in 2011-12), of which 480 required further investigation (577 in 2011-12). This needs to be noted in context that there are approximately 20,000 benefit claims in the area covered by Norwich City Council.
59. The team achieved 55 sanctions and prosecutions (106 in 2011-12), of which 38 were NCC led (57 in 2011-12). There are a number of factors related to the reduction, including one officer reducing her hours by 55%, the DWP changing their driver to concentrating on higher value cases, a dip in the number of referrals and one officer spending part of their time dealing with financial investigations.
60. The total overpaid benefit (including administrative penalties) for the 55 proven fraud cases was £266,203.70 (£265,280 in 2011-12) at an average of £4,840.06 per case (£2,503).
61. In addition to the benefit fraud cases, one customer was given a simple caution for a council tax discount offence and the team had direct input into the recovery of seven (five in 2011-12) council properties (four of which were the result of benefit fraud investigations).

## Overall audit opinion

62. The provision of assurance services is the primary role for internal audit in the UK public sector. The role requires the head of internal audit and risk management to report an annual internal audit opinion based on an objective assessment of the framework of governance, risk management and control.
63. Based on the available evidence as summarised in the annual governance statement, together with the results of internal audit work in 2012-13 and beyond, it is the opinion of the head of internal audit and risk management that **adequate assurance** can be given on the overall adequacy and effectiveness of the council's internal control environment. This is an improvement on the previous year's opinion, which resulted in limited assurance.

## LGSS internal audit assurance reviews – progress on recommendations

Significant issues	Response	Implementation Date	Progress as at July 2013
<b>Investment property portfolio:</b>			
Significant weaknesses in control processes relating to procedures, lettings and IT systems, resulting in an unsatisfactory assurance opinion	Recommendations accepted. However, following the transfer to NPS, timescales for completion of the actions will depend on the outcome of the new management structure.	Action plan to be updated by end July 2012	New management structure in place and action plan complete.
<b>Accounts payable:</b>			
Access to make changes to vendor data not sufficiently restricted and no independent authorisation or review of changes made. Inadequate segregation of duties between ordering, receipting and inputting invoices onto Oracle	Recommendations accepted. Access to be reduced and sample checking to be considered. Access levels to Oracle will be reviewed.	June 2012	Team leader now in place. Access to make changes has been restricted. Access levels currently being reviewed
<b>Council tax:</b>			
Recovery section not required to provide reporting on council tax arrears to senior management and no structured methodology on dealing with arrears reports and debt management.	Recommendations accepted. 1. The draft debt management policy will be approved and communicated to all relevant members of staff. We will also formulate a policy for the prioritisation of debt recovery procedures. 2. We will take action to address the backlog in the review of arrears.	September 2012	1. Policy approved by cabinet in December 2012  2. Procedures now in place as a result of the audit. The council tax team meet monthly to review outstanding arrears and debt management
<b>Procurement:</b>			
Key council policies/strategies relating to	Recommendations accepted. 1. We will update the council's	September 2012	1. Anti-fraud and corruption strategy agreed by CLT.

Significant issues	Response	Implementation Date	Progress as at July 2013
<p>counter-fraud are not regularly reviewed. In particular, the anti-fraud and corruption strategy does not reflect the Bribery Act 2010. The council's standing orders relating to contracts have not been updated since March 2008.</p> <p>The procurement team do not actively or consistently address the potential risks of supplier failure.</p>	<p>strategies at least every two years to ensure that they remain current and up to date. In particular, the anti-fraud and corruption strategy will be updated to reflect the Bribery Act.</p> <p>2. We will introduce detailed procurement procedures for quotations and tenders to support contract standing orders and circulate them to all relevant officers.</p> <p>3. The procurement team will identify and address the potential risks of supplier failure and the subsequent exposure of the council.</p>		<p>2. Contract procedure rules (standing orders) are being reviewed as part of the update of the constitution.</p> <p>A contract management framework is now in place. This will assist training needs to be identified and provided.</p> <p>3. The recently developed and approved business relationship and contract management strategy is accompanied by a contract management toolkit. Part of the toolkit is a monitoring sheet for contract managers relating the need to keep risk registers.</p> <p>The need to operate adequate risk processes, including resilience plans that embrace all the council's own requirements, is now included in all relevant service specifications published with tenders</p>
<b>Highways agency:</b>			
<p>48 members of staff have access to the council's penalty charge notice (PCN) database, including 33 staff who also have access to the council's cash receipting system</p>	<p>The cash receipting system needs to be available for all staff who can take payments, the council has set up a multi-tasking environment and this will need a corporate decision to change this and limit cash receipting to a selected few.</p> <p>In future, we will review access to the PCN database on at least an annual basis to ensure access granted remains appropriate</p>	April 2012	<p>Access rights reviewed recently and as a result access to the PCN database was removed for a number of staff</p>

Significant issues	Response	Implementation Date	Progress as at July 2013
<b>Provision market:</b>			
Weaknesses in control processes relating to lack of strategic policy, lack of detailed procedures, public liability insurance, content of leases, rental basis.	Recommendations accepted. An action plan to address the issues will be taken to CLT with a view to full implementation by March 2013	March 2013	The management plan for the market was taken to the business heads of service group in September 2012 and approved by the deputy chief executive (operations). 11 of the 13 actions are complete; the remaining two are in progress.
<b>Northgate revenues and benefits IT system:</b>			
There has not been a review of Northgate user access rights since 2008.	Recommendations accepted. We will ensure at least annual review of user access rights, in conjunction with the users' departmental managers, to ensure access rights are current and appropriate	April 2012	Complete. The administrator rights have been removed for the individuals concerned and an audit of all Northgate users has been completed
<b>Civica customer contact IT system:</b>			
The council does not obtain any assurance that controls performed by 'Civica' over information security and other IT activities are designed and operate effectively. There has not been a review of Civica user access rights since 2008. Staff outside of the customer contact team that use the Civica system are not routinely trained on how to use the system.	Recommendations accepted. 1. Management will seek to validate that critical third parties supplying IT services have a robust internal control framework. 2. We will ensure at least annual review of user access rights, in conjunction with the users' departmental managers, to ensure access rights are current and appropriate. 3. Access to Civica will only be granted once appropriate training has been received.	August 2012	1. NCC is discussing with Civica the potential for them to provide an ISAE 3402 report (independent report on the effectiveness of their internal control framework)  2. The privileged access rights have been removed for the individuals concerned and an audit of all Civica users is in progress  3. Managers will be instructed to discuss the mandatory e-learning data protection act course with new employees at the first one-to-one/probationary interview for completion by the second interview. HR will be asked to update their induction checklist accordingly. Awaiting response from head of HR and learning