Report to	Audit committee	**Item**

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23 June 2015

Report of Head of internal audit and risk management, LGSS

Subject Annual audit report on internal audit and fraud 2014-15

10

Purpose

To inform members of the head of internal audit's annual audit opinion for 2013-14 and the work of internal audit and the fraud team which supports the opinion. The report and the audit opinion within it form part of the evidence to support the council's annual governance statement 2013-14.

Recommendation

To receive the annual audit opinion and note the work of internal audit and the fraud team for 2013-14.

Corporate and service priorities

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

Ward/s: All wards

Cabinet member: Councillor Stonard – Resources and income generation

Contact officers

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Background documents

None.

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 2015, the council "*must 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.*"

3. 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.

4. The standards require that the head of internal audit presents an annual report to an authority's audit committee, which in practice is timed to support the authority's annual governance statement.

5. The annual report is a summary of all internal audit work carried out during the year. Each individual audit report is discussed at its draft stage and agreed action plans put in place. The annual report therefore represents in summary form a considerable degree of consultation with managers during the year.

6. Internal audit work is carried out to fulfil the audit plan, endorsed by the committee at its meeting on 11 March 2014 and since revised in consultation with the chief finance officer. The audit plan is derived from corporate and service risk registers as well as any inherent risks such as a susceptibility to fraud associated with an individual system. Internal audit work therefore seeks to give assurance that the risks identified in the registers and within the systems risk matrix are mitigated by a sound system of internal control.

7. This report provides members of the audit committee with:

   - the head of internal audit opinion for 2014-15;
   - an overview of the council's risk exposure and its overall system of internal control;
   - the work undertaken by internal audit in 2014-15;
   - review the outcomes from key internal audit reports;
   - an overview of the performance of internal audit;
   - the work of the fraud team in 2014-15.

INTERNAL AUDIT REPORT FOR 2014-15

Head of Internal Audit Opinion

8. This report gives a summary of the work carried out by internal audit in the financial year 2014-15 and the results of that work.   From the work undertaken during the year, my overall opinion on the council's system of internal control is that:

> Substantial assurance can be given that there is generally a sound system of internal control, designed to meet the council's objectives and that controls are generally being applied consistently. This is the same level of assurance that was assigned in 2013-14.
>
> Controls relating to key financial systems were concluded to be generally at a "Substantial" level.

9. The basis for my opinion is derived from an assessment of the range of individual opinions arising from assignments, contained within the internal audit risk-based plan that have been undertaken throughout the year. This assessment has taken account of the relative materiality of these areas and management's progress in respect of addressing control weaknesses. A summary of audit opinions is shown in the following table:

Table 1 – Summary of Audit Opinions 2014 - 15

Category	Full	Substantial	Moderate	Limited	No
Financial systems	2	7	0	0	0
Other audits	0	6	5	0	0
Total	2	13	5	0	0
Summary (with 13-14 comparison)	10% (8%)	65% (63%)	25% (21%)	0% (4%)	0% (4%)

(Includes 2013-14 audits finalised in 2014-15)

Review of Audit Coverage

Audit Opinion on Individual Audits

10. The committee is reminded that the following assurance opinions can be assigned for an audit:

Table 2 – Assurance Categories

Level of Assurance	Definition
Full Assurance	There is a sound system of control designed to address the relevant risks with controls being consistently applied.
Substantial 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.
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.
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.
No Assurance	There is no system of internal control. Risks are not being managed.

11. Audit reports issued in 2014 -15, other than those relating to investigations or project reviews, include one of the above audit opinions. Embedded assurance applies to projects / audits where auditors attended project boards or other working groups. Unless otherwise stated, all individual reports represented in this annual report are final reports and have been agreed with management, together with the accompanying action plans.

Audit assurance work

The status of 2014-15 audits is shown in Table 3 below:

Table 3 – Reports Issued 2014-15

Status	Number
2014-15 Final reports / embedded assurances completed to date	22*
Substantially complete, including at draft stage	8

* Includes 2013-14 reports finalised during 2014-15

12. Table 4 below details the assurance levels, or other description where an assurance opinion was not appropriate, of all audits reported on in 2014-15.

Table 4 – Summary of Audit Opinions 2014-15

Service / Audit	Audit Opinion / Description
Financial systems:	
Oracle Purchasing	Substantial
Payroll	Substantial
NNDR x 2	Full
Housing benefits	Substantial
Treasury and cash flow management	Substantial
Purchase cards	Substantial
Council tax	Substantial
Accounts Payable	Substantial
Corporate:	
Governance of shared services	Substantial
New bank contract	Embedded assurance
Business relationship management:	
Corporate information assurance	Embedded assurance
ICT audits:	
Civica (workflow)	Moderate
Northgate (revenues & benefits)	Moderate
Workforce (HR)	Substantial
Parking Gateway (permits)	Moderate
BACSTEL-IP (BACS)	Moderate
Regeneration & development:	
CIL income	Substantial
Strategy, people & neighbourhoods:	
Provision market	Moderate
Probity – income from street trading	Substantial
Customers, communications and culture:	
Managing customer demand	Substantial
Land charges	Substantial

13. Outlined below is a summary of the audits that have been finalised during the year where an assurance opinion of moderate has been given. These represent a summary of the findings for audits leading to:

- Red rated recommendations (action that is considered imperative to ensure that the council is not exposed to high risks); and / or

- Amber rated recommendations (action that is considered necessary to avoid exposing the council to significant risks).

14. The committee should note that the majority of these issues have previously been reported as part of the defined cycle of update reports provided to the audit committee. The purpose of this section of the report is to give assurance to the committee as to the effective progress being made to address the weaknesses identified within the individual reports.

Provision market – moderate assurance

15. There was assurance that stall holders are paying the correct rent as set out in their leases, plus service charges; debt levels are fairly static, with regular meetings held between the markets and sundry income teams to manage outstanding debts; and health and safety and insurance matters are mostly satisfactory. However, rents have not been reviewed for a number of years, and a few historical discrepancies were found between the rents charged and the rent according to the zoning system. In addition, although there are adequate arrangements for following up debts, progress on recovery is not summarised anywhere, which could cause difficulties in the absence of key staff. Finally, the market traders' handbook has not been updated for a while, and arrangements to ensure that existing stall holders have adequate public liability insurance need to be tightened. Eight recommendations were agreed, two of which are already in place. The remainder are due to be implemented by June 2015, and a follow up review has been scheduled for then.

Civica IT system – moderate assurance

16. Civica is the corporate document management and workflow system used by two thirds of council employees and it indirectly interfaces with other council application systems. There was assurance across most of the areas including input, processing and output controls; system interface controls; and backup and disaster recovery. However, there are no operational guidance notes for some of the modules; a possible upgrade had not been implemented; procedure manuals out of date; several major incidents logged. Management was already aware of the issues, and the system is in the process of being upgraded. Six recommendations were agreed, some of which are complete, while others are dependent on the system upgrade in June 2015. A follow up review has been scheduled for then.

Northgate IT system – moderate assurance

17. The Northgate system supports the back office operation of Revenue & Benefits processes. There was assurance across most of the areas including system administration procedures including roles and responsibilities; output controls; system interface controls; and backup and disaster recovery. However, procedure for recording changes to corporate systems is incomplete; the audit log functionality on Northgate is currently disabled and audit log information is not maintained on the system and some risks specific to application systems have not been identified. Five recommendations were made, three of which are complete. One finding was disputed by the service and management is currently considering its response. The audit log issue is complex and would require a significant commitment from LGSS and Norwich officers. Management is currently considering the risks and the options.

Parking Gateway IT system – moderate assurance

18. The Parking Gateway system is used to record, administer and progress all Penalty Charge Notices (PCNs) issued as part of the authority's on-and off-street

enforcement activities. The system supports the back office operation of Parking Services' processes and contains modules for processing and managing various operations in the department. There was assurance across most of the areas including system administration procedures; input and output controls; system interface controls; and backup and disaster recovery. However, the procedure for recording changes to corporate systems is incomplete; some documentary evidence for system upgrade testing is incomplete and procedure manuals not subsequently updated; incomplete audit logs; and some risks specific to application systems have not been identified. Five recommendations were agreed which are now complete.

BACSTEL-IP system – moderate assurance

19. BACSTEL-IP is the channel for accessing BACS electronic funds transfer services using the BACS payment service website or using the BACS approved software for BACSTEL-IP. There was assurance over accuracy and completeness of BACS output reports; management and monitoring information; and backup and business continuity procedures. However, Some BACS procedure documents are incomplete or out of date, and have not been consolidated into a single document; the benefits team does not check and authorise weekly benefits payment files that are created from the Northgate system; some of the authorised forms that were used to issue payment smartcard to officers could not be located; and inadequate segregation of duties in the BACS process for benefits payment file creation and transmission. Six recommendations were agreed which were due to be implemented by the end of December 2014. A follow up review has been scheduled for June 2015.

Other information assurance

20. In addition to the reviews referred to in paragraphs 16-19, the audit manager sits on the corporate information assurance group, which monitored progress to comply with public sector network (PSN) and payment card industry (PCI) compliance, both of which have now been achieved. The group also reviews network issues, data protection, information risk and assurance, security breaches, and information management.

Project work and special reviews

21. During 2014-15, internal audit has continued to be responsive to requests for support from managers in the completion of unplanned reviews and special investigations. The time required to complete these reviews has been accommodated in the plan by the time set aside for special investigations and the contingency element.

22. A member of audit was part of the project team set up to ensure a successful transfer of the council's bank account, following the decision by the Co-operative Bank to cease local authority banking.

23. Internal audit was not involved in any major investigations during the year. There were a small number of low-level data breaches which were reviewed by the executive head of business relationship management and democracy (as the council's senior information risk officer) and involved the audit manager, in accordance with the council's incident response plan. No cases led to any disciplinary action, but several actions were put in place to reduce the risk of recurrence.

Follow ups

24. Internal audit reviews are followed up to ensure that recommendations have been implemented; the results of each follow up are reported to audit committee. A summary of the status of significant recommendations from audits followed up, plus those previously shown as incomplete, is summarised in Table 5:

Table 5: Implementation of Audit Recommendations

	Red		Amber	
Audit Title	**Complete**	**Incomplete**	**Complete**	**Incomplete**
Planning income	1		2	1
Disaster recovery			2	
Parking Gateway IT system			5	
Purchase cards			1	
Norman Centre			1	
Emergency planning			3	
Pool cars				1
The Halls			1	
Council tax				1
NNDR			1	1
Housing benefits				
Sports facilities				
TOTALS	**1**	**0**		

Other areas of non-assurance work

25. Other areas of non-assurance and consultancy work which were carried out in 2014-15 are as follows:

- National fraud initiative (see below). The audit manager (Norwich) is the key contact for each year's data matching exercises, and ensured that all data was correctly submitted and co-ordinated the proper investigation of the subsequent matches.

- Prepared the annual governance statement and supporting evidence in conjunction with heads of service and CLT.

- Completed the Audit Commission's annual fraud survey.

- Maintained the corporate risk register in conjunction with heads of service and reported to CLT, audit committee and cabinet

- Updated the council's risk management policy for approval by cabinet.

National Fraud Initiative (NFI) 2012-13

26. This is the main data matching exercise by the Audit Commission which occurs every two years, the results for which were received at the end of January 2013.

27. There were 74 reports, mainly covering benefits and housing, and a total of 2,677 matches requiring possible investigation.

28. The majority of matches related to housing benefit, which were investigated during 2013-14 and 2014-15 by the fraud team. Staff in various service areas also continued to review other matches to identify any further action that needed to be taken. As a result **all** of the reports have now been closed.

29. The exercise uncovered one housing fraud which led to the recovery of a council property.

30. In addition, £166,518 of housing benefit overpayments was identified. Eleven cases totalling £79,221 were due to fraud, resulting in four prosecutions, five administrative penalties and two official cautions. 44 cases totalling £87,297 were due to either official error (19) or customer error (25). All the overpayments are recoverable by reductions in weekly benefits.

31. Finally, a duplicate creditor payment of £2993 from 2010 was identified. Following investigations by the audit manager and other council staff a full refund was received.

32. Audit committee receives regular updates on the status of NFI investigations.

National Fraud Initiative (NFI) 2014-15

33. The 2014-15 NFI exercise was in two parts. One was the council tax single person discount exercise which now occurs annually and separately to the main NFI exercise.

34. The results were made available in December 2014 and 2,533 matches were passed to the revenues & benefits operations manager to consider options for investigating; there is no assumption of fraud just because a match appears in the results.

35. The results from the main NFI exercise were made available at the end of January 2015, and there have been some supplementary releases since then, resulting in 2,771 matches for possible investigation. Work is well under way to investigate these – to date 24 of the 85 reports (28%) have been closed with no fraud being detected.

Performance indicators

36. The following shows the key performance indicators in the service specification with Norwich and the results for 2014-15:

- Internal audit plan to be endorsed by CLT and audit committee by 30th June each year: The plan for 2014-15 was endorsed in March 2014 (the plan for 2013-14 was endorsed by audit committee in March 2013).

- % of internal audit plan delivered – target 100%. Actual 77% in terms of audits to draft stage (2013-14 77%); 90% in terms of days delivered against the plan.

    The original audit plan was based on the planned restructure of the internal audit and risk service being in place from April 2014; however, this has been delayed, with the result that the planned resource available during 2014-15 was less than anticipated.

- % of productive time achieved by the division against the total resource days available – target 85%. Productive time was 83.4% (2013-14 83.2%).

  Productivity is classified as available time (ie excluding annual leave, bank holidays, sickness) spent working on audits, governance and risk management, as opposed to non-audit time, which includes overheads such as administration and training.

- Draft IA reports issued within 15 days of receipt of agreed management comments: 100% (2013-14 100%).

- Final reports issued within 10 days of receipt of management comments: 100% (2013-14 100%).

- Progress reports to audit committee 6 monthly - achieved. Progress reports are presented to every audit committee, which usually meets five times a year (same in 2013-14).

- Reviews of the strategic risk register by CLT, cabinet and audit committee – achieved. The corporate risk register was regularly reviewed by CLT and presented to audit committee in July 2014, November 2014 and March 2015. In addition, the risk management policy was updated and approved by cabinet in December 2014, together with the latest corporate risk register.

- Although not part of the service specification, the audit manager has an appraisal target to achieve an average score of 4 out of 5 for post-audit feedback questionnaires. The average score achieved was 4.4 (4.9 in 2013-14).

Professional Standards

37. Public Sector Internal Audit Standards (PSIAS) were adopted by the Chartered Institute of Public Finance and Accountancy (CIPFA) from April 2013. The standards are intended to promote further improvement in the professionalism, quality, consistency and effectiveness of Internal Audit across the public sector.

38. The objectives of the PSIAS are to:

- Define the nature of internal auditing within the UK public sector;
- Set basic principles for carrying out internal audit in the UK public sector;
- Establish a framework for providing internal audit services, which add value to the organisation, leading to improved organisational processes and operations;
- Establish the basis for the evaluation of internal audit performance and to drive improvement planning.

39. A self-assessment against the standards was presented to audit committee in September 2014 and is summarised in the following table. It concluded that Internal Audit is broadly compliant.

Table 6 – PSIAS Self- Assessment 2014/15

Attribute Standards:

Ref	Standard	Ref	Description	Assessment
1000	Purpose, Authority and Responsibility	1010	Recognition of the Definition of Internal Auditing, the Code of Ethics and the Standards in the Internal Audit Charter	Compliant
1100	Independence and Objectivity	1110	Organisational Independence	Compliant
		1111	Direct Interaction with the Board	Compliant
		1120	Individual Objectivity	Compliant
		1130	Impairment to Independence or Objectivity	Compliant
1200	Proficiency and Professional Care	1210	Proficiency	Compliant
		1220	Due Professional Care	Compliant
		1230	Continuing Professional Development	Compliant
1300	Quality Assurance and Improvement Programme	1310	Requirements of the Q.A. and Improvement Programme	Mainly Compliant
		1311	Internal Assessments	Compliant
		1312	External Assessments	Not Compliant
		1320	Reporting on the Q.A. and Improvement Programme	Not Compliant
		1321	Confirms with International Standards	Not Compliant
		1322	Disclosure of Non-Conformance	Compliant

Performance Standards:

Ref	Standard	Ref	Description	Assessment
2000	Managing the Internal Audit Activity	2010	Planning	Compliant
		2020	Communication and Approval	Compliant
		2030	Resource Management	Compliant
		2040	Policies And Procedures	Compliant
		2050	Co-ordination	Compliant

		2060	Reporting to Senior Management and the Board	Compliant
2100	Nature of Work	2110	Governance	Compliant
		2120	Risk Management	Compliant
		2130	Control	Compliant
2200	Engagement Planning	2201	Planning Considerations	Compliant
		2210	Engagement Objectives	Compliant
		2220	Engagement Scope	Compliant
		2230	Engagement Resource Allocation	Compliant
		2240	Engagement Work Programme	Compliant
2300	Performing the Engagement	2310	Identifying Information	Compliant
		2320	Analysis and Evaluation	Compliant
		2330	Documenting Information	Compliant
		2340	Engagement Supervision	Compliant
2400	Communicating Results	2410	Criteria for Communicating	Compliant
		2420	Quality of Communications	Compliant
		2421	Errors and Omissions	Compliant
		2430	Compliance with International Standards	Not Compliant
		2431	Engagement Disclosure of Non—Conformance	Compliant
		2440	Disseminating Results	Compliant
		2450	Overall Opinions	Compliant
2500	Monitoring Progress			Compliant
2600	Resolution of Senior Management's Acceptance of Risks			Compliant

40. The outcome of the assessment is therefore generally positive with professional Internal Audit Standards being broadly complied with. Where there is less than full compliance, an action plan will be prepared and monitored during 2015-16.

Fraud team and counter fraud activity 2014-15

41. The majority of the team's activities for 2014-15 continued to be related to benefit fraud investigations. However, 2014-15 was the last year for reporting benefit fraud cases as from 1 April 2015 this work has been undertaken by the Department for Work and Pensions (DWP) under the Single Fraud Investigation Service (SFIS) umbrella (the LGSS fraud team at Norwich transferred to the DWP on 1 April).

42. The team carried out considerable work in preparation for the transfer of benefit fraud work to the DWP, including face-to-face meetings with the DWP and meetings with a number of service leads to work on information sharing and planning for workflow after the transfer.

43. There remains a number of fraud risks outside of welfare, such as council tax, business rates, housing (application, tenancy, succession, right to buy), and procurement.

44. LGSS was successful in securing funding from DCLG to tackle non-welfare frauds across the partner organisations. The fraud team leader based at Norwich had a major role in the background work for the bid, which is based on developing a regional counter fraud centre of excellence. Some appointments have already been made, and the LGSS head of audit, together with counter fraud staff, will meet council officers in June 2015 to discuss housing-related counter fraud work at Norwich.

Continuing counter fraud initiatives - housing

45. The visiting officer attached to the home options team carried out visits on behalf of the fraud team last year and continued to be an extremely useful resource. As well as conducting visits for the fraud team, he has also raised a number of concerns that have been passed on to other council departments and external government agencies. His vigilance has led to a reduction in the number of people on the council waiting list, by way of verification visits.

Liaison and joint working

46. The team continued to work and liaise with the DWP fraud and compliance teams on a regular basis. This included invitation to joint-working, evidence gathering, interview and further action (i.e. prosecution).

47. As well as the DWP, the team worked with other government departments to tackle fraud and share concerns. These include the police, other councils, UK Border Agency and the Security Industry Authority.

Training provided by the fraud team

48. Annual fraud awareness sessions were held with a number of front-line and back-of-house staff to make them aware of what the team investigates and how they can assist by raising concerns. A number of individuals followed this up by attending one-to-one sessions with the team leader to gain a better understanding of how the team operates and helping them make better quality referrals.

Fraud team performance

49. For benefit purposes there are three types of proven fraud:

- Simple Caution is the offering of a warning for first time offenders and/or low level cases where the claimant has fully admitted the offence at interview;

- Administrative Penalty is either a 30% or 50% fine (depending on the period of the offence) and can be offered without a customer attending an interview under caution, as there is no requirement to admit an offence;

- Prosecution is used in more serious cases or where the customer has re-offended and it is in the hands of the courts what, if any, sentence to pass

50. In 2014-15 there were 596 referrals for benefit fraud, of which 411 required further investigation (898 and 511 respectively in 2013-14). In context, there are approximately 18,000 claiming benefit from Norwich City Council so the number of concerns about fraud is relatively low.

51. The team achieved 96 sanctions and prosecutions (40 in 2014-15), of which 79 were LGSS-led, as opposed to DWP-led or joint working.

52. The total overpaid benefit identified through fraud team activity was £594,237 (£249,151 in 2013-14).

53. In addition to the above the team had a major role in the recovery of six council dwellings as a result of investigations (two in 2014-15).