

**Internal Audit**

# **Internal Audit Annual Report and Opinion 2014-15**

**Graham Liddell, Head of Internal Audit**

**June 2015**



**Brighton & Hove  
City Council**

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## 1. Introduction and background

- 1.1 This report summarises the work carried out by internal audit and the corporate fraud team, including the Head of Internal Audit's Annual Opinion for 2014/15.
- 1.2 The Accounts and Audit Regulations (England) 2011 require local authorities to maintain an adequate and effective system of internal audit of its accounting records and its system of internal control in accordance with proper practice. These include a requirement for the Head of Internal Audit to give an annual opinion on the control environment.
- 1.3 The Head of Internal Audit's opinion is based on:
- findings from individual internal audit reviews and the corporate fraud team
  - management's understanding and response to control shortfalls, including the extent to which audit recommendations are being actioned and implemented
  - known changes to systems and control frameworks
  - assurance work carried out by third parties
  - the Council's risk management strategy and reporting arrangements.

## 2 Annual Opinion

### Annual audit opinion

In the opinion of the Head of Internal Audit, **reasonable assurance** can be provided on the overall effectiveness of the council's control environment for the year ended 31 March 2015, but only **limited assurance** on the effectiveness of the council's purchasing and contract management practices.

- 2.1 The evidence to support the assessment of reasonable assurance on the overall effectiveness of the control environment includes:
- robust controls over most of the core financial systems
  - a positive attitude to managers, particularly senior management, in addressing control weaknesses.
- 2.2 The assessment of limited assurance on the effectiveness of the council's arrangements for procurement and contract management is based on:
- an increase in the number of limited assurance reports being issued than in previous years, with the main area of concern relating to a lack of compliance with the council's procurement and contract management procedures
  - further weaknesses in purchasing and contract management practices identified through fraud and audit investigations
  - the council being exposed to losses from contracts for cash handing and with the housing local delivery vehicle.

### 3 Summary of internal audit findings

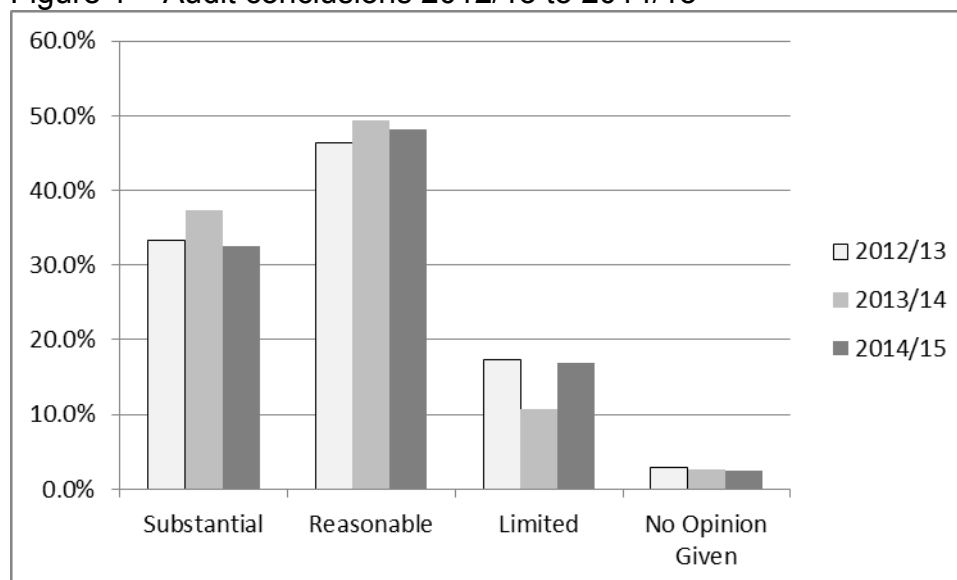
#### Overall findings

3.1 During 2014/15, we completed 83 audit reviews and gave assurance ratings as follows:

- substantial - 27 audits
- reasonable - 40 audits
- limited - 14 audits
- opinion not applicable - 2 audits

3.2 This represents a shift away from substantial and towards limited assurance compared to 2013/14 (see figure 1).

Figure 1 – Audit conclusions 2012/13 to 2014/15



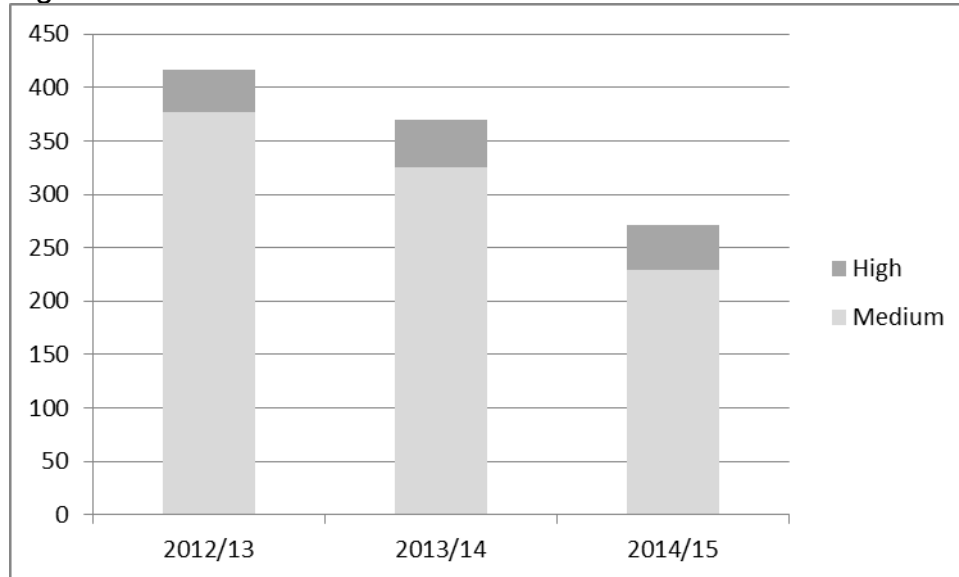
3.3 However, this does not necessarily indicate that the overall control environment is weakening:

- our results from one year to the next are not directly comparable because, apart for some core financial systems, we do not audit the same areas each year
- the results for 2014/15 are broadly in line with 2012/13 (see figure 1)
- as discussed in section 4, the common theme across many of the limited assurance reports relates to procurement and contract management.

## Number of audit recommendations made

- 3.4 During 2014/15 we made a total of 42 high priority and 229 medium priority recommendations. Over the last three years, we have reduced the total number of recommendations but the number of high priority recommendations has remained remaining broadly consistent (figure 2).

Figure 2 – Recommendations made 2012/13 to 2014/15

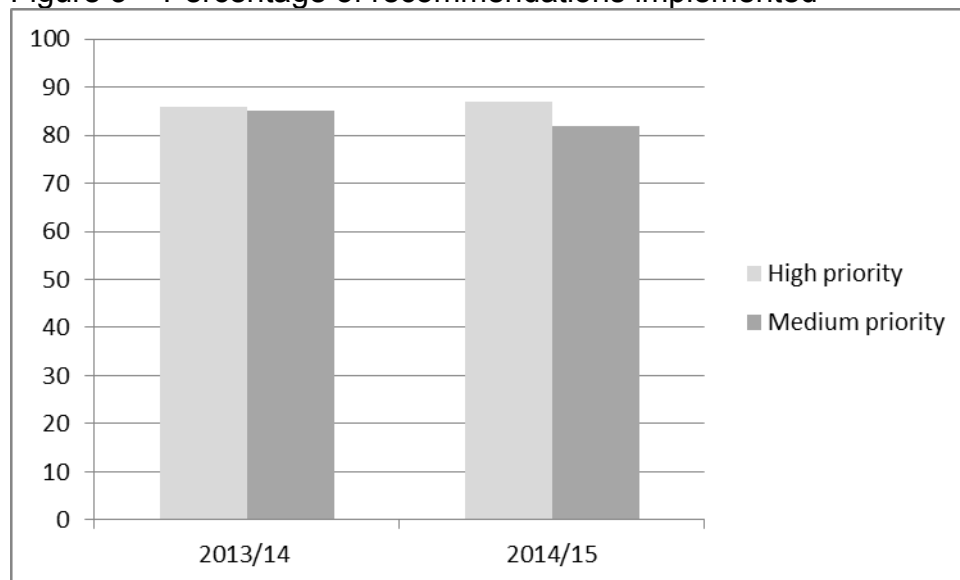


- 3.5 During 2013/14 and 2014/15 we have changed the way we report our findings to make fewer and more relevant recommendations. The overall decline in the number of recommendations is, therefore, a result in a change in internal audit policy rather than an indicator of a change in the effectiveness of the control environment. The consistent number of high priority recommendations made over the past three years would suggest that the control environment has neither improved or declined significantly.

## Audit recommendations implemented

- 3.6 During 2014/15 the council implemented 87% of our high priority recommendations and 82% of medium priority recommendations. For high priority recommendations this represents an improvement from 2013/14 but a decline in the implementation of medium priority recommendations. Previously the implementation rate was almost identical regardless of priority (see figure 3).

Figure 3 – Percentage of recommendations implemented



- 3.7 The increasing implementation rate of high priority recommendations is particularly encouraging and is likely to be the result of the attention given to these recommendations by the Executive Leadership Team.
- 3.8 2013/14 was the first year we carried out systematic reviews of the implementation of all high and medium priority recommendations. Our current practice is to carry out implementation reviews six months after issuing an audit report. For 2015/16, we will provide managers with online access to recommendations and access rights to update the progress they are making. The purpose of this initiative is to encourage managers to take greater ownership of recommendations and to enable us to track the progress being made throughout the year.

## 4 Internal audit findings - detail

### Procurement and contract management

- Two substantial and two reasonable assurance reports
- Four procurement audits assessed as limited assurance:
  - cash collection contract handover
  - children's services procurement
  - highways minor works (follow up)
  - office cleaning contract
- Further weaknesses in procurement and contract management identified through:
  - fraud and audit investigations
  - service focused audits (transport workshop, for example)
- Council exposed to losses from contracts for cash handing and with the housing local delivery vehicle

4.1 We identified a range of control weaknesses including:

- contract documents not finalised
- contract documents not retained
- a lack of formal evidence of tendering and/or use of contract standing order waivers
- poor client contract liaison
- efficiency savings as detailed in a contract not being enforced
- ineffective controls to prevent and recover overpayments.

4.2 The risks to the council are substantial:

- successful procurement and contract management is a precondition to the council achieving value for money
- during a period of change it is not possible to rely on custom or practice or the retained knowledge of staff
- national studies have shown that procurement is (after housing benefit) the area most susceptible to fraud in local authorities.

4.3 The council has taken some positive steps to address these risks including:

- expanding the central procurement team to provide training across the council and increase capacity to advise and support service managers
- establishing a procurement board.

4.4 The procurement board has the potential to play a critical role in improving the standard of procurement and contract management across the council. However, the procurement team provides advice rather than being responsible for enforcing compliance and so it may be difficult for the board (or the Audit & Standards Committee) to gain assurance that procurement and contract management procedures are being followed in practice.



## Core financial systems

- Seven substantial and eight reasonable assurance audits.
- Two limited assurance reports
  - housing benefit
  - payroll overpayments
- Ernst & Young has been able to rely on internal audit work

- 4.5 Core financial controls are generally robust and the council need to ensure that they remain so and are not compromised by the pressure to achieve savings. Our work for 2014/15 has not identified any general trend that would suggest that controls are being compromised.
- 4.6 Our review of housing benefit found that a reduction in the number of data quality checks carried out appeared to have resulted in an increased the error rate of benefits awarded. This increases the risk that the DWP might require a clawback of the grant paid to the council. The housing benefit team has reviewed the workflow for quality checks and changed its practices.
- 4.7 Our other limited assurance report (payroll overpayments) found shortfalls in the investigation and recovery of historic salary overpayments. The council introduced new procedures to improve recovery in August 2014 and these were starting to have an impact at the time of our report.

## IT audit

- Overall IT control environment (preliminarily) assessed reasonable
- Two substantial and seven reasonable assurance reports
- Two limited assurance reports
  - BACS
  - ICT Service Levels

- 4.8 The council continues to invest in its IT services and this is reflected in our assessment of the overall IT control environment as reasonable. This is an improvement from our assessment of limited assurance in 2013/14.
- 4.9 The limited assurance assessment of BACS is the result of a long-standing technical issue which has been reported in previous years. The ICT department is developing an action plan to reduce the risk to the council. ICT does not have formal service level agreements for the services it provides and this is reflected in our assessment of limited assurance for ICT service levels.

## Governance

- Three substantial and four reasonable assurance reports
- Some serious breaches in how the governance framework is being applied

- 4.10 The council has put in place the key elements of a governance framework and processes for declaration of interests, gifts and hospitality, performance management and absence management. The council has a well-established risk management function and secured the Silver Award for Investors in People for 2015.
- 4.11 However, the council has also suffered breaches in how the governance framework has been applied. During the year we supported an investigation into allegations of an undisclosed relationship between the Head of Housing and the council's provider of temporary accommodation provider. This resulted in the dismissal of the Head of Housing in March 2015 and is subject to ongoing investigation by Sussex Police. The council has engaged the former chief executive of Hertfordshire County Council to carry out an organisational learning review. We have contributed to this review and will use its findings to inform our work for 2015/16.

## Service focused (including reviews of establishments)

- Seven substantial and 16 reasonable assurance reports
- Five limited assurance reports
  - city clean expenditure
  - transport workshop follow up
  - housing local delivery vehicle
  - direct payments and personal budgets
  - residents parking permits

- 4.12 The limited assurance reports for the transport workshop and City Clean expenditure identified some similar themes, particularly in respect of purchasing practices and stock control.
- 4.13 We found that the council was exposed to losses from its contract with the housing local delivery vehicle (Brighton and Hove Seaside Homes):
- the developer's fee of £483k due to the council in respect of 22 properties was outstanding. Following the audit half of this has been paid.
  - because of a drafting error in the overarching agreement, there is a dispute as to who is responsible for paying the building insurance costs of properties that have transferred to Brighton and Hove Seaside Homes. Currently the council is paying £123k per annum. For the period 2011 and 2016 this equates to an estimated £600k of unplanned costs being borne by the council
- 4.14 The audit of direct payments found that:
- contracts signed by service users are not always on file

- controls are not always operating to ensure payments are being made in accordance with the service user's agreed package of care
  - insufficient monitoring of client contributions and clients' dedicated bank account statements
  - regular reviews of the service users' needs are not always happening.
- 4.15 The audit of parking permits identified the following significant issues;
- there is no effective reconciliation of blank permit stock received, held and used
  - reconciliations between permits issued, income received, the amount banked are not currently being undertaken. This could result in missing income not being detected.

### **Schools (including services provided by the council and reviews of specific schools)**

- Four substantial and one reasonable assurance reports
- One limited assurance report following an audit visit to a school
- Significant concerns were identified regarding the administration of income at a school following allegations raised by a whistleblower

- 4.16 This work represents an increase in the number of individual school audits from just two in 2013/14.
- 4.17 In general we found controls to be robust within the council's provision of school services and at individual schools. However, we recognise that for individual schools the control environment depends relies heavily on a very small number of staff and sometimes things go wrong. This was reflected by our findings of control failures at two schools.
- 4.18 We will continue our programme of school visits during 2015/16 and will respond promptly when concerns are raised at any individual school.

### **Project assurance**

- i360 - substantial assurance
- Workstyles and VfM phase 4 - reasonable assurance reports

- 4.19 We reviewed the assurance arrangements for three major projects all of which are high profile and significant for the council. The audit of the VfM phase 4 looked at the overall control arrangements for this programme. More detailed work in individual projects and outcomes will be carried out in 2015/16.

## 5 Internal audit performance

5.1 2014/15 was a challenging year for internal audit. The team was without a permanent head of service and played a leading role in carrying out a highly complex and high profile investigation into allegations about the Head of Housing. However, the team achieved a marked improvement in its performance in 2014/15 (table 1). This represents a substantial achievement by the whole team. Highlights include:

- 92% of audit plan delivered (82% in 2012/13)
- Client satisfaction levels maintained at 92%
- Implementation of high priority recommendations increased from 85% to 87%

5.2 Nonetheless, our performance for the year falls short of the targets we set as part of agreeing the audit plan. For 2015/16 we are focusing on:

- delivering a greater proportion of audits within budget
- issuing draft reports more quickly after completion of fieldwork and final reports after receiving responses
- improving further the implementation of high priority and medium priority recommendations.

Table 1 – Internal Audit performance measures 2013/14 and 2014/15

| Performance measure   | 2013/14  | 2014/15  | Target |
|---|----------|----------|--------|
| Completion of planned audits                                  | 82%      | 92%      | 100%   |
| Client satisfaction   | 92%      | 92%      | 90%    |
| High priority recommendations implemented                     | 85%      | 87%      | 98%    |
| Low priority recommendations implemented                      | 86%      | 82%      | 85%    |
| Compliance with professional standards                        | 99%      | 99%      | 100%   |
| Productive time   | 61%      | 70%      | 71%    |
| Audit reviews delivered within budget                         | 71%      | 80%      | 100%   |
| Draft report issued 10 days after completion of fieldwork     | 33%      | 58%      | 100%   |
| Final report issued 10 days after responses to draft received | 87%      | 75%      | 100%   |
| Staff holding professional qualifications                     | 90%      | 90%      | 80%    |
| Number of training days provided per employee                 | 3.5 days | 4.5 days | 5 days |

5.3 The service has also made good progress in implementing its quality assurance improvement programme including:

- improving the visibility of the service through corporate communications
- enhancing our focus on client feedback through customer questionnaires
- developing an online system to help service managers track their progress on implementing audit recommendations
- developing our reporting format to improve impact, quality and consistency of our reports.

5.4 The service is currently updating its quality assurance improvement programme. This programme will include areas where further work is required from 2014/15 including:

- developing stronger links between internal audit and the corporate fraud teams
- further “cold” (retrospective) reviews of the quality of audit work carried out including reviews of supporting evidence.

## **6 Corporate fraud**

6.1 On 1 October 2014 the responsibility for investigating Housing Benefit and Council Tax Benefit Fraud transferred to the DWP under the Single Fraud Investigation Service (SFIS) project. Three members of the corporate fraud team transferred across to SFIS. Following this transfer, a revised corporate fraud team was set up consisting of a corporate fraud manager, two investigators and an administrative support officer.

6.2 The new team has focused on non-housing benefit fraud by:

- supporting proactive including data matching
- investigating referrals relating to allegations on issues such as housing tenancy, procurement and payroll.

### **Proactive work including data matching**

6.3 Together with other local authorities in England and Wales, the council participated in the National Fraud Initiative (NFI). The Council was legally obliged to supply data to the Audit Commission which carried out a data matching exercise to identify potential instances of fraud. Those cases relevant to Brighton & Hove were referred back to the council to be followed up. The Audit Commission was abolished on 31 March 2015 and has the responsibility for NFI has transferred to the Cabinet Office.

6.4 NFI identifies a very large number of cases for local authorities to follow up (more than 19,000 at Brighton & Hove). This follow up work will carry on into 2015/16 and beyond. To date we have identified:

- overpayments totalling £36,698 (Private Residential Care Homes £33,073 and Personal Budgets £3,625)
- 945 concessionary travel passes and 10 blue badges that required cancellation because the holder had died.

6.5 The corporate fraud team is considering how to use technology more proactively to prevent and detect fraud. This could include carrying out earlier local data matching exercises or investing in software to validate identity and support tenancy investigations.

6.6 The council submitted a joint bid to the DCLG in conjunction with East Sussex County Council to tackle Blue Badge fraud during 2014/15 and were successful in receiving £183,000 spread over two years. This campaign has already identified cases of misuse, resulting in fines, which have received a high profile in the local press. The Corporate Fraud Team is developing further its relationship with other local authorities through the Sussex Tenancy Fraud Forum, the East Sussex Counter Fraud Hub and East Sussex Fraud Officers Group.

6.7 The corporate fraud team has a key role in promoting an anti-fraud culture in the council in 2014/15 and has developed a fraud e-learning awareness training package This will be launched across the council as part of a wider anti-fraud and corruption communications initiative during June and July 2015.

### **Investigating referrals**

6.8 The team received 499 housing benefit referrals (up to 30 September) and 120 other referrals (mostly relating to potential housing tenancy fraud). Outcomes included:

- Identification of fraudulent housing and council tax overpayments of £425,000
- 19 council properties and one housing association property being released. Based on the established Audit Commission formula of £18,000 per property this represents a £270,000 saving to the public purse. More importantly, however, each property recovered represents a home that the council can make available to help address the significant housing pressures faced by the citizens of the Brighton and Hove
- the dismissal of staff involved in fraudulent activity.

## Case studies

- A match from the National Fraud Initiative (NFI) indicated that a claimant did not have leave to remain in the UK. Jointly working with the UK Border Agency we confirmed that the claimant's leave to remain expired in 2003 and that the stamp in the passport was false. The resulting housing benefit overpayment was £29,153.67 housing benefit and £1234.20 council tax benefit. The claimant was subsequently prosecuted and received 6 months on each offence concurrently suspended for 2 years and 140 hours unpaid work.
- An anonymous letter was received from the public stating that a claimant was claiming housing and council tax benefit and had an undeclared partner. The investigation resulted in both the claimant and their partner being arrested and subsequently charged with benefit fraud. The overpayment of council tax benefit was £8,681 and housing benefit of £98,498. The sentence imposed was 6 months on each count suspended for 18 months plus 100 hours unpaid work plus £500 costs.
- A tenant who fraudulently sublet their council flat in Brighton was successfully prosecuted and fined more than £5,000. The tenant made £3,199 in profit by subletting their property to students. The tenant pleaded guilty to social housing fraud through their solicitor and was ordered to pay a £3,500 fine and £2,100 in costs.
- An allegation was received relating to an employee selling school equipment on ebay using a private email account. The allegation was investigated and the loss was calculated to be £3077. The employee concerned admitted the fraud, repaid the amount in full and was dismissed.
- Two council employees were sanctioned for housing benefit fraud. Disciplinary hearings were held during and both were dismissed.

## Appendix 1 - 2014/15 Internal Audit Reviews

| Classification        | Title  | Opinion     |
|-----------------------|--|-------------|
| Contract/ Procurement | Cash Collection Contract Handover              | Limited     |
| Contract/ Procurement | Children's Services – Procurement              | Limited     |
| Contract/ Procurement | Highways Minor Works (Follow up)               | Limited     |
| Contract/ Procurement | Office Cleaning Contract                       | Limited     |
| Contract/ Procurement | Corporate Banking Contract                     | Reasonable  |
| Contract/ Procurement | ICT Contracts                                  | Reasonable  |
| Contract/ Procurement | Education PFI                                  | Substantial |
| Contract/ Procurement | Approved Lists                                 | Substantial |
| Financial Systems     | Employee Overpayments                          | Limited     |
| Financial Systems     | Housing Benefits                               | Limited     |
| Financial Systems     | Bailiff Services                               | Reasonable  |
| Financial Systems     | Business Rates                                 | Reasonable  |
| Financial Systems     | Council Tax                                    | Reasonable  |
| Financial Systems     | Debtors  | Reasonable  |
| Financial Systems     | Periodic Payments                              | Reasonable  |
| Financial Systems     | Staff Expenses (Follow-up)                     | Reasonable  |
| Financial Systems     | Treasury Management                            | Reasonable  |
| Financial Systems     | Business Rates                                 | Reasonable  |
| Financial Systems     | Budget Management                              | Substantial |
| Financial Systems     | Creditors                                      | Substantial |
| Financial Systems     | Housing Rents                                  | Substantial |
| Financial Systems     | Main Accounting System                         | Substantial |
| Financial Systems     | Management on Non-Current Assets               | Substantial |
| Financial Systems     | Payroll  | Substantial |
| Financial Systems     | Procurement Cards                              | Substantial |
| IT Audit              | BACS   | Limited     |
| IT Audit              | ICT Service Levels                             | Limited     |
| IT Audit              | ICON Cash Management                           | Reasonable  |
| IT Audit              | Information and Data Sharing                   | Reasonable  |
| IT Audit              | Mobile & Portable Devices                      | Reasonable  |
| IT Audit              | Payment Card Industry – Data Security Standard | Reasonable  |
| IT Audit              | SIMS Application audit                         | Reasonable  |
| IT Audit              | Software Licensing                             | Reasonable  |
| IT Audit              | Business Rates (New System) - Data Migration   | Substantial |
| IT Audit              | Capital Investment Programme - ICT             | Substantial |
| IT Audit              | ICT Governance (Follow-up)                     | Reasonable  |
| Governance            | Declarations of Interests, Gifts & Hospitality | Reasonable  |
| Governance            | Performance Management (Follow-up)             | Reasonable  |
| Governance            | Records Management Policy                      | Reasonable  |
| Governance            | Data Protection and Freedom of Information Act | Reasonable  |
| Governance            | Attendance-Absence Management                  | Substantial |
| Governance            | Better Care Fund                               | Substantial |
| Governance            | Risk Management - Service Level Arrangements   | Substantial |



|                     |  |                |
|---------------------|--|----------------|
| Service Focused     | City Clean Expenditure                           | Limited        |
| Service Focused     | Direct Payments and Personal Budgets             | Limited        |
| Service Focused     | Housing Local Delivery Vehicle                   | Limited        |
| Service Focused     | Transport Workshop Follow-up                     | Limited        |
| Service Focused     | Residents Parking Permits                        | Limited        |
| Service Focused     | Asylum Seekers                                   | Reasonable     |
| Service Focused     | Blue Badges                                      | Reasonable     |
| Service Focused     | Client Billing (Adult Social Care Contributions) | Reasonable     |
| Service Focused     | Housing Allocations                              | Reasonable     |
| Service Focused     | Leaving Care                                     | Reasonable     |
| Service Focused     | On-Street and Off-Street Car Parking             | Reasonable     |
| Service Focused     | Payment of Grants                                | Reasonable     |
| Service Focused     | PCNs (Follow-up)                                 | Reasonable     |
| Service Focused     | PIER (Management Data)                           | Reasonable     |
| Service Focused     | Premises Security                                | Reasonable     |
| Service Focused     | Property Legal Compliance                        | Reasonable     |
| Service Focused     | Regulatory Enforcement Activities/Licensing      | Reasonable     |
| Service Focused     | Sea Front Services                               | Reasonable     |
| Service Focused     | Tenant Incentive Scheme                          | Reasonable     |
| Service Focused     | Building Control                                 | Substantial    |
| Service Focused     | Brighton Centre - Ticketing and Catering         | Reasonable     |
| Service Focused     | Housing Rent Arrears (Welfare Reform Impact)     | Substantial    |
| Service Focused     | Learning Disabilities                            | Substantial    |
| Service Focused     | Parking - Pay by Telephone                       | Substantial    |
| Service Focused     | Right to Buy                                     | Substantial    |
| Service Focused     | Welfare Reform                                   | Substantial    |
| Service Focused     | Children's Centres                               | Substantial    |
| Service Focused     | Public Health                                    | Substantial    |
| Service Focused     | Care Act Planning and Integration                | Reasonable     |
| Schools             | Blatchington Mill Investigation                  | Not applicable |
| Schools             | Patcham High                                     | Limited        |
| Schools             | St Bernadette's Catholic Primary                 | Reasonable     |
| Schools             | Rudyard Kipling Primary                          | Substantial    |
| Schools             | St. John the Baptist Catholic Primary            | Substantial    |
| Schools             | School Meals Contract                            | Substantial    |
| Schools             | Schools Admissions                               | Substantial    |
| Project Assurance   | VFM Phase 4                                      | Reasonable     |
| Project Assurance   | Workstyles Project                               | Reasonable     |
| Project Assurance   | Major Projects (i360)                            | Substantial    |
| Grant Certification | Certification of Grant Claims                    | Not applicable |

