

AUDIT COMMITTEE

Development of Internal Audit and Assurance 21st January 2015

Report of Internal Audit Manager

PURPOSE OF REPORT

To seek the Committee's support for proposals for strengthening the Council's information governance and other assurance arrangements (covering Information and Communications Technology (ICT), information management, corporate anti-fraud and internal audit generally)

This report is public

RECOMMENDATIONS

- (1) That the Audit Committee supports proposals for the development of the ICT service and the corporate information governance function as outlined in the report.
- (2) That Audit Committee supports the setting-up of a corporate anti-fraud team in collaboration with Preston City Council and Fylde Borough Council on the basis outlined in the report.
- (3) That Audit Committee supports proposals for the development of assurance reporting and endorses the proposed widening of the Internal Audit service's remit.

1 Introduction

1.1 The Audit Committee's terms of reference include:

8.2 To monitor arrangements for discharging the Council's responsibilities for efficient and effective financial and operational resource management...; and

8.18 To monitor the effective development and operation of risk management and corporate governance...

1.2 As part of the 2014/15 budget, Cabinet supported an outline investment plan and associated growth estimated at £120K per year for ICT security and Public Services Network (PSN) compliance. The growth was duly approved at Budget Council on 26 February 2014, its future use being subject to a further report to Cabinet.

1.3 Linked to this, the Council's positioning regarding information governance has been commented on in the last two Annual Governance Statements. The 2013/14 statement, approved by Audit Committee in September 2014, acknowledged that, following a significant body of work surrounding the Public Services Network (PSN), further actions were still required "*to ensure that the council's arrangements for collecting, storing, using and sharing information are robust and enable the most efficient and effective use of that information*".

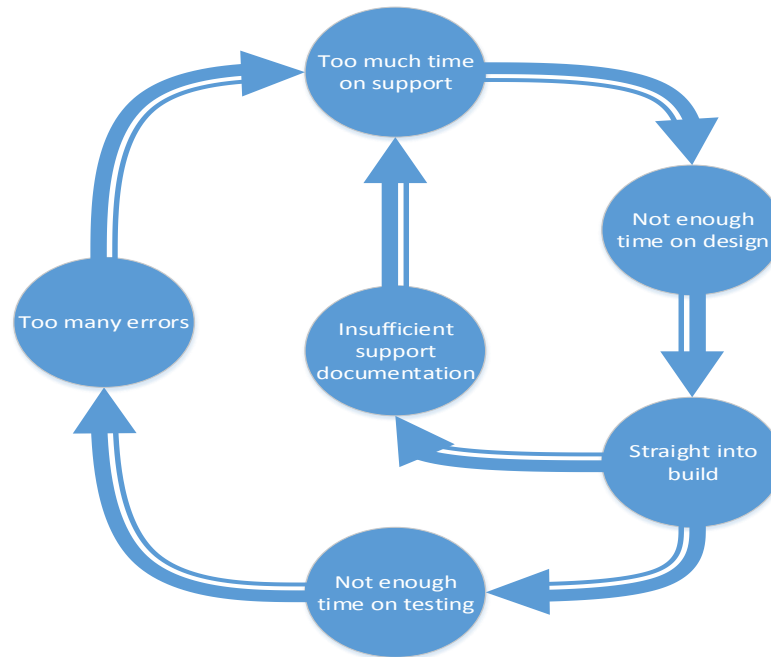
1.4 In addition to addressing those needs from both ICT and general information governance perspectives, this report takes the opportunity to consider the Council's response to other recent developments regarding anti-fraud arrangements.

2 Information Security and Governance

2.1 Information and Communications Technology (ICT)

- 2.2 Sound ICT is essential for effective service delivery and as such, any delays, outages or other difficulties in the supply of the ICT service can have significant adverse impact, potentially across the whole organisation. This is recognised, hence the approval of the budget growth almost a year ago.
- 2.3 In terms of the PSN, after a very difficult exercise under a very stringent regime, compliance was first gained in May 2014. Nationally, the arrangements have been the subject of criticism, because of inconsistencies in assessment experiences of various councils to some degree but more fundamentally, because of an imbalance in the absolute need for addressing real and perceived security risks at the expense of service provision – with the latter losing out significantly in some cases. Moreover, indications are that it has proved a very expensive exercise for local government as a whole.
- 2.4 That is not to say that there have been no benefits derived from the experience, however. On a more positive note, the Council does have a far more robust ICT network and Officers have already learned much, in getting this far. It is also apparent that Government has recognised councils' difficulties and it is committed to improving arrangements.
- 2.5 Unfortunately though, this was not in time to influence the timing of the Council's subsequent PSN assessment, as this still had to be completed and submitted last August, only 3 months after gaining the last accreditation. Once again this tied up resources and resulted in additional costs, although by no means to the extent experienced on the previous occasion. Nonetheless, it did result in further delays in progressing the more proactive work to develop service restructure proposals for the future. The £120K additional budget available in this year has been spent on putting in place infrastructure and interim consultancy support to resolve outstanding tasks from the first PSN assessment, as well as dealing with the requirements of the second one.
- 2.6 Government's change in stance has influenced its response to the second assessment, however. Officers have only very recently received any actual feedback; initial indications are encouraging and it is hoped that confirmation of compliance will be received sometime this month.
- 2.7 More specifically, Government has now brought in significant changes for the governance for PSN. For example, it has established a PSN Programme Board to help improve the compliance process and capitalise on the opportunities that PSN presents, such as supporting the joining up of public services in an efficient and effective manner. The Local Government Association (LGA), the public sector based Society of IT Management (SOCITM) and other local authority representatives are included on the Board. Furthermore, the Council's ICT Manager is currently the Regional Chair for SOCITM in the North West, which gives a good opportunity to both contribute to and keep abreast of future developments.
- 2.8 Whilst undertaking the network security remediation work in order to meet PSN requirements, it became very clear that ways of working and skills levels within ICT required strengthening to meet and keep up to date with industry standards. Developing appropriate plans to tackle this takes time, however – especially as day to day service provision must continue. An external company was engaged to undertake a skills review, in order to inform restructuring proposals.

- 2.9 As background, the current structure of three teams within ICT, (these being Service Desk, Technical Support and Applications Support), has been in place for at least the last 15 years. Staff in each section have to prioritise their work between support and development and often, as a result, areas of development including design, testing, and hand-over to Service Desk, are sacrificed. Instead, just trying to get and keep systems up and running becomes the priority. With the focus being on resolving issues that arise from this, there has been inadequate time to devote to strategy. The following diagram sums up the service's way of working, which in the industry is referred to as a "circle of too much support".



- 2.10 In short, the key findings of the external review were therefore as expected, in that the ICT service is understaffed and under-skilled in critical areas. Furthermore, the service also needs to draw on external support where this is more cost-effective to do so, for example in the provision and support for wi-fi and other aspects where 24/7 cover and support are needed.
- 2.11 To address this position, Cabinet has been asked to approve the development of the ICT service and restructuring proposals will be presented to Personnel Committee shortly. In the current climate of rapidly increasing change both from technology and as a result of different ways of working brought about by budget pressures, the Council needs an ICT service that provides reliable systems, manages a wide variety of technologies and is able to plan for and respond to change in an agile manner. Use of the previously approved budget growth will enable this.
- 2.12 **Information Governance**
- 2.13 In parallel with addressing ICT related vulnerabilities, it has been acknowledged that the Council also needs to develop and improve its standards of information governance generally throughout the organisation.
- 2.14 The key components of the Council's current information governance arrangements are:
- Information Management Officer
 - Information Management Group
 - Existing policies and procedures
 - On-line training resources

- 2.15 A self-assessment of the Council's current position has been carried out using the National Archive's information management self-assessment tool. A summary chart and headline results coming out of this review are set out in **Appendix A**.
- 2.16 The conclusion from this analysis is that corporately, resources and arrangements currently devoted to information management are insufficient to address the development issues identified in this review and to maintain appropriate standards into the future. Key areas for development are therefore identified as being:
- Raising understanding of the importance of 'Knowledge and Information Management' (KIM)
 - Identifying and managing significant information management risks
 - Raising understanding of the information needs of the Council and putting in place standards and procedures to ensure these are met
 - Establishing clear roles and responsibilities for information management and ensuring that staff and elected Members receive appropriate training, guidance and support
 - Developing a culture which ensures a commitment to high standards of information management and to identifying and taking advantage of information sharing opportunities
- 2.17 Given the nature of information developments, particularly those relating to digital information and the associated technology, the expectation is that resources will be required not just in the immediate term, to address the gaps identified and raise standards to an acceptable level, but also to maintain those standards into the future. Furthermore, drawing on the arrangements that other local authorities have in place, buying in support, either through collaboration with other authorities or from the private sectors, is not considered to be a viable, cost effective option, at least for the medium to longer term.
- 2.18 Accordingly, Cabinet has also been asked to approve the expansion and development of the in-house corporate information governance function, with an increase of one post being envisaged. It is proposed that managerial responsibility for Information Governance would transfer to Internal Audit.

3 Corporate Anti-Fraud Arrangements

3.1 Background

3.2 The National Fraud Authority ("NFA") estimates that fraud in local government amounts to at least £2.2 billion. In its publication "Protecting the Public Purse 2013", other than Housing/Council Tax Benefit, the Audit Commission identified a number of areas of fraud as being those that local authorities are typically likely to be subject to.

3.3 The Audit Commission goes on to say:-

"Councils face reduced funding and new national counter-fraud arrangements. They need to assess fraud risks effectively to target resources where they will produce most benefit. They should:

- *Maintain their capacity to investigate non-benefit fraud following the introduction of the Single Fraud Investigation Service ("SFIS");*
- *Follow the lead of London Boroughs and focus more effort on detecting non-benefit fraud, which directly affects their revenue; and*
- *Ensure they have the right skills to investigate all types of fraud, which vary in complexity."*

- 3.4 The public is entitled to expect the City Council to conduct its business with integrity, honesty and transparency and demand the highest standards of conduct from those working for it. Local authorities have a duty to safeguard public funds and take responsible steps to ensure this. If fraud is suspected, authorities are tasked with actively investigating allegations.
- 3.5 Historically both Lancaster and Preston City Councils have, with great success, concentrated their counter fraud work around the prevention and detection of housing benefit /council tax benefit related fraud, with occasional cases relating to other fraudulent activity or irregularity being referred to the team for further investigation.
- 3.6 The DWP contributes financially (through Housing Benefit Administration Grant) to facilitate the fraud prevention and detection work directly linked with benefit fraud.
- 3.7 Recently, however, Government has confirmed that all Local Authority Fraud Investigators will transfer to the Department of Work and Pensions (DWP) in a phased process, thus creating a Single Fraud Investigation Service (SFIS).
- 3.8 As part of these arrangements, shared service staff currently employed by Preston City Council are scheduled to transfer to DWP from 1 June 2015. This move will result in a loss of specialist resources, funding and skills. At the same time, the Council will continue to be required to participate in the National Fraud Initiative (“NFI”).
- 3.9 Additionally, the landscape in which the Council operates is changing as a result of:
- it now being responsible for determining its own Localised Council Tax Support (LCTS) Scheme;
 - Business Rates administration changes, with the potential for increased rate avoidance tactics and increased local impact; and
 - there being a higher profile regarding fraud and its impact on public funds generally, at a time when councils and other public bodies are facing huge financial challenges.
- 3.10 These factors impact directly on the scale and range of risks inherent within the Authority and its future capacity and resources. With all of these issues in mind, there is a business need to determine a suitable framework that ensures the Council is still reasonably able to prevent fraud from occurring, following the creation of SFIS. Where this is not possible, there should be a systematic and proportionate response, enabling the timely and effective detection, investigation and prosecution of fraudsters.
- 3.11 **Current Position**
- 3.12 The Council’s Financial Regulations and the Anti-Fraud, Bribery and Corruption Policy assigns responsibility for the corporate reporting and investigation of fraud and other financial irregularities to the Council’s Internal Audit function. In recent years, the majority of fraud cases detected (other than benefits) have tended to be relatively low level theft or other impropriety. There have been no cases over £10,000 requiring a report to the Audit Commission.
- 3.13 The existing shared Benefits Fraud Team consists of 10.6 full time equivalent staff operating over 3 sites. It includes counter fraud officers/managers accredited through the DWP’s Professionalism in Security (“PinS”) qualification. In addition several team members hold BTEC Professional Certificates in investigation.
- 3.14 **Proposal**
- 3.15 Cabinet has been asked to support the setting-up of a corporate anti-fraud team in collaboration with Preston City Council and Fylde Borough Council.
- 3.16 The scope of this corporate function would include business rates, council tax discounts and significantly, council tax support cases, which will not be covered by the Single Fraud Investigation Service.

- 3.17 Furthermore, under the Prevention of Social Housing Fraud Act 2013, local authorities have been given powers to investigate and prosecute tenancy fraud, providing a further opportunity to explore partnership working arrangements in social housing. This is relevant to Lancaster in relation to its own Council Housing service and in Preston, the Community Gateway Association has expressed an early interest in discussing service provision, should a shared Corporate Fraud Team be established.
- 3.18 The team would also be tasked to investigate alleged fraud, bribery and corruption by any employees, councillors, contractors, consultants, suppliers, service users and members of the public who have dealings with the Council. In summary the section will be responsible for:
- Prevention, detection, investigation and prosecution of all fraud against the Council
 - Assisting the HR Team with appropriate disciplinary matters
 - Providing assurance that the risk of fraud is minimised wherever possible
 - Working with Internal Audit on any other matters regarding fraud, bribery and corruption risks affecting the Council.
- 3.19 If this approach were to go ahead, the team would seek to work closely with other interested stakeholders, including Housing Associations and Lancashire County Council, to help detect fraud in other prime areas.
- 3.20 It is currently envisaged that a new Corporate Fraud Team established on this basis would consist of 4 posts. They would continue to be employed by Preston City Council and there would be a further partnership agreement put in place.
- 3.21 Where possible, the new Corporate Fraud Team would be staffed from the existing shared Benefit Fraud Team, ahead of the transfer to SFIS.
- 3.22 There are several options for service location and management, ranging from a virtual team located in several places, or a single unit based in one location, or a hybrid arrangement. At this stage, regardless of location, it is proposed that the Corporate Fraud Team forms part of Internal Audit resources. Officers from the partner authorities would agree the exact arrangements in due course.

3.23 Financial Implications

- 3.24 In essence, initially the proposed creation of a shared Corporate Fraud Team would be funded through redirecting the savings anticipated from the transfer of the bulk of benefit anti-fraud work to SFIS, as shown in the table below:

	2015/16	2016/17	2017/18	2018/19
Savings:	£000	£000	£000	£000
Fraud Staff TUPE – saving in LCC contribution to the Shared Service	(95)	(127)	(127)	(127)
Additional Costs				
Contribution to the Corporate Fraud Team (approx. 40%)	41	53	53	53
Administration Grant Reduction	-	74	74	74
Net Cost / (Saving)	(54)	0	0	0

- 3.25 Financial arrangements for sharing/allocating costs and savings would be developed further, drawing on the principle that the function should be self-financing, i.e. the money the team prevents being lost through fraudulent activity should more than offset the cost of running the team. The evaluation of this would be developed and monitored on an ongoing basis, to ensure that value for money is being achieved. At present, the proposal does not assume any direct savings from the team's prevention work.

- 3.26 In addition to the above, Government recently challenged Councils to use innovative financial management to tackle fraud. It set up a £16M funding pot (covering a two year period), with the purpose of encouraging bids from local authorities, working in partnership, to recoup money owed and tighten safety nets to prevent crime.
- 3.27 Preston City Council, with support from its existing local authority fraud partners (Lancaster CC & Fylde BC), submitted a successful bid for funds and it has been awarded £125,750 to help the partnership establish an investigative capacity over a 2 year period. The use of these funds has not yet been determined, but they should also mean that additional savings can be gained.
- 3.28 Separately, Officers have signed up to Government's recently announced Fraud and Error Reduction Incentive Scheme (FERIS) that runs until the end of 2015/16. This should provide financial rewards for authorities that further tackle fraud and error within their housing benefit caseload (rather than corporate fraud). The resources for participating in this will also be managed jointly, through shared arrangements.
- 3.29 As indicated earlier, the work of the proposed team will cover both General Fund and Housing Revenue Account services and each account will therefore be expected to bear an element of the Council's share of the cost. It is too early to estimate the level of cost likely to fall in each area.

4 Internal Audit and Assurance

- 4.1 Constitutionally, the Audit Committee has delegated responsibility for considering and commenting on the adequacy of Internal Audit and options for its delivery. The current structure of the Internal Audit section is as follows:

Job Type	FTE	Grade
Internal Audit Manager	1	8
Principal Auditor (vacant)	1	5
Senior Auditor	1	4
Assistant Auditor	0.8	3

- 4.2 The Internal Audit section currently has a vacancy in the post of Principal Auditor; this has been held vacant pending the proposals contained in this report and the report to Cabinet being developed and considered.

4.3 Current Position

- 4.4 Whilst the Council's Audit Committee operates substantially in accordance with recommended standards as set out by CIPFA¹, there is scope to broaden and strengthen the committee's coverage and effectiveness through developing a corporate 'assurance framework'. Currently, assurance is primarily provided to the Committee through audit reports (both Internal and External) and through its scrutiny of the production of the financial accounts.

- 4.5 The Audit Committee has a key role in considering and understanding what assurance is available to support the production of the Annual Governance Statement. Guidance therefore suggests that the Committee should be seeking to ensure that assurance is planned and delivered with the following objectives in mind:

- Clarity of what assurance is required
- Clear allocation of responsibility for providing assurance activities;
- Avoiding duplication, bearing in mind the differing objectives of assurance activities;
- Improving the efficiency and cost effectiveness of assurance

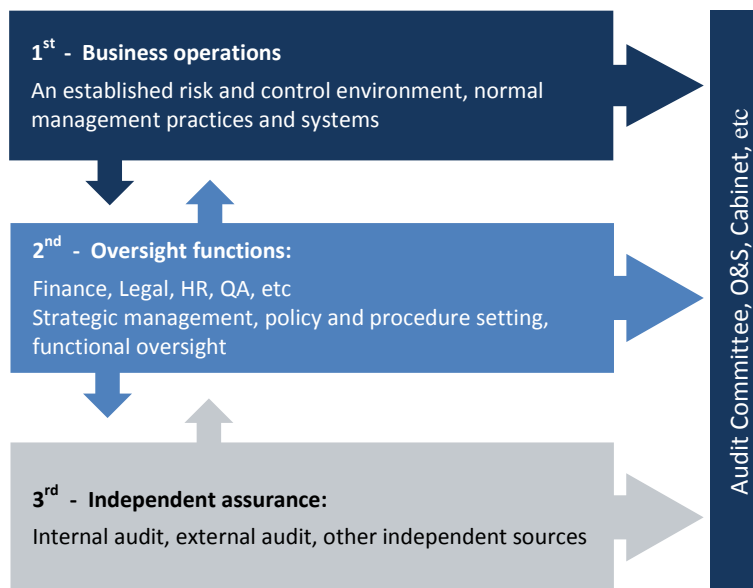
¹ Audit Committees - Practical Guidance for Local Authorities and Police (CIPFA, 2013)

- Obtaining assurance of appropriate rigour and independence across a range of assurance providers.

4.6 Proposal

4.7 Having a clear assurance framework in place will support the committee in considering the annual review of effectiveness for the AGS and will also support the approval of the internal audit risk-based plan, as it enables the committee to identify the extent to which it will rely on internal audit for its assurance requirements.

4.8 The ‘three lines of defence’ model (depicted in the diagram below) provides a useful way of outlining an organisation’s risk and control environment, and therefore its assurance framework.



First Line

- The first level of the control environment is the business operations which perform day-to-day risk management activity

Second Line

- Oversight functions such as Finance, Legal and HR set directions, define policy and provide assurance

Third Line

- Internal and external audit are the third line of defence, offering independent challenge to the levels of assurance provided by business operations and oversight functions.

4.9 The current vacancy within Internal Audit provides an opportunity to review the service provided and incorporate a wider ‘assurance’ function into the existing remit of Internal Audit. This would enable Internal Audit to develop and coordinate the identification and collation of assurance from across all three levels of the assurance model, with particular emphasis on the reporting of assurance to the Audit Committee.

4.10 Given the corporate nature of the work, specific responsibilities for fulfilling this wider role would be attached to the senior members of the team, i.e. the Internal Audit Manager and, to a lesser extent, the Principal Auditor.

4.11 This development would sit readily alongside enhanced roles in relation to corporate anti-fraud and information governance, should those particular proposals be taken forward. Given the Internal Audit Manager’s additional managerial commitment involved in those proposals, it is proposed that the vacant Principal Auditor post be filled and that overall, existing levels of resource in the Internal Audit team are maintained.

4.12 This approach may require some relatively minor changes to job roles within the function, but any costs involved would be minor and would be contained within existing budgets.

4.13 Options and Options Analysis

4.13.1 Option 1. Retain existing Internal Audit arrangements. The scope and approach of Internal Audit will remain the same;

4.13.2 Option 2. Develop a more comprehensive corporate approach to assurance through extending the remit of Internal Audit.

	Option 1- retain existing arrangements	Option 2 – incorporate responsibilities for coordinating assurance into the Internal Audit function
Advantages	None identified.	An opportunity to develop corporate understanding of the Council's sources of assurance and its associated organisational performance; better value for money Greater clarity regarding sources of assurance; better able to avoid duplication of effort. Provides an opportunity for Internal Audit plans and work to be more focused on significant risk areas. Increased scope and effectiveness of the Audit Committee in reviewing the Council's governance arrangements
Disadvantages	The effectiveness of Internal Audit and the Audit Committee do not develop. Does not fit well with other plans for information governance and anti-fraud arrangements.	None identified
Risks	Potential for wasted resources / duplication of effort through a lack of understanding about assurance	May divert resources away from other Internal Audit activity

4.14 **Officer Preferred Option**

4.15 Option 2 is preferred. As a service to the effective governance and management of the organisation, there is clear scope to develop the Council's systems for the collation and evaluation of assurance. This principle aligns well with the proposed developments in information governance and corporate anti-fraud arrangements.

5 **Details of Consultation**

5.1 Where appropriate, consultation has been undertaken with the Council's partner authorities. Any specific staffing consultation would be undertaken in accordance with the Council's protocols, where the Council is the employing authority

6 **Conclusion**

6.1 Much work has been done to develop proposals that strengthen the Council's service provision and governance arrangements, whilst containing costs within existing budgets and/or providing opportunities to secure savings. Whilst the service areas concerned may not necessarily be appreciated directly by the public, nonetheless they are essential for effective service delivery, sound governance, and the safeguarding of resources.

RELATIONSHIP TO POLICY FRAMEWORK

As stated in the Corporate Plan, a key element in ensuring its successful delivery is having sound governance arrangements in place. The proposals also fit with the Council's ethos.

CONCLUSION OF IMPACT ASSESSMENT

(including Health & Safety, Equality & Diversity, Human Rights, Community Safety, HR, Sustainability and Rural Proofing)

Any impacts would be addressed through the delivery of particular services.

LEGAL IMPLICATIONS

Legal Services have been consulted and have no observations to make in respect of the proposed anti-fraud provisions and with regards to ICT/Information Management proposals they are acceptable subject to appropriate consultation with the affected staff.

FINANCIAL IMPLICATIONS

As set out in the report.

In summary, savings of at least £84K would be achieved next year, with the potential for this to increase, predominantly through the results of anti-fraud work. Although savings should accrue from such activity in subsequent years, at present, for prudence the proposals are assumed to be budget neutral.

OTHER RESOURCE IMPLICATIONS

Human Resources/ Information Services / Property / Open Spaces:

As referred to in the report.

SECTION 151 OFFICER'S COMMENTS

The s151 Officer has been consulted and has no further comments.

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and has no comments to add.

BACKGROUND PAPERS

None.

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