

Open Report on behalf of Pete Moore, Executive Director of Finance and Public Protection

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| Report to: | Audit Committee |
| Date: | 25 March 2019 |
| Subject: | International Audit Standard - Response to Management Processes Questions |

Summary:

This report provides the Committee with an assessment around whether the County Council and Pension Fund financial statements may be mis-stated due to fraud or error.

Recommendation(s):

To consider if the assessment accurately reflects the Council's management processes to minimise the risk of fraud or error in the County Council and Pension Fund financial statements.

Background

Each year the External Auditors are required to obtain an understanding of the Council's management processes in a number of areas. The International Auditing Standards specify the areas concerned and each one is listed below, together with the details of our current processes.

Note: A material mis-statement for the Authority's accounts in 2018/19 is £13m for the Council and £22m for the Pension Fund.

1. An assessment of the risk that financial statements may be materially mis-stated due to fraud

There are a variety of controls to ensure that the accounts are accurate and reflect properly authorised expenditure and income due to the Council.

Accounting – the form of the accounts is mainly prescriptive from the CIPFA code of practice and the accounting processes are determined by the Executive Director of Finance and Public Protection. There are regular reconciliations covering bank reconciliation, payments, payroll and suspense accounts. Access to make journal entries in the accounts is restricted and year end manual accruals in excess of £100k are subject to separate authorisation.

Orders and Payments – access is restricted through formal schemes of authorisation. Few payments are now made by cheque, but where they are used cheque payments in excess of £50k require release by senior finance staff. There are formal procurement and tendering rules for contracts.

There is segregation of duties between purchase and payment and appropriate levels of authorisation have been set.

Monitoring expenditure and income – every area of expenditure and income is the responsibility of a named budget holder. Throughout the year Budget Holders are required to regularly review the accuracy of payments and income.

Statement of accounts – there are a variety of year end reconciliations and checks. Line managers review officers' work, and the accounts are reviewed by the County Finance Officer.

2. An assessment of the risk that the Pension Fund statements may be materially mis-stated due to fraud

In addition to the arrangements described above, there are a number of specific controls and requirements which apply to the administration of the Lincolnshire Pension Fund. The fund is not subject directly to any laws and regulations that are any different to other bodies in the same sector:

- UK law which applies to pension schemes including Act of Parliament and regulations
- European law
- Case law which is relevant to pension schemes

The Local Government Pension schemes are regulated by a range of specific statutory requirements, the main ones being:

- Local Government Pension Fund (Management and Investment of Funds) Regulations 2016
- Local Government Pension Scheme Regulations 2013

The accounts format and content is covered by the Pensions SoRP and underpinned at a high level by the Accounts and Audit Regulations as well as the specific Codes published under statute such as the CIPFA Codes covering the accounts.

The Council employs external investment managers to make most investment decisions and a custodian holds the investment certificates which add further assurance to the overall control environment. The Council receives annual auditor assurance reports from these organisations.

The Pensions Committee approves the investment policy of the Fund and monitors its implementation during the year. The Committee meets, as a minimum, on a quarterly basis and special meetings are convened if considered necessary. The Committee membership includes representatives from the County Council, district councils, other employers and trade unions. The Council has a Pensions Board in place which overviews the governance arrangements for management of the Fund as well as compliance with the requirements of the Pensions Regulator.

3. Identifying and responding to risks of fraud in the organisation

Our proactive counter fraud work and whistleblowing arrangements help us fight against fraud and reduce our exposure to the risk of fraud. Our annual report provides information on the outcomes of this work.

The Council has recognised the importance of protecting the public purse and has maintained a robust response through its dedicated Counter Fraud Team.

The risk of fraud is included in our risk management processes. We have developed a Fraud Risk Register; this is regularly updated and is reported to the Audit Committee.

We also work with other local authorities to share good practice and undertake joint work e.g. raise awareness. This is enhanced by the Lincolnshire Counter Fraud Partnership – reporting directly to the Chief Finance Officer Group and tasked with carrying out county-wide fraud proactive exercises in areas of high fraud risk. We also take account of best practice and emerging fraud issues published by the CIPFA Counter Fraud Centre and in the national strategy: Fighting fraud and Corruption Locally.

Outcomes and progress of our proactive counter fraud work is monitored by our Audit Committee.

The difficulties experienced with the introduction of the Council's new financial system (Business World) have been rectified and the financial control environment improved - adequate.

Internal Audit has scheduled follow up testing in key control areas and continues to perform data analytical work.

During 2018 an external firm was engaged to undertake a payments recovery audit dealing with duplicate payments, unrecovered VAT and unrecovered balances on vendor statements. This covered 5 financial years. The results of this work uncovered £555k net (£167k duplicates, £233k VAT and £155k vendor statements).

Access controls and segregation of duties will be reviewed and strengthened as part of Business World rebuild.

Appendix A includes our response to a series of fraud related questions which will also help to inform External Audit's assessment of the risk of fraud and error within the Authority and Pension Fund financial statements.

4. Communication to employees of views on business practice and ethical behaviour

Employees are made aware of these via:

- The induction process
- The Code of Conduct for Employees
- The Council's value statement
- The Constitution, particularly Financial Regulations
- Internal communications through our intranet GEORGE
- Training courses and eLearning

Responses to the 2017 Employee Survey confirmed that staff had been informed of core values and behaviours. The survey also showed that employees were aware of the whistleblowing policy and process.

A Governance Review – culture and values has been undertaken in 2018/19. This showed a strong culture around integrity and values and that the ethical framework for the Council is working effectively.

5. Communication to those charged with governance of the processes for identifying and responding to fraud

The Audit Committee is informed by:

- The review of the Counter Fraud and Whistleblowing policies which are based on good practice
- Fraud Risk Register Reports
- Approval and progress reports on the delivery of our Counter Fraud Work Plan
- The Authority's Annual Governance Statement
- Internal and External Audit Plans and Reports
- The Final Accounts scrutiny and other External Audit Reports

6. Awareness of any actual or alleged instances of fraud

During the last 12 months, our counter fraud team has been involved in a number of investigations. The combined value does not represent any material effect on the financial statements. The Authority has also recovered fraud losses in year and has taken all reasonable action to seek redress, where possible.

7. **Compliance with laws and regulations and the potential for litigation and claims that would affect the financial statements**

The Authority's Constitution provides the framework for the Council's governance arrangements and, as well as this:

- The Monitoring Officer is responsible, after consultation, for reporting to full Council or Executive, if it is considered that any proposal, decision or omission would give rise to unlawfulness.
- Legal Comments are contained in reports to Council, the Executive and Committees to advise on compliance with the policy framework and the Constitution.
- The Executive Director – Finance and Public Protection has responsibility to highlight any proposal, decision or course of action which will involve any unlawful expenditure and the financial impact of any decision.
- The Council has a strong overall control environment which aims to reduce the risk of potential litigation and claims arising. Regular Internal Audit reviews occur to ensure compliance with established controls.
- A robust assurance framework underpins the Council's governance arrangements – it is regularly updated and periodically reviewed to ensure continued effectiveness.
- There are clear policies in place which are routinely updated and communicated throughout the Authority. The Council has strong, well established corporate functions which, along with the ongoing support from its legal advisors, help to minimise the risk of non-compliance with laws and regulations.
- The risk management process assesses the key risks facing the Council and takes measured risks that seek to minimise impact and maximise benefits / innovation.
- Our insurance cover helps us minimise our exposure to potentially large claims.
- Instances of potential claims will be acknowledged, if appropriate, as a contingent liability in the financial statements of the authority.

Conclusion

Given the above information the Council is assessed as **low risk** that the financial statements may be materially mis-stated due to fraud or error.

Consultation

a) Policy Proofing Actions Required

N/A

Appendices

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| These are listed below and attached at the back of the report | |
| Appendix A | Response to fraud and error questions |

Background Papers

No background papers within Section 100D of the Local Government Act 1972 were used in the preparation of this report.

This report was written by Lucy Pledge, who can be contacted on 01522-553692 or lucy.pledge@lincolnshire.gov.uk .