

South Essex Homes Limited

Report of the Head of Internal Audit
to

Audit Committee

on

17 May 2017

Report prepared by: Linda Everard

Head of Internal Audit Annual Report 2016/17

A Part 1 Public Agenda Item

1 Purpose of the Report

- 1.1 To provide, for the 2016/17 financial year:
- the rationale for and an audit opinion on the adequacy and effectiveness of South Essex Homes (the company's) risk management, control and governance processes
 - a statement on conformance with the UK Public Sector Internal Audit Standards (the Standards) and the results of the Quality Assurance and Improvement Programme.

2 Recommendations

2.1 The Audit Committee:

- **accepts the Head of Internal Audit's Annual Report for 2016/17**
- **satisfies itself that the contents of this report are appropriately reflected in the company's Annual Governance Statement.**

3 Background

- 3.1 The Head of Internal Audit's Annual Report and Opinion provides the company with an independent source of evidence regarding both the design of its risk management, control and governance framework and how well it has operated throughout the year.
- 3.2 The company is not required to produce a Governance Statement for its own purposes. However as a wholly owned subsidiary, it is required to provide Southend-on-Sea Borough Council (the Council) with evidence of the robustness of these arrangements in support of the disclosures it needs to make in its Annual Governance Statement.
- 3.3 The opinion is predominantly based upon the audit work performed during the year as outlined in the risk based Audit Plan agreed with the Executive Management Team and the Audit Committee.
- 3.4 As outlined in the Internal Audit Charter, audit coverage is determined by prioritising the significance of company's activities to its ability to deliver its Aims.

This is done:

- using a combination of Internal Audit and management risk assessments (including those set out in risk registers)
- in consultation with Group Managers, Directors and the Chief Executive, to ensure the work is focused on key risks.

3.5 At least, six monthly meetings are then held with the Chief Executive and Directors to:

- reflect on the original risk profile and work planned
- determine whether any changes are required to it or the Audit Plan.

Organisationally, this reflects a very mature approach to operating an internal audit function.

3.6 All individual audit reports are presented to the Audit Committee having first discussed and agreed them with the relevant Group Manager, Director and or the Chief Executive.

4 Head of Internal Audit Opinion for the year ended 31 March 2017

4.1 ***Overall, the risk management, control and governance framework designed by the company to deliver its objectives; and operated throughout the year, has remained satisfactory.***

The opportunity to strengthen the arrangements for letting and managing contracts, has been identified and is being addressed by the company.

4.2 **The basis for forming this opinion is an assessment of:**

- the design and operation of the underpinning governance and assurance framework
- the range of individual opinions arising from risk based and other audit assignments that have been reported during the year taking into account the relative significance of these areas
- whether management properly implement actions arising from audit work completed, to mitigate identified control risks within reasonable timescales
- any other assurance available from independent sources.

4.3 The Head of Internal Audit has not reviewed all risks and assurances relating to the company's activities in coming to her opinion.

5 Supporting Commentary

5.1 **Appendix 1a** summarises the audit opinions from each audit completed this year.

5.2 The following paragraphs then:

- summarise the findings from this audit work
- highlight the key areas requiring improvement
- expand on how assurance obtained from other relevant sources has been used to support the overall opinion.

- 5.3 Where necessary, actions have been agreed with officers to improve the arrangements where the more serious control issues were identified during the audits.

Governance and Assurance Arrangements

- 5.4 A robust **Risk Management** Framework had been designed and implemented within the company in that:

- the approach was found to be fit for purpose
- roles and responsibilities had been clearly defined
- there was evidence of compliance with the approved Strategy
- the arrangements were appropriately embedded into operational and strategic management activities.

The Strategy showed a clear commitment to further embedding and strengthening these arrangements. Action was being taken to:

- produce guidance on what the one to five ratings of likelihood and impact means and how to apply them
- evaluate the company's aspirations around risk maturity against a defined model, and use this to inform the next Risk Management Strategy and Action Plan.

- 5.5 The company had made good progress in getting most of the amendments proposed in the original audit report, made to the **Service Level Agreements** (SLAs) it has with Southend-on-Sea Borough Council (the Council). As a result the SLAs more clearly and comprehensively set out the company requirements. They still needed to be approved by both parties. Further discussions were required to resolve the outstanding issues with the IT SLA, before this could be signed off.

The following matters needed to be included in the respective contract monitoring meetings:

- legal cases where the provider has represented the company and the opportunity to improve working practices has been identified, including where issues were raised by the court
- outcomes of the HR employee relation cases.

Discussions were in train to see whether useful benchmarking performance information could be provided for each service provided under an SLA.

Finally, although all the SLAs designate a Lead Officer, there was still a need to clarify their specific monitoring / management responsibilities within each document.

- 5.6 Other internal assurance has also been taken from the:

- performance and effectiveness assessments completed by the Audit Committee
- arrangements established to validate the Management Assurance Statement assessments.

(Refer to the Audit Committee Annual Report)

Service Risks and Key Financial Systems

5.7 Good progress had been made in implementing the actions contained in the original **Careline report**. As a result:

- the arrangements for quality assuring calls taken by Careline staff had been strengthened with this information being more tangibly used to identify training and development needs. The training plan was to be delivered by the 31 March 2017
- a more targeted set of reports were being used to performance manage key Careline activities
- a formal programme of testing the disaster recovery process and recording this had been introduced, to ensure lessons learnt were captured and acted upon
- roles and responsibilities for testing Careline equipment had been clarified and more detailed procedures introduced explaining how these should be carried out.

The element of the Tunstall contract costs that related to Careline still needed to be identified and added to its budget. Although approval had been obtained to gradually increase the charges for this service to nearer the market norm. Action was also being taken to:

- move to monitoring how well Tunstall deals with system faults within 24 instead of 48 hours and ensure all calls reported were being captured by them
- complete the business review of the Careline service and develop a plan to agree and deliver any necessary re-branding and marketing
- establish how best implement a stock management system as well as a stock holding and ordering policy.

5.8 There was a good process in place for reporting **responsive repairs** work to the contractor. The company had established a framework for then managing delivery of the contract, which worked well. Opportunities to strengthen aspects of this and use it more effectively to improve overall performance monitoring were identified.

Urgent action was being taken to bring the delegated authorities for approving works and variation orders, in line with those agreed by the Executive Management Team.

Further work was also planned to:

- introduce independent checks to ensure the annual changes to the Schedule of Rates are correct
- introduce monitoring arrangements for completing rejected and / or recalled work as well as delivering community benefits and training targets
- improve the arrangements for reporting post inspections to give greater transparency on the number of visits made and allow senior managers to better consider the potential risks if levels of inspections fail to meet the targets set.
- improve the arrangements for tracking the implementing of actions agreed to improve service delivery, monitoring.

- 5.9 The **Right to Buy** process urgently needed to be updated to reflect the requirements of the Housing Act 1985 (amended) in respect of notifying secure tenants of their Right to Buy.

Nevertheless, staff demonstrated a good understanding of the statutory requirements and good practice guidance when processing applications despite out of date procedures. Action was being taken to update them by setting out expectations for each step in the process (including how they should be evidenced) as well as strengthening the management checks undertaken before the offer is made.

There were also opportunities to work more effectively with other services (e.g. Adaptations, Asset Management and Housing) to ensure all the relevant information is obtained wherever possible, before offers are made.

The company was looking to work more proactively with the Counter Fraud & Investigation Directorate to both identify and stop right to buy fraud at the earliest possible stage in the process. This is a very positive step and is to be commended.

- 5.10 Overall, satisfactory arrangements were in place regarding the **Housing Rents system** (iWorld), to both raise and then collect rental income from Council house tenants. The element of the system managed by the company was well controlled.

Going forward, evidence will be retained to demonstrate that the reconciliation between rent account information on iWorld and that provided by the Council, has been independent checked. Action was being taken to enable the same type of reconciliation to be undertaken annually for non-domestic properties and assets.

Process under the control of Southend-on-Sea Borough Council

Management continued to accept the risk that the Tenancy Management Team can amend both tenancy and rent accounts on iWorld because of the way system access risks were grouped together. This risk was mitigated by periodic, independent checks of newly created rent accounts and tenancy terminations to confirm:

- separation of duties had been maintained
- staff had not actioned something outside the agreed parameters for their role.

Once the next iWorld upgrade is implemented, the system will prevent users accessing or modifying accounts of tenants where there might be a conflict of interest.

- 5.11 Overall, the **Accounts Receivable** arrangements for ensuring all relevant income was billed for, in a timely manner, and debt collected were satisfactory.

The Rechargeable Works Policy (which made up the majority of invoices raised), clearly defined how outstanding debt would be recovered from tenants. A similar document was required for companies and ad-hoc debts. All the other supporting policies and procedures were fit for purpose and had been reviewed in the last 12 months.

All management fees were accurately invoiced in a timely manner. Requests to raise rechargeable works invoices only provided an approximate charge. The invoice could not be raised until work was shown as completed on iWorld (the company's housing database). However, the Accounts Receivable team was not checking the system regularly therefore invoices were not being raised in a timely manner.

The management of credit notes was considered to be well controlled. Few refunds were given but approval limits should be documented within the Scheme of Delegation.

Reminder letters had not been sent to debtors regularly as the Accounts Receivable team had not routinely been running reports that triggered the debt recovery process. Nevertheless, the three stage reminder system used was deemed to be appropriate. The company had a number of debts owed which are over two years old. Action was required to determine whether they were recoverable or needed to be written off. Write offs had also been approved in line with the Scheme of Delegation.

The Finance team had appropriate access rights to Agresso's Accounts Receivable module. Periodic action was required to check that remained so. The Accounts Receivable Control Account was reconciled properly with the General Ledger on a monthly basis and validated. The regular report produced on the company's financial position should be amended to include debt management information.

Implementing Action Plans

- 5.12 Action plans from audit reports have only been revisited this year if the control weaknesses identified were more significant (e.g. where a partial or minimal assurance opinion was given). The results of this work have been reported to the Audit Committee as part of the Quarterly Performance Report.

Senior management have been responsible for satisfying themselves that high and satisfactory opinion audit report action plans have been properly implemented. This is monitored through the Operational Management Team.

6. Conformance with Professional Standards

Head of Internal Audit Opinion

- 6.1 ***The service has substantially conformed to the relevant professional standards throughout the year.***

Resourcing

- 6.2 In July 2015, Southend-on-Sea Borough Council decided to undertake a service review of Internal Audit so permanent recruitment was stopped. All subsequent vacancies were covered by:
- resources bought in through framework contracts with external suppliers
 - agency or casual staff and staff on short term contracts.
- 6.3 BDO was appointed to complete the service review, which occurred during January / February 2016. It was concluded in August 2016 at which time permission to recruit and rebuild the in-house team was granted.
- 6.4 By August 2016, the combined in-house team of nine auditor posts had gone from carrying four to seven vacancies, one of which has been covered by a long term contractor. It became a substantially contracted out service, with the Head of Internal Audit also covering the contract manager role.

The lack of management capacity during this period has had a significant impact on the performance of the service and its ability to deliver its normal performance targets. Recruitment for permanent staff commenced in January 2017. However, the remainder of the report needs to be considered within this context.

Audit Plan 2016/17

6.5 The target was to delivery 100% of the Audit Plan by the May Audit Committee meeting. In the event:

- 7 reports have been issued
- 3 reports are currently being finalised with officers
- 1 audit is in progress.

Appendix 1b shows the final status of the Audit Plan. Therefore the Head of Internal Audit's annual audit opinion is based upon the work completed.

The outstanding reports will be reported to the Audit Committee in July 2017.

Other Performance Indicators

6.6 The service had a performance target this year of issuing draft reports to clients within 15 working days following the final meeting with officers to feedback on work done. Unfortunately this requirement was not been met in the latter part of the year due to changes in the mix of staff resources available to the team.

6.7 During the year, the service revised its approach to obtaining feedback from stakeholders at the conclusion of audits so it focused more on obtaining evidence of compliance with some of the less tangible elements of the UK Public Sector Internal Audit Standards (the Standards).

The key message from the surveys undertaken is the need for there to be a more seamless service regardless of whether work is undertaken by the in-house Internal Audit team or contracted in resources.

Cost

6.8 The cost of the service remains competitive, as discussed by the Audit Committee when a new three year Service Level Agreement was approved by in February 2016.

Quality and Improvement Programme

6.9 I can confirm I have maintained an appropriate Quality and Improvement Programme (QAIP) during the year for the in-house team or work undertaken by contractors when being managed by the in-house team. As required by the Standards, this consisted of:

- on-going supervision and review of individual audit assignments completed by in-house staff or contractors working to in-house staff
- reporting on a limited set of performance targets to the Audit Committee each quarter (for all work done including that of the external supplier)
- undertaking a self assessment which evaluates conformance with the Standards.

Due to resource constraints, there have been no independent files reviews of in-house staff or contractors work completed this year.

I have received assurance from the external suppliers that where they have undertaken work using their own audit approach, this is also compliant with the Standards.

- 6.10 The service completed its annual self assessment of compliance with the Standards. This has been provided to the company with details of the actions the team plans to take over the coming year to improve its working arrangements, which include:
- updating the Charter and supporting documents to reflect changes in the management arrangements at the company
 - organising the independent external assessment of the service's compliance with professional standards and then refreshing the audit approach / Audit Manual
 - introducing a more structured approach to working with Group Managers on the delivering of the Audit Plan
 - destroying all audit files that fall outside the data retention policy period.

It also captures processes that will be reintroduced as the proportion of in-house resources increase.

Other Disclosures

- 6.11 As required by the Standards, I can confirm that the Internal Audit service has:
- operated in a manner that maintains its organisational independence throughout the year
 - been able to determine the scope of reviews, perform the work and report on its findings without interference neither has there been any inappropriate resource limitations imposed upon it.

Conclusion

- 6.12 Therefore, it is possible to conclude that the company maintained an adequate and effective internal audit service during 2016/17.
- 6.13 The service will continue to maintain an action plan that captures opportunities to strengthen its operating arrangements as and when they arise. The results of this work will be reported to the Audit Committee periodically.

7 Issues for the Annual Governance Statement

- 7.1 No issues have come to my attention relating to either the company or the operation of its Internal Audit Service that I believe need to be disclosed in its Annual Governance Statement, other than those already identified.

8 Diversity and Equal Opportunities

- 8.1 There are no direct diversity or equal opportunities issues to consider as a result of this report.

9 Risk

- 9.1 Failure to operate a robust assurance process (which includes an internal audit function) increases the risk that there are inadequacies in the internal control framework that may impact upon the ability of the company to deliver its objectives.

10 Financial Implications

- 10.1 The Audit Plan was delivered within approved budgets.

11 Resident Consultation

- 11.1 None.

12 Background Papers

- UK Public Sector Internal Audit Standards
- CIPFA, Local Governance Application Note for the UK Public Sector Internal Audit Standards
- CIPFA, The Role of the Head of Internal Audit in Public Service Organisations 2010
- CIPFA, Audit Committees, Practical Guidance for Local Authorities and Police 2013.

13 Appendices

Appendix 1a Assurance Summary 2016/17

Appendix 1b Internal Audit Plan 2016/17 as at 5 May 2017