

LONDON BOROUGH OF MERTON

INTERNAL AUDIT ANNUAL REPORT YEAR ENDING 31ST MARCH 2020

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1. Head of Audit Assurance Opinion

1.1 As Head of Internal Audit for the London Borough of Merton, I am required to provide the Council with an opinion on the adequacy and effectiveness of the internal control environment: I base my opinion upon:

- All internal audit assignments undertaken during the year
- Any follow up action taken in respect of previous audit work
- Any significant recommendations not accepted by management and the consequent risks
- Matters arising from previous reports to the Standards and General Purposes Committee
- Any limitations, which may have been placed on the scope of the internal audit.

Opinion

I am satisfied that sufficient internal audit work has been undertaken to allow me to draw a reasonable conclusion as to the adequacy and effectiveness of the Council's control environment. In giving this opinion, it should be noted that assurance can never be absolute and, therefore, only reasonable assurance can be provided, subject to the limited assurance opinions detailed in this report.

1.2 Where weaknesses in controls have been identified, action plans are in place. It is important that departments ensure that audit actions are implemented in a timely manner to ensure effective controls are in place.

2 The Internal Audit Assurance Framework

2.1. A key responsibility of Internal Audit is to give the organisation assurances about the levels of internal control being exercised in the areas of risk and in particular, where there are transactions that are considered "material" to the Council.

2.2. In order to give such an assurance, a balanced programme of Internal Audit reviews is constructed each year. This Annual Internal Audit Plan contains elements of all the Council's activities selected using a "Risk Based" approach. There are many tools used to achieve a balanced plan including undertaking systems reviews, regularity audits (e.g. schools), contract and computer audit, fraud and misappropriation reviews and an annual review of major financial systems such as the main accounting system, payroll, Council Tax and Housing Benefits.

2.3 For each audit carried out, Internal Audit provides an opinion as to the quality of the control environment in the following processes:

- Risks have been identified, evaluated and managed
- Internal controls reduce risks to acceptable levels
- Action is being taken to promptly remedy significant failings or weaknesses
- The current levels of monitoring are sufficient

2.4 Each audit is given an opinion based on 4 levels of assurance depending on the conclusions reached and the evidence to support those conclusions. Members and management should note that the assurance level is an opinion of controls in operation at the time of the audit. The auditor will agree with management a number of recommendations which, when implemented, will result in a reduction of the exposure to risk. Each recommendation is given a priority ranking and an implementation date and these are monitored on a regular basis by the Internal Audit team. Priority 1 recommendations are defined as being those where major issues have been identified for the attention of senior management.

Levels of assurance	
Full Assurance	There is a sound system of control designed to achieve the system objectives and manage the risks to achieving those objectives. No weaknesses have been identified.
Substantial Assurance	Whilst there is a largely sound system of control, there are some minor weaknesses, which may put a limited number of the system objectives at risk.
Limited Assurance	There are significant weaknesses in key control areas, which put the system objectives at risk.
No Assurance	Control is weak, leaving the system open to material error or abuse.

PRIORITY OF RECOMMENDATIONS	
1	Major issues that we consider need to be brought to the attention of senior management.
2	Important issues which should be addressed by management in their areas of responsibility to avoid exposure to significant risk.
3	Minor issues where the risk is low. Action is advised to enhance control or improve operational efficiency.

2.5. In addition, each recommendation emanating from the audit review is given a priority rating of 1, 2 or 3 for implementation, with priority 1 being a high risk requiring immediate attention. All recommendations are followed up by Internal Audit to ensure that they have been implemented.

- 2.6. The audit plan for 2019/20 covered those area of high fraud risk, as identified through the Council's own assessments and through information from CIPFA, and other sources, where fraud risks are highlighted. Examples of these are procurement cards and direct payments.
- 2.7 These audits reviewed the controls in place, although no fraud was identified in any of these reviews, a number of recommendations were made to improve the controls.

3 Planned coverage and output

- 3.1 The total number of audit days commissioned for 2019/20 was 765 days. We can report that we have completed 100% of the total number of commissioned audit days.
- 3.2 The plan was compiled with reference to the Council's Corporate Risk register and following discussions with each departmental management teams (DMTs). This ensured that audit work was focused on the Council's key risks and targeted areas where senior managers required independent assurance over controls in their service areas.
- 3.3 Changes to the plan and updates on progress were discussed at DMT's quarterly and significant changes reported to the Standards and General Purposes Committee in the progress reports.
- 3.4 In terms of reports delivered by the audit team, the audit plan at the start of the year included 48 audits. The plan is always flexible to allow for movement in the number of audits in the plan and the days delivered reflecting changing client needs. The overall number of reports will be subject to change over the course of the year as audits may be deferred or no longer required. However, additional reviews may be added if concerns are raised about a specific control area or existing reviews may have their budgets increased. During the year, there were 6 additional audits requested. These have ranged from full audits to focused audit investigations. These included:
- Planning
 - School fund review
 - Voluntary sector
 - Conflict of issue concern
 - Contract compliance
 - Court case preparation
- 3.5 These referrals to Internal Audit help to demonstrate the continued good engagement from departments and their awareness of the role of Internal Audit and the work that they can undertake to support their service. The Council's risk profile is constantly changing. Therefore, Internal Audit and the internal audit plan need to be flexible to be able to respond to these changing and emerging risks.
- 3.6 The Internal Audit function is conscious of the significant pressure on resources that the Council is facing and has continued to identify where we can support

management through looking to identify potential efficiencies and making recommendations for possibly fewer but better controls wherever possible.

4. Internal Audit Assurances 2019/20

- 4.1. There were 43 audit reviews undertaken during 2019/20, of these 32 have provided an assurance opinion (8 reviews were advisory and 3 relate to grant claims or signing off accounts). There were 24 substantial assurances (75%) and 8 limited assurances (25%).
- 4.3 A full list of the assurances can be found in Appendix A. Action Plans for improvements are in place for all audits. The following tables summarise the results by audit type:

Table 1 Internal Audit Assurances by Audit Type 2019/20

Assurance	assurance	Limited	Totals
Procurement	1	0	1
schools	5	1	6
Financial	8	2	10
IT	0	1	1
Service Specific	6	4	10
Corp Gov	4	0	4
Totals	24	8	32

Financial systems

- 4.4 There were six key financial systems reviewed this year, which all received a substantial assurance.

Table 2 Key Financial systems audit assurance for last 3 years

Financial System	Assurance 2017/18	Assurance 2018/19	Assurance 2019/20
Payroll (iTrent)	Satisfactory	Substantial	Substantial
Accounts Payable	Satisfactory	Substantial	Not audited
Fixed Assets	Satisfactory	Not audited	Substantial (valuation review)
Debtors	Not audited	Not audited	Substantial
Housing benefits	Satisfactory	Not audited	Not audited
Treasury management/pension investment	Limited	Substantial	Substantial
Council Tax	Not audited	Not audited	Substantial
National Non-Domestic Rates (NDR)	Satisfactory	Not audited	Not audited
General Ledger	Satisfactory	Substantial	Not audited
Pension Administration	Not audited	Not audited	Substantial

- 4.5 In addition to the in-house work, there has been a joint 3 borough audit undertaken on the iTrent payroll system. This was led by the London Borough of Sutton as host authority for the system, and they commissioned an audit report, the scope for which was agreed by all 3 boroughs using the system (Kingston, Sutton and Merton). The audit was awarded Substantial Assurance opinion which is the same opinion as given in 2018/19.
- 4.6 Other financial reviews this year have been carried out on Petty Cash Imprest, which had a substantial assurance and BACS/CHAPS and Procurement Cards had a Limited assurance. Duplicate payment testing has also been carried out.

Key Areas for 2019/20

- 4.7 Internal Audit has continued to improve their level of engagement with all levels of management. This has been achieved by attending regular DMT's to discuss audit progress, meeting with key stakeholders prior to the start of the audit to agree the audit brief.
- 4.8 When the audit plan is set, discussions are held with all key people for input; this engagement has enabled the Internal Audit team to focus on the key areas of risk as well as work closely with management to formulate actions to address areas where improvement is required.
- 4.9 As set out in the above section we have identified areas of good practice and an effective control environment across the majority of the systems, processes and establishments reviewed. This includes the Council's key financial systems.
- 4.10 However there are a number of areas where further improvements are required to strengthen the control environment and we have summarised the key issues below.

Table 3: Priority 1 recommendations

Audit	Assurance Opinion	Number of P1's	Implemented
BACS/CHAPS	Limited	4	Yes
Procurement Card – Transfer System (Pay Pal)	Limited	2	Yes

Payment Card Industry Data Security Standard	Limited	3	No
Tree Maintenance	Limited	1	No
Perseid School	Limited	6	Yes
Deprivation of Liberty safeguards	Substantial	2	Yes
Interim Staff Review	Substantial	6	Yes
Prepaid Cards*	Limited	5	n/a
No Recourse to Public Funds*	Limited	2	n/a
Direct Payments*	Limited	4	n/a

*reports to be finalised

Key issues (These have previously been reported to Standards and General Purposes Committee)

- 4.11 **BACS/CHAPS** -At the time of audit, the treasury management processing document required updating to detail the process for non-treasury CHAPS payments. It was found that there had been a significant increase in non-treasury CHAPS payments since the last audit review. Requests for CHAPS payments should be reviewed to ensure they can be justified and remain cost effective for the Council. The process for checking supporting documentation requires review as the different teams involved were unclear on their roles and responsibilities.
- 4.12 Audit testing found 7 out of 14 payments checked that the voucher request had not always been fully completed at the time of the payment being processed. The BACS Preparation/Transmission form is prepopulated with names of officers that can request and transmit a BACS payment request. A review of the names on the form found that several named officers are no longer working with the Council, it was also found that two officers have the ability to process as well as authorise and submit BACS submissions.
- 4.13 Access to the PayGate system found that the system functionality to force password change is either disabled or not in place. Some employees in IT Services have retained their access to the PayGate system but are no longer involved in the processing of BACS payments.
- 4.14 **Procurement Cards**– Transfer System (Pay Pal)- Although it is detailed in the Procurement Card user guide that PayPal is excluded from Procurement card use, PayPal was found to be used by 32 cardholders in 2018/19 and by 10 cardholders in 2019/20 (April to June).
- 4.15 The use of PayPal for procurement card expenditure is not permitted by the authority as the statement name can be defined by the account holder and therefore, potentially differ to that of the actual payee. Sample testing of Paypal transactions found that 2 out of 8 receipts did not state the supplier's details.
- 4.16 **Payment Card Industry Data Security Standard**- An Annual IT PSN Health Check had been completed by an external firm for the Council in August 2019,

which identified 3 critically, 6 highly and 11 moderately risky findings, which still required completion.

- 4.17 There was no documentary evidence to demonstrate that the Council conducts quarterly PCI DSS vulnerability scanning or evidence to how Senior Management are monitoring the compliance programme.
- 4.18 **Tree Maintenance** - There was no clear direction on how trees are managed by the council. At the time of the audit there was no final Strategy, Policy and Business Plan for the management and maintenance of the Council tree stock. As a result, the service focused on responding to resident requests rather than to a set maintenance program. There was also a significant backlog of resident's tree work requests that had not been entered onto the Highways tree system or responded to.
- 4.19 **Perseid School**- At the time of audit, the school did not have a three-year budget plan and no significant recovery plan for the deficit budget. Budget monitoring did not include commitment accounting. The school did not undertake IR35 checks when making payments for work done at the school. Access rights to the school financial system could not be verified by the school.
- 4.20 **Deprivation of Liberty safeguards** At the time of audit, the service had a 2 year contract for the provision of independent mental capacity, which started in 2011 with an option to extend for a further 12 months. This contract had continued to be extended since then. The contract is a set fee of £20,000 per year, but it was found that its use had decreased each year. A review needs to be undertaken to ensure it is providing value for money as well as meeting the needs of the service.
- 4.21 Sample checking of spot purchases invoices found that invoices had been incorrectly paid. A process needs to be put in place to review invoices for correctness, ensuring that the service has been provided.
- 4.22 **Interim Staff Review** - This audit received Substantial assurance although a number of issues were highlighted for improvement. Where there were longer term agency placements, attempts to recruit need to be evidenced clearly. Managers need to ensure that leaver's forms are completed for all agency leavers to ensure that their IT access is discontinued and IT equipment returned.
- 4.23 Supporting documentation and Comensura records must be completed to evidence the correct procedures followed for the recruitment of agency staff. Contract documentation was not in place for all consultants. Procedures for the appointment of sessional staff was not consistent across the council.

Draft reports –(These will be reported at final report stage to the next Standards and General Purposes Committee) awaiting management comments:-

- 4.24 **Prepaid Cards**- The guidance document previously recommended by Internal Audit in 2016 had been drafted by the service but had not been finalised. There were 14 active accounts open on the system for employees that had left the

employment of the council. Sample testing found that service agreements were not in place for all transactions. Receipts were not available for all expenditure and in 70% of transactions it was not clear why payments had been made on the prepaid card as the users were also in receipt of payments through BACS.

- 4.25 **No Recourse to Public Funds-** As part of the assessment process it is a requirement for the council to check the immigration status of clients requesting assistance. It was found that three adults and two families were not registered on the NRPF connect database. Reviews carried out by social workers were not always consistent and evidence of immigration checks undertaken.
- 4.26 **Direct Payments** -The service user's agreement were found to be under review as they did not fully comply with the most current legislation. A review of a sample of client found that agreements missing, undated or unsigned. Evidence of regular monitoring was unavailable at the time of audit.

5. Implementation of recommendations

- 5.1 During 2019/20 Internal Audit made a total of 218 recommended improvement actions including 24 Priority 1 (P1's) actions. Management has responded to each of our recommendations stating whether action will be taken to implement.
- 5.2 At the time of this report 193 actions (82%) were fully implemented, of these, 21 P1 actions were implemented and 4 are still in progress (1 P1 from 2018/19 is still in progress).
- 5.3 For those outstanding actions, an expected implementation date is provided by the manager. Monthly reports are sent out to all managers for actions due and where these are over two months overdue, the Head of Service also receives a copy. If an action is more than 3 months overdue, then the appropriate Director is informed. Any overdue outstanding audit actions are then reported to Standards and General Purposes committee. No recommendations are overdue and need to be reported to this meeting.

6. Review of the Effectiveness of the System of Internal Audit

- 6.1 A requirement laid down in the Accounts and Audit (England) Regulations 2015 states that 'the relevant body shall, at least once a year, conduct a review of the effectiveness of its internal audit'. An annual self-assessment against CIPFA's Code of Practice for Internal Audit in Local Government has to be carried out each year and an external assessment every 5 years.
- 6.2 A self-assessment has been undertaken against the Public Sector internal audit standard (PSIAS). This demonstrated substantial compliance with the standards. An external Assessment against the PSIAS was carried out in May 2018 and provided substantial assurance. Where actions have been identified these will be reviewed and included in the Quality Action Implementation Plan and progress reviewed.

6.3 The key focus of the review of the effectiveness of internal audit is the delivery of the service to the required standard in order to produce a reliable assurance on internal controls and the management of risks in the authority. In coming to a view on the effectiveness of the system of internal audit, the following factors are all indicators that should be taken into accounts.

- Performance of the internal audit provider (in-house and/or contractors) in terms of both quality and cost.
- Views of external audit & reliance placed on work by internal audit.
- Role and effectiveness of the Standards and General Purposes Committee.
- The extent to which internal audit adds value to the organisation and helps delivery of objectives.

6.4 During 2019/20, the internal audit service has achieved the following:-

- Delivery of 100% of the audit plan
- 100% client satisfaction for audit work

7 Fraud Investigations

7.1 The Council's Anti-Fraud and Anti-Corruption strategy sets out the Council's approach to detecting, preventing and investigating fraud and corruption. This strategy is supported by the Council's whistleblowing policy, which was reviewed and updated in 2018 and by the Council's code of conduct. The Internal Audit section has a key role in implementing this strategy and to ensure that the internal controls in place are robust to prevent fraud occurring or to tighten controls where fraud has occurred.

7.2 The South West London Fraud Partnership was established on the 1st April 2015 as a 5 borough shared fraud investigation service between LB Merton, RB Kingston, LB Sutton, LB Richmond and led by LB Wandsworth.

7.3 During 2019/20, the SWLFP has undertaken counter fraud activities in the following areas:

- National Fraud Initiative (NFI)
- Blue badge/parking permits
- Council tax reduction/discount
- Employee fraud
- Housing tenancy fraud/abuse

Investigation caseloads

7.4 In total 142 cases have been opened in 2019/20 as a result of the referrals received and concerns highlighted through proactive fraud drives and NFI

matches during the year. A breakdown of fraud referrals accepted for investigation is shown in the table below:

2019/20 Fraud Category	Sanction Target	Open Cases b/fwd	New Cases in Year	Total Cases	Closed No Sanction	Closed With Sanction	Open Cases c/fwd
Tenancy Fraud	9	41	42	83	37	12	34
Right to Buy	5	7	7	14	7	5	2
Hsg Apps Rejected	20	2	75	77	1	75*	1
Blue badge	n/a	3	4	7	3	1	3
Employee	n/a	9	9	18	3	5	10
CTR/SPD/HB	n/a	1	3	4	2	1	1
Other	n/a	13	7	20	13	0	7
Totals	34	76	147	223	66	99	58

* NFI data match on waiting list

- 7.5 **Tenancy Fraud-** Twelve properties were recovered in 2019/20. This allows for those on the Councils waiting list to be provided with the opportunity for a housing tenancy. Work is ongoing, including three cases with legal for consideration of legal action.
- 7.6 **Right to buy-** applicants are passed to the Fraud partnership and the application checked to Housing Benefit: five RTB applications have been withdrawn following intervention by the SWLFP.
- 7.7 Housing application rejected- 75 applicants have been removed from the housing list following a National Fraud Initiative data match. This would have identified that they were no longer eligible for a housing application

Corporate Fraud (internal)

- 7.8 The corporate fraud cases involving employees for 2019/20, resulted in: -
- 1 disciplinary hearing (dismissed)
 - 2 resignation
 - 2 Prosecutions in progress
 - 3 No Further action
 - 10 in progress

National Fraud Initiative (NFI)

7.9 The NFI matches are: - Creditors, Market Traders, Personal Alcohol Licences, Parking, Payroll, Pensions, Personal Budgets, Residential Care, Council Tax & Electoral Registration. This data is matched between councils and within Merton.

7.10 NFI 2018 – Reports have been released; with additional matches having been released on 31st May 2019. SWLFP are currently reviewing the reports to determine and agree with service the programme of work.

NFI	TOTAL	Closed	In progress	fraud	To review
NFI 2018/19 – Main NFI	6707	291	1612	1/0	4804
Re-Check - Ctax to ER –2019	1,629	0	0	0	1,62
Re-Check - Ctax to ER –2020	1,984	0	0	0	1.984
	10,320	291	1,612	1	8,417

8. LOCAL GOVERNMENT TRANSPARENCY CODE

8.1 Under the code the Council is required to publish the following data regarding its Fraud Investigation activity. Listed below are 2019/20 figures (with 2018/19 comparative figures shown within brackets).

Accredited number of occasions they use powers under the Prevention of Social Housing Fraud (Power to Require Information) (England) Regulations 2014, or similar powers		
	19/20	(18/19)
Prevention of Social Housing Fraud (Power to Require Information) (England) Regulations 2014	12	14
The Council Tax Reduction Schemes (Detection of Fraud and Enforcement) (England) Regulations 2013	3	7
Total number (absolute and full time equivalent) of employees undertaking investigations and prosecutions of fraud		
	Absolute	FTE
Fraud Investigation - SWLFP #	15 (15)	14.5 (14.5)
Total number (absolute and full time equivalent) of professionally accredited counter fraud specialists		
PINS trained Fraud Specialist	7 (6)	7.0 (6.0)
CIPFA Certificate in Investigative Practices	1 (2)	1.0 (2.0)
CIPFA Accredited Counter Fraud Specialist	4 (4)	4.0 (4.0)
Total amount spent by the authority on investigation and fraud prevention		
	19/20	(18/19)
Fraud Partnership	£123.2k	£121.1k
Total number of fraud cases investigated.		
SPD/Council tax reduction/ Housing/Tenancy related Investigations	3 125	4 199
Right to Buy	12	11
Permit Fraud Investigation (blue badge)	4	9
Other Investigations	<u>21</u>	<u>14</u>
TOTAL	165	237

8.2 To ensure that sufficient knowledge and capability for fraud investigation was maintained Merton entered into a partnership with four neighbouring boroughs, the SWLFP. For 2019/20, the number of Fraud investigation officers and officers with specialist fraud qualifications relates to the pool of officers within the SWLFP team that can be called upon, Merton’s funding contribution equates to 2 FTE investigators.