

LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE AUDIT COMMITTEE

HELD AT 7.00 P.M. ON TUESDAY, 26 MARCH 2013

**ROOM C1, FIRST FLOOR, TOWN HALL, MULBERRY PLACE, 5 CLOVE
CRESCENT, LONDON, E14 2BG**

Members Present:

Councillor Carlo Gibbs (Chair)

Councillor Stephanie Eaton

Councillor Abdal Ullah

Councillor David Snowdon

(Deputy Leader of the Conservative
Group)

Councillor Motin Uz-Zaman

(Chair, Overview & Scrutiny Committee)

Other Councillors Present:

Officers Present:

Chris Holme

– (Acting Corporate Director - Resources)

Minesh Jani

– (Head of Audit and Risk Management ,
Resources)

Tony Qayum

– (Anti Fraud Manager, Internal Audit, Resources)

Oladapo Shonola

– (Chief Financial Strategy Officer, Resources)

Paul Thorogood

– (Interim Service Head Finance and HR
Development, Resources)

Antonella Burgio

– (Democratic Services)

Others In Attendance

Shona Milton

– Auditors KPMG

Andrew Sayers

– (KPMG)

Mike Clarkson

– Deloitte & Touche

Tim Hughes

– Sector

Dan Wilson

– Sector

The Chair welcomed Dan Wilson and Tim Hughes of Sector who had been invited to speak to the Committee on the matter of investment. He noted the Chief Financial Officer's request that this presentation and discussion would be more appropriately undertaken after the Committee had considered the Quarterly Treasury Management report. Accordingly, the Chair moved to all vary the order of business and item 4.2 was considered prior to item 4.1.

1. APOLOGIES FOR ABSENCE

Apologies absence were received from Councillors Craig Aston, David Edgar and Anwar Khan

The following substitutions were noted: Councillor Snowdon attended in place of Councillor Aston and Councillor Uz-Zaman in place of Councillor Edgar.

2. DECLARATIONS OF INTEREST

No declarations of disclosable pecuniary interest were made.

3. UNRESTRICTED MINUTES

The minutes of the meeting held on 14 January 2013 were presented. Ms Shona Milton noted that a correction at minute 4.1 in paragraph 3 was required and requested the following amendment.

“Regarding the certification of claims and returns, Mr Sayers advised that there were six certified claims reported, two of which were subject to qualification.

He noted the technical qualification against housing audit resulting from a DCLG error. This qualification although not originating the Council was reported to the awarding body in accordance with the grant certification requirements.”

RESOLVED:

Subject to the above amendment the minutes of the meeting were approved

Update on Matters Discussed at the Previous Meeting:

1. It was confirmed that councillor Ullah had pursued the matter of differential valuations arising from the valuations sought in conjunction with the audit of the right to buy scheme.
2. Mr Jani, Head of Risk Management and Audit gave an update confirming that the internal audit of Boishakhi Community Trust Limited had been completed. A meeting had been held with members of the Baishaki Mela Trust two weeks prior and he advised that some action had been required for priority 2 recommendations also noting that a large number of audit recommendations had been implemented. . Concerning the control aspect of the audit, Mr Jani reported that the Trust had been co-operative. . He advised that an audit summary would be presented at the next Audit Committee. Councillor Gibbs expressed concern that the audit had been conducted after the Mela event and enquired if reviews could be undertaken more quickly. Mr Jani advised that in 2012, audit recommendations had coincided with the Mela event and so controls had been put in place while the event was in-train. In 2013, Trust staff were already aware of the required processes and therefore it was expected that the audit should be easier.

The Committee noted the verbal updates.

4. UNRESTRICTED TOWER HAMLETS REPORT

4.1 Presentation from SECTOR

Dan Wilson and Tim Hughes of Sector introduced themselves. Mr Wilson, Head of Credit and Investments, advised the Committee his role was to study markets and their activity. Mr Hughes, Client Manager, advised his role was cash management for clients and customer management, providing support as required. He advised that he worked daily with the Chief Financial Strategy Officer managing the cash requirements of the Council to ensure optimum return for minimum risk as stipulated in the Council's current investment strategy.

Mr Hughes advised that part of the reason for the observed decrease in returns over the past year was the conservative nature of the Council's investment strategy. He noted that most of the investment was in liquid short-term investments which delivered the lowest market yield available. On this matter, the Chief Financial Strategy Officer advised that he had recently been given a mandate to broaden the scope to access better returns. Mr Hughes advised that extending the counterparty list would give access to better returns and this could be undertaken on a short-term basis.

Concerning the Council's investment with OCBC in preference to Santander UK, Mr Hughes advised that Sector had not recommended investment in Santander UK because it does not meet the Council's minimum credit criteria OCBC on the other hand meet the criteria. The Chief Financial Strategy Officer advised that the Council had previously invested with Santander UK; however, since the credit crisis and subsequent downgrade of a number of UK financial institutions, it has not been possible to continue investing with Santander and some other UK banks.. However it was intended that flexibility was increased during the next financial year. Additionally he noted that whilst the Council may wish to invest with a financial institution they may not necessarily require funding. , For example HSBC are not looking to accept deposits despite meeting the Council's minimum credit criteria.

Concerning financial ratings, Mr Wilson advised that many ratings had been reduced by agencies such as Moody's and Fitch, not because the investments were less safe than they had been previously but because these organisations had changed their ratings criteria, hence there was a smaller investment pool.

Concerning Managers' fees, the Chief Financial Strategy Officer confirmed that Sector was paid by results. Payment comprised a fixed fee plus a performance element. Members enquired whether the Chief Financial Strategy Officer could be pressured to obtain maximum investment returns and Mr Shonola advised that he was not authorised to act in this way; hence Sector was not able to apply pressure to get maximum returns.

Concerning whether the Council should consider being less risk averse and allocate a larger percentage (e.g. 10%) to larger risk investments, Mr Hughes advised that such a decision would lie with the Council but a proposal could be considered if the authority wished. On this matter, the Chief Financial Strategy Officer advised that the strategy was presently well-balanced in accordance with the agreed strategy and contained some low and medium rated risks. He added that the 2013/14 Investment Strategy will provide further flexibility that will allow the Council to invest in some A+ and A rated banks and he recommended that investments with banks lower than A rated should not be undertaken. The Acting Director of Resources further advised that the situation was kept under review because it was necessary ensure that risks were balanced. Mr Wilson advised it was also necessary to quantify risks to confirm whether or not there was value-added in taking them. He noted that issues became clouded where liquidity risk occurred and this made looking at how to invest more difficult. He noted that the Council could, if it wished, invest in small building societies which would support local economies and support the Council's ethical stance and advised doing so would bring greater risks. Therefore the Council needed to consider how far down the liquidity-or-risks scale it wanted to travel to benefit from better returns.

Concerning whether Sector took account of the non-financial benefits of certain investments (e.g. the social benefits of investing with small building societies who would promote local economies by lending to individual borrowers), Mr Wilson advised that Sector worked within the parameters and policy decisions set by their clients who, if they wished, were able to step outside their chosen security - liquidity yield. The Chief Financial Strategy Officer advised that the Council's guidance stated that it must look at security first but if the Council wished to permit this type of investment he was able to explore what options were available. He added that any schemes to lend to local businesses/entities will have to be agreed outside of the Investment Strategy.

Councillor Ullah noted that options for ethical investing had been considered previously; however the Council was required to be a good steward of its public money and therefore the strategy needed to consider safety and due diligence in investing the Council's money.

Councillor Gibbs enquired whether the Council might directly invest with UK-based small/medium enterprises (SME) to support local business. Mr Wilson advised that there were organisations with whom the Council could invest, but the Council needed to be aware that a percentage of such businesses would inevitably become bankrupt and therefore it needed to consider what loss it would be prepared to bear. Additionally a bigger quantity of investments would be made and therefore a bigger range of investments would need to be monitored by the Council.. He noted that banks were not presently lending to SMEs therefore any such proposal would need to be considered outside of the Council's investment strategy. The Chief Financial Strategy Officer advised that a form of investment of this kind was possible through the proposals around the Council's Housing Revenue Account; The Acting

Director of Resources noted Members would need to consider if they wished to pursue this as the issue of balancing risk against the need for stability remained. Additionally it was noted that investing in local HRA's would mean that money was tied up for a long term and would not provide quick returns.

Councillor Eaton enquired whether those on apprenticeship training might also receive training in treasury management and Mr Shonola advised that this would be investigated.

RESOLVED:

That the presentation be noted

4.2 Treasury Management Activity for Period Ending 28th February 2013

The Chief Financial Strategy Officer introduced the report and highlighted the following elements:

- the changes to the investment strategy at paragraph 6.1
- the criteria for investment set out at paragraph 9 had been approved by the Council
- investment returns set out at paragraph 10.5
- the maturity profile detailed at paragraph 10.5 and
- counterparty exposure detailed at paragraph 10.7
- investment returns since inception of the cash management arrangement with Sector at paragraph 11.

He advised the Committee that the average performance over the financial year had been slightly below target by 0.01%. The rate of return over the year also was reduced.

In response to Members' questions the following information was provided:

The Chief Financial Strategy Officer agreed that investment inception dates would be included within the investment portfolio data reported to the Committee.

Action: O Shonola, Chief Financial Strategy Officer

The term 'projection' indicated the maturity period/bucket in which the investments listed in the 'Investment Portfolio' occurred.

50% of Council assets were linked to Bank of Scotland (BoS) and Royal Bank of Scotland (RBS) because these were the institutions which were backed by the Government.

Concerning whether investment in OCBC posed a significant risk because of the systemic risk associated with the Chinese banking system, Members were advised that the OCBC investment was short-dated..

Regarding what other investment options the Council might choose, Mr Hughes advised that Sector would consider investments according to criteria agreed in the Council's investment strategy and opportunities that occurred in the market. Hence investments would be tailored accordingly with respect to the Council's criteria.

Concerning the loss, in cash terms, resulting from the decrease of investment performance during the last year, Members were advised that the loss would be about £20-£30,000 per basis point.

Members requested comparative data of rates and returns for other local authorities and it was agreed that this would be reported as part of future treasury management reports.

Action: O Shonola, Chief Financial Strategy Officer

RESOLVED:

That the report be noted

5. UNRESTRICTED KPMG REPORTS FOR CONSIDERATION

5.1 External Audit Plan (KPMG)

KPMG partner, Andrew Sayers presented the report circulated at agenda item 5.1. He advised the Committee that the key audit areas of the plan were:

- savings plans,
- property plant and equipment,
- actuarial asset value of retirement benefits, and
- accounts receivable and accounts payable.

As the Council's auditors, KPMG would examine the processes being followed in each of these four areas and noted the previous matters raised regarding the audit of the accounts receivable/payable processes.

Mr Sayers also advised the Committee of KPMG's independence and objectivity responsibilities as required under the code; these were summarised at page 9 of the report.

Referring to the salient parts of the report, Mr Sayers advised that KPMG would complete an audit of the pension fund alongside the main financial accounts audit. He advised that the main area of audit risk regarding the pension fund was the valuation of investments.

He confirmed the fees proposed for 2012/13 set out at page 21 of the report. This set out the basis of the audit fee. He advised that any queries raised would be considered as additional fees and that KPMG was able to receive queries from the Committee and take these up with the Executive.

In response to Members' questions the following information was discussed:

Concerning the scope of the savings plan Key risk that had been identified at page 3 of the report, Mr Sayers advised that the auditors would look to ensure that processes were in place so that the Council could take forward its investments. This would be undertaken in the form of top-line monitoring.

Concerning how the scale of fees was derived, Mr Sayers advised that these were set by the Audit Commission and a fee reduction had been achieved through the procurement the process carried out by the Audit Commission.

Concerning how many additional investigations the Council could expect the Auditors to recommend, Mr Sayers advised that KPMG would seek additional audits only where necessary. Additionally a safety mechanism against excessive additional audits was imposed by the Audit Commission. KPMG would ensure that money was not spent outside the permitted sphere by interrogating how Council money was well spent and investigation to ascertain why funds had been spent on particular audits. If spending was discovered that was against the Council's general policies, the Council would be asked to justify its spending. Mr Sayers additionally advised that any elector was able to refer to KPMG and he would consider each referral to assess if they needed to be investigated.

Noting the fee reduction achieved because of the fee scales set by the Audit Commission and economies of scale gained through outsourcing local government audits, Councillor Eaton enquired whether the Audit Commission had operated efficiently, Mr Sayers advised that he was unable to comment on Audit Commission matters. However he advised that KPMG had offered a price that it felt that delivered the required audit levels at a suitable price. He noted additionally that some work being undertaken by KPMG was different to that that the Audit Commission had formerly carried out.

Concerning whether KPMG undertook medium-term financial analysis of local authority investments and funding gaps in comparative terms, Mr Sayers advised that KPMG did not undertake a benchmarking across local government; however should any concerns develop in this regard, the matter would be raised with the Council.

RESOLVED:

That the report be noted.

6. UNRESTRICTED TOWER HAMLETS REPORTS FOR CONSIDERATION

6.1 Quarterly Internal Audit Assurance Report

Minesh Jani, Head of Risk Management and Audit presented the report circulated at agenda item 6.1 which summarised the work of internal audit for the period December 2012 to February 2013 and incorporated a summary of

audits at appendix 1. He noted that two limited assurances had been returned for creditors systems audit and for Harry Roberts nursery school probity audit.

In response to Members' questions following information was provided:

While assurances had been returned, for creditors systems audit and Harry Roberts nursery school probity audit, neither had revealed evidence of fraud and improvements in functionality had been found.

In responding to the audit, the headteacher had acknowledged that more needed to be done in terms of probity. Mr Jani noted that recent audits of other schools had revealed similar issues and that commonly audit issues concerned governance and schemes of delegations; therefore he suggested that this area could be improved through staff training and by improving schools' understanding of processes.

Councillor Snowdon noted that the smaller schools appeared to deliver limited assurances on similar matters and agreed that there would be benefits in addressing the most frequent qualifications via a programme of staff training. Mr Holme noted that the Council was not authorised to impose sanctions on schools and recommended that a collaborative approach be used to resolve issues. Mr Clarkson advised that Deloitte carried out many school audits nationally and these returned much evidence of school fraud. It was his view that this occurred because control mechanisms were not working properly or well understood therefore training would help gain understanding and why compliance was necessary.

Concerning the outstanding recommendations resulting from the audit of occupational health stores, the Chair enquired whether the priority-one recommendation and two priority-two recommendations outstanding at December 2012 had been subsequently completed and was advised that this would be investigated and reported back.

Action: Minesh Jani, Head of Risk Management and Audit

Noting the weaknesses reported in the lettings and nominations systems audit, completed in January 2013, Councillor Uz-Zaman requested that an update to this audit be reported to Committee 12 months hence.

Action: Minesh Jani, Head of Risk Management and Audit

RESOLVED:

That the report be noted.

6.2 Internal Audit Plan 2013/14

Minesh Jani, Head of Risk Management and Audit presented the report circulated at agenda item 6.2 which advised Members of proposals for the

annual internal audit plan 2013/14. He advised that the methodology used was the same as that employed in 2012/13, setting out the areas of risk that the Council believed it faced and enabling these to be addressed via a proper plan over the period. The planned audits would be shared between the Council's audit team Deloitte. Mr Jani recommended that to avoid incurring additional external auditor fees, some of the external audits should also be undertaken by Council auditors.

In response to Members' questions the following information was provided:

Councillor Eaton requested that a retrospective element be introduced into the review of CRB checks

Action: Minesh Jani, Head of Risk Management and Audit

Concerning why a recent conviction was not picked up through the audit, Councillor Eaton was advised that CRB details related to the conviction of the person disclosed in the audit would be provided to Members outside of the meeting

Councillor Eaton noted that ASB officers were not updating the log of investigation's daily and suggested that an audit ASB officers be undertaken to investigate why the updates are not been logged onto the database.

Action: Minesh Jani, Head of Risk Management and Audit

RESOLVED:

That the report be noted.

6.3 Progress on National Fraud Initiative 2010 and New Initiative 2012

Tony Qayum, Corporate Antifraud Manager presented the report circulated at item 6.3 which provided an update on the current progress of the National Fraud Initiative 2010 and gave an overview of antifraud work undertaken taken in the past six months. He highlighted the following matters:

- methodology and scope of the exercise detailed in paragraphs 4.2 - 4.4
- outcomes reported in paragraph 5 had provided more useful data than had previously been available
- the antifraud team proposed to look at lessons learned from the data matching exercise in 2010 and how this information could be better used in its next audit of this kind

In response to Members' questions the following information was provided:

The NFI exercise had revealed that 33 people living across London had been involved in overpayments of housing benefits made through Tower Hamlets. Mr Qayum noted that, were any Council employee found to be involved, it would be considered gross misconduct and the matter investigated.

In discussing whether the Council quantified the costs of recovery action against losses if action were not taken, the Committee was advised that there was no effective way of knowing the costs of recoveries as these varied from incident to incident and so it was not possible to determine whether prosecution was more efficient than other sanctions that could be applied. It was noted that the Department for work and pensions tended more towards prosecution.

RESOLVED:

That the report to be noted

6.4 Social Housing Update

Mr Tony Qayum, Corporate Anti-fraud Manager and Paul Thorogood, Interim Service Head for Finance and HR Development presented the report circulated at item 6.4 which provided an update on the work of the social housing team and its successes, to-date, in the recovery of unlawfully let public sector dwellings. Mr Qayum reported that the initiative had been very successful and, due to changes in funding, he suggested that this work could be pursued further in the next year to ensure there was good housing stock management and to highlight areas of weakness. Mr Holme noted also that the antifraud work contained a polity policy incentive element. Councillor Uz-Zaman noted the results reported and advised that he supported the initiative.

In response to Member's questions, the following information was provided: Funding for the initiative was £15,000. Eligibility decisions for this funding lay with DCLG and a decision was to be announced shortly. Housing fraud officers had been retained while the Council waited to hear whether this had been achieved.

In addition to Tower Hamlets Homes, registered social landlords (RSL) had also been approached to utilise methods employed through the initiative and the Council was able to offer advice on how RSL's might improve their antifraud systems.

Data matching procedures were used to ensure that housing benefit applications were genuine. Additionally the Council was working jointly with other neighbouring local authorities to create an east London hub for fraud investigation as well as normal methods such as Experion checks, regular data-sharing (for data matching purposes). Court action and termination of right to buy were also used at operational level to prevent tenancy fraud.

RESOLVED:

That the report be noted

7. ANY OTHER UNRESTRICTED BUSINESS CONSIDERED TO BE URGENT

Nil items

The meeting ended at 8.43 p.m.

Chair, Councillor Carlo Gibbs
Audit Committee