

LONDON BOROUGH OF TOWER HAMLETS

MINUTES OF THE AUDIT COMMITTEE

HELD AT 6.30 P.M. ON TUESDAY, 23 JULY 2019

COMMITTEE ROOM ONE - TOWN HALL MULBERRY PLACE

Members Present:

Councillor Val Whitehead (Chair)
 Councillor Abdal Ullah
 Councillor Mufeedah Bustin
 Councillor Marc Francis
 Councillor Ehtasham Haque
 Councillor Kyrsten Perry

Other Councillors Present:**Apologies:**

Councillor Ayas Miah
 Councillor Andrew Wood

Others Present:

Angus Fish	– Deloitte
Jonathan Gooding	– Deloitte
Syed Nahid Uddin	– Member of Public

Officers Present:

Bharat Mehta	– (Audit Manager)
Neville Murton	– Corporate Director, Resources)
Paul Rock	– (Head of Internal Audit, Anti-Fraud and Risk)
Anthony Sotande-Peters	– (Interim Strategic Risk Advisor, Risk Management and Audit)
Lino Messoro	– Corporate Anti-Fraud Assistant
David Seagroatt	– Senior Auditor
Farhana Zia	– Senior Committee Services Officer

1. APPOINTMENT OF VICE-CHAIR

The Chair asked for nominations for vice-chair. Councillor Kyrsten Perry proposed Councillor Abdal Ullah for vice-chair of the Audit Committee, which was seconded by Councillor Marc Francis.

The Committee **RESOLVED** to elect Councillor Abdal Ullah as vice-chair of the Audit Committee.

2. DECLARATIONS OF DISCLOSABLE PECUNIARY INTEREST

Councillor Krysten Perry declared she is Chair of the Pensions Committee.

Councillor Val Whitehead declared she is a trustee and treasurer of Toyhouse libraries, which receives some grant funding from the council. However she does not have any pecuniary benefit from it.

3. MINUTES OF THE PREVIOUS MEETING(S)

The minutes from the 11th April 2019 meeting were agreed and approved to be an accurate record of the meeting.

Councillor Whitehead informed Members the query raised under matters arising in relation to consultants had been answered by HR via email and this had been circulated. As such they were no longer required to attend a meeting of the Committee.

4. DELOITTE ITEMS FOR CONSIDERATION

4.1 External Audit Report 2018-19

Items 4.1 and 5.1 were taken in conjunction of each other. Deloitte presented their findings in relation to the external audit they had undertaken and Mr Neville Murton, Corporate Director for Resources and Mr Kevin Bartle, Divisional Director for Finance, Procurement and Audit commented and added to the findings.

By way of introduction, Mr Kevin Bartle, Divisional Director for Finance, Procurement and Audit addressed the Committee stating the draft Accounts being presented at the meeting were not complete and therefore could not be signed off by the Committee. Mr Bartle said that whilst it was disappointing not to achieve the deadline of 31st July, the finance team was putting in significant effort to provide the information requested by the external auditors so to ensure the situation was rectified as soon as possible.

In response to questions from Members the following was noted:

- Mr Murton, Corporate Director for Resources was asked to put into context the significance of not meeting the deadline. Mr Murton said it was not unusual for local authorities not to get the accounts signed off by the deadline of 31st July. Quite a few other Authorities were in the same position. He said the statutory deadline had moved from September to August and now the end of July, and although this was not an excuse as to why the deadline had not been achieved, other factors had played a part. There had been a restructure of the finance team, and this had impacted staff morale and delivery. However the finance team was working alongside the external auditors and had an action plan in place to ensure a robust response was provided to the outstanding queries. Mr Murton indicated that by the end of September the accounts would be in a state whereby they could be signed off.
- In response to whether there would be financial penalties for not meeting the deadline, Mr Gooding, external Auditor clarified the local

authority would not be fined for missing the deadline but may experience reputational damage.

The Chair invited Mr Gooding, external auditor from Deloitte to present his report.

Mr Gooding said the auditing of the accounts was an on-going process and involved a lot of work. He acknowledged the restructure had impacted on the delivery of information requested such as the lists of schedules and query resolution. For example, the trial balance for the Pension Fund had not been received. Mr Gooding said this consequently meant the separate opinion on the Pensions Fund could not be provided to the Committee.

Mr Gooding said the scope of their audit had not changed as per the plan which was submitted to the Audit Committee in April 2019. The update report made several recommendations on the significant risks identified. Mr Gooding referred to the risk of management override control, which is a risk external auditors must presume exists and said that the journals to test the effectiveness of transactions made and identify the risk of fraud were received when they were finalising their report, as a result they had yet to complete their testing. Mr Gooding continued saying the report provided a commentary on significant risks such as the valuation of property assets, capital expenditure, pension liability and the implementation of IFRS 9 and IFRS 15. Observations in relation to the narrative and how this can be approved were also included in the report.

Mr Angus Fish, from Deloitte then took members through the remainder of the report stating pages 12 -15 of the supplement agenda pack gave an opinion against each risk. Control observations were cited at pages 20-23 and suggestions on how the accounts can be improved were listed at page 24.

In response to Member questions the following was noted:

- In response to what the risks of management overriding controls was, Mr Gooding said this refers to journal entries made on the accounting system, whereby management have overridden the controls and have applied their own judgements. In other words, they have manipulated the estimates. In order to test for fraudulent entries Deloitte require access to the data, to review it.
- In response to why it has been difficult to obtain access to data, Mr Murton said there is a huge volume of data that needs to be extracted and the size of the data presents challenges. Mr Gooding added that descriptions were missing making it hard to trace who had posted the journal. However the missing information had been worked through and progress was being made. Mr Bartle added that providing information when the Council switches auditors, as is the case for this Council, means information required by the external auditors needs to be presented in a different way and this can pose challenges.

- In response to what involvement Grant Thornton, another accounting firm, had in producing the accounts, Mr Murton clarified they had had no involvement. Mr Murton clarified for Members that Deloitte had been contracted to provide an opinion over the accuracy and completeness of the Council's accounts and prior to Deloitte, KPMG were the Council's auditors. Mr Murton said Grant Thornton were involved in the initial scoping of the finance restructure but this was not connected to the annual assurance process for the accounts.
- In response to how confident the external auditors were that they would complete their audit by the end of September, Mr Gooding said there was a Deloitte team on site at the Council throughout August to progress the work, resolve outstanding queries and finalise the audit but progress had been slow.
- In response to how many other Local Authorities had missed the deadline last year, Mr Bartle said approximately 30-40 authorities out of three to four hundred local authorities nationwide. Mr Bartle continued and said that this does add pressure but he was determined to ensure the accounts were ready for sign off by the end of September. Mr Bartle said the restructure of the finance function had a big impact, but he would be reviewing the processes followed and would be taking forward a lesson's learnt exercise.
- In response to if the previous year's audit would in any way be reviewed to identify any control deficiencies and the role of Internal Audit, Mr Bharat Mehta, Audit Manager, stated that the recommendations made by the external auditors would be reviewed by Internal Audit and where appropriate included in the Annual Internal Audit Plan, which the Audit Committee has oversight for. Mr Murton added the change of auditors had caused problems, however there was a need for the Council to improve its accounting procedures. It was essential for the local authority to get this right next year. A lot more work was required during the year rather than the end of the financial year to start the audit process.
- In response to when did it become apparent the deadline of 31st July was not going to be achieved, Mr Bartle said approximately two to three weeks ago. Whilst the teams were working hard to achieve the goal of 31st July, it gradually materialised that the accounts would not be delivered in time for the deadline. Mr Bartle said regular meetings with Deloitte managers made it clear this deadline would be unattainable.

Members concurred there was considerable work the Finance team had to do in rectifying the situation and to ensure the reputational risk to the Authority was limited.

Members of the Committee **RESOLVED** to **NOTE**:

1. the unaudited Annual Financial Report including the Statement of Accounts for the financial year ending 31st March 2019;
2. the officer action plan to address audit matters arising; and
3. the initial report from the external auditors as presented at item 4.1 of the agenda. A final report will be brought to the next meeting of this committee.

5. TOWER HAMLETS ITEMS FOR CONSIDERATION

5.1 Annual Financial Report 2018-19

This item was dealt with in conjunction with item 4.1 above.

5.2 Audit Committee Terms of Reference, Quorum, Membership and Dates of Meetings 2019/20

Ms Farhana Zia, Senior Committee Officer presented the Audit Committee's terms of reference, quorum, membership and dates of meeting for 2019-20 report.

Ms Zia said the report informed Members of the decision made at the Annual General Meeting of the Council held on the 15th May 2019, which approved the proportionality and the establishment of Committees, Sub-Committees and Panels of the Council.

Mr Paul Rock, Head of Internal Audit added the terms of reference, appended at Appendix 1 had been updated to reflect the best practice guidance from CIPFA.

Members were asked to note the report.

Members of the Committee **RESOLVED** to:

1. **NOTE** its Terms of Reference, Quorum, Membership and Dates of future meetings as set out in Appendices 1,2 and 3 of the report.

5.3 NFI Progress Report

Mr Graeme Thomson, Programme Director Counter Fraud (Data Analytics, Capability Development, and Pilots) Counter Fraud Centre of Expertise, Cabinet Office, gave a presentation on the work of his department and the National Fraud Initiative (NFI).

Mr Thomson briefly explained that the NFI had been running since 1994 and was initially the responsibility of the Audit Commission before being moved to the Cabinet Office. Mr Thomson said his team was responsible for setting the professional standard in counter fraud and providing data analytics to central and local government.

Mr Thomson said the Digital Economy Act 2017 paved the way forward for cross departmental and local government sharing of information. His team is

responsible for setting up pilot schemes to embed good practice across the sector. For example, pilots had been set up for debt recovery which involved HMRC and ten local authorities. Data extraction and data matching exercises were undertaken biennially in order to identify fraud from the public purse.

In addition, Mr Thomson stated that the Cabinet Office manage the Internal Fraud hub, which records action taken against civil servants who had committed fraud. Departments were working to ensure individuals were not employed elsewhere in the civil service after they had been convicted and/or disciplined for fraud related offences. The aim was to extend this pilot to local government but this would require a change in government policy.

Other pilots running were with Companies Houses, to identify fraudulent companies, the Insolvency Service and the Charity Commission. Once the pilots had been evaluated, data would be shared with local authorities.

In response to questions from Members the following was noted:

- Members welcomed the presentation and the important work of sharing data to identify fraud. However Members asked for central government to be aware of the downside of automatically identifying fraud and the freezing of benefits. Councillor Marc Francis said he saw many constituents who had experienced difficulty with HMRC whereby their benefit was frozen pending investigation. This causes hardship and can lead to a spiral of debt. Mr Thomson responded saying no decision to flag up fraud was made without discussion. Artificial intelligence was not used in making decisions and there is due diligence in the work they do. However he welcomed the observations of Members and asked that any further comments or suggestions be made via the Council's counter-fraud team.

The Chair, Councillor Val Whitehead thanked Mr Thomson for this presentation.

Mr Lino Messore, from the Counter Fraud team then proceeded to present the NFI progress report

Mr Messore said the data matching exercise was undertaken in late 2018, when data was supplied for data matching purposes by all relevant parties, including the Council. Mr Messore said through the NFI system cases of potential fraud are identified for investigation and are rated as low, medium or high risk. The table at paragraph 3.13 showed the material risks emerging from the examination of the data. So far the Counter Fraud team had looked at 4,500 matches and paragraph 3.16 of the report showed the actual and estimated outcomes for 2018.

In response to questions from Members the following was noted:

- Of the 4,500 referrals, 3,900 matches were closed off without issue.

- Pension recovery cases related to pensioners who had died but the authority had not been notified and an overpayment had occurred. The counter fraud team recovered 130 blue badges where the recipient had died and the badges were still in circulation.
- In response to how many cases led to prosecution, Mr Rock, Head of Internal Audit said the NFI data matching exercise was not just about prosecuting individuals but also a data cleansing exercise picking up anomalies such a wrong digit in a National Insurance number.
- Mr Rock confirmed that the Corporate Fraud Team worked alongside other colleagues within the Council to identify and investigate fraud. Regarding Blue Badge fraud the team worked with housing enforcement officers and anti-social behaviour teams.

The Committee **RESOLVED** to:

1. Note the progress made against the National Fraud Initiative Exercise for 2018/19.

5.4 Internal Audit and Counter Fraud Progress Report

Mr Paul Rock, Head of Internal Audit, Fraud and Risk introduced this report stating that the report provided an update on the progress made against the delivery of the 2019/20 Annual Internal Audit Plan, as well as the current counter fraud performance and audits which have received limited assurance ratings.

Mr Rock said written responses had been obtained from Service Heads who had achieved limited assurances, due to the length of the agenda and these had been emailed to Members for information and perusal. Normally, Service Heads were required to attend the Audit Committee to answer questions relating to their audit and action plans.

Mr Rock referred Members to paragraph 3.8 of the report and said the Internal Audit team was stretched in delivering the internal audit plan, however work was underway to recruit to vacant posts and to identify an audit partner to provide specialist support. Mr Rock also referred Members to paragraph 3.12 and said he was working with HR to recruit an independent audit member for the committee in line with the recommendation made in the peer review.

In response to questions from Members the following was noted:

- Internal Audit has a wider remit than the external auditors. Internal Audit provide financial stewardship, review plans and ensure there is value for money in the whole organisation whereas the purpose of external audit is to focus on the Council's accounts.
- In response to resources allocated to the Internal Audit function and the continuity of staff, Mr Rock said the Corporate Leadership Team

had recognised the need to employ permanent staff over temporary staff and he hoped to recruit to the vacancies in his team shortly.

- **ACTION:** In reference to paragraph 3.7 of the report, Mr Mehta Audit Manager said he would email details of the three deferred audits to Members via email.
- In relation to the Markets Audit, Member asked what controls were in place to ensure the recommendations of Internal Audit were implemented. Mr Mehta explained a follow up audit is undertaken six months after the initial review to gauge if the recommendations and changes in process have been implemented.
- With regard to the DOLs assurance, the Chair asked if the response received from the service was adequate. Mr Mehta said the service had made good progress against the recommendations and a follow up audit would be undertaken in due course.
- Mr Rock clarified the Internal Audit Plan was agreed by the Audit Committee at its April 2019 meeting and was a risk based plan taking into account risk identified by various stakeholders including the Corporate Leadership Team. Mr Rock said the plan would remain under review and be amended to take into account emerging risks.

The Committee **RESOLVED** to:

1. Note the contents of the report and the overall progress and assurance provided, as well as the findings/assurance of individual reports.

5.5 Q1 Risk Management Update 2019/20

Mr Anthony Sotande-Peters, Interim Strategic Risk Advisor introduced this report stating that the purpose of the report was to inform Members of the ways in which risks are identified and managed. The report provided a summary of risk activities over the first quarter 2019/20 and appended at Appendix 1 was Corporate Risk Register. Appendix 2 cited the detailed summary and updates from risk owners.

Risk registers for each Directorate had been sent to Members as requested.

In response to questions from Members the following was noted:

- Mr Sotande-Peters confirmed the risks cited on page 211 of the agenda would be revised taking into account the Ofsted findings in relation to Children Services.

The Committee **RESOLVED** to:

1. Note the corporate risk and recommend changes and updates as necessary;

2. Request risk owner(s) with risk that the Committee believes require further scrutiny to provide a detailed update on the treatment and mitigation of their risk including impact on the corporate objectives at its next meeting; and
3. Ensure that an effective risk management framework is in place within the council and leading the council to be a risk mature, dynamic risk organisation.

5.6 Head of Internal Audit Annual Report

Mr Paul Rock, Head of Internal Audit, Fraud and Risk presented his Annual Head of Internal Audit Report. Mr Rock said the report provided the annual audit opinion in accordance with the requirements of Public Sector Internal Audit Standard. The opinion supported the governance conclusions that are included in the Annual Governance Statement, which forms part of the statement of accounts required under the Accounts and Audits Regulations 2015.

Mr Rock referred Members to page 231 of the agenda, paragraph 10.1 and said he was limiting the scope of the annual opinion to exclude Information Technology (IT) related risks as no audits had been undertaken in this area during 2018/19. Mr Rock said he viewed IT related risks to be a significant risk and as such would be included in the 2019/20 internal audit plan. Mr Rock said specialist IT auditors would be contracted to undertake this work.

Mr Rock continued stating the team was under resourced and this continued to be a risk. Members had already heard plans are underway to recruit to vacant posts to improve Internal Audit's performance plus appoint a third-party audit partner by the 30th September.

In response to questions from Members the following was noted:

- In reference to the table at page 228, Members asked why management were not responding to the actions/recommendations made by internal audit reviews. Mr Rock said he was investigating why this was however he was clear that Service Heads and Directors needed to be more responsive and accountable. Mr Rock said the Committee had an important role in holding them to account.
- Mr Bartle added he had confidence in Mr Rock to deliver the Internal Audit Plan and make the changes required to ensure better performance and outcomes.

The Committee **RESOLVED** to:

1. **NOTE** the content and opinion of the Head of Internal Audit as outlined within the Head of Internal Audit Annual Report which includes a summary of the work undertaken during 2018/19.

5.7 Annual Governance Statement

Mr Paul Rock, Head of Internal Audit, Fraud and Risk presented the Council's Annual Governance Statement. Mr Rock said the Annual Governance Statement was a requirement of the Accounts and Audit Regulations 2015 and should reflect the CIPFA/SOLACE principles on Delivering Good Governance in Local Government Framework. The Council was required to undertake a review of its corporate governance processes, systems and give assurances on the governance framework.

The Annual Governance Statement needs to be signed by the Chief Executive and the Mayor by the agreed statutory deadline. However Mr Bartle said that the signing may need to be delayed in light of the draft accounts not being complete.

In response to questions from Members the following was noted:

- Discussion took place regarding the Annual Governance Statement and if this should be approved by the Committee.
- Councillor Marc Francis said that whilst the statement looked at the Governance structures in Tower Hamlets, the model adopted by the Council had issues in the early days and there was evidence the structures and processes in decision making were not tight enough and this needed to be recognised. Councillor Francis gave an example of where confused governance was in place, with no clear decision making pathway. Mr Rock thanked Councillor Francis for his comments and said he would look into this further.
- **ACTION:** Members requested the Statement be revised to better reflect the constitution and current decision making processes.

The Committee **RESOLVED** to:

1. **NOTE** the report and comments of Members and will review the Annual Governance Statement at its next meeting.

5.8 Treasury Management Report for 2018-19

Mr Neville Murton, Corporate Director for Resources presented the Treasury Management Report for 2018-19. Mr Murton said £100m from the 2018-19 budget was set aside for investment in pooled funds of which £76m had been invested. Further investment in pooled funds was paused due to high market volatility as the equity markets fell sharply over the 3 months to 31st December 2018.

Mr Murton referred Members to table 6, page 297 of the agenda pack and said a capital loss of £2.5m occurred and the portfolio valuation was £73.5m instead of the invested amount of £76m. Mr Murton continued saying the investment portfolio credit worthiness had improved from A+ to AA-.

With regards to external rates of borrowing, table 2 page 294, Mr Murton said the average rate of borrowing had decreased for 3.25% to 1.16%. Mr Murton said the balance between risk and returns had been managed well over the

period with the redemption of LOBO and re-borrowing from the Public Works Loan Board – table 3 and as such the overall picture was positive.

In response to questions from Members the following was noted:

- The LOBO agreements were put in place 30 to 40 years ago and have become costly so where possible the Council has redeemed these in favour of borrowing from the PWLB. Mr Bartle added that the LOBO agreements are not easy to get out of as they incur penalties.
- With regard to pooled funds these are equity based investments so carry a higher risk. Treasury management need to balance risk and reward. Therefore as capital is at risk this will reduce the credit score as shown in table 6. The credit score should not be confused with the credit rating which has improved from A+ to AA-, as this shows the credit worthiness of investments. Mr Bartle added Members may wish to consider the security of money invested, the liquidity and the yield.
- In response to what was being done to negate the effects of inflation Mr Murton said generally low risk funds had been invested in. Pooled funds are a move away from this and carried more risk. However with the help of the Council's advisors Arlingclose, the investments are closely monitored and it was envisaged that within a period of 5 to 10 years the capital value of the investments would increase. Decisions are made on the risk appetite of the organisation and are judgment based.
- In response to what protection there is for the investments made, Mr Murton said there was no protection in terms of pooled funds, however the Pension Fund was more exposed to equities because with the Pension Fund there is an expectation that it must produce a return as the deficit needs to be made up.

The Committee **RESOLVED** to:

1. Note the contents of the treasury management activities and performance against targets for the year ending 31st March 2019.
2. Note the Council's investments as set out in Appendix 1. The balance outstanding as at 31st March 2019 was £383,150m which includes £6m pension fund cash awaiting investment.

5.9 EXCLUSION OF PRESS & PUBLIC

The Chair **Moved** and it was: -

RESOLVED:

That in accordance with the provisions of Section 100A of the Local Government Act 1972, as amended by the Local Government (Access to Information) Act 1985, the press and public be excluded from the remainder of

the meeting for the consideration of the Section Two business on the grounds that it contained information defined as exempt or confidential in Part 1 of Schedule 12A to the Local Government, Act 1972.

The Member of public present at the meeting departed prior to item 5.10 being discussed.

5.10 Poplar Baths - Refinancing

6. ANY OTHER BUSINESS THE CHAIR CONSIDERS URGENT

The Chair sought agreement of Committee Members to hold an extraordinary meeting of the Audit Committee in light of the draft accounts having not been finalised as well as the Committee's decision to receive a revised Annual Governance Statement, plus further consider the proposal outlined in the exempt report.

The Committee **RESOLVED** to:

Hold an extraordinary meeting of the Audit Committee on Monday, 30th September 2019 at 6:30 p.m. in Committee Room 1.

The meeting ended at 9.38 p.m.

Chair, Councillor Val Whitehead
Audit Committee