

AUDIT COMMITTEE

MINUTES of a meeting of the Audit Committee held at Committee Room - County Hall, Lewes on 22 November 2018.

PRESENT Councillors Colin Swansborough (Chair) Councillors Gerard Fox (Vice Chair), John Barnes, Matthew Beaver, Bob Bowdler and Philip Daniel

LEAD MEMBERS Councillor David Elkin

ALSO PRESENT Kevin Foster, Chief Operating Officer
Ian Gutsell, Chief Finance Officer
Russell Banks, Chief Internal Auditor
Nigel Chilcott, Audit Manager
Simon White, Audit Manager, Counter Fraud
Graham Glenn, Acquisition and Disposal Manager
Bethan Bolland, Executive Officer
Haley Woollard, Principal Accountant, Treasury & Taxation.

20 MINUTES OF THE PREVIOUS MEETING HELD ON 20 SEPTEMBER 2018

20.1 The Committee RESOLVED to agree the minutes as a correct record of the meeting held on 20 September 2018.

21 APOLOGIES FOR ABSENCE

21.1 Apologies for absence were received from Councillor Daniel Shing.

22 DISCLOSURES OF INTERESTS

22.1 Councillor John Barnes declared a personal, non-prejudicial interest under item 11 and 14, as he is a Rother District Councillor and an Etchingam Parish Councillor. Councillor Matthew Beaver declared a prejudicial interest under item 14, as he is a Hastings Borough Councillor and has expressed a view on the planning permission for one of the sites.

23 URGENT ITEMS

23.1 There were none.

24 INTERNAL AUDIT PROGRESS REPORT - QUARTER 2, 2018/19 (01/07/18 - 30/09/18)

24.1 The Audit Manager introduced the report. He explained that the number of completed audits for quarter is slightly lower than previous quarters. This is due to a number of reasons including the investigation activity the Internal Audit Team have carried out during the quarter and that a number of audits are at the draft report stage and are awaiting finalisation.

24.2 The Audit Manager summarised the completed audit outcomes of which three audits received an opinion of reasonable assurance, and one had an opinion of partial assurance. The partial assurance opinion was for the audit of Orbis Budget Management. The findings of this audit reflect the differences in financial management processes, and a follow up audit will be undertaken next year. The Audit Manager outlined the investigation work carried out during the quarter and confirmed that 100% of high priority actions from previous audits have been implemented. The Internal Audit Team has achieved all performance targets for the quarter. The Chief Internal Auditor continues to be able to provide reasonable assurance that the Council has in place an effective framework of governance, risk management and internal control.

Orbis Budget Management audit

24.3 The Committee asked for further information on why the Orbis Budget Management audit received a partial assurance opinion. The Committee also asked if this was linked to the Chartered Institute of Public Finance and Accounting (CIPFA) report on Surrey County Council's (SCC) finance function.

24.4 The Chief Operating Officer responded that the audit looked at the budget management systems across the three organisations. Work is in progress to develop additional budget monitoring applications across Orbis to assist budget managers to get greater clarity in the financial information they receive. The work includes looking at the efficiency of the systems in use and whether further investment is needed. It is not a reflection of the mature financial management systems that already exist in each of the organisations. The audit was undertaken in the early stages of this work, and it is acknowledged that further progress is needed.

24.5 The Chief Internal Auditor added that Orbis managers are managing budgets and getting information across three different financial systems, which has to be integrated together. The opinion reflects the view that the financial information is not as clear as it should be for budget managers. The Finance Team are working to provide more clarity and to consolidate budget information. They also provide support to managers to help them understand the information they receive.

24.6 The Committee asked if further investment in systems would be needed. The Chief Operating Officer responded that the resources for financial monitoring are included within existing budgets. However, if further investment is required it will be subject to a business case being established. The Chief Finance Officer outlined that current work includes the creation of a centre of expertise for accounting and systems. The centre of excellence is looking at the different accounting practices that exist within each of the partners to establish best practice. The Chief Finance Officer commented that he is comfortable with the direction of travel to achieve improvements.

24.7 The Chief Operating Officer explained that the CIPFA report is a report on SCC's financial resilience and the effectiveness of their finance function. It is not a reflection on the finance and support arrangements for East Sussex County Council (ESCC) and Brighton and Hove City Council (BHCC). It does not reflect the position of the Orbis service overall. The Committee asked if SCC staff are working for ESCC as part of partnership, and whether training and support is being provided. The Chief Operating Officer confirmed that support is being provided to SCC staff, including advice and support from David Kuenssberg, Director of Finance & Resources (BHCC) and Ian Gutsell, Chief Finance Officer (ESCC).

24.8 The Committee requested an update report on the implementation of the management actions from the Orbis Budget Management audit for the next committee meeting in March 2019. The Chief Operating Officer confirmed that an update report on the management actions will be provided for the next meeting, and that a follow up audit has been included in the Internal Audit Plan for next year.

Investigations – conflict of interest

24.9 The Committee asked if the undeclared conflict of interest would have come to light if the allegation had not been reported via the confidential reporting hotline. It also asked at what level of management the member of staff involved in the case worked. The Audit Manager responded that this case may not have come to light if it had not been brought to attention of the Team via the confidential reporting hotline. The Chief Internal Auditor explained that the member of staff involved was middle management and did not declare a conflict of interest. The Council does have a robust disclosure of interests system and a confidential reporting hotline, but there is little more the organisation can do if there are deliberate attempts to conceal conflicts of interest.

24.10 The Committee asked if the confidential reporting hotline is robust enough to deal with malicious allegations. The Chief Internal Auditor responded that it is robust enough to deal with malicious allegations. He explained that the Team carry out a preliminary assessment of all allegations with Human Resources and Management to establish whether there is any substance to the allegation. The Audit Manager outlined that in addition to the investigation report, an internal control report is produced to identify opportunities to improve processes and procedures. Sanctions may include disciplinary action and any criminal activity is reported to the Police.

24.11 Councillor Philip Daniel commented that there should be greater transparency around contract terms and conditions and the procurement process, which would help with exposing conflicts of interest. The Audit Manager Counter Fraud outlined that the Counter Fraud Team will be doing work on cultural education on declarations of interest. The Chief Internal Auditor confirmed that the Internal Audit Plan picks a number of contracts to audit each year, to ensure procurement processes have been adhered to.

24.12 The Committee RESOLVED to:

- 1) note the report; and
- 2) request an update report for the March 2019 Audit Committee meeting on the implementation of the management actions agreed in response to Orbis Budget Management audit.

25 COUNTER FRAUD UPDATE AND WORK PLAN (INCLUDING THE PROPOSED UPDATED ANTI-MONEY LAUNDERING POLICY)

25.1 The Audit Manager, Counter Fraud introduced the report. He outlined the formation of the Counter Fraud Team and summarised their current work. This includes a number of investigations for the Orbis partners and the submission of the data sets for the National Fraud Initiative. The latest submission on behalf of the partners was submitted in October with results from the matching exercise expected in January 2019. The Team will also be looking at all the partners' counter fraud policies to update them, which is why the Anti-Money Laundering Policy has been refreshed and is being brought to Committee prior to approval by the Governance Committee.

25.2 The Committee asked for clarification of the organisations the Audit Manager Counter Fraud works for, and how many staff there are in the Counter Fraud Team. In addition to the Audit Manager, Counter Fraud there is a Principal Auditor, a Senior Auditor and two investigators based at Brighton to deliver Housing fraud work to Brighton and Hove City Council. The Audit Manager, Counter Fraud manages the Orbis partnership team and also provides audit services to two other councils.

25.3 The Committee asked whether the customer identification system in anti-fraud work conflicts with the new General Data Protection Regulation (GDPR). The Audit Manager, Counter Fraud responded that as most of the Councils' customers are fairly well known to the Councils and there has been little impact. The main risk areas are around property transactions

and the Legal Teams carry out identity checks as part of undertaking the property transaction work.

25.4 The Committee RESOLVED to:

- 1) note the report and priorities raised; and
- 2) note the updated Anti-Money Laundering policy (contained in Appendix A) prior to submission to the Governance Committee for approval.

26 RISK MONITORING - BREXIT RISK

26.1 The Chief Operating Officer introduced the report. The report has been produced in response to the discussion of the Strategic Risk Register at the September Audit Committee meeting. The Brexit risk is currently reflected as part of the risks that are on the Strategic Register Risk Register. The report seeks the Committee's views on the way in which the risk from a disorderly Brexit should be dealt with on the Register. The report also outlines the work that has already been undertaken on this area of risk, including work that has been carried out with our South East Seven (SE7) partner authorities. The engagement with local government outlined in the report reflects the position 6 months ago, and there has been further engagement since this time.

Brexit Risk

26.2 The Committee discussed the likelihood and risks arising from a disorderly Brexit (i.e. with no transitional arrangements in place). The Committee agreed that there should be a separate item on the Strategic Risk Register for a disorderly Brexit, which should show details of the contingency planning and potential mitigation measures for the main risks. It will be especially important to cover the disruption effects related to a disorderly Brexit and displacement activity (e.g. Newhaven port which may take traffic from Dover).

26.3 The Chief Operating Officer responded he will take the advice from the Committee and create a disorderly Brexit item on the risk register. This will include the work that has already been done such as assessment in the workforce risk and the contingency planning that is taking place for national issues.

26.4 Councillor Bowdler asked if the Council has assessed the risk of further illegal immigration. The Chief Operating Officer outlined that asylum seeking placement activity and unaccompanied children is unrelated to the Brexit risk, and is covered in the Reconciling Policy, Performance and Resources (RPPR) budget setting process.

Risk from Funding Formula changes to Smaller Schools

26.5 The Committee discussed the risk arising from changes to the national funding formula for schools, which may have a particular impact on smaller schools. The Committee's concerns centre around the potential impact on primary schools, where a change in emphasis towards per pupil funding may make it more challenging to meet fixed costs. The risk to the Council arises from the possibility of smaller schools getting into financial difficulty and the impact this might have on school place planning and home to school transport costs. Some members of the Committee considered this is a developing strategic risk for the Council in the longer term, and should be on the Strategic Risk Register.

26.6 The Chief Operating Officer outlined that the risks are covered in the departmental risk register. These issues relate to the Council's statutory responsibility for school place planning and school performance, which are undertaken by the Children's Services department. As such they are within the programme of work being dealt with by the People Scrutiny Committee.

26.7 The Committee agreed that it would like further assurance that there are measures in place to deal with the financial risks arising out of the impact of funding changes on smaller schools. The Committee agreed to form a small working group comprised of Councillor Barnes and Councillor Fox who will meet with the Director of Children's Services to seek further assurance over the financial risks and report back to the Committee.

26.8 The Committee RESOLVED to:

- 1) have the disorderly Brexit risk as separate item on the Strategic Risk Register; and
- 2) seek further assurance on the risks arising from the impact of changes to funding on smaller schools from the Director of Children's Services via a small working group of Committee members.

27 ANNUAL AUDIT LETTER

27.1 The Chief Finance Officer introduced the report which provides details of the annual audit letter and fees from the Council's External Auditor, KPMG. This will be the last financial year that KPMG will audit the Council's accounts and those of the East Sussex Pension Fund. From 2018/19 onwards Grant Thornton will be the Council's External Auditors.

27.2 The Committee noted the annual audit letter and asked if the issue raised regarding the risk to the pension fund arising from hard to value investments is being monitored. The Chief Finance Officer responded that the Pension Committee is fully aware of the issue and is taking steps to look at the risk from hard to values investments.

27.3 The Committee RESOLVED to note the Annual Audit Letter and the fee update for 2017/18.

28 TREASURY MANAGEMENT STEWARDSHIP REPORT 2017/18 AND MID YEAR REPORT 2018/19.

28.1 The Chief Finance Officer introduced the report which outlines key issues in Treasury Management performance and the implementation of the Treasury Management Strategy. During the 2017/18 financial year the Council received £1.3 million from investments and repaid £4.8 million of Public Works Loan Board (PWLB) debt. There was no additional borrowing during this period, and there were no further opportunities to repay or restructure debt.

28.2 In the first 6 months of the current financial year (2018/19) the Council has invested £5 million in the CCLA Property Fund. The Council will repay £4.6 million of PWLB debt and £23 million of Lender Option, Borrower Option (LOBO) loans. The Council continues to look for opportunities to increase income, and reduce loans and the 'cost of carry' (which is the cost of loans the Council has taken out, less any income earned on deposits). The Treasury Management Strategy will be refreshed as part of RPPR process and a report will be presented to Cabinet in January 2019.

28.3 The Committee discussed the report and asked for clarification on a number of points:

- The repayment of the PWLB debt did not include any penalty payments as the loans had matured.
- The repayment of the LOBO loan was made from cash balances and was not financed by further PWLB borrowing.
- The Chief Finance Officer agreed to provide the Committee with further information on the Council's 'cost of carry' in comparison with other local authorities, and an explanation for the change in interest rates in the table in paragraph 7.1 of appendix D, after the meeting.

28.4 The Committee welcomed the investment in the CCLA Property Fund, which it noted was a very diversified property portfolio. The CCLA Fund had a very good investment strategy and the Chief Finance Officer offered to circulate a copy of due diligence report to the Committee. The Committee asked if the value of the fund fell as part of a mark to market loss, how this would be reflected in the Council's accounts. The Principal Accountant, Treasury and Taxation responded that at present it is out of scope as there is a statutory override, so the Council would not have to make a provision in its accounts at present. This override will continue for the next five years and then will be reviewed.

28.5 The Committee noted the CCLA investment and asked what the plans were for similar investments to increase income for the Council. The Chief Finance Officer outlined that the CCLA investment is part of a longer term strategy and the Treasury Management Team will look at further opportunities as part of the refresh of the Treasury Management Strategy. Lessons learnt from the CCLA investment will be applied to further work in this area, which will take a staged approach (e.g. a £5 million investment and then another £5 million).

28.6 The Committee RESOLVED to note the Treasury Management performance in 2017/18 incorporating the mid-year review for the first half of 2018/19.

29 WORK PROGRAMME

29.1 The Committee discussed the work programme and RESOLVED to have an update report on implementation of management recommendation of the Orbis Budget Management audit at the March 2019 Audit Committee meeting.

30 PROPERTY ASSET DISPOSAL AND INVESTMENT STRATEGY (INCLUDING LINKS TO THE COMMUNITY ASSET TRANSFER POLICY)

30.1 The Acquisition and Disposal Manager introduced the report. The Council has £550 million worth of non-highways assets on the property balance sheet, and most of the assets are fairly illiquid. There is a core of around £25 million worth of assets that have been the focus of the work on the Strategy, which could be delivered over the next five years. The work on the Strategy does not include direct property investment. However, the Strategy does include the ability to invest directly into new opportunities. For example, the Council could invest in a site that it owns to develop business units rather than sell the site. The report outlines the business processes and the sort of resources required for the implementation of the Strategy. This includes how the Strategy works with asset management planning, property planning and investment planning processes within the Council.

30.2 The Committee asked whether all assets and leased buildings are under central management. The Chief Operating Officer responded that the corporate landlord model is in place for most assets, but there are still a few smaller assets managed directly by departments. This is being reviewed as part of the RPPR process in terms of the operational estate. The management of the portfolio of operational assets, and the portfolio of non-operational and investment assets, are both functions within the Property Team. Corporate policy links asset management with the investment part of the property function.

30.3 The Acquisition and Disposal Manager outlined that from a portfolio management point of view, there are other financial and non-financial returns that can be achieved rather than simply achieving a capital receipt. Implementation of the Strategy includes a wider modelling of economic benefits. The Committee noted the process of site and asset reviews and where a higher level of social value benefit is possible, an opportunity for a Community Asset Transfer (CAT) of an asset may be identified. The Committee suggested that it would be good to

publicise the Community Asset Transfer process where an asset is transferred for specific social or community value outcomes, and that it is important to have a good explanation of the process.

30.4 The Committee asked whether there is a view on the equity to debt ratio and a minimum acceptable level of return, when the Council is looking at redeveloping or investing in an asset. The Acquisition and Disposal Manager replied that the equity to debt ratio and the level of return is taken into account on a site by site basis.

30.5 The Committee asked what was meant by paragraph 3.3 in the conclusion of the report. The Acquisition and Disposal Manager explained that this refers to the impact that changes to the delivery of services may have on property portfolio, which will in turn feed into the Property Asset Disposal and Investment Strategy work. The Committee asked if there was a risk of a premature disposal of assets in a scenario where the Council's finances change in the future. The Acquisition and Disposal Manager responded that the review process checks to see if an asset is suitable for alternative uses before it is declared surplus. So there is a process in place to assess whether an asset may need to be retained for future use.

30.6 The Committee RESOLVED to note the report covering the period April 2018 to September 2018.

31 ANY OTHER NON - EXEMPT ITEMS PREVIOUSLY NOTIFIED UNDER AGENDA ITEM 4

31.1 There were none.

32 EXCLUSION OF PUBLIC AND PRESS

32.1 The Committee RESOLVED to exclude the public and press.

33 PROPERTY ASSET DISPOSAL AND INVESTMENT STRATEGY - ADDITIONAL INFORMATION

33.1 The Acquisition and Disposal Manager introduced the report. The Committee discussed the summary analysis of the initial list of core sites and an indication of options available to support the investment strategy.

33.2 The Committee RESOLVED to note the information in the report.

34 ANY OTHER EXEMPT ITEMS PREVIOUSLY NOTIFIED UNDER AGENDA ITEM 4

34.1 There were none.

The meeting ended at 12.00 pm.

Councillor Colin Swansborough (Chair)
Chair