

AUDIT AND GOVERNANCE COMMITTEE MINUTES - 18 JULY 2017

Present: Councillor Stevens (Chairman), Duveen, Lovelock, McElligott, McKenna, Page, Steele & Terry

Apologies: Councillor Rodda

Also in attendance:

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| Peter Lewis | Strategic Finance Director |
| Alan Cross | Head of Finance |
| Sanjay Desor | Chief Technical Accountant |
| Ray Guard | CIPFA |
| Maria Grindley | Director and Engagement Lead, EY LLP |
| Paul Harrington | Chief Auditor |
| Alex Jaques | Managing Director - Homes for Reading Ltd |
| Peter Sloman | Chief Executive |
| Jo Taylor | EY LLP |

1. MINUTES

The Minutes of the meeting of 19 April 2017 were confirmed as a correct record and signed by the Chairman.

(Noted re: Minute 35, a report would be submitted to the meeting on 28 September 2017 on Housing Benefit issues, which would include an update on Housing Benefit subsidy claims)

2. INTERNAL AUDIT ANNUAL ASSURANCE REPORT

The Chief Auditor submitted a report presenting, at Appendix 1, the Internal Audit Annual Assurance Report, as required by the Accounts and Audit regulations and the Public Sector Internal Audit Standards. The report gave the Chief Auditor's opinion on the overall adequacy and effectiveness of the organisation's governance arrangements, risk management and internal control environment, drawing attention to any issues particularly relevant to the preparation of the Annual Governance Statement. It also drew out key themes arising from the work of the Audit Team during the 2016/2017 financial year, and compared them with the audit work undertaken with that planned, summarising the performance of the Internal Audit function against its performance measures and targets.

The report explained that detailed audit reports had been issued to the relevant Service Managers on the results of individual audits throughout the year, and to the relevant Directors and Heads of Service where unsatisfactory internal control had been identified. In addition, quarterly reports had been issued to, and discussed with, the Corporate Management Team (CMT) and the Audit & Governance Committee in order to report on standards of internal control, to provide appropriate focus on weaknesses and to progress remedial action where necessary.

The Annual Assurance Opinion for 2016/17 stated that the Chief Auditor Team had concluded that only limited assurance could be given that the arrangements to secure governance, risk management and internal control within those areas audited in 2016/17 were suitably designed and applied effectively. The Chief Auditor's

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opinion reflected the relatively high number of limited assurance opinions recorded during the year and took account of comments made by other inspection bodies, such as the External Auditor and Ofsted. It was particularly concerning that there were key weaknesses within some of the Council's financial systems. Examples of issues of concern were set out in the report and revealed that a key theme throughout was a lack of compliance with the policies and procedures that were in place. The fragile financial position of the Council, the focus on delivering a challenging package of savings and the frequent turnover of staff and reliance on interim managers in key areas was seen as contributing to the limited assurance opinion.

The report stated that the Corporate Management Team understood the challenges that had been drawn out through Internal Audit and was addressing them in its Annual Governance Statement and implementation plan (see Minute 3 below).

Members asked a number of probing questions about the contents of the report and sought assurance that rigorous action was being taken to resolve the concerns.

Resolved: That the 'limited assurance' opinion given by the Chief Auditor and the reasons for this opinion, as described in the report and explained at the meeting, be noted with grave concern.

3. ANNUAL GOVERNANCE STATEMENT 2016/17 AND IMPLEMENTATION PLAN

The Strategic Finance Director submitted a report introducing the 2016/17 Annual Governance Statement (AGS). The report explained that the Council was required to prepare and publish an AGS each year as an accompaniment to the authority's financial statements. The report had appended the Draft Annual Governance Statement 2016/2017 and the implementation plan. The report explained that the Council was responsible for ensuring that its financial management was adequate and effective and that it had a sound system of internal control, which facilitated the effective exercise of the Council's functions, including arrangements for the management of risk. The AGS was a record of the overall effectiveness of governance arrangements within the Authority; it reflected the latest guidance from CIPFA/SOLACE on a strategic approach to governance and demonstrated how the key governance requirements had been met. The report had appended the plan showing progress against the actions identified in the AGS. Overall, 10 headline actions had been identified, all of which had been or were in the process of being implemented.

The report commented on the Chief Auditor's opinion (see Minute 2 above), that only limited assurance could be given on the arrangements to secure governance, risk management and internal control were suitably designed and applied effectively in respect of audit work completed in 2016/17. Principally, the 'limited assurance' opinion was not derived from a lack of clear rules and procedures within the Council, but from a lack of compliance with them.

Additionally, the Council's External Auditor for the 2016/17 accounts, EY, had issued an adverse value for money conclusion on 17 November 2016. This meant that they had concerns over the Council's arrangements for securing financial resilience and for how it secured value for money in its use of resources. Although they had not identified any significant deficiencies in the design or operation of an internal control

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that might result in a material misstatement in the financial statements and which the Council was unaware, they had found that some of the basic financial controls were not working as expected. In particular, the regular completion of reconciliations was not being completed in a timely fashion. EY highlighted that the financial and performance information used by the Council was not always accurate and reliable and therefore did not help informed decision making.

EY had made statutory recommendations in February 2017 under Section 24 Schedule 7 (2) of the Local Audit and Accountability Act 2014. The Council had formally considered and approved an officer response to these recommendations at its February 2017 meeting and agreed progress towards addressing the recommendations would be monitored by the Audit & Governance Committee (see also Minute 9 below). EY had issued an unqualified opinion on the Council's 2015/16 financial statements on 17 November 2016. This meant that they believed the 2015/16 financial statements gave a true and fair view of the financial position of the Council and of its expenditure and income for that year. EY's audit of the financial statements had identified various adjustments to the draft accounts which the Council had agreed to make. The audit had raised recommendations to improve controls over bank and housing rent account year end reconciliation procedures and IT controls over applications and infrastructure, which the Council was addressing.

Resolved:

- (1) That the Annual Governance Statement for 2016/17, as appended to the report, be approved for publication with the Council's accounts;
- (2) That the Chief Executive, in consultation with the Leader of the Council and the Chairman of the Audit and Governance Committee, be authorised to make any necessary amendments to the Annual Governance Statement for 2016/17, prior to its publication in September 2017;
- (3) That the progress made to implement the actions reported in the 2016/17 Annual Governance Statement, as detailed in the implementation plan, which was appended to the report, be noted whilst at the same time expressing serious concern at the Chief Auditor's 'limited assurance' opinion (see also Minute 2 above) following the internal audits carried out in 2016/17, as well as the findings of the inspections by the External Auditors and Ofsted and as a result the Committee would require a further report to be submitted to its meeting on 28 September 2017 to provide confidence that adequate progress was being made to address the actions in the implementation plan and in particular to provide reassurance that the 'culture of non-compliance' with policies and procedures was being tackled.

4. INTERNAL AUDIT QUARTERLY PROGRESS REPORT

The Chief Auditor submitted a report providing the Committee with an update on key findings emanating from Internal Audit reports issued since the last quarterly progress

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report in April 2017. The report set out a summary of the audit reports in respect of General Ledger, Accounts Payable, Accounts Receivable, Bed & Breakfast Payments, E-tendering, Section 106 Follow-up Review and Governance Review. The report also contained a table showing the audit reviews currently in progress and those planned for the next quarter.

Resolved: That the report be noted.

5. CORPORATE STRATEGIC RISK REGISTER

The Strategic Finance Director presented a report with appended a schedule updating the Committee on the Q1 status of the Council's 2017/18 Strategic Risk Register, in line with the requirements of the Council's Risk Management Strategy. Entries within the Register reflected the risks identified by the Corporate Management Team thereby strengthening their strategic perspective, management response and controls. The inclusion of risks within any level of risk register did not necessarily mean there was a problem but reflected the fact that officers were aware of potential risks and had devised strategies for the implementation of mitigating controls. Each entry within the register was scored based on an assessment of their impact and likelihood, to provide an assessment of the residual level of risk. Plans were in place to mitigate the risks identified in the Strategic Risk Register.

Resolved: That the Q1 status of the Council's 2017/18 Strategic Risk Register be noted.

6. BUDGET MONITORING 2017/18

The Head of Finance submitted a report on Budget Monitoring that had been considered by the Policy Committee at its meeting on 17 July 2017 and was presented for information. The Committee noted that, based on the position at the end of May 2017, budget monitoring forecasted an overspend of around £1.216m, and that plans to address this position, if it persisted, would be presented to the Policy Committee in September 2017. Members also requested further information on the gross overspend and proposed mitigations in the next report.

Resolved: That the report be noted.

7. TREASURY OUTTURN REPORT FOR 2016/17 & RELATED UPDATE

The Head of Finance submitted a report presenting, at Appendix 1, the Annual Treasury Outturn Report 2016/17. The report explained that the Treasury Outturn report was intended to explain how the Council had tried to minimise net borrowing costs over the medium term, ensure it had enough money available to meet its commitments, ensure reasonable security of money lent and invested, maintain an element of flexibility to respond to changes in interest rates, and manage treasury risk overall. It also outlined some current treasury and related issues likely to impact the Council during 2017/18, in the context of the Council's revised financial plan and the measures considered by the Policy Committee at its meeting on 17 July 2017, which had been put forward to enable the Council to operate within the financial constraints of the current year's Budget.

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A Cross gave a presentation at the meeting summarising key treasury management issues.

Resolved: That the annual Treasury Outturn Report for 2016/17 be noted.

8. HOMES FOR READING LTD - ARRANGEMENTS

The Head of Finance submitted a report providing the Committee with information about the arrangements the Council had established in relation to Homes for Reading Ltd (HfR), and asking the Committee to identify any information it would need to fulfil its scrutiny function in relation to Homes for Reading Ltd, the Council's wholly owned company that has been set up to purchase and manage a portfolio of around 500 private sector rented properties over the next 5 years.

The report had appended for background information to the establishment of the Company:

- Council report - 22 March 2016;
- Policy Committee report - 13 March 2017;
- An Edited Extract from HfR Business Plan - Council Financial Implications.

The Committee noted that there would be an internal audit review of Homes for Reading Ltd later in the year (Quarter 4), which would be undertaken with the primary purpose of looking at measures in place to protect the interests of the Council. The scope of the review had not yet been finalised but would cover a wide remit from the procurement of properties to their ongoing maintenance. The Policy Committee had the responsibility for acting as the shareholder in respect of Homes for Reading Ltd but the Company's accounts could be shared with the Audit & Governance Committee to assist with its scrutiny role. The Committee would also be interested to receive the internal auditor's view on the how the performance of the Company could impact on the Council and the Council's exposure to any deficit that may occur if the Company did not break even.

Alex Jaques, Managing Director, Homes for Reading Ltd, was present at the meeting and addressed the Committee on this item.

Resolved:

- (1) That the set up arrangements associated with Homes for Reading Ltd be noted;
- (2) That the Audit & Governance Committee's duty to "provide oversight of governance arrangements and the overall financial position in relation to the company" be noted;
- (3) That the details be provided of the Company's financial position and performance, housing portfolio and any other relevant matters to assist members of the Audit & Governance Committee in their overview and scrutiny role in relation to Homes for Reading Ltd as

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well as receiving an assessment of any liabilities or benefits for the Council resulting from the performance of the Company.

(Councillor Lovelock declared an interest in this item. Nature of Interest: Councillor Lovelock was a Director of Homes for Reading Ltd).

9. PROGRESS IN IMPLEMENTING EXTERNAL AUDITOR'S (SECTION 24) RECOMMENDATIONS REPORTED AT BUDGET COUNCIL

The Strategic Finance Director introduced a report setting out the progress that had been made in responding to the actions identified in a letter issued by the Council's external auditor, EY, in accordance with Section 24 of the Local Audit and Accountability Act 2014. The letter and the Managing Director's response to the recommendations had been considered by the Council at its meeting on 21 February 2017. The report included a table setting out the external auditor's recommendations, the Council's initial response and details of the current position.

Resolved:

- (1) That the progress in implementing the External Auditor's recommendations, which had been reported to the Council on 21 February 2017, be noted;**
- (2) That the External Auditor's opinion of the progress made to address their recommendations be sought for inclusion in the report to be considered at the next meeting on 28 September 2017.**

10. ACCOUNTS 2016/17 & EXTERNAL AUDITOR UPDATE

The Head of Finance presented a report on the Accounts for 2016/17, which had appended the External Auditor's (EY) update on progress report. The report explained that the Council was required to publish its draft accounts by 30 June and that the External Auditors had just started their work to review them. The External Auditors would report their conclusions on the Accounts and their value for money opinion to the next meeting on 28 September 2017. EY's progress report identified some issues to be resolved in relation to bank reconciliation; control account reconciliation and journal control. These issues would have an impact on EY's testing processes and audit work and this would lead to an increase in the audit fee to reflect the extra systems testing that would be required. In addition, the issues would need to be addressed by taking on extra support to resolve them.

Resolved:

- (1) That the publication of the Council's Draft Accounts for 2016/17 be noted;**
- (2) That the External Auditor's update on progress, as appended to the report, be noted.**

(The meeting started at 6.30pm and closed at 8.15pm).