

CFO Response on behalf of Management

Appendix 1

Mr Hassan Rohimun
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Dear Mr Hassan Rohimun

Walsall MBC Financial Statements for the year end 31 March 2016: Understanding management processes and arrangements

Thank you for your letter dated 1st April. Please find below the responses in relation to your questions:

1. What are the Management processes in relation to:

- **Undertaking an assessment of the risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments)**

An assessment of the key risks to the financial statements is undertaken annually. This covers areas where there is a higher risk of misstatement or error and ensures that sufficient controls and checks are in place to mitigate the risk. The assessment includes the review of findings from external audits interim audit of the accounts and internal audits annual review of key financial systems which includes the risk of fraud, coverage of internal controls including approvals, segregation of duties, potential for override of controls, etc. From these, management are able to gain some assurance that key financial, IT and internal control systems are in place and working effectively. Management also ensure that recommendations arising from audits are actioned promptly.

The nature of the assessment also includes a review and sign off by the CFO of accounting estimates, judgments and decisions, a senior accountancy officer review of working papers of the financial statements, appropriate segregations of duties in respect of entries within the accounts, journal controls, and creditor/debtor balance reviews, ensuring that revenue is appropriately recognised in the accounts.

Key procedures are reviewed and kept up to date, and when new systems or policy changes occur (for example the annual review of treasury management (TM) policy statements and practices), training / briefings are provided.

Management processes include a review of results of the external auditors audit of the accounts each year and the ISA260 report, and ensures follow up of key recommendations. Recommendations from internal and external audit reports are actioned promptly and management review progress in implementation. The Head of Finance also ensures that follow up actions from the previous year's audit of the accounts have been fully implemented to ensure reduced risk of misstatement.

The CFO and the Chief Executive are also required to provide assurance in the form of the Annual Letter of Representation on matters relating to the financial statements, to which the Monitoring Officer (MO) contributes.

Review of arrangements for counter fraud and anti-corruption are undertaken regularly. The last review was undertaken in 2015 and reported to Audit Committee in September. Training is provided on key policies and procedures including the Code of Conduct, internal controls, risk, etc and appropriate segregation of duties is maintained.

Training is also provided in key areas of the statement and changes in accounting policies and their implications on the statements are regularly delivered. The review of the statement of accounts focuses on the suitability of accounting policies and treatments, changes in policy, major areas of judgement such as provisions, and any significant adjustments. Once this has been covered and assurance received, the accounts are approved.

Recommendations and actions from internal audit reports are followed up to ensure control weaknesses are mitigated. Follow ups are made on No or Limited Assurance audits to ensure action is being taken to improve internal controls and minimise the risk of fraud or error. Progress is reported to Audit Committee.

- **Identifying and responding to risks of fraud in the Authority, including any specific risks of fraud which Management have identified or that have been brought to its attention, or classes of transactions, accounts balances, or disclosure for which a risk of fraud is likely to exist**

The council's processes are detailed in the anti fraud / anti corruption policy, containing the fraud and corruption response plan. Fraud reporting responsibilities are also detailed in the confidential reporting policy (Whistle Blowing), which is supplemented by an on-line notification tool. A counter fraud review was undertaken and reported to Audit Committee on 1 September 2015, and the Committee received and endorsed a refreshed counter fraud policy and anti money laundering policy and received the Protecting the English Public Purse (PEPP) 2015 report. Where fraud or corruption is reported, there are robust mechanisms in place to address these.

The council has counter fraud resources within audit and the benefits service and makes use of NFI.

The Internal Audit plan covers the main areas of internal control risk. The council's specific fraud risks have been identified in a Fraud Risk Register which maps key fraud risks to internal audit coverage. Core financial systems are audited each year, each audit resting and reviewing specific areas of internal control and fraud risks, including the testing and appropriateness of controls such as segregation of duties, etc. Any weaknesses are reported and required to be dealt with promptly.

Internal Audit produce reports on their work activity including where suspected fraud has taken place and has been investigated. Members have the opportunity to scrutinise the activity noted within the summary reports. Where significant matters, including fraud, are identified by Internal Audit, these are brought to the attention of the Audit Committee as soon as possible to give assurance that appropriate remedial action has or is being undertaken.

Internal Audit reports regularly on its audit work, including reporting on audits where No or Limited Assurance audit opinions have been received.

Cases of suspected fraud are investigated thoroughly and actions reported to the CFO and to the Audit Committee. The Head of Internal Audit ensures the CFO is advised of all matters in relation to fraud and that appropriate investigations are put in place. The Head of Internal Audit liaises with senior officers in the responsible areas to assess the risks and agree any further actions required to mitigate risks.

Specifically, an area of suspected significant fraud was identified and reported to Internal Audit in relation to Supported Housing and there is an ongoing internal investigation into this matter and a criminal investigation by the Police. This and other alleged, suspected or actual fraud have been reported to Audit Committee and made available to external audit.

- **Communicating to employees its views on business practice and ethical behaviour (for example by updating, communicating and monitoring against the Authority's code of conduct)?**

All employees are issued with an employee Code of Conduct on employment and, during induction, the importance of ethical behaviour is made clear. The Code was approved in January 2014; last Code update was June 2015. The Code is also referenced in other HR and counter fraud policies and is made available on the intranet. The Code of Governance also sets out responsibilities and expectations in relation to good business practice and ethical behaviour.

- **Encouraging employees to report their concerns about fraud**

The latest counter fraud policy update was reported to Audit Committee on 1 September 2015 and included a planned training module for all employees to raise awareness of counter fraud arrangements and reporting mechanisms. Counter fraud policies and the whistle blowing policy provide clear guidance on reporting arrangements for suspected or actual fraud. As stated above, internal audit reports to the Committee summarise allegations of fraud, and action taken. The council is clear that it has a zero tolerance approach to fraud corruption and communicates this to employees.

- **Communicating to the Audit Committee (and those charged with governance) the processes for identifying and responding to fraud or error?**

Audit Committee oversees the council's counter fraud arrangements. Counter fraud policies and updates are reported to and endorsed by the Committee. These include the process for identifying and reporting suspected or actual fraud. Updates are provided to the Committee on counter fraud activity and this forms part of the Audit Committee annual work plan. The fraud risk register was updated in August 2015 and this informs the annual audit plan. A counter fraud update was reported to Audit Committee on 1 September 2015. In relation to error, internal audit planned work covers core financial systems and other key areas of risk in relation to internal control.

Audit Committee are advised that irregularities may be noted in a number of different ways; during regularity audit reviews; or be reported from a number of sources, including council

managers, employees, occasionally via the confidential reporting policy (whistle blowing), and externally. Irrespective of how the allegations are reported, each will be subject to investigation. Some result in little investigatory time having to be spent, others can take longer. Relevant action, where found to be appropriate, will always be taken, i.e. disciplinary, court proceedings, police referral and recovery of losses.

2. What are Management's views about whether there are areas within the organisation that are at risk of fraud?

In any organisation the size and complexity of Walsall MBC, there is a risk of fraud and whilst this can be mitigated with an appropriate control framework and effective prevention and deterrence strategies, it cannot be fully eliminated. The council has a fraud risk register which was updated in August 2015. This maps fraud risks to the internal audit plan and areas of high risk are high priority for internal audit activity. These include core financial systems, housing benefit and council tax benefit (council tax reduction), payroll, procurement and contracts.

The council has a comprehensive internal control framework which includes both proactive and reactive counter fraud activity. The council has a clear policy on counter fraud and money laundering and counter fraud arrangements which are communicated to employees (and stakeholders where appropriate e.g. to contractors via contract documentation). All employees (and members) are made aware of the Code of Conduct. Internal audit activity focuses on high risk areas in terms of audit planning.

There are sound procedures and process in place for employees or others to report suspected or actual fraud and these are always robustly investigated. The council also participates in NFI data matching.

3. Does Management have knowledge of any actual or suspected or alleged instances of fraud or fraudulent financial reporting?

Yes. All actual, suspected or alleged instances of fraud were reported to Audit Committee during the year and external audit were made aware of these.

4. Where the answer to question 3 above is 'yes' what was Management's response to the situation identified?

An internal investigation by the Money, Home, Job fraud team was instigated and the matter referred by management in that area to Internal Audit. An Internal Audit investigation commenced and the matter was also referred to the police. The individual concerned in the alleged fraud was suspended and subsequently resigned. There is currently an ongoing criminal investigation into this matter. A detailed action plan was agreed which is currently being worked through.

5. Is Management satisfied that internal controls to prevent and detect fraud, including segregation of duties, exist and work effectively?

The adequacy of controls is detailed in the Head of Internal Audit's annual report on the overall adequacies of the internal control environment. When this was last reported to Audit Committee on 20 July 2015 the overall opinion given was as follows: "In my opinion, formed solely on the basis of the work undertaken by Internal Audit and its partner organisation in 2014/5, and the

positive action taken or intended to be taken by managers to implement agreed audit report actions, a significant level of assurance can be provided in relation to the overall adequacy and effectiveness of Walsall Council's framework of governance, risk management and control (the internal control environment)."

The Audit Committee receive 6 monthly summaries of planned audit work undertaken. Any audit reports which receive a No or Limited assurance opinion are directly reported to Audit Committee. These audits are subject to early follow up. If at the follow up audit, agreed high priority findings have not been addressed and the assurance opinion remains limited or below, then this is reported to the Audit Committee where accountable managers and their Executive / Assistant Director, may be required to attend to give necessary assurances that appropriate corrective action is being taken.

Audit Committee also receive 6 monthly progress reports on unplanned activity undertaken by the Internal Audit service. The Committee may require, and indeed it does require, accountable managers and their Executive / Assistant Director to attend to give necessary assurances that appropriate corrective action is being taken on control issues identified. Internal Audit reports on significant areas of fraud or irregularity are shared with the Council's external auditor.

The Annual Effectiveness Review of the System of Internal Control and Internal Audit and Annual Governance Statement 2014/15 presented to Audit Committee on 23 September 2015 contains the findings and recommendations of the review of the effectiveness of the council's system of internal control. This report concluded that the effectiveness of the system of internal control is adequate overall. No new significant areas of weakness were identified in the 2014/15 AGS.

During 2015/16, a number of areas of control weaknesses have been identified in a number of areas, including the following planned areas, where a Limited Assurance opinion was given (there were no audits with a No Assurance opinion):

Planned Audits:	Service
Solihull Framework for Integrated Facilities Management (draft)	IFM
Residential Charging (final)	Adult Social Care
ICT Risk Management (draft)	ICT
Social Media (draft)	ICT
Christ Church Primary School (final)	Education
Jane Lane School (final)	Education

The following 'Limited Progress' follow up reports, relating to previous years' audits, have also been issued:

- Personal budgets including direct payments
- Asset management

9 unplanned/ irregularity reports were also issued. All of the Limited Assurance audits reports were made available to external audit and progress reports on

unplanned/irregularity reports presented to Audit Committee.

Directors have confirmed that there are action plans in place which are being closely managed for the above.

6. Are there any deficiencies in internal control?

Deficiencies in internal control are reported in audit reports and followed up as appropriate, specifically for reports with a No or Limited assurance (see above). Additionally, the Head of Finance follows up all audit reports in respect of core financial systems to ensure high priority actions are being implemented. Audit reports are shared with external audit, along with summaries in respect of unplanned/irregularity activity and any resulting action.

7. Are you aware of any instances where controls have been overridden?

Management are not aware of any instances of controls being overridden.

8. Is there any organisational or management pressure to meet financial or operating targets?

Walsall MBC, as any Authority, is under financial pressure from reduced government funding and increases in demand and cost pressures, particularly within Adult Social Care and Children's Services. Managers are expected to deliver to agreed service targets and delivery requirements within the approved budget wherever reasonably possible. It is recognised that changes in demand, legislation, etc may occur once a budget has been set. The council undertakes a comprehensive risk assessment of the budget and has appropriate processes in place to manage these – including an appropriate level of general reserves and contingencies should in place to manage these scenarios.

Management are not aware of any undue pressure to meet operating or financial targets.

Financial reporting processes are set out in the budget management and control manual, vital skills training for non-financial managers, and are supported by specific procedures and accounting policies.

Accounting arrangements are undertaken in accordance with all relevant Codes of Practice. Comprehensive final accounts guidelines and outturn proformas, along with risk assessments of the financial outturn, senior officer review of reports and the accounts, officer review of provisions, reserves, carry forwards, accruals and liabilities, ensure override of controls or inappropriate influence is minimised.

Analytical review of the income and expenditure account and balance sheet adds to this. Major variances between years and in years are reviewed for accuracy.

The Accounts are independently audited.

9. Are there any particular areas of the accounts that are more susceptible to false entries or omission or other forms of manipulation? Are Management aware of any such manipulation having occurred?

The CFO undertakes an assessment of the accounts at least annually and any changes arising from regulations which could impact. This assessment covers areas of the accounts where entries, omissions or other form of manipulation could take place, including a review of accounting estimates, judgments and decisions used in producing the accounts, a senior accountancy officer review of working papers of the financial statements to identify errors or omissions, ensuring appropriate segregations of duties are in place in respect of entries within the accounts and journal controls, creditor/debtor balance reviews and ensuring that revenue is appropriately recognised in the accounts. These mitigate any risk of false entries or omission.

Management are aware of and have reported to you concerning the support housing fraud investigation.

10. How does Management gain assurance that all relevant laws and regulations have been complied with?

The council has a corporate governance framework in place against which elected members and officers are held to account to act in accordance with the law and regulations. The council has appointed a monitoring officer (MO) to ensure that the council acts lawfully and provides the MO with sufficient resources to enable him to carry out his role. In addition, the council has an Internal Audit section to test and report on compliance and performance against the governance framework. The Council has an Audit Committee and Standards Committee to oversee issues of governance.

Management gains assurance through various mechanisms, as set out below, however management cannot obtain full assurance, only reasonable assurance, which is gained through its knowledge of the organisation and the controls in place. The various mechanisms are:

- That the council has robust contract and finance rules and a scheme of delegations in place which are updated on a regular basis. Audit Committee has oversight of changes to these and also receives reports detailing decisions made under officers delegated powers within the financial year.
- The Chief Executive and other corporate officers set out clear expectations in respect of behaviours and conduct in respect of adherence to statutory and council rules, regulations and procedures, supported by a suite of procedures, guidance manuals and procedures advising how to comply and who can provide support and advice in these matters.
- Through Executive Director, Assistant Director and Head of Service assurances a part of the final accounts process.
- Through the work of the Internal and External Auditors, and the Chief Finance Officer, assessing and reporting on controls and any breaches.
- Through the actions of professional officers across the council complying with the corporate governance framework
- Through committee reporting processes where reports requiring decision making are required to have been consulted on with Finance and Legal Officers to ensure appropriate advice is given.
- Through the committee reporting process which provides for legal comment on all reports where the council is exercising functions.
- Through provision of a range of intelligence and updates on legislative changes and their implications including through external means, such as LGA, LGIU, professional bodies, and internal means such as policy briefings.

11. Have there been any instances of non-compliance during 2015/16?

As reported in the 2014/15 audit risk assessment there has been an instance of non-compliance in respect of Appointeeships in Adult Social Care. The impact was assessed and accounted for in the statement of accounts, with the value not being material. Further work has taken place during 2015/16 to put in place processes to prevent any further issues of non-compliance, with the outcome of this work expected to conclude in 2016/17.

12. Are there any actual or potential litigation or claims that would affect the financial statements?

None that will not already be included within the accounts, which are currently being finalised and will be reported to the Audit Committee in June prior to external audit of the accounts. External audit has been advised of all actual or potential limitation or claims as they have arisen or become known.

13. How does Management satisfy itself that it is appropriate to adopt the going concern basis in preparing the financial statements?

The CFO carries out a 'going concern' assessment. This includes an assessment of net worth, assets and liabilities, use of ratio analysis and the wider balance sheet position. The council has agreed and reports monthly on a set of financial health indicators, which forms part of this assessment along with reporting on other key indicators such as Prudential Code indicators, revenue and capital outturn forecasts, the position on general and earmarked reserves, and a constant review and update of the council's medium term financial outlook, alongside future funding, income and cost predictions and forecasts. The assessment does not focus on just the current years but into the foreseeable future. The MTFO is constantly updated to reflect future changes and fluctuation, specifically in terms of funding and income streams, and significant cost pressures such as pension, pay etc.

Additionally, assurance is obtained from the Letter of Representation which is signed off by the Chief Executive and approved by Audit Committee, and through a thorough understanding of the financial position of the council and the statement of accounts.

Going concern is reviewed and reported to the Audit Committee within the statement of accounts. The council's balance sheet shows a negative balance. This is largely due to the net pension liability, however this liability is to be paid over many years and would not be due for payment immediately as the balance sheet suggests. In addition, it is planned for the pension liability to decrease and achieve a breakeven position in 20 years, and contribution rates have been set for the next year on this premise. Taking these into account, the underlying balance sheet is sound.

The CFO is satisfied that it is appropriate to adopt the going concern basis for the foreseeable future.

Yours sincerely

James Walsh – Chief Finance Officer (On behalf of Management)