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Dear Catherine

Audit of Durham County Council's Financial Statements (including the Pension Fund) 2014/15 – Compliance with International Auditing Standards

Thank you for your letter dated 11 June 2015 regarding the above.

I have noted the response provided by Don McLure as the Council's Section 151 Officer, in relation to the management arrangements in place for those areas covered by the International Auditing Standards you refer to, and would like to add the following comments from the Audit Committee's perspective.

ISA 240 Consideration of fraud in the audit of the financial statements

- 1) How does the Audit Committee, in its role as those charged with governance, exercise oversight of management processes in place relating to fraud?***

The Audit Committee maintains an oversight of management processes in place for assessing the risk that the financial statements may be materially misstated by considering all the sources of assurances that it has available to it on the effectiveness of the control environment. This is demonstrated through quarterly internal audit progress reports and the Annual Audit Opinion and Internal Audit Report that is presented to the Committee by the Chief Internal Auditor and Corporate Fraud Manager.

The Audit Committee also receives quarterly risk reports from the Risk and Governance Manager where key strategic risks are brought to the attention of the Committee.

The Audit Committee is responsible for considering proposed changes to the Council's Counter Fraud and Corruption Strategy and the Confidential Reporting Code (Whistleblowing) a revised version of both was approved by the Committee in May 2014. The Audit Committee will also consider any changes to the Fraud Response Plan that supports the strategy and to the Council's Money Laundering policy and monitor their effectiveness. These are due to be reviewed by the Committee in 2015/16.

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Members of the Committee are aware of how to report any suspected fraud and are satisfied that employees are encouraged to report their concerns about fraud and both are supported by the Confidential Reporting Code (Whistleblowing) which was formally reviewed and amended in May 2014 with a further review to be put to the Audit Committee for approval on 29 June 2015.

2) *How does the Audit Committee oversee management processes to identify and respond to the risk of fraud and possible breaches of Internal Control? Is the Audit Committee aware of any breaches of internal control during 2014 / 2015?*

The Committee is responsible for considering any proposed amendments to the Council's Code of Local Governance prior to approval by Full Council, and maintains an understanding of key corporate policies and procedures that are an integral part of the Council's Internal Control Framework to help mitigate the risk of fraud e.g. officers and members code of conducts, financial procedure rules, contract procedure rules, officer scheme of delegations, complaints procedures and performance management arrangements.

3) *Has the Audit Committee any knowledge of any actual, suspected or alleged fraud during the period 1 April 2014 to 31 March 2015?*

The Audit Committee is aware that all suspected cases of corporate fraud must be reported to the Chief Internal Auditor and Corporate Fraud Manager and are advised of all potential and proven cases reported. Bi-annual Protecting the Public Purse reports also advise the Committee of the number of Housing Benefit and Council Tax Benefit fraud cases handled.

Details of all actual, suspected or alleged fraud and action taken in response are as reported by the Chief Internal Auditor and Corporate Fraud Manager through bi-annual reports. New potential cases of corporate fraud will also be reported to the Committee as and when they arise and updates are provided through Internal Audit Quarterly progress reports.

Therefore the Committee is aware of a number of proven and potential frauds.

4) *Has the Audit Committee any suspicion that fraud may be occurring within the organisation?*

The Committee has a good understanding of where fraud may be occurring and actively seek assurance on any specific risks that are identified. These are alerted to the Committee through quarterly internal audit progress reports.

In addition the Committee approve the annual Internal Audit Plan and provide challenge to the counter fraud work planned each year to ensure that adequate assurance is provided on high fraud risk areas.

The Audit Committee receives specific updates, twice a year, on Counter Fraud Activity and is aware of a number of actions being undertaken or planned to help embed a strong counter fraud culture.

The Committee is kept informed of the Audit Commission's National Fraud Initiative exercise and the outcomes. The Committee is also kept informed of key messages from other national initiatives and publications that highlight potential fraud risks that the Council could be exposed to for example a presentation of Durham County Council's Counter Fraud Activity was delivered by the Chief Internal Auditor and Corporate Fraud Manager in July 2014. Therefore we are able to challenge how the risk of fraud and corruption is being managed within the authority and to actively seek assurance that management arrangements in place are effective.

5) *Is the Audit Committee satisfied that internal controls, including segregation of duties exist and work effectively?*

The Committee is satisfied through the answer to question two above. In addition the Committee receive the Annual Audit Opinion and Internal Audit Report from the Chief Internal Auditor and Corporate Fraud Manager that gives assurance the internal controls are working effectively and also receive regular quarterly reports on Internal Audit progress. The Committee also review the draft Annual Governance Statement where in addition to the assurance from the Chief Internal Auditor and Corporate Fraud Manager the Committee also receive statements from Corporate Directors that controls are working effectively.

6) *How do you encourage staff to report their concerns about fraud and what concerns about fraud are staff expected to report?*

The Audit Committee is responsible for considering proposed changes to the Council's Confidential Reporting Code (Whistleblowing) a revised version was approved by the Committee in May 2014. This was formally communicated through an employee briefing to all staff.

Members of the Committee are aware of how to report any suspected fraud and are satisfied that staff are encouraged to report their concerns about fraud and both are supported by the Confidential Reporting Code (Whistleblowing).

7) *From a fraud and corruption perspective, what are considered by the Audit Committee to be high risk posts within the organisation?*

The Committee is aware that certain posts, such as those involved with treasury management activities and those with access to the Council's bank accounts and cash, carry a higher risk and consequently covered by fidelity guarantee insurance.

The Committee also receives assurance from Internal Audit from planned work around key financial systems and the counter fraud plan that is reported through quarterly Internal Audit progress reports and the bi-annual fraud reports.

8) *Is the Audit Committee aware of any related party relationships or transactions that could give rise to instances of fraud?*

The Committee is aware of the processes and controls in place to identify and monitor related party transactions and the relevant reporting requirements for this. The Committee

is not aware of any related party relationships or transactions that could give rise to instances of fraud.

- 9) *Is the Audit Committee aware of any entries made in the accounting records of the organisation that it believes or suspects are false or intentionally misleading?***

The Committee is not aware of any specific entries made in the accounting records of the Council that it believes or suspects are false or intentionally misleading.

- 10) *Is the Audit Committee aware of any organisational, or management pressure to meet financial or operating targets?***

The Committee is not aware of any inappropriate organisational or management pressure to meet financial or operating targets.

ISA 250 Consideration of laws and regulations in an audit of financial statements

- 11) *How does the Audit Committee gain assurance that all relevant laws and regulations have been complied with?***

The Audit Committee is responsible for the annual review of the Council's Local Code of Corporate Governance and approving the Annual Governance Statement and is therefore aware of management arrangements in place for identifying and responding to changes in laws and regulations and any significant governance issues arising as a result.

The Audit Committee gains independent assurance over the effectiveness of the arrangements in place through the work of Internal and External Audit and other external review bodies.

The Audit Committee receives regular updates on the management of strategic risks that include risks relating to non-compliance with laws and regulations.

ISA 501 Specific consideration of the potential for, and actual, litigation and claims affecting the financial statements

- 12) *Is the Audit Committee aware of any actual or potential litigation of claims that would affect the financial statements?***

The Audit Committee is aware of the monitoring and reporting arrangements in place of financial risks associated with potential litigation claims and seeks to gain assurance that revised processes are effective and that any material amounts, significant risks or control implications are brought to its attention.

ISA 550 Related parties

13) *What controls are in place to identify, authorise, approve, account for and disclose related party transactions and relationships?*

The Committees is aware that all Members and the Corporate Management Team are required to complete an annual return of related party relationships and transactions and guidance notes have been issued to support their completion. Where any related transactions are declared extracts are obtained from Accounts Payable to identify actual payments made and received.

In addition, Internal Audit carries out periodic reviews of all employees and members' declarations to help identify any potential undeclared relationships and / or fraudulent transactions using outputs from data matching exercises. The last review was conducted during 2013 / 2014.

The Committee is also aware that Corporate Finance are preparing a list of all related party transactions, with an explanation of the nature of these and whether any transactions have been entered into with these related parties during 2014 / 2015. These will be included in the 2014 / 2015 statement of accounts for the Committee's approval in July 2015.

14) *Confirm that the Audit Committee has disclosed to the auditor the identity of the entity's related parties and appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the framework.*

The Committee confirms that the identity of all the authority's related parties have been appropriately disclosed in accordance with the requirements of the framework.

ISA 570 Consideration of the going concern assumption in an audit of the financial statements

15) *How has the Audit Committee assessed and satisfied itself that it is appropriate to adopt the going concern basis in preparing the financial statements?*

The Audit Committee will consider a report of the Corporate Director, Resources at its meeting on 29 June 2015 relating to an assessment of the going concern assumption. The Committee is satisfied that it is appropriate to adopt the going concern basis in preparing the 2014 / 2015 financial statements.

16) Has the Audit Committee identified any events or conditions since the assessment was undertaken which may cast significant doubt on the organisation's ability to continue as a going concern?

The Audit Committee has not identified any events or conditions since this assessment was considered which cast any doubt on the Council's ability to continue as a going concern.

If you have any further questions or comments on the content of this letter please do not hesitate to contact me.

Yours sincerely

Councillor Edward Bell
Chair of Durham County Council Audit Committee