

Copeland Borough Council

Section 24 Statutory recommendations

14 March 2022



Copeland Borough Council
Copeland Centre
Catherine Street
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14 March 2022

Dear Members

[Recommendations made under section 24 schedule 7 of the Local Audit and Accountability Act 2014](#)

Our responsibilities

Our responsibilities are to give an opinion on the financial statements and assess the arrangements for securing economy, efficiency and effectiveness in Copeland Borough Council's use of resources, and we also have additional powers and duties under the Local Audit and Accountability Act 2014. These include powers to issue a public interest report, make written recommendations, apply to the Court for a declaration that an item of account is contrary to law, and to give electors the opportunity to raise questions about the Council's accounts and to raise objections received in relation to the accounts.

We have concluded that, it is appropriate for us to use our powers to make written recommendations under section 24 of the Act, due to inadequate arrangements in financial governance and the Council's capacity and capability to effectively respond and implement a large number of review recommendations raised by the Department for Levelling Up, Housing and Communities, Grant Thornton and the Chartered Institute of Public Finance and Accountancy (CIPFA), with the direct financial and human resource costs adding further pressure to a very fragile financial position. Further details are set out in the attached report.

What does the Council need to do next?

Schedule 7 of section 24 of the Local Audit and Accountability Act 2014 requires the following actions:

The Council must consider the recommendations at a meeting held before the end of the period of one month beginning with the day on which it was sent to the Council.

At that public meeting the Council must decide:

- Whether the recommendations are to be accepted
- What, if any, action to take in response to these recommendations.

Schedule 7 of section 24 also specifies the meeting publication requirements that the Council must comply with.

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Council Context

Late financial statements and external audits

Copeland Borough Council has a relatively small finance team. The recruitment and retention of skilled and qualified finance staff in the locality has been an ongoing and longstanding issue, which the Council attributes primarily due to the neighbouring Nuclear Decommissioning Authority (NDA), who offer more favourable terms and conditions to employees.

The Council recruited a new Service Director of Financial Resources in June 2018, who commenced recruitment and filled some vacancies, whilst recognising the training requirements needed for the team to function properly. Added to this, the Council has worked collaboratively with neighbouring councils and bought in skills and experience from CIPFA and LG Futures, but recognises this incurs additional cost and is not an ideal substitute for an internal fully staffed and skilled finance team. The retention of key finance team members remains an ongoing challenge for the Council. We recognise that the Estates team has been strengthened. Copeland Borough Council's (the Council) 2018/19 and 2019/20 and 2020/21 financial statements and value for money conclusions have not yet been completed. The Council has produced draft statement of accounts for the 2019/2020 financial year, but none as yet for 2020/21.

Cyber attack

Combined with the staffing and skills shortage, the Council suffered a major cyber-attack in August 2017, which disabled both financial and other critical service IT systems creating long-lasting effects on the Council's ability to function properly. This was a zero-day exploit, meaning that the ransomware attacked an unknown security vulnerability not previously identified by software vendors. Government in October 2020 affirmed that, the attack on Copeland Borough Council was a significant incident that had major and long-term consequences. All ICT systems were affected, some of which were lost forever. The Council's custom of keeping all system data back-ups online rather than through isolated, air-gapped offline backup data storage meant that backups were also infected and inhibited the Council's ability to restore systems. With no full, up-to-date asset register, forensic investigations needed to be completed to more fully understand what data and information had been lost. The Council had to make tough choices on prioritising areas to get back to business as usual. It rightly focused on those most vulnerable residents of the Borough and other essential services from a public health perspective, such as revenue and benefits distribution and waste collection. Financial reporting systems and feeder systems were badly affected by the attack and required a rebuild, but this was a lower priority area in the wider context of the Council's other key functions, roles and responsibilities.

External Audit progress update context

Copeland Borough Council's (the Council) 2018/19 and 2019/20 and 2020/21 financial statements and value for money conclusions have not yet been completed. The Council has produced a draft set of financial statements for 2019/20, which will be updated on completion of the 2018/19 to take account of the audit changes made.

The last certificate closing the audit was issued for 2017/18 in February 2021. The 2017/18 accounts, following the devastating cyber attack, were not fully supported by working papers and contained numerous errors, including two material matters regarding buildings valuation and expenditure cut off, which resulted in limitation of scope related qualifications in the 2017/18 audit report opinion. The weaknesses prevalent also led to serious governance failings as covered in detail in our 2017/18 Audit Findings Report and qualified adverse VFM conclusion.

We are largely complete on the 2018/19 audit subject to the Council carrying out a new revaluation of its Property, Plant and Equipment and Investment property assets, which will require adjustments to the financial statements and Narrative Report. We also issued statutory recommendations in February 2021, for the Council to:

- Introduce robust arrangements for the production of late 2018/19, 2019/20 and 2020/21 financial statements, which meet statutory requirements and international financial reporting standards
- Implement outstanding audit recommendations and Annual Governance Statement governance related weaknesses and actions, especially those related to ICT and business continuity, and regularly update management and members with progress and implementation of improved controls; and
- Carry out independent Internal Audit and Audit Committee effectiveness reviews to assess their impact on improving the Council's internal control environment.

We acknowledge that, the Council has made some progress on these statutory recommendations but further work is required, especially to bring the Council back into line with financial statement statutory reporting deadlines to support fully informed decision making and to implement the various recommendations now raised in the independent reviews carried out by CIPFA on the effectiveness of its Internal Audit service and the Audit Committee. The Council has made progress on the accounts preparation and responses to our audit queries, but further work on valuation of property plant and equipment is required. The Council has recently made progress on ICT governance weaknesses but the development of robust business continuity plans still need to be implemented.

Background to the recommendations

We have concluded that, it is appropriate for us to use our powers to make written recommendations under section 24 of the Act, due to inadequate arrangements in financial governance and the Council's capacity and capability to effectively respond and implement a large number of external review governance related recommendations raised by the DLUHC, Grant Thornton and CIPFA, with the direct financial and human resource costs adding further pressure to a very fragile financial position.

Financial Governance weaknesses - Grant Thornton and DLUHC Review

In Grant Thornton's 2017/18 Value for Money work we identified weaknesses in informed decision-making regarding scrutiny and content of the Medium Term Financial Strategy (MTFS), capacity within the finance team, delays in producing statutory accounts and material errors within the draft accounts. In October 2020, the Council sought a capitalisation directive for 2021/22 of £1.5m, using existing monies it had previously borrowed for capital purposes but now needed for its revenue budget to enable a balanced budget position. Confirmation of a provisional offer from DLUHC was received in February 2021, which allowed for a balanced budget to be set, as approved by Full Council on 23 February 2021. The reported gap for the 2022/23 Budget at the time was £4.2m, which the S151 Officer has reported will require a further £1.5m capitalisation direction in 2022/23 and without further exceptional support and use of reserves it will leave the Council in the territory of issuing a section 114 notice. This at the time meant that, the Council was unable to set a balanced budget with expenditure exceeding revenue and effectively no new expenditure is permitted. In February 2022, DLUHC confirmed the approval of the 2021/22 £1.5m capital direction and has given provisional approval on the additional £1.5m direction for 2022/23, subject to the Council implementing the DLUHC Report recommendations.

The Council currently believe if the second capital direction to the value of £1.5m does not materialise the Council can cover this gap through the use of redirected unearmarked reserves. The general fund reserves and earmarked reserves are projected to be £2.2m, set at the minimum level, and £3.4m respectively as at 31 March 2023. The additional £1.5m 2022/23 capital direction is subject to conditions, which if not met will mean the Council will have to utilise the majority of its remaining unearmarked reserves of £2.133m, leaving a very small reserve position of £0.633m plus general fund reserve of £2.2m as at 31 March 2023. We note that the Council has now committed a £1.6m contribution to Local Government Re-organisation as it transitions to the new Cumberland Unitary Authority, planned for April 2023. We find this leaves the Council in a financially challenging position, especially in the context of the numerous financial budgeting and reporting governance weaknesses, highlighted by both us as the appointed auditor and the DLUHC review issued on 8 December 2021.

One of the significant challenges presented in the DLUHC review was the affordability of a very ambitious capital programme. We acknowledge that, the Council has not committed significant borrowing as yet but it has set a 3 year capital programme in 2022/23, spanning post Local Government Reorganisation (LGR) era. Given the precarious revenue position the Council is currently in, it has to be extremely careful not to overcommit on its capital ambitions.

Background to the recommendations

Capacity and capability to implement significant external recommendations

We have significant concerns around the Council's capacity and capability to deal with what is a large volume of significant recommendations raised through a combination of the DLUHC review, CIPFA's reviews of Internal Audit and Audit Committee effectiveness as generated by our previous Statutory Recommendations and several other external audit key recommendations. Despite pending LGR and the demise of the existing Council, significant and fundamental financial and governance arrangement improvements are needed as part of Copeland Borough Council's legacy contribution to the new Cumberland Unitary Authority.

DLUHC review

The DLUHC review has identified a significant number of key and other recommendations, which the Council accepted and agreed to at an exceptional general meeting held on 13th January 2022. Some of the key recommendations include:

- Refresh the Medium Term Financial Strategy (MTFS) to balance the budget to the year 2022/23 and 2023/24 when local Government reform is expected to take place. More explicit sensitivity analysis to aid management and member's understanding of the impact changes to assumptions could have on future budgets. MTFS needs to fully recognise the costs of LGR and the impact on Minimum revenue provision to finance capital expenditure
- Refresh capital programme to assess on-going achievability of schemes and as business cases are put forward robustly assess affordability. Capital programme be refreshed and aligned with a revised MTFS to capture affordability of these programmes
- Robust arrangements must be put in place to address the backlog of production of the statement of accounts
- Segregation of the Director of Corporate Finance dual role of responsibility for both internal audit and the finance function.

Note some of these recommendations do overlap with those previously raised by us as the Council's external appointed auditor.

Background to the recommendations

Capacity and capability to implement significant external recommendations (continued)

CIPFA reviews on Internal Audit and Audit Committee effectiveness

In response to our February 2021 Statutory Recommendations, the Council commissioned CIPFA to undertake two independent reviews of its Internal Audit Service and Audit and Governance Committee effectiveness. CIPFA reported in August 2021 and found the Internal Audit Service only partially conforms to the requirements of the Public Sector Internal Audit Standards and the CIPFA Local Government Application Note. The review identified 16 recommended improvements in addition to the s151 Officer not having responsibility for both Finance and Internal Audit, including the high priority need for:

- Internal Audit staff training development programme as none are fully AAT qualified or have the IIA Certified Internal Auditor qualification
- consistent supervisory evidencing of review of Internal Audit team's work
- enhanced and documented Internal Audit's own quality assessment and improvement programme
- expanded information in the audit plans to provide more detail to the Audit Committee, such as a brief outline of the scope of the proposed audit, and the priority of each audit, linked to Council's priorities and the strategic risk register.

The Audit Committee effectiveness review was reported in September 2021. The review concluded that "the foundations for an effective Audit Committee are in place at the Council, but there is a need and scope to enhance the skills and knowledge of the members to improve the Audit Committees effectiveness". 11 recommendations were made. We understand that the Council's action plan in response to the recommendations is due to be taken to the next meeting of the Audit Committee in 2022. The review identifies limited challenge by members on the agenda items being presented to the Audit Committee and raises a number of recommendations to provide training and resources to Audit Committee members to develop their skills and knowledge. This is consistent with our observations of the Audit Committee. The review also identified further weaknesses including the Committee does not undertake an annual self-assessment of committee effectiveness nor prepares an annual report to Full Council

A robust Internal Audit service and Audit Committee are really important third lines of defence within the Council's control environment and these suggested improvements need to be implemented with immediate effect to protect the Council.

Background to the recommendations

Capacity and capability to implement significant external recommendations (continued)

Grant Thornton 2018/19 audit significant recommendations

Our audit findings for 2018/19 overlap significantly with the findings of both the DLUHC and CIPFA reviews outlined above. However, our audit in 2018/19 and follow up to our 2017/18 findings has identified a number of other key Value for Money related recommendations that are still extant for the Council to respond to. These include:

- Review the Council's assurance framework to identify key sources of assurance, identify and reduce gaps and eliminate duplication by reviewing the three lines of assurance of management assurance, oversight of management activity and independent assurance.
- Introduce regular reviews of key governance policies and procedures including critical areas such as the Constitution, which has had recent delays to agreed revisions, register of interests, Whistle blowing and Confidential reporting policies.
- Council's Fraud Prevention and Anti-Corruption Strategy was approved at the meeting of the April 2018 Audit and Governance Committee, however no further related papers have been considered by the Committee since.
- Ensure the Strategic Risk Register is regularly taken to the Audit Committee, last done in November 2020, and taken through SLT, which management say it is but there is no clear audit trail of this process in place.
- Introduce a formal process to monitor Overview and Scrutiny Committee activity and related recommendations to improve the Council's governance and scrutiny arrangements, which is critically important given their pivotal role in monitoring appropriate action on the various external high priority and significant recommended improvements the Council currently faces.
- Introduce annual self-assessment of effectiveness reviews of key committees.
- Ensure any future capital directions are adequately tracked, reported and monitored to demonstrate value for money is being secured given the clear failings with the management of the £1.8m capital direction used to cover cyber attack costs in 2018 and 2019.

An independent IT Health Check (ITHC) was conducted in November 2017, whilst the cyber incident was still live for the Council with a lengthy recovery period, and a further ITHC in May 2019. The latter report identified 99 findings at which point they stopped their analysis. 36 of the 99 recommendations were graded critical or high. This confirms that, the Council had not sufficiently strengthened its network during 2017/18 or 2018/19 to protect itself against malicious cyber activity. We acknowledge that the Council had to focus originally on service user business critical areas.

Background to the recommendations

Capacity and capability to implement significant external recommendations (continued)

Grant Thornton 2018/19 audit significant recommendations (continued)

The Council commissioned external contractors to assist with the recovery from the cyber-attack. However, these contractors were largely general IT staff and not third-party cyber incident recovery specialists. The Council then rebuilt its critical IT systems on end-of-life equipment.

Given the severity and pervasive nature of the findings raised by the ITHC in May 2019 and the significant reduction in the risk score for IT resilience in the SRR from 20 to 9 from quarter 1 to 4 in 2018/19, it is evident that the Council, both management and those charged with governance, did not have sufficient means, understanding, oversight, or awareness of the severity of the risks it faced because of the weaknesses present in its IT control environment during 2018/19.

We do acknowledge that, the Council has made progress in rebuilding and strengthening its IT environment since the appointment of the Head of ICT in early 2019. Key milestones such as the achievement of the Cyber Essentials Plus certification in April 2020, and subsequent recertification in August 2021 and the implementation of a brand new network and ERP system in 2021, show that the direction of travel on ICT control environment is positive. The Council continues to coach other councils on cyber awareness.

Summary of the recommendations

We have concluded that it is appropriate for us to use our powers to make written recommendations under section 24 of the Local Audit and Accountability Act 2014, as the Council has to:

- ensure that the financial plans for 2022/23 and beyond contain sufficient consideration of financial pressures to maintain the Council's general fund reserves at the required level of £2m, with sensitivity analysis that adequately covers the Council's LGR financial commitments, interest rate increases and Minimum Revenue Provision costs arising from increased borrowings
- address a substantial number of significant governance related concerns raised by us as the external appointed auditor, DLUHC and CIPFA.

The position described represents a failure of governance with:

- serious short term financial sustainability concerns with an unaudited March 2021 position coupled with no robust medium term financial plan in place to allow the Council to make fully informed decisions on securing a balanced budget position
- risks of overcommitting on the Council's capital ambitions especially in the context of LGR and any legacy decisions, which may have significant consequences for the financial sustainability of the new Cumberland Unitary Authority
- capacity and capability challenges to implement a substantial number of significant external governance related recommendations
- immediate action needed to strengthen the Council's Internal Audit Service and Audit and Governance Committee.

Page 11 to 14 set out our 5 statutory recommendations. Schedule 7 of the Local Audit and Accountability Act 2014 requires the Council to consider these recommendations in a public meeting and decide whether the recommendations are to be accepted and what actions are to be taken in response. To uphold transparency and good governance it is expected your external appointed auditor will be present at the public meeting to present this report and field any questions that may arise.

Recommendations made under section 24 schedule 7 of the Local Audit and Accountability Act 2014

Area	Recommendation	Management response/ Responsible Officer / Due date
Improving financial governance	1. Continue to put in place robust arrangements for the production of late 2019/20, 2020/21 and 2021/2022 financial statements, which meet statutory requirements and international financial reporting standards.	<p>This recommendation has been accepted as management reported to Council on 13th January; arrangements continued to be refined for the audit of the outstanding financial statements as the audits progress. The 2018/19 audit is nearing completion and draft 2019/20 accounts ready for audit. A plan for bringing the audits up to date has been discussed with Grant Thornton and will be further discussed with the Audit Committee at its next meeting. The Council has also, under advice from the auditors recommissioned its valuations from 18/19 onwards.</p> <p>Mayor / Director of Resources June 2022 and ongoing</p>

Recommendations made under section 24 schedule 7 of the Local Audit and Accountability Act 2014

Area	Recommendation	Management response/ Responsible Officer / Due date
Improving financial governance	2. Ensure the critical financial governance weaknesses identified by DLUHC review and Grant Thornton on medium term financial planning, budgeting assumptions and sensitivity analysis are implemented with immediate effect to enable the Council to set realistic financial revenue plans for the short term.	These recommendations have been accepted as management reported to Council on 13th January; the recommendations relating to medium term financial planning, budgeting assumptions and sensitivity analysis have been included in the Mayor's 2022/23 budget that was approved in February. Director of Resources / Mayor February 2022

Recommendations made under section 24 schedule 7 of the Local Audit and Accountability Act 2014

Area	Recommendation	Management response/ Responsible Officer / Due date
Improving financial governance	3. Protect against overcommitment on the Council's capital ambitions especially in the context of dependency on capital directions and the transition to LGR.	<p>This recommendation has been accepted as management reported to Council on 13th January; We are pleased that the CIPFA report recognised that LGR should hinder investment in services, the Council's Capital Strategy presented to Council in February identified affordability as a key pillar in its decision making.</p> <p>Director of Financial Resources / Mayor March 2022</p>

Recommendations made under section 24 schedule 7 of the Local Audit and Accountability Act 2014

Area	Recommendation	Management response/ Responsible Officer / Due date
Improving governance	4. Develop a composite and robust action plan from all the Grant Thornton, DLUHC and CIPFA external reviews, ensuring there is appropriate capacity and capability in place to implement the required governance improvements with adequate and regular oversight and challenge from Full Council, Overview and Scrutiny and the Audit Committee.	<p>This recommendation is accepted, a composite action plan and will be discussed with the Audit Committee to ensure there is appropriate capacity and capability in place to implement the required governance improvements.</p> <p>Mayor/ Chief Executive/ All Directors/ Council June 2022 and ongoing in terms of its delivery</p>
Improving governance	5. Immediate action is required to strengthen the Council's internal governance arrangements, especially its Internal Audit service and Audit and Governance Committee effectiveness.	<p>This recommendation is accepted. Following previous recommendations by the Auditor the Council has undertaken a review of Internal Audit, and is now implementing those actions, and a review of the Effectiveness of the Audit Committee which it is discussing at its next Audit Committee.</p> <p>Mayor/ Chief Executive June 2022</p>

