



NOTTINGHAM CITY HOMES

REVIEW OF THE SERVICE CHARGE ARRANGEMENTS

Report issued:	June 2009
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Audit Plan:	2009/10
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The matters raised in this report are only those that came to the attention of the auditor during the course of the internal audit review and are not necessarily a comprehensive statement of all the weaknesses that exist or all the improvements that might be made. This report has been prepared solely for management's use and must not be recited or referred to in whole or in part to third parties without our prior written consent. No responsibility to any third party is accepted as the report has not been prepared, and is not intended, for any other purpose. TIAA neither owes nor accepts any duty of care to any other party who may receive this report and specifically disclaims any liability for loss, damage or expense of whatsoever nature, which is caused by their reliance on our report.

Business Assurance

Review of the Service Charge Arrangements

- EXECUTIVE SUMMARY -

INTRODUCTION

1. We have reviewed the Service Charge arrangements at Nottingham City Homes. The review was carried out in April 2009 as part of the planned internal audit work for 2009/10.

SUMMARY

2. Two Key Risk Control Objectives were identified and tested and based on the findings from this work an overall evaluation of the overall adequacy of the internal controls was established. (figure 1 below).

Figure 1 - Evaluations of the Effectiveness of the Internal Controls

Evaluation
Limited Assurance

KEY FINDINGS

3. The key control and operational practice findings that need to be addressed in order to strengthen the control environment are set out in the Management and Operational Effectiveness Action Plans. The prioritisation of the findings are summarised below (figure 2):

Figure 2 - Summary of Priorities of Findings

Urgent	Priority	Routine	Operational
1	2	1	1

MANAGEMENT RESPONSES

4. Recommendations for improvements should be assessed by the Company for their full impact before they are implemented.

RELEASE OF REPORT

5. The table below sets out the history of this report.

Date draft report issued:	7 th May 2009
Date management responses recd:	16 th June 2009
Date final report issued:	17 th June 2009



MANAGEMENT ACTION PLAN
PRIORITY 1, 2 AND 3 RECOMMENDATIONS

Risk	Finding	Recommendation	Priority	Management Comments	Implementation Timetable	Responsible Officer
Costs of communal services are not recovered.	Six leasehold properties were found which had been sold that were not included on the leasehold database and subsequently had not been charged any service charges for 2007/08.	A full reconciliation be performed in conjunction with the Legal Services department at Nottingham City Council to ensure that all flats sold have been included on the leasehold database.	1	<i>A list of properties from the Leaseholder and Rechargeable Repairs Team (LRRT) master spreadsheet will be sent to Legal Services for reconciliation with their records to ensure that we have an accurate stock figure. Following the implementation of the service charge module from September 2009 it is proposed that the LRRT will take control of the ending of tenancies.</i>	June 2009	Samantha Else – Leasehold Manager
Failure to direct the process through approved policy & procedures.	No contingency plans are in place to mitigate against the unavailability of the consultant who conducts the file merging process to perform the service charge calculations.	Contingency plans be developed to provide cover for the consultant.	2	<i>Following the implementation of the service charge module from September 2009 the consultant will no longer be required as part of the annual process.</i>	September 2009	Samantha Else – Leasehold Manager (supported by Simon Temporal – Leasehold Officer)

PRIORITY GRADINGS

1	URGENT	fundamental control issue on which action should be taken immediately.
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2	IMPORTANT	control issue on which action should be taken at the earliest opportunity.
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3	ROUTINE	control issue on which action should be taken.
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Risk	Finding	Recommendation	Priority	Management Comments	Implementation Timetable	Responsible Officer
The costs of services provided are not recovered through the service charges.	The lease agreement includes the amount for lift replacement but does not state the principle for establishing a sinking fund.	Lease agreements be amended to make reference to the principle of a sinking fund. would consideration be given by TIAA to change this recommendation to where possible amend Lease agreements to make reference to the principle of a sinking fund	2	<i>NCH will approach Legal Services at NCC regarding this proposal which is a decision which will need to be made by NCC if it is practical to implement the change. If proposal is adopted, full consultation with leaseholders will be required and carried out.</i>	<i>December 2009</i>	<i>Samantha Else – Leasehold Manager</i>
Failure to direct the process through approved policy & procedures.	Service charge collection rates are not reported to the Board.	Collection data and other service performance statistics be reported to Committee or Board on a regular basis.	3	<i>The debt is currently managed by NCC. A proposal has been agreed by NCC that NCH will manage the debt 'in house' once the Northgate Leaseholder Service Charge Module goes live. Board and Committee reporting will be carried out on a regular basis in line with the company's reporting timetable.</i>	<i>October 2009</i>	<i>Samantha Else – Leasehold Manager</i>

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OPERATIONAL EFFECTIVENESS MATTERS

Item	Management Comments
Consideration be given to changing the service charge debtor ageing categories to show which charging year the debt relates to.	<i>Consideration has been given on this item.</i>

ADVISORY NOTE

Operational Effectiveness Matters need to be considered as part of management review of procedures, rather than on a one-by-one basis

- DETAILED REPORT -

SCOPE AND LIMITATIONS OF THE REVIEW

6. The review considered the arrangements for calculating the service charges for properties managed by the Company; the collection of service charges and recovery of arrears. The review also considers the arrangements for monitoring that the service charges fully recover the costs for which they are being levied.
7. The limitations and the responsibilities of management in regard to this review are set out in the Annual Plan.

ASSESSMENTS OF THE KEY RISK CONTROL OBJECTIVES

8. This review identified and tested the controls that are being operated by the Company and an assessment of the combined effectiveness of the controls in mitigating the key control risks is provided. The assessments are:

Substantial Assurance	robust series of internal controls in place which should ensure continuous and effective achievement of the control objective.
Reasonable Assurance	reasonable number of internal controls in place, however may not be operated all the time.
Limited Assurance	the controls in place are not sufficient to ensure the continuous and effective achievement of the control objective.
No Assurance	fundamental breakdown or absence of core internal controls.

MATERIALITY

9. There are 1050 leasehold properties on which the Company can levy service charges. The total amount of service charge debit raised for 2008/09 was £133,710 to leaseholders and £68,260 to tenants (excluding gas maintenance charge).

AUDIT FINDINGS

10. Risk	Failure to direct the process through approved policy & procedures.
Risk Control Objective	Arrangements in place provide for compliance with established policies, procedures, laws and regulations.
Evaluation	<u>Reasonable Assurance</u>

11. The following matters were identified in reviewing the Key Risk Control Objective:
 - 11.1 Service charges for Nottingham City Homes tenants are charged and collected along with the rent amounts through the Company's housing management system. The process of calculating the amount of Service Charge to be levied to leaseholders is managed by the Leaseholder and Rechargeable Repairs Team and is invoiced by Nottingham City Council.
 - 11.2 The Leaseholder and Rechargeable Repair Manager, who is supported by a Leasehold Officer, Leasehold Assistant and a Rechargeable Repairs Officer, has

overall responsibility for ensuring the Company has adequate Service Charge arrangements in place. The Leaseholder and Rechargeable Repair Manager has been in the post for the last seven months.

- 11.3 The actual costs incurred for the year 1st April to 31st March are detailed on the invoice along with an estimate of the costs for the following year. This is then adjusted for actual costs in the following year. These are invoiced in September. Any service charge amounts under £25 are not automatically invoiced to the leaseholder but would be rolled forward into the following year. Nottingham City Council performs the collection of leaseholder service charges and collection rates are provided to the Head of Rents. This information is not reported to Committee or Board.

Recommendation: Collection data and other service performance statistics be reported to Committee or Board on a regular basis.

- 11.4 Aged analysis of debts is provided by Nottingham City Council showing the amounts that are current (under 28 days old), 29-90 days and over 91 days. As all invoices for service charges are produced in September, at the time of the audit review (April) all outstanding amounts were in the 91+ days category.

Operation effectiveness matter: Consider changing the debt ageing categories to show which charging year the debt relates to.

- 11.5 The actual costs relating to blocks/schemes are provided by the Service Heads to the Leasehold Officer who splits these by property. A consultant is used on a yearly basis to perform a file merge in order to send the information to Nottingham City Council for the invoices to be produced. No contingency plans are in place to mitigate against the unavailability of the consultant.

Recommendation: Contingency plans be developed to provide cover for the consultant.

- 11.6 Service charges are referred to in the Leasehold Management Policy dated November 2006. This is due to be reviewed and updated in the current year.
- 11.7 There are documented ISO flowchart procedures in place dated March 2008.
- 11.8 There is a dedicated Leaseholders section on the Company's website detailing what may be included in the charges and how they are calculated.
- 11.9 All complaints come through the Customer Relations Team. Analysis by the Customer Relations Manager showed that there were three complaints relating to the Leaseholder Team in the previous 12 months. All relating to repairs to leasehold properties rather than the service charges levied.

12. Risk	Losses arising from unauthorised action by staff.
Risk Control Objective	Arrangements in place provide for safeguarding the organisation's assets and interests from avoidable losses.
Evaluation	<u>Limited Assurance</u>

13. The following matters were identified in reviewing the Key Risk Control Objective:

Risk: Costs of communal services are not recovered.

- 13.1 Nottingham City Council reports the Right To Buy applications to the Leasehold Assistant. The items to which service charges will be levied are prepared together with non-itemised costs based on repair/renewal estimates and notified to the

prospective leaseholder prior to completion. The Legal Services department at NCC inform the Leaseholder Team upon completion and the property is added onto the Leaseholder Property spreadsheet.

- 13.2 There have been no new Nottingham City Homes properties brought on charge within the last 18 months.
- 13.3 A list of all flats sold within the previous 20 months was checked against the leasehold database. Six properties were found that had been sold which were not included on the leasehold database and subsequently had not been charged any service charges for 2007/08. These had been sold in August to October 2007 and in March 2008. Discussions with the Leasehold Assistant identified that the leasehold team had not received the information from Legal Services at Nottingham City Council informing of the sale until April 2009.

Recommendation: A full reconciliation be performed in conjunction with the Legal Services department at Nottingham City Council to ensure that all flats sold have been included on the leasehold database.

- 13.4 Service charges are referred to within the tenancy agreement and leases. A section headed "flat expenses" gives details of the amounts which will be payable by the leaseholder after they have bought the property.
- 13.5 The tenancy agreement states, under the responsibilities of the Company to the tenant, that repairs will be made to communal areas to blocks of flats and maisonettes and gives examples of such repairs and maintenance provided.

Risk: The costs of services provided are not recovered through the service charges.

- 13.6 A checklist is used by the leaseholder Team to ensure that all relevant items have been included in the service charge. Plans are drawn up by the Asset management Team on an annual basis of what major works are to be completed for the next year. This is because the funding is provided after the level of the HRA is known. All of the costs of caretakers, wardens, etc that are specific to the block are recovered through the service charge.
- 13.7 A sinking fund is included in service charges where applicable. The anticipated replacement value is increased by an inflationary figure annually. The lease agreement includes the amount for lift replacement but does not state the principle for establishing a sinking fund.

Recommendation: Lease agreements be amended to make reference to the principle of a sinking fund.

- 13.8 The CORE regional strategic summary for 2007/08 on Local Authority Lettings of General Needs property in the East Midlands Government Office Region shows that the average service charge for the East Midlands region was £5 against a national average of £8. The average for Nottingham City Homes properties is £5 including £1 for gas servicing.
- 13.9 All lift replacement periods are between 23 and 26 years. Lifts are the only major works where a sinking fund is provided for. A spreadsheet for the lift replacement costs was obtained. The service charge element reflects the costs of the planned future works.

Risk: Income is lost through failure to ensure that service charges are collected in a timely manner.

- 13.10 NCC manages all leaseholder arrears. Nottingham City Homes tenants service charges are included in the rental amount. The central rents team manages the arrears process. Details of service charges for tenants are included in rent statements, which are sent out quarterly.



- 13.11 All decisions for write offs of leaseholders service charges are taken by and authorised by Nottingham City Council. Write offs of tenant service charges are in accordance with the Financial Regulations for rent write offs.
