

Audit and Governance Committee

Report of Assurance Manager

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To: Audit and Governance Committee

DATE: 20 March 2017

Internal audit activity report quarter four 2016/2017

Recommendation

That members note the content of the report

Purpose of Report

1. The purpose of this report is to summarise the outcomes of recent internal audit activity at both councils for the committee to consider. The committee is asked to review the report and the main issues arising, and seek assurance that action will be/has been taken where necessary.
2. The contact officer for this report is Adrianna Partridge, Assurance Manager for South Oxfordshire District Council (SODC) and Vale of White Horse District Council (VWHDC), telephone 01235 422485.

Strategic Objectives

3. Running an efficient council.

Background

4. Internal audit is an independent assurance function that primarily provides an objective opinion on the degree to which the internal control environment supports and promotes the achievements of the council's objectives. It assists the councils by evaluating the adequacy of governance, risk management, controls and use of resources through its planned audit work, and recommending improvements where necessary. After each audit assignment, internal audit has a duty to report to management its findings on the control environment and risk exposure, and recommend changes for improvements where applicable. Managers are responsible for considering audit reports and taking the appropriate action to address control weaknesses.

5. Assurance ratings given by internal audit indicate the following:

Full assurance: There is a good system of internal control designed to meet the system objectives and the controls are being consistently applied.

Substantial assurance: There is a sound system of internal control designed to meet the system objectives and the controls are being applied.

Satisfactory assurance: There is basically a sound system of internal control although there are some minor weaknesses and/or there is evidence that the level of non-compliance may put some minor system objectives at risk.

Limited assurance: There are some weaknesses in the adequacy of the internal control system which put the system objectives at risk and/or the level of non-compliance puts some of the system objectives at risk.

Nil assurance: Control is weak leaving the system open to significant error or abuse and/or there is significant non-compliance with basic controls.

6. Each recommendation is given one of the following risk ratings:

High Risk: Fundamental control weakness for senior management action

Medium Risk: Other control weakness for local management action

Low Risk: Recommended best practice to improve overall control

2016/2017 Audit Reports

7. Since the last audit and governance committee meeting, the following audits and follow up reviews have been completed:

Completed Audits

Full Assurance: 0

Substantial Assurance: 1

Satisfactory Assurance: 0

Limited Assurance: 2

Nil Assurance: 0

	Assurance Rating	No. of Recs	High Risk Recs	No. Agreed	Medium Risk Recs	No. Agreed	Low Risk Recs	No. Agreed
Joint								
Creditor Payments 2016/2017	Limited	10	3	3	5	5	2	2
CSP Procurement 2016/2017	Substantial	2	0	0	1	1	1	1
Treasury Management 2016/2017	Limited	5	2	2	3	3	0	0
SODC								
None								
VWHDC								
None								

Follow Up Reviews

	Initial Assurance Given	No. of Recs	Implemented	Partly Implemented	Not Implemented	Ongoing	No longer applicable
Joint							
Gifts and Hospitality 1617	Substantial	1	1	0	0	0	0
ICT 1516	Satisfactory	8	3	0	2	1	2
Risk Management 1617	Limited	14	0	2	3	9	0
Facilities Management 1617	Limited	3	1	0	0	0	2
HR Management 1516	Satisfactory	5	2	0	3	0	0
Safeguarding 1617	Substantial	3	1	0	2	0	0
Insurance 1516	Limited	18	11	5	0	1	1
SODC							
None							
VWHDC							
None							

8. **Appendix 1** of this report sets out the key points and findings relating to the completed audits which have received limited or nil assurance, and satisfactory or full assurance reports which members have asked to be presented to committee

9. Members of the committee are asked to seek assurance from the internal audit reports and/or respective managers that the agreed actions have been or will be undertaken where necessary.
10. A copy of each report has been sent to the appropriate service manager, the strategic management board, the section 151 officer and the relevant member portfolio holder. In addition to the above arrangements, reports are now published on the councils' intranet.
11. Internal audit continues to carry out a six month follow up on all non-financial and non-key financial audits to establish the implementation status of agreed recommendations. All key financial system recommendations are followed up as part of the annual assurance cycle.

Overdue Recommendations

12. **Appendix 2** of this report summarises all overdue recommendations within each service area. The report has been circulated to the relevant service manager, heads of service, the strategic management board and the portfolio holder.

Financial Implications

13. There are no financial implications attached to this report.

Legal Implications

14. None.

Risks

15. Identification of risk is an integral part of all audits.

ADRIANNA PARTRIDGE
ASSURANCE MANAGER

1. Creditor Payments 2016/2017

1. INTRODUCTION

- 1.1 This report details the internal audit review of procedures, controls and the management of risk in relation to creditor payments. The audit has a priority score of 22. The draft report was issued on 2 December 2016 and the final report was issued on 3 March 2017.
- 1.2 The following areas have been covered during the course of this review to provide assurance that:
- appropriate policies and procedures are in place which are adhered to with roles, responsibilities and authorisers for creditors clearly documented;
 - invoices are promptly processed and supported by appropriate documentation;
 - manual, direct debit and BACS transfer payments are strictly controlled, appropriately authorised and paid correctly;
 - adequate controls are in place to prevent duplicate payments;
 - refunds are appropriately authorised and actioned;
 - VAT is being appropriately allocated for creditor payments.

2. BACKGROUND

- 2.1 Creditor payments or accounts payable are payments by the councils to third party suppliers for goods or services purchased. Capita exchequer services provide the system administration for creditor payments through the financial management system Agresso.
- 2.2 SODC
At the time of the audit review (31 October 2016), there were 4,230 invoices received since April 2016, which totalled £19,708,349.54. Of these, 2,111 were purchase order invoices totalling £10,033,496.42 and 2,119 were non-purchase order invoices totalling £9,674,853.12.
- 2.3 VWHDC
At the time of the audit review (31 October 2016), there were 3,988 invoices received since April 2016, which totalled £17,589,842.98. Of these, 1,419 were purchase order invoices totalling £9,996,360.55 and 2,569 were non-purchase order invoices totalling £7,593,842.98.

3. PREVIOUS AUDIT REPORTS

- 3.1 SODC
Creditor payments was last subject to an internal audit review in February 2016 and six recommendations were raised. All six recommendations were agreed. A limited assurance opinion was issued.
- 3.2 Of the six recommendations, one has been implemented and five recommendations are no longer applicable and have been superseded.

No joint recommendations have been restated as part of this review.

3.3 VWHDC

Creditor payments was last subject to an internal audit review in February 2016 and five recommendations were raised. All five recommendations were agreed. A limited assurance opinion was issued.

3.4 All five recommendations are no longer applicable and have been superseded. No joint recommendations have been restated as part of this review.

4. 2016/2017 AUDIT ASSURANCE

4.1 **Limited assurance:** There are some weaknesses in the adequacy of the internal control system which put the system objectives at risk and/or the level of non-compliance puts some of the system objectives at risk.

4.2 Ten joint recommendations have been raised in this review. Three high risk, five medium risk and two low risk.

5. MAIN FINDINGS

5.1 Policies and procedures

5.1.1 The councils have in place financial procedure rules, which are part of the Constitution, which sets out how the councils manage their finances, including creditor payments. Review confirmed that the constitutions are up-to-date and were last updated in August 2016 and available to the officers via the councils' website. It is noted that the updates to the Constitution were approved at both Council meetings in July 2016.

5.1.2 Procedures are in place for creditor payments, which clearly defines the roles and responsibilities of both council officers and Capita exchequer services staff. The procedures are available to relevant officers via the intranet. It is noted that Capita exchequer services also have procedures in place for the process they undertake as part of creditor payments.

5.1.3 Area assurance: Full
No recommendations have been made as a result of our work in this area.

5.2 Invoice process

5.2.1 Capita's Darlington team receive the councils' invoices and Capita exchequer services process them for payment. Invoices are receipted, scanned and checked, prior to payment being made to the supplier. A target of paying supplier invoices within 30 days is 99%, and usage of purchase orders is encouraged to speed up the payment process. A sample of 40 (20 SODC & 20 VWHDC) invoices were selected and review found that:-

- eight (four SODC & four VWHDC) were non-purchase order invoice and were on the agreed exemption list.
- six (two SODC & four VWHDC) were paid after 30 days from invoice

date, of which:-

- Two SODC invoices were sent to the council offices in Milton Park, instead of Darlington;
 - One VWHDC invoice was not received and a copy invoice was requested;
 - Two VWHDC invoices had delays in being approved; and
 - One invoice was delayed in being registered onto the Agresso system, but was paid promptly as soon as it was registered.
- all invoices were linked to the suppliers' account and transaction, and an audit trail was available in a form of a flowchart and logbook.

5.2.2 Daily checks are undertaken of any outstanding invoices and weekly reports are sent to the councils on invoices that still require authorisation. Invoices parked are also sent on to the councils on a weekly basis to establish if the invoices can be paid. Review of both outstanding and parked invoices' reports confirmed that they are reviewed and managed appropriately.

5.2.3 Capita's performance against targets are monitored on a monthly basis as part of the five councils partnership finance and accountancy monthly review meetings. It is noted that the monthly meetings are between the finance and procurement client team and Capita's accountancy and finance team. Review of the latest (November 2016) performance stats confirmed that exchequer services performance is meeting target; however, a comparison review of the performance information currently presented and reviewed compared to the previous performance information reviewed found that the client team previously had more information to monitor and manage the service appropriately.

5.2.4 Area assurance: Satisfactory
Two recommendations have been made as a result of our work in this area (Recs 1 and 2).

5.3 **Payments**

5.3.1 Manual payments are made for urgent payments separate from the weekly payment runs. These are requested through an urgent payment voucher and dealt with the same way as the normal payment requests within the Agresso system. Review of 21 (10 SODC & 11 VWHDC) urgent payments made since 1 April 2016 to 31 October 2016 confirmed that the payments were appropriate. However, it is noted that one SODC urgent payment was made against an invoice that was addressed to both SODC and VWHDC, which should have been rejected as invoices can only be addressed to one council.

5.3.2 BACS is the default payment with cheque payments used as an exception, while there are no suppliers set up for payment by direct debit. It is noted that the procedure notes - accounts payable (non PO) states that bank details must be obtained on headed company notepaper or a signed letter for individuals, so that the supplier can be set up to be paid by BACS. However, since April 2016 the process for setting up suppliers, including obtaining bank details, changed whereby Capita exchequer services only accept changes to suppliers if a supplier form is

completed, and the procedures have not been updated to reflect the changes. Weekly payment runs for both BACS and cheque payments are sent to the councils for authorisation, and review confirmed email authorisation prior to payment being processed. Review of BACS payment rejections established that rejections are not managed appropriately, as the supplier master file is not updated if a rejection is due to the bank account being closed.

5.3.3 Area assurance: Limited
Three recommendations have been made as a result of our work in this area (Recs 3, 4 and 5).

5.4 Duplicate payments

5.4.1 Within the Agresso system is a built in control preventing invoices from being registered if any invoices that are scanned has the same supplier name and invoice number. The invoice is sent to Capita exchequer service team's workflow to review. An Agresso report of invoices paid since 1 April 2016 to 31 October 2016 was received and review established that there were 13 (three SODC and ten VWHDC) duplicate invoices. Review of the 13 duplicate invoices found that:-

- Three (SODC) invoices were registered and paid, however one was identified as a duplicate payment after payment and a refund was requested;
- Ten (VWHDC) invoices were registered, but were identified as duplicate payments and journals were done to reverse the transaction.
- Eight (three SODC & five VWHDC) invoices were processed to both the correct supplier and another supplier;
- Six (two SODC & four VWHDC) invoices had a PO raised, but matched to both the correct supplier and somehow another supplier.

It is noted that part of the duplicate invoice review, a control weakness was established on the grants payment system as there is no segregation of duties between the officer creating the grants payment and the officer approving the payment.

5.4.2 The Agresso system has a built in control in place to mitigate the risk of duplicate payment being made as it will only allow one payment to be made against an invoice once. It is noted that there still is potential for duplicate payments if:-

- duplicate suppliers are created;
- the sundry supplier account is used when the supplier already has an existing account.

An Agresso listing of all open & closed supplier accounts was obtained and review established that there are 3,455 (1,914 SODC and 1,541 VWHDC) open supplier accounts, of which 177 (93 SODC & 84 VWHDC) were possible duplicate accounts. Review of 40 (20 SODC & 20 VWHDC) suppliers found 26 (14 SODC & 12 VWHDC) suppliers to have duplicate accounts set up on the Agresso system.

5.4.3 Sundry supplier accounts are used as one-off payments to suppliers that have not been set up onto the Agresso system. Review of the sundry supplier account report in 2016/2017 to 31 October 2016 established that 327 (174 SODC and 153 VWHDC) transactions totalling £110,937.13

(£49,753.63 SODC and £61,183.50 VWHDC) were paid through the account. Review of a sample 20 (10 SODC and 10 VWHDC) sundry account transactions found that:-

- Six (three SODC & three VWHDC) suppliers had an existing supplier account on the Agresso system;
- One (SODC) supplier had multiple payments made through the sundry account.

It is noted that the review of the sundry supplier accounts have stopped since the new five councils' partnership started on 1 August 2016.

5.4.4 Area assurance: Limited

Five recommendations have been made as a result of our work in this area (Recs 6, 7, 8, 9 and 10).

5.5 Credit notes and refunds

5.5.1 Procedures are in place to cover the management of refunds in the form of credit notes received being offset against invoices. Credits since 1 April 2016 to 31 October 2016 was obtained and review of 40 (20 SODC & 20 VWHDC) credit notes confirmed that:-

- credit notes are offset against the invoice;
- segregation of duties exist between the officer raising and approving the credit note;
- credit notes were managed and approved appropriately;
- credit notes were linked to the suppliers' account and transaction, and an audit trail was available in a form of a flowchart and logbook.

5.5.2 On a monthly basis as part of SLA performance, Capita exchequer services sends the councils a report of supplier accounts with a debit balance. From review of the balances as at the end of September 2016, there are 62 (33 SODC & 29 VWHDC) suppliers, totalling £86,525.95 (£33,085.15 SODC & £53,440.80 VWHDC) that owed to the council. It is noted that an invoice is not issued to the supplier to recoup the debit balance, but is offset against future payments that become due.

5.5.3 Area assurance: Full

No recommendations have been made as a result of our work in this area.

5.6 VAT

5.6.1 The VAT part of invoices, which are received from suppliers, are coded to B0901 X002 on the Agresso system. Accountancy have a nominated officer in place and both the intranet and the accounts payable procedures advise officers to contact the nominated officer if they have any queries regarding VAT. Review of 40 (20 SODC & 20 VWHDC) invoices confirmed that VAT was appropriately recorded.

5.6.2 Area assurance: Full

No recommendations have been made as a result of our work in this area.

OBSERVATIONS AND RECOMMENDATIONS

INVOICE PROCESS

1. Invoice payments

(Low Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Supplier invoices are processed and paid in a timely manner.</p> <p><u>Findings</u> A sample of 40 (20 SODC & 20 VWHDC) invoices were selected and review found that:-</p> <ul style="list-style-type: none"> • six (two SODC & four VWHDC) were paid after 30 days from invoice date, of which:- <ul style="list-style-type: none"> ○ Two SODC invoices were sent to the council offices in Milton Park, instead of Darlington; ○ One VWHDC invoice was not received and a copy invoice was requested; ○ Two VWHDC invoices had delays in being approved; and ○ One VWHDC invoice was delayed in being registered onto the Agresso system, but was paid promptly as soon as it was registered. <p><u>Risk</u> If suppliers are not paid in a timely manner, there is a risk of late payment charges or reputational damage.</p>	<p>A notification should be sent to service areas to ensure that invoices are paid promptly, which states:-</p> <ul style="list-style-type: none"> • they remind their suppliers to send all invoices to Darlington; and • they review and approve all invoices efficiently. 	<p>Head of Financial Services (Capita)</p>
Management Response		Implementation Date
<p>Recommendation is Agreed There will always be invoices sent to the wrong addresses or paid late, however there does need to be a re-enforcement of the messages to council staff and suppliers regarding the correct processes to follow. This will be picked up as part of the new Financial Management System (Integra) implementation.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		<p>31 March 2017</p>

2. Performance stats

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Performance measures are in place and submitted to the councils for appropriate monitoring of the service</p>	<p>Exchequer services should send the finance & procurement client team the SLA performance stats, so that the client team can monitor</p>	<p>Finance Exchequer Manager</p>

<p>provided.</p> <p><u>Findings</u> Comparison review of the current performance information reviewed, since the new five councils partnership (1 August 2016) compared to the previous performance information reviewed found that the revenues and benefits client team previously had more information for the client team to monitor and manage appropriately.</p> <p><u>Risk</u> If the councils are not receiving the fullest information to monitor creditor performance, there is a risk that the councils not being aware of any inefficiencies in the service provided.</p>	<p>performance of the service provided effectively.</p>	
<p>Management Response</p>		<p>Implementation Date</p>
<p>Recommendation is Agreed The change in manager meant there was a period of time when the SLA information was not being sent, this has now been rectified and SLA information is being provided as requested.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		<p>Implemented</p>

PAYMENTS

3. Invoice addressed to

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Supplier invoices are addressed to one council and rejected if addressed to both councils.</p> <p><u>Findings</u> One SODC urgent payment was a VAT invoice and review found that the invoice was addressed to both SODC and VWHDC, which Capita should have rejected, but instead was paid by SODC. Invoices cannot be address to both councils, it should be addressed to either SODC or VWHDC.</p> <p><u>Risk</u> If invoices are addressed to both councils, there is risk of the invoice being registered onto both councils' Agresso systems resulting in suppliers being paid twice and the systems' controls not preventing the duplicate payment. Furthermore, there is a</p>	<p>If suppliers submit creditor invoices addressed to both councils, Capita should reject and return the invoices and request that the invoice is addressed to either SODC or VWHDC.</p>	<p>Head of Financial Services (Capita)</p>

risk regarding VAT implications.		
Management Response		Implementation Date
<p>Recommendation is Agreed We have reiterated the message to the Capita mailroom in Darlington that they should reject any invoices not appropriately addressed. There may always be an occasion whereby one slips through and this is why it is important invoices are checked by Council staff prior to approval.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		Implemented

4. Procedure notes

(Low Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Procedure notes are up-to-date and documents the current process undertaken.</p> <p><u>Findings</u> The procedure notes - accounts payable (non PO) state that if the supplier is not already paid by BACS bank details on headed company notepaper for organisations, or a signed letter for individuals is required.</p> <p>However, Capita exchequer services now only accept a change to supplier, i.e. whether it is a change in the name, address or bank details, if a supplier amendment form or new supplier form is completed.</p> <p><u>Risk</u> If procedure notes are not updated or in place, there is a risk of officers unknowingly taking inappropriate actions.</p>	<p>The procedure notes - accounts payable (non PO) should be reviewed and updated to include the process of completing the supplier amendment form/new supplier form prior to requesting Capita exchequer services to change supplier details.</p>	<p>Finance Officer (Client)</p>
Management Response		Implementation Date
<p>Recommendation is Agreed The procedure notes will be updated to reflect the current working practices. There will, however, be wholesale changes to the councils' procedures notes once the new Financial Management System (Integra) has been implemented. The Client team will work with Capita to implement these changes.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		31 March 2017

5. Bank details

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Amendments are made to the supplier bank details after BACS</p>	<p>After Capita exchequer services obtains notification of BACS payment rejections,</p>	<p>Finance Exchequer Manager</p>

<p>payments are rejected.</p> <p><u>Findings</u> Examples of BACS rejects were obtained and it was established that BACS rejections are not suitably managed. A payment initially made to a supplier was rejected on 18/04/2016 with the reason account closed, however two further payments were made to the same supplier and bank account, and again rejected on 24/05/2016 and 31/05/2016 with the same reason.</p> <p><u>Risk</u> If supplier bank details are not updated or deleted after BACS payments are rejected, there is a risk of more payment rejection in the future resulting in late payment charges or reputational damage.</p>	<p>checks should be undertaken on the supplier master files and bank details are either updated or deleted, if deleted payment method changed to cheque payment and the service area is notified.</p>	
<p>Management Response</p>		<p>Implementation Date</p>
<p>Recommendation is Agreed The Accounts Payable team used to leave the bank account details in the system if there was a BACS reject. However, the Finance Exchequer Manager has now changed this process so when we receive a BACS reject, the bank account details are removed from the system so the BACS payment is not attempted again.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		<p>Implemented</p>

DUPLICATE PAYMENTS

6. Duplicate invoices - received twice

(High Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Duplicate invoices are identified prior to them being registered onto the system and payments are not made.</p> <p><u>Findings</u> Review of the 13 duplicate invoices found that:-</p> <ul style="list-style-type: none"> • Three (SODC) invoices were registered and paid, however one was identified as a duplicate payment after payment and a refund was requested. <p><u>Risk</u> If duplicate invoices are not identified prior to registration, there is a risk of duplicate payments being made.</p>	<p>a) A review should be undertaken of duplicate invoices and for any duplicate payments made, a refund should be requested to recoup the payment as soon as possible.</p> <p>b) Regular reviews of duplicate invoices should be undertaken to prevent duplicate payments from occurring.</p>	<p>Finance Exchequer Manager</p>

Management Response	Implementation Date
<p>Recommendation is Agreed</p> <p>A review of the creditors ledger has been undertaken, which has looked at all invoices within the accounts payable ledger and applied a variety of matching criteria to identify the high risk duplicate invoices. Of the duplicate invoices which were subsequently identified, a number of them had not been paid to the suppliers. Of the ones where a duplicate payment had been made, recovery of the monies had commenced.</p> <p>A regular review of the creditor ledger will be carried out to ensure where duplicate payments are made the controls are reviewed and recovery is commenced.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>	30 June 2017

7. Purchase order controls - duplicate processing of invoices

(High Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> The Agresso system prevents purchase orders from manually being linked to another supplier.</p> <p><u>Findings</u> Review of the 13 duplicate invoices found that:-</p> <ul style="list-style-type: none"> • Eight (three SODC & five VWHDC) invoices, only received once but registered twice, were registered to both the correct supplier and another unrelated supplier; • Six (two SODC & four VWHDC) invoices had a PO raised, but were matched to both the correct supplier and somehow another supplier. <p><u>Risk</u> If purchase orders are being manually linked to another supplier, there is a risk that invoices can be registered to numerous suppliers resulting duplicate payments.</p>	A control should be in place on the Agresso system preventing purchase orders that are raised for one supplier being manually linked to another supplier without explanation.	Finance Exchequer Manager
Management Response	Implementation Date	
<p>Recommendation is Agreed</p> <p>The Agresso system has controls in place to flag invoices which are matched against the right purchase order number, but the wrong supplier. We have reiterated to the team the requirement to check these flags with due rigour prior to posting the invoice.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>	Implemented	

8. Duplicate suppliers

(High Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Suppliers only have one open account on the Agresso system, if they have the same address and banking details.</p> <p><u>Findings</u> Review of 40 (20 SODC & 20 VWHDC) suppliers found 26 (14 SODC & 12 VWHDC) suppliers to have duplicate accounts set up on the Agresso system.</p> <p>It is noted that exchequer services undertook a review of duplicate suppliers and submitted the review to the finance and procurement team in September 2016; however, at the time of the audit review (October 2016) duplicate supplier accounts were still open on the Agresso system.</p> <p><u>Risk</u> If suppliers have more than one account on the Agresso system, there is a risk of invoices being registered more than once and payments being against the wrong account.</p>	<p>Regular reviews should be undertaken on the supplier master file to ensure that possible duplicate suppliers are reviewed and if necessary, closed on the Agresso system.</p>	<p>Finance Exchequer Manager</p>
Management Response		Implementation Date
<p>Recommendation is Agreed This task has already been completed by the Exchequer Finance Manager and is with the council for review, once the council confirm they are happy for the accounts payable team to close these accounts, then the process will be completed and all duplicate supplier will be removed.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		<p>31 March 2017</p>

9. Payment vouchers

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> The sundry supplier account is only used for one-off payments to suppliers not set up on the Agresso system.</p> <p><u>Findings</u> The Capita exchequer services team receive payment vouchers asking to be processed against the sundry supplier account, which is intended for one-off supplier payments. However, no checks are undertaken by Capita</p>	<p>Payment vouchers received to make payment through the sundry supplier account should be reviewed and challenged prior to payment.</p>	<p>Finance Exchequer Manager</p>

<p>exchequer services, or the requester and authoriser of the payment voucher to ensure a supplier does not already exist.</p> <p>Review of 20 (ten SODC & ten VWHDC) sundry account transactions found that:-</p> <ul style="list-style-type: none"> • Six (three SODC & three VWHDC) suppliers had an existing supplier account on the Agresso system; • One (SODC) supplier had multiple payments made through the sundry account. <p><u>Risk</u> If payment vouchers received for payment through the sundry supplier account are not reviewed, there is a risk of transactions being processed through different accounts resulting in duplicate payments.</p>		
Management Response		Implementation Date
<p>Recommendation is Agreed</p> <p>The Exchequer Finance Manager has asked the accounts payable team to review the payment vouchers that are received to check if the supplier is already on the system. Going forward past April 2017 the councils will be on Integra and the payment vouchers will be electronic so there will be system checks in place to flag any errors.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		30 April 2017

10. Sundry supplier account usage

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Service areas undertake relevant checks, i.e. establish if an account exists on the Agresso system, prior to using the sundry supplier account to pay a supplier.</p> <p><u>Findings</u> Review of 20 (ten SODC & ten VWHDC) sundry account transactions found that:-</p> <ul style="list-style-type: none"> • Six (three SODC & three VWHDC) suppliers had an existing supplier account on the Agresso system; • One (SODC) supplier had multiple payments made through the sundry account. <p><u>Risk</u> If checks are not undertaken prior to the sundry supplier account</p>	<p>An email should be sent to service areas reminding them to:-</p> <ul style="list-style-type: none"> • check to confirm if the supplier already exists on the Agresso system, and • determine if the supplier will be used again, if so, to complete the new supplier form so they can be set up onto the Agresso system, prior to raising a payment voucher on the sundry suppliers account. 	Finance Exchequer Manager

<p>being used, there is risk of transactions being processed through different accounts resulting to duplicate payments.</p>		
<p>Management Response</p>		<p>Implementation Date</p>
<p>Recommendation is Agreed The accounts payable team have started to look at the payment vouchers in more detail to make sure the supplier is not already set up in the system. Once the councils go live on Integra in April, there will be an electronic version of the payment voucher which will mean the council will have to confirm if the supplier is a one off payee.</p> <p>Management response: Phil Brown, Operations Director - Finance & Accountancy (Capita)</p>		<p>30 April 2017</p>

2. Treasury Management 2016/2017

1. INTRODUCTION

- 1.1 This report details the internal audit review of procedures, controls and the management of risk in relation to treasury management. The audit has a priority score of 18. The draft report was issued on 3 March 2017 and the final report was issued on 8 March 2017.
- 1.2 The following areas have been covered during the course of this review to provide assurance that:
- appropriate policies and procedures are in place for the treasury management function which are harmonised across both councils;
 - there is adequate separation of duties with clearly resourced and defined roles and responsibilities for the treasury management function;
 - investment and borrowing is dealt with appropriately and in accordance with policies and procedures;
 - the council is adhering to the current CIPFA code of practice;
 - treasury management performance is appropriately monitored and reported; and
 - suitable access level controls are in place for the treasury management and banking system.

2. BACKGROUND

- 2.1 Local authorities' treasury management activities are prescribed by statute i.e. the Local Government Act 2003, and the regulations issued under that Act. This is where the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management Code of Practice derives its legal status. CIPFA define treasury management as "*The management of the organisation's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.*".
- 2.2 From 1 August 2016, the accountancy function, including treasury management, transferred to Capita as part of the 5 Councils Partnership contract.
- 2.3 As at 30 September 2016, SODC had an average investment balance of £141,657,000 across treasury, non-treasury and property investments with mid-year investment income of £2,261,000 against a budget of £1,332,000. VWHDC had an average investment balance of £52,914,000 across treasury and property investments with mid-year investment income of £865,000 against a budget of £287,000.

3. PREVIOUS AUDIT REPORTS

- 3.1 Treasury management was last subject to an internal audit review in March 2016 and one joint recommendation was raised. The recommendation was agreed and a substantial assurance opinion was issued.
- 3.2 The recommendation was implemented by delivery of treasury management training to councillors immediately before the 23 January 2017 audit and governance committee.

4. 2016/2017 AUDIT ASSURANCE

- 4.1 **Limited assurance:** There are some weaknesses in the adequacy of the internal control system which put the system objectives at risk and/or the level of non-compliance puts some of the system objectives at risk.
- 4.2 Three joint recommendations have been raised in this review and one specific to SODC and one specific to VWHDC. Two recommendations are high risk and three are medium risk.

5. MAIN FINDINGS

5.1 Policies and procedures

- 5.1.1 Each council's constitution covers treasury management and includes assigning the role of ensuring effective scrutiny of the treasury management strategy to the joint audit and governance committee. It also sets out the section 151 officer's role regarding organising and monitoring the investment of council funds and other treasury management functions.
- 5.1.2 The treasury management activities of each council needs to comply fully with legal statute and the regulations of the council. These include CIPFA's Treasury Management Code of Practice 2001 and subsequent amendments which sets out four minimum requirements for the councils to comply with the code. One of these is to have an annual strategy and plan in advance of the year and another is to consider prudential indicators as part of the strategy. The remaining two relate to reporting which is covered below. SODC has a Treasury Management Strategy and VWHDC has a Treasury Management and Investment Strategy. Although the titles of the documents differ, both include a treasury management strategy, an investment strategy and prudential indicator limits. From review, the strategies were found to be up to date, comprehensive and suitably authorised. However, they would benefit from harmonisation in some areas.
- 5.1.3 Each council has Treasury Management Practice (TMP) guidance documents setting out how treasury management policies and objectives will be achieved and how activities will be managed. Different versions of the TMP's are available and there are differences between the TMP1 stated in the strategy and the most recent version of the TMP1 in the electronic accountancy directory.

5.1.4 The councils had a joint contract for treasury management advice with Capita Asset Services (CAS), a subsidiary of Capita Group Plc, for the period to 15 October 2016. Since then, advice has continued to be provided and Capita's target operating model sets out that operational support for the day to day cash management will be provided by CAS as a regulated provider.

5.1.5 Area assurance: Limited
Two recommendations have been made as a result of our work in this area (Recs 1 - 2).

5.2 Roles and responsibilities

5.2.1 Roles for treasury management stakeholders are stated within the strategy for each council and include the roles of the council, joint audit and governance committee (JAGC) and the section 151 officer. However, the strategy does not refer to the role of JAGC ensuring effective scrutiny of the treasury management strategy as stated in the constitution. It is not clear how the 5 councils partnership client team overseeing the finance service, interfaces with the councils' section 151 officer as far as treasury management and this is not covered by the current strategy which was drawn up prior to the service being outsourced. It is understood a review is currently being undertaken to identify any elements of the treasury management strategy, or other policies, that require updating to reflect the new outsourcing arrangements. However, internal audit have concerns that, should current arrangements continue, Capita will be authoring policies as well as carrying out the service provision and, since Capita prepare the treasury management reports, Capita will in effect be reporting on their own performance.

5.2.2 An accountant is assigned with day to day responsibility for each council's treasury management function and the officers can cover for the other should the need arise. A daily calculation is carried out by these officers for each council to identify any funds available for investment or a need to draw on funds, such as from money market funds or call accounts. The calculation and decisions are reviewed and authorised by either the principal accountant, accountancy manager (revenue) or the head of finance. The majority of the checking is undertaken by Capita.

5.2.3 From checks undertaken on a sample of 20 transactions for each council, there was evidence supporting the daily calculation being carried out each day and having been checked and authorised by an independent officer. The cover appears to be suitable but all of the resource except the head of finance is from Capita.

5.2.4 Area assurance: Limited
One recommendation has been made as a result of our work in this area. (Rec 3).

5.3 Investment and borrowing

5.3.1 The criteria for selecting counterparties to invest with and limits for

investments is set out in each council's treasury management strategy and investment strategy. Transactions can be a mixture of long and short term investments arranged through brokers, Money Market Fund account withdrawals and investments and call account withdrawals and investments. Whilst reviewing the list of loan transactions it was noted that the total that SODC had invested with Newcastle Building Society was £12,500,000 against a limit of £12,000,000. No evidence was available of approval being sought for exceeding the limit from the section 151 officer as is required in the constitution. It is acknowledged that the limit has been increased to £15,000,000 within the next strategy.

5.3.2 A sample of 20 individual investment transactions was reviewed for each council with checks undertaken to ensure daily investment calculations were available supporting the decisions, the daily calculation was independently reviewed and authorised, the investment was in accordance with the investment strategy and limits and the transaction was correctly coded within the general ledger. No areas of concern were noted regarding the transactions other than two typographical errors which had no impact upon the decisions and a duplicate record in an investment listing that was not duplicated in the cash flow calculation or daily calculation.

5.3.3 The scope and flexibility to borrow in the short term is set out in prudential indicators and limits. Each council has a borrowing strategy within the treasury management strategy but neither council has had a need for borrowing during 2015/2016 or 2016/2017 to date as at the time of review.

5.3.4 SODC
Area assurance: Satisfactory
One recommendation has been made as a result of our work in this area (Rec 4).

5.3.5 VWHDC
Area assurance: Full
No recommendations have been made as a result of our work in this area.

5.4 **CIPFA code of practice**

5.4.1 The Local Government Act 2003 and supporting regulations requires the councils to 'have regard to' the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the councils capital investment plans are affordable, prudent and sustainable. The CIPFA code of practice makes recommendations designed to provide the basis for all public service organisations to create clear treasury management objectives and to structure and maintain sound treasury management policies and practices.

5.4.2 The councils' treasury management strategies and treasury management practices meet the primary requirements of the code. However, CIPFA

suggest that councils should use the lowest rating from all three rating agencies when evaluating investment opportunities. Both councils do not follow this advice as it is considered to limit the amount of available counterparties too much. Instead, the investment limits will be set by reference to assigned ratings. This is clearly explained in both councils' strategies.

5.4.5 Area assurance: Full
No recommendations have been made as a result of our work in this area.

5.5 **Monitoring and reporting**

5.5.1 A requirement of the CIPFA code is that security and liquidity benchmarks are considered and approved and these indicators are used to assess performance of treasury functions. Performance against benchmarking indicators are reported in the annual mid-year and year end treasury reports. These are presented to the joint audit and governance committee in January and September respectively each year. Only two of the four VWHDC benchmarking measures set out in the strategy are reflected within the annual report but all of those for SODC are addressed.

5.5.2 Each council is required to report local authority borrowing and lending to the Government by way of a quarterly return. At the time of review, the most recent return was as at 30 September 2016 and this was found to be supported by working papers for each council detailing how the figures submitted were arrived at.

5.5.3 A listing is maintained by each council logging loans made and recording treasury activity as and when transactions take place. The spreadsheets were used for sample checks within the other objectives of this review and were found to be comprehensive and up to date.

5.5.4 SODC
Area assurance: Full
No recommendations have been made as a result of our work in this area.

5.5.5 VWHDC
Area assurance: Satisfactory
One recommendation has been made as a result of our work in this area (Rec 5).

5.6 **Access level controls**

5.6.1 Financial transactions are recorded within the general ledger held in the Agresso financial system and access to that system is covered within the annual general ledger audit. The banking transactions are a part of the council's banking contract with Barclays Bank and officers use the Barclays Internet Banking (Barclays.net) package to access online banking records.

5.6.2 In order to use Barclays.net, software needs to be loaded onto the

workstation and users are issued with a USB device and access card with a pin. There are three officers acting as administrators of the system who create new users and reset pins but they do not have treasury management responsibilities. The access cards are reissued every two years and an audit trail is available showing user access history. From review of Barclays.net user access reports and an audit log for the system no areas of concern were identified.

5.6.3 Area assurance: Full
No recommendations have been made as a result of our work in this area.

OBSERVATIONS AND RECOMMENDATIONS

POLICIES AND PROCEDURES

1. Treasury management strategy (Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Treasury management strategies for VWHDC and SODC are harmonised and clearly state roles of all stakeholders.</p> <p><u>Findings</u> From comparison of the treasury management strategies for SODC and VWHDC the following differences were noted:-</p> <ul style="list-style-type: none"> • The strategy for SODC refers to section 32 of the Local Government Act. The strategy for VWHDC refers to section 33 of the same act for the same detail. • The current position in the strategy for SODC refers in table 3 to classification as at 31/12/14. Table 3 for VWHDC refers to classification as at 31/12/15. • The minimum revenue provision in SODC's strategy refers to guidance in section 21 of the Local Government Act 2003. The VWHDC strategy refers to section 21(1A) of the same act. <p>Furthermore, the role of the Joint Audit and Governance Committee (JAGC) set out in the strategy does not refer to the JAGC ensuring effective scrutiny of the treasury management strategy as stated in the constitution.</p> <p><u>Risk</u> If the treasury management strategy does not address all roles and responsibilities then it may not be in accordance with the councils'</p>	<p>The treasury management strategies for both council's should be:-</p> <ol style="list-style-type: none"> a) Harmonised to address differences identified. b) Updated to cover the role of the JAGC to ensuring effective scrutiny of the treasury management strategy 	<p>N/A</p>

constitution.	
Management Response	Implementation Date
Recommendation is Agreed	Implemented
Management response: Simon Hewings, Chief Accountant (Capita)	

2. Treasury management practices (Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Treasury management Practices (TMP's) should be kept up to date and in accordance with TMP's that are stated within treasury management strategies.</p> <p><u>Findings</u> There are 12 TMP's within the accountancy electronic directory dating from February 2014. TMP1 covers credit and counterparty risk management and is included within the treasury management strategy for each council. The version held in the accountancy electronic directory differs substantially in content to that in the strategy. The remaining TMP's are out of date and do not reflect the current position regarding the outsourced service. The TMP's include TMP11 for the use of external service providers.</p> <p>Furthermore, there are older version of the TMPs located within the SODC specific treasury management folders.</p> <p><u>Risk</u> If there is more than one version of a TMP in use then it may not be clear which is the most up to date hence there may be uncertainty as to which practice note officers should be following.</p>	TMP's should be reviewed and updated to ensure they are current and reflect the councils' treasury management strategies and revised roles following the outsourcing of treasury management functions.	Chief Accountant (Capita)
Management Response		Implementation Date
Recommendation is Agreed in Principle TMP's will be reviewed with the S151 officer and the finance and procurement manager (client team), to reflect the current outsourced arrangements.		31 March 2018
Management response: Simon Hewing, Chief Accountant (Capita)		

ROLES AND RESPONSIBILITIES

3. Roles and responsibilities

(High Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Roles and responsibilities within treasury management are clearly defined and documented including client contractor roles, monitoring and reporting arrangements.</p> <p><u>Findings</u> Capita are producing the treasury management monitoring reports so will in effect be reporting upon their own performance. Furthermore the current TMP5 refers to separation of duties between those setting treasury management policy and those implementing and controlling the policies. The last policy was authored by an officer now employed by Capita.</p> <p>Roles and responsibilities within treasury management as far as the interface between the client, contractor and section 151 officer are not clear. Since 1 August 2016, treasury management functions have continued to be provided by Capita on the same basis, and with the same officers, as when the service was in house. This relies on Capita not changing responsibilities in order for the service continue as is.</p> <p><u>Risk</u> If roles and responsibilities are not clearly defined then there is a risk that Capita's treasury management services is not independently reviewed and monitored.</p>	<p>Roles and responsibilities for treasury management functions, including producing policies and reporting on contractor performance, should be clearly defined and include details of how the 5 councils partnership client team interface with the councils' section 151 officer.</p>	<p>Head of HR, IT and Technical Services</p>
Management Response		Implementation Date
<p>Recommendation is Agreed It is agreed that roles and relationships regarding treasury management should be clearly defined. This will be included in a broader piece of work in which the respective responsibilities of the joint client team and retained staff (included s151 officer) are to be mapped and clarified in details.</p> <p>Management response: Andrew Down, Head of HR, IT and Technical Services</p>		<p>30 September 2017</p>

INVESTMENT AND BORROWING

4. Exceeded limit – SODC only

(High Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Any instances where treasury</p>	<p>a) Retrospective approval/acknowledgeme</p>	<p>N/A</p>

<p>management strategy limits are exceeded are managed in accordance with the council's constitution and correct authorisation is given.</p> <p><u>Findings</u> At the time of review the council's investments with Newcastle Building Society totals £12.5 million. The treasury management strategy states that the maximum investment per counterparty for building societies with assets between £3,000 million and £5,000 million is £12 million in total. An update in November 2016 lists Newcastle with assets of £3,741 million so the limit for council investments is £12 million.</p> <p>The council's constitution allows the Chief Finance Officer (section 151) to make exceptions to the limits in the treasury management investment strategy in any financial year up to £3,000,000 subject to satisfactory assessment of risk and gain and in consultation with the cabinet member for finance. There was no evidence available to support approval for exceeding the limit being sought.</p> <p><u>Risk</u> If the council exceeds limits set out in investment strategy without appropriate authorisation and review of associated risks then the council may not be acting a prudent manner and officers may be acting outside of their authorised limits.</p>	<p>nt should be sought from the section 151 officer and cabinet member for finance for exceeding the limit in the treasury management strategy.</p> <p>b) A mechanism should be introduced to ensure cumulative lending to individual organisations is monitored to identify instances where limits may be breached to ensure appropriate action is taken and authorisation is sought.</p>	
Management Response		Implementation Date
<p>Recommendation is Agreed Report to the joint audit and governance committee in January 2017.</p> <p>Management response: Simon Hewing, Chief Accountant (Capita)</p>		Implemented

MONITORING AND REPORTING

5. Benchmarking – VWHDC only

(Medium Risk)

Rationale	Recommendation	Responsibility
<p><u>Best Practice</u> Progress against treasury management benchmarks is clearly stated within the annual treasury management report.</p> <p><u>Findings</u> VWHDC's treasury management strategy sets out four benchmark measures. Two of these are clearly</p>	<p>The treasury management annual outturn reports should clearly refer to, and record performance against, each benchmark set out in the treasury management strategy.</p>	<p>Chief Accountant (Capita)</p>

<p>reported within the annual outturn report. However the following two benchmarks do not appear to be addressed within the annual report:-</p> <ul style="list-style-type: none"> • Maximum investment of daily balances (in-house) • Maintenance of a balanced portfolio <p><u>Risk</u> If the council does not set out performance against all agreed benchmarks then it may not be compliant with the CIPFA code.</p>		
Management Response		Implementation Date
<p>Recommendation is Agreed in Principle The 2017/2018 strategy approved by the joint audit and governance committee in January 2017, no longer includes these benchmarks. However, the 2016/2017 outturn report due in July 2017 will refer to any performance issues.</p> <p>Management response: Simon Hewings, Chief Accountant (Capita)</p>		30 September 2017