

	The Stevenage & Uttlesford Audit Partnership Internal Audit Report Car Loans & Leasing 2006-07	
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To: Daniel Harris, Finance Projects Manager

For Information: Scott Crudgington, Assistant Chief Executive [Finance]
Pauline Coletta, Head of Finance
Sue Kingsley-Smith / Suzanne Brightwell, Senior Corporate Administration Officers

1. Introduction

An audit of Car Loans and Leasing has been carried out as part of the 2006-07 Audit Plan. Detailed testing has been carried out on the systems of control and the management of risk within this area.

2. Findings and Recommendations

The detailed findings and recommendations are set out in the report attached as Appendix A to this memo. The completed Management Action Plan is attached as Appendix B.

3. Conclusions

Our audit has confirmed that some recommendations from the previous audit report issued October 2003 remain outstanding. The systems of control are not always complied with, resulting in an increased risk of error and misadministration. We have made recommendations for improvement, in areas mostly known to corporate administration staff. These areas relate to interest rates charged, eligibility, policy compliance and the computer system.

S H Martin
Audit Partnership Manager
December 2006

APPENDIX A

CAR LOANS & LEASING 2006-07

1.1 AREAS COVERED DURING THE AUDIT

The key areas of **possible** risk identified at the planning stage of the audit were as follows:

- a) Arrangements to terminate the car lease scheme have not been made and staff have not been notified;
- b) There are outstanding commitments to associated lease car companies;
- c) The terms and conditions of the car loan scheme are not clear or adhered to, and legal agreements are not completed;
- d) There are no documented procedures and insufficient trained staff to operate the scheme;
- e) Council staff are not aware of the scheme and its benefits.
- f) Car loans are granted to ineligible employees with no supporting evidence held on file;
- g) Interest rates are not set properly and are not agreed by the Council;
- h) Loan repayments are incorrectly calculated, claimed and accounted for;
- i) There is no reconciliation between employee payroll deduction and amount per loan/lease agreement;
- j) There are no recovery procedures in place;
- k) Existing loans are not repaid before a new loan is granted;
- l) There is no insurance to cover SBC in the event of employee defaulting on the loan.
- m) Information is not held in accordance with the Data Protection Act.

The methodology stated in the terms of reference document was used to establish and test the controls that management have in place for mitigating or reducing the above risks to an acceptable level.

1.2 OVERALL AUDIT OPINION

Key controls exist but with some inconsistency in application. There is evidence that some loans have been issued contrary to policy. We have identified areas of risk that could be reduced by implementing the recommendations in this report.

1.3 PREVIOUS RECOMMENDATIONS 2003/04

The previous audit report contained 26 recommendations. We reviewed these recommendations and identified that 9 had been implemented and 11 were no longer applicable due to the ending of the leased car scheme. The remaining 6 recommendations are incorporated in the following current recommendations and are identified as being made previously.

1.4 CURRENT RECOMMENDATIONS

1.4.1 LEASED CAR SCHEME

A Corporate announcement advising the leased car scheme will end was posted on the Intranet – Human Resources site and letters were sent to relevant employees on 26/04/05. The letter detailed the compensation options available to staff. The acceptance process of these options was tested and found to be satisfactory with the exception of an interest free loan.

1.4.2 Interest Free Loan

The notification to staff below Grade PO5 with a lease car advised that there was an option for SBC to provide an interest free loan. The letter also stated that the Council had determined that the Council would meet any tax or NI costs that would normally fall on staff as a “benefit in kind”. One member of staff requested the option of an interest free loan; and a £10,000 loan was issued for a 3 year period on 28th April 2005.

After researching the Inland Revenue website we considered that the Council may be at risk regarding ‘benefit in kind’ liabilities for the employee and the Council. The interest free loan had not been declared on the P11D return and there were tax implications for the employee.

The Council has been put at risk due to the failure to correctly account for employee tax and NI liabilities due to the ‘fee loan’ amount being in excess of the £5000 the threshold set by Inland Revenue before it’s considered to be a ‘beneficial loan’. The Exchequer Manager confirmed this was discussed by the Council’s working group but was overlooked when writing the final terms and conditions for the withdrawal of the car lease scheme. Therefore as the loan given is for £10,000 this is now considered a ‘beneficial’ loan and the employee is liable for tax. The Exchequer Manager has discussed this issue with the Head of Human Resources explaining the error that has been identified and propose the following process to rectify the current risk to the council:

- Establish what the loan repayments and interest due would have been.
- Agree with employee / HR the amount of loan interest payable for the amount above £5K, being a further £5K.
- Exchequer Manager to write a memo explaining the mistake and declaring the amount of interest payable by the employee.
- Deduct the amount payable from the employee’s salary and compensate with a supplementary payment, thus eliminating the Inland Revenue ‘benefit in kind’. This eliminates any liabilities for the employee and the Council to make any P11D declarations.
- As from November 2006 the loan principle will have reduced to £5000, and inline with the IR threshold for a beneficial loan.
- Review the employee’s salary in March 2007 to ensure there is no further tax /NI costs outstanding.

We recommend that the Exchequer Manager implement the proposed action to eliminate the risk of tax and NI costs to the employee and Council. The action should include:

- i. Write a memo to the Head of Human Resources explaining the mistake and declaring the amount of interest payable by the employee.
- ii. Notify the employee of the necessary action required including signing a new credit agreement.
- iii. Complete the necessary loan records to ensure any liability on behalf of the employee and Council is removed.
- iv. Ensure that Corporate Admin have the appropriate records on file to show the loan not to have been deemed a benefit in kind.

1.4.3 Unredeemed credit notes

Our tests on lease car files revealed some supplier credit notes. As we were aware that Exchequer were having problems in processing credit notes as identified during the Creditors Audit 2005-06, we completed further tests to ensure the credit notes had been processed appropriately. We found that a total of £1986.59 credit remained unredeemed:

- There are 4 credit notes for HSBC total £565.57 that remain uncleared on Integra as Status 8 – Posted to Ledger. There is one invoice value £45.87 held since 31/07/2005 as Status 8, which can be off set; leaving a remaining credit balance of £519.70 owed by HSBC.
 - In addition there is one outstanding Lombard credit note for £1421.02 it was still showing as 0 – Summary Entry, despite Corporate Admin certifying it on 03/10/2005. Exchequer had placed the document image on Integra but had not changed the status to 8– Posted to Ledger. The last invoice for Lombard was cleared on 25/08/06. Exchequer were contacted and agreed to contact Lombard and request a cheque to be sent.
- a. **We recommend** that Corporate Admin contact HSBC requesting payment of credit balance of £519.70, as there will be no future leases being entered into and therefore no foreseeable invoices to off set against.
 - b. **We also recommend** that Corporate Admin ensure Exchequer receive a cheque payment from Lombard for £1421.02 redeeming the outstanding credit note.

1.4.4 Remaining leases

The last remaining staff car leases will expire in November 2006. There is also a lease for the Mayor's car, which will expire in April 2007 and there is uncertainty as to who will administer any future lease.

We recommend that Corporate Admin advise the Mayor's office to lease or purchase the next Mayor's car through the Corporate Procurement Manager who can also advise on the administration involved.

CAR PURCHASE [LOAN] SCHEME

1.4.5 Procedure notes

Car loan procedure notes are not up to date.

As previously recommended procedure notes for the car loan scheme should be agreed, updated and documented for the benefit of future and existing staff to ensure continuity in the service provided.

1.4.6 Eligibility

The car purchase scheme states that loans will be offered to assist staff based on job need. We identified that this is not the case and people who are neither classed as essential or casual car users are obtaining a loan. On occasions the loan scheme and credit agreement terms and conditions are not met prior to the loan being advanced or conditions are breached after the advance is made. We identified which staff are

classed as essential users and also determined which staff were claiming mileage allowance. A comparison was made with the active loans, which identified that:

- i. As at 01/04/06 of the 35 employees with loans, 14 had not made any claims for business mileage during 2005-06.
- ii. We also identified that the employee's grade or salary is checked but not recorded on file.
- iii. Some authorising signatures are not easily identified.
- iv. Corporate Administration staff process the claims but it is Divisional / Section Head managers who determine eligibility, placing a reliance on the Head of Service to agree eligibility.
- v. In the past Corporate Admin have felt that they could not reject a loan application if it was authorised by the Head of Service.

We also tested 10 loan files [7 current and 3 completed] issued since August 2000. We identified the following 9 incidents of non-compliance:

- vi. 2 loans issued were more than the values of the cars [CPS No.1382, 1326]
- vii. 1 Credit Agreement could not be found [1327]
- viii. 1 Invoice not available, only an order [1327]
- ix. 1 No registration document [1327]
- x. 1 No insurance document [1327]
- xi. 1 Engineers report did not give estimated value or life expectancy. [1292]
- xii. 1 car was older than 3 years; the loan should be a maximum of 4 years, but a 5 period was given. [1358]
- xiii. 1 vehicle purchased is a panel van and the insurance is for the employee's partner [van driver, self employed] as main driver and the employee being named. [1358]. It is evident that vehicle was not purchased for the employees' use and therefore the loan should not have been granted. The loan is due to expire 10th October 2008.
- xiv. We also reviewed a loan that had previously been questioned by Corporate Admin but had not been satisfactorily concluded. The vehicle purchased with loan CPS1364 is registered in the employees partner's name and insured for the partner with only the employee as a named driver and is not insured for business purposes. It's therefore reasonable to conclude that the employee has not purchased the vehicle for his use contrary to terms and conditions of the car purchase scheme. The loan is due to expire 29th March 2007.

- a. **We recommend** that Corporate Admin staff record the employee salary check on the application form. Suggest the application form is updated to include results of this check and who completed it.
- b. **We recommend** that the application form be updated with a space for printed names next to all signatures.
- c. **We also recommend** that the application form is changed to include a statement preceding the Division / Section Head signature to indicate that they confirm this employee is entitled to a loan via the Car Purchase Scheme because they need to be mobile to properly perform his/her job. This defines the responsibility as being the employee's Manager to confirm eligibility.
- d. **We recommend** that future loans should not exceed the value of the car. As per the terms and conditions para.2.2, which states '*The loan will not exceed the purchase price of the new or second hand car*'.
- e. **We recommend** that all future loans must be issued in strict adherence with the Car Purchase Scheme terms and conditions and the credit agreement. Any application considered not to be eligible should be rejected with a memo explaining the reason/s for rejection. Any subsequent appeal or request to still issue the loan should be processed via the Chief Executive [Finance] for authorisation.
- f. **We recommend** that if after the loan has been advanced, a check reveals the loan is in breach of the rules or agreement, the employee must be requested to repay

the loan. Where management decide not to invoke the Council's rights, then the reasons why should be recorded and authorised by the Assistant Chief Executive [Finance].

- g. With regards to the 2 loans CPS 1358 & 1364 that were revealed to be in contravention of the scheme after the loan had been advanced; **we recommend** that the Financial Projects Manager discusses these cases with the Head of Human Resources to agree what action is to be taken. We would like to be informed of the outcome.
- h. **We recommend** that care be taken to ensure all credit agreements are securely filed. In addition consider scanning the originals and holding electronically.

We consider the Car Purchase Scheme to be the responsibility of Corporate Admin and Finance. We **previously recommended** that either the individual managers be reminded to only authorise claims from eligible staff members, or if consideration to extending the scheme to all staff regardless of need is to be given, then this should be proposed to and agreed by SMB and the procedure notes updated accordingly.

Consideration can be given to the possibility that the Council may receive a better level of interest than on loans placed by Treasury through the money market. This is a possible incentive to widen the scheme to all employees. However, this needs to be balanced with the increased risk of non-payment and an increased level of debt.

Following the appointment of the Finance Projects Manager, the Senior Corporate Admin Officer was requested to draft a report to Strategic Management Board [SMB] that made some recommendations to change the scheme controls and conditions. The Finance Projects Manager is to include another option, which is to end the scheme.

- i. Therefore, pending the future decision of SMB to end or continue the car purchase scheme, **we recommend** prompt action be taken to implement the recommendations of this report where relevant to existing loans.

1.4.7 Driving Licences

Due to staff not having to show that they are actually allowed to drive before they are awarded a loan, it was **agreed** during the previous audit that driving licences would be requested as part of the essential documentation before a loan is awarded.

We recommend that the requirement to produce a valid driving license is added to the terms and conditions and procedures to ensure a copy is maintained on file for all loans.

1.4.8 Checks on vehicle ownership

Checks are not made to confirm that the vehicle has remained with the applicant. Mileage claims could be checked to help with this, as well as an annual check on insurance cover. **Previously it was agreed** that an annual check on ownership would be completed.

We therefore recommend that Corporate Administration introduce their intended annual ownership checks of mileage claims and insurance to ensure compliance with the terms and conditions of loan, retaining photocopies on file. The scheme procedures and documentation should be updated to incorporate these checks.

1.4.9 Loan repayments – early redemption

The Car Loan Database is used to produce a schedule of repayments, which includes the amount of interest due after each payment is made. This schedule is also used to calculate the early redemption figure charged. We contacted the database supplier and reviewed the database system interest and rebate calculation to confirm the accuracy of charges made for loans and those redeemed early. We found the calculations used in the database were satisfactory and in line with current consumer

credit act legislation. We also tested a sample of loans and an early redemption loan, which we found to be accurate and correctly charged.

Our testing of the calculations for used loan repayments revealed that a consistent formula is used in line with original NJC Purple book options. We noted that the latest NJC 'green book' does not include any reference to Car Purchase Schemes, therefore making the scheme more 'common practice'. There is no documented record of the method of loan interest calculation being agreed by the Assistant Chief Executive [Finance].

- a. **We recommend** the method of calculating the loan interest repayments is entered in the updated scheme terms and conditions.
- b. **We also recommend** that the updated version of the terms and conditions be presented to the Assistant Chief Executive [Finance] for his authorisation.

1.4.10 Debt control / insurance on repayments / leavers

In the past there have been staff with loans that have left the Council and the loans have not been repaid. There is currently no insurance policy in place to cover the loan repayments if this occurs. **As previously agreed** with us, Corporate Admin looked into the possibilities of a loan repayment insurance policy. In July 2004, the Council's Insurance brokers confirmed that this type of cover was not available from their current insurers and also stated that it is not the sort of cover any insurers are keen to provide. Where this is offered, it tends to be as part of 'combined policies' or as a 'perk'.

As part of the controls to mitigate the risk of non-payment it was agreed at the previous audit that a formal policy on leavers is needed. Corporate Admin have changed the procedures to minimise the risks where possible by introducing, in conjunction with the ICT department, an updated leavers form which specifies immediate notification is required of any leaver with a car loan. In addition the Finance Projects Manager has the intention to take a tougher stance on leavers repaying their loans before they leave, by means of deduction from the final salary as per the scheme conditions. Where this was not possible, in a recent case, a charge has been placed on the ex-employee's property after they had defaulted on an arrangement to repay the outstanding loan. Administering staff are intending to make this clearer when they issue the loan. There are legal requirements surrounding the repayment of a loan after an employee has left which is why staff are keen to revert to what is detailed in the actual terms and conditions of the car purchase scheme.

We recommend that Finance Projects Manager ensure the procedures for debt recovery are documented, and the terms and conditions updated.

1.4.11 Interest rate charged

Previously, our 2003-04 internal audit report on Car Loans highlighted that a DMT [now SMB] approved memo from 1988 outlined that amendments to interest rates would be in line with the Local Government Finance Report [LGFR] - the 2006-07 LGFR rate is 6.0 per cent.

There is no current procedure detailed calculating the interest rate to be charged for car loans or how it should be reviewed. The interest rate has remained fixed at 6.5% since 2002.

An alternative system also used within the Council previously was recalled by the Exchequer Manager, she recalled the Finance SDU would use the Inland Revenue average official rates considered in relevance to 'beneficial' loan arrangements and add 2% thus mitigating the risk of any employee and the Council being liable for tax due to the issue of a beneficial loan. At present this would be set at 7.0 %.

- a. In line with the **previous audit report, we recommend** that the Finance Projects Manager reviews the alternative methods of setting the interest rate to be charged for Car Loans and recommends a formula to be agreed by the Assistant Chief Executive [Finance] with an additional proposal for annual reviews of the rate to take place.

The loans are issued on a fixed rate fixed term basis. The fixed sum credit agreement issued to and signed by staff does not specify that the loan is fixed. Wording on SBC credit agreement needs to be changed to make it clear that the interest rate is fixed for the period of loan.

- b. **We recommend** the SBC credit agreement is updated to detail the interest rate being fixed for the loan period. We have provided Corporate Admin with some example credit agreements that can be used for sample wording.

1.4.12 Computer system

We noted during the 2003/04 audit that the car loan computer system is only used for calculating loan repayments. There was an issue regarding the initial payments being taken from salaries prior to the due date. This issue has been resolved and Corporate Admin should now be able to fully utilise the system. We have been paying an annual licence of £200 for a product that we are not using.

We recommend that the car loan computer system be fully used.

Glenn Bayford
October 2006

APPENDIX B

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07						
Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.2	<p>We recommend that the Exchequer Manager implement the proposed action to eliminate the risk of tax and NI costs to the employee and Council. The action should include:</p> <ul style="list-style-type: none"> i. Write a memo to the Head of Human Resources explaining the mistake and declaring the amount of interest payable by the employee. ii. Notify the employee of the necessary action required including signing a new credit agreement. iii. Complete the necessary loan records to ensure any liability on behalf of the employee and Council is removed. iv. Ensure that Corporate Admin have the appropriate records on file to show the loan not to have been deemed a benefit in kind. 	H	Agreed	Exchequer Manager	i & ii will be implemented by Jan 2007. iii & iv will be implemented by end of Mar 07 so that this prevents an additional tax liability for the employee.	See Officer comments Jan & Mar 2007.
1.4.3a	<p>We recommend that Corporate Admin contact HSBC requesting payment of credit balance of £519.70, as there will be no future leases being entered into and therefore no foreseeable invoices to off set against.</p>	L	Agreed	Senior Corporate Administration Officers		December 2006

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07

Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.3b	We also recommend that Corporate Admin ensure Exchequer receive a cheque payment from Lombard for £1421.02 redeeming the outstanding credit note.	L	Agreed	Senior Corporate Administration Officers		December 2006
1.4.4	We recommend that Corporate Admin advise the Mayor's office to lease or purchase the next Mayor's car through the Corporate Procurement Manager who can also advise on the administration involved.	M	Agreed	Senior Corporate Administration Officers	Mayor's office already advised – action ongoing	Already Actioned
1.4.5	As previously recommended procedure notes for the car loan scheme should be agreed, updated and documented for the benefit of future and existing staff to ensure continuity in the service provided.	M	Agreed	Senior Corporate Administration Officers		March 2007
1.4.6a	We recommend that Corporate Admin staff record the employee salary check on the application form. Suggest the application form is updated to include results of this check and who completed it.	L	Agreed	Senior Corporate Administration Officers		For all new loans w.e.f. 4.12.06
1.4.6b	We recommend that the application form be updated with a space for printed names next to all signatures.	L	Agreed	Senior Corporate Administration Officers		For all new loans w.e.f. 4.12.06

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07

Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.6c	We also recommend that the application form is changed to include a statement preceding the Division / Section Head signature to indicate that they confirm this employee is entitled to a loan via the Car Purchase Scheme because they need to be mobile to properly perform his/her job. This defines the responsibility as being the employee's Manager to confirm eligibility.	M	Agreed	Senior Corporate Administration Officers		For all new car loans w.e.f. 4.12.06
1.4.6d	We recommend that future loans should not exceed the value of the car. As per the terms and conditions para.2.2, which states <i>'The loan will not exceed the purchase price of the new or second hand car'</i> .	M	Agreed	Senior Corporate Administration Officers		Immediately
1.4.6e	We recommend that all future loans must be issued in strict adherence with the Car Purchase Scheme terms and conditions and the credit agreement. Any application considered not to be eligible should be rejected with a memo explaining the reason/s for rejection. Any subsequent appeal or request to still issue the loan should be processed via the Chief Executive [Finance] for authorisation.	M	Agreed	Financial Projects Manager		Immediately

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07

Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.6f	We recommend that if after the loan has been advanced, a check reveals the loan is in breach of the rules or agreement, the employee must be requested to repay the loan. Where management decide not to invoke the Council's rights, then the reasons why should be recorded and authorised by the Assistant Chief Executive [Finance].	M	Agreed	Financial Projects Manager		Immediately on finding loans in contravention of the scheme
1.4.6g	With regards to the 2 loans CPS 1358 & 1364 that were revealed to be in contravention of the scheme after the loan had been advanced; we recommend that the Financial Projects Manager discusses these cases with the Head of Human Resources to agree what action is to be taken. We would like to be informed of the outcome.	M	Agreed in principle	Financial Projects Manager	Need to review these cases	March 2007
1.4.6h	We recommend that care be taken to ensure all credit agreements are securely filed. In addition consider scanning the originals and holding electronically.	L	Agreed	Senior Corporate Administration Officers	Agree that paperwork should be securely filed – awaiting secure storage from Premises Management Do not agree that all paperwork needs to be held electronically as well	December 2007

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07

Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.6i	Pending the future decision of SMB to end or continue the car purchase scheme, we recommend prompt action be taken to implement the recommendations of this report where relevant to existing loans.	M	Agreed	Financial Projects Manager		March 2007
1.4.7	We recommend that the requirement to produce a valid driving license is added to the terms and conditions and procedures to ensure a copy is maintained on file for all loans.	L	Agreed	Senior Corporate Administration Officers		March 2007
1.4.8	We therefore recommend that Corporate Administration introduce their intended annual ownership checks of mileage claims and insurance to ensure compliance with the terms and conditions of loan, retaining photocopies on file. The scheme procedures and documentation should be updated to incorporate these checks.	L	Agreed	Senior Corporate Administration Officers		March 2007
1.4.9a	We recommend the method of calculating the loan interest repayments is entered in the updated scheme terms and conditions.	M	Not agreed	Financial Projects Manager	Scheme being suspended	March 2007
1.4.9b	We also recommend that the updated version of the terms and conditions be presented to the Assistant Chief Executive [Finance] for his authorisation.	M	Not agreed	Financial Projects Manager	Scheme being suspended	

MANAGEMENT ACTION PLAN: CAR LOANS & LEASING 2006-07

Appendix/ Para	Recommendation	Significance L Low M Med H High	Agreed/ Not agreed	Officer Responsible	Officer Comments	Implement'n date
1.4.10	We recommend that Finance Projects Manager ensure the procedures for debt recovery are documented, and the terms and conditions updated.	M	Agreed	Financial Projects Manager	Revisions to the scheme recently agreed at SMB until the scheme is within in approx 4 months after consultation with the Unions.	Immediate
1.4.11a	In line with the previous audit report, we recommend that the Finance Projects Manager reviews the alternative methods of setting the interest rate to be charged for Car Loans and recommends a formula to be agreed by the Assistant Chief Executive [Finance] with an additional proposal for annual reviews of the rate to take place.	M	Not agreed	Financial Projects Manager	Not applicable – scheme being suspended and existing loans do not allow for provision to change rate.	
1.4.11b	We recommend the SBC credit agreement is updated to detail the interest rate being fixed for the loan period. We have provided Corporate Admin with some example credit agreements that can be used for sample wording.	M	Not agreed	Senior Corporate Administration Officers	Not applicable – scheme being suspended	
1.4.12	We recommend that the car loan computer system be fully used.	M	Agreed in principle	Senior Corporate Administration Officers	Need to review how we implement this	T.B.A. – when we know the work involved and whether this is a viable option