

## Executive Summary

**To:** Senior Group Accountant  
Treasury and Capital Accountant  
Accountancy Services Manager

**For Information:** Head of Finance (Final Only)

**Date Final Report Issued:** 18<sup>th</sup> March 2009

### 1. Introduction

This report details the Internal Audit of the procedures and controls in place over Treasury Management and has been undertaken in accordance with the 2008/09 Internal Audit Plan. A risk based audit methodology has been applied in undertaking audit testing.

### 2. Findings and Recommendations

Based on our audit findings, Internal Audit has assigned **Moderate Assurance**<sup>1</sup> to the systems and procedures which underpin the Treasury Management process.

On the basis of the Internal Audit work undertaken, 1 high priority, 6 medium priority and 2 low priority recommendations to improve the control environment and to minimise the risks in achieving service objectives have been made. The high priority recommendation is:

The Treasury Management procedures are updated so that a designated bank signatory authorises long-term investment transfers. In addition, periodic quality checks should be undertaken to ensure that investments have been authorised in accordance with the Council's Treasury Management procedures.

The other recommendations relate to the areas of Policies and Procedures, Daily Cash-flow process, External financial advice, Long-Term investments and Monitoring and Reporting. There are no recommendations arising as a result of our work in the area of Year-End procedures.

The detailed findings and recommendations are set out in the detailed report section. A Management Action Plan is attached as Appendix A, it has been agreed and completed by the officers responsible, as identified on the Plan.

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<sup>1</sup> See Appendix B for Assurance Opinion and Priority Definitions

## Detailed Report

### Treasury Management 2008/09

#### 1 Audit Objective

- 1.1 The audit was designed to establish whether management have implemented adequate and effective controls over the Treasury Management process.

#### 2 Audit Approach and Methodology

- 2.1 The audit approach was developed with reference to the procedures in the Internal Audit Manual and by an assessment of risks and management controls operating within each area of the scope.

- 2.2 The following procedures were adopted:

- documentation of the system;
- identification of risks within the system, and controls in existence to allow the control objectives to be achieved; and
- evaluation and testing of controls within the system.

- 2.3 From these procedures we have identified weaknesses in the system of control, produced specific proposals to improve the control environment and have drawn an overall conclusion on the design and operation of the system.

#### 3 Audit Scope

- 3.1 Audit work was undertaken to cover the following areas:

- Policies and Procedures
- Daily Cash-Flow process
- External financial Advice
- Investments
- Monitoring and Reporting
- Year-End procedures

#### 4 Audit Opinion

Based on our audit findings, Internal Audit has assigned **Moderate Assurance**<sup>1</sup> to the systems and procedures which underpin the Treasury Management process.

#### 5 Audit Findings

- 5.1 Our audit findings are reported on an exception basis.
- 5.2 There are no recommendations arising as a result of our work in the Year-End procedures area.

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<sup>1</sup> See Appendix B for Assurance Opinion and Priority Definitions

5.3 The areas in the audit scope that require management consideration are detailed below:

#### 5.4 **Policies and procedures**

5.4.1 There is no formal documentation to evidence that the Treasury Management practices manual is reviewed and approved on an annual basis.

5.4.2 It is recommended that the front page of the Treasury Management practices manual states:

- The date it was last reviewed by the Senior Group Accountant;
- The date when the Accountancy Services Manager last approved the manual; and
- The date of the next annual review.

#### 5.5 **Daily Cash-Flow process**

5.5.1 The daily cash-flow forecast document is initialled as checked, however the reviewer is not dating the check. There is no documented evidence that the check has been undertaken in a timely manner.

5.5.2 It is recommended the daily cash-flow forecast document is dated when it is checked.

#### 5.6 **External Financial Advice**

5.6.1 The preliminary checks performed before an investment is made are not formally documented.

5.6.2 It is recommended that a checklist of preliminary checks performed before an investment is made is developed and implemented. The checklist should be signed off by an appropriate Officer before the investment funds are released.

5.6.3 The original signed contract with the external financial advice provider (Sector) could not be located. The agreement with Sector was found to have been out of contract between October and November 2008, until a retrospective agreement from October 2008 to October 2009 was reached in November 2008. The Treasury Management section was unable to provide Internal Audit with a signed copy of the contract extension.

5.6.4 It is recommended the Treasury Management section retains a working copy of the External Financial Advice contract and any subsequent extensions. In addition, a shared outlook calendar should be set up to include action dates to alert and prompt the Treasury Management section of the need to renew the contract.

## **5.7 Investments**

- 5.7.1 A long-term investment transfer in April 2008 had not been approved in accordance with the Council's Treasury Management procedures. The Treasury Management section did provide email correspondence to support the investment and informed Internal Audit that the appropriate officers were made aware of the investment.
- 5.7.2 It is recommended that the Treasury Management procedures are updated so that a designated bank signatory authorises long-term investment transfers. In addition, periodic quality checks should be undertaken to ensure that investments have been authorised in accordance with the Council's Treasury Management procedures.
- 5.7.3 The Council's Temporary Investment spreadsheet is kept up to date by the Treasury and Capital Accountant, however it is not subject to periodic management review.
- 5.7.4 It is recommended the Senior Group Accountant reviews the Temporary Investment Spreadsheet on a monthly basis. This review should be evidenced and include sample checks to source documentation.

## **5.8 Monitoring and Reporting**

- 5.8.1 Action points arising from Treasury Management team meetings are not formally documented in the minutes or formally followed up at the next meeting.
- 5.8.2 It is recommended that actions points arising from Treasury Management team meetings are documented in the minutes. In addition, the follow up of previous action points should be added as a standing agenda item to Treasury Management team meetings.
- 5.8.3 The Temporary Investment Reconciliation is prepared by the Treasury and Capital Accountant on a monthly basis, however it is not subject to periodic management review.
- 5.8.4 It is recommended the Senior Group Accountant reviews the Temporary Investment Reconciliation on a monthly basis. The reconciliation should be signed and dated as prepared and reviewed.
- 5.8.5 The Investments and Loans portfolio spreadsheet is updated by the Treasury and Capital Accountant on a weekly basis, however it is not subject to periodic management review. In addition, the Investments and Loans portfolio spreadsheet is updated on a continuous basis and as a result the previous period "snapshot" positions are not retained.

5.8.6 It is recommended the Senior Group Accountant reviews the Investments and Loans portfolio spreadsheet on a monthly basis. This review should be evidenced. In addition, month end portfolio positions should be saved and retained.

## **6 Follow up of previous recommendations**

6.1 In January 2008 Internal Audit issued a final report which had 4 recommendations due to be implemented by June 2008. Internal Audit have followed up the progress made in implementing previous recommendations and report that 4 out of 4 recommendations have been fully implemented.

## **7 Icelandic banking collapse update**

7.1 The Council did not have any funds invested with Icelandic banks at the time of the collapse. A number of Councils in the UK have taken the following actions to protect their money:

- Moratorium on international investments
- Relaxed limits on the amount that can be invested in any one institution
- Investments in wider range of institutions to spread risk
- Move towards shorter-term investments, including overnight deposits
- Tightening of investment criteria to minimise risk
- Extra powers for officers to act quickly under delegated authority.

7.2 The Treasury and Capital Accountant provided the following responses on the 21<sup>st</sup> January 2009 to the above actions:

### **1. Moratorium on international investments**

The Council does not have a moratorium on international investments.

We have a notice money account with a Swedish bank that has a high credit rating and a risk averse approach to business and a stable outlook.

We also have deposits with foreign banks that were placed before the Icelandic banks crisis, all of which mature before the end of May 2009. As things currently stand it's unlikely the funds will be reinvested with the foreign institution in question.

Every bank is scrutinised before we place any term deposit funds and at present the preference is to deal with highly credit UK high street banks because of the UK Governments commitment to funding these banks should they require it.

2. Relaxed limits on the amounts that can be invested in any one institution

The Council took the opposite view and tightened our banking group limits from £7.5m to £5m approved at full council. The thinking behind this was to spread risk. We have now reviewed our position and will be asking for the former limits to be re-instated. This is because it is proving difficult to place funds with highly credit rated UK names.

There is now an embargo on investing longer than 1 year.

3. Investments in a wider range of institutions to spread risk

See above.

There are now very few highly credit rated UK financial institutions so spreading risk is not an option unless we invest with lesser credit rated institutions.

4. Moving towards shorter-term investments, including overnight deposits

Dealing in overnight and short term investments would mean a loss in investment interest return. However the Council has over the last few months had high balances of liquid funds, i.e. deposits which can be called back on a same day basis, this was purely as a requirement to meet cash outflows after doing many longer term deposits earlier in the year to take advantage of the high interest rates.

Our notice money accounts pay considerably more than overnight rates and are on average on a par with 3 month fixed levels (higher rates have been obtained than were originally offered through officer negotiation).

The Council's objective is to meet cash flow requirements, while minimising risk and maximising returns on investments. This means having a range of investments from call accounts to short and longer term fixed.

5. Tightening of Investment criteria to minimise risk

As already mentioned we reduced banking group limits from £7.5m to £5m although we are seeking to go back to the original £7.5m as the lower limit is compromising our ability to invest with the very top rated financial institutions.

We receive daily credit ratings updates, commentaries etc, and our list of recommended investment counterparties is amended accordingly.

## 6. Extra power for officers to act quickly under delegated authority

I'm not sure under what circumstances officers would need power to act more quickly than in normal circumstances.

Placing deposits requires more deliberation than normal, i.e. checking credit ratings and any adverse news reports etc before entering into any agreement.

In terms of calling back funds in the light of adverse news then call accounts are already accessible instantly (as long as before 12 noon) by any officer delegated to transact funds.

Fixed term deposits cannot be called back before maturity date under any circumstances. The penalty for doing so would be so severe we'd never see any of the funds if we tried to do so. This is understandable because in the current banking climate the banking system would collapse with investors calling deposits back every time there are negative reports, rumours etc on an institution.

### **Acknowledgement**

We would like to take this opportunity to thank the management and staff of the Treasury Management section for their assistance during the audit.

**MANAGEMENT ACTION PLAN**  
**Treasury Management 2008/09**

<b>Rec. No.</b>	<b>Para. No.</b>	<b>Recommendation</b>	<b>Priority</b>	<b>Officer Responsible</b>	<b>Management Response</b>	<b>Implementation date</b>
1	5.4.2	It is recommended that the front page of the Treasury Management practices manual states: <ul style="list-style-type: none"> <li>• The date it was last reviewed by the Senior Group Accountant;</li> <li>• The date when the Accountancy Services Manager last approved the manual; and</li> <li>• The date of the next annual review.</li> </ul>	M	Senior Group Accountant	Agreed  There is a revision going to the Council in April, which if agreed will affect who the Council can invest with, the recommendation will be implemented by June 2009.	June 2009
2	5.5.2	It is recommended the daily cash-flow forecast document is dated when it is checked.	L	Head of Finance and authorised officers	Agreed in full  Already implemented.	March 2009
3	5.6.2	It is recommended that a checklist of preliminary checks performed before an investment is made is developed and implemented. The checklist should be signed off by an appropriate Officer before the investment funds are released.	M	Senior Group Accountant	Agreed  An investment check list will be added to the reverse of the cash sheets which can then be initialled or ticked as appropriate.	April 2009



**MANAGEMENT ACTION PLAN  
Treasury Management 2008/09**

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4	5.6.4	It is recommended the Treasury Management section retains a working copy of the External Financial Advice contract and any subsequent extensions. In addition, a shared outlook calendar should be set up to include action dates to alert and prompt the Treasury Management section of the need to renew the contract.	M	Senior Group Accountant	Agreed in full A shared Outlook calendar has been set up and a prompt added to go out to tender on the appropriate date.	April 2009
5	5.7.2	It is recommended that the Treasury Management procedures are updated so that a designated bank signatory authorises long-term investment transfers. In addition, periodic quality checks should be undertaken to ensure that investments have been authorised in accordance with the Council's Treasury Management procedures.	H	Senior Group Accountant	Agreed in full This action is covered by the investment check list that will be implemented in recommendation three, as it will cover investments which occur by means of a transfer.	March 2009
6	5.7.4	It is recommended the Senior Group Accountant reviews the Temporary Investment Spreadsheet on a monthly basis. This review should be evidenced and include sample checks to source documentation.	M	Senior Group Accountant	Agreed in full	April 2009

**MANAGEMENT ACTION PLAN  
Treasury Management 2008/09**

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7	5.8.2	It is recommended that actions points arising from Treasury Management team meetings are documented in the minutes. In addition, the follow up of previous action points should be added as a standing agenda item to Treasury Management team meetings.	L	Senior Group Accountant	Agreed in full Already Implemented.	March 2009
8	5.8.4	It is recommended the Senior Group Accountant reviews the Temporary Investment Reconciliation on a monthly basis. The reconciliation should be signed and dated as prepared and reviewed.	M	Senior Group Accountant	Agreed in full	April 2009
9	5.8.6	It is recommended the Senior Group Accountant reviews the Investments and Loans portfolio spreadsheet on a monthly basis. This review should be evidenced. In addition, month end portfolio positions should be saved and retained.	M	Senior Group Accountant	Agreed in full	April 2009

### Assurance Opinion and Priority Definitions

In order to assist management in using our reports we categorise our **Assurance opinions** according to our assessment of the controls in place and the level of compliance with these controls.

Assurance Opinion	Definition
<p><b>Full</b></p>	<p><b>Evaluation opinion:</b> there is a sound system of control designed to achieve the system objectives; and</p> <p><b>Testing opinion:</b> the controls are being consistently applied.</p> <p>Full Assurance will be attributed to a system where no recommendations are made or where in the auditor's judgement the recommendations relate to actions that are considered desirable and which should result in enhanced control or better value for money.</p>
<p><b>Substantial</b></p>	<p><b>Evaluation opinion:</b> basically a sound system but there are weaknesses which put some of the control objectives at risk, and/or;</p> <p><b>Testing opinion:</b> there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.</p> <p>Substantial Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered necessary to avoid exposure to significant risks.</p>
<p><b>Moderate</b></p>	<p><b>Evaluation opinion:</b> basically a sound system of control but there are some more significant/serious weaknesses which put system objectives at risk, and/or:</p> <p><b>Testing opinion:</b> the level of non-compliance with some controls may put certain system objectives at risk.</p> <p>Moderate Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered necessary to avoid exposure to more significant risks.</p>
<p><b>Limited</b></p>	<p><b>Evaluation opinion:</b> weaknesses in the system of controls are such as to put the system objectives at risk, and/or;</p> <p><b>Testing opinion:</b> the level of non-compliance puts the system objectives at risk.</p> <p>Limited Assurance will be attributed to a system where in the auditor's judgement the recommendations relate to actions that are considered imperative to ensure that the Council is not exposed to high risks.</p>

Assurance Opinion	Definition
<b>No</b>	<p><b>Evaluation opinion:</b> control is generally weak leaving the system open to significant error or abuse, and/or;</p> <p><b>Testing opinion:</b> significant non-compliance with basic controls leaves the system open to error or abuse.</p> <p>No Assurance will be attributed to a system where in the auditors' judgement they can place no reliance on the controls and procedures in operation either because they do not exist or because they are weak leaving the system open to abuse or error.</p>

### Priority Categories

We categorise our **recommendations** according to their level of priority and we consider the level of risk associated with the weaknesses identified.

- High** Recommendations relate to major issues that have a significant impact on achieving service objectives and are to be implemented immediately or within one month where practical.
- Medium** Recommendations relate to issues that are expected to impact on achieving service objectives and are to be implemented within two months where practical.
- Low** Recommendations relate to issues that have a lesser impact on achieving service objective and are to be implemented within six months where practical.