



Carlisle City Council

Report to Audit Committee

Report details

| | |
|-----------------------------|---|
| Meeting Date: | 8 December 2022 |
| Portfolio: | Finance, Governance and Resources |
| Key Decision: | Not applicable |
| Policy and Budget Framework | YES |
| Public / Private | Public |
| Title: | Internal Audit Report – Treasury Management |
| Report of: | Corporate Director Finance & Resources |
| Report Number: | RD51/22 |

Purpose / Summary:

This report supplements the report considered on Internal Audit Progress 2022/23 and considers the risk-based Internal Audit review of Treasury Management.

Recommendations:

The Committee is requested to

- (i) receive the final audit report outlined in paragraph 1.1;

Tracking

| | |
|------------|----------------|
| Executive: | Not applicable |
| Scrutiny: | Not applicable |
| Council: | Not applicable |

1. Background

- 1.1. An audit of Treasury Management was undertaken by Internal Audit in line with the agreed Internal Audit plan for 2022/23. The audit (Appendix A) provides substantial assurances and includes 1 medium-graded recommendation.

2. Risks

- 2.1 Findings from the individual audits will be used to update risk scores within the audit universe. All audit recommendations will be retained on the register of outstanding recommendations until Internal Audit is satisfied the risk exposure is being managed.

3. Consultation

- 3.1 Not applicable

4. Conclusion and reasons for recommendations

- 4.1 The Committee is requested to
i) receive the final audit report outlined in paragraph 1.1

5. Contribution to the Carlisle Plan Priorities

- 5.1 To support the Council in maintaining an effective framework regarding governance, risk management and internal control which underpins the delivery the Council's corporate priorities and helps to ensure efficient use of Council resources

Contact details:

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Appendices attached to report:

- **Internal Audit Report – Treasury Management**

Note: in compliance with section 100d of the Local Government Act 1972 the report has been prepared in part from the following papers:

- None

Corporate Implications:

Legal - In accordance with the terms of reference of the Audit Committee, Members must consider summaries of specific internal audit reports. This report fulfils that requirement

Property Services - None

Finance – Contained within report

Equality - None

Information Governance- None

Audit of Treasury Management

Draft Report Issued: 18th November 2022
Director Draft Issued: 21st November 2022
Final Report Issued: 24th November 2022



Audit Report Distribution

| | |
|-------------------------|---|
| Client Lead: | Head of Financial Services Accountancy Services Manager |
| Chief Officer: | Corporate Director of Finance and Resources Chief Executive |
| Others: | Technical Finance Officer |
| Audit Committee: | The Audit Committee, which is due to be held on 8 th December 2022 will receive a copy of this report. |

Note: Audit reports should not be circulated wider than the above distribution without the consent of the Designated Head of Internal Audit.

1.0 Background

- 1.1. This report summarises the findings from the audit of Treasury Management. This was an internal audit review included in the 2022/23 risk-based audit plan agreed by the Audit Committee on 15th March 2022.
- 1.2. Treasury management is described by the Chartered Institute of Public Finance and Accountancy (CIPFA) as the management of an 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.
- 1.3. In practice, this means actively monitoring and managing the Council's banking transactions to ensure that cash is available to pay for debts as they fall due, while minimising borrowing costs as a result of debt and ensuring an acceptable balance is struck between security, liquidity and return, for any investments held.
- 1.4. Council loans (debt) outstanding at the end of September 2022 totalled £12.6M of which £0.48M was due for repayment (short-term debt). Investments at the end of September 2022 including CCLA Property Fund (£3.9M) totalled £29.9M.

2.0 Audit Approach

Audit Objectives and Methodology

- 2.1 Compliance with the mandatory Public Sector Internal Audit Standards requires that internal audit activity evaluates the exposures to risks relating to the organisation's governance, operations and information systems.
- 2.2 A risk-based audit approach has been applied which aligns to the five key audit control objectives (see section 4). Detailed findings and recommendations are reported within section 5 of this report.

Audit Scope and Limitations.

- 2.3 The Client Lead for this review was Head of Financial Services and Accountancy Services Manager. The agreed scope was to provide independent assurance over management's arrangements for ensuring effective governance, risk management and internal controls of the following risks:
 - Financial procedure rules, strategies, policies and procedures are not aligned to Treasury Management current practice.
 - Cash balances, borrowing, lending and investing is not managed effectively.
 - Transactions are not accurately and securely recorded in a transparent manner.
 - Treasury management performance is not accurately monitored and reported in a timely manner.

- 2.4 There were no instances whereby the audit work undertaken was impaired by the availability of information.

3.0 Assurance Opinion

- 3.1 Each audit review is given an assurance opinion intended to assist Members and Officers in their assessment of the overall governance, risk management and internal control frameworks in place. There are 4 levels of assurance opinion which may be applied (See **Appendix C** for definitions).

- 3.2 From the areas examined and tested as part of this audit review, we consider the current controls operating within Treasury Management provide **substantial assurance**.

Note: as audit work is restricted by the areas identified in the Audit Scope and is primarily sample based, full coverage of the system and complete assurance cannot be given to an audit area.

4.0 Summary of Recommendations, Audit Findings and Report Distribution

- 4.1 There are two levels of audit recommendation; the definition for each level is explained in **Appendix D**. Audit recommendations arising from this audit review are summarised below:

| Control Objective | High | Medium |
|--|----------|----------|
| 1. Management - achievement of the organisation's strategic objectives achieved (see section 5.1) | - | - |
| 2. Regulatory - compliance with laws, regulations, policies, procedures and contracts (see section 5.2) | - | 1 |
| 3. Information - reliability and integrity of financial and operational information (see section 5.3) | - | - |
| 4. Security - safeguarding of assets (see section 5.4) | - | - |
| 5. Value – effectiveness and efficiency of operations and programmes (see section 5.5) | - | - |
| Total Number of Recommendations | - | 1 |

- 4.2 Management response to the recommendations, including agreed actions, responsible manager and date of implementation are summarised in Appendix A. Advisory comments to improve efficiency and/or effectiveness of existing controls and process are summarised in Appendix B for management information.

4.3 Findings Summary (good practice / areas for improvement):

The Treasury management function was found to be operating effectively by experienced and qualified staff.

Clear direction is provided to the Treasury Management function by the Financial Procedure rules, Treasury Management Strategy Statement and Treasury Management Practices guidance.

The scheme of delegation was found to be working effectively, although evidence of formal authorisation and counterparty confirmation should be maintained for all investments.

Segregation of duties between dealing, accounting and authorisation is observed.

Cash flow forecasts and daily balance recording is accurately maintained.

All the required insurances are in place.

Appropriate security arrangements to protect Treasury Management evidence are in place.

Treasury Management performance is transparent and reported on a regular basis to the Executive.

Regular budget monitoring is undertaken for Financial Services which includes Treasury Management performance.

Treasury management documents are reconciled to the general ledger annually.

Comment from the Corporate Director of Finance and Resources:

A positive audit review highlighting the excellent work undertaken by the experienced and knowledgeable staff in the Treasury Function. Compliance with both internal policies and external guidance is of paramount importance given the level of funds which need to be managed on a daily basis. I am assured by the substantial rating and thank the auditors for their diligence in undertaking this review.

5.0 Audit Findings & Recommendations

5.1 Management – Achievement of the organisation's strategic objectives

- 5.1.1** Officers are directed on Council Treasury Management requirements by the Financial Procedure Rules, Treasury Management Strategy Statement and the Treasury Management Practices guidance, which incorporates relevant procedures.
- 5.1.2** The Treasury Management Practices and procedures document was recently updated in September 2022. The document largely reflects current practice, although some of the details may require fine tuning. For example, recording of training (see 5.5.1). Procedures for investment transactions that fall outside of the standard HSBC net process (see 5.2.1) are not currently documented. To further increase accuracy and robustness of the review already undertaken, document management arrangements would normally be recommended. This should include names of officers carrying out the review, further increasing accountability for content accuracy. Due to the impending Local Government Reorganisation, this is not now considered to add significant value.
- 5.1.3** The Council does not use specialist Treasury Management software and transactions are recorded using spreadsheets, documents and pdf files. Management may wish to consider if all routine tasks including file locations and update regularity are proportionately captured in Treasury Management procedures. This is considered important because of the technical nature of the service provided and the business continuation difficulties that may be encountered if the Technical Finance Officer was absent at short notice.

5.2 Regulatory – compliance with laws, regulations, policies, procedures and contracts

- 5.2.1** The Scheme of delegation details Officers that can authorise release of funds for investment. One of the four Investment transactions tested was a transfer to an HSBC deposit account which did not follow the standard HSBC net authorisation process. The authoriser was aware of the transaction and copied into the investment negotiation, although formal authorisation could not be evidenced. It is also noted for this transaction that confirmation of the investment from the Counterparty has not been recorded in line with the Treasury Management Practices guidance.

Recommendation 1 – Formal authorisation and confirmation to be recorded for all Treasury management Investments

5.2.2 Segregation of duties was found to be observed in line with the Treasury Management Practices guidance, although coding advice has to be sought from the primary dealer by the Systems Team in order to accurately remove treasury transactions from suspense. The primary dealer is also responsible for posting interest accruals for investments and loans.

5.3 Information – reliability and integrity of financial and operational information

5.3.1 A cash flow model is updated daily for known, significant income and expenditure cash movements. This spreadsheet is also populated with the actual daily bank balance and the variance between forecast and actual balance is recorded. The daily balance estimates were found to be accurate, with a variance of over £100k identified on only four occasions in the month tested. All the variances were favourable demonstrating forecast accuracy of expenditure. Variances can arise because the exact date of income deposits are not always known. On the few occasions where the variance is above £100k, management may wish to consider investigating and recording the reasons, further demonstrating continuous improvement of the service.

5.3.2 Daily balances files are generally found to be recorded regularly and accurately. One investment tested was found to be recorded as a single total investment with one counterparty, although the investment consisted of four smaller transactions, all with different rates of return.

5.4 Security – Safeguarding of Assets

5.4.1 The Treasury Management Practices document requires that Insurances are taken out for Fidelity, Professional Indemnity and Business Interruption. Audit were provided with evidence that all the required insurances are in place with Zurich Municipal. Where specific job titles are quoted in the insurance policy, one was found to be marginally inaccurate and the Insurance Officer queried this with Zurich.

5.4.2 A Treasury Management folder has been set up on the 'Accountancy' server which holds all Treasury Management related documents and spreadsheets. ICT provided evidence of Officers with security access to the files. As a result, one officer was removed from the security group, although this was not considered a significant risk.

5.4.3 A recommendation was made in a previous audit of the Main Accounting System to regularly check security access and it is advised that this regular review is maintained.

5.5 Value – effectiveness and efficiency of operations and programmes

- 5.5.1** Key officers involved in Treasury Management were found to be experienced and have appropriate professional qualifications. Training requirements are reviewed for all Financial Services staff, in line with corporate appraisal requirements. The Treasury Management Practices documents details that Treasury management staff and members will go on courses provide by the Council's Treasury Management Consultants, CIPFA and money brokers. It also details that a record will be kept on all staff training received, although the training record could not be evidenced. It is advised that management consider if the Treasury Management Practices guidance should be updated to reflect current practice.
- 5.5.2** Link Asset Services Limited are the Council's Treasury Management Consultancy Services and they provide regular updates on approved Counterparty lists and associated credit ratings. This significantly reduces risk to the council that counterparties to transactions could default before final settlement. For one of the transactions tested, the correct credit rating was not accurately reflected on the investment spreadsheet. Although the Investment spreadsheet is maintained to a good standard, the counterparty sheet requires review and update. Management may wish to consider if approved counterparties and credit ratings can be demonstrated at the point of investment, without comprehensive transfer of all counterparty and credit rating updates from the LINK update to the Investment spreadsheet.
- 5.5.3** LINK asset services also provide regular, detailed investment review reports to the Treasury Management Team. These reports form the basis of regular quarterly performance reporting to the Executive in line with the Council's Financial Procedure rules; the Executive and Council also receive an Annual Strategy Statement and outturn report. To further increase transparency and accountability of Treasury Management reporting to 'the Council', It is advised that key governance groups are always specified and that reporting arrangements detailed in reports are checked for alignment to all other key Treasury Management guidance.
- 5.5.4** Regular Treasury Management budget monitoring is undertaken and at August 2022 there was a significant favourable variance of £650k. This is due to savings on net interest paid on new borrowing (£355k), Savings on minimum revenue provision (£200k) and surplus on interest received (£113k). The 650k makes up a significant part of the overall Finance and Resources favourable variance of £788k.
- 5.5.5** Reconciliations between the bank and general ledger were tested previously as part of the main accounting audit and found to be effective. For the Treasury Management audit, evidence of reconciliation between the recording of treasury management transactions and the general ledger was provided and this was also found to be effective.

Appendix A – Management Action Plan

| Summary of Recommendations and agreed actions | | | | | |
|--|----------|--|--|----------------------------|---------------------|
| Recommendations | Priority | Risk Exposure | Agreed Action | Responsible Manager | Implementation Date |
| Recommendation 1 – Formal authorisation and confirmation to be recorded for all Treasury management Investments | M | Financial loss through fraud or error. | A process will be put in place to ensure oversight of investments placed | Head of Financial Services | 01/12/22 |

Appendix B – Advisory Comments

| Ref | Advisory Comment |
|-------|---|
| 5.1.3 | Consider if all routine tasks including file locations and update regularity are proportionately captured in Treasury Management procedures. Consider updating procedures for investment transactions that fall outside of the standard HSBC net process. |
| 5.3.1 | Consider investigating and recording the reasons for large cash flow variances, further demonstrating continuous improvement. |
| 5.4.3 | It is advised that a regular review of access rights is undertaken. |
| 5.5.1 | Consider if the Treasury Management Practices guidance should be updated to reflect current arrangements for attending approved training courses and maintaining a record of training. |
| 5.5.2 | Consider if approved counterparties and credit ratings can be demonstrated at the point of investment, without comprehensive transfer of all counterparty and credit rating updates from LINK to the Investment spreadsheet. |
| 5.5.3 | To further increase transparency and accountability of Treasury Management reporting to 'the Council', It is advised that key governance groups are always specified and that reporting arrangements detailed in reports are checked for alignment to all other key Treasury Management guidance. |

Appendix C - Audit Assurance Opinions

There are four levels of assurance used; these are defined as follows:

| | Definition: | Rating Reason |
|---------------------|--|--|
| Substantial | There is a sound system of internal control designed to achieve the system objectives and this minimises risk. | <p>The control framework tested are suitable and complete are being consistently applied.</p> <p>Recommendations made relate to minor improvements or tightening of embedded control frameworks.</p> |
| Reasonable | There is a reasonable system of internal control in place which should ensure system objectives are generally achieved. Some issues have been raised that may result in a degree of unacceptable risk exposure. | <p>Generally good systems of internal control are found to be in place but there are some areas where controls are not effectively applied and/or not sufficiently embedded.</p> <p>Any high graded recommendations would only relate to a limited aspect of the control framework.</p> |
| Partial | The system of internal control designed to achieve the system objectives is not sufficient. Some areas are satisfactory but there are an unacceptable number of weaknesses that have been identified. The level of non-compliance and / or weaknesses in the system of internal control puts achievement of system objectives at risk. | <p>There is an unsatisfactory level of internal control in place. Controls are not being operated effectively and consistently; this is likely to be evidenced by a significant level of error being identified.</p> <p>High graded recommendations have been made that cover wide ranging aspects of the control environment.</p> |
| Limited/None | Fundamental weaknesses have been identified in the system of internal control resulting in the control environment being unacceptably weak and this exposes the system objectives to an unacceptable level of risk. | <p>Significant non-existence or non-compliance with basic controls which leaves the system open to error and/or abuse.</p> <p>Control is generally weak/does not exist.</p> |

Appendix D

Grading of Audit Recommendations

Audit recommendations are graded in terms of their priority and risk exposure if the issue identified was to remain unaddressed. There are two levels of audit recommendations; high and medium, the definitions of which are explained below.

| | Definition: |
|---------------|--|
| High | Significant risk exposure identified arising from a fundamental weakness in the system of internal control |
| Medium | Some risk exposure identified from a weakness in the system of internal control |

The implementation of agreed actions to Audit recommendations will be followed up at a later date (usually 6 months after the issue of the report).