Report to Audit Committee	**Agenda Item:**
	A.5

Meeting Date: 8 July 2021

Portfolio: Finance, Governance and Resources

Key Decision: Not applicable

Within Policy and
Budget Framework   YES

Public / Private   Public

Title: Internal Audit Report - Payroll

Report of: CORPORATE DIRECTOR FINANCE & RESOURCES

Report Number: RD19/21

Purpose / Summary:

This report supplements the report considered on Internal Audit Progress 2020/21 and considers the main financial system review of Payroll.

Recommendations:

The Committee is requested to

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

Tracking

Audit Committee:	**8 July 2021**
Scrutiny Panel:	**Not applicable**
Council:	**Not applicable**

1. BACKGROUND INFORMATION

1.1 A main financial system audit of Payroll was undertaken by Internal Audit in line with the agreed Internal Audit plan for 2020/21. The audit (**Appendix A**) provides reasonable assurances and includes 7 medium-graded recommendations.

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

The Committee is asked to

i) receive the final audit report as 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.

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Appendixes	**Internal Audit Report – Payroll – Appendix A**		

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers:
• **None**

CORPORATE IMPLICATIONS/RISKS:

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.

Finance – Contained within the report

Equality – None

Information Governance – None

Audit of Payroll

Audit Report Distribution

Client Lead:	Payroll and ITrent Supervisor
Chief Officer:	Corporate Director Finance and Resources Deputy Chief Executive Chief Executive
Others:	Payroll Advisor Information Governance Manager
Audit Committee:	The Audit Committee, which is due to be held on 8th July 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 Payroll. This was an internal audit review included in the 2020/21 risk-based audit plan agreed by the Audit Committee on 30th July 2020.

1.2   Staff costs are the largest item of expenditure for most Council services. It is therefore important that payments are accurate, timely, made only where they are due for services to the Council and that payments accord with individuals' conditions of employment. It is also important that all payments are accurately and completely recorded and accounted for. In doing so the Payroll service must analyse and implement legislative changes insofar as they affect local government workforce including all in relation to HM Revenue and Customs, the Pensions Regulator, and Local Government Pension Scheme.

1.3   In November 2020 the HR & Payroll Service transferred from the Finance & Resources Directorate to Community Services as part of a wider restructure of Council services.

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 Payroll and ITrent Supervisor and 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:

- Failure to achieve business objectives due to insufficient governance.
- Lack of checks and controls, resulting in incorrect payroll processing.
- Systems controls are not adequate and unauthorised access is gained (including fraudulent records) and/ or payroll is not run successfully.
- Fines and reputational damage due to inappropriate access or release of confidential data.

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 B** for definitions).

3.2   From the areas examined and tested as part of this audit review, we consider the current controls operating within Payroll provide **reasonable 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 C**. 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)	-	4
2. **Regulatory** - compliance with laws, regulations, policies, procedures and contracts (see section 5.2)	-	2
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)	-	1
Total Number of Recommendations	**-**	**7**

4.2   Management response to the recommendations, including agreed actions, responsible manager and date of implementation are summarised in Appendix A.

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

A good system of processes and checks are in place to deliver the monthly payroll for the Authority and nine Community Centres.

Payroll is part of the wider HR and payroll service with two specialist staff in place. The absence of a Head of Service (recruitment in progress) has impacted on some of the managerial activities undertaken, such as regular review of the operational risk register, and completion of the 2021/22 service plan.

Payroll delivery is critical to the Authority, works on a strict timetable, and the service would benefit from further planning for continuity of service, should either of the two key staff be absent at short notice.

Review of documented procedures for further alignment to the requirements of the financial regulations would enhance both transparency and business continuity.

Comment from the Deputy Chief Executive:

The recruitment of an interim Head of Service for HR and Payroll will assist with the adoption and completion of these seven recommendations. The 2021/22 Service Plan will also focus on the business continuity and organisational resilience aspects of this review.

5.0 Audit Findings & Recommendations

5.1 Management – Achievement of the organisation's strategic objectives

5.1.1 The Payroll Team structure is in place and supported by current job descriptions which have been regularly reviewed.

5.1.2 The Authority's financial regulations detail the overarching requirements of the Payroll Service. There are some key documented procedure notes in place that align to the financial regulations. The service would benefit from a thorough review of all the requirements of the financial procedures relating to payroll, ensuring that documented procedures interpret all requirements and detail how the service maintains compliancy. For example, how the service is kept updated on, and fully complies with taxation and national insurance regulations, and how it ensures proper authorisation procedures are in place for variations to pay.

5.1.3 Procedure notes are written in a processing style and may benefit from review to ensure they will be fully understood if a new member of staff is brought in to run the payroll at short notice. There is a suite of wider policies, guidance documents and forms on the intranet, some of which would benefit from review ensuring that they remain current.

Recommendation 1 – Review of staff procedure notes, and wider suite of policies, guidance documents and forms on the intranet to ensure alignment to financial regulations, clarity for new members of staff, and regular update.

5.1.4 A payroll critical service recovery plan is in place, documented on the intranet and dated October 2018, in line with other services. The plan would benefit from further development to demonstrate that all key disaster scenarios have been considered, and there are comprehensive, fully tested, and documented planning arrangements in place that will be actioned effectively in an emergency. For example, the documented recovery action for 'loss of staff', details, 'use other staff, reduce customer service levels'. Further documentation would help to clarify who the other staff are, whether they are technically skilled in payroll services, internal or external to the Authority, and if there are clearly documented procedures in place for them to follow.

Recommendation 2 – Review the critical service recovery arrangements to ensure that there are fully tested and documented planning arrangements in place for <u>all</u> key scenarios, that can be actioned at short notice.

5.1.5 Documented monthly payroll checklists are in place, one for the four Carlisle payrolls and one for the nine Community Centres. Both check lists were provided for February 2021. The Carlisle checklist was signed and dated by the staff member that carried out the processes, but the Community Centre checklist was not.

Recommendation 3 – A consistent approach should be adopted to verify that all activities on both payroll checklists are completed.

5.1.6 There is a salary timetable in place for 2021/22 which is accessible to all staff on the intranet.

5.1.7 The payroll staff work closely together and regularly communicate on payroll matters. The wider HR & Payroll team hold an informal meeting to catch up on staff movements and other changes in staff circumstances. Payroll staff do not have regular appraisals to assess performance and review training requirements. Internal Audit are planning to work with Organisational Development to ensure appropriate action is taken corporately to ensure appraisals are both complete and timely.

5.1.8 The corporate service planning cycle did not take place in 2020/21 following the first COVID-19 lock down in March 2020. The last available service plan for HR & Payroll was for 2019/20. Management have informed Audit that the 2021/22 HR and Payroll Service Plan will be progressed when recruitment for a new HR Manager is concluded.

5.1.9 There are two risks detailed in the HR & Payroll Operational risk register relating directly to the Payroll Service. The risks are not subject to regular review by payroll staff in line with the risk management framework. The key risk of Payroll staff being absent at short notice is not considered in the operational risk register (this should also be considered in the response to recommendation 2). Assurance that mitigating actions are working correctly is not regularly sought, and they have not been fully tested.

Recommendation 4 – Payroll operational risks to be reviewed on a quarterly basis in line with the risk management framework and include the key risk that staff may be absent at short notice.

5.1.10 Regular financial monitoring is in place for HR & Payroll Services with no issues reported.

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

5.2.1 The Authority runs payroll services for 9 local community centres. There are contracts in place for 8 of the 9 Community centres.

Recommendation 5 – Contracts to be put in place for the provision of payroll services to all Community centres.

5.2.2 HR & Payroll have a data retention log in place, in line with the corporate records management policy. The log details the length of time that classifications of data should be held, although this does not wholly align with the requirements of the financial regulations. The data retention log does not consider how the Authority complies with the data retention requirements of individual community centre contracts. There is a disposals log in place, but document disposals have not been made and the log has not been maintained.

Recommendation 6 – Personal data to be retained and disposed of for the Authority and Community Centres in line with the corporate records management policy.

5.3	Information – reliability and integrity of financial and operational information

5.3.1 The standard errors and warnings report run monthly draws attention to potential payroll data errors in ITrent. As salaries have risen over time, and the parameters set have remained the same, the report regularly warns about high salaries unnecessarily. It is advised that the parameters are adjusted, reflecting current levels of pay.

5.3.2 A high net pay report is collated and investigate monthly.

5.3.3 Permanent new starters were found to be attached to payroll accurately. Claims for overtime, enhancement payments, and notification of casual employment forms were all found to be authorised by an appropriate manager, and then filed on the Payroll server for future reference. Four out of the five leaver forms randomly tested were found to be authorised by an appropriate manager, although verification of authorisation had not been retained for one of them.

5.4 Security – Safeguarding of Assets

5.4.1 Payroll data is held off site on a pen drive for the purpose of business continuity. The data is encrypted and password protected.

5.4.2 ITrent access rights are monitored appropriately and as a built-in control for the prevention of fraud, ITrent does not allow Payroll staff to adjust their own pay.

5.4.3 For permanent staff there is segregation of duty between the HR pre-employment checks and the attachment of contracts to ITrent by payroll staff, increasing the safeguard against bogus employees. For casual staff, there is segregation of duty between the recruiting manager who carries out pre-employment checks, and Payroll staff.

5.5 Value – effectiveness and efficiency of operations and programmes

5.5.1 Payroll staff have completed the mandatory Data Protection and Cyber Security e-learning.

5.5.2 There are some small historical differences with statutory and non-statutory deductions, between the payroll software, general ledger and bank that are unresolved. It is advised that these small differences are investigated, and arrangements put in place to ensure that they do not arise in the future.

5.5.3 It is also advised that the development of further ITrent and Business Object reports is investigated with a view to improving the accuracy and efficiency of payroll data provided to finance for BACS payments and general ledger uploads.

5.5.4 Changes in tax code notifications are regularly updated.

5.5.5 MHR (ITrent providers) regularly notify the payroll service when there is a new upgrade available for ITrent, although not all releases are updated.

Recommendation 7 – Management to keep a record of the availably of software releases and document the reasons if ITrent is not updated with a release.

Appendix A – Management Action Plan

Summary of Recommendations and agreed actions					
Recommendations	**Priority**	**Risk Exposure**	**Agreed Action**	**Responsible Manager**	**Implementation Date**
Recommendation 1 – Review of staff procedure notes, and wider suite of policies, guidance documents and forms on the intranet to ensure alignment to financial regulations, clarity for new members of staff, and regular update.	M	Service cannot wholly demonstrate that they have interpreted and applied the financial regulations that relate to payroll. New staff are unclear on how to run payroll at short notice. Key forms and documents are not current.	Ensure that there are clear procedure and guidance documents for payroll staff, that align to financial regulations. Ensure that documents and forms are updated on the intranet and dated so that all staff know they are using/viewing the most update version.	HR Manager /Payroll & i-Trent Supervisor	31/03/22
Recommendation 2 – Review the critical service recovery arrangements to ensure that there are fully tested and documented planning arrangements in place for <u>all</u> key scenarios, that can be actioned at short notice.	M	Payroll unable to be run. Comprehensive planning not in place for alternative arrangements.	Review the critical service recovery arrangements and agree on a plan and ensure it is documented.	Deputy TC & CE / HR Manager /Payroll & i-Trent Supervisor	31/12/21

Summary of Recommendations and agreed actions					
Recommendations	**Priority**	**Risk Exposure**	**Agreed Action**	**Responsible Manager**	**Implementation Date**
Recommendation 3 – A consistent approach should be adopted to verify that all activities on both payroll checklists are completed.	M	Key processes have not been completed in line with documented procedures and Management are unaware.	Payroll Processing Checklists are initial and dated appropriately.	i-Trent & Payroll Supervisor/ Payroll Officer	01/04/21 - Done
Recommendation 4 – Payroll operational risks to be reviewed on a quarterly basis in line with the risk management framework and include the key risk that staff may be absent at short notice.	M	Risks escalate out of control and management are unaware.	Operational risks to be regularly reviewed and updated in line with the risk management framework. Operational risks to include the key risk that staff may be absent at short notice.	HR Manager /Payroll & i-Trent Supervisor	31/12/21
Recommendation 5 – Contracts to be put in place for the provision of payroll services to all Community centres.	M	Terms of the arrangement are unclear and subject to challenge. Contracts not signed or dated could be subject to legal challenge.	Chase completion of payroll contract with Currock Community Centre which can then be signed off by Legal Services.	Payroll & i-Trent Supervisor / Legal Services (Legal Trainee)	30/09/21

Summary of Recommendations and agreed actions					
Recommendations	**Priority**	**Risk Exposure**	**Agreed Action**	**Responsible Manager**	**Implementation Date**
Recommendation 6 – Personal data to be retained and disposed of for the Authority and Community Centres in line with the corporate records management policy.	M	Carlisle City Council may not comply with UK GDPR and could be subject to legal challenge.	To dispose of payroll filing in line with retention and disposal rules. Ensuring that the disposal log is updated correctly.	HR Manager / Payroll & i-Trent Supervisor	31/03/22 (depending on Covid 19 & access to the office)
Recommendation 7 – Management to keep a record of the availably of software releases and document the reasons if ITrent is not updated with a release.	M	Reasons for not updating ITrent available software releases not fully transparent.	To create and keep an update a log of i-Trent system updates.	HR Payroll & i-Trent Supervisor Manager/ Lead ICT Officer	30/06/21

Appendix B - 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.	The control framework tested are suitable and complete are being consistently applied. Recommendations made relate to minor improvements or tightening of embedded control frameworks.
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.	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. Any high graded recommendations would only relate to a limited aspect of the control framework.
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.	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. High graded recommendations have been made that cover wide ranging aspects of the control environment.
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.	Significant non-existence or non-compliance with basic controls which leaves the system open to error and/or abuse. Control is generally weak/does not exist.

Appendix C

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).