



Carlisle City Council

Report to Audit Committee

Report details

Meeting Date:	08 July 2022
Portfolio:	Finance, Governance and Resources
Key Decision:	Not applicable
Policy and Budget Framework	YES
Public / Private	Public
Title:	Internal Audit Report – Main Accounting System
Report of:	Corporate Director Finance & Resources
Report Number:	RD16/22

Purpose / Summary:

This report supplements the report considered on Internal Audit Progress 2021/22 and considers the review of Main Accounting System

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 Main Accounting System was undertaken by Internal Audit in line with the agreed Internal Audit plan for 2021/22. The audit (Appendix A) provides reasonable assurances and includes 4 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

- 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:

Contact Officer: Michael Roper

Ext: 7520

Appendices attached to report:

- **Internal Audit Report – Main Accounting System – Appendix A**

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 Main Accounting System (MAS), Budget Monitoring and Medium-term Financial Plan (MTFP)

Draft Report Issued: 18th March 2022

Director Draft Issued: 6th May 2022

Final Report Issued: 25th May 2022



Audit Report Distribution

Client Lead:	Head of Financial Services
Chief Officer:	Corporate Director of Finance and Resources Chief Executive
Others:	Accountancy Services Manager Finance Officer (Systems, Controls and Development)
Audit Committee:	The Audit Committee, which is due to be held on 8 th July 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 Main Accounting System (MAS), Budget Monitoring and Medium-term Financial Plan (MTFP). This was an internal audit review included in the 2021/22 risk-based audit plan agreed by the Audit Committee on 15th March 2021.
- 1.2. The main accounting system records all financial transactions and provides information for the preparation of management accounts, statutory accounts and financial returns. To ensure the reliability of financial information for both decision making and reporting purposes, it is essential that effective accounting controls are operated on a regular and consistent basis.
- 1.3. Budget monitoring is the system of comparing actual income, expenditure and commitments to the planned budget, recording explanations for key variances and informing budget holders and management through regular reporting.
- 1.4. The Medium-term Financial Plan sets out the current framework for planning and managing the council's financial resources, to develop its annual budget strategy and update its current five-year financial plan.

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 the Head of Financial Services 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:
 - Accounting transactions and balances are not recorded in an accurate and timely manner
 - Budget monitoring arrangements do not detect and report significant variances
 - Medium term financial planning process fails to identify significant costs and income streams

- 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 MAS, Budget Monitoring, MTFP 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 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 (N/A)	-	-
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)		1
4. Security - safeguarding of assets (N/A)	-	-
5. Value – effectiveness and efficiency of operations and programmes (see section 5.5)	-	2
Total Number of Recommendations	-	4

- 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):

A detailed Medium-term Financial Plan is documented and follows a robust annual process of review, scrutiny and authorisation by The Executive, Business and Transformation Scrutiny Panel and Full Council.

Comprehensive annual training on Council financial processes is available to all staff and supplemented with robust training notes.

Transactions posted to suspense accounts are reviewed and cleared on a timely basis.

Regular monthly budget monitoring reports with explanations for variances are produced and distributed on a timely basis.

Timely debtors and creditors control account reconciliations are carried out with review and authorisation recorded.

Financial system security access is effectively managed.

Review of document management arrangements will help to further demonstrate completeness and accuracy of the financial guide.

Re-instating the supervisory review and authorisation of monthly bank reconciliations will further enhance the controls already in place.

Authorisation process review will help to maintain the accuracy and completeness of journal posting.

Alignment of resource transfers to the Financial Procedure Rules will further enhance transparency of virements.

Comment from the Director of Finance and Resources:

A useful audit review which has highlighted some specific areas for review in order to enhance the Council's budget monitoring procedures and to aid decision making. I welcome the report and accept the recommendations.

5.0 Audit Findings & Recommendations

5.1 Management – Achievement of the organisation's strategic objectives

5.1.1 The MTFP follows a robust annual process of review, scrutiny and authorisation by The Executive, Business and Transformation Scrutiny Panel and Full Council. The process followed aligns with the requirements of the Financial Procedure Rules in the Council's Constitution. Following presentation of a detailed report by the Corporate Director of Finance and Resources, senior governance groups are given the opportunity to scrutinise the data and raise queries which are captured in the relevant minutes. The content of the report was found to explain the financial principles underpinning the MTFP, along with its links to other strategies and is supported by further robust working papers.

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

5.2.1 The Financial Procedure Rules in the Council's Constitution detail the authorisation requirements for transferring resources between approved estimates or heads of expenditure, without creating additional overall budget liability. Where an approved budget is a lump-sum budget or contingency intended for allocation during the year, its allocation is not treated as a virement, provided that the amount is used in accordance with the purpose for which it has been established; and the Executive has approved the basis and the terms, including financial limits, on which it will be allocated.

Resources that have been transferred between approved estimates or heads of expenditure in the virement tracker spreadsheet are allocated either a 'VIRT' (virement) number or a BGTA (budget adjustment) number. The authorisation process for two of the virements tested with 'VIRT' did not fully align to the virement authorisation process detailed in the Financial Procedure Rules, although management explained that they were not considered to be virements.

It is recommended that where resource transfers between approved estimates or heads of expenditure are recorded in the tracker spreadsheet, further detail is provided to enhance transparency of alignment to financial procedure rules.

Recommendation 1 – Further align resource switches to the financial procedure rules

5.3 Information – reliability and integrity of financial and operational information

5.3.1 A sizeable electronic financial guide has been developed to direct staff on specific financial processes. The guide would benefit from regular review and update, although the risk of staff guidance not being current is mitigated to an extent through low staff turnover and experienced Finance Officers. Additional documented guidance for key processes is available throughout Accountancy and assessment for inclusion in the central financial guide is advised.

It is further advised that consideration is given to the proportionality of the review due to Local Government Reorganisation.

Recommendation 2 – Review document management arrangements for the financial guide

5.4 Security – Safeguarding of Assets

5.4.1 Financial system security access is effectively managed and there is a robust arrangement for completing and authorising new user application forms and making changes to existing user access. As an additional layer of security, it is advised that the Head of Financial Services and/ or the Accountancy Services Manager confirm the appropriateness of user access, following receipt of a periodic overview report. Access rights were found to be removed when Officers leave the authority, although not always in a timely manner (sometimes several weeks after). There are likely to be compensating central ICT controls, although risk assessment of financial system access for staff leavers is advised.

5.5 Value – effectiveness and efficiency of operations and programmes

5.5.1 Comprehensive annual training on Council financial processes is available to all staff and supplemented with robust training notes. Financial processes training is not compulsory and only 3 of the current 23 budget managers were found to have attended since 2014. It is advised that management consider the risk that due to low attendance, budget managers may not have received the required direction to manage their budgets effectively. It is further advised that consideration is given to alternative training platforms such as Skill Gate, enabling self-study at a convenient time and location.

5.5.2 Transactions posted to suspense accounts are reviewed and cleared on a timely basis.

- 5.5.3** Timely 'SMS' monitoring reports are distributed comparing year-to-date budget with actual spend. Explanations are provided for all variances although management may wish to further consider the cost/ benefit of doing so. For example, audit testing found that a variance of £301k was broken down into 23 smaller variances with an explanation provided for each. Three material variances over £15k each, accounted for 97% of the £301k, with the remaining 20 lesser variances (both positive and negative) making up the remaining £3k.
- 5.5.4** There are some examples where variance explanations are stated simply as being over or under budget. It is advised that if a variance explanation is given, it should always include the reasons why it is over or under budget. Budget holders should provide Finance Officers with suitable explanations of variances within their service areas.
- 5.5.5** Regular monthly 'FIS' reports are also distributed, comparing the forecast full year actual spend against budget. The forecast full year actual spend is based on actual spend plus purchase orders raised plus balance of remaining budget. Management may wish to consider if the forecast full year actual spend could be enhanced by offering budget holders the opportunity to adjust the balance of remaining budget where they feel this may not accurately reflect known spending pressures for the remainder of the financial year. An accurate budget profile is key to predicting year end spend and these should be regularly reviewed by the relevant budget holder.
- 5.5.6** A bank reconciliation for the three main Council banks is reviewed and recorded daily. The figures from the daily reconciliation are used as the starting position to complete a regular monthly bank reconciliation in the format required for year-end External Audit. The monthly reconciliation is carried out by a different Officer to the daily reconciliation. Historically, the monthly bank reconciliation included a supervisory review and authorisation, although this has not been completed recently due to a change in staff circumstances. To enhance the regular, documented bank reconciliations undertaken, it is recommended that the supervisory review and authorisation is re-instated to further confirm accuracy and completeness.

Recommendation 3 – Reinstate the monthly bank reconciliation supervisory review and authorisation

- 5.5.7** The Scheme of Sub-delegation for Finance and Resources details that the following can authorise journals: Corporate Director of Finance and Resources, Head of Financial Services and Accountancy Services Manager. Audit testing found some examples of journals that were not authorised at the time of posting. Some classes of journal are authorised in bulk after posting, as part of the year-end timetable and processes, although the actual authorisation was not available to view.

- 5.5.8** To further improve the efficiency and effectiveness of the journal transfer authorisation process, management may wish to consider removing the authorisation requirement for individual journals and replace this with monthly management review and authorisation of material journal postings only. This is considered an effective risk-based authorisation process which focuses on detection of only material transfers made in error.
- 5.5.9** There isn't a de-minimis value set for journal transfers and management may wish to consider the cost/ benefit of posting low value journals.
- 5.5.10** It is advised that journal transfers are made using a fully digital process, removing the option of scanned and emailed hand-written journals where possible.
- 5.5.11** A defined email authorisation from the responsible manager is a robust control. It is advised that the addition of 'cut and paste' signatures for authorisation should be avoided because they can be easily copied by non-authorisers.

Recommendation 4 – Review the journal authorisation process

- 5.5.12** Debtors and creditors control account reconciliations are carried out daily. A monthly supervisory review and authorisation of the daily reconciliations is recorded. Further debtors and creditors control account reconciliations in an alternative format are recorded monthly, although management are currently reviewing the requirement to do so moving forward. It is advised this review is concluded.

Appendix A – Management Action Plan

Summary of Recommendations and agreed actions					
Recommendations	Priority	Risk Exposure	Agreed Action	Responsible Manager	Implementation Date
Recommendation 1 – Further align resource transfers to the financial procedure rules	M	Inappropriate virements are made without suitable consideration and authorisation.	Further details will be provided on budget adjustments to ensure they align to a relevant Financial Procedure Rule	Head of Financial Services	30/09/22
Recommendation 2 – Review document management arrangements for the financial guide	M	Staff error due to lack of direction on how to carry out financial processes.	Any policies and procedures that are used in finance will be reviewed but consideration of resource requirements and potential moves to new processes under LGR will be taken	Head of Financial Services	31/03/23
Recommendation 3 – Reinstate the monthly bank reconciliation supervisory review and authorisation	M	Bank reconciliation errors may not be identified in a timely manner.	The monthly bank reconciliation review will be reinstated	Head of Financial Services	30/09/22
Recommendation 4 – Review the journal authorisation process	M	Journal errors may not be identified in a timely manner.	The current journal authorisation process will be reviewed to determine whether email authorisation provides greater control than attaching electronic signatures	Head of Financial Services	30/09/22

Appendix B – Advisory Comments

Ref	Advisory Comment
5.3.1	All staff guidance covering key processes to be held centrally as part of the financial guide. Proportionality of content review should be considered due to Local Government Reorganisation.
5.4.1	Head of Financial Services and/ or the Accountancy Services Manager to confirm the appropriateness of user access, following receipt of a periodic overview report. Review timeliness of financial system access removal.
5.5.1	Management to consider the risk that due to low attendance on financial processes training, budget managers may not have received the required direction to manage their budgets effectively. Consideration to be given to alternative training platforms for financial processes training (Skill Gate for example), enabling self-study at a convenient time and location.
5.5.3	Management may wish to consider the cost/ benefit of providing explanations for all budget variances.
5.5.4	If a variance explanation is given, it should always include the reasons why they are over or under budget, as an alternative to stating they are over or under budget.
5.5.5	Management may wish to consider if the forecast full year actual spend could be further improved by offering budget holders the opportunity to adjust the balance of remaining budget where they feel this may not accurately reflect known spending pressures for the remainder of the financial year.
5.5.8	Consider removing the authorisation requirement for individual journals and replacing this with monthly management review and authorisation of all journal postings, sorted by materiality.
5.5.9	Consider setting a de minimis value for journal transfers.
5.5.10	Consider making the journal transfer process fully digital.
5.5.11	Cut and paste signatures for journal authorisation should be avoided because they can be copied easily by non-authorisers.
5.5.12	The review of the requirement for additional monthly debtors and creditors control reconciliations should be concluded.

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).