



Internal Audit Report
Chief Executive's Service
Report Number – 09/007
Treasury Management
May 2010

Final Report

Finance Division
Chief Executive's Service
Perth & Kinross Council
2 High Street
Perth PH1 5PH

Internal Audit Report

Background and Introduction

This audit was carried out as part of the approved audit plan for 2009/2010 with the audit testing carried out during October and November 2009.

The Council's Chief Executive's Service Finance Division Treasury Management team are based at 2 High Street, Perth and are responsible for managing the Council's cash flow position and capital funding requirements including the related borrowing and lending with a range of external organisations.

The Council's 12 Treasury Management Practice documents (TMP's) and related policies and procedures are aligned to the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management in Public Services.

The Head of Finance submits compliance monitoring reports in respect of Treasury Management activities to the Strategic Policy and Resources Committee (SP&R). The compliance and monitoring reports include reporting against Prudential Indicators in respect of Treasury Management activities.

Acknowledgements

Internal Audit acknowledges with thanks the co-operation of Treasury Management staff during this audit.

Control Objectives and Opinions

This section describes the purpose of the audit and summarises the results. A 'control objective' is a management objective that requires the maintenance of adequate and effective internal controls to ensure that it is achieved. Each control objective has been given a rating describing, on the basis of the audit work done, the actual strength of the internal controls found to be in place. Areas of good or poor practice are described where appropriate.

Control Objective: To ensure the Council's Treasury Management Policy and practices comply with the CIPFA Code of Practice on Treasury Management in Public Services.

Auditor's Comments: Audit testing confirmed the Council's Treasury Management policies and procedures comply with the CIPFA Code of Practice on Treasury Management in Public Services. However the contents of, Treasury Management Practice 4 require to be reviewed and amended to ensure there is clarity concerning the permitted types of investment instrument and counterparty.

Reviews of the Council's Treasury Management policies and practices are carried out by the Treasury Management team as required, subject to a minimum annual review. However, the manual, which contains hard copies of the Treasury Management Policies and practices, is only updated as part of the annual review process and not as changes occur. More frequent updates would be beneficial to take account of changes as would the introduction of a version control system.

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Strength of Internal Controls:	Moderately Strong
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Control Objective: To ensure Treasury Management transactions are correct, properly authorised, recorded, reconciled and held securely.	
<p>Auditor's Comments: The value of four of fifteen investment transactions tested by the Auditor were found to exceed Treasury Management dealing limits. Also, while the Approved Lending & Investment Policy and a Prudential Indicator states no investment period can exceed 364 days; one investment transaction tested was for a period of 365 days. These breaches of compliance were not identified and the transactions were therefore not reported as breaches in the 2008/09 Annual Treasury Compliance Report made to SP&R in September 2009 or any of the SP&R Quarterly Treasury Activity and Compliance Reports.</p> <p>In addition the Auditor was unable to confirm the validity of some historic investments. because Treasury Management staff overtype 'Approved Investment Counterparties' List details as changes occur resulting in a loss of management trail.</p>	
Strength of Internal Controls:	Moderate

Control Objective: To ensure there is regular reporting and compliance monitoring of Treasury Management activities.	
<p>Auditor's Comments: Audit testing confirmed there is regular monitoring of the Council's cashflow position by the Treasury Management team who monitor large or recurring payments or income and ensure funds are invested in the optimum manner.</p> <p>There is regular compliance monitoring of Prudential Indicators, Treasury Policies and Limits and reporting to SP&R. The reporting, however, does not make it clear that compliance with all of the Council's 12 TMP's is included within the report, in accordance with CIPFA guidance.</p>	
Strength of Internal Controls:	Moderately Strong

Management Action and Follow-Up

Responsibility for the maintenance of adequate and effective internal controls rests with management.

Where the audit has identified areas where a response by management is required, these are listed in Appendix 1, along with an indication of the importance of each 'action point'. Appendix 2 describes these action points in more detail, and records the action plan that has been developed by management in response to each point.

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It is management's responsibility to ensure that the action plan presented in this report is achievable and appropriate to the circumstances. Where a decision is taken not to act in response to this report, it is the responsibility of management to assess and accept the risks arising from non-implementation.

Achievement of the action plan is monitored through Internal Audit's 'follow up' arrangements.

Management should ensure that the relevant risk profiles are reviewed and updated where necessary to take account of the contents of Internal Audit reports. The completeness of risk profiles will be examined as part of Internal Audit's normal planned work.

Feedback

Internal Audit welcomes feedback from management, in connection with this audit or with the Internal Audit service in general.

Distribution

This report has been distributed to:

B Malone, Chief Executive;

J Irons, Depute Chief Executive

I Innes, Head of Legal Services;

J Symon, Head of Finance;

S MacKenzie, Chief Accountant;

P Dickson, Complaints & Governance Officer;

M Kay, Senior Committee Officer;

External Auditor.

Authorisation

The auditor for this assignment was D McCreadie. The supervising auditor was D Farquhar.

This report is authorised for issue:

Jackie Clark
Chief Internal Auditor
Date: 24 May 2010

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Appendix 1: Summary of Action Points

No.	Action Point	Risk/Importance
1	Documented Treasury Management Routines	Low
2	Treasury Management Practices	Low
3	Non Compliance with Lending Policy	Medium
4	Approved Counterparty Lists	Medium
5	Monitoring of Treasury Management Practices	Low
6	Treasury Management Dealing Limits	Medium
7	Reconciliation of Treasury Management Records	Low
8	Independent Review of Treasury Management	Medium
9	Temporary Borrowing Record	Low

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Appendix 2: Action Plan

Action Point 1 - Documented Treasury Management Routines

A Treasury Management Practices (TMP) and procedures manual is maintained by the Service. Changes to the manual are approved as required by SP&R, however the Service update the manual on an annual basis and not when SP&R approve changes. The last update to the manual was in November 2008 with the 2009 annual review being progressed during the time of the audit.

The failure to update the manual as changes occur means parts of the manual are out of date, for example the manual includes an outdated Policy for Local Temporary Loans and also an outdated Approved Lending and Investment Policy. Updates to these documents were approved by SP&R in February and June 2009. respectively

Some sections of the manual were more than a year out of date, for example a section referring to a bank contract which expired in March 2008. The Service advised the failure to update this section was already known to require review.

The lack of version control does not facilitate identification of changes made, the person authorising changes, nor the date changes made.

Management Action Plan

The Treasury Management Practices and Procedures Manual will in future be updated in light of changes to Treasury Policies as they are approved by SP&R. Changes to working practices will also be reviewed as they occur.

A comprehensive annual review will still be undertaken each November.

A version control system for the Treasury Management Practices and Procedures Manual will therefore also be introduced.

Importance:	Low
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	Copy of version control record.

Auditor's Comments

Satisfactory

Action Point 2 - Treasury Management Practices

Audit testing revealed an inconsistency between Treasury Management Practice (TMP) Schedule 4.1 'Treasury Management Techniques' and the Approved Lending & Investment Policy (Schedule 4.6 of the same TMP).

The TMP Schedule 4.1 'states that the Council is limited to using the following 'instruments' for investing surplus funds:

Government Stocks & Bonds

Temporary Deposits – Other UK Local Authorities

Temporary Deposits – UK Clearing Banks and subsidiaries

Temporary Deposits – UK Building Societies

However, the Approved Lending & Investment Policy does not permit the option of investing in Government Stocks and Bonds but contrary to Schedule 4.1, does permit investing with Foreign Banks and Institutions. The Service accepted the need for clarity and stated that the Policy deliberately does not permit investing in Government Stocks and Bonds, although the Council has the statutory powers to do so.

Without clear Policies there is a risk of misinterpretations or inconsistencies.

Management Action Plan

The Treasury Management Practice (TMP) Approved Lending & Investment Policy TMP 4.6 will be reviewed to be fully aligned with TMP 4.1. The result will be the updated TMP 4.1 will include the option for the Council to invest in Foreign Banks and Institutions.

Importance:	Low
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	Copy of revised TMP 4.1 which is aligned to TMP 4.6.

Auditor's Comments

Satisfactory

Action Point 3 - Non Compliance with Lending Policy

Audit testing of a sample of fifteen investment transactions revealed four instances where investments were made in excess of the Treasury Management staff dealing limitations detailed in the 'Treasury Management Daily Limitations to Authority' list. The Service stated these transactions were carried out by a temporary member of staff who did not seek the appropriate retrospective authority.

Also, one amount was invested for 365 days which contravenes the Approved Lending & Investment Policy and a Prudential Indicator which states no investment period can exceed 364 days. The Service stated this was due to a clerical error by the counterparty which was not corrected when checking the investment confirmation letter.

None of the above were reported in the 2008/09 Annual Treasury Compliance Report made to SP&R in September 2009 or any of the Quarterly Treasury Activity and Compliance Reports as the Service was not aware of the breaches.

Management Action Plan

Although the 4 breaches of daily dealing limits were due to a temporary member of staff, all staff will, however be reminded of their daily dealing limits, and the need to seek authorisations where required.

The Service will also remind the Treasury Management Clerical Assistant that the accuracy of third party confirmations need to be carefully checked and they must notify Treasury Management staff immediately of any queries or discrepancies.

Importance:	Medium
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	Copy of reminder to staff.

Auditor's Comments

Satisfactory

Action Point 4 - Approved Counterparty List

The Approved Counterparties List specifies those organisations with which the Council funds can be invested. Treasury Management staff maintain lists by overtyping existing lists as changes occur.

The lack of a management trail detailing changes to such lists prevented the Auditor from checking 4 of 15 sampled investments to ensure they were with approved counterparties at the time the funds were invested.

Management Action Plan

The Service will ensure that previous versions of Approved Counterparty Lists are in future retained for a period of 13 months. These lists will be kept to provide supporting evidence that deals were made in accordance with the prevailing criteria, thereby providing a full audit trail.

Importance:	Medium
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	Copy of a superseded Approved Counterparty List.

Auditor's Comments

Satisfactory

Action Point 5 - Monitoring of Treasury Management Practices

The Council's Statement of Accounts states that the Council has fully adopted CIPFA's Code of Treasury Management Practices (TMP's). The Code of Practice states that an organisation should report 'on any circumstances of non-compliance with the organisation's Treasury Management Policy statement and TMP's'.

Audit testing revealed that whilst there is regular compliance monitoring and reporting of Prudential Indicators, Treasury Policies and Limits to SP&R, the reporting makes no reference to the Council's 12 TMP's.

The Service stated that whilst the reporting did not specifically refer to TMP's, the monitoring and reporting of these activities was being undertaken.

Management Action Plan

Treasury Management will amend the wording in Compliance and Monitoring reports to ensure the Compliance section wording is clear and explicitly refers to the reporting against all of the Council's Treasury Management Policies and Practices.

Importance:	Low
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	SP&R Compliance Report showing reporting against all TMP's.

Auditor's Comments

Satisfactory

Action Point 6 - Treasury Management Dealing Limitations

There are processes in place for limitations to the authority of individual officers to enter in to deals and these are documented within the TMPs.

There is scope for improvement in the monitoring and review of deals entered into by Treasury Management staff.

Management Action Plan

The daily Transaction Listing Sheet, which details all counterparty deals entered into, will be reviewed daily by the Corporate Accounting Manager. The sheet will be endorsed to confirm that the deals are within the dealing limitations, in accordance with the approved counterparty list or if outside the limitations of authority, that the deal has been appropriately countersigned.

TMPs will be updated to reflect this enhanced control.

Importance:	Medium
Responsible Officer(s):	A O'Brien, Corporate Accounting Manager
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	June 2010
Required Evidence of Completion:	Endorsed daily Transaction Listing sheet and updated procedure.

Auditor's Comments

Satisfactory

Action Point 7 - Reconciliation of Treasury Management Records

The TMP 'Treasury Management Segregation of Duties' state that 'The Treasury Management Officer reconciles the financial accounting ledger to the Council's records on a monthly basis. These reconciliations are then reviewed and checked by the Senior Accountant'

Audit testing of six reconciliations revealed there was no consistent approach to evidence compliance with the TMP, or noting the action taken to resolve differences highlighted as a result of the reconciliation exercise.

The Service advised that whilst the reconciliations had been carried out, they acknowledged that the monthly reconciliation sheets were not always signed as evidence. The Service also advised that the Senior Accountant review is usually undertaken by reviewing two months' reconciliations at the same time.

Management Action Plan

The Service will remind the Treasury Management Officer that any action taken to investigate and resolve differences highlighted as a result of the reconciliation exercise should be noted on the monthly reconciliation sheets which should also be signed and dated to evidence completion of the exercise.

The Senior Accountant review of the reconciliations will take place every month. Procedures will be updated to reflect the above changes.

Importance:	Low
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Completed
Required Evidence of Completion:	Updated reconciliation procedure.

Auditor's Comments

Satisfactory

Action Point 8 - Independent Review of Treasury Management

The Treasury Management Officer and Senior Accountant review Treasury Management activities. However, there is no regular independent periodical review of these treasury decisions, and activities.

The lack of any independent check of routines may mean that errors and/or inaccurate reporting may go unnoticed.

Management Action Plan

The Head of Finance will nominate an appropriate officer who will carry out regular independent and documented reviews of treasury decisions and activities. These checks will include items such as reviewing random deals to Counterparty limits and checking that timely reconciliations are taking place.

Importance:	Medium
Responsible Officer(s):	J Symon, Head of Finance
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	June 2010
Required Evidence of Completion:	Extract evidencing independent review of treasury activities.

Auditor's Comments

Satisfactory

Action Point 9 - Temporary Borrowing Record

Audit testing of a sample of five Treasury Management temporary borrowings highlighted one case where the Treasury Management recorded a borrowing of £37,689.33 differed from the £37,296.36 record shown on the record maintained by the Central Accounting Team.

The Service indicated that the difference of £392.97 was historic being at least ten years old and most likely caused by accrued interest.

Management Action Plan

The Service will arrange for a journal adjustment of £392.97 to be processed in 2009/2010 to increase the value of the Charities Account spreadsheet record maintained by the Central Accounting Team. This action will ensure that the Central Accounting record and the Treasury Management record both agree, going forward these records will be compared and agreed each year.

Importance:	Low
Responsible Officer(s):	J Jennings, Senior Accountant
Lead Service:	Chief Executive's
Date for Completion (Month / Year):	Complete
Required Evidence of Completion:	Copy of Central Accounting Record and Treasury Record both showing £37,689.33.

Auditor's Comments

Satisfactory

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