



## INTERNAL AUDIT REPORT



### TREASURY MANAGEMENT 2016/17

<b>Issue Date:</b>	3 <sup>rd</sup> November 2016	<b>Issued to:</b>	Simon Riley	Head of Finance and Corporate Services and S151 Officer
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# TREASURY MANAGEMENT 2016/17

## EXECUTIVE SUMMARY

### 1. INTRODUCTION AND INTERNAL AUDIT OPINION

The Treasury Management function at Harborough District Council (HDC) is delivered in house by the Finance Services Team. The Council's Treasury Management Strategy (TMS) complies with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management in Public Services. The Strategy is subject to annual Council approval and is supported by a set of Treasury Management Practices (TMPs), which were under review at the time of the audit. Treasury management activity is reported at the appropriate level and within the agreed timescales.

The Council's estimated longer term debt portfolio stood at £1.49m as at 1<sup>st</sup> April 2016 and no short term borrowing has been made during the financial year to date. The Council's investment priorities are *security* first, *liquidity* second, followed by *return*. Sample testing of 15 treasury management investment transactions confirmed 100% compliance with all of the expected controls.

Whilst documented procedures are not currently in place for the treasury management reconciliation process; sample testing confirmed that overall, appropriate controls are in place and operating effectively.

The Council has insurance cover in place but a copy of the Insurance Policy Schedule was not held on file to confirm that appropriate fidelity insurance cover was held for officers engaged in treasury management activities.

The Council has appointed external treasury management advisors to provide advice and guidance with regards to minimising costs of borrowing and maximising returns on investments. The Council are required to achieve £92k income on investments during 2016/17. A review confirmed that net income of £38,128 had been achieved on investments as at 31st July 2016, a favourable variance of 24% when compared to the original budget.

Based on these findings, the framework of controls currently in place provide **Substantial Assurance** that the identified risks have been appropriately mitigated. Detailed findings are set out in section 2. The assurance opinion is based upon testing of the design of controls to manage the identified risks and testing to confirm the extent of compliance with those controls, as summarised in the table below:

Internal Audit Assurance Opinion	Direction of Travel				
	N/A				
	Risk	Design	Comply	Recommendations	
H				M	L
<b>Risk 1: Non-compliance with statutory and regulatory requirements and best practice guidance</b>	Substantial	Substantial	0	0	1
<b>Risk 2: Loss of monies</b>	Sufficient	Substantial	0	1	0
<b>Risk 3: Inaccurate, incomplete or untimely transactions and record keeping</b>	Substantial	Sufficient	0	0	1
<b>Risk 4: Failure to achieve appropriate financial returns on investments</b>	Substantial	Substantial	0	0	0
<b>Total Number of Recommendations</b>			<b>0</b>	<b>1</b>	<b>2</b>



## 2. SUMMARY OF FINDINGS

### **Risk 1: Non-compliance with statutory and regulatory requirements and best practice guidance**

The Council identifies legislation and best practice relevant to treasury management. Part 4(6) of the Council's Constitution (Financial Procedure Rules) was last updated in February 2014 and states that the Council has adopted the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice for Treasury Management in Public Services. The Treasury Management Strategy (TMS) and Prudential Indicators for 2016/17 were approved by Council on 22<sup>nd</sup> February 2016 and cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, Communities and Local Government (CLG) Minimum Revenue Provision (MRP) Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

The accompanying report that was presented to Council on 22<sup>nd</sup> February 2016 confirmed that the Treasury Management Practices (TMPs), which govern treasury decisions, documentation, reporting and governance arrangements, were currently being reviewed and updated. It was proposed that the TMPs be reviewed by the Governance and Audit Committee in detail to ensure full compliance with the Code of Practice. At the time of the audit, the TMPs were still under review, however, a copy of the draft TMPs were provided to Internal Audit for information purposes.

The Council's estimated longer term debt portfolio stood at £1.49m as at 1<sup>st</sup> April 2016 and no short term borrowing has been made during the financial year to date. Review of the draft TMPs confirmed that processes applicable to the borrowing function and detailed guidance on how borrowing decisions are made have been documented accordingly. TMP 5.2 (Statement of Duties / Responsibilities of Treasury Staff) confirms that the Section 151 Officer has delegated powers to make the most appropriate form of borrowing from the approved sources. Prior to entering into any lending, it is the responsibility of the Section 151 Officer to be satisfied, by reference to the Council's legal services department and external advisors as appropriate, that the proposed transaction does not breach any statute, external regulation or the Council's Financial Regulations. The Council's TMS is reviewed, updated and approved annually and the draft TMPs were under review at the time of the audit, with the next review due to take place in 2018.

Documented procedures are not currently in place for the treasury management reconciliation process, however, Internal Audit review confirmed that investment records are reconciled to the general ledger on a monthly basis and long term loan records (PWLB) are reconciled to the general ledger at year-end.

**Recommendation 1** addresses this finding.

Roles and responsibilities in relation to treasury management are formally documented and assigned to individual officers. In addition, all officers involved in treasury management are able to access the relevant legislation, regulations and policies and all have appropriate qualifications and experience relevant to their role. The Council's treasury management advisors (Capita Asset Services) hold various courses annually to accommodate the training requirements of staff involved in the treasury management function, as well as those involved at the strategic level.

Treasury management activity is reported to Council in a Mid-Year Treasury Management Report and following the financial year-end, the Annual Treasury Report. Treasury management activity is also reported to the Corporate Management Team (CMT) on a regular basis.

Following a recommendation from the 2016/17 Financial Resilience audit, it was agreed that opportunities would be taken to identify Members financial training needs to effectively scrutinise budget performance and financial governance. Treasury Management training is due to take place during 2016/17 and this was confirmed with the



Head of Finance and Corporate Services / S151 Officer. This action will continue to be followed up as part of the standard Internal Audit process and no further recommendation has been made.

Based upon these findings, the assurance rating for the controls in respect of this risk is **Substantial Assurance**.

### **Risk 2: Loss of monies**

The Council's investment priorities are *security* first, *liquidity* second, followed by *return*. In accordance with the guidance from the CLG and CIPFA, and in order to minimise the risk to investments, the Council has clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list.

The Council applies the creditworthiness service provided by Capita Treasury Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies (Fitch, Moody's and Standard and Poor's). The creditworthiness service monitors potential counterparty ratings on a real time basis with knowledge of any changes issued electronically to the Council. If a downgrade results in a counterparty no longer meeting the Council's minimum criteria, its further use as a new investment will be withdrawn immediately. It was confirmed that it had not been necessary to remove any approved institutions from the Counterparty List during this financial year.

The Council recognises that ratings should not be the sole determinant of the quality of an institution and that it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The aim of the strategy is to generate a list of highly creditworthy counterparties which will also enable diversification and thus avoid undue concentration of risk. The intention of the strategy is to provide security of investment and minimisation of risk. A counterparty list is in place to provide information with regards to approved institutions and the maximum amount and period of investments.

Transactions between the Council's bank account and that of approved institutions are processed via CHAPS. It was confirmed that appropriate controls are in place for these transactions, whereby independent approval for all payments is required. All relevant sources of information are reviewed on a daily basis to ensure that maturing investments, including interest, are received accurately and at the correct time. Furthermore, it was confirmed that interest in relation to the Council's long term loans (PWLb) was paid by direct debit on a monthly basis.

Sample testing of 15 treasury management investments confirmed that in all cases:

- A daily banking sheet had been completed by an appropriate officer and authorised at the appropriate level;
- Investments were within the limits of the TMS (value / duration) and were invested with an approved, creditworthy counterparty;
- Interest due had been calculated accurately;
- Authorised confirmation letters issued from HDC to the relevant counterparty were held on file;
- Third party (broker / counterparty) confirmations were held on file;
- All monies owed (principal / interest) were received in full and at the correct time; and
- An appropriate audit trail was held on file.

A copy of the Crime Insurance Proposal Form and a corresponding invoice were held on file, and whilst appropriate fidelity insurance cover was detailed within both documents, a copy of the Insurance Policy Schedule was not held on file to confirm that appropriate fidelity insurance cover was in place for officers engaged in treasury management



activities. It was however noted, that the invoice in relation to the 2016/17 fidelity insurance cover was paid by BACS on 15<sup>th</sup> July 2016. **Recommendation 2** addresses this finding.

Based upon the audit findings, the assurance rating for the design of controls in respect of this risk is **Sufficient Assurance** and the rating for compliance with these controls is **Substantial Assurance**.

**Risk 3: Inaccurate, incomplete or untimely transactions and record keeping**

A cash flow forecast is prepared at the beginning of the financial year to take account of all major sources of income and items of expenditure. Cash flow monitoring is undertaken to determine the availability of surplus cash for investment or the need to take short term borrowing. It was noted that no short term borrowing had been undertaken during the financial year to date. The forecast cleared balances are obtained via HSBCnet on a daily basis and when the cash flow projections indicate a surplus cash balance, funds are invested with approved institutions as detailed on the counterparty list. A daily bank sheet is completed and authorised and all relevant details are recorded in the Temporary Loan Investments spreadsheet. Investment records are reconciled to the general ledger on a monthly basis to ensure that all transactions are accurate and complete.

Sample testing confirmed that overall, appropriate controls are in place and operating effectively to manage the risks associated with the treasury management reconciliation process. It was noted however, that the April and May 2016 investment reconciliation paperwork had not been signed to confirm that an independent review had taken place. In addition, the year-end reconciliation in relation to long term loans (PWLB) had not been formally reviewed by an independent officer, it was however confirmed that the Head of Finance and Corporate Services / S151 Officer had carried out ad hoc reviews of the accounts and working papers and no issues were identified during audit sample testing. **Recommendation 3** addresses these findings.

Based upon the audit findings, the assurance rating for the design of controls in respect of this risk is **Substantial Assurance** and the rating for compliance with these controls is **Sufficient Assurance**.

**Risk 4: Failure to achieve appropriate financial returns on investments**

The Council recognises the value of employing external providers of treasury management services in order to acquire access to specialist skills and resources. Capita Asset Services, Treasury Solutions are the Council's external treasury management advisors and are able to provide the Council with advice and guidance with regards to minimising its costs of borrowing and maximising returns on its investments.

The overarching objective behind the Council's Medium Term Financial Strategy (MTFS) is to ensure that the Council's financial resources are applied in a manner which achieves the strategic priorities set out in the Corporate Delivery Plan. The MTFS 2016/17 – 2019/20 refers to the Council's approach to treasury management and its objective of making the Council less risk averse and more risk aware in order to improve the return on the available funds. Appropriate strategies are in place to communicate the Council's risk based approach with regards to borrowing and investments.

The Council's capital expenditure plans are one of the key drivers of treasury management activity. This is reflected within the TMS and Prudential Indicators for 2016/17 which were formally approved by Members on 22<sup>nd</sup> February 2016. The treasury management function ensures that the Council's cash is organised in accordance with the relevant codes of practice, so that sufficient cash is available to meet the capital investment plans.

This involves both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities.



The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. The Council are required to achieve £92k income on investments during 2016/17. The results of this indicator will be reported in the Annual Treasury Report after the end of the financial year, and performance is monitored on a regular basis by CMT. A review confirmed that net income of £38,128 had been achieved on investments as at 31<sup>st</sup> July 2016, a favourable variance of 24% when compared to the original budget.

Based upon these findings, the assurance rating for the controls in respect of this risk is ***Substantial Assurance***.

### **3. LIMITATIONS TO THE SCOPE OF THE AUDIT**

This is an assurance piece of work and an opinion is provided on the effectiveness of arrangements for managing only the risks specified in the Audit Planning Record.

The Auditor's work does not provide any guarantee against material errors, loss or fraud. It does not provide absolute assurance that material error, loss or fraud does not exist.

### **4. ACTION PLAN**

The Action Plan in Appendix 1 provides a number of recommendations to address the findings identified by the audit. If accepted and implemented, these should positively improve the control environment and aid the Council in effectively managing its risks.



**APPENDIX 1**

**Action Plan**

Rec No.	ISSUE	RECOMMENDATION	Management Comments	Priority	Officer Responsible	Due date
1	<p>Documented procedures are not currently in place for the treasury management reconciliation process.</p> <p>There is a risk that staff may potentially carry out inaccurate, inefficient and inconsistent working practices if documented procedures are not in place.</p>	<p>Documented procedures should be in place for the treasury management reconciliation process to ensure that efficient working practices are applied consistently and to provide appropriate resilience (business continuity).</p>	<p>The Audit evidenced that investment records are reconciled to the general ledger on a monthly basis and long term loan records (PWLB) are reconciled to the general ledger at year-end. It is proposed that as part of the formal adoption of the draft Treasury Management Practices (TMPs) that documented processes are captured and subsequently subject to the same review process as the TMPs</p>	Low	Head of Finance and Corporate Services and S151 Officer	31 <sup>st</sup> March 2017

Rec No.	ISSUE	RECOMMENDATION	Management Comments	Priority	Officer Responsible	Due date
2	<p>A copy of the Insurance Policy Schedule was not held on file to confirm that appropriate fidelity insurance cover was in place for officers engaged in treasury management activities. It was noted however, that the invoice in relation to the 2016/17 fidelity insurance cover was paid by BACS on 15<sup>th</sup> July 2016.</p> <p>The Insurance Policy Schedule should provide confirmation that appropriate cover is in place to indemnify the Council from financial loss resulting from fraud.</p>	<p>A copy of the Insurance Policy Schedule should be retained on file to confirm that appropriate fidelity insurance cover is in place for this financial year.</p>	<p>This will be actioned</p>	<p>Medium</p>	<p>Financial Services Manager</p>	<p>30<sup>th</sup> December 2016</p>
3	<p>The April and May 2016 investment reconciliation paperwork had not been signed to confirm that an independent review had taken place.</p> <p>In addition, the year-end reconciliation in relation to long term loans (PWLB) had not been formally reviewed by an independent officer.</p> <p>There is a risk that errors and / or irregularities may go undetected if an independent review is not carried out on the treasury management reconciliation process.</p>	<p>All treasury management reconciliations should be reviewed accordingly, after which they should be signed to confirm that an appropriate management check has been undertaken.</p>	<p>Formal sign off process of independent review will be actioned</p>	<p>Low</p>	<p>Financial Services Manager</p>	<p>30<sup>th</sup> June 2017</p>



## Glossary

### The Auditor's Opinion

The Auditor's Opinion for the assignment is based on the fieldwork carried out to evaluate the design of the controls upon which management rely and to establish the extent to which controls are being complied with. The table below explains what the opinions mean.

Level	Design of Control Framework	Compliance with Controls
<b>SUBSTANTIAL</b>	There is a robust framework of controls making it likely that service objectives will be delivered.	Controls are applied continuously and consistently with only infrequent minor lapses.
<b>SUFFICIENT</b>	The control framework includes key controls that promote the delivery of service objectives.	Controls are applied but there are lapses and/or inconsistencies.
<b>LIMITED</b>	There is a risk that objectives will not be achieved due to the absence of key internal controls.	There have been significant and extensive breakdowns in the application of key controls.
<b>NO</b>	There is an absence of basic controls which results in inability to deliver service objectives.	The fundamental controls are not being operated or complied with.

### Category of Recommendations

The Auditor prioritises recommendations to give management an indication of their importance and how urgent it is that they be implemented. By implementing recommendations made managers can mitigate risks to the achievement of service objectives for the area(s) covered by the assignment.

Priority	Impact & Timescale
<b>HIGH</b>	Management action is imperative to ensure that the objectives for the area under review are met.
<b>MEDIUM</b>	Management action is required to avoid significant risks to the achievement of objectives.
<b>LOW</b>	Management action will enhance controls or improve operational efficiency.