



## **FINAL REPORT**

### **Internal Audit Report**

Corporate Services Department

### **Review of Creditors 2007/08**

November 2007

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## **1. BACKGROUND**

- 1.1 The Creditors Section which is based at Campbeltown within the Corporate Services Department, ICT & Financial Services, receives invoices from all Council departments for processing. The Section processes about 12,000 invoices monthly and around 150,000 in a full year.
- 1.2 The Creditors Section relies heavily on the operations carried out by departmental creditor staff under the direction of local management. To assist with this process a user manual was issued for guidance to all departments by the Creditors Section to be effective from April 2005 describing in detail the accounts payable procedures.
- 1.3 The Creditors Supervisor meets with all Departments annually to discuss and find solutions to any operational problems. The Creditors Supervisor also occasionally attends Education Service, Administration & Financial Assistants (AFA) meetings, whilst his assistant deals with DMR (Devolved Management of Resources) problems.
- 1.4 A review of the Creditors Section was last carried out as part of the 2005/2006 Internal Audit Programme.
- 1.5 The 2005/2006 audit concentrated on establishing whether departments were complying with the procedures set out in the user manual referred to above. Also some work was carried out on the introduction of the Professional Electronic Commerce Online System (Pecos).
- 1.6 This year's audit review has concentrated on issues raised during a meeting recently held between the Creditors Supervisor and Internal Audit.
- 1.7 Various creditor issues were discussed and the Supervisor's opinion obtained as to any difficulties or problems needing to be addressed with regard to each issue.
- 1.8 These issues were then considered by the Audit Manager and an audit programme drafted.
- 1.9 This audit programme was then agreed with the Creditors Supervisor before the audit commenced.

## **2. AUDIT SCOPE AND OBJECTIVES**

The broad objectives of the review were to test departmental Creditor operations, to ensure that the issues raised by the Creditors Supervisor were being addressed in a satisfactory manner by the Creditors Section and/or by departments. The matters raised and tested were:-

- Authorisation Procedures;
- Authenticated Receipts Procedures;
- PECOS procedures in advance of the Internal Audit/KPMG joint audit;
- Problems with Departments;
- Statutory PI Procedures;
- Urgent Payment Procedures;

- Suppliers' Master File;
- C.I.S. Deductions;
- Discounts Allowed;
- Ledger Coding; and
- Duplicate Payments.

The adequacy of the arrangements to meet the objectives has been assessed using a grading of one to five ticks (✓ 's). Five ticks indicate that good arrangements are in place, and one tick that inadequate arrangements are in place. The assessments are set out in section 6.2 (Figure 1). The assessments have been made by considering the value and significance of the findings and recommendations.

### **3 AUDIT APPROACH**

The following approach was used to satisfy the objectives of the audit;

- An Audit Agreement Document (AAD) was prepared and forwarded to the Creditors Supervisor for his agreement. The Agreement set out the main objectives of the audit approach and scope.
- An interview was arranged then with the Creditors Supervisor to agree the AAD before commencing the audit.
- Relevant testing was then completed.
- A draft report was prepared and a copy passed to the Creditors Supervisor, the Exchequer Manager and the Head of ICT & Financial Services for comment and agreement. After comments were received the report was amended as appropriate and copies of the final report issued to all Directors, relevant Heads of Service and all Finance Managers and other designated staff for their attention and action.
- The final report includes an action plan, which lists all agreed actions and a copy has been provided to the Chief Executive.

### **4 SUMMARY OF MAIN FINDINGS**

The overall conclusion is that the Creditors Supervisor and his staff have a sound understanding of the creditors systems and that they work together in a professional manner to achieve the section's objectives.

The main findings and conclusions shown against each of the 11 areas tested are set out below. Detailed findings to back up the conclusions are shown at Appendix 1.

#### **4.1 Authorisation Procedures**

The Creditors Supervisor is satisfied that his staff are finding that the lists of Authorised Signatories kept in the Creditors section are now easier to access and use, and that the checking of signatories is working to his reasonable satisfaction. Nevertheless there a number of matters that arose from the audit.

- The responsibility for ensuring that authorisation of all invoices within a batch lies with the batch authoriser and all batch authorisers must be totally aware of this responsibility. Audit has been assured by the Finance Managers that this is the case.

- In order to improve control the Creditors Supervisor should consider carrying out spot checks on a sample of batches incorporating invoices under £10K and report any errors found to the Exchequer Manager. Separate procedures are in place already to authorise all invoices valued in excess of £10K. The Creditors Supervisor says that “as no errors have been identified over the years the system has been operating and to begin these random checks would not be cost effective”. Internal Audit has noted this as an area for checking next year.
- The Creditors Section would benefit from the availability of up to date spreadsheet lists of authorised signatories prepared by each Department. These, in the main, are already available (Operational Services and Community Services have such lists). It is recommended that all Departments prepare spreadsheet lists of current authorised signatories and make them available on the Council’s public folders. The lists should be password controlled and updated on a regular basis.
- The Creditors Section has commenced the compilation of a list of all known authorised signatories for the whole Council. From the departmental lists already available it is replicating the data on a spreadsheet which shows details of levels and values that staff are authorised to sign for. A page number is also shown which matches to a page in a folder which shows the actual signature. This is expected to be completed by 31 March 2008 and will be a valuable asset to the section when it is in place.
- Copies of authorised signatory signatures should not be available on the public folders.

#### **4.2 Authenticated Receipts (AR)**

- The system for controlling the receipt of AR is operating well, but could be improved by deciding on the best course of action to follow in the event of stopped payments to the contractor not having the desired effect i.e. AR still not forwarded to the Council. It is recommended any contractor who fails to supply AR after payments are stopped should be reported to the Revenue. The Creditors Supervisor says that “he doesn’t accept this point as experience has shown that there has only ever had cause to stop payments to a couple of suppliers and there is no legal requirement to make contact with HMRC”.

#### **4.3 PECOS**

- The Creditors Supervisor has recently met with the PECOS management and is now less concerned about PECOS processes ;
- There is a facility for further meetings between the Creditors Supervisor and Pecos management to sort out problems;
- It is planned for the DMR system to be replaced in schools by the Pecos system within the near future;
- Internal Audit feels that the cessation of the DMR system and its replacement by PECOS within the timescales planned will, in view of the problems to be resolved, be difficult to achieve, but that once Education

Services are fully using PECOS its use throughout the Council will roll out much quicker;

- In view of the savings which should arise from the use of PECOS it is important therefore that the timescales set for the replacement of the DMR system are achieved as far as is possible.
- In order to assist this process regular meetings will be required between the various key staff involved in implementing the changes i.e. Creditors, PECOS and School Administration and Accountancy staff;
- As the process rolls on the Creditors Supervisor will be required to issue purchase cards to all Primary Schools as needed. The issue and control of these purchase cards will require careful scrutiny by audit. Internal Audit has noted this matter for inclusion in a future audit programme.

#### **4.4 Problems with Departments**

- The Creditors Supervisor said there were no major problems with particular departments;
- He visits each Department annually to discuss any problems with the payments system both from his point of view and the clients;
- He keeps notes of the meetings and follows up all agreed actions. These notes are handwritten and rather informal. It is recommended that more formal notes of these meetings are kept by the Creditors Supervisor.

#### **4.5 Statutory PIs**

- Audit has concluded that the system is well controlled. However, it was noticed that PECOS payments were included within Corporate Services statistics and also that clothing grants were incorporated into Community Services. It is felt that the information to management would be improved if these statistics were separately shown. It is recommended therefore that the Exchequer Manager considers presenting the PI statistics to managers in a form which reflects these matters.

#### **4.6 Urgent Payments**

- There were no matters to report here.

#### **4.7 Suppliers Master file**

- The supplier/ creditor master file register currently includes data which is superfluous or out of date. To enable the register to be cleared of this unnecessary data there is to be an upgrade to Oracle and testing by Strategic Finance and Creditors. The upgrade is expected to be in place by the end of November 2007.
- A purge of the file will be then carried out to be completed by the end of March 2008. The Creditors Supervisor has pointed out that that a similar exercise is carried out every few years.

- It is important that this upgrade and purge is carried out within the indicated timescales.

#### **4.8 CIS Deductions**

- The current deductions are relatively immaterial amounts. There is however the possibility that the deductions will increase in the future. The Creditors Supervisor has commented that "although the amounts involved are relatively minimal the legislation must be adhered to and that processes adopted must be fool-proof to prevent any possibility of incurring penalties. Internal Audit has therefore noted this matter for future audit.

#### **4.9 Discounts Allowed**

- There is no clear issue regarding discounts allowed from PECOS invoices but, it may be worthwhile for Internal Audit in conjunction with KPMG to review this further.

#### **4.10 Ledger Coding**

- The Creditors Supervisor has reported that inactive ledger codes can cause his section difficulties. This can occur for example if a cheque needs to be reversed but the original ledger code has been withdrawn by Strategic Finance. He asked if anything could be done to assist.
- Strategic Finance has agreed to pass the Creditors Supervisor details of any future codes withdrawn and to continue to press ICT for an electronic solution.

#### **4.11 Duplicate Payments**

- The Creditors Supervisor has indicated that duplicate payments are not a material problem and that the system is set up to identify payments for investigation before a payment is made;
- Presented to internal audit was an example of a potential duplicate payment which fitted into that category and was picked up by the system before payment was made;
- This was an invoice from a consultant engineer passed for payment by the Operational Services Department. It has raised the question as to how such an invoice was passed by the department for payment and how to prevent a similar occurrence in the future;
- The "duplicate" payment appears to have been a one off event arising from an error by the consultants. The Principal Engineer agreed that his procedures could be improved to prevent a similar occurrence in the future and that he needed to amend his procedures. He is to amend his computer software accordingly.

### **5 ACTION PLAN**

- 5.1 The action plan attached at Appendix 2 has been compiled with the co-operation and agreement of the Head of ICT and Financial Services, and the Creditors Supervisor. All other officers named in the Action Plan have also been consulted.

- 5.2 It is the consideration of Internal Audit that, in an effort to improve the quality of financial information, monitoring and control, the recommendations should be implemented in accordance with the agreed action plan. Management have set achievable implementation dates and will be required to provide reasons to the Audit Committee for failure to implement within the agreed timescale. Where management decide not to implement recommendations it must evaluate and accept the risk associated with this decision.
- 5.3 A system of grading audit findings, which have resulted in an action, has been adopted in order that the significance of the findings can be ascertained. Each finding is classified as fundamental, material or minor. The definition of each classification is set out below: -

<p><b>Fundamental</b> - major observations on high level controls and other important internal controls. Significant matters relating to factors critical to the success of the objectives of the system. The weakness may therefore give rise to loss or error;</p>
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<p><b>Material</b> - observations on less important internal controls, improvements to the efficiency and effectiveness of controls which will assist in meeting the objectives of the system and items which could be significant in the future. The weakness is not necessarily great, but the risk of error would be significantly reduced if it were rectified;</p>
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<p><b>Minor</b> - minor recommendations to improve the efficiency and effectiveness of controls, one-off items subsequently corrected. The weakness does not appear to affect the ability of the system to meet its objectives in any significant way.</p>
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## 6 OVERALL CONCLUSION AND ASSESSMENT AGAINST OBJECTIVES

- 6.1 Despite the weaknesses identified, the payments procedures appear to be operating satisfactorily. However, during the course of the audit, areas were identified as requiring improvement and therefore, various recommendations have been made. These have been discussed with management and an action plan agreed. Any issues not accepted by management are done so with their knowledge and acceptance of risk and control weakness.



6.2 Figure 1 below sets out a summary of the overall conclusions arising from the audit in terms of the specific objectives detailed at section 2.

**Figure 1: Summary of overall conclusions**

<b>Specific objectives</b>	<b>Assessment</b>
Authorisation Procedures	✓✓✓✓
Authenticated Receipts	✓✓✓✓
PECOS.	✓✓✓✓
Problems with Departments	✓✓✓✓
Statutory PIs	✓✓✓✓
Urgent Payments	✓✓✓✓
Suppliers Master file	✓✓✓
CIS Deductions	✓✓✓✓
Discounts Allowed	✓✓✓✓
Ledger Coding	✓✓✓✓
Duplicate Payments	✓✓✓✓
<b>Key:</b> ✓✓✓✓✓ - Arrangements accord with good practice and are operating satisfactorily. ✓✓✓✓ - Arrangements accord with good practice, but certain minor matters noted as requiring improvement. ✓✓✓ - Adequate arrangements in place, but certain matters noted as requiring improvement. ✓✓ - Arrangements in place offer scope for substantial improvement. ✓ - Concern is expressed about the adequacy of the scope of these arrangements	

## 7 ACKNOWLEDGEMENTS

7.1 Thanks are due to the Exchequer Manager and the Creditors Supervisor and his section, for their assistance during the audit and the preparation of the report and action plan.

7.2 Argyll & Bute Council's Internal Audit section has prepared this report. Our work was limited to the objectives set out in paragraph 2 of this report. We cannot be held responsible or liable if information material to our task was withheld or concealed from us, or misrepresented to us.

7.3 This report is private and confidential for the Council's information only and is solely for use in the provision of an internal audit service to the Council. The report is not to be copied, quoted or referred to, in whole or in part, without prior written consent.

**APPENDIX 2  
 ACTION PLAN**

<b>ACTION PLAN NO</b>	<b>PARAGRAPH</b>	<b>GRADE</b>	<b>WEAKNESSES IDENTIFIED</b>	<b>AGREED ACTION</b>	<b>RESPONSIBLE OFFICER</b>	<b>DATE OF IMPLEMENTATION</b>
1	App.1 Para 1	Material	Creditors Section would benefit from the availability on the Councils Public Folders of an up to date spreadsheet list of authorised signatories from each Department. These are in the main already available. (Operational and Community Services have such lists)	The Creditors Section is to prepare spreadsheet lists of current authorised signatories and make them available on the Council's public folders. The lists should be password controlled and updated on a regular basis.	Creditors Supervisor	31 March 2008
4	App. 1 Para 7	Material	The Supplier/ Creditor master file register currently includes data which is superfluous or out of date.	There is to be an upgrade to Oracle and testing by Strategic Finance and Creditors. The upgrade is expected to be in place by the end of October 2007. A purge of the file will be then carried out to be completed by the end of March 2008.	Creditors Supervisor and Senior Accounting Assistant Corporate Accounting	31 March 2008