

Cumbria Shared Internal Audit Service  
Internal Audit Report for Cumbria OPCC and Cumbria Constabulary



## Audit of Treasury Management

Draft Report Issued: **27th March 2020**

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## Audit Resources

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## Audit Report Distribution

For Action:	Michelle Bellis (Deputy Chief Finance Officer) Lorraine Holme (Financial Services Manager)
For Information:	Roger Marshall (Joint Chief Finance Officer)
Audit Committee	The Joint Audit Committee which is due to be held on 28 May 2020 will receive the report.

**Commented [BM1]:** This meeting is likely to be cancelled and moved to June TBC

*Note: Audit reports should not be circulated wider than the above distribution without the consent of the Audit Manager.*

### Cumbria Shared Internal Audit Service



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## Executive Summary

### 1. Background

- 1.1. This report summarises the findings from the audit of Treasury Management. This was a planned audit assignment which was undertaken in accordance with the 2019/20 Audit Plan. This review forms part of a rolling programme of financial system audits which ensures that all main financial systems are independently reviewed on a regular basis.
- 1.2. The Chartered Institute for Public Finance and Accountancy (CIPFA) defines treasury management as “*the management of the organisation’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks*”.
- 1.3. It is important that treasury activities are managed properly, in a way that balances risk with return, but with the prime consideration being given to the security of the capital sums involved.
- 1.4. The Commissioner has adopted the CIPFA Code of Practice on Treasury Management, and is required to approve an annual Treasury Management Strategy Statement in accordance with CIPFA Code of Practice on Treasury Management. The Strategy must also incorporate an Investment Strategy as required by the Local Government Act 2003. Together, both these strategies cover the financing and investment strategy for each financial year.

### 2. Audit Approach

#### 2.1. Audit Objectives and Methodology

- 2.1.1. 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. A risk based audit approach has been applied which aligns to the five key audit control objectives which are outlined in section 4; detailed findings and recommendations are reported within section 5 of this report.

## 2.2. Audit Scope and Limitations

2.2.1. The Audit Scope was agreed with management prior to the commencement of this audit review. The Client Sponsor for this review was the Deputy Chief Finance Officer. The agreed scope of the audit was to provide assurance over management's arrangements for governance, risk management and internal control in the following areas:

- Compliance with and communication of the treasury management strategy
- Investments made in line with the treasury management policy
- Transactions approved in accordance with the treasury management policy

2.2.2. There were no instances whereby the audit work undertaken was impaired by the availability of information:

## 3. Assurance Opinion

3.1. Each audit review is given an assurance opinion and these are intended to assist Members and Officers in their assessment of the overall level of control and potential impact of any identified system weaknesses. There are 4 levels of assurance opinion which may be applied. The definition for each level is explained in **Appendix A**.

3.2. From the areas examined and tested as part of this audit review, we consider the current controls operating within Treasury Management 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. Summary of Recommendations, Audit Findings and Report Distribution

4.1. There are three levels of audit recommendation; the definition for each level is explained in **Appendix B**.

4.2. There are two audit recommendations arising from this audit review and these can be summarised as follows:

Control Objective	No. of recommendations		
	High	Medium	Advisory
1. <b>Management</b> - achievement of the organisation's strategic objectives	-	-	-
2. <b>Regulatory</b> - compliance with laws, regulations, policies, procedures and contracts (see section 5.1.)	-	1	1
3. <b>Information</b> - reliability and integrity of financial and operational information	-	-	-
4. <b>Security</b> - safeguarding of assets	-	-	-
5. <b>Value</b> - effectiveness and efficiency of operations and programmes	-	-	-
<b>Total Number of Recommendations</b>	-	1	1

4.3. **Strengths:** The following areas of good practice were identified during the course of the audit:

- There is an approved Treasury Management Strategy in place that defines the policies and objectives of the Police and Crime Commissioner's Treasury Management activities. This is reviewed on an annual basis and provides transparency on the Commissioner's approach to investment and borrowing activity and on the arrangements in place to mitigate treasury management risks.
- Treasury Management Practice Schedules, which follow the guidance in CIPFA's Code of Practice for Treasury Management, have been prepared to accompany the Strategy and provide a more detailed description of the Commissioner's expectations in relation to treasury management activity.
- The Treasury Management Practice Schedules, also reviewed annually, identify the risks associated with treasury management activities and set out the day to day arrangements in place to ensure they are controlled. This includes details on the delegation of responsibilities, separation of duties, reviewing and reporting of treasury management activities.
- The day to day management of the treasury management activity has been delegated to the Deputy Chief Finance Officer who oversees the work carried out by the Financial Services Team.
- The Financial Services Team, are provided with a copy of the updated Treasury Management Strategy and Treasury Management Practice Schedules following their review each year. Copies of the documents are also readily available on the Team's shared network drive.
- Only authorised users have access to the Bankline systems and access controls are in place within the system.

- There is a clear separation of duties between the dealers and the releasers on Bankline ensuring that at least two individuals are involved in payments to third parties and inter account transfers.
- Weekly treasury activity reports are provided to the DCFO for review. The reports, which provide a summary of the daily cash balances for the week, a cashflow summary for the current financial year, interest due and received on investments placed in the year and details of outstanding investments are signed off as evidence of review.
- Cash liquidity is managed on a daily basis, ensuring sufficient funds are available as required whilst maximising investment of surplus funds.
- A cashflow forecast is maintained for a rolling 12 month period. This includes known income elements, such as that due for precepts or interest on maturing investments and estimated monthly expenditure in respect of major costs for payroll and creditors.
- The credit worthiness of counterparties is monitored on an ongoing basis in conjunction with the Commissioner's treasury management advisors (Link Asset Services) who provide timely updates and advice on the standing of counterparties. This service uses a risk weighted scoring system model based on ratings from the three main rating agencies - Fitch, Moodys and Standard and Pools.
- Investments are made with approved Counterparties in accordance with the limits set by the Treasury Management Strategy.
- Quarterly reports on treasury management activity are prepared in order to provide assurance to the Commissioner and Joint Audit Committee that prudential indicators have been complied with and that transactions have been carried out in line with the Treasury Management Strategy.

4.4. **Areas for development:** Improvements in the following areas are necessary in order to strengthen existing control arrangements:

4.4.1. *High priority issues:*

- None identified

4.4.2. *Medium priority issues:*

- For the sample of investments selected for audit testing there was no evidence retained that:
  - a) The DCFO had approved investments made for periods greater than three months, as is required by the Treasury Management Practice Schedule 5.
  - b) Any independent approval had been obtained by the Dealer to roll over an existing investments for a further period of six months.

4.4.3. *Advisory issues:*

- The copy of the Treasury Management Practice Schedules published on the OPCC website related to 2018-19.

**Comment from the Joint Chief Finance Officer**

*I am pleased that the audit has overall revealed continuing strengths in this inherently risky area of financial activity. From personal experience I do believe that senior finance staff are consulted regarding longer term investment decisions, but fully accept the recommendation and response from the Deputy Chief Financial Officer that this needs to be more formally documented. I also note the DCFO's under taking to update the Treasury Management Practices.*

## Management Action Plan

### 5. Matters Arising / Agreed Action Plan

5.1. **Regulatory** - compliance with laws, regulations, policies, procedures and contracts.

● **Medium priority**

Audit finding	Management response
<p><b>(a) Authorisation of Investments</b></p> <p>The Treasury Management Practice Schedules (TMPS) set out various responsibilities in terms of investments. This includes for example:</p> <ul style="list-style-type: none"> <li>• That the approved dealers have the delegated power to enact transactions within the constraints of the TMPS and the limits laid down within the Counterparty Selection Criteria and approved Counterparty list. (TMP 5)</li> <li>• That each treasury deal transacted via the Bankline system can be authorised by Financial Services Officers. (TMP 5)</li> <li>• That the Deputy Chief Finance Officer (DCFO) will oversee and approve investments made for periods greater than three months. (TMP 5)</li> </ul> <p>Audit testing was carried out on a sample of investments made over the last 12 months and our results identified that all investments were made with approved counterparties and were within the limits set.</p> <p>Six of the investments selected were for a period of more than three months. For those examined, there was no evidence that the DCFO had given approval prior to the investment being made. This included one £2M investment that was 'rolled over' for a further six month period. For this particular deal, in addition to there being no evidence of approval by the DCFO there was no evidence that the arrangements to extend the deal were subject to scrutiny and review.</p> <p>Discussions held at the time of the audit indicated that the DCFO approval was generally obtained</p>	<p><b>Agreed management action:</b></p> <p>Although verbal permission is obtained from the Deputy CFO in these cases, it is appreciated that this does not constitute an audit trail. In future a new procedure will be put in place whereby an email will be sent to either the Deputy CFO or Joint CFO to seek approval for investments over 3 months in duration. The responding approval will be retained as part of the audit trail. The same principle will be applied to the rolling over of investments and email approval obtained and retained for audit purposes.</p>



<p>via a discussion between the Financial Services Manager – Treasury and the DCFO. As a result there was no evidence of her approval.</p>	
<p><b>Recommendation 1:</b> To ensure that management can demonstrate that the authorisation requirements set out in the Treasury Management Practice Schedules are being complied with, arrangements should be in place to retain evidence of the DCFO's approval of investments that exceed three months.</p> <p>Management should also consider how to demonstrate that approval to rollover existing investments has been given and by whom.</p>	
<p><b>Risk exposure if not addressed:</b></p> <ul style="list-style-type: none"> <li>• Unable to demonstrate compliance with the Treasury Management Strategy and Practices.</li> <li>• Inappropriate investment decisions are taken which may result in cashflow problems.</li> </ul>	

Responsible manager for implementing:  
**Deputy Chief Finance Officer**  
Date to be implemented:  
**27 March 2020 (completed)**

• **Advisory issue**

Audit finding	Management response
<p><b>(b) Publication of Treasury Management Practice Schedules</b> Treasury Management Practice Schedules have been prepared and are reviewed on an annual basis. Evidence that the TMPS for 2019-20 had been presented to the Commissioner at the Public Accountability Conference and to Joint Audit Committee was recorded in minutes of their meetings.</p> <p>It was noted as part of audit testing that the copy of the TMPs published on the Police and Crime Commissioners website was the 2018-19 version. The site had not been updated with the 2019-20 copy of the procedures.</p>	<p><b>Agreed management action:</b> The publishing of the 2019/20 Treasury Management Practices (TMPs) was an omission. The TMPs for 2020/21 have been finalised and will be uploaded to the PCC website.</p>
<p><b>Recommendation 2:</b></p>	

Arrangements should be in place to ensure that the most recently approved Treasury Management Practice Schedules are uploaded to the OPCC website on a timely basis.	
Risk exposure if not addressed: <ul style="list-style-type: none"><li>Lack of transparency</li></ul>	Responsible manager for implementing: <b>Deputy Chief Finance Officer</b> Date to be implemented: <b>30 March 2020 (completed)</b>

## Audit Assurance Opinions

There are four levels of assurance used; these are defined as follows:

	Definition:	Rating Reason
<b>Substantial</b>	There is a sound system of internal control designed to achieve the system objectives and this minimises risk.	<p>The controls tested are being consistently applied and no weaknesses were identified.</p> <p>Recommendations, if any, are of an advisory nature in context of the systems and operating controls &amp; management of risks.</p>
<b>Reasonable</b>	There is a reasonable system of internal control in place which should ensure that system objectives are generally achieved, but some issues have been raised which may result in a degree of risk exposure beyond that which is considered acceptable.	<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 developed.</p> <p>Recommendations are no greater than medium priority.</p>
<b>Partial</b>	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 which have been identified and the level of non-compliance and / or weaknesses in the system of internal control puts the system objectives at risk.	<p>There is an unsatisfactory level of internal control in place as controls are not being operated effectively and consistently; this is likely to be evidenced by a significant level of error being identified.</p> <p>Recommendations may include high and medium priority matters for address.</p>
<b>Limited / None</b>	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-compliance with basic controls which leaves the system open to error and/or abuse.</p> <p>Control is generally weak/does not exist. Recommendations will include high priority matters for address. Some medium priority matters may also be present.</p>

## 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 three levels of audit recommendations used; high, medium and advisory, the definitions of which are explained below.

Definition:		
<b>High</b>	●	Significant risk exposure identified arising from a fundamental weakness in the system of internal control
<b>Medium</b>	●	Some risk exposure identified from a weakness in the system of internal control
<b>Advisory</b>	●	Minor risk exposure / suggested improvement to enhance the system of control

### Recommendation Follow Up Arrangements:

- High priority recommendations will be formally followed up by Internal Audit and reported within the defined follow up timescales. This follow up work may include additional audit verification and testing to ensure the agreed actions have been effectively implemented.
- Medium priority recommendations will be followed with the responsible officer within the defined timescales.
- Advisory issues are for management consideration.