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Mr Bryan Smail
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Municipal Buildings
West Bridge Street
Falkirk
FK1 5RS

12 June 2015

Dear Bryan

**Falkirk Council 2014/15
Review of Systems of Internal Control**

Audit Scotland's Code of Audit Practice requires us to assess the systems of internal control put in place by management. In carrying out this work, we seek to gain assurance that Falkirk Council:

- has systems for recording and processing transactions which provide a sound basis for the preparation of financial statements and the effective management of its assets and interests
- has systems of internal control which provide an adequate means of preventing and detecting material misstatement, error, fraud or corruption
- complies with established policies, procedures, laws and regulations.

The purpose of this review was to evaluate whether the internal controls operating within the main financial systems are adequate so as to enable us to place reliance on them when forming an opinion on the 2014/15 financial statements. It should be highlighted that these reviews were restricted to the key controls in place to meet our audit objectives for each system.

In accordance with *International Standard on Auditing (ISA) 330: the auditor's response to assessed risk* paragraphs 14 and 15 our audit judgements are based on current year testing of controls and, where appropriate, prior year results.

Auditing standards require external and internal auditors to work closely together to make optimal use of available audit resources, therefore we seek to rely on the work of internal audit wherever possible.

The following table summarises the main financial systems that were tested during 2014/15. It also identifies those where we are placing reliance on prior years' testing and those where we have placed formal reliance on internal audit work to avoid duplication of effort:

System	External audit testing in 2014/15	Reliance on prior year audit work	Reliance on aspects of internal audit work in 2014/15
General ledger		✓	
Payroll	✓		✓
Capital accounting		✓	✓
Cash and cash equivalents		✓	
Treasury management		✓	
Trade receivables	✓		
Trade payables (including corporate procurement cards)		✓	
Council tax billing and collection	✓		
Non-domestic rates billing & collection			✓
Housing rents		✓	

Note - internal audit findings do not feature in this letter and are reported separately to management.

Audit Findings

Overall, we have concluded that the key controls within the council's main financial systems are operating satisfactorily. Where controls have not been tested or where the evidence of a control's effective operation does not exist, we will adjust our planned coverage of the financial statements to obtain sufficient evidence that they are free of material misstatement.

Based on the audit work we carried out we did not identify any areas exposed to significant risk. However, there are some areas where there is scope for improvement and these are included in the action plan agreed with management which accompanies this management letter.

A number of other minor issues were also identified and notified to management during the course of our audit work but these do not feature in this letter.

Follow-up of 2013/14 internal controls management letter

We also followed up the issues reported to management in 2013/14 to ensure that progress has been made in implementing the agreed actions. Of the 13 issues and risks reported last year, we have identified 2 instances (payroll related) where the action is either outstanding or the action taken has not led to improvement. These issues have been included in the 2014/15 action plan and we will continue to monitor progress in these areas. Additionally, work on the formal review of non-domestic rates charity relief cases is in progress.

Management Action

The weaknesses identified in this management letter are only those that have come to our attention during the course of our normal audit work and, therefore, are not necessarily all the weaknesses that may exist.

Although we have identified a number of areas for improvements to the systems of internal control, it is the responsibility of management to decide on the extent of the internal control systems appropriate to Falkirk Council. We would stress, however, that an effective system of internal control is an essential part of the efficient management of any organisation.

The matters included in the action plan at Appendix 1 have been agreed with management.

Acknowledgement

The contents of this management letter have been agreed with relevant officers to confirm factual accuracy. The co-operation and assistance we received during the course of our audit is gratefully acknowledged.

Yours sincerely

Jim Rundell
Senior Audit Manager

Cc:

- Mary Pitcaithly, Chief Executive
- Ian Renton, HR Systems & Payroll Manager
- Paul Ferguson, Revenues Manager
- Amanda Templeman, Acting Deputy Chief Finance Officer
- Karen Algie, Head of HR and Customer First
- Gordon O'Connor, Internal Audit Manager

Falkirk Council 2014/15

Review of Systems of Internal Control

Action Plan

Key Risk Areas and Planned Management Action

Ref	Audit issue, risk and recommendation	Management action/response	Responsible officer / Target date
Payroll			
1	<p>Payroll validation: Upon review of the employee validation procedures carried out by payroll section it was noted that Development, Social Work, Roads, and Education Services had not submitted their January validation returns. This represents a significant proportion of the Council workforce, and includes services where staff turnover might be expected to be relatively high, thus increasing potential for error. Also the control spreadsheet which payroll maintain to record the monthly returns received from services has not been kept up to date.</p> <p>Risk: Increased risk of inaccurate or fraudulent payments being processed, and of payments being made to individuals who have left the council's employment.</p> <p>Recommendation: As a key control over ensuring that payments are made only to valid employees, validation checks should be carried out as scheduled and responses monitored. It should be re-emphasised to service managers that response to these validation checks is mandatory.</p> <p>Also reported in 2013/14.</p>	<p>Since completion of the Audit, confirmation has been received that the January reports for Development, Roads and Social Work have been checked.</p> <p>A new follow up procedure will be introduced in response to this recommendation. The reports will continue to be issued monthly and will be subject to a 6 week follow up by the Payroll Officer and a further follow up 4 weeks later. The requirement to provide confirmation of checking forms part of the financial regulations. If confirmation has not been received following these two reminders, the breach of financial regulations will be reported to the Chief Finance Officer (or his delegate) for further action.</p> <p>It should be noted that a system of electronic delivery of these reports is being developed and is expected to be implemented for the 2016/17 financial year. The means of confirmation will be reviewed and agreed with Internal Audit as part of this change.</p>	<p>HR Systems & Payroll Manager</p> <p>30 September 2015</p> <p>30 April 2016</p>

Ref	Audit issue, risk and recommendation	Management action/response	Responsible officer / Target date
2	<p>Overpayments: Prior to April 2015, each payroll officer was responsible for monitoring overpayments to staff within their own payroll group. This was done via notes held on employee's individual files. However, no formal monitoring process was in place which could track all overpayments made. A new control spreadsheet has been introduced for 2015/16 which will record all overpayments in one location, but will capture only those overpayments occurring from April 2015 onward.</p> <p>Risk: Overpayments are not fully recovered.</p> <p>Recommendation: The council wide monitoring system should include all previously recorded overpayments so that a total opening recoverable balance can be established. Subsequent overpayments and recoveries should be reflected in the new system to derive an ongoing balance for total overpayments recoverable.</p>	<p>It should be noted that although the procedures have been reviewed and improved in relation to overpayments, the responsibility placed on Payroll Officers (and indeed on Payroll Team Leaders) to monitor overpayments remains unchanged from the position prior to April 2015.</p> <p>The recommendation to assimilate overpayments recorded under the previous monitoring arrangements is not accepted. We are satisfied that whilst improvements could and have been made, the arrangements in place previously are sufficient to ensure that the overpayments that existed are being recovered in accord with Council Policy without implementing this recommendation.</p>	Ongoing Monitoring by HR Systems & Payroll Manager
3	<p>Reconciliation of payroll to financial ledger:</p> <p>(i) It has not been normal practice to produce a formal monthly reconciliation for net pay, as is the case for NI, PAYE and other payroll adjustments.</p> <p>(ii) We noted that reconciliations carried out for NI, PAYE, etc did not appear to have been independently checked.</p> <p>Risk: Errors/mispastings are not detected timeously, and will likely require significant staff resource to correct at a later date.</p> <p>Recommendation: Produce formal</p>	<p>A more formalised procedure for reconciliation of the net pay accounts will be implemented.</p> <p>Although this matter was reported in 2013/14, it was agreed that this would be reviewed together with Internal Audit. That review concluded that it would not be necessary for the in-year reconciliations to be independently checked and countersigned but that the final reconciliations for the year</p>	HR Systems & Payroll Manager 30 September 2015

Ref	Audit issue, risk and recommendation	Management action/response	Responsible officer / Target date
	<p>quarterly net pay reconciliations, subject to review and authorisation by a senior officer, with all other payroll reconciliations also subject to independent review.</p> <p>Also reported in 2013/14.</p>	<p>would be signed off, as has in fact happened for 2014/15 subsequent to the visit from External Audit.</p>	
Accounts receivable			
4	<p>Invoices for amounts less than £20:</p> <p>From discussion with Revenues officers we have established that the council issues a large number of very small invoices (less than or equal to £20) across all services.</p> <p>Risk: The administrative cost of raising these invoices and pursuing non payment may exceed the amounts recovered.</p> <p>Recommendation: Consideration should be given to reviewing the underlying costs of invoicing and credit control, and possible application of a minimum charging policy to ensure that recovery of administrative costs is maximised.</p>	<p>Given the increasing move towards charging for services we are promoting pre-payment where possible and limit invoicing to where this is not possible or practical.</p> <p>The current cost per invoice (including recovery) is around £2-£3 on average. However for unpaid invoices the default recovery action (Court action and/or referral to sheriff officers) may not be appropriate for lower value debts. We have a high number of regular Social Work invoices at around £13.00 so will introduce a £10 minimum and then review based on feedback from services.</p>	<p>Revenues Manager £10 limit in place from 2/6/15.</p>
5	<p>Debts greater than 6 years old:</p> <p>Within the total for accounts receivable there is a significant balance of overdue invoices outstanding for more than 6 years (around £240k excluding Falkirk Community Stadium Ltd).</p> <p>Risk: These long outstanding amounts cannot be collected.</p> <p>Recommendation: Provision should be made for non recovery of debts where there is no likelihood of any meaningful amount being repaid.</p>	<p>Some debts have had more recent activity which means they are not prescribed (and recovery therefore can be enforced), but in 2014/15 we were aware that debts that were not recommended by us to services were written-off (due to being prescribed). We have spoken with the appropriate staff within the area(s) involved and would expect this to be remedied in</p>	<p>Revenues Manager 31 March 2016</p>

Ref	Audit issue, risk and recommendation	Management action/response	Responsible officer / Target date
		<p>2015/16.</p> <p>The bad debt provision does already allow for the non-collection of these debts.</p>	
Council tax billing and collection			
6	<p>Empty property verification: From a review of a sample of empty property visit reports, a small number were noted where the result of the visit had been inconclusive, but there was no indication as to subsequent confirmation of the property status.</p> <p>Risk: Discount continues to be allowed on a non qualifying property.</p> <p>Recommendation: Procedures for inspection of void/empty properties should include an audit trail which evidences the subsequent resolution of any initially unsatisfactory property visit.</p>	<p>Where a visit has been undertaken we would generally have documentary evidence on file, but with immediate effect we will introduce a secondary stage where we cannot inspect through an unannounced visit.</p> <p>We will telephone/write to liable person to arrange a date and time to visit. If we receive no response we will remove the relief (until a visit can be carried out).</p> <p>This work will be carried out within our compliance team.</p>	<p>Revenues Manager</p> <p>30 September 2015</p>
Treasury management			
7	<p>Treasury management policy: The council's treasury management policy has not been updated to reflect changes in regulations which now allow councils to lend to registered social landlords.</p> <p>Risk: Although no such transactions have occurred, nor are any envisaged currently, if the situation arose where this became relevant the policy issue could cause delays, or could result in claims of irregularity.</p> <p>Recommendation: Treasury management policy should be updated at the next opportunity, in order that any future transactions of this nature can be accommodated.</p>	<p>Our Treasury Management Practices will be updated to reflect this amendment. We will also include it in our Interim Strategy Report that is presented to the Executive Committee for review and thereafter is referred onto Council for Approval.</p>	<p>Capital & Treasury Manager</p> <p>Treasury Management Practices updated by 31 July 2015.</p> <p>Interim Strategy Review Report to Executive in November 2015 will include amendment.</p>