

Government and Public Sector
Internal Audit Services

Northampton Borough Council Internal Audit Report 2010-11 Bank Reconciliations Review

Report No. 10_11 NBC 09 – Final Report

Assurance rating this review	High Assurance
Assurance rating previous review	Moderate Assurance

Distribution List

Bill Lewis – Head of Finance
Isabell Procter – Director of Finance and Support
Matthew Lee – Exchequer Team Leader
Phil Morrison – Finance Manager
Audit Committee

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Background and scope

Introduction

The bank reconciliations review was undertaken as part of the 2010/11 Internal Audit plan agreed by the Audit Committee.

This report has been prepared solely for Northampton Borough Council in accordance with the terms and conditions set out in our contract dated 1st January 2007. We do not accept or assume any liability or duty of care for any other purpose or to any other party. This report should not be disclosed to any third party, quoted or referred to without our prior written consent.

Background

This review was undertaken as part of the Core Financial Systems audit work included within the 2010/11 Internal Audit Plan. This review considered controls and processes in place with regards to bank reconciliations as at the time of our internal audit fieldwork, which took place during November 2010.

Approach and Scope

Approach

Our work is designed to comply with Government Internal Audit Standards [GIAS] and the CIPFA Code.

Scope

In accordance with our Terms of Reference (Appendix 1), agreed with the Finance Manager and the Head of Finance, we undertook a limited scope audit of bank reconciliations.

This limited scope audit involved a review of the design of the key controls together with detailed testing to determine whether the controls are operating in practice.

Limitations of scope

The scope of our work was limited to those areas identified in the terms of reference.

Staff involved in this review

We would like to thank all client staff involved in this review for their co-operation and assistance.

Name of client staff

Matthew Lee – Exchequer ~~Team~~ Leader
Angela Litchfield - Accountant - Corporate Team
Jenny Coombes – Reconciliation Officer

Our opinion and assurance statement

Introduction

This report summarises the findings of our review of bank reconciliations.

Each of the issues identified has been categorised according to risk as follows:

Risk rating	Assessment rationale
●● Critical	<p>Control weakness that could have a significant impact upon, not only the system, function or process objectives but also the achievement of the Authority's objectives in relation to:</p> <ul style="list-style-type: none"> • the efficient and effective use of resources • the safeguarding of assets • the preparation of reliable financial and operational information • compliance with laws and regulations.
● High	<p>Control weakness that has or is likely to have a significant impact upon the achievement of key system, function or process objectives.</p> <p>This weakness, whilst high impact for the system, function or process does not have a significant impact on the achievement of the overall Authority objectives.</p>
● Medium	<p>Control weakness that:</p> <ul style="list-style-type: none"> • has a low impact on the achievement of the key system, function or process objectives; and/or • has exposed the system, function or process to a key risk, however the likelihood of this risk occurring is low.
● Low	<p>Control weakness that does not impact upon the achievement of key system, function or process objectives; however implementation of the recommendation would improve overall control.</p>

Summary of Findings

Our detailed findings and recommendations are set out in the findings and recommendations section of this report. The table below summarises the number of findings raised and the priority rating assigned.

Risk Rating	Number of findings
Critical	0
High	0
Medium	0
Low	2
Total	2

Opinion

We are required to provide an opinion on the adequacy and effectiveness of internal control in relation to the area under review. Our opinion is based on the work performed as set out in the agreed terms of reference and is subject to the inherent limitations set out in the limitations and responsibilities section of this report. We also provide an assurance statement for the area under review.

Design of the controls under review

We identified 1 weakness in the design of controls in relation to bank reconciliations. This weakness has been assessed as low risk. In our opinion, this weakness is not likely to have a significant impact on the achievement of the key objectives of the bank reconciliations process.

Operation of the controls under review

We identified 1 instance where the controls were not operating as designed in practice at the time of our audit. This weakness has been assessed as low risk. Based upon the sample testing we performed, in our opinion this weakness is not likely to have a significant impact on the achievement of the key objectives of bank reconciliations.

Value for Money

During our review we did not identify any specific value for money issues.

Assurance statement

High Assurance

Our work found some low impact control weaknesses which, if addressed would improve overall control. However, these weaknesses do not affect key controls and are unlikely to impair the achievement of the objectives of the system. Therefore we can conclude that the key controls have been adequately designed and are operating effectively to deliver the objectives of the system, function or process

Detailed findings and recommendations

Our detailed findings and recommendations are set out in the findings and recommendations section of this report. Management responses are included which identify actions to be taken, responsibility and timeframe.

Follow-up

The table below summarises the recommendations made during our 2009/10 review of bank reconciliations and their current status.

Risk Rating	Number of findings	Implemented or no longer relevant	Outstanding or partially implemented
Critical	0	0	0
High	0	0	0
Medium	3	2	1
Low	2	1	1
Total	5	3	2

A follow-up review of all the agreed actions should be undertaken as part of the 2011/12 internal audit plan.

Limitations and responsibilities

Limitations inherent to the internal auditor's work

We have undertaken the review of bank reconciliations, subject to the following limitations.

Internal control

Internal control, no matter how well designed and operated, can provide only **reasonable** and not absolute assurance regarding achievement of an organisation's objectives. The likelihood of achievement is affected by limitations inherent in all internal control systems. These include the possibility of poor judgement in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

Future periods

The assessment of controls relating to bank reconciliations is that historic evaluation of effectiveness is not relevant to future periods due to the risk that:

- the design of controls may become inadequate because of changes in operating environment, law, regulation or other; or
- the degree of compliance with policies and procedures may deteriorate.

Responsibilities of management and internal auditors

It is management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.

We shall endeavour to plan our work so that we have a reasonable expectation of detecting significant control weaknesses and, if detected, we shall carry out additional work directed towards identification of consequent fraud or other irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected.

Accordingly, our examinations as internal auditors should not be relied upon solely to disclose fraud, defalcations or other irregularities which may exist, unless we are requested to carry out a special investigation for such activities in a particular area.

Findings and recommendations

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Management response	Officer responsible & implementation date
Control Design						
1	Lack of documentation of current processes may leave the Authority exposed if key individuals were to leave.	The bank reconciliation guides are not regularly reviewed and therefore may not fully represent working practices.	<ul style="list-style-type: none"> Low 	<p>The bank reconciliation guides should be reviewed and updated to reflect current practices where necessary.</p> <p>In addition consideration should be given to including the following:</p> <ul style="list-style-type: none"> procedure for dealing with unrepresented cheques and when these should be written off time limit for completing bank reconciliations after month end 	<p>We are in the process of updating our guides, this is an ongoing process due to the bank change to HSBC.</p> <p>Unrepresented cheques that are over 6 months old are followed up as part of the bank reconciliation, by the reconciliation officers.</p> <p>Procedure will be reviewed</p> <p>Time limit for completion of all bank reconciliations at month end is within 7 working days of the period end. This deadline is monitored against on the Monitoring of all reconciliations spreadsheet held in Finance</p>	<p>Dawn Perryman Ongoing</p> <p>Dawn Perryman 30th January 2011</p>

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Management response	Officer responsible & implementation date
Operating effectiveness						
2	<p>Lack of audit trail demonstrating preparation of reconciliations.</p> <p>Reconciliations are not supported by appropriate documentation.</p>	<p>Through testing a sample of 3 reconciliations for each bank account the following exceptions were noted:</p> <ul style="list-style-type: none"> The July 2010 Special Interest Account reconciliation had not been signed as prepared. The July 2010 Credit Suspense Account reconciliation had not been signed as prepared. The September 2010 Special Interest Account reconciliation had a cashbook balance of £50,000 but the supporting Excellerator report did not have a balance within the cashbook tab. 	Low	<p>All reconciliations should be signed by the person who prepared them to ensure there is a clear audit trail.</p> <p>For each reconciliation performed, balances on the reconciliation should be agreed back to supporting documentation.</p> <p>The Authority should investigate the lack of a cashbook balance on the September 2010 Special Interest Account.</p>	<p>Lack of signature was a one off. It is standard procedure for reconciliations to be signed by the person preparing them.</p> <p>This is an isolated minor issue with the Excellerator report for that month. Angela Litchfield is investigating.</p>	<p>Dawn Perryman Implemented</p> <p>Dawn Perryman 30th January 2011</p>

Follow-up of prior years' recommendations

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Original Management response	Current status
Control Design						
1	Manual matching is inefficient and increases the risk of human error and omission.	<p>The majority of bank accounts on the Agresso general ledger system have now been set up so that transactions on the cash book and bank statements are matched automatically. The criteria for this matching are:</p> <ul style="list-style-type: none"> • Transaction text has to agree exactly • Amount has to agree exactly • The dates have to be within a 7 day period of each other. <p>This matching process has created efficiencies by reducing the amount of manual work that has to be performed on the reconciliations.</p> <p>However currently all items on the cashbook are manually matched to transactions on the bank statement for the following accounts:</p> <ul style="list-style-type: none"> • Credit Suspense Account • General Rate Fund Account <p>There is no clear reason for not using the automatic matching process on these accounts as both are high volume accounts where automatic matching would be beneficial.</p>	<ul style="list-style-type: none"> • Medium Risk 	<p>The Authority should make use of the automatic matching functionality of the Agresso system for the Credit Suspense and General Rate accounts.</p>	<p>Agreed</p> <p>Since this audit was undertaken the General Rate fund account has been closed. The action will be implemented for the Credit Suspense account.</p> <p>Alan Barnes With immediate effect</p>	Implemented

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Original Management response	Current status
2	Reconciliations may not be performed on a timely basis.	The Authority does not have a timetable to ensure the completion of all bank reconciliations.	<ul style="list-style-type: none"> ● Low Risk 	A timetable detailing monthly deadlines for the completion of all reconciliations should be implemented as soon as possible.	Agreed, The deadline for this is now included in the responsible staff 1-2-1. It is set at 3 days under normal circumstances Alan Barnes Implemented	Outstanding See issue raised # 1

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Original Management response	Current status
Operating Effectiveness						
3	Lack of audit trail demonstrating preparation of reconciliations. Lack of review may mean that errors are not identified.	Through testing a sample of 3 reconciliations for each bank account the following exceptions were noted: <ul style="list-style-type: none"> • The July 2009 Special Interest Account reconciliation tested had not been signed as prepared. • The July 2009 Special Interest Account reconciliation and the July Payments Account reconciliation were not signed as reviewed. 	● Medium Risk	All reconciliations should be signed by the person who prepared them to ensure there is a clear audit trail. All reconciliations should be reviewed by an independent officer.	Agreed This appears to be a one off incident and was early in the new process. The process is that the responsible officer prepares the reconciliation, it is then reviewed by their team leader and further reviewed by his team leader. We feel that this is sufficient review. Alan Barnes With immediate effect	Partially Implemented No issues were identified regarding bank reconciliations not being reviewed. However a similar issue has been noted regarding not signing reconciliations as prepared See finding # 2

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Original Management response	Current status
4	<p>Reconciliations are not supported by appropriate documentation. Errors have been missed due to the lack of independent review.</p>	<p>For the special interest account for July 2009 the following issues were noted:</p> <ul style="list-style-type: none"> The bank balance as per the reconciliation is £50,000, but the balance on the bank statements is £70,000. Therefore the bank statement balance as per the bank reconciliation and bank statement do not agree. The balance as per the cash book is £2,050,000.00. The balance as per the accelerator report, which interrogates the ledger, is £3,089,372.42. Therefore the balance as per the cash book on the reconciliation does not agree to the actual figure. The supporting documentation for the reconciling items does not match the total reconciling items on the reconciliation. <p>The September reconciliation was also tested and no such issues were identified. Therefore it appears that the issues had been resolved. It is important to note that the July reconciliation had not been reviewed as detailed in finding number 3.</p>	<ul style="list-style-type: none"> Medium Risk 	<p>For each reconciliation performed, balances on the reconciliation should be agreed back to supporting documentation. Management should investigate the specific differences for the July 2009 Special Interest Account. All bank reconciliations should be reviewed independently to ensure that errors are identified and this should be evidenced through the reviewer signing the reconciliation.</p>	<p>Agreed This appears to be a one off incident and was early in the new process. The process is that the responsible officer prepares the reconciliation; it is then reviewed by their team leader and further reviewed by his team leader. We feel that this is sufficient review.</p> <p>Alan Barnes With immediate effect</p>	<p>Implemented</p>

Ref	Specific Risk	Control weakness found	Risk rating	Recommendations	Original Management response	Current status
5	Financial records are inaccurate as out of date cheques have not been cancelled and reflected on the ledger.	It was determined through review of reconciliations and discussion with staff that old unrepresented cheques were only being reviewed and cleared from August 2009 onwards.	<ul style="list-style-type: none"> Low 	The Authority should ensure that old, unrepresented cheques (that is those cheques over 6 months old), are cleared on a monthly basis.	<p>Agreed</p> <p>This is the normal process; it was suspended during the implementation period as a lower priority than implementing the proper reconciliations. The cheques are now sent on a weekly basis to further reduce the possibility of an older cheque being presented</p> <p>Alan Barnes With immediate effect</p>	Implemented

Appendix 1 - Terms of Reference

Internal audit 2010/11

Bank Reconciliations

October 2010

Background

This review is to be undertaken as part of the Core Financial Systems audit work included within the 2010/11 Internal Audit Plan. This review will consider controls and processes in place with regards to Bank Reconciliations as at the time of our internal audit fieldwork, which is due to take place during November 2010.

Objective

The objective of this review is to verify that all bank accounts are regularly reconciled and subject to independent review.

Our scope and approach

Our work will focus on identifying the guidance, procedures and controls in place to mitigate key risks through:

- Documenting the underlying guidance, policy and processes in place and identifying key controls.
- Considering whether the policies and procedures in place are fit for purpose
- Testing key controls.

The key points of focus will be whether:

- All bank accounts are subject to regular independent review;
- Reconciliations are performed to the ledger system via the cashbook, and reasons for any imbalance properly investigated and actioned;
- Staff have received adequate training to enable them to perform reconciliations;
- Clear guidance is available to assist in the reconciliation process;
- Use of suspense accounts is limited and items promptly cleared; and
- Re-performance of reconciliations to ensure accurately completed.

We will discuss our findings with the Finance Manager and any other nominated representatives, to

develop recommendations and action plans. A draft report will be issued to the Head of Finance and Finance Manager, along with other relevant officers, for review and to document management responses.

Information request

Listed below is information that may be required at the commencement of the audit, if available:

- Copies of procedure notes
- Copies of reconciliations between the Authority's bank account and the ledger/cashiers system.

The list is not intended to be exhaustive. Evidence should be available to support all operating controls. Other information identified during the review of Bank Reconciliations may be requested on an ad hoc basis.

Limitations of Scope

The scope of our work will be limited to the areas identified in this Terms of Reference.

Deliverables from PwC

Our deliverable will be a report detailing our findings with regard to our assessment of the design and effectiveness of controls in place over the Bank Reconciliations system.

Stakeholders and responsibilities

Key Stakeholder(s)

Assignment Role	Contact(s)	Responsibilities
Audit sponsor	Phil Morrison, Finance Manager	<ul style="list-style-type: none"> Review and approve terms of reference Review draft report. Review final report. Hold initial scoping meeting Review and meet to discuss issues arising and develop management responses and action plan

Other roles and responsibilities

Role	Contacts	Responsibilities
Head of Finance	Bill Lewis	<ul style="list-style-type: none"> Review and approve terms of reference Review draft report. Review final report
Director of Finance	Isabell Procter	<ul style="list-style-type: none"> Review draft report. Review final report
Audit Committee Portfolio Holder	Audit Committee Members David Perkins	<ul style="list-style-type: none"> Review final report

Our team

Engagement Leader	Richard Bacon
Engagement Manager	Chris Dickens
Team Manager	Matthew Plummer
Audit Executive	Thomas Hann

Appendix 2 - Assurance ratings

Level of assurance	Description
High	<p>No control weaknesses were identified; or</p> <p>Our work found some low impact control weaknesses which, if addressed would improve overall control. However, these weaknesses do not affect key controls and are unlikely to impair the achievement of the objectives of the system. Therefore we can conclude that the key controls have been adequately designed and are operating effectively to deliver the objectives of the system, function or process.</p>
Moderate	<p>There are some weaknesses in the design and/or operation of controls which could impair the achievement of the objectives of the system, function or process. However, either their impact would be less than significant or they are unlikely to occur.</p>
Limited	<p>There are some weaknesses in the design and / or operation of controls which could have a significant impact on the achievement of key system, function or process objectives but should not have a significant impact on the achievement of organisational objectives. However, there are discrete elements of the key system, function or process where we have not identified any significant weaknesses in the design and / or operation of controls which could impair the achievement of the objectives of the system, function or process. We are therefore able to give limited assurance over certain discrete aspects of the system, function or process.</p>
No	<p>There are weaknesses in the design and/or operation of controls which [in aggregate] could have a significant impact on the achievement of key system, function or process objectives and may put at risk the achievement of organisation objectives.</p>

In the event that, pursuant to a request which Northampton Borough Council has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PricewaterhouseCoopers (PwC) promptly and consult with PwC prior to disclosing such report. Northampton Borough Council agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Northampton Borough Council shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC, Northampton Borough Council discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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