

AGENDA ITEM 4(a)



# The Highland Council

Interim Report

2015/16

Prepared for Members of The Highland Council

Draft: June 2016  
Final: September 2016

# Key contacts

Stephen Boyle,, Assistant Director  
[sboyle @audit-scotland.gov.uk](mailto:sboyle@audit-scotland.gov.uk)

Maggie Bruce, Senior Audit, Manager  
[mbruce@audit-scotland.gov.uk](mailto:mbruce@audit-scotland.gov.uk)

Jim Convery, Senior Auditor  
[jconvery@audit-scotland.gov.uk](mailto:jconvery@audit-scotland.gov.uk)

Audit Scotland  
3rd Floor, Ballantyne House  
84 Academy Street  
INVERNESS  
IV1 1LU

Telephone: 0131 625 1500

Website: [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk)

The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies ([www.audit-scotland.gov.uk/about/ac/](http://www.audit-scotland.gov.uk/about/ac/)). Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General ([www.audit-scotland.gov.uk/about/](http://www.audit-scotland.gov.uk/about/)).

Stephen Boyle has been appointed as the engagement lead for the audit of The Highland Council for the period 2012/13 to 2015/16.

This report has been prepared for the use of The Highland Council and no responsibility to any member or officer in their individual capacity or any third party is accepted.

# Contents

Introduction .....	3
Internal Control.....	4
Governance arrangements .....	10
Appendix A: 2015/16 Action Plan .....	12
Appendix B: 2014/15 Internal Controls report follow up.....	29

# Introduction

1. This report summarises the findings from the interim audit work carried out as part of the 2015/16 audit of The Highland Council. The nature and scope of the audit were outlined in our Annual Audit Plan presented to the Audit and Scrutiny Committee on 24 March 2016 and follows the requirements of Audit Scotland's Code of Audit Practice which was published in May 2011.
2. Our work covered the following areas:
  - the operation of the internal controls in key financial systems
  - progress made by the council in implementing the agreed actions included in our 2014/15 *Review of Internal Controls* report
  - review of the council's governance arrangements.
4. Our report has been prepared on an exception basis and highlights only those areas where we identified control weaknesses or where procedures could be further improved. The issues reported are those which have come to our attention during the course of our normal work and are not necessarily, therefore, all the risk areas that may exist.
5. It remains the responsibility of management to determine the extent of the internal control system appropriate to the council. We would stress, however, that an effective system of internal control is an essential part of the efficient management of any organisation.

## Management action

6. Appendix A is an action plan setting out our recommendations to address the risks we have identified during the course of our audit. Officers have considered the issues and agreed to take the specific steps in the column headed 'Management response and action'.
7. Members and the Executive Leadership Team should ensure that they are satisfied with the proposed action and have a mechanism in place to assess progress and monitor outcomes.

## Acknowledgement

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

# Internal Control

9. 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 the 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 or detecting material misstatement, error, fraud or corruption
  - complies with established policies, procedures, laws and regulations.
10. In accordance with ISA 330, paragraphs 14 and 15, our audit judgements are based on current year testing of controls and, where appropriate, prior year results. Where controls have not been tested or where control weaknesses are identified by internal or external audit testing, auditing standards require us to consider the impact of these weaknesses on our planned approach to the audit of the financial statements, and to amend it as necessary in order to obtain sufficient evidence that they are free from material misstatement.
11. The council implemented a new financial management system with effect from 1 April 2015 and as this system is fundamental to the preparation of the financial statements and our audit opinion, we have reviewed the key controls in operation within the subsidiary systems which make up the financial management system. The table on page 5 summarises these, and other key systems.
12. We have not included the capital accounting system within this list as in previous years we have been unable to rely on the controls in operation within this system. Instead we plan to get our assurances by undertaking targeted testing of the capital accounting entries within the 2015/16 financial statements. The council's new financial management system includes a capital accounting module but this has yet to be implemented.
13. Auditing standards require internal and external auditors to work closely together to make optimal use of available audit resources. We seek to rely on the work of internal audit wherever possible, and planned to take formal reliance from internal audit's work in the four areas set out on page 5 to support our opinion on the 2015/16 financial statements. In addition to the four areas set out on page 5, internal audit are also undertaking work to support the Audit & Risk Manager's opinion on the adequacy and effectiveness of the council's key financial systems and governance arrangements.
14. As internal audit have yet to complete their work we will report how their findings impacted on our approach to the audit of the financial statements in our annual audit report.

Key system for the production of the financial statements	External audit coverage	Planned reliance on Internal Audit
<b>New financial management system</b>		
General ledger	✓	
Accounts payable	✓	
Accounts receivable		✓
Cash management		✓
<b>Other key systems</b>		
Payroll	✓	
NDR billing & collection	✓	
Council tax billing & collection	✓	
NDR and council tax valuation		✓
Housing rents		✓
Treasury management	✓	
Voluntary redundancy scheme	✓	

## 2015/16 system of internal control

### Overall assessment

15. Our overall assessment is that the level of internal control in place within the following key systems is sufficient to enable us to take our planned assurances for the audit of the 2015/16 financial statements:
- payroll
  - non domestic rates billing and collection
  - council tax billing and collection
  - treasury management
  - voluntary redundancy scheme
16. There were, however, significant weaknesses within the controls in operation within the general ledger and accounts payable systems during 2015/16 and so we were unable to take our planned controls assurance from these systems. We have set out below the weaknesses we have identified, together with the impact on our approach to the audit of the financial statements.

### Authorisation of journal entries

17. Our review identified that Finance staff can post and authorise their own journal entries and that there is no independent review of journal entries after they have been processed. This lack of authorisation and review of journal entries increases the risk of error in the accounts. Last year we highlighted in our Annual Audit Report that errors in processing some of the year end journals had resulted in significant misstatements in Services' income and expenditure within

the unaudited Comprehensive Income and Expenditure Statement. As a result of these findings, we have amended our approach to the final accounts audit to increase our testing of journal entries.

**Refer Action Plan No. 1**

### Reconciliations

18. Bank and control account reconciliations provide assurance that transactions and balances are complete and accurately recorded in the general ledger. Our testing noted that the council's bank and sales and purchase ledger control account reconciliations were not completed timeously during 2015/16 and were not up to date at the time of our audit (January 2016). We have been advised that all bank and control account reconciliations will be brought up to date prior to submission of the unaudited accounts. We will review the year end reconciliations as part of our final accounts audit and, dependent on the results, amend our audit approach as required.

**Refer Action Plan No. 2**

### Suspense accounts

19. A suspense account is an account in the general ledger in which amounts are temporarily recorded when the proper account could not be determined at the time that the transaction was recorded. Once the proper account is determined, the amount should be moved from the suspense account. Our testing noted that suspense account balances were not being promptly investigated and cleared during 2015/16. We have been advised that all suspense account balances will be cleared prior to submission of the financial statements for audit. We will review the year end suspense account balances as part of our final accounts audit and, dependent on the results of this testing, amend our audit approach if required.

**Refer Action Plan No. 3**

### Budgetary control

20. The budgetary control reports produced by the new financial management system allow budget holders to drill down and see which employees are being charged to their budget. Budget holders are not, however, asked to periodically confirm the validity of the employees charged to their budget.

**Refer Action Plan No. 4**

21. The new financial management system introduced purchase order commitment accounting to the council for the first time. In February 2016, the Purchase Card Administrator wrote to all Integra users highlighting that *'if order lines are not receipted and invoiced correctly by staff then this will lead to excessive charges in the ledger and an incorrect balance on the monthly budgetary control reports'*. The Purchase Card Administrator provided a list of outstanding purchase orders and asked all staff to review them and take corrective action, where necessary, in advance of the year end. Although we have been advised, by Finance staff, that this issue only affects the budgetary control reports, we have amended our approach to the final accounts audit to increase our testing of year end purchase ledger balances in order to gain the assurances necessary to support our opinion on the financial statements.

**Refer Action Plan No. 5**

#### **Trial balance**

22. A trial balance report is produced daily to ensure that the general ledger system is in balance. The system records the user who generated the report but there is no evidence that the report has been reviewed by a more senior member of staff within the Finance Section, or what action has been taken when anomalies are identified.

**Refer Action Plan No. 6**

23. Audit testing identified that the trial balance report had not been in balance for most of 2015/16. Finance staff were aware of the issue which related to a negative entry being treated as a positive by the system but it was not corrected until February 2016. We are concerned that the system was able to change a negative entry to a positive entry without user intervention resulting in a single sided entry being posted to the general ledger. Systems generally have inbuilt controls that do not allow single sided entries to be posted and that require users to confirm the validity of postings that fall out with normal parameters.

**Refer Action Plan No. 7**

#### **Accounts payable**

24. Procedural guidance notes detailing how to process changes to suppliers' bank account details within the new financial management have yet to be updated although staff involved in the process have prepared notes for their own use.

**Refer Action Plan No. 8**

25. The Integra Training Manual sets out how an invoice should be entered onto the purchase ledger system. The Manual recommends attaching a scanned copy of the invoice in the system so that it can be reviewed by the budget holder when authorising the transaction for payment, and be held in Integra in case of future queries. Our review of 30 invoices where no purchase order had been raised noted that this guidance was not being consistently followed. In 19 cases, the invoice had been signed as approved prior to being scanned onto the system. However, in 1 case the invoice was not evidenced as approved for payment before being scanned, and in the remaining 10 cases no supporting documentation had been scanned onto the system.

**Refer Action Plan No. 9**

26. Invoices input to the Profess feeder system do not require to be approved by the budget holder on the either Profess or on Integra prior to payment. This absence of approval means that unauthorised invoices could be input to the system and paid without approval. As a result, we amended our approach and substantively tested a sample of 7 invoices which had been input via the Profess system to ensure that they had been stamped as approved for payment prior to being scanned on to the system. Our testing found that all 7 invoices had been approved by appropriate staff prior to payment.

**Refer Action Plan No. 10**

### **System back ups and disaster recovery**

27. The council's new financial management system (Integra) is hosted by CAPITA. CAPITA have advised the council that system back ups are taken daily and stored off site and that a disaster recovery plan is in place and tested annually to ensure it remains fit for purpose. The council, however, has no evidence to support CAPITA's assurance that back ups are taken and stored off site nor that the CAPITA's disaster recovery plan is regularly tested.

**Refer Action Plan No. 11**

### **Cash management system**

28. Since the introduction of the new financial management system, all income received is processed through the new cash management system. During 2015/16, the cash management system posted all income, including pension fund income, to one bank code (the AXIS income bank account) in the council's general ledger. In order to ensure that bank balances were recorded in the correct ledger code, transfers then had to be made by journal entry once the bank account reconciliations were brought up to date. This process was very resource intensive and could have been avoided if the cash management system had been set up to post income received to the correct bank account in the general ledger from the outset. Management has advised that, with effect from 1 April 2016, the cash management system is able to post income transactions directly to the correct bank accounts codes in the general ledger.



## Follow up of the 2014/15 Review of Internal Controls report

29. Our review of progress made in implementing the agreed actions included in the action plan within the 2014/15 Review of Internal Controls report is set out in Appendix B. Follow up of six of the twelve agreed actions will be undertaken as part of our final accounts audit as this is the most efficient approach. Two of the actions relate to the Housing Rents system which Internal Audit have agreed to review this year. Of the remaining 4 actions:
- three have been implemented
  - one (relating to bank reconciliations) has been raised again within the body of the report at paragraph 18 and within the 2015/16 action plan.

# Governance arrangements

30. The council is responsible, through its Chief Executive, for establishing arrangements for ensuring the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies usually involve those charged with governance (including audit committees or similar groups) in monitoring these arrangements.
31. As part of the wider scope of public audit, auditors have a responsibility to review and report on audited bodies' governance arrangements as they relate to:
- corporate governance
  - the prevention and detection of fraud and irregularity
  - standards of conduct and arrangements for the prevention and detection of corruption.
32. In this part of the report we set out our findings from our review of the council's governance arrangements.

## Audit findings

### Standing orders, scheme of delegation and financial regulations

33. The Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 introduced the requirement for pension funds to set up a Pensions Board which would be responsible for assisting the administering authority in complying with scheme regulations and the requirements of the Pensions Regulator. The inaugural meeting of the Highland Council Pensions Board was held on 4 September 2015. The council's standing orders and scheme of delegation has yet to be updated to include reference to the Pensions Board, its remit and its interaction with the Pensions Committee.

**Refer Action Plan No. 12**

34. The Local Authority Accounts (Scotland) Regulations 2014 introduced a number of key changes with regard to the processes for approval and publication of both the unaudited and audited financial statements. The council's financial regulations have yet to be updated to reflect the requirements of these Regulations.

**Refer Action Plan No. 13**

35. In response to our 2014/15 *'Major capital investments in councils: a follow up report'*, officers agreed to amend financial regulations to reflect their decision to only provide relevant strategic committees with reports on total costs against the original budget and timescale for projects in excess of £5 million. As of March 2016 this action had yet to be implemented.

**Refer Action Plan No. 14**

---

## Risk management strategy

36. The Audit and Scrutiny Committee last reviewed the council's risk management strategy in 2013. The risk management strategy should be regularly reviewed to ensure it remains fit for purpose and reflects best practice.

**Refer Action Plan No. 15**

## Debt write offs

37. Officers have delegated powers to write off debts under £5,000 without first obtaining members' approval. Whilst this is administratively efficient, those charged with governance are not advised of how much council tax, non domestic rates, housing rents and sundry debt has been written off by officers under these delegated powers and so have no opportunity to scrutinise or challenge the level of write-offs.

**Refer Action Plan No. 16**

## State aid

38. State aid refers to forms of public assistance, given to undertakings on a discretionary basis, which has the potential to distort competition and affect trade between Member States of the European Union. State aid rules are set by the European Commission. The council's European Team provide guidance on compliance with State Aid Regulations but are only contacted on an ad hoc basis by services. The council does not routinely monitor compliance against state aid limits.

**Refer Action Plan No. 17**

## Data protection

39. The Data Protection Act (1998) places a duty on the council to protect personal information that it holds and to provide individuals with access to the particular information that the council holds about them on request. It is, therefore, important that the council and its employees ensure the confidentiality, integrity, quality and availability of all the information it holds and takes steps to ensure that it does not break the law. Our review of the council's data protection arrangements noted that:

- less than 10% of council officers have completed the online data protection course since it was introduced in July 2011.
- the council's register of data sharing agreements is recorded on an excel spreadsheet. At the time of our review, this spreadsheet was incomplete and out of date
- no register of data processing agreements was found to exist although it is referred to in the council's Data Protection Policy.

**Refer Action Plan No. 18**

# Appendix A: 2015/16 Action Plan

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
<b>Internal Controls</b>				
1	<p><b>Journal entries</b></p> <p>Our review identified that Finance staff can post and authorise their own journal entries and that there is no independent review of journal entries after they have been processed. This lack of authorisation and review of journal entries increases the risk of error in the accounts. Last year we highlighted in our Annual Audit Report that errors in the processing some of the year end journals had resulted in significant misstatements in Services' income and expenditure within the unaudited Comprehensive Income and Expenditure Statement. As a result of these findings, we have amended our approach to the final accounts audit to increase our testing of journal entries.</p> <p><b>Risk:</b> the risk of error in the accounts is increased</p> <p><b>Recommendation:</b> a journal approval process should be introduced supplemented by an independent review of journal entries posted to unusual ledger codes or for unusual (including round sum) amounts.</p>	<p>The ability to process journal entries is predominately limited to staff within the Finance service who should have the appropriate skills and knowledge to correctly process journal entries.</p> <p>Should any entries be processed in error it is anticipated these would be picked up by budget holders when viewing their budget holder reports.</p> <p>A central review of all year-end journals of a material size will be undertaken as part of the year end process.</p>	Head of Corporate Finance	30/6/17

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
2	<p><b>Reconciliations</b></p> <p>Bank and control account reconciliations provide assurance that transactions and balances are correctly recorded in the general ledger. Our testing noted that the council's bank and sales and purchase ledger control account reconciliations were not completed timeously during 2015/16 and were not up to date at the time of our audit (January 2016).</p> <p><b>Risk:</b> the reconciliation process does not provide assurance that all transactions are complete and accurately recorded in the financial ledger</p> <p><b>Recommendation:</b> bank and control account reconciliations should be completed at the end of each month and reconciling items promptly investigated and cleared.</p>	<p>Due to the introduction of the new finance system there were delays in the completion of some processes as new ways of working were being established.</p> <p>All reconciliations were completed by the year end.</p> <p>Sales and purchase ledgers are reconciled to control reports daily.</p> <p>New procedure notes for bank reconciliations have been written and the reconciliations are now taking place on a monthly basis.</p>	Head of Corporate Finance	30/9/2016

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
3	<p><b>Suspense accounts</b></p> <p>A suspense account is an account in the general ledger in which amounts are temporarily recorded when the proper account could not be determined at the time that the transaction was recorded. When the proper account is determined, the amount should be moved from the suspense account. Our testing noted that suspense account balances were not being promptly investigated and cleared during 2015/16.</p> <p><b>Risk:</b> transactions are not properly accounted for within the financial statements submitted for audit</p> <p><b>Recommendation:</b> suspense accounts should be regularly reviewed, investigated and cleared.</p>	<p>All suspense accounts were dealt with appropriately as part of the year end processes. Efforts will be made to keep the clearing of suspense accounts as up to date as possible but sometimes bank reconciliations will take priority.</p>	<p>Head of Corporate Finance</p>	<p>30/9/2016</p>

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
4	<p><b>Budgetary control</b></p> <p>The budgetary control reports produced by the new financial management system allow budget holders to drill down and see which employees are being charged to their budget. Budget holders are not, however, asked to periodically confirm to the validity of the employees charged against their budget.</p> <p><b>Risk:</b> unauthorised employees are paid through the council's payrolls</p> <p><b>Recommendation:</b> budget holders should be asked to periodically confirm the validity of the employees charged against their budget.</p>	<p>The integration of payroll data into the monthly budget holder reports is seen as an improvement as managers can now drill down from their summary report into specific transaction detail for all categories of expenditure.</p> <p>Finance staff who support budget holders will remind them to check the validity of their employee costs and the guidance note on budgetary control (part of the financial regulations) also alludes to the verification of costs charged.</p> <p>A short guidance note on 'what to do with the budget holder report' will be written and a link to the note will be provided as part of the monthly report that is sent to budget holders.</p>	Head of Corporate Finance	30/11/2016

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
5	<p><b>Budgetary control</b></p> <p>The new financial management system introduced purchase order commitment accounting to the council for the first time. In February 2016, the Purchase Card Administrator wrote to all Integra users highlighting that <i>‘if order lines are not receipted and invoiced correctly by staff then this will lead to excessive charges in the ledger and an incorrect balance on the monthly budgetary control reports’</i>. The Purchase Card Administrator provided a list of outstanding purchase orders and asked all staff to review them and take corrective action, where necessary, in advance of the year end.</p> <p><b>Risks:</b> budgetary control reports are inaccurate which reduces the value of budget monitoring, and expenditure/creditors are overstated in the financial statements.</p> <p><b>Recommendations:</b> staff should be reminded of how to use the purchase order, goods receipting and commitment accounting functions within the purchase ledger. Periodic reviews should be undertaken to confirm that the system is being used correctly and that expenditure within the general ledger is valid and charged to the correct accounting period.</p>	<p>The introduction of commitment accounting in the new finance system is an improvement on the old system where this facility was not available.</p> <p>The guidance note referred to at finding 4 of this report will include reference to understanding commitment accounting. Periodic guidance is also issued by the procurement team (as per example e-mail cited)</p> <p>It is not considered a risk that expenditure or creditors would be overstated in the financial statements as a result of this as commitments would not be included in the annual expenditure as the goods or services will not have been received (if they have there would be an actual expenditure transaction and not a commitment)</p>	Head of Corporate Finance	30/11/2016



Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
6	<p><b>Trial balance</b></p> <p>A trial balance report is produced daily to ensure that the general ledger system is in balance. The system records the user who generated the report but there is no evidence that the report has been reviewed by a more senior member of staff within the Finance Section, or what action has been taken when anomalies are identified.</p> <p><b>Risk:</b> anomalies in the daily trial balance report may not be investigated and corrected timeously if the report is not reviewed by a senior member of staff</p> <p><b>Recommendation:</b> the review of the daily trial balance report by a senior officer should be evidenced and the action taken to investigate and resolve anomalies recorded.</p>	<p>The staff member who does the daily reconciliation will investigate any anomalies and that is normally timeous. If action is not timeous the system will be imbalanced for a prolonged period.</p> <p>A senior member of staff is notified only on an exception basis if there are anomalies.</p> <p>Resolution of anomalies is likely to be done in conjunction with the finance system provider and a log of all calls to the provider is maintained.</p> <p>It is not considered necessary for a senior member of staff to review the daily trial balance report.</p>	N/A	N/A

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
7	<p><b>Trial balance</b></p> <p>Audit testing identified that the trial balance report had not been in balance for most of 2015/16. Finance staff were aware of the issue which related to a negative entry being treated as a positive by the system but it was not corrected until February 2016. We are concerned that the system was able to change a negative entry to a positive entry without user intervention which resulted in a single sided entry being posted to the general ledger. Systems generally have inbuilt controls that do not allow single sided entries to be posted, and that require users to confirm the validity of postings that fall out with normal parameters.</p> <p><b>Risk:</b> the system cannot be relied on to accurately process entries input by users</p> <p><b>Recommendation:</b> an explanation should be requested from CAPITA as to why the system was able to change a negative entry to a positive entry without user intervention resulting in a single sided entry being posted to the general ledger. Assurance should be obtained that the system has been amended to prevent this happening in the future.</p>	<p>The system has controls to identify where errors may occur.</p> <p>This particular problem was in the way the interface with the AXIS system had been set up and on discovery of this issue a correction was immediately requested. Whilst the correction was awaited the balance was consistently checked to ensure there was no movement in the position.</p> <p>The underlying cause of the error has been corrected by the supplier</p> <p>We are confident that sufficient other controls are in place to be able to rely on the system. During the production of the accounts all other transactions have been found to be in balance and this is further evidenced in the balanced trial balance.</p>	N/A	N/A

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
8	<p><b>Accounts payable</b></p> <p>Procedural guidance notes detailing how to process changes to supplier bank account details within the new financial management have yet to be updated although staff involved in the process have prepared basic notes for their own use.</p> <p><b>Risk:</b> requests to change suppliers' bank details may not be processed correctly in the absence of clear procedural guidance</p> <p><b>Recommendation:</b> procedural guidance notes should be updated so that staff are clear as to how to process a request for a change in a supplier's bank details.</p>	Guidance notes will be updated.	Head of Corporate Finance	31/10/2016

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
9	<p><b>Accounts Payable</b></p> <p>The Integra Training Manual sets out how an invoice should be entered onto the purchase ledger system. The Manual recommends attaching a scanned copy of the invoice in the system so that it can be reviewed by the budget holder when authorising the transaction for payment, and be held in Integra in case of future queries. Our review of 30 invoices where no purchase order had been raised noted that this guidance was not being consistently followed. In 19 cases, the invoice had been signed as approved prior to being scanned on to the system. In 1 case, however, the invoice was not evidenced as approved for payment before being scanned, and in the remaining 10 cases no supporting documentation had been scanned onto the system.</p> <p><b>Risk:</b> payments made are not supported by an approved invoice or other supporting documentation</p> <p><b>Recommendation:</b> invoices or other supporting documentation should be scanned onto Integra in support of all payments made.</p>	<p>The ability to attach a scanned copy of an invoice into the finance system is a new development not present in the old finance system. At present it is only recommended that an invoice is attached due to the extra resource that would be needed to complete this task. As the council moves towards electronic invoicing more invoices will be attached to transactions.</p> <p>All approvals are done on the Integra system so a signature on a physical invoice is not necessary.</p> <p>In line with the financial regulations and historic practice all invoices should be stored appropriately. Budget holders are responsible for ensuring the validity of any transaction prior to approving it.</p>	N/A	N/A

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
10	<p><b>Accounts payable</b></p> <p>Invoices input to the Profess feeder system do not require to be approved by the budget holder on the either Profess or on Integra prior to payment. This absence of approval means that unauthorised invoices could be input to the system and paid without approval. As a result, we amended our approach and substantively tested a sample of 7 invoices which had been input via the Profess system to ensure that they had been stamped as approved for payment prior to being scanned on to the system. Our testing found that all 7 invoices had been approved by appropriate staff prior to payment.</p> <p><b>Risk:</b> payments are made on unauthorised invoices</p> <p><b>Recommendation:</b> invoices input to systems which feed into the general ledger should be subject to the same system authorisation processes as those input directly to Integra.</p>	<p>Invoices processed through the Profess system are required to be manually approved by an appropriate budget holder prior to processing as the Profess system does not allow for electronic authorisations in the same way as Integra.</p> <p>There will always be this disparity between how invoices are approved but there is no difference in the requirement for all invoices to be approved by an appropriate budget holder prior to payment.</p> <p>We rely on the budget holder to identify any unauthorised transactions as part of their budget monitoring.</p>	N/A	N/A

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
11	<p><b>System back ups and disaster recovery</b></p> <p>The council's new financial management system (Integra) is hosted by CAPITA. CAPITA have advised the council that system back ups are taken daily and stored off site and that a disaster recovery plan is in place and tested annually to ensure it remains fit for purpose. The council, however, has no evidence to support CAPITA's assurance that back ups are taken and stored off site nor that the CAPITA's disaster recovery plan is regularly tested.</p> <p><b>Risk:</b> the council may be unable to recover its financial management system in the event of a catastrophic failure</p> <p><b>Recommendation:</b> the council should ask CAPITA to evidence its system back up and disaster recovery arrangements.</p>	<p>The council will ask for evidence of the annual disaster recovery test completed by Capita as well as the system back up process.</p>	<p>Head of Corporate Finance</p>	<p>31/12/2016</p>

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
<b>Governance</b>				
12	<p><b>Standing orders and scheme of delegation</b></p> <p>The Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 introduced the requirement for pension funds to set up a Pensions Board which would be responsible for assisting the administering authority in complying with scheme regulations and the requirements of the Pensions Regulator. The inaugural meeting of the Highland Council Pensions Board was held on 4 September 2015. The council's standing orders and scheme of delegation have yet to be updated to include reference to the Pensions Board, its remit and its interaction with the Pensions Committee.</p> <p><b>Risk:</b> standing orders and the scheme of delegation do not reflect the council's current structure</p> <p><b>Recommendation:</b> standing orders and the scheme of delegation should be updated to include reference to the Pensions Board and its interaction with the Pensions Committee.</p>	The standing orders and scheme of delegation will be updated.	Head of Corporate Finance	31/12/16

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
13	<p><b>Financial regulations</b></p> <p>The Local Authority Accounts (Scotland) Regulations 2014 introduced a number of key changes with regard to the processes for approval and publication of both the unaudited and audited financial statements. The council's financial regulations have yet to be updated to reflect the requirements of the 2014 Accounting Regulations.</p> <p><b>Risk:</b> the council does not comply with the requirements set out in the 2014 Accounting Regulations.</p> <p><b>Recommendation:</b> financial regulations should be updated to reflect the requirements of the 2014 Accounting Regulations.</p>	<p>A report containing suggested revisions to Financial Regulations was considered by the Audit &amp; Scrutiny Committee on 16 June 2016 with the changes recommended to Council on 29 June 2016.</p> <p>One of the revisions included the necessary reference to the 2014 Accounting Regulations.</p>	Actioned	Actioned
14	<p><b>Financial regulations</b></p> <p>In response to our 2014/15 <i>'Major capital investments in councils: a follow up report'</i>, officers agreed to amend financial regulations to reflect their decision to only provide relevant strategic committees with reports on total costs against the original budget and timescale for projects in excess of £5 million. As of March 2016 this had yet to be implemented.</p> <p><b>Risk:</b> financial regulations are not kept up to date and do not reflect current practices</p> <p><b>Recommendation:</b> financial regulations should be updated to reflect the decisions taken by officers to only report on significant (greater than £5 million) capital projects.</p>	<p>The change to Financial Regulations was considered by the Audit &amp; Scrutiny Committee on 26 May 2015 and approved by Council on 25 June 2015. However, an omission by officers meant that the Regulations were not updated.</p> <p>This was rectified in conjunction with the changes referred to at no.13 above.</p>	Actioned	Actioned



Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
15	<p><b>Risk management strategy</b></p> <p>The Audit and Scrutiny Committee last reviewed the council's risk management strategy in 2013.</p> <p><b>Risk:</b> the risk management strategy is not up to date and does not reflect current best practice.</p> <p><b>Recommendation:</b> the risk management strategy should be regularly reviewed to ensure it remains fit for purpose and reflects best practice.</p>	<p>The Strategy is still based on best practice (ISO 31000) but requires some update to reflect changes within the Council eg changes to job titles. However, the impact of Voluntary Redundancy and the redesign of the Council will result in significant changes being required to the strategy.</p> <p>Therefore, it is considered that a more effective use of resources will be to review the strategy once the redesign work has been completed and the new Council structure and management arrangements are in place.</p>	Corporate Audit & Performance Manager, Finance Service	30/09/17

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
16	<p><b>Debt write offs</b></p> <p>Officers have delegated powers to write off debts under £5,000 without first obtaining members' approval. Whilst this is administratively efficient, those charged with governance are not advised of how much council tax, non domestic rates, housing rents and sundry debt has been written off by officers under these delegated powers and so have no opportunity to scrutinise or challenge the level of write-offs.</p> <p><b>Risk:</b> members are not aware of how much debt is written off under delegated powers.</p> <p><b>Recommendation:</b> members should receive a report at the end of each financial year advising how much council tax, non-domestic rates and housing rent balances have been written off under delegated powers.</p>	<p>As part of its statutory performance indicators the Council reports on its debt collection rates. A focus on increasing those rates, together with the requirement for member approval of any debt over £5,000 is felt to provide members with sufficient assurance around income collection.</p>	N/A	N/A

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
17	<p><b>State aid</b></p> <p>State aid refers to forms of public assistance, given to undertakings on a discretionary basis, which has the potential to distort competition and affect trade between Member States of the European Union. State aid rules are set by the European Commission. The council's European Team provide guidance on compliance with State Aid Regulations but are only contacted on an ad hoc basis by services. The council does not routinely monitor compliance against state aid limits.</p> <p><b>Risk:</b> the council may breach state aid regulations as there is no monitoring against state aid limits</p> <p><b>Recommendation:</b> the council should review its arrangements for ensuring compliance with state aid regulations.</p>	The council's arrangements for ensuring compliance with state aid regulations will be reviewed.	Head of Corporate Finance	31/03/2017

Ref.	Audit Finding	Management Response & Action	Responsible Officer	Date
18	<p><b>Data protection</b></p> <p>The Data Protection Act (1998) places a duty on the council to protect personal information that it holds and to provide individuals with access to the particular information that the council holds about them on request. It is, therefore, important that the council and its employees ensure the confidentiality, integrity, quality and availability of all the information it holds and takes steps to ensure that it does not break the law. Our review of the council's data protection arrangements noted that:</p> <ul style="list-style-type: none"> <li>• less than 10% of council officers have completed the online data protection course since it was introduced in July 2011</li> <li>• the council's register of data sharing agreements is recorded on an excel spreadsheet. At the time of our review, this spreadsheet was incomplete and out of date</li> <li>• no register of data processing agreements was found to exist although it is referred to in the council's Data Protection Policy.</li> </ul> <p><b>Risk:</b> the council's Data Protection arrangements are not robust enough to prevent a contravention of the Date Protection Act resulting in penalties for the council</p> <p><b>Recommendation:</b> the council's Data Protection arrangements should be reviewed to ensure that they are robust and operating as intended.</p>	<p>The findings were highlighted through an internal audit report on data protection and actions to address the issues are being coordinated through the Information Management Governance Board (IMGB).</p> <p>The council has separately gone through a voluntary audit from the information commissioner and completed an action plan as a result of that audit, again managed through the IMGB.</p> <p>The Council's Fol and Data Protection Manager is reviewing the register of data sharing agreements.</p> <p>The IMGB agreed with internal audit that a register of data processing agreements is not required and the Data Protection Policy will be amended accordingly.</p>	FOI and Data Protection Manager	31/03/2017

# Appendix B: 2014/15 Internal Controls report follow up

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
<b>Cash and cash equivalents</b>			
1	<p>Reconciling items identified on the council's bank reconciliations are not investigated and cleared timeously. For example:</p> <ul style="list-style-type: none"> <li>bank giro credits returned as unpaid from the bank for the whole of the 2014/15 financial year are shown as a reconciling item on the No 3 bank account reconciliation</li> <li>unresolved differences from previous financial years (August 2009 onwards) continue to be carried as reconciling items on the general income bank account reconciliation from year to year.</li> </ul> <p><b>Risk:</b> the bank reconciliation process does not provide assurance that all transactions are complete and accurately recorded in the financial ledger.</p> <p><b>Recommendation:</b> reconciling items should be promptly investigated and cleared.</p>	<p>The importance of regular reconciliations is recognised and following the implementation of the new financial system in 2015/16 we are working towards bringing all reconciliations up to date and maintaining monthly reconciliations including the timely investigation and clearing of reconciling items.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Target Date:</b> 31 March 2016</p>	<p>Refer to paragraph 18 in body of report and to the second action in the 2015/16 action plan. Bank reconciliations were not completed timeously during 2015/16.</p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
2	<p>The council's general income bank account reconciliation includes the pension fund's income bank account although this bank account is not part of the council's bank balances. The pension fund income bank account is separately reconciled and disclosed within the pension fund's financial statements.</p> <p><b>Risk:</b> the council's bank balances are misstated through the inclusion of the pension fund income bank account</p> <p><b>Recommendation:</b> the pension fund income bank account should not be included as part of the council's general income bank account reconciliation.</p>	<p>Since the implementation of the new financial system in 2015/16, the pension fund income bank account is no longer included within the council's general income bank account reconciliation.</p> <p><b>Responsible Officer:</b> Head of Corporate Finance</p> <p><b>Target Date:</b> 30 September 2015</p>	<p>We will follow this up as part of our final accounts audit work and report our findings in our annual audit report.</p>
3	<p>Surplus cash balances placed on deposit by the council's Treasury section are all coded to the same general ledger code. The financial statements require these deposits to be classified as a cash equivalent, short term investment or long term investment depending on the length of time the money is invested for. In previous years we have found errors in the classification of these deposits within the unaudited accounts.</p> <p><b>Risk:</b> the financial statements are misstated due to the misclassification of surplus cash placed on deposit.</p> <p><b>Recommendation:</b> consideration should be given to setting up additional ledger codes to enable cash deposits to be correctly classified at inception.</p>	<p>Additional ledger codes have now been created in the new financial management information system (FMIS).</p> <p><b>Responsible Officer:</b> Head of Corporate Finance</p> <p><b>Target Date:</b> 30 September 2015</p>	<p>We will follow this up as part of our final accounts audit work and report our findings in our annual audit report.</p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
<b>Housing benefits</b>			
4	<p>The council's guidance on the processing of benefits claims requires to be updated to reflect the introduction of the council tax reduction scheme with effect from 1 April 2013.</p> <p><b>Risk:</b> staff do not have up to date guidance on how to process claims.</p> <p><b>Recommendation:</b> the guidance should be updated.</p>	<p>This recommendation is agreed.</p> <p><b>Responsible Officer:</b> Finance Systems &amp; Change Manager</p> <p><b>Target Date:</b> 31 December 2015</p>	<p>This action has been implemented via training documentation rather than by updating the guidance. We have been advised that Council Tax Reduction is in effect Council Tax Benefit but under a different name and that the assessment rules are the same. A wider review of the procedural guidance is planned and this will change all references from council tax benefits to the council tax reduction scheme.</p> <p><b>Action complete.</b></p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
5	<p>A weekly reconciliation is undertaken between the housing benefits system and the housing information system. Our review of this reconciliation noted that a reconciling item, identified in week 35, had not been investigated and resolved by the year end. When we queried this amount, we were advised that this was a housing benefit overpayment transaction which had been posted to a rent account in error. Officers are currently investigating whether this was a system or human error so as to prevent it reoccurring.</p> <p><b>Risk:</b> the reconciliation process does not provide assurance that all transactions are complete and accurately recorded in the financial ledger.</p> <p><b>Recommendation:</b> reconciling items should be promptly investigated and cleared.</p>	<p>We will investigate the circumstances surrounding this posting, both system wise and staff error wise, to find out why the system allowed this transaction to be posted to a rent account. We will ask finance staff to create a housing benefit overpayment account through the normal interface so that the transaction can be corrected. A procedure will also be set up to identify any future occurrences and how they should be dealt with.</p> <p><b>Responsible Officer:</b> Head of Housing</p> <p><b>Target Date:</b> 31 March 2016</p>	<p>Procedure now in place to investigate HBO REN discrepancies and correct any errors found.</p> <p><b>Action complete.</b></p>



Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
<b>Housing rents</b>			
6	<p>Once the annual rent increase has been applied, changes to the weekly rent charge should be reconciled to supporting documentation as part of the weekly reconciliation process. This 'gross debit reconciliation' is not currently being undertaken.</p> <p><b>Risk:</b> rental income (and debtors) is misstated within the financial statements.</p> <p><b>Recommendation:</b> a gross debit reconciliation should be undertaken as part of the weekly reconciliation process.</p>	<p>As part of the weekly reconciliation, a gross debit reconciliation will be undertaken.</p> <p><b>Responsible Officer:</b> Head of Housing Service Finance Manager</p> <p><b>Target Date:</b> 30 November 2015</p>	<p>As noted in the table on page 5, we agreed that Internal Audit would review the housing rents system in 2015/16. Internal Audit have yet to complete their work in this area and so we will report our findings from our review of this work in our annual audit report.</p>
7	<p>A weekly reconciliation is prepared to demonstrate that all payments received from council house tenants have been correctly posted to their rent accounts and the financial ledger. Differences identified through these reconciliations are not investigated and cleared by Housing or Finance staff.</p> <p><b>Risk:</b> rent payments made by tenants are not correctly recorded in the housing information system and/or the financial ledger.</p> <p><b>Recommendation:</b> reconciling items should be promptly investigated and cleared.</p>	<p>As part of the weekly reconciliation, all differences identified will be investigated by Housing and Finance staff.</p> <p><b>Responsible Officer:</b> Head of Housing Service Finance Manager</p> <p><b>Target Date:</b> 30 November 2015</p>	<p>As noted in the table on page 5, we agreed that Internal Audit would review the housing rents system in 2015/16. Internal Audit have yet to complete their work in this area and so we will report our findings from our review of this work in our annual audit report.</p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
<b>Accounts payable</b>			
8	<p>No records are kept of telephone calls made to Her Majesty's Revenues and Customs (HMRC) to confirm a supplier's Construction Industry Scheme (CIS) status.</p> <p><b>Risk:</b> the wrong deduction rate is applied to contractor payments resulting in penalties levied by HMRC.</p> <p><b>Recommendation:</b> telephone discussions with HMRC staff about suppliers CIS status should be recorded to evidence deduction rates applied.</p>	<p>Records of telephone calls with HMRC will be kept.</p> <p><b>Responsible Officer:</b> Head of Corporate Finance</p> <p><b>Target Date:</b> 30 September 2015</p>	<p>A record of telephone calls with HMRC is now kept.</p> <p><b>Action complete.</b></p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
<b>Targeted testing on capital accounting entries</b>			
9	<p><b>Heritage assets:</b> heritage assets are to be brought on to the council's balance sheet for the first time in 2014/15 at insurance values. The council's museum collections make up £6.3 million of the £8.7 million of heritage assets identified by the council but there is no detailed listing of individual items making up this figure.</p> <p><b>Risk:</b> there is insufficient evidence to support the valuation of heritage assets disclosed within the accounts.</p> <p><b>Recommendation:</b> the council should catalogue its museum collections so that it is clear how insurance valuations have been established.</p>	<p>Museum pieces are currently catalogued on manual systems. Work is ongoing to computerise these records but due to the volume of artefacts involved this will take many years. Due to the nature of the collections it is not possible to assign values to all individual items, many of which are unique in nature and/or irreplaceable. The £6.3 million insurance valuation is based on the professional judgement of the museum curators and the council's insurance expert.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Target Date:</b> Ongoing</p>	<p>We will follow this up as part of our final accounts audit work and report our findings in our annual audit report.</p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
10	<p><b>Heritage assets:</b> the provost's chain belonging to the former Burgh of Dornoch did not pass to Highland Regional Council at reorganisation in 1975 but was instead kept, along with the ancient royal Burgh charter, within the town until July 2010 when the Community Council Chairwoman wore it to mark the First Minister's visit. Despite press coverage at the time, the council, as statutory successor to the Burgh, has yet to take possession of these heritage assets.</p> <p><b>Risk:</b> these heritage assets are not adequately insured and safeguarded against theft.</p> <p><b>Recommendation:</b> the council should take possession of these heritage assets to ensure that they are adequately insured and safeguarded against theft.</p>	<p>The Provost's chain is currently being valued and appropriate insurance and security arrangements will be put in place.</p> <p><b>Responsible Officer:</b> Director of Finance</p> <p><b>Target Date:</b> 31 March 2016</p>	<p>We will follow this up as part of our final accounts audit work and report our findings in our annual audit report.</p>

Ref.	Audit Finding	Planned Action / Responsible Officer / Target Date	Update
11	<p><b>Disposals:</b> when part of an asset which is not separately identified on the asset register is disposed of, the value of that part of asset is not removed from the asset register until the remaining asset is due to be revalued in line with the council's revaluation cycle.</p> <p><b>Risk:</b> assets are incorrectly valued on the asset register resulting in a misstatement of the financial statements.</p> <p><b>Recommendation:</b> when part of an asset is sold, the remaining part should be revalued to ensure that the year end asset register is complete and accurate prior to preparation of the accounts.</p>	<p>Procedures will be put in place to ensure that revaluations are carried out when appropriate.</p> <p><b>Responsible Officer:</b> Head of Corporate Finance</p> <p><b>Target Date:</b> 31 March 2016</p>	<p>We will follow this up as part of our final accounts audit work and report our findings in our annual audit report.</p>
12	<p><b>Disposals:</b> when carrying out a review of property disposal reports officers identified a number of assets which were sold for significant amounts which were not on the asset register. No explanation has been provided to explain why these assets were not included on the asset register.</p> <p><b>Risk:</b> the asset register does not include a complete record of all assets owned by the council.</p> <p><b>Recommendation:</b> the council should reconcile the asset register to records held by the property department to ensure the asset register is complete and accurate.</p>	<p>We are currently moving our fixed asset register to the new FMIS and are aiming to include a reconciliation with the records held by the property department as part of the process.</p> <p><b>Responsible Officer:</b> Head of Corporate Finance</p> <p><b>Target Date:</b> 31 March 2016</p>	<p>The council chose not to move its fixed assets registers to the capital accounting module within the new financial management system in 2015/16 as initially planned.</p> <p>We will follow this action up as part of our final accounts audit work and report our findings in our annual audit report.</p>

