

## INTERNAL AUDIT REPORT

**FROM:** Audit and Risk Manager                      **SUBJECT:** Main Accounting System

**TO:** Head of Finance                                      **DATE:** 25 September 2013  
Strategic Finance Manager

**C.C.** Chief Executive  
Deputy Chief Executive (AJ)  
Principal Accountants

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### 1. INTRODUCTION

- 1.1. In accordance with the Audit Plan for 2013/14, Ian Wilson, Senior Internal Auditor, has completed an examination of the above subject area and this report presents the findings and conclusions for information and action where applicable.
- 1.2. Wherever possible, results obtained have been discussed with the staff involved in the various procedures examined and their views are incorporated, where appropriate, in any recommendations made. My thanks are extended to all concerned for the help and co-operation received during the audit.

### 2. SCOPE AND OBJECTIVES OF AUDIT

- 2.1. The purpose of the examination was to report a level of assurance on the adequacy of controls to address the key risks in relation to the maintenance of the Council's accounting records and preparation of final accounts.
- 2.2. The usual cyclical approach applying elements of CIPFA Systems-Based Auditing Matrices has been followed, in this case covering all themes incorporated under the Main Accounting Systems module except for budgetary control (which is to be examined under separate assignment) and Whole of Government Accounts. The scope of assessment and testing covered the following areas:

- § Policies and Procedures
- § Financial Information System
- § Coding Structure
- § Feeder Systems
- § Journal and Internal Transactions
- § Suspense and Holding Accounts
- § Bank Reconciliations
- § Capital Accounting
- § Final Accounts

2.3 The findings are based substantially on financial data analysis and reference to documents and records available (mostly electronic material that could be retrieved directly). Clarification and further information has been sought from various staff, although mainly from the Principal Accountants Roger Wyton, Marcus Miskinis and Andy Crump.

2.4 With the exception of capital accounting and final accounts, which focused on the 2012/13 financial year, control testing has focused on activity during the current financial year to date.

### 3. FINDINGS

#### 3.1 Recommendations from Previous Report

3.1.1 The last audit report on accounting systems, issued in March 2010, produced the following recommendations:

§ During the annual review of user access the Total users report should be reconciled against the access permissions report used by the FSM;

§ All suspense accounts should be emptied on a monthly basis.

3.1.2 The user review issue was subsequently taken up by the audit of the Total system under the IT business application audit programme. The audit, reported in November 2011, concluded that adequate arrangements were in place overseen by the former Financial Services Manager. Verbal enquiries have confirmed that these still are operated, overseen by the Principal Accountant (Technical).

3.1.3 On the second recommendation, the report had highlighted an issue of some long-standing items in expenditure suspense. The practicalities of clearing this account at set intervals were challenged in response, preferring a combination of regular checks and pursuing of items more than one month old. This is taken into account in the considering findings on Suspense Accounts below.

#### 3.2 Policies and Procedures

3.2.1 The structure and content of local authority accounts is determined by a number of different influences including government legislation, government regulation, accounting standards and CIPFA. The Council's Constitution and the Code of Financial Practice make specific provisions effectively vesting authority and responsibility for the Council's accounting framework in the Head of Finance.

3.2.2 The recorded details concerning the accounting procedures that are to be followed have always been fragmented among several sources rather than a single procedural manual which the assessment model assumes. Primarily it is two Codes of Practice issued by CIPFA that govern them:

§ Code of Practice on Local Authority Accounting in the United Kingdom;

§ Service Reporting Code of Practice.

Both the above Codes are reviewed by CIPFA and re-issued annually.

- 3.2.3 From verbal discussion it was ascertained that two designated Principal Accountants have the responsibility for keeping track of changes to the relevant Codes and reviewing the accounting arrangements accordingly. They are assisted in this by attending CIPFA-sponsored seminars.
- 3.2.4 Local accounting policies are manifest in the standard text templates from which the annual Statements of Accounts are compiled (there have been some noticeable changes in recent years, especially in the realm of capital accounting). As a test, the contents of the Statement of Accounts for 2012/13 were briefly examined with reference to the Disclosure Checklist incorporated in the Accounting Code of Practice. No areas of non-compliance or lack of clarity were noticed.
- 3.2.5 The annual closure of accounts is the area seemingly best served by standard documented procedures which is understandable given the wider distribution of responsibilities corporately. Otherwise, procedural sources are generally a combination of operational and training manuals for the Total Financial Management System and any procedural notes compiled by individual staff for their own respective areas of responsibility. Excel spreadsheets are extensively used for control processes such as periodic reconciliations, thus standardised templates have evolved.
- 3.2.6 Taking into account the size and centralised nature of the accounting function with its core of highly experienced staff, the fragmented form of evidence on policy and procedures is not seen as presenting a significant issue on control assurance.

### 3.3 Financial Information System (FIS)

- 3.3.1 The Total system has now been in place for over seven years and remains subject to ongoing third party support. Application controls for Total are subject to separate review and the latest report (November 2011) did not reveal any issues on system operation.
- 3.3.2 Extracts from the FIS database and data match testing generally confirmed that the system provides financial data to relevant standards and that transactions are correctly posted promptly and correctly to the appropriate accounts. At the time of the audit the year-end balances for 2012/13 had not yet been brought forward to 2013/14, so testing was performed by data matching on the balances brought forward from 2011/12 to 2012/13 which showed no anomalies.

### 3.4 Coding Structure

- 3.4.1 The FIS is designed to ensure as far as possible that every accounting item is routed to its appropriate head via a valid financial code. Key to this is the rejection at source of debtors/creditor transactions and postings from certain feeder system interfaces where invalid codes are detected.
- 3.4.3 Access rights to create, amend or delete codes in the FIS are restricted to Accountancy staff.
- 3.4.2 A chart of accounts is maintained in Excel spreadsheet form accessible by link from the Total general ledger display available to all users with operational and enquiry-only permissions. Data match tests between the spreadsheets and Total revealed a small number of omissions in the former (since reported to Accountancy), but also a large number of cost centre codes in the spreadsheet (655 out of 1,729 entries) not represented in Total. The details have been reported for investigation.

#### **Risk**

***Avoidable postings to suspense may result from using invalid codes in feeder systems.***

#### **Recommendation**

**The Master Hierarchical Cost Centre schedule should be periodically reviewed and discontinued codes deleted.**

### 3.5 Feeder Systems

- 3.5.1 The only external feeder systems that post directly to the general ledger are the HRMS payroll and PARIS income and bank transaction processing applications. Transactions from HRMS with invalid ledger codes are posted to suspense. PARIS transactions are vetted at source against in-built recognition criteria and those that fail are either rejected on input (cash receipting entries) or posted to PARIS suspense (by far the most active of the suspense accounts). Debtors and creditors are an integrated part of the Total system and transactions in these modules are vetted on input and those with invalid ledger codes rejected.
- 3.5.2 Periodic checks ensure that the total of debit and credit postings in the ledger balance to zero and this was confirmed by direct audit test.
- 3.5.3 The review found reconciliations of debtors and creditors control accounts being performed with due regularity. Test reconciliations of debtors and creditors control accounts performed as part of the audit showed no discrepancies. The payroll net balancing account showed an uncleared balance, although not of significant amount (in consultations there was reference to a coding problems in the HRMS system awaiting remedial action by Warwickshire County Council).

3.5.4 Two feeder systems interface to the Total Creditors module – Civica OPENRevenues (rent allowances, council tax/NNDR refunds) and ActiveH (housing and corporate property repairs and maintenance). These cause cheque and BACS payments to be generated, a process which is overseen by the Financial Administration Manager.

3.5.5 In the case of Civica, the process is automated and generates e-mail alerts to the Financial Administration Manager at each run. For ActiveH the Financial Administration Manager has to request the file import. Control reconciliations for these interfaces are reviewed under separate audit assignments.

### 3.6 Journals and Internal Transactions

3.6.1 Access rights to enter ledger journals into the FIS are restricted to Accountancy staff and, for certain cost allocations, Financial Administration Team staff. There are two main types of ledger journals used on a day-to-day basis – the general journal and code correction journal. General journals are used routinely to allocate income and expenditure elements from various ‘holding’ codes, post items from some (but not all) suspense accounts and process periodic internal recharges. Code correction journals are distinguishable from general journals only by a type code in the system and their purpose is to correct coding errors discovered. Other journal types include year-end accruals and final accounts balance transfers.

3.6.2 The system automatically validates the codes at input of journals and ensures a zero net balance for all entries. All journals are uniquely numbered by the system and identify the originating users.

3.6.3 An analytical review of current year general journal transactions showed inconsistent standards in use of clear header narratives, although a sample examined showed line entry descriptions that gave clear details to compensate. Further enquiry identified those with unhelpful and seemingly unconnected header descriptions as originating from templates (a typical example was weekly allocation of leisure centre income all showing the header description ‘VAT (Dr)’).

3.6.4 It was ascertained from enquiry these ‘default’ header descriptions can be overwritten. As a good practice principle this should be encouraged.

#### **Risk**

***Clarity of journal entries does not accord with good practice.***

#### **Recommendation**

**Staff should be encouraged to enter clear header narratives in journal including overwriting default entries from journal templates where applicable.**

- 3.6.5 A test examination of what appeared to be non-routine general journals showed them to be valid with appropriate supporting information.
- 3.6.6 A similar analytical review was undertaken on code correction journals. This generally showed valid application to correct coding errors and, where appropriate, that action had been taken to prevent recurrence at source. Particularly noticeable were instances of payroll postings where required code changes or split coding arising from organisational restructure had not been made at source in the early months. Apart from these there was no further evidence of repetitive patterns suggesting failure to correct miscoding at source.
- 3.6.7 Tests confirmed that debtor accounts are not routinely raised for internal recharging and that cheques drawn payable to the Council are minimal, for valid reasons and paid in to the Council's bank accounts promptly.
- 3.7 Suspense and Holding Accounts
- 3.7.1 A search through the chart of accounts showed eight accounts with the word 'Suspense' in the title (full or abbreviated). At the time of the audit, two of them had nil balances and no current year transaction activity, and two further accounts showed nil balances and a moderate level of activity.
- 3.7.2 The other four accounts were examined more closely. The Income Suspense account had a small balance and showed evidence of daily monitoring but relies on information from sources external to Accountancy for clearing some items. The bulk of posting from this account is done through the PARIS system. The Expenditure Suspense account was the subject of the recommendation from the last report and the balance and activity patterns appear consistent with the proposed action in response.
- 3.7.3 The two accounts with the most extensive transaction activity by far are the PARIS Income Suspense and its contra equivalent 'PARIS Suspense Daily'. It is perhaps debatable whether this truly constitutes a ledger suspense account as it represents items in the PARIS system's own suspense 'bin' that failed the recognition checks and are cleared in PARIS rather than by ledger journal.
- 3.7.4 The PARIS Income Suspense balance at the time of the audit far outstripped any other of the suspense accounts at £415,000, although this represents the average influx for only a 3-day period. Unlike journals, there are authorised users in Revenues and the Document Management Centre that can clear PARIS suspense items as well as Accountancy staff.
- 3.7.5 What exactly constitutes a 'holding account' is not entirely clear from sources such as the chart of accounts and budget information. In past reviews, these were thought to include cost centres in respect of:

- § support service units;
- § rechargeable work;
- § corporate property holding accounts.

3.7.6 The corporate property holding accounts have since disappeared from the chart of accounts and a review of the rechargeable work cost centres did not show significant balances meriting further review.

3.7.7 In recent years, there has been a noticeable reversal of previous trends towards recharging from support service unit cost centres periodically throughout the year, an approach now effectively abandoned reverting to recharge at year-end only. It is assumed that the influence of lean systems principles has contributed towards this.

3.7.8 Holding 'codes' from which allocations are made at regular intervals have been revealed from the review of journals. In terms of expenditure involved, the principal services where there is a periodic recharge in evidence are:

- § Media Room services, and printer/copier charges;
- § Warwickshire County Council Legal Services charges and disbursements.

### 3.8 Bank Reconciliations

3.8.1 The examination confirmed that regular reconciliations are performed monthly by a designated Accountancy officer and signed off by an independent senior officer.

3.8.2 At the time of the audit, the Income reconciliation had been completed up to the end of July 2013 and Expenditure reconciliation completed to June with July in progress.

3.8.3 Test checks of base ledger and bank figures were successfully verified to source records.

### 3.9 Capital Accounting

3.9.1 This area had been previously reviewed as a separate assignment and only brought back into the main accounting stream in the 2013 audit planning process. This last review was reported in September 2012.

3.9.2 The examination has re-confirmed the following controls in place:

- § clear policies on capital charges, valuations and depreciation in accordance with relevant codes of practice, guideline, etc.;
- § an effective asset register system maintained and underpinned by adequate supporting evidence including annual reconciliation to accounting records;

§ position on capital expenditure reported quarterly to the managing body (Executive).

### 3.10 Final Accounts

3.10.1 The audit examination coincided with statutory audit of accounts. In view of this, a 'light touch' review of this area was preferred focusing on evidence of process.

3.10.2 The examination confirmed effective procedures and controls in place to ensure an orderly close-down process and preparation of the final accounts within key deadlines and in accordance with relevant standards and regulations.

## 4 CONCLUSIONS

4.1 The examination has concluded that a robust control framework is established for the Council's accounting operations. The findings give SUBSTANTIAL assurance that the structures and processes operate effectively to manage the applicable risks.

4.2 Two minor reservations emerged relating to the accuracy of the primary record of valid ledger codes and clarity of journal descriptions.

## 5 MANAGEMENT ACTION

5.1 The recommendations incorporated to address these areas are reproduced in the appended Action Plan for management response.

Richard Barr  
Audit and Risk Manager