

**Audit Reports with Moderate or Low Level of Assurance issued
Quarter 1 2019/20**

Loans to External Organisations – 6 June 2019

1 Introduction

- 1.1 In accordance with the Audit Plan for 2019/20, an examination of the above subject area has been undertaken and this report presents the findings and conclusions drawn from the audit for information and action where appropriate.
- 1.2 Wherever possible, findings have been discussed with the staff involved in the procedures examined and their views are incorporated, where appropriate, into the report. My thanks are extended to all concerned for the help and cooperation received during the audit.

2 Background

- 2.1 Loans to external organisations is a new venture which began with the first being set up in December 2017.
- 2.2 Since the first loan was set up there have been an additional eight loans allocated to external organisations. There are currently six active loans and a further two approved but not yet active.
- 2.3 The total sum for the nine approved loans is £8,362,642 with interest rates ranging from 0%-10%.

3 Scope and Objectives of the Audit

- 3.1 The audit was undertaken to test the management and financial controls in place.
- 3.2 In terms of scope, the audit covered the following areas:
- Loan availability and application
 - Loan approval
 - Repayment of loans
- 3.3 The audit programme identified the expected controls. The control objectives examined were:
- Applications are available to all qualifying external organisations.
 - Applications are valid and submitted correctly.
 - Loans are approved and allocated fairly.
 - The Council will not be disadvantaged through the non-repayment of loans.

- The Council achieves a good rate of return on its finances.
- Loans are lawful.
- Relevant documentation is available for allocated loans.
- Insurance implications are considered.
- Loans are monitored and used for their intended purpose.
- Loan funding is transferred to the correct bank account and in a timely manner.
- Payments are banked correctly.
- Late payments and arrears are recovered.
- Write-offs are appropriate.

4 **Findings**

4.1 **Recommendations from Previous Report**

4.1.1 There are no previous recommendations due to this being a new audit.

4.2 **Loan Availability and Application**

4.2.1 Loan funding and availability is not currently advertised publicly. As there is not a set amount of money available for loans, senior management contend that publicising or promoting the availability would attract an excessive number of applications, most of which could not be supported. Counter-balanced against that is obviously the issue of transparency and possibly even the principle of equity.

4.2.2 In general, loans are used to help support organisations within the local community when lending is seen as a viable solution to their problems. This is over and above the RUCIS grants process that is also in place. Some larger loans are also made available where the monies are to be used to help the Council achieve its aims in relation to the Local Plan.

4.2.3 However, there is currently no formal application process in place that would allow for any organisations approaching the Council for funding to know how their enquiries will be dealt with.

Risk

There may be a reputational risk if other organisations or council tax payers feel that funds are loaned unfairly.

Recommendation

To prevent loans being allocated to selected applicants, an application process should be formed. This will allow a fair and equal opportunity for a wider audience to apply.

4.2.4 All loans had either a business plan or business cases to support them, with four cases having both a business plan and a business case in place. There were four business plans and seven business cases documented and saved with the relevant loan information.

- 4.2.5 These supporting documents provide the Council with information on the way the business is run, the financial details, how the loan funds will be spent and the expected outcome. There is a business plan template available for applicants to use.
- 4.2.6 Not all applicants are able to provide business plans (e.g. community groups). In these situations, business cases are used to support the application. These are presented to Committee as reports with the relevant information included for consideration.
- 4.3 **Loan Approval**
- 4.3.1 There is no formal policy in place for providing loans to external organisations. However, business plans and cases are used to support the applications which are presented to Executive Committee for approval. All loans have been approved this way with some also being presented to full Council.
- Risk**
- Loans may be issued incorrectly.**
- Recommendation**
- The Council should consider establishing a formal policy and set of procedures to use when providing loans to external organisations. This will help to ensure approvals are fair and a good investment for the Council.**
- 4.3.2 Credit checks are not always carried out due to the type of organisations requiring funding (e.g. some are community groups for which credit checks aren't possible). Credit checks have been carried out for four of the loans and documentation has been retained, although there was no central file into which all relevant documentation was held.
- Advisory**
- Consider storing all loan information securely, in a central repository, so that relevant staff can locate and access the information held.**
- 4.3.3 Accounts were provided for the four companies that had produced a business plan. Where business plans were not suitable, business cases have provided information that assess affordability and the risk of non-repayment. There were business plans or cases available to support all of the applications. The Head of Finance confirmed that business plans or business cases had been reviewed for all loans issued, with checks carried out using the information provided in them.
- 4.3.4 Four of the six active loans have security in place. This is documented in the loan agreements and supported by separate legal documentation. The two without security are Council-owned buildings which are leased to the

organisations. In these cases, any non-repayment could result in early termination of the lease.

- 4.3.5 Where parent company guarantors have been used, credit checks have been carried out on them and these have been documented.
- 4.3.6 The Head of Finance calculates the interest rates charged for each case. Although it often doesn't apply, State Aid helps to inform the rate of interest charged. Each case is viewed on an individual basis taking into account the information provided in the business plan, the amount of funding and the length of the term. Interest calculations and borrowing schedules were documented for all active and closed loans.
- 4.3.7 However, whilst the documentation in relation to each loan has been provided, there is no formal risk assessment process in place to follow when loan provision is being considered. This would form part of the formal policy and procedures if they were to be put in place.
- 4.3.8 There were signed and dated agreements in place for all of the active loans. They set out the terms and conditions and include the amount borrowed and the interest rates. Some specify when repayments should begin whilst others refer to a repayment plan which is provided to the borrower separately. In one case, funds had been sent before the agreement had been signed. Loans issued since this have all had checks carried out to ensure relevant signed paperwork was in place before issuing funds.
- 4.3.9 The signed legal agreements provided were stored in secure folders on the server with limited access.
- 4.3.10 Where loans are being used to improve properties owned and insured by the Council, the Insurance and Risk Officer is not being informed of the changes.

Risk

There may be insurance implications where changes have been made to Council-owned properties.

Recommendation

Changes made to Warwick District Council properties, using loan funds, should be reported to the Insurance and Risk Officer in a timely manner.

4.4 Repayment of Loans

- 4.4.1 Checks are carried out to ensure that loans are used for their intended purpose. Funds are only released when drawdown requests have been completed and presented with copies of invoices for the work carried out. Drawdown requests and invoices were provided for all of the active loans.
- 4.4.2 Bank details are checked by the Finance Admin Manager before any payments are transferred. Payments can only be sent on set days and these

are set out in the signed agreements.

- 4.4.3 Repayment has begun for three of the active loans. One borrower was due to start repaying their loan in July 2018 but has had the date postponed three times. They have now begun making payments as of April 2019.
- 4.4.4 In the case where the borrower had failed to begin making repayments, input from Legal Services was requested after six months of non-payment. This has resulted in a new payment plan being set up with a postponed repayment start date. A direct debit has been agreed and actioned and any further failure to make payments may result in termination of the lease and legal action to recover funds from the property used as security.
- 4.4.5 The Finance Admin Manager monitors repayments, following up on any that are missed or late. Initially he contacts the organisation with a reminder to pay. If there is continued non-repayment, he involves the Chief Executive or the Deputy Chief Executive and requests input from Legal Services.
- 4.4.6 As yet, no loans have been written off and there is no intention to write off any loans until all other recovery methods have been exhausted.

5 **Summary & Conclusion**

- 5.1 Following our review, we are able to give an overall MODERATE degree of assurance that the systems and controls that are currently in place in respect of Loans to External Organisations are appropriate and are working effectively.
- 5.2 The auditor noted that the processes followed had evolved reducing the risks since the first loans had been provided. We would have been able to give a SUBSTANTIAL level of assurance if there had been a policy or procedure in place to support this. However, due to the lack of transparency when providing loans, we feel we cannot give an overall level of substantial assurance at this time.
- 5.3 The assurance bands are shown below:

Level of Assurance	Definition
Substantial Assurance	There is a sound system of control in place and compliance with the key controls.
Moderate Assurance	Whilst the system of control is broadly satisfactory, some controls are weak or non-existent and there is non-compliance with several controls.
Limited Assurance	The system of control is generally weak and there is non-compliance with controls that do exist.

- 5.4 There were issues, however, identified during the course of the audit relating to:
- An omission of an application process.
 - An absence of a formal policy.

- The lack of timely notification to the Insurance & Risk Officer regarding changes to Council-owned properties.

5.5 A further 'issue' was identified where an advisory note has been reported. In this instance, no formal recommendation is thought to be warranted as there is no risk if the action is not taken. However, if the changes are made, the existing control framework would be enhanced. This is in respect of loans documentation being stored securely in one central repository.

6 **Management Action**

6.1 The recommendations arising above are reproduced in the Action Plan for management attention.