

## INTERNAL AUDIT REPORT

**FROM:** Audit and Risk Manager  
**TO:** Head of Finance  
**C.C.** Chief Executive  
Finance Administration  
Manager  
Senior Finance Administration  
Officer

**SUBJECT:** Mortgages  
**DATE:** 1 February 2013

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### 1 Introduction

- 1.1 In accordance with the Audit Plan for 2012/13, 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. This topic was last audited in September 2009.
- 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 No mortgages have been granted by the council since 1993 when the requirement for councils to provide mortgages, under the right to buy legislation, ended.
- 2.2 At the time of the last audit in 2009 there were ten mortgages still running and there was a balance outstanding of approximately £54,000.
- 2.3 All outstanding mortgages are due to mature by July 2015.

### 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:
- Accounting
  - Interest rates
  - Arrears
  - Insurance
  - Redemption

3.3 The audit programme identified the expected controls. The control objectives examined were:

- Appropriate and up-to-date information is held regarding the status of each mortgage.
- An appropriate interest rate is used for each mortgage.
- Correct amounts of interest are charged on each outstanding mortgage.
- Appropriate action is taken to reduce arrears.
- Appropriate efforts are made to recover debts before they are written off.
- The provision of insurance for mortgagees is cost neutral for the council.
- The council receives assurance that mortgaged properties are appropriately insured.
- The council receives the correct amount when mortgages are redeemed.

## **4 Findings**

### **4.1 Accounting**

- 4.1.1 Individual spreadsheets are maintained for each mortgage, as opposed to using a specific system. Each spreadsheet includes calculations for the monthly debit, worked out for every six months using the relevant interest rates and insurance premiums (see below) and these, along with any payments recorded, are carried forward into a summary spreadsheet that calculates the remaining, outstanding balance.
- 4.1.2 The spreadsheets were set up in 2008/09 and were run in tandem with the Reallink system for a year. The relevant Principal Accountant advised that this change was borne out of necessity as the old system was no longer supported. The use of spreadsheets was considered to be the most cost effective method of managing the few mortgages that remained at the time.
- 4.1.3 He also advised that the tandem running performed had confirmed that the spreadsheets were calculating the figures correctly in line with the old system. As a result of this, detailed testing on the formulae within the spreadsheets was not performed, although a cursory overview suggested that they were correct. There was an additional control in that, when the spreadsheets were provided to me, the majority of the worksheets were locked, with only a few cells allowing data entry (for payments etc.).
- 4.1.4 Payments received in respect of each mortgage are identified on a monthly basis by the Senior Finance Administration Officer (SFAO) via a review of the PARIS Income Management software.
- 4.1.5 A report was produced from PARIS showing all of the payments into the relevant fund and these were checked against the relevant mortgage spreadsheets. This test confirmed that all payments had been credited appropriately.

### **4.2 Interest Rates**

- 4.2.1 The SFAO advised that the interest rates are provided by one of the Principal Accountants, based on information provided by the Department for Communities and Local Government (DCLG).
- 4.2.2 The last update, on file, from the DCLG was received in 2009. The Principal Accountant advised that he had not received any updates since then and, as the council had not had any external borrowing until recently, the figure set by the Secretary of State was still in force.
- 4.2.3 Upon review of the mortgage spreadsheets it was confirmed that this interest rate was reflected appropriately.
- 4.2.4 The calculation of the interest payments is undertaken via formulae within the spreadsheets (see above). It was noted, however, that there is no interest being charged regarding an account in arrears (see below) as the principal was shown as being paid off and no interest calculations were performed regarding the outstanding debt.

4.2.5 A recommendation would normally be made to rectify this. However, a write-off of this outstanding balance is proposed that would make such a recommendation obsolete (see below). However, should a decision be made not to write off this debt, then this may need to be revisited.

### **4.3 Arrears**

4.3.1 The SFAO advised that reminder letters may be sent to mortgagees that have not made a payment for a long time. He indicated that the recovery process would be the same as for other sundry debts, although powers would be limited as the council already holds a charge on the property.

4.3.2 As noted above, there is currently one account in arrears. Sporadic payments are being made into this account, although they are mainly to pay the insurance premium for the year and are not reducing the balance.

4.3.3 All of the other accounts are in 'positive' arrears. Neither the SFAO or the relevant Principal Accountant were aware of the terms and conditions of the mortgages as to whether overpayments were allowed to be made in order to reduce the principal sum outstanding and the associated interest payments.

4.3.4 Overpayments totalling £2,042.27 had been made on these four accounts (as at the time of the last scheduled payments), ranging between £156.98 and £754.20.

### **Risk**

**Payments may not be being dealt with correctly under the agreed terms and conditions.**

### **Recommendation**

**A decision needs to be reached as to how these overpayments are dealt with (either being repaid or being used to calculate amended terms and interest payments in future if this is allowed for under the terms and conditions of the mortgages).**

**(NB precedent may have been set as a previous overpayment on one of these accounts had been used to reduce the principal outstanding following the previous audit report.)**

4.3.5 The SFAO advised that, as far as he was aware, none of the mortgages had been written off, apart from small amounts outstanding due to differences when accounts were redeemed.

4.3.6 The possibility of writing off the one account in arrears was raised by the SFAO as he suggested that it was costing more in staff time to deal with the account than was actually outstanding.

4.3.7 This was raised with the Strategic Finance Manager and the relevant Principal Accountant and it was suggested that there was no reason why this couldn't be undertaken. However, as it was a Housing debt, the Head of Housing & Property Services would be responsible for authorising the write off. An email has been sent to him, although a response is still awaited.

## **Risk**

**Costs to the council, in terms of staff resources, are greater than the amount that can be recovered from the mortgagee.**

## **Recommendation**

**Action should be taken as appropriate upon receipt of the response from the Head of Housing & Property Services.**

### **4.4 Insurance**

- 4.4.1 The SFAO informed Internal Audit that four of the current mortgagees have their insurance arranged through the council. This was confirmed upon receipt of a spreadsheet from the Insurance & Risk Officer (IRO).
- 4.4.2 Upon review of the mortgage spreadsheets, it was confirmed that these charges were found to be included as appropriate.
- 4.4.3 The other mortgagee arranges their own buildings insurance. Whilst evidence had previously been obtained to verify that this insurance was indeed in place, there were no current details held.
- 4.4.4 Upon discussion with both the SFAO and IRO they each assumed that the other was chasing this up.

## **Risk**

**A property which the council holds a mortgage interest in is not appropriately insured.**

## **Recommendation**

**The mortgagee who arranges her own buildings insurance should be contacted to obtain evidence that this insurance is in place.**

### **4.5 Redemption**

- 4.5.1 The SFAO advised that he has written to all outstanding mortgagees a couple of times in the last five years, asking if they want to redeem their mortgage and has provided redemption statements to them.
- 4.5.2 The calculations are performed on the mortgage spreadsheets, by entering the expected redemption date. A sample calculation was performed on one of the spreadsheets and it was found to calculate the correct figure (assuming that the current overpayment does not reduce future interest payments as highlighted above).
- 4.5.3 One mortgage had recently been redeemed, although this was one that was in arrears and interest was not being charged, so there was no real calculation to be made. A payment was made by the mortgagee that almost cleared the balance and a small amount was written off.

## **5 Summary & Conclusion**

- 5.1 Following our review, we are able to give a SUBSTANTIAL degree of assurance that the systems and controls in place for the management of Mortgages are appropriate and are working effectively.
- 5.2 Minor issues were, however, identified relating to the method of dealing with overpayments, the ability to write off one outstanding mortgage that is in arrears and the lack of evidence obtained with regards to buildings insurance where the mortgagee arranges their own insurance.
- 5.3 A further issue was identified relating to the charging of interest where an account was in arrears. However, as this debt may be written off, it was not felt necessary to raise a recommendation in relation to this issue.

## **6 Management Action**

- 6.1 The recommendations arising above are reproduced in the attached Action Plan (Appendix A) for management attention.

Richard Barr  
Audit and Risk Manager