

Report to the Corporate Governance Committee

Subject: Review of the Effectiveness of Key Controls (Financial Regulations)

Date: 8 February 2024

Introduction

Along with the Standing Orders, the Financial Regulations are another cornerstone of Stanway Parish Council's nascent risk management framework. The Financial Regulations set out policy statements and the Key Controls¹ for the management of the Council's financial affairs. Although the Financial Regulations were revised in September 2023 when the wording was simplified, save for one new procedure (relating to purchase orders), all Key Controls are the same as earlier versions of the Financial Regulations dating back to at least 2007.

Bases for and Limitations of the Review

To be confident in a system of internal control, it is necessary to monitor the Key Controls and periodically assess their effectiveness. Not only are periodic reviews part of basic risk management, but they are also embodied in the Annual Governance Statement declared individually by each member including the statement: 'We maintained an adequate system of internal control . . . and reviewed its effectiveness [emphasis added]'.

This first ever review:

- looked at the effectiveness of Key Controls in three operational areas: (1) Procurement and Payments; (2) Counterparty Credit Exposure Management; and (3) Bank Account Signatories;
- is an impartial appraisal of whether Key Controls operated as intended; and
- is not a deep dive investigation of causes and impacts.

The numbers against the Key Controls in the following commentary correspond to the numbered paragraph within the Financial Regulations.

Procurement and Payments

Several Key Controls are in place to: contain expenditure within budgets; deliver value for money; minimise legal risk; and ensure money is not lost through fraud, dishonesty or error. At Annexure One there is a one-page overview giving the purpose of each Key Control and assessing its effectiveness.

During the period 1 October to 31 December 2023, the Council made 154 payments totalling £76,269. Of these, 53 payments (around one third) were made despite one or more Control Failures². The more frequent Control Failures were as follows:

- 19 payments when a Purchase Order had not been issued (Key Control 20.3 and 20.4);
- 17 payments after the invoice had missed the cut-off (Key Control 21.1);
- 16 payments to suppliers with which there was no written contract (Key Control 20.5); and
- 16 payments to new suppliers when identity and bank details had not been verified (Key Control 21.10).

On each occasion, payments were added to a Payments List (Key Control 21.2) and subsequently resolved for payment by the Corporate Governance Committee (Key Control 21.3) despite identified Control Failures.

Counterparty Exposure Management

Owing to the size of its budget, the Council is unlikely to qualify for the protections of the Financial Services Compensation Scheme. Therefore, to mitigate the downside risk of counterparty default, Key Controls prescribe limits for deposits in a single account and the total of all deposits with a single financial institution.

The following deposits breached the prescribed limits:

- As of 31 January 2024, the balance of the current account with Unity Trust Bank was £188,651 (Key Control 8.8 and 8.11).
- As of 19 December 2023, the balance of the deposit account with Barclays Bank UK PLC was £66,842 (Key Control 8.9).

Bank Account Signatories

Key Controls limit access to bank accounts and require 'four eyes' authentication to ensure: payments are checked and properly authorised; and money is not lost through dishonesty or error.

A third party (who is neither an Officer nor a Member of the Council) is a signatory to the accounts with Nationwide Building Society and Barclays Bank UK PLC (Key Control 8.3). That person was encouraged to countersign payment transaction instructions (Key Control 8.5 and 22.2).

Summary of Findings

This review assessed the effectiveness of Key Controls in only three areas of operation and, in respect of payments, reviewed only one quarter's information. Although no resultant losses were identified, Control Failures are apparent across the Council's operations, which indicates weaknesses in the system of internal control. Left unaddressed such weaknesses may lead to financial, reputational, legal, regulatory, security, and operational consequences.

Of particular note is the ongoing failure of Key Controls relating to access to bank accounts which puts more than one third of the Council's current cash holdings at increased risk of loss. In light of the values at risk, this is regarded as a materially significant Control Failure.

Related to the failure of the Key Controls for access to bank accounts, is the failure of the Key Controls to mitigate the risk of counterparty default, resulting in another third of the Council's cash holdings being exposed to increased risk of loss.

The Corporate Governance Committee previously raised concerns regarding the failure of Key Controls for procurement and supplier engagement. This review found these operational activities continue to present challenges, with Control Failures identified in around one third of payments. Although many of the individual payments were less than £100, a total of £16,905 was at increased risk of loss during the last quarter of 2023.

Remedial Actions

It is beyond the scope of the review to recommend specific actions to remedy the identified Control Failures; however, the Corporate Governance Committee should consider the findings and determine what actions are appropriate.

Guide to terms used in this paper.

¹ 'Key Controls' are the primary procedures relied upon to mitigate a risk or to prevent a loss.

² 'Control Failure' denotes the failure of a Key Control to operate as expected regardless of whether the outcome is positive, negative or neutral.

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Effectiveness of Key Controls (Financial Regulations - Payments Processes)

Period from: 01/10/2023
 Period to: 31/12/2023
 Overall control effectiveness this period Ineffective - More than 10pc of payments with Control Failures
 Number of payments this period 154
 Value of payments this period (£) 79,142
 Value of payments made with control failures (£) 16,905
 Number of control failures 122
 Number of payments made with control failures 53 (34%)
 Number of payments made with more than one control failures 35 (23%)
 Number of payments made with more than three control failures 12 (8%)

Financial Regulation	Key Control statement	Purpose of the Key Control	Key Control Effectiveness	Number of Control Failures
FR18.2	Expenditure will not be authorised unless the Council has the statutory legal power to incur such expenditure.	The Council has the legal power to spend public money		0
FR18.3	Expenditure will not be authorised that exceeds the budget for that cost code, other than by resolution of the ...	Revenue expenditure remains within budget		3
FR18.4	Capital expenditure will not be authorised unless adequate funds have been secured from grants, loans or a ...	Capital expenditure is not incurred without adequate funding from grants or loans		0
FR18.6	Expenditure will be authorised up to the budget for that cost code, subject to the authority thresholds in the ...	Expenditure is authorised at a level commensurate with the value of the spend		4
FR19.3	The basic procedure for the selection of a supplier for goods or services will be as given in the following table ...	Contracts for goods and services represent value for money		0
FR19.4	All invitations to tender and requests for proposals issued by the Council will ...	Quotes and tenders from different suppliers can be compared on a like-for-like basis		12
FR19.6	The decision as to the selection of the supplier ... will be minuted or recorded in an email.	Decisions are properly recorded		1
FR20.3 & FR20.4	The RFO will not issue a purchase order for any proposed supply that does not conform with all applicable paragraphs ...	Orders to suppliers are supported by appropriate written instructions		19
FR20.5	All supplies will be subject to a written agreement between the Council and the supplier ...	Agreements with suppliers are in writing		16
FR21.1	Invoices for payment will be delivered to the RFO no later than five working days before the meeting at which payment is ...	Invoices match supplier agreements and purchase orders		17
FR21.2 & FR21.3	... reject any invoice that does not satisfy the criteria set out in paragraphs ...	Payments are not made if controls are not observed		25
FR21.4	... will review such list and, having satisfied itself that payments are due, will resolve to authorise the payments.	Payments are not made if controls are not observed		9
FR21.7	On occasion it may be necessary to approve a payment outside the cycle of regular meetings ...	Ad hoc payments are properly approved		0
FR21.10	... details of a current supplier, especially bank account information, will be verified and approved in writing ...	Payments are made to the right counterparty		16
FR22.1	... the Clerk or the RFO will instruct the Council's bankers to make a payment.	Bank instructions are properly set up		0
FR22.2	... instruction for payment ... will be ... authorised by at least two persons, at least one of whom will be a Member.	Bank instructions are properly authorised		0

Key:

More than 5pc Control Failures
 Fewer than 5pc Control Failures
 No Control Failures