Paul Manning
Executive Director of Finance and Corporate Resources
South Lanarkshire Council
Council HQ
Almada Street
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Dear Paul

South Lanarkshire Council - Review of internal controls in financial systems 2019/20

1. 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 regulation.

2. Our interim work is used to inform our approach to the audit of the annual accounts. Interim audit work includes controls testing, income and expenditure verification and wider dimension audit work. We set out our programme of work in the annual audit plan submitted to the Risk and Audit Scrutiny Committee of 19 February. Our interim audit work was interrupted by the outbreak of COVID-19 and the consequent suppression measures put in place by the UK and Scottish governments. This has meant that we have been unable to complete our audit testing or wider dimension work at the interim stage. We will, where possible, complete programmed work alongside our annual accounts audit work or adjust our audit approach as necessary. We will include comment, as appropriate, in our annual audit report.

3. Our annual audit plan indicated that we would submit a management report for the consideration of management and members at the June meeting of the Risk and Audit Scrutiny Committee. As the council have been operating under modified governance arrangements and as the scope of our work has been reduced, we have elected to provide the shorter version of our interim reporting options, a management letter, concluding on work completed to date.

4. Weaknesses identified represent those that have come to our attention during the audit work completed to date and are therefore not necessarily all of the weaknesses which may exist. It is the responsibility of management to decide on the nature and extent of the internal control system appropriate to the council.

Conclusions

5. We are reporting solely on those elements of interim work completed to date. On the basis of this audit work, we concluded that system controls are operating as specified and that there are no issues which would impact on out audit approach. However, we have identified IT systems access as an area where controls could be strengthened.

System coverage

6. The key systems that were, or were to be, tested at the interim audit stage were as follows:

- General ledger
- Payroll
- Council tax
- Non-domestic rates

- Accounts receivable
- Accounts payable
- Housing rents
- Cash and banking

Key findings

System user access

7. System access is a fundamental IT control to ensure system security and data integrity. Users of the Oracle system are assigned user profiles which are intended to enforce segregation of duties to ensure officers have appropriate permissions to carry out specified tasks. A yearly audit review is usually carried out to ensure users' access levels are appropriate. This has not been completed for 2019/20.

> **Management response**
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> The delay in the completion of the annual user audit was due to staff bereavement. The audit is now complete.

8. The Bankline system is a secure online banking system which allows the council to manage cashflow and make payments to suppliers. There is no formal review of users' access to the Bankline system. We also noted that there is no formal communication process in place to remove former employees timeously from the system.

9. The absence of periodic reviews of users' systems access rights and failure to timeously remove staff no longer needing access, entails a higher risk of fraud or error.

> **Management response**
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> While a formal quarterly review process has been implemented, it should be noted that there were already a number of other controls in place which mitigate any financial risk to the Council. These include the fact that there are only a few named individuals able to make external payments and that all payments (and transfers) require two users to process – one to set up the payment and one to authorise. No user can set up and authorise the same payment or transfer. For payments and transfers greater than £15m three users are required – one to set up the payment and two to authorise. Other users have either read only, or can only transfer monies between internal accounts, and therefore there is no financial risk.

Approval of journal entries

10. The council's financial ledger is the system for recording all transactions and preparing the financial statements. Journal entries are how the council's financial ledger is manually updated. To minimise the risk of error and fraud we would expect each journal entry to be prepared and authorised by different members of staff. This control is not in operation.

11. The ability of officers to approve their own journals increases the risk that invalid, erroneous or fraudulent journals could be posted to the financial ledger. We have previously reported this as an area of risk and management have asserted that any risk is mitigated by other controls in place.

National fraud initiative

12. The National Fraud Initiative (NFI) in Scotland brings together data from local government, health boards and other public sector bodies. Matching data obtained from the systems of participating bodies allows the identification of potentially fraudulent claims on the public purse including housing benefit fraud, occupational pension fraud and payroll fraud. If fraud or overpayments are not identified in a body, and the NFI exercise has been undertaken properly, assurances may be taken about internal arrangements for preventing and detecting fraud.

13. Participating bodies received matches for investigation in January 2019. All recommended matches plus any further matches based on findings and the risk of error or fraud should have been investigated by 30 September 2019 and the results recorded on the NFI system.

14. We can confirm that the council has investigated all high risk matches and updated the NFI system as required.

Best Value

15. Best Value is assessed over the five-year audit appointment as part of the annual audit work. A Best Value Assurance Report (BVAR) for South Lanarkshire Council was published in March 2019. In response to the report an action plan that was approved by the council in June 2019.

16. An action plan update was reported to the Performance and Review Scrutiny Forum in February 2020. We have held initial discussions with management on the reported progress and we will provide an update on the BVAR recommendations in our annual audit report.

Acknowledgement

17. The contents of this letter 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.

Yours sincerely

Fiona Mitchell-Knight

Audit Director