

## Agenda Item 3 AUDIT REPORT

### Summary

To report on the Council's Governance arrangements prior to the May 2019 elections and up to the dismissal of our Clerk.

### Background

Following the dismissal of our Clerk the rather slow return of the Council's papers has gradually revealed issues with our financial controls and flaws in our risk management. This paper highlights matters, or possible omissions, that have come to light and their potential consequences.

### Legal

The Accounts and Audit Regulations 2015 require smaller authorities, each financial year, to conduct a review of the effectiveness of the system of internal control and prepare an Annual Governance statement;

The Local Audit (Smaller Authorities) Regulations 2015; Local Audit and Accountability Act 2014

### Details

#### 1.0 Internal Audit

1.1 Following the abolition of the Audit Commission a new organisation was established to be responsible for issuing proper practice directions in relation to the accounts and financial controls of smaller authorities such as Parton. There was also created a body to appoint an auditor to smaller Councils unless they are exempt from close external monitoring such as Parton. That body for Cumbria is the firm of PKF Littlejohn whose main offices are in London. Members, around last May time, may remember that we were advised that we were an exempt authority from the full rigours of that auditing regime and could certify that we were exempt. Broadly that exemption applies to Council with expenditure of less than £25,000. Rather simplistically Government seemed to think that the additional financial burden on accounts costs were not merited for Council's with small levels of expenditure. That appears to have been a financially based view only. We are still obliged to provide an Annual Governance statement (known as AGAR) to those accountants after considering our Internal Auditor's report. These can be found in the Finance section of our web site and links are provided later on in this report. Those documents have to be correct.

1.2 The purpose of the annual governance statement is for the Council to report publicly, to its electors, on its arrangements for ensuring that its business is conducted in accordance with the law, regulations and proper practices and that public money is safeguarded and properly accounted for.

1.3. Regulation 5(1) of the Accounts and Audit Regulations 2015 requires our Council to *"undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance."* Whilst the public sector internal audit standards, issued in 2013, have not been applied to smaller authorities, such as Parton, the Regulations do oblige us to take into account non-statutory guidance in undertaking an effective internal audit. This report addresses the guidance and our apparent failures.

1.4 The Parish Council should have an independent internal auditor who is to give an opinion of the Parish Council's internal controls. From my own examination of the records passed back to us from our former Clerk I do have some concerns as to the veracity of the AGAR documents we have approved over the years and which have been signed by our former Chair and Clerk. This concern is particularly relevant to the financial year ending May 2019. Further, whilst our Internal Auditor's report has always comprised of the formal AGAR document only (a tick box statement which can be found here <https://partonparishcouncilcom.files.wordpress.com/2019/11/annual-internal-audit-report-2018-19.pdf> ), and which is the minimum requirement, many a Parish Council calls for an additional formal written report from their Internal Auditor. We have never done so. As a result our Internal Auditor does not seem to have been before Council, as far as I can see, to be questioned on our former Clerk's financial controls. I will refer later (para 5.1) to some parts of the Auditor's AGAR report that seem to be at odds with the facts set out in this report. It is the Internal Auditor's responses on his AGAR document that inform the Parish Council's responses to the assertions we make when we tick boxes in our annual governance statement (<https://partonparishcouncilcom.files.wordpress.com/2019/11/annual-governance-and-accountability-return-201819-part-2-1.pdf>). If the Auditor's form is incorrect then so is our Governance statement.

1.5 Another purpose of internal audit is to review and report to the Council on whether its systems of financial and other internal controls over its activities and operating procedures are effective.

1.6 The person or persons carrying out internal audit must be independent with an absence of any actual or perceived conflict of interest. He/she must be competent to carry out the role in a way that meets the business needs of the Council. It is for the Parish Council to decide, given its circumstances, what level of competency is appropriate, and to keep this issue under review. I have not been able to find either evidence that the Council has set out the nature of competencies it requires nor that it has undertaken any reviews. In fact I cannot find evidence that the Council ever made a decision to seek an Internal Auditor or set out any person specification. Whilst the Council has regularly agreed to re-employ our Internal Auditor each year it does not seem to have set out the T's and C's of his appointment. In the papers returned by our former Clerk I have not found any letter or formal contract of engagement with that auditor. Recommended practice indicates that *"The work of internal audit should be subject to an engagement letter on first appointment by the authority, setting out the terms of the appointment."* We seem to be in breach of that obligation.

1.7 Internal audit is also an on-going function which should be undertaken regularly throughout the financial year to test the continuing existence and adequacy of the authority's internal controls. It should result in an annual assurance report to members designed to improve effectiveness and efficiency of the activities and operating procedures under the authority's control. Each year we are advised that all is in order and as a result we have not taken action over procedures or to review their operation. In my view a proper review is long overdue.

1.8 We should, at least annually, carry out a review of the effectiveness of our overall internal audit arrangements and that should include an assessment of

- the scope of internal audit;
- independence;
- competence;
- relationships with the clerk and the authority; and

- audit planning and reporting.

We don't do that. It has to be undertaken by members and cannot be delegated to an officer. Our Clerk does not seem to have guided us on the need for such reviews. Despite that failure we duly certify each year that our Governance is fine! We should, perhaps, consider setting up a small working party to carry out the review and report the results to a full meeting of the Council.

1.9 I have not found any evidence that our Internal Auditor actually exists. The former Clerk has declined on about six occasions now to provide me with his contact details even though we apparently employ that auditor and so should hold that information. On the fourth time of asking the former clerk alleged that that alleged auditor does not wish to provide his contact details. This simply beggars belief. Mr Young, our former Chair did have an advance copy of this report, principally for his view as to whether he objected to its public disclosure and he did not express any view. It may be noteworthy that he did not challenge the suggestion that the Internal Auditor may not exist. When the Clerk was advised that his appeal against dismissal would not proceed until he provided the contact details of the Auditor he withdrew his appeal. I will leave you to form your own view on whether the auditor exists. The question needs to be resolved.

## 2. Objectives of the Audit

2.1. To examine the system of internal controls to ensure that the Parish Council may obtain an adequate level of assurance for its activities.

## 3. Scope of the Work and the areas of Audit Work examined.

3.1 The Scope of Work for an auditor covers the eleven key control tests identified in the Internal Audit part of the AGAR. (<https://partonparishcouncilcom.files.wordpress.com/2019/11/annual-Internal-audit-report-2018-19.pdf>) Only ten of these need to be examined as the Parish Council does not have any petty cash.

3.2. To properly complete the audit the following areas of activity must be examined and tested by the Internal Auditor:

- Payroll arrangements
- Creditors – proper invoices and VAT details and payments for items properly approved of by Council
- Risk Management
- Income collection and Banking arrangements
- Accounting records,
- Assets
- Debtors
- Budgetary Control (including year-end procedures)

## 4. My Findings on these key areas

#### 4.1. Payroll

4.1.1 The Parish Council has had just the one employee who works agreed hours but has not been paid in accordance with NJC pay scales. When he sought a pay rise last April he never advised Council of the NJC scales nor sought a level of pay that is found in those scales. Council did not agree to back date any pay rise but he arranged to be paid back to the 1<sup>st</sup> April despite Council agreeing to his pay review from the 24<sup>th</sup> April. He has been employed for some 20 years but when asked for his contract of employment he produced to us a contract of the 1<sup>st</sup> April 2019 and which included Ts and Cs that Council had not agreed to. Council did not even agree to give him a new contract. His alleged contract also appeared to give him a pay rise each year even though Council had not agreed to that. Well there are no minutes approving of this new arrangement. The former Clerk alleged that our former Chair gave him this new contract of employment with new terms and conditions. The Chair had no authority to do so – if he did. Having had sight of this report the former Chair did not deny or confirm his alleged involvement in that alleged new contract.

4.1.2. It is believed that PAYE has been dealt with as HMRC has not made any claim.

#### 4.2. Creditors

4.2.1. A cursory examination appears to reveal that some creditors received payments without any prior approval by the Council to their appointment. No checks were ever made whenever payments are requested to be authorised as to the Council minute approving the expenditure.

4.2.2. Cheques for payment were prepared by the former Clerk but, as far as I can ascertain, not always with the relevant invoices being presented to Members each month to view and check before they signed the cheques. Our Council operated under the 2016 NALC Financial Regulations from April 2016 (minute 8 April 2016 minute refers) which required –

*The RFO shall prepare a schedule of payments requiring authorisation, forming part of the Agenda for the Meeting and, together with the relevant invoices, present the schedule to council*

He failed and it seems that the Internal Auditor did not pick that up. Those Regulations also required the RFO to ensure that

*All invoices for payment shall be examined, verified and certified by the RFO to confirm that the work, goods or services to which each invoice relates has been received.*

The Clerk's expense reimbursement payments were not checked to see just what he was being reimbursed for. I am not saying that such claims were false merely that Council never checked their validity. Members can see from para 4.4.3 that I have been unable to locate any invoice from our Internal Auditor and if none was submitted then that is a further infringement. The former Clerk has declined to provide a response to my enquiry over the apparent lack of such invoices

Members signing cheques did not always countersign the cheque counterfoil to confirm that the detail on the stub coincided with the information on the cheque. Financial Regulations at the time stating

*6.4 To indicate agreement of the details shown on the cheque with the counterfoil the signatories shall each also initial the cheque counterfoil.*

Such countersignatures as there are can best be described as squiggles that are quite unrecognisable as identifying any particular signatory. There could have been scope there for cheques, without payees, being signed and then the payee filled in afterwards and perhaps a different payee on the counterfoil. I am not saying that that took place – I do not know – it merely highlights a possible lack of financial control, and risk, that we need to address. Looking through the cheque counterfoils, though, it was interesting to note that ones for the Internal Auditor were not countersigned by whoever signed the cheque.

4.2.3. All payments were allegedly checked to the invoices for the year by our alleged Internal Auditor. In the absence of our ability to question our Internal Auditor we cannot investigate whether he properly checked invoices etc. before signing the AGAR Internal Audit report.

4.2.4. All donations/ grants paid that had been agreed by the Council were not properly recorded as donations/Section 137 payments in the minutes. I did mention the correct requirements for recording s137 payments in the Budget report for last Council in para 4.24.

#### 4.3. Risk Management/Governance arrangements

4.3.1. Financial regulations of the Council read *“The council is responsible in law for ensuring that its financial management is adequate and effective and that the council has a sound system of internal control which facilitates the effective exercise of the council’s functions, including arrangements for the management of risk.”* The Regulations continue that *“The accounting control systems determined by the RFO shall include measures to ensure that risk is properly managed”*.

4.3.2 Our Financial Regulations continue that *“The council is responsible for putting in place arrangements for the management of risk. The Clerk shall prepare, for approval by the council, risk management policy statements in respect of all activities of the council. Risk policy statements and consequential risk management arrangements shall be reviewed by the council at least annually.”* Whilst we have recently adopted the new NALC Financial Regulations the above obligations were included in earlier versions of the NALC Regulations. These obligations do not seem to have been enacted by the Council in the past. I can’t find any risk management policy

4.3.3 Risk management is an ongoing activity that comprises four elements:

- identifying risks;
- assessing risks;
- addressing risks; and
- reviewing and reporting.

4.3.4 In order to manage risk, an authority needs to know what risks it faces. Identifying risks is therefore the first step in the risk management process. Then it needs to assess the potential consequences of a risk occurring and consider how likely this is. Not considering the competence of an Internal Auditor, or even entering into a formal contract with him, could be a risk.

4.3.5 Despite these obligations, and the lack of evidence that we have ever undertaken any risk assessments or put in place any formal protocol for addressing risks our Internal Auditor on his AGAR form stated that *“This authority assessed the significant risks to achieving its objectives and reviewed the adequacy of arrangements to manage these”*. The Clerk and former Chair then signed

the annual Governance Statement also saying that we had undertaken such risk assessments! That does not appear to have been correct.

4.3.6 Clearly this is another area that needs to be addressed.

4.3.7 The Council appears to be in breach of the play equipment conditions in its Insurance policy and this was never brought to Members attention, as far as I can ascertain. That policy has a condition that, for it to remain in force in relation to any playground injuries etc., we must inspect the equipment weekly. I don't think that we do. I did provide a report on the equipment at the last Council indicating that an inspection had been undertaken last October but its recommendations had not been implemented. The former Clerk took no action! In the event of any injuries our Insurers will expect us to be able to show that we complied with the insurance condition if it is to meet any claim. This exposes the Council to potential risk. Reserves are unlikely to meet damages in the worst case scenario. The best option here maybe to fence off the equipment until appropriate arrangements are in place. There may be other insurance conditions that we should be ensuring we meet.

4.3.8 We need to review our Insurance policy to ensure that it is adequate for the Council's needs.

4.3.9. The Council has adequate Financial Regulations and Standing Orders in place. Each follow the NALC standard. However in the past it seems clear that we have not always complied with them. Councillors are guided by their Clerk and Responsible Financial officer and come to rely on that post holder to undertake his duties meticulously. Apart from the issues of risk raised in this section of this report the Clerk never dealt with reserves properly as required by the Financial Regulations.

4.4. Income collection and Banking arrangements

4.4.1. The Council does not receive any Income apart from the Precept, vat refund and a small amount through rent and perhaps bank interest.

4.4.2. It appears that all income due has been paid but, in the light of the concerns expressed in this report, this should merit closer examination.

4.4.3. It is assumed that VAT refunds are up to date but closer examination is required. For example, I have not found any VAT invoice from our Internal Auditor and I believe that audit services are liable to VAT. In the absence of a VAT invoice then there should not have been any payment. If there was no VAT invoice then we will not have recovered the VAT we are entitled to recover. The former Clerk has been questioned about this (on the 14<sup>th</sup> December 2019) but declines to provide a response.

4.4.4. The Council holds a Current account but does not seem to have any other account. Perhaps a deposit account may merit investigation for reserves?

4.5. Accounting Records

4.5.1. The Council appears to keep a manual Income and Expenditure record throughout the year which should be adequate for a very small Council. However no legal power relied upon for expenditure was recorded next to each entry - nor the minute / motion. We should get into the habit of ensuring that all that we do is sanctioned by a statutory power to do so and record the power we rely on. This avoids inadvertently stepping outside of the law. We have been doing this since our Clerk was dismissed.

4.5.2. The Clerk reports to Council every month on the income and expenditure balance and at the end of the year a Bank reconciliation is carried out, which is confirmed by the Chair. However the Clerk never advised Council when he was using reserves nor that the annual precept had been spent long before the financial year end. There was no reserves policy and nothing was ever placed into earmarked reserves to build up savings to meet any long term proposals e.g taking a lease of the Football Field. Members were actually being kept in the dark on the finer details of their accounts and which are matters that should have been brought to Members notice.

#### 4.6. Assets

4.6.1. The Asset Register appears to be up to date as at 31st March 2018. It is assumed that title deeds for our land holdings are with the Council's Solicitors but I have been unable to find confirmation thus far. This needs to be checked out. There may be adequate security for our deeds....or maybe not.

#### 4.7. Debtors

4.7.1. There do not appear to be any accounts raised for debts but then it may be unlikely that we will provide any services to others to owe us money

#### 4.8. Budgetary Control

4.8.1. The precept and budget had been discussed and agreed by a Parish Council meeting on the 8th January 2020. The report on that evidenced financial difficulties facing the Council and which should not have been allowed to occur or flagged up much earlier. That report was posted on the Internet and it is the first time that this Council has publicly disclosed to the Tax Payers our budget proposals. We are required to post up our agreed budget and that will be done. However, the Council never has done in the past. We are slowly remedying failures of the past.

4.8.2. When any matter was brought to Council by our former Clerk for approval of expenditure he never indicated whether there was any allocation in the budget for that expenditure and approval would have been given whether we could afford it or not. That is clearly a wholly inappropriate way in which to deal with decision making on the spending of Tax Payers money. The recently agreed report template includes a requirement to draw to the attention of Members the budget impact of any proposed expenditure.

### 5. Conclusions

5.1. My cursory examination of the internal control and Governance arrangements indicate to me that they have been far from satisfactory and exposed the Council to risk. It seems surprising therefore that the alleged Internal Auditor could have confirmed on his standard AGAR report form (<https://partonparishcouncilcom.files.wordpress.com/2019/11/annual-internal-audit-report-2018-19.pdf>) that

- Appropriate accounting records have been properly kept throughout the financial year
- This authority complied with its financial regulations, payments were supported by invoices, all expenditure was approved and VAT was appropriately accounted for

- This authority assessed the significant risks to achieving its objectives and reviewed the adequacy of arrangements to manage these.
- The precept or rates requirement resulted from an adequate budgetary process; progress against the budget was regularly monitored; and reserves were appropriate.
- Accounting statements prepared during the year were prepared on the correct accounting basis (receipts and payments or income and expenditure), agreed to the cash book, supported by an adequate audit trail from underlying records and where appropriate debtors and creditors were properly recorded
- During summer 2018 this authority has correctly provided the proper opportunity for the exercise of public rights in accordance with the requirements of the Accounts and Audit Regulations. (It never made its budget known publicly for example)

5.2 An explanation should be sought from that Auditor in the hope that he can properly show that everything had been dealt with correctly.

5.3 I do not see, in the light of the above issues, that we can tick every box on the Annual Governance AGAR forms for this year with the level of honesty that they require in view of the matters set out in this report. The public then is entitled to know why and this report will provide that explanation.

5.3 These notes should perhaps be forwarded to PKF Littlejohn so that those auditors are aware of the shortcomings under the stewardship of our former Clerk (and Chair) and that I doubt that we can file a positive annual governance statement for the current financial year confirming that everything is properly in order. That may mean action by those auditors to undertake a thorough audit of this Council and which will mean that we will have to pay their fees which may make a big hole in our reserves. Due to the Clerk being very slow to return Council papers, and they have not all yet been returned, the delivery of this analysis has not been possible until now. It would have been preferable to have been before members when determining the Budget. I understand that if a Parish Council can show that it is working towards achieving proper compliance with the relevant protocols highlighted in this report then we may be subject to a soft touch review by external auditors provided that we continue to put in place appropriate safeguards. This report should be seen then as the first step.

## **6. Recommendations**

### **6.1. Recommendations:**

6.1.1 That PKF Littlejohn be passed a copy of this report and their guidance be obtained

6.1.2 That our Internal Auditor be required to attend at Council to explain these matters

6.1.3 That the former Clerk be required to provide the Internal Auditors contact details without any further delay

6.1.4 That we consider the termination of the appointment of our Internal Auditor if Council is not satisfied with the explanations provided to the issues in this report and appoint a new Internal Auditor without delay. Perhaps the auditor used by many Parish Councils in Cumbria and who is being used by Whitehaven Town Council?



6.1.5 That the Police be advised of these matters and request that they consider whether any offence may have been committed here

6.1.6 That, in due course, advice be sought as to whether a claim may be made against our former clerk to recover any losses that the Council may sustain if they arise as a result of any omission or misconduct.