

Brentwood Borough Council

INTERNAL AUDIT REPORT

Accounts Payable

Audit 1.2015

LEVEL OF ASSURANCE

| Design | Operational Effectiveness |
|----------|---------------------------|
| Moderate | Limited |



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REPORT STATUS

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| Auditors: | Tejal Patel, Assistant Manager |
| Dates work performed: | May 2015 |
| Final Meeting Date: | 13 May 2015 with Jane Mitchell and Ramesh Prashar |
| Draft report issued: | 8 June 2015 |
| Final report issued: | 29 June 2015 |

DISTRIBUTION LIST

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|---------------|----------------------------------|
| Chris Leslie | Finance Director |
| Jane Mitchell | Payments and Procurement Officer |

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EXECUTIVE SUMMARY

CLIENT STRATEGIC RISKS

Risk 1 Finance pressures

- Target levels for income are not achieved.

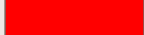
This review relates to the risk that the Council does not achieve targets set for income.

LEVEL OF ASSURANCE (SEE APPENDIX II FOR DEFINITIONS)

Design Moderate Generally a sound system of internal control designed to achieve system objectives with some exceptions.

Effectiveness Limited Non-compliance with key procedures and controls places the system objectives at risk.

SUMMARY OF RECOMMENDATIONS (SEE APPENDIX II)

High  2

Medium  4

Low  1

Total number of recommendations: 7

OVERVIEW

The Council is required to operate a sound system of control over their financial processes to prevent and detect error or fraud. In March 2015 false bank account details were provided to the Council purporting to come from a key supplier. A supplier invoice for approximately £42,000 was subsequently paid into the fraudster's bank account. At the Council's request, this review assessed the controls operating in Accounts Payable with particular regard to processing changes to standing data and payments to third party suppliers.

Our review found the following areas of good practice:

- The Finance policies, new supplier form and changes to supplier details forms are currently in the process of being revised.
- Finance procedures for key financial processes have been documented and made available to all Finance staff on the accountancy drive.
- Approval of invoices for payment are made via automatic controls on the Council's e-financials system which were reviewed in more detail as part of the Main Financial Systems review in 2014/15.

We also found some areas for improvement or development:

- Although a review of all supplier information has been initiated, not all suppliers have been directly contacted to ensure details are correct.
- Where changes to suppliers are made a supplier change document should be completed, authorised, and kept with the supplier notification of change.
- All Finance procedures should be consolidated into procedure documents for key financial processes and a fraud policy detailing what steps to undertake in an instance where fraud maybe suspected has not been documented.
- Supplier changes reports, run to verify any changes to suppliers, are not always evident before a payment batch is released and there is no evidence of segregation of duties in regards to checking the reports.
- The new supplier form at the time of review did not include who has requested and approved the new supplier to be added onto the system.

DETAILED FINDINGS AND RECOMMENDATIONS

Risk: Financial processes are not well documented and/or communicated and officers are not aware of their duties and responsibilities, including those for when fraud is suspected.

| Ref. | Finding | Sig. | Recommendation |
|------|---|----------------------------|---|
| 2 | <p>The Council has Accounts Payable procedures in place documenting the key processes. These include the review of supplier bank account details and changes to supplier details. These procedures are available to all staff via the intranet and shared accountancy folder. Some of the procedures in place are currently under review. With regards to supplier information and change of details, the Council has the following two procedures in place: changing supplier details on e-Financials and setting up new suppliers. However, a fraud policy has not been documented.</p> <p>Our review of the procedures for setting up new suppliers found that they document how new suppliers to the Council are verified to ensure they are bona-fide, prior to any payments being made to them. The procedures state that only members of the Accounts Payable team have access to the supplier entry mechanism on e-Financials and that departments needing a new supplier are required to complete a new supplier form. The procedures further describe what areas are reviewed by Accounts Payable and how the changes are made onto the e-Financials system.</p> <p>However, we noted that the new supplier procedures did not include the requirement for approval within Accounts Payable prior to input onto the system and version control was not evident on both procedures. Moreover, although adequate steps have been described and detailed regarding all finance procedures we found that there were currently a total of 39 separate procedure documents and that they had not been grouped into key financial process procedure documents for example all procedures relating to Accounts Payable in one document.</p> <p>If procedures are not adequately detailed and consolidated there is a risk that procedures may not be appropriately followed resulting in financial errors or fraud.</p> | <p>M</p> <p>L</p> <p>M</p> | <p>The Council should review the 'setting up new suppliers' procedures to ensure that approval of new supplier is evident in the process.</p> <p>All finance procedures should be consolidated into separate key financial process procedure documents to ensure a central point of reference with regards to each process. Version control should be utilised to ensure that the document is reviewed and updated on a regular basis.</p> <p>The Council should ensure that a fraud policy is documented and in place to make certain that staff are aware of steps to be undertaken in an instance of fraud or error.</p> |

DETAILED FINDINGS AND RECOMMENDATIONS

Risk: Financial processes are not well documented and/or communicated and officers are not aware of their duties and responsibilities, including those for when fraud is suspected cont.

| Ref. | Finding | Sig. | Recommendation |
|---------------------|--|--|---|
| MANAGEMENT RESPONSE | | RESPONSIBILITY AND IMPLEMENTATION DATE | |
| 1. | As noted in the finding, procedures for setting up new suppliers have been reviewed and implemented. These include the requirement for approval by Accounts Payable prior to input into the system, which can only be done by Accounts Payable officers. | | <p><i>Responsible Officer: Responsible Officer: Jane Mitchell (Payments and Procurement Officer)</i></p> <p><i>Implementation Date: 18 June 2015</i></p> |
| 2. | Agree with the recommendation. All accounts payable procedure notes will be consolidated into one document. | | <p><i>Responsible Officer: Responsible Officer: Jane Mitchell (Payments and Procurement Officer)</i></p> <p><i>Implementation Date: 30 September 2015</i></p> |
| 3. | There is a Fraud Response Plan for Managers on the Council's Intranet. | | <p><i>Responsible Officer: Responsible Officer: Jane Mitchell (Payments and Procurement Officer)</i></p> <p><i>Implementation Date: 18 June 2015</i></p> |

DETAILED FINDINGS AND RECOMMENDATIONS

Risk: Changes made to supplier standing data are not verified, recorded and independently reviewed.

| Ref. | Finding | Sig. | Recommendation |
|---|--|---|--|
| 3 | <p>Changes to supplier bank details are made via receipt of a change of details notification. This is verified by Accounts Payable by calling the supplier to check that the changes are valid. The number to call is obtained via the supplier website or an old invoice. Once the change of supplier bank details is verified the changes are made onto the system. However, this process was not followed for the fraud incident. Furthermore, twice a week before the payment run a supplier details and changes report is run. The changes report highlights any changes to details which are reviewed to ensure appropriate supporting documentation is in place before payments are made. The payments report is filed with the payment run documentation. The Council has put in place a checklist to evidence that these checks have been undertaken.</p> <p>We selected a sample of 20 payment runs from January 2015 to April 2015 to determine whether supplier changes reports were in place and had been verified and checked appropriately. From our testing we found the following:</p> <ul style="list-style-type: none"> • A checklist was evident for all 20 payment runs confirming the review of new suppliers and changes to suppliers • An R99 report was evident for all 20 payment runs confirming the review of supplier bank details • A R46 report was only evident for 7 out of 20 payment runs confirming the review of changes to supplier details. <p>Furthermore, there was no evidence of verification by a second person to ensure that appropriate checks had been undertaken, therefore no segregation of duties. If the Council does not ensure that appropriate reports are produced for each payment run and verified independently there is a risk that fraudulent payments could be made resulting in financial loss.</p> | M | <p>The Council should ensure that R46 changes to supplier information report is run and evidenced with the payment batch reports before any payments are made on each occasion. Reports should be further verified independently in order to ensure segregation of duties.</p> |
| MANAGEMENT RESPONSE | | RESPONSIBILITY AND IMPLEMENTATION DATE | |
| <p>New manual procedure has been introduced for checking that all changes in supplier information are bona fide before each payment run. The procedure includes a requirement for the changes to be verified by a second officer to ensure segregation of duties.</p> | | <p><i>Responsible Officer: Jane Mitchell (Payments and Procurement Officer)</i> <i>Implementation Date: 30 June 2015</i></p> | |

DETAILED FINDINGS AND RECOMMENDATIONS

Risk: Changes made to supplier standing data are not verified, recorded and independently reviewed.

| Ref. | Finding | Sig. | Recommendation |
|---|---|---|--|
| 4 | <p>Supplier details are added onto the system once a new supplier form is completed by staff requesting a new supplier. Currently, the form is under review to ensure that an appropriate paper trail is in place and that the new supplier is authorised prior to it being added onto the system.</p> <p>We obtained and reviewed the new supplier form and from our testing we found that the form adequately sets out the required information to input onto the system. However, we noted that the form does not evidence who has authorised the new supplier to be added onto the system. We also selected a sample of 20 new suppliers at the Council from January 2015 and confirmed that a new supplier form was in place for all items tested.</p> | M | The Council should update the new supplier form to ensure that there is a clear audit trail for who has requested and authorised the new supplier to be added onto the system. |
| MANAGEMENT RESPONSE | | RESPONSIBILITY AND IMPLEMENTATION DATE | |
| <p>The recent changes to the New Supplier Form do include details of which officer within the Council has requested the supplier to be added to the database. The revised procedures include this requirement. The procedures also include training to ensure all Accounts Payable officers understand the relevance of this requirement and comply with the procedure.</p> | | <p><i>Responsible Officer: Jane Mitchell (Payments and Procurement Officer)</i></p> <p><i>Implementation Date: 30 June 2015</i></p> | |

APPENDIX I - STAFF INTERVIEWED

| NAME | JOB TITLE |
|----------------|-----------------------------------|
| Ramesh Prashar | Financial Services Manager |
| Jane Mitchell | Payments and Procurements Officer |

BDO LLP appreciates the time provided by all the individuals involved in this review and would like to thank them for their assistance and cooperation.

APPENDIX II - DEFINITIONS

| LEVEL OF ASSURANCE | DESIGN of internal control framework | | OPERATIONAL EFFECTIVENESS of internal controls | |
|--------------------|--|--|---|--|
| | Findings from review | Design Opinion | Findings from review | Effectiveness Opinion |
| Substantial | Appropriate procedures and controls in place to mitigate the key risks. | There is a sound system of internal control designed to achieve system objectives. | No, or only minor, exceptions found in testing of the procedures and controls. | The controls that are in place are being consistently applied. |
| Moderate | In the main there are appropriate procedures and controls in place to mitigate the key risks reviewed albeit with some that are not fully effective. | Generally a sound system of internal control designed to achieve system objectives with some exceptions. | A small number of exceptions found in testing of the procedures and controls. | Evidence of non compliance with some controls, that may put some of the system objectives at risk. |
| Limited | A number of significant gaps identified in the procedures and controls in key areas. Where practical, efforts should be made to address in-year. | System of internal controls is weakened with system objectives at risk of not being achieved. | A number of reoccurring exceptions found in testing of the procedures and controls. Where practical, efforts should be made to address in-year. | Non-compliance with key procedures and controls places the system objectives at risk. |
| No | For all risk areas there are significant gaps in the procedures and controls. Failure to address in-year affects the quality of the organisation's overall internal control framework. | Poor system of internal control. | Due to absence of effective controls and procedures, no reliance can be placed on their operation. Failure to address in-year affects the quality of the organisation's overall internal control framework. | Non compliance and/or compliance with inadequate controls. |

| Recommendation Significance | |
|-----------------------------|--|
| High | A weakness where there is substantial risk of loss, fraud, impropriety, poor value for money, or failure to achieve organisational objectives. Such risk could lead to an adverse impact on the business. Remedial action must be taken urgently. |
| Medium | A weakness in control which, although not fundamental, relates to shortcomings which expose individual business systems to a less immediate level of threatening risk or poor value for money. Such a risk could impact on operational objectives and should be of concern to senior management and requires prompt specific action. |
| Low | Areas that individually have no significant impact, but where management would benefit from improved controls and/or have the opportunity to achieve greater effectiveness and/or efficiency. |

APPENDIX III - TERMS OF REFERENCE

BACKGROUND

On 25 March 2015 the Accounts Payable (AP) team at Brentwood Borough Council received a fraudulent email purporting to be from a key supplier, informing them that their bank account details had changed. The amendment was processed without any further validation, and a supplier invoice for approximately £42,000 was subsequently paid into the fraudster's bank account. At the council's request, this review will assess the controls operating in AP with particular regard to processing changes to standing data and payments to third party suppliers.

PURPOSE OF REVIEW

The purpose of this audit is to assess the design and operating effectiveness of controls around the Accounts Payable function at Brentwood Borough Council, with a focus on the management of standing data and supplier payments

KEY RISKS

Based upon the risk assessment undertaken during the development of the internal audit operational plan, through discussions with management, and our collective audit knowledge and understanding, the key risks associated with the area under review are:

- Other potentially fraudulent changes to supplier standing data have not been identified and validated
- Financial processes are not well documented and / or communicated and officers are not aware of their duties and responsibilities, including those for when a fraud is suspected
- Changes made to supplier standing data are not verified, recorded and independently reviewed
- Payments to suppliers are not made in accordance with procedures and scheme of delegation.

SCOPE OF REVIEW

The review will consider the following areas:

- Confirmation that the AP team has reviewed all changes made to supplier bank details since January 2015
- Review of the financial procedure documents in place, ensuring they reflect good practice and that users are aware of them
- How changes to supplier data are processed and reviewed
- Controls around payments to suppliers.

APPENDIX III - TERMS OF REFERENCE

EXCLUSIONS

Our work will be restricted to the areas of consideration within our scope of the review.

APPROACH

Our approach will be to conduct interviews to establish the controls in operation for each of our areas of audit work. We will then seek documentary evidence that these controls are designed as described. We will evaluate these controls to identify whether they adequately address the risks. Testing of the effectiveness of controls will be carried out where appropriate.

LOCATIONS

Fieldwork will be performed exclusively at Brentwood Borough Council offices.

APPENDIX III - TERMS OF REFERENCE

DOCUMENTATION REQUEST

Please provide the following documents in advance of our review (where possible):

- Financial Policy documents and standing orders
- AP process maps and procedure documents
- User and access rights reports for all key financial systems
- Authorised Signatory and delegated authority reports, showing authorisation levels and responsibilities of all officers
- Report of all purchase order and non-purchase order invoices paid for the period April 2014 to date
- Report of all changes made to supplier standing data made 1 January 2015 to date.

Any documents provided will assist the timely completion of our fieldwork, however we may need to request further documentation and evidence as we progress through the review process.


KEY CONTACTS

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BRENTWOOD BOROUGH COUNCIL

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