REPORT NO: 25/2010

AUDIT & RISK COMMITTEE

26th JANUARY 2010

IMPACT OF AGRESSO IMPLEMENTATION ON THE INTERNAL CONTROL FRAMEWORK

REPORT OF THE HEAD OF CONSORTIUM

CORPORATE AIM	**A well managed organisation**

1) PURPOSE OF THE REPORT

1.1 To inform the Committee of the short-term impact that the implementation of the Agresso Financial Management System has had on the Council's internal control framework and the measures taken to mitigate that impact.

2) RECOMMENDATIONS

2.1 That Members consider the report.

3) REASON FOR REPORTING

3.1 The Consortium brought forward its planned audits of the Council's key financial systems from Quarter 4 to Quarter 3 at the request of the Council's External Auditors. The request was made to allow the External Auditor to determine the extent to which he could place reliance on the work of internal audit in developing his Audit Opinion. Initial testing established that, as a result of Agresso implementation, some key controls, upon which the External Auditor would expect to place reliance, were in place but were not operating.

3.2 The initial internal audit findings were discussed with the External Auditor and it was agreed that it would be unhelpful to complete the audits before the key controls were operating as specified. The External Auditor also expressed the opinion that good governance required that the Audit and Risk Committee be advised of the impact of inoperative key controls on the Council's internal control framework.

3.3 The Director of Corporate Services commissioned the Consortium to identify the extent to which key controls has been compromised during the Agresso implementation process; determine what action is being taken to re-establish the control framework; and to evaluate the effectiveness of proposed mitigations.

4) IDENTIFIED CONTROL WEAKNESSES

4.1 The audit identified three areas where weaknesses in the prescribed control framework could be associated with the ongoing process of Agresso implementation:

- Review and clearance of suspense accounts;
- Bank reconciliations; and
- Arrangements for the correct VAT coding of income;

4.2 The balance on the Income Suspense Account on 8th January 2010 was in excess of £12 million and comprised something over 130 income payments with values of up to £4 million. In 2008/09 it was normal practice for the Suspense Account to be cleared on a weekly basis. Effective monitoring of the Suspense Account is critical to effective budgetary control and forms part of the Council's counter-fraud arrangements.

4.3 On 4th January 2010, the most recent bank reconciliation was for the period to the 30th April 2009. Normal practice would be for the bank statement as at the last working day of each month to be reconciled to the Council's General Ledger System by the middle of the following month. Regular reconciliations allow for the timely identification of material banking errors: they also represent a significant counter-fraud measure by allowing for the timely identification of unauthorised transactions.

4.4 Errors in the set up of income codes on the General Ledger led to the overstatement of VAT collected by almost £600,000. The coding error was identified during the preparation of the first VAT Return of 2009/10 and adjustments were made to ensure the correctness of the payments made by the Council to HMRC, however any uncorrected errors in the final accounts might impact on the Council's Partial Exemption Threshold – implying an unfavourable and ongoing financial impact.

5) CAUSES OF CONTROL WEAKNESSES

5.1 The audit identified high workloads as a common contributory factor in all cases. Delays in reviewing the Suspense Account were due entirely to that cause. Delays in carrying out bank reconciliations resulted in part from the failure of the Council's bankers to deliver the required e-reports relating to the new Payment Account but high workloads delayed the pursuit of those reports and the subsequent start of work on the backlog of reconciliations.

5.2 The immediate cause of the overstatement of VAT was that in setting up a number of income codes VAT was treated inappropriately: the effect was that a range of zero-rated income streams, such as grants and repayments of treasury management investments, were treated as if the standard rate of VAT applied when posted to the General Ledger. There was a delay in the identification of the setting up errors because pressure of work at the start of the financial year delayed the posting of transactions from the Agresso Income Manager to the General Ledger.

6) REMEDIAL ACTION AND MITIGATIONS

6.1 Since the audit was commissioned, the Finance Team has agreed a plan of action to allow for the reestablishment of controls. This has involved the re-prioritization of work.

6.2 The balance on the Suspense Account had been reduced to £2.65 million by 12th January 2010 and the number of suspense transactions had been reduced by a quarter. A schedule of items in the Account has been circulated to responsible officers to identify and allow for the proper allocation of those transactions.

6.3 The workload of one of the Finance Team's Accountancy Assistants has been re-prioritized to give absolute priority to the completion of bank reconciliations. Between 4th and 12th January, bank reconciliations to the end of June 2009 had been completed. Progress to date suggests that reconciliations will be up to date by the end of January: at that point the key control will be operating effectively.

6.4 The errors in the treatment with VAT were identified by the routine checks in place to assure the accuracy of the statutory VAT Returns. Consultants engaged to support the implementation process addressed the set-up errors and the Finance Team has corrected the accounting records and continue to monitor VAT transactions to ensure that all fixes have been applied effectively.

7) IMPACT ON AGRESSO'S PERFORMANCE

7.1 The weakening of controls during the implementation process increased the risk of error in processing or reporting but there is no evidence that any such material errors occurred.

7.2 The issues identified in this report did not have any identifiable impact on the delivery of financial services. Progress continues with the development of electronic submission of payroll data; paperless invoice processing has been implemented and increasing use is being made of the facility; the facility to raise debtors electronically is also in place. While there has been some reduction in the speed of invoice processing, this cannot be linked directly to the new systems. Available statistics indicate that arrangements to recover debts have become more effective in 2009/10.

8) RISK MANAGEMENT

RISK	IMPACT	COMMENTS
Time	**High**	No time critical issues arise from this report
Viability	**Low**	The report does not raise any specific issues relating to ongoing viability of services
Finance	**Low**	None of the issues considered impacts on the Council's ongoing financial status
Profile	**Low**	No controversial issues are raised
Equality & Diversity	**Low**	There is no reference to equalities issues

Background Papers
None

Report Author
Richard Gaughran
Tel No: (01572) 722577
e-mail: enquiries@rutland.gov.uk