



West Midlands Combined Authority

Internal Audit Report:

Treasury Management – 2023

Report Date: 16 January 2024

Report Distribution: Mark Finnegan – Lead Treasury Accountant
Louise Cowen – Head of Financial Management
Linda Horne – Executive Director, Finance and Business Hub

1. Executive summary

Introduction and Background

- 1.1 A review of the WMCA Treasury Management operations was included in the Annual Internal Audit Plan 2023/24 approved by the Audit, Risk and Assurance Committee (ARAC). The purpose of the review was to conduct a high-level appraisal of the Treasury Management System established within the WMCA to provide independent assurance regarding the efficiency and the effectiveness of the Treasury Management process.
- 1.2 All key financial systems are required to be reviewed annually. The Treasury Management System (TMS) was last reviewed as part of the 2022/23 Internal Audit Plan. The opinion was “Substantial”. Hence this review is a high-level review which focussed only on the key controls in order to provide assurance that controls remain effective and are operating satisfactorily. The review also evaluated the new “Treasury Live System” following the recent concerns reported to Statutory Officers, in September 2023 in regard to the control environment within the “Treasury Live System” relating to Forward Dealt Loans
- 1.3 To this effect additional tests were undertaken to ascertain whether the issues reported to Statutory Officers had been effectively addressed.
- 1.4 Details of the outcome of the review are set out below.

Objectives, potential risks, and scope of audit work

Our audit was conducted in conformance with the Public Sector Internal Audit Standards and considered the following:

Objectives:	<ol style="list-style-type: none">1. Seek to gain assurance that the Treasury Management function is operated in accordance with the Combined Authority’s Financial Regulations and Contract Procedure Rules, in compliance with the WMCA Constitution and Treasury Management Strategy (TMS).2. To evaluate and assess the controls in place for the day-to-day operation of the Treasury Management function to gain assurance that these controls continue to operate effectively and are fit for purpose.3. To evaluate if the control measures implemented in response to the reported concerns are satisfactory and the Treasury Live System used for treasury management transactions remains fit for purpose.
Potential Risks:	<p>The following system risks were identified:</p> <ul style="list-style-type: none">• Treasury management activities are not managed in accordance with the Treasury Management Strategy, the Constitution and the CIPFA Code of Practice.• Treasury Management roles and responsibilities are not clearly defined.

	<ul style="list-style-type: none">• Not all transactions are appropriately approved and authorised which may lead to unauthorised transactions taking place.• Weak or insufficient separation of duties may lead to errors and unauthorised transactions.• Insufficient evidence for transactions in place and transactions are not fully recorded and accounted for.• Control accounts are not prepared and regularly reconciled.• Regular monitoring of activities and reporting arrangements are not in place.
Scope:	In line with the agreed Terms of Reference the scope of this audit covers the controls and processes in place within the Treasury Management Systems from April 2023 to September 2023 regarding the day to day operation but extended as necessary to cover the remedial activities relating to the concerns recently reported to Statutory Officers.
Limitations to the scope of our audit:	<p>The review was limited to transactions covering the periods from April 2023 to September 2023 and was limited in scope due to the frequency of reviews and the high level of assurance obtained at the last review reported in February 2023.</p> <p>Audit tests were carried out on a selection of random samples of transactions covering the relevant period to obtain necessary assurance to ascertain the effectiveness of the existing system.</p>

Overall conclusion

Our conclusion is that the framework is strong, and compliance is satisfactory. Our overall conclusion based on Internal Audit Standard Assurance Matrix, is that the system is “satisfactory.” This means - Our audit provides **Satisfactory** assurance over the adequacy of the controls reviewed as part of the process to mitigate risks to an acceptable level.

No Assurance	Limited	Satisfactory	Substantial
Immediate action is required to address fundamental gaps, weaknesses or non-compliance identified. The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of objectives in the area audited.	Significant gaps, weaknesses or non-compliance were identified. Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives in the area audited.	There is a generally sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives in the area audited.	A sound system of governance, risk management and control exists, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited.

Key issues identified.

We rate each issue identified in section below, based on the following:

Red Action is imperative to ensure that the objectives for the area under review are met	Amber Action is required to avoid exposure to significant risks in achieving objectives	Green Action is advised to enhance risk control or operational efficiency
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We have identified one **Amber** issue and one **Green** issue (See section below) where improvements could be made, arising from the issues which have been identified.

Forward Dealt Loans.

Internal Audit reviewed the actions taken by service management to address the concerns reported to Statutory Officers in September 2023 to ascertain whether appropriate remedial actions had been taken to address the issues.

In context, the concerns reported to Statutory Officers indicated that there had been a number of circumstances (five cases to be precise) where the operational loan boundary - set to maintain an even spread of investments across counterparties - had been exceeded due to a system failure. Although no approved treasury limits were breached, the failure relates to a component within the “Treasury Live” system which had not been fully activated and not been fully “Stress Tested” to determine fitness for purpose. All the counterparties involved were local authorities with low-risk ratings. However, as the issue relating to the operational boundary had already been dealt with by statutory officers, the main audit concern was therefore to determine what appropriate remedial action had been undertaken to address the identified issues and to facilitate a live “Stress Test” of the system in order to provide senior

management with an appropriate level of assurance regarding the current position and “risk potential” faced by the system.

The “Treasury Live” system was developed for Public Sector Treasury Management and therefore is a dedicated or bespoke programme for local authorities across the UK which was developed in compliance with CIPFA Standards. Since the incidence was reported to Statutory Officers service management had taken appropriate steps to request a “fix” from the developers of the system to prevent future incidents occurring.

To address the above Internal Audit engaged with the WMCA Treasury Lead Accountant to carry out a “Walk through Test” on the updated system. The test demonstrated that the “fix” had successfully been activated to prevent any accidental or unconscious over-allocation beyond the limits set within the WMCA’s Treasury Management Strategy. However, the system could still allow the limits to be exceeded manually after first alerting the inputter that they are about to exceed the set limit. This gives the inputter an opportunity to “reconsider”. Hence the inputter has the option to override the system. But this could only happen intentionally or consciously.

The system is however, underpinned by three key additional controls.

- Division of duties – Approver and Inputter are separate individuals.
- Bank approval – The bank approver may prevent any detected counterparty over-allocations that are in excess of the pre-set limits.
- Monthly reconciliations – Monthly reconciliations of cash holding and cash movement are sent to a senior manager for information and return confirmation of completeness. However, these are not “Certified” by the reviewing manager. Hence this aspect could be further strengthened to enhance internal control.

The Archiving Process Within MS Teams

- Evidence of transactions and approvals are maintained within MS ‘Bank’ Channels within teams, however the security and retention periods for this data source could not be obtained during this review.
- The storage of information on MS Teams may not be suitable in the long term as storage capacity may be exhausted and data may become inaccessible and lost.
- It may be more appropriate to hold this information offline in an archive whether on SharePoint or on a separate drive on the network where controlled access to the data can be controlled and facilitated. We therefore would recommend a review of data storage and access to archived information.

Appropriate recommendations to address the issues raised above are set out below on section 2 of this report.

Examples of good practice identified.

We identified the following examples of good practice within the system and in the management of risk.

- There is a Treasury Management Strategy which complies with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice.
- The Treasury Management strategy is reviewed and approved annually by ARAC.

- There is division of responsibility regarding the administration of key functions within the TM team. Investment decisions are separated from inputting. Hence creating appropriate level of control against risk of error or fraud.
- Following the operational boundary control limit issue on the “Treasury Live” system which was reported to Statutory Officers, the system has been upgraded to flag up any attempted input in excess of the TM strategy; this allows the inputter to pause for reflection prior to completing the operation.
- In addition to the above, new written procedures have been drawn up to strengthen controls in order to minimise identified risks.
- Additionally, there is a further line of control within WMCA’s banking software prior to the release of funds when investments decisions are made. Bank approvers can reject any transactions over the counterparty limits set out in the investment strategy and monthly reconciliations are sent to senior management.
- There is a regular reporting routine in place for month end reporting of cash flow movements and periodical reporting to ARAC via the Treasury Management Mid-Year and Outturn reports.

Acknowledgement

Several employees gave their time and co-operation during this review. We would like to record our thanks to all the individuals concerned for their time and efforts.

2. Findings and recommendations

Action is required to avoid exposures to significant risks in achieving objectives.

Amber

Forward Dealt Loans.

Findings:

Although the issues relating to the “Treasury Live” system failure reported to Statutory Officers have been addressed; It is still possible to override the system manually. While it is noted that the monthly reconciliations which are sent to senior management offers a level of transparency which provides additional security and safeguards, this may not be sufficient to address manageable residual risks as the reports to management are not certified. To this effect the existing level of senior management review may need strengthening.

In view of the above, it is recommended that the reconciliation sheet includes a simple statement saying, “Certified by”, followed by the designation and signature of a responsible member of the senior management team who would take responsibility for approvals exceeding loan limits as well as confirmation of the accuracy of the reconciliation outcomes.

Implications:

The updated system and additional controls implemented to address the system error may not be sufficient to address the possibility of further errors of the counterparty investment limits set by the TM strategy. Current arrangements may not be sufficiently transparent and lack sufficient evidence of senior management ownership. Therefore, additional measures may be required to plug any existing gaps.

Recommendations:

1. The monthly investment reconciliations should be certified by an appropriate member of the senior management team and any identified breaches of the Treasury Management Strategy should immediately be reported to Statutory Officers.
2. All future changes made to the “Treasury Live” system, or any relevant TM financial application should undergo a “stress test” which should be signed off by senior management. The tests should incorporate identified risks to ensure their fitness for purpose before full implementation and senior management sign off.

Agreed Actions/Management Comments:

1. Update of monthly reconciliation format to include certification of counterparty exposure compliance to be introduced.
2. Treasury Live system “stress tests” to be documented and thereafter signed off by senior management following each update to operating parameters and/or – as a minimum - following the approval of the Treasury Management Strategy annually.

Responsible Officer:

Target Date:

<p>Lead Treasury Accountant</p>	<ol style="list-style-type: none"> 1. January 2024 2. March 2024 (or earlier if operating parameter changes altered prior to approval of 2024/24 TMS)
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Action is advised to enhance the archiving and access to records within MS Team Green

The Archiving process within MS Teams.

Findings:

Evidence of transactions and approvals are maintained on 'Bank' Channels within Microsoft teams. However the security and retention periods for this data source could not be obtained during this review.

Implications:

Approval records are not held alongside the associated transaction resulting in difficulties in reconciling transactions.
 The period for retaining data within the MS Teams system may not reflect the required retention periods set for accounting purposes.
 The data may not be securely held offline and there may be limited access to data in time if storage capacity is reached within MS Teams.

Recommendations:

Consideration should be given to the effectiveness of MS Teams for the recording and retention of financial approvals and confirmed by Digital and Data team.

Agreed Actions/Management Comments:

Lead Treasury Accountant (in collaboration with peers from other impacted teams) to liaise with Digital and Data team to confirm long term viability of MS Teams for recording and retention of financial approvals and scope alternate archiving systems if required.

<p>Responsible Officer: Lead Treasury Accountant</p>	<p>Target Date: March 2024</p>
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Limitations inherent to the internal auditor's work

This report has been prepared solely for the Combined Authority in accordance with the terms and conditions set out in the terms of reference. Internal audit does not accept or assume any liability of duty of care for any other purpose or to any other party. This report should not be disclosed to any third party, quoted, or referred to without prior consent. Internal audit has undertaken this review subject to the limitations outlined below.

Internal control

- Internal control systems, no matter how well designed and operated, are affected by inherent limitations. These include the possibility of poor judgement in decision making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

Responsibilities of management and auditors

- It is management's responsibility to develop and maintain sound systems of risk management, internal control and governance for the prevention and detection of irregularities and fraud. Internal audit work should not be a substitute for management's responsibilities for the design and operation of these systems.
- Internal audit endeavours to plan audit work so that it has a reasonable expectation of detecting significant control weakness and if detected, will carry out additional work directed towards identification of consequent fraud or other irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected.
- Accordingly, these examinations by internal auditors should not be relied upon solely to disclose fraud or other irregularities which may exist.

Stage	Date
Draft issued	13 November 2023
Exit meeting	13 December 2023
Final issued	16 January 2024
ARAC meeting date	30 January 2024