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## **Online Banking and Internal Control Checks**

### **Introduction / Background:**

This report provides information on advice issued by the National Association of Local Councils (NALC) relating to parish councils' use of online banking, and the potential implications for the way in which the parish council operates with regard to the authorisation of payments.

### **The Current Position:**

Banking arrangements have developed enormously over the last few years, and at an increasing pace. Part of this is that the use of cheques is becoming more and more rare. Many businesses and individuals much prefer to receive payment by electronic means and are now discouraging the use of cheques. For example, HMRC will no longer allow the Post Office to accept cheques for the payment of tax and national insurance payments.

Recognising the trend, in 2014<sup>\*1</sup> the Government repealed Section 150(5) of the Local Government Act 1972, which required that *'every cheque or other order for the payment of money shall be signed by two members of the council'*.

In repealing this requirement, the Government stated: *'This rule is a significant barrier to these councils using electronic means of payment, and the effect is to impose additional burdens and costs both on them and on the private firms and other public sector bodies they make payments to'*.

The parish council, like many others, has been using online / telephone banking now for a couple of years. There are, on average, around 5 or 6 payments made electronically per month, including salary and wages payments to staff, tax and national insurance contributions to the HMRC and payroll costs to Robert Ogle Accountants.

### **The Risk:**

Having been set up initially via a bank mandate signed by 3 members, the parish council's bank account is operated solely by the parish clerk, including any payments made through electronic banking. This presents a very fundamental risk of fraud, since the parish clerk could make any payment to any person, including unauthorised payments.

### **NALC advice:**

NALC has recently issued guidance in relation to this, as follows:

*Councils must not relinquish the 'two-member signatures' control over cheques and other orders for payment until they have put in place safe and efficient arrangements in accordance with the guidance noted below from the NALC*

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<sup>1</sup> The Legislative Reform (Payments by Parish Councils, Community Councils and Charter Trustees) Order 2014; SI2014/580

*Finance and Audit Advisor: ‘The over-riding requirement resulting from the abolition of S150 (5) is that each and every local council seeking to depart from the two-signature rule must “implement and maintain robust controls on expenditure as an integrated part of their overall financial control system”. It is not a requirement that two people authorise electronic payments, however, it is a general principal that more than one person should be involved in any payment, whether that is before, at or after the point at which the payment is made. Councils must consider the appropriate systems, procedures and controls available by banking providers.*

*For example; councils could consider such a system:*

*With regard to banks:*

- *All signatories have viewing access to the council’s bank accounts;*
- *One councillor (signatory) authorises the payments using the electronic banking/on line system;*
- *All signatories are sent a text alert to notify them of payments being authorised; and*
- *All signatories able to view all transactions electronically With regard to internal controls:*
- **RECOMMENDATION FOR SHIPLAKE PARISH COUNCIL**
- **Clerk sets up the schedule of payments, the list of payments is sent to all members;**
- **A list of payments is approved at a council meeting;**

The parish clerk has checked with the account manager at the Cooperative Bank, who has stated the bank cannot/ will not facilitate any of the bank-related measures. It is understood this is a typical response from banks when asked about this matter.

At the moment, the parish clerk provides a schedule of proposed payments to the full parish council (all members) and makes payment only when the schedule has been approved by the parish council in a public meeting. This includes both electronic and cheque payments.

The fraud risk is that members have no sight of what actually is paid electronically out of the parish council’s account, meaning it would be straightforward in the first instance for the clerk to make unauthorised payments.

### **Insurance:**

The parish council holds fidelity insurance to protect it against any losses suffered through fraud. The insurers have been asked whether the parish council’s existing controls, outlined above, would ensure the parish council’s fidelity insurance cover would remain intact, or whether it could be compromised in the event of any fraud. Unsurprisingly, the insurers will not give a definitive response, stating instead that it is the parish council’s responsibility to comply with the provisions of the insurance cover and ensure there are adequate internal controls in place to prevent fraud.

The relevant policy provision states:

***Fund Transfers***

*Duties will be segregated in respect of electronic, fax, or telephone funds transfers, so that no one individual can complete a payment from beginning to end without referral to others.*

This is mirrored in the advice given by the NALC Finance and Audit Advisor.

It has been explained to the insurers that parish council procedures require referral to the full parish council prior to electronic payments being made, while pointing out this alone would not prevent the parish clerk from making unauthorised payments. Fidelity insurance cover is intended to provide protection where controls and procedures have been circumvented, so it should be the case that providing there are acceptable procedures in place, fidelity insurance cover should provide a backstop if ever the procedures are bypassed. However, the insurance provider would not provide a guarantee that this would be the case.

To sum up, the position as it stands at the moment is that the parish council cannot put in place the bank related controls outlined by NALC because of the stance taken by the banks – this is an issue that will need to be taken up nationally by NALC. In the meantime this means that, if the parish council wishes to continue with the use of electronic banking, it should put in place the best possible checks to ensure it minimises the risk of fraud and maximises the prospects of fidelity insurance cover being applicable in the event of any fraud.

One way of meeting this requirement, and improving oversight over payments, is to provide a full bank statement to members at least monthly, to enable members to satisfy themselves that there have been no unauthorised payments in the period. Options include, in descending order of control:

- Providing weekly bank statements to all members
- Providing weekly bank statements to the Chair and Vice-Chair
- Providing monthly bank statements to all members (probably as part of the monthly budget monitoring reports)

**RECOMMENDATION FOR SHIPLAKE PARISH COUNCIL**

- **Providing monthly bank statements to the Chair and Vice-Chair.**

All other insurance requirements should be incorporated into procedures within revised Financial Regulations.

**Summary and Options:**

In relation to the process / approval of payments, a crucial insurance and control requirement is that “*Duties will be segregated ... so that no one individual can complete a payment from beginning to end without referral to others*”. The parish council procedures would appear to cover this requirement by virtue of the pre-approval by members of any payments made.

It would only be where procedures are circumvented and unauthorised payments made that the parish council would run the risk of suffering financial losses. Fidelity insurance cover is in place to provide a protection against procedures being circumvented and should, therefore, apply, although the parish council's insurer will (understandably) not guarantee the applicability of fidelity insurance cover in the event of any unauthorised payments. The parish council can strengthen its arrangements for preventing fraud and complying with insurance requirements by adding to its current procedures.

Options for members to consider are:

- Cease online payments and revert to payment by cheque for all payments until banks are prepared to enable better controls to protect parish councils – *this would maximise control but be detrimental to staff and out of step with banking developments and commercial expectations*
- Continue (only) with existing arrangements – *this provides a degree of control and may meet insurance expectations for fidelity insurance cover in the event of any unauthorised payments*
- **RECOMMENDATION FOR SHIPLAKE PARISH COUNCIL**
- **Continue with existing arrangements, and augment these by providing bank statements to members as above – this would strengthen existing arrangements, and the expectation of insurers, while enabling a contemporary approach to (selected) payments.**

R V Hudson  
Clerk to the Council

Reviewed and approved Monday March 18<sup>th</sup> 2019

Chairman:.....  
RFO:.....