

Item: 7

Monitoring and Audit Committee: 5 February 2026.

Internal Audit – Treasury Management.

Report by Chief Internal Auditor.

1. Overview

- 1.1. The internal audit plan 2025/26 includes a review of Treasury Management. This audit has been completed and the internal audit report is attached as Appendix 1 to this report.
- 1.2. Treasury management is a critical function within the Council, underpinning the effective stewardship of public funds and supporting the delivery of the Council's strategic objectives.
- 1.3. The Council's Treasury Management Strategy Statement outlines its commitment to managing investments and borrowing in a manner that prioritises security, liquidity and yield, in accordance with the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code and the Prudential Code.
- 1.4. The objective of this audit was to provide assurance that the Council's treasury management activities are effectively governed, compliant with statutory and regulatory requirements and appropriately managing financial risks in support of strategic objectives.
- 1.5. The audit provides Substantial assurance that procedures and controls relating to Treasury Management are well controlled and managed.
- 1.6. The internal audit report, attached as Appendix 1 to this report does not include any recommendations.

2. Recommendations

- 2.1. It is recommended that members of the Committee:
 - i. Scrutinise the findings contained in the internal audit report, attached as Appendix 1 to this report, relating to the procedures and controls in respect of treasury management activities, in order to obtain assurance that action has been taken or agreed where necessary.

For Further Information please contact:

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Implications of Report

1. **Financial:** None directly related to the recommendations in this report.
2. **Legal:** None directly related to the recommendations in this report.
3. **Corporate Governance:** In terms of the Scheme of Administration, the consideration of Internal Audit findings and recommendations and the review of actions taken on recommendations made, are referred functions of the Monitoring and Audit Committee.
4. **Human Resources:** None directly related to the recommendations in this report.
5. **Equalities:** An Equality Impact Assessment is not required in respect of Internal Audit reporting.
6. **Island Communities Impact:** An Island Communities Impact Assessment is not required in respect of Internal Audit reporting.
7. **Links to Council Plan:** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Council Plan strategic priorities:
 - ☐ Growing our Economy.
 - ☐ Strengthening our Communities.
 - ☐ Developing our Infrastructure.
 - ☐ Transforming our Council.
8. **Links to Local Outcomes Improvement Plan:** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Local Outcomes Improvement Plan priorities:
 - ☐ Cost of Living.
 - ☐ Sustainable Development.
 - ☐ Local Equality.
 - ☐ Improving Population Health.
9. **Environmental and Climate Risk:** None directly related to the recommendations in this report.
10. **Risk:** Internal Audit evaluates the effectiveness and contributes to the improvement of the risk management processes.
11. **Procurement:** None directly related to the recommendations in this report.
12. **Health and Safety:** None directly related to the recommendations in this report.
13. **Property and Assets:** None directly related to the recommendations in this report.
14. **Information Technology:** None directly related to the recommendations in this report.

15. Cost of Living: None directly related to the recommendations in this report.

List of Background Papers

Internal Audit Plan 2025/26.

Appendix

Appendix 1: Internal Audit Report – Treasury Management.



Internal Audit

Audit Report

Treasury Management

Draft issue date: 17 November 2025

Final issue date: 1 December 2025

Distribution list:	Director of Enterprise and Resources
	Head of Finance
	Service Manager (Corporate Finance)
	Team Manager (Corporate Finance)
	Senior Accounting Officer (Treasury)

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Audit Opinion

Based on our findings in this review we have given the following audit opinion.

Substantial

The framework of governance, risk management and control were found to be comprehensive and effective.

A key to our audit opinions and level of recommendations is shown at the end of this report.

Executive Summary

This audit reviewed the Treasury Management function within Orkney Islands Council, focusing on governance, risk management, cash flow, lending, borrowing, capital investment, fraud prevention, and reporting controls. The review concluded that the Council has implemented a robust framework of controls that align with Chartered Institute of Public Finance and Accountancy (CIPFA) codes, statutory requirements, and best practice standards.

Key strengths identified include:

- Annual review and approval of the Treasury Management Strategy Statement (TMSS), which integrates capital planning and risk management.
- Strong segregation of duties, dual authorisation, and secure access controls across treasury operations.
- Effective use of external advisors, with performance monitored and supplemented by regular training for staff and committee members.
- Daily cash flow monitoring and timely investment of surplus funds.
- Compliance with investment and borrowing policies, with prudent use of internal resources and monitoring against statutory limits.
- Secure and well-documented payment processes, with accurate recording and validation of transactions.
- Proactive fraud prevention measures, confirmed by an external review conducted by the Royal Bank of Scotland (RBS) in September 2025.
- Oversight by the Investments Sub-committee through quarterly and annual reporting, benchmarking and scrutiny of performance.

Treasury risks are actively managed and integrated into business continuity planning and risk registers. No material control weaknesses were identified, and no recommendations have been raised.

The assistance provided by officers contacted during this audit is gratefully acknowledged.

Introduction

Treasury management is a critical function within Orkney Islands Council, underpinning the effective stewardship of public funds and supporting the delivery of the Council's strategic objectives.

The Council's Treasury Management Strategy Statement (TMSS) for 2025/26 outlines its commitment to managing investments and borrowing in a manner that prioritises security, liquidity and yield, in accordance with the CIPFA Treasury Management Code and the Prudential Code.

This review was conducted in conformance with the Global Internal Audit Standards in the UK Public Sector.

Audit Scope

The audit scope included:

- Governance and oversight arrangements.
- Compliance with approved treasury policies, limits and statutory requirements.
- Investment and borrowing activities, including risk management and performance monitoring.
- Cash flow forecasting and liquidity management.
- Controls over treasury transactions, including segregation of duties, authorisation and reconciliation processes.
- Use and oversight of external treasury advisors.
- Accuracy and timeliness of treasury reporting and decision-making.

Audit Findings

1.0 Governance and Strategy

- 1.1 The Council has a Treasury Management Strategy Statement (TMSS) that is reviewed annually by the Policy and Resources Committee and subsequently approved at the General Meeting of the Council. The TMSS outlines the Council's approach to borrowing, investment, risk management, and performance monitoring. It is aligned with the CIPFA Treasury Management Code and the Prudential Code for Capital Finance in Local Authorities. The Strategy includes detailed prudential indicators, investment limits and governance arrangements.
- 1.2 Treasury Management procedures are embedded within the Council's Financial Regulations (Section 22), which delegate executive authority to the Head of Finance, ensuring accountability and compliance.

- 1.3 Responsibility for monitoring Treasury Management activities is delegated to the Investments Sub-committee. The audit reviewed meeting minutes and reports from September 2024 to May 2025 and confirmed that the Sub-committee receives regular updates and provides scrutiny of fund manager performance and strategic decisions.
- 1.4 Up-to-date procedures are in place and the function is managed by an experienced team with a strong understanding of individual responsibilities and associated risks.
- 1.5 Contingency arrangements are in place to ensure continuity of operations during staff absences, and communication of procedural changes is effective due to the small, well-integrated team structure.
- 1.6 Members of the Investments Sub-committee receive regular training sessions, supplemented by external advisors, with logs confirming attendance. Treasury management staff also attend this training.

2.0 Risk Management

- 2.1 The Finance Service demonstrates a proactive approach to risk management through its TMSS which includes a comprehensive assessment of key risks and references controls to mitigate these.
- 2.2 Treasury management is considered within a threat and risk assessment used to inform business continuity planning and feeds into the Enterprise and Resources risk register and the Council's corporate risk register, where appropriate.
- 2.3 The lending and borrowing controls in place are intended to achieve maximum possible returns without exposing the organisation to unacceptable risks or loss. All borrowing is conducted in sterling.
- 2.4 Investment limits are established based on credit ratings and the credit standing of counterparties is reviewed regularly.

3.0 Cash Flow

- 3.1 Cash flow is monitored daily by the Senior Accounting Officer using the Treasury Live system. Forecasts are based on bank balances, expected payments and receipts, with additional checks via an office diary.
- 3.2 Surplus funds are invested promptly in Money Market Funds (MMFs) or transferred between accounts. Deficits are covered using immediate access accounts. The Council does not maintain an overdraft facility, which is deemed appropriate given the low frequency of overdrawn instances.
- 3.3 A sample of eight daily cash flow forecasts confirmed that procedures are followed consistently. Forecasts are supported by bank documentation, reviewed by senior staff, and actions are recorded.

4.0 Lending

- 4.1 The TMSS outlines permitted investments, institutions, limits, and monitoring requirements. Investments are diversified and prioritise security and liquidity.

- 4.2 Creditworthiness is assessed using Link Group reports. All sampled institutions had acceptable ratings.
- 4.3 All investment decisions reviewed were compliant with the investment policy. Investments are managed to avoid interference with cash flow needs. Daily forecasts and short-term liquidity positions are maintained.
- 4.4 All sampled transactions were valid, authorised by appropriate staff and supported by documentation. Records are securely stored.
- 4.5 Transactions were accurately recorded in Integra and reconciled with the internal tracking document and supporting documentation. The internal tracking document is password protected and is a strong control tool supporting compliance and accuracy.
- 4.6 The internal tracking document identified that overnight the short-term investments exceeded the 25% counterparty limit set out in the Treasury Management Strategy Statement (TMSS). The breach was promptly corrected, demonstrating that the control is operating effectively.
- 4.7 Expanded testing confirmed no further errors and the resulting additional evidence showed that investment limits are managed with diligence.

5.0 Borrowing

- 5.1 The Council's borrowing policy is clearly defined within the Treasury Management Strategy Statement (TMSS) and Financial Regulations. All borrowing decisions are delegated to the Head of Finance and must comply with the CIPFA Code and statutory powers under the Local Government (Scotland) Act 1973.
- 5.2 Borrowing is only undertaken when other funding sources (e.g. reserves, grants) are unavailable. The TMSS outlines approved borrowing types, financial limits, and repayment methods. The Council maintains an under-borrowed position and uses internal resources to avoid unnecessary external debt.
- 5.3 Borrowing is monitored against Prudential Indicators, including the Capital Financing Requirement (CFR), operational boundary, and authorised limit. As of 31 March 2025, total borrowing was £50 million, well within the authorised limit of £85 million for 2024/25. At as 30 June 2025, the borrowing remained at £50 million.
- 5.4 Borrowing records are maintained in a secure internal system and reconciled monthly to the Council's financial ledger. Interest and repayment schedules are calculated and verified.
- 5.5 Loan repayments are managed effectively, with invoices from the Public Works Loan Board (PWLB) received in advance. Repayments are tracked and confirmed against internal records.
- 5.6 The TMSS includes consideration of future borrowing needs, interest rate forecasts, and alternative funding options. The Council's borrowing strategy prioritises risk containment over return maximisation.

6.0 Capital Investment

- 6.1 The Treasury Management Strategy Statement (TMSS) has been updated to reflect the 2017 Prudential Code requirement for an annual capital strategy. This provides a high-level overview of capital planning, risk management and financial sustainability.

- 6.2 Capital investment performance is monitored quarterly and benchmarked using external reports (e.g. Link Group). Local performance indicators are in place and reviewed by the Investments Sub-committee.

7.0 Payments

- 7.1 Payments are processed through RBS Bankline, which uses dual-factor authentication and individual logins. Access is restricted to authorised finance staff, and PINs are securely managed.
- 7.2 There is clear separation between staff initiating, checking, and authorising transactions. Payments require dual authorisation by management, and audit trails are maintained via email.
- 7.3 Payment records are securely stored on the Council's restricted network. Sampled payments were properly documented, authorised, and matched to the loans register.
- 7.4 Transactions were traced to Integra and found to be promptly recorded and correctly coded. Ledger entries are validated and corrected where necessary.
- 7.5 Unallocated income is tracked and investigated. As of 30 October 2025, only four items remained unallocated, none of which were treasury related.
- 7.6 Fees paid to brokers and advisors were verified against ledger entries and found to be accurate and appropriately recorded.

8.0 External Service Providers

- 8.1 Controls over external service providers are appropriate and well-documented. Contracts are current and authorised staff are clearly designated. Performance of treasury advisors is monitored through regular reporting provided and this is scrutinised at committee.

9.0 Fraud Prevention

- 9.1 RBS Bankline procedures include clearly defined user authorisation levels. Access is restricted to finance staff, and roles are appropriate to job responsibilities.
- 9.2 The Council's network enforces regular password changes. Bankline access requires secure PIN machines and web portal authentication, meeting RBS security standards.
- 9.3 Access rights are reviewed regularly, and all users were confirmed to be in appropriate roles. No inappropriate access was identified.
- 9.4 RBS conducted a Fraud and Operational Review for the Council in September 2025 which was a practical assessment of fraud prevention measures. This led to some operational detail updates being made and information on current fraud trends being shared with the team.

10.0 Monitoring and Reporting

- 10.1 The Investments Sub-committee provides regular scrutiny of treasury activities. Quarterly and annual reports are presented to the Sub-committee. Investment performance is assessed quarterly and benchmarked against market standards. Reports include economic updates, interest rate forecasts and fund manager reviews.

- 10.2 The annual performance report complies with CIPFA guidance, includes a full review of treasury decisions and performance, and confirms compliance with policy and statutory limits.
- 10.3 Within the latest quarterly review presented in September, covering the period 1 April to 30 June 2025, the Council's treasury management activities were assessed.
- 10.4 Temporary investments yielded an average return of 4.33%, closely aligned with the Sterling Overnight Index Average (SONIA) Benchmark (4.36%). The Strategic Reserve Fund outperformed its benchmark, achieving a 4.2% return against a target of 3.3%.
- 10.5 Total debt stood at £50 million with an average cost of borrowing of 3.93% and a weighted average duration of 30.8 years. A new £10 million PWLB loan was secured in April 2025 at 4.81% to support capital financing needs.
- 10.6 Credit risk was effectively managed, with a weighted average risk number of 1.09 and no breaches of investment limits. The Council's liabilities remained below the benchmark, indicating a conservative borrowing strategy.
- 10.7 The Council demonstrated awareness of macroeconomic trends, including inflation, interest rate movements, and geopolitical risks, and adjusted its investment strategy accordingly.

11.0 Environmental, Social and Governance Considerations

- 11.1 Changes to the CIPFA Treasury Management Code 2021 saw Environmental, Social and Governance (ESG) incorporated into Treasury Management Practice 1. The following wording (page 18 of the Treasury Management Code), provided by the treasury management advisors, suggests the scope of what is included: "The organisation's credit and counterparty policies should set out its policy and practices relating to environmental, social and governance (ESG) investment considerations. This is a developing area, and it is not implied that the organisation's ESG policy will currently include ESG scoring or other real-time ESG criteria at individual investment level."
- 11.2 The advisors continue to monitor developments in ESG integration and will update clients as market practices evolve. This provides assurance that ESG considerations are appropriately reflected within the Council's treasury management practices and are compliant with the CIPFA Treasury Management Code.

Key to Opinion and Priorities

Audit Opinion

Opinion	Definition
Substantial	The framework of governance, risk management and control were found to be comprehensive and effective.
Adequate	Some improvements are required to enhance the effectiveness of the framework of governance, risk management and control.
Limited	There are significant weaknesses in the framework of governance, risk management and control such that it could be or become inadequate and ineffective.
Unsatisfactory	There are fundamental weaknesses in the framework of governance, risk management and control such that it is inadequate and ineffective or is likely to fail.

Recommendations

Priority	Definition	Action Required
High	Significant weakness in governance, risk management and control that if unresolved exposes the organisation to an unacceptable level of residual risk.	Remedial action must be taken urgently and within an agreed timescale.
Medium	Weakness in governance, risk management and control that if unresolved exposes the organisation to a significant level of residual risk.	Remedial action should be taken at the earliest opportunity and within an agreed timescale.
Low	Scope for improvement in governance, risk management and control.	Remedial action should be prioritised and undertaken within an agreed timescale.