

APPENDIX 1

Rochford District Council

SAS610

DRAFT

**Report to Finance and Procedures
Overview and Scrutiny Committee**

November 2004

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1 Introduction

Our work to date

- 1.1 Within our Audit Plan for 2002 – 2004, as supplemented by our Mini Audit Plan, we outlined the work that we would be carrying out in order to meet our Code of Audit Practice responsibilities.
- 1.2 We have now completed the final phase of our work on the 2003/04 Statement of Accounts and this report gives the results of this work. Our work has focused on an assessment of the Authority's arrangements in two specific areas of our audit responsibilities:
- Our audit opinion on the Authority's financial accounts; and
 - Issues relating to Systems of Internal Financial Control not covered at our interim visit.
- 1.3 Detailed recommendations in response to the key findings identified by our review are provided in the attached Action Plan. These recommendations have been discussed with appropriate officers and their responses are included in the Plan.
- 1.4 We emphasise that in this report we do not provide a comprehensive statement of all weaknesses which may exist in the accounting and control systems, but only those matters which have come to our attention as a result of audit procedures performed.

Status of our report to the Authority

- 1.5 This report has been prepared for Members' and Officers' information only and is not intended to include every matter that may have come to our attention. We accept no responsibility for any reliance that might be placed on it for any purpose by third parties, to whom it should not be shown without our prior written consent.

Acknowledgement

- 1.6 We would like to thank the staff of the Authority, in particular those of the Financial Services Unit for the co-operation and assistance provided during the audit.

2 Opinion audit work

- 2.1 The Corporate Director (Finance and External Services) is responsible for preparation of the Authority's financial statements in accordance with the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2003.
- 2.2 As the appointed auditors, our main objective is to form an independent view on the Statement of Accounts.

Scope of our work

- 2.3 Our audit covers all the Statements of Account. In accordance with the Code of Audit Practice we must assess whether the Statements present fairly the financial position of the Authority as at 31 March of the financial year and its income and expenditure for the year in question.
- 2.4 In completing these assessments we consider a number of aspects which may have an impact on our ability to issue an unqualified opinion. These aspects include:
- Assessing systems reliance;
 - Reviewing the accounts preparation process; and
 - Completing analytical review, testing balances and considering the adequacy of disclosures.

Our Findings

Systems reliance

- 2.5 In advance of the detailed testing of the completed financial statements, we have reviewed the core financial systems in place across the Authority which contribute to the preparation of accurate financial statements, to assess the extent to which we can place reliance on them for this purpose.
- 2.6 Our approach to the audit of the core financial systems has involved considering key control areas for each system and satisfying ourselves that they are operating as intended and are sufficient to prevent material misstatements within the accounts. In assessing the reliability of systems as a basis for providing financial information, we have prepared systems notes for each financial system and performed walkthrough tests of key controls.
- 2.7 Where possible, we have placed reliance on Internal Audit's work and thereby avoided unnecessary duplication of audit effort on the systems work relevant to our audit opinion. To ensure this approach was valid, we have undertaken the following exercises:
- Reviewed Internal Audit's working papers and reports;
 - Considered the robustness of the core financial systems on the evidence of this work; and
 - Re-performed a sample of Internal Audit's testing of key controls, to establish that Internal Audit's conclusions are soundly based and that we do not disagree with them.
- 2.8 Following our review of their working papers, we have been able to place reliance on some of the work of Internal Audit this year. However, we still feel that there are some further improvements that can be made, in particular in ensuring that all controls are adequately reviewed and evidenced as such, and that the controls have been reviewed throughout the year under review.

- 2.9 Testing of individual systems has indicated a number of control weaknesses that exist at present. These include:
- The use of correct dates on debtors invoices being raised, resulting in potential problems with cut-off;
 - Chasing of overdue Housing Rent debts, giving rise to possible issues over recoverability of debtors; and
 - Authorisation procedures in respect of discounts and exemptions for NNDR.
- 2.10 However, our principal concern arising from the systems review has been the failure to complete, or evidence completion, of a number of the key reconciliations within the core financial systems. Whilst we are aware that there are, in certain instances, reasons for these failures, reconciliations are a key control within each of the systems and any failures represent significant control issues that weaken the overall system of internal control.
- 2.11 As a result of the above issues, we planned to carry out additional work as part of the final accounts audit to obtain the necessary assurance over the accuracy of the financial statements presented for audit.

The Accounts Preparation Process

- 2.12 In general, we have found an improvement with the level of preparedness of the Authority for audit this year, with the vast majority of information being available on our arrival, and a complete set of approved accounts being provided on the first day of the audit.
- 2.13 Whilst the Authority is to be congratulated for this achievement, it is important that further steps are taken to improve the closedown process in light of the continued shortening of deadlines for accounts approval and audit clearance in 2005 and 2006.

Analytical Review and Testing of Balances

- 2.14 Whilst we experienced some delays in obtaining explanations and supporting evidence for variances arising from our analytical review of information within the financial statements, we have obtained satisfactory explanations and analysis of all balances to support explanations for the variances within the accounts.

Adequacy of Disclosures

- 2.15 A number of presentational changes have been suggested to improve the clarity of certain notes to the accounts and we have, at the time of drafting this report, just received a copy of updated accounts that should reflect these changes. These include:
- The increase made to the provision for HRA bad debts has not been included as a separate line within the HRA;
 - Amortised premiums and discounts included after net cost of service within the CRA;
 - Statement of accounting policies amended for the fact that non-operational assets had not been re-valued as at 1 April 2004;
 - A number of changes to the disclosures required in respect of FRS17;
 - Additional disclosure in respect of a significant post balance sheet event within the accounts; and
 - A difference in the value of council dwellings recorded in notes to the HRA and Balance sheets.

- 2.16 In addition, we have identified a number of areas where the disclosure within the accounts could be clarified in the future. Where necessary, recommendation that the Authority considers amending the disclosure for the 2004/05 accounts have been documented within Appendix B to this report, although we do not consider these points to be of sufficient significance that they require an adjustment to the 2003/04 accounts.

SAS 610 responsibilities

- 2.17 Statement of Auditing Standard 610 (“SAS 610”) requires auditors to communicate relevant matters relating to the audit with “those charged with governance”, who at Rochford District Council have been agreed as the Finance & Procedures Overview & Scrutiny Committee. The content of this report forms part of our reporting on the results of our final accounts audit to the Finance & Procedures Overview & Scrutiny Committee, and will be supplemented by the preparation of our Annual Audit Letter.

- 2.18 In particular we are required to report:

- Expected modifications to the audit report;
- Unadjusted misstatements;
- Material weaknesses in accounting and internal control systems identified during our work;
- Qualitative aspects of accounting practices and financial reporting; and
- Any other relevant matters.

- 2.19 Our comments in these areas are set out below:

Audit Report

- 2.20 There are no proposed modifications to the auditors’ report.

Unadjusted misstatements

- 2.21 During the course of our audit we identified what we regard as a number of non-trifling misstatements for which no amendments were made to the statement of accounts. In accordance with the requirements of SAS 610.5(b), these are detailed within Appendix A.

- 2.22 As these misstatements were not considered by management to be material we propose signing an unqualified audit opinion on the accounts. However, in accordance with SAS 610.6, we will require written representation of the reasons for not making the amendments. Whilst the impact of the misstatements is below the materiality level which we set for the audit, they are significant amounts which should ideally be reflected in the accounts.

Accounting and Control systems

- 2.23 As a result of our work on the financial systems, we have noted a number of matters to Officers in a separate document. However, we would draw Members’ attention to the key issue identified from this work, namely the problems related to reconciliations mentioned in paragraph 2.10 which has resulted in additional work being performed as part of our year end audit..
- 2.24 The Authority has produced, and included within the accounts as required, a Statement on Internal Control. We have reviewed this and found it to be consistent with our wider understanding of the control environment.

Accounting Practices and Financial Reporting

- 2.25 In addition to the comments noted above, we specifically wish to draw the attention of the Finance & Procedures Overview & Scrutiny Committee to the following points.

Bad debt provision

- 2.26 Our work on the bad debt provision has identified that the provision is currently larger than the remaining outstanding debt and as such the Authority is therefore over-providing against the old debt. Our review of amounts has identified that there is an over provision of £60k.

- 2.27 We have also reviewed the overall process used by the Authority in calculating the annual bad debt provision, and note that although income continues to be received in respect of older years the provision in respect of these years is often at 100%. We are aware that this has been the method of calculation for a number of years. However, in light of the over provision there is a need for a detailed review of the percentages used in calculating the various bad debt provisions, with the percentages being based on past collection rates for the age of debt.

Bank reconciliation

- 2.28 During our systems work at the interim we noted that there was an ongoing issue with the completion of the monthly bank reconciliation which had, for some time, included a balancing figure.

- 2.29 We have reviewed the reconciliation as part of our work on the financial statements and have noted that, to date, the reconciliation continues to include a balancing figure. Although the amount involved is small, there is a need to ensure the reconciliations are accurate and that reconciling are investigated and adjusted for as soon as possible.

Earmarked reserves

- 2.30 During our work we have noted that there have been, during the year, a large number of additional earmarked reserves created. The Authority currently has a total of forty four earmarked reserves, and whilst we are aware that many of these have been created for specific purposes we do not feel that there should be such a significant number of reserves. In order to reduce the number of reserves, all of them should be subject to a detailed review and only retained where there is a long-term commitment to a project, such as the Park development. All of the remaining reserves should be credited back to the General Fund.

Long Term Debtors

- 2.31 Whilst reviewing long term debtors it was noted that there is an apparent misunderstanding within the Authority about which balances should be included within this category. Our review indicated that certain of the debts within this balance, namely service charges, are actually due within 24 months rather than in excess of a year. These amounts are therefore incorrectly disclosed within the financial statements.

- 2.32 A further issue arises from this incorrect disclosure, in that the recoverability of these debts has not been considered as part of the review of the Authority's bad debt provision at year end. This may result in an under provision at the year end.

Benefits amendment

- 2.33 Prior to the completion of the Audit, the Authority identified an amendment that was required in respect of benefit expenditure. Specifically it was noted that an amount of income recorded in 2003/04 actually related to 2002/03. This amendment has been required as a result of the day on which the year end fell, which was in the middle of a week, which resulted in some payments made at the end of that week relating to both years.
- 2.34 Our review of the amendment made has noted that some of the payments are in respect of both 2002/03 and 2003/04 and therefore the amendment has been overstated. A rough calculation of the amounts indicates that this is approximately £71k.

FRS17

- 2.35 The Council is provided with the relevant pension scheme information for inclusion in the final accounts by the actuary to the scheme, this being received via Essex County Council. We understand that the Council places reliance on this information and performs minimal review of it to ensure it is in line with expectations. As the information is included in the Council's accounts, a review of the information should be performed to ensure it is appropriate.
- 2.36 In addition, as noted under paragraph 2.15 above, this review should help to identify those areas where there are omissions in the information required, allowing the Council to follow up and obtaining the necessary information.

Other Matters

- 2.37 There are no other matters arising from our work that we wish to bring to the Finance & Procedures Overview & Scrutiny Committee's attention.

3 Financial Aspects of Corporate Governance

- 3.1 It is the Authority's responsibility to put in place proper arrangements to ensure the proper conduct of its financial affairs, and to monitor their adequacy and effectiveness in practice. It is our responsibility to review those arrangements.

Scope of our work

- 3.2 Our work is structured around four key elements, in line with our Code of Audit Practice responsibilities:
- Financial Standing of the Authority;
 - Systems of Internal Financial Control;
 - Standards of Financial Conduct, and the Prevention and Detection of Fraud and Corruption; and
 - Legality of Transactions that might have significant financial consequences.

- 3.3 This section deals with our work on Systems of Internal Financial Control Code objective and in particular the Authority's Statement of Internal Control. Our work in respect of all other areas is ongoing and will be reported within the Annual Audit Letter.

Systems of Internal Financial Control

- 3.4 We previously concluded on the work completed as part of our interim visit within our Interim report as issued to officers. We are currently in the process of discussing and agreeing the content of this report.

Statement on Internal Control

- 3.5 All local authorities are required to review at least annually the effectiveness of their systems of internal control, and to include a Statement on Internal Control (SIC) in the 2003/04 accounts.
- 3.6 We are satisfied that the SIC included in the accounts reflects compliance with CIPFA's guidance and is not inconsistent with other information of which we are aware from our audit of the Council's accounts. The SIC sets out areas where the Council needs to perform work to improve internal control arrangements, and is currently considering how to address these.

Financial Standing

- 3.7 Authorities should have robust arrangements in place to meet financial obligations and to ensure financial standing is soundly based. The consequences of poor financial standing are significant, with the risk of reductions in service provision, and threats to the achievement of priority objectives.
- 3.8 We are in the process of completing our work in this area and will report the findings of this within the Annual Audit and Inspection Letter.

Financial Conduct, Fraud and Corruption

- 3.9 The Authority should ensure that its affairs are managed in accordance with proper standards of financial conduct, and put in place appropriate arrangements to prevent and detect fraud and corruption.
- 3.10 We discharged our obligations by:
- Reviewing the Authority against a checklist of the arrangements that we would expect it to have in place;
 - Discussing the scope of work performed during the year with Internal Audit, to ascertain the level of coverage;
 - Discussing specific cases of frauds reported elsewhere to determine whether they have been perpetrated at the Authority;
 - Follow up review of progress against the key recommendations arising from the preparation of Auditor Scored Judgements for the recent Comprehensive Performance Assessment; and
 - Reporting to the Audit Commission all reported frauds over £1,000.

Our findings

- 3.11 Over a number of years the Authority has developed and implemented a number of policies and strategies to prevent and detect fraud. As a result the arrangements in place generally appear to be strong, although some minor improvements are required to respond to weaknesses identified as a result of our review against the 2003 Auditor Scored Judgements, details of which are included in Appendix B.

Legality

- 3.12 The Authority has the responsibility of putting in place adequate arrangements to ensure that its financial affairs are conducted within the law and regulations.
- 3.13 We discharged our responsibility by reviewing the Authority's Statement of Accounts and appropriate Council and Committee agenda papers and minutes, discussing matters with officers, considering Audit Commission advice, reviewing the applicability of national issues and re-visiting the Auditor Scored Judgements reached as part of our contribution to the Comprehensive Performance Assessment undertaken by the Audit Commission.

Our findings

- 3.14 We are satisfied that the Authority is taking appropriate steps to respond to new legal issues that arise, based on our specific review of the overall arrangements in place and recent steps taken to respond to developments such as the Disability Discrimination Act.

Appendix A – Unadjusted misstatements

Schedule of unadjusted misstatements.

The table below details the misstatements recorded during the audit that have not been adjusted for within the Statement of Accounts.

	Income £'000	Expenses £'000	Assets £'000	Liabilities £'000	Reserves £'000
Items above materiality					
No misstatements above materiality were identified.					
Items below materiality					
Overprovision for bad debts – amount in excess of current outstanding long term debtors.		(60)	60		
Reclassification of service charge debtors from long to short term. The value is £87k but only impacts on the balance sheet.			-		
Amendment to the Benefit adjustment for prior years (as made by Rochford).		71			(71)
		11	60	-	(71)

Appendix B - Recommendations arising from 2004 audit

Conclusions from work	Recommendations	Priority	Management response	Responsibility	Timing
Final Accounts The following recommendations arose from our review of the Authority's financial statements:					
Bad debt provision As a result of our review of the overall process used by the Authority in calculating the bad debt provision, we have noted that despite income still being received in respect of older years, the provision for these years often remains at 100%. We are aware that this has been the method of calculation for a number of years.	The Authority should perform a detailed review of the percentages used in calculating the bad debt provisions, basing any revised percentages on past collection rates for the age and type of debt.	High			
Bank reconciliation During our systems work at the interim we noted that there was an ongoing issue with the completion of the monthly bank reconciliation which had, for some time, included a balancing figure. We have reviewed the reconciliation as part of our work on the financial statements and have noted that, to date, the reconciliation continues to include a balancing figure.	There is a need to ensure the reconciliations are accurate and that reconciling are investigated and adjusted for as soon as possible	High			

Conclusions from work	Recommendations	Priority	Management response	Responsibility	Timing
Earmarked reserves					
The Authority currently has forty four earmarked reserves, with a number having been created during the current year. Whilst we are aware that many of these will have been created for specific purposes or projects, it is not best practice to retain such a significant number of earmarked reserves.	All earmarked reserves should be subject to a detailed review and only retained where there is a long-term commitment to a project, such as the Park development.	High			
Long term debtors					
Whilst reviewing long term debtors we noted some concerns with the disclosure of balances within this category. Our review indicated that certain of the debts within this balance are actually due within 2-4 months rather than in excess of a year. These amounts were therefore incorrectly disclosed within the financial statements.	The Authority should review all long term debtors at each year end to ensure amounts are correctly disclosed within the financial statements.	Medium			

Conclusions from work	Recommendations	Priority	Management response	Responsibility	Timing
STANDARDS OF FINANCIAL CONDUCT, AND THE PREVENTION AND DETECTION OF FRAUD AND CORRUPTION					
The following recommendations arose from our review of the Trust's Standards of Financial Conduct, and arrangements for the Prevention and Detection of Fraud and Corruption.					
Employees currently do not acknowledge that they have read and understood the staff Code of Conduct. Written acknowledgement provides assurance that staff are aware of what is required of them and should help to reduce instances of the code being broken.	Staff should be required to sign a document stating that they have read and understood the code of conduct.	Medium			
There is currently no centralised contact for receiving allegations of fraud or to provide guidance on issues arising. As a result there is a risk that some allegations may be overlooked or inappropriate actions taken in response to issues identified.	A central contact should be instated to act as a co-ordinator for all reported fraud and to advice as necessary.	Medium			
There is no standard basis for reporting and recording of fraud information. This inconsistency in reporting/recording may lead to some items not being investigated and reported appropriately. In addition, items may not be reported until a long-time after they have occurred and therefore there can not be any response on the allegation.	A protocol should be set up detailing what details should be recorded, who to contact and a set format for reporting developed.	Medium			