

Audit Detailed Report

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Systems and Accounts Audit Memorandum

Epping Forest District Council

Audit 2006/07

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Report

Introduction

- 1 The Code of Audit Practice (the Code) requires that external auditors undertake an audit of the financial statements of Local Authorities.
- 2 We are required to plan and perform our work in accordance with the International Standards on Auditing (UK and Ireland) (ISAs).
- 3 This report details issues identified during the audit of the financial statements of Epping Forest District Council, including both pre-statements work and post-statements substantive procedures.

Background

- 4 The objective of the audit is to give an opinion as to whether the financial statements:
 - present fairly the Council's financial position and its income and expenditure for the year; and
 - have been prepared in accordance with CIPFA's Statement of Recommended Practice (SORP), relevant legislation and applicable accounting standards (FRS).

Audit approach

- 5 In order to give an opinion, an assessment of the financial statements is made to determine whether they:
 - are free from material misstatement;
 - comply with statutory and other requirements applicable to the accounts; and
 - comply with relevant requirements for accounting presentation and disclosure.
- 6 This assessment is undertaken in two stages; pre statements testing before the financial statements are approved by Council and post statement testing after they have been approved.

Pre statements testing

- 7 Our pre statements testing consisted of the following elements:
 - *Identifying the risks of material error in the financial statements at the audited body level.* This included an assessment of external and internal factors, business risks, financial performance, internal control and other risks and was performed based on existing knowledge, recent Audit Commission work

carried out at the council such as Use of Resources, review of minutes and other key documentation.

- *Identifying the risks of material error in the financial statements at the systems level.* We have sought to understand and document all the significant financial systems relevant to financial reporting. This consists of the procedures and records that are established to initiate, record, process and report the transactions and to maintain accountability for the related assets and liabilities.
 - *Determining a testing strategy.* Our testing strategy is the way in which we seek to obtain sufficient assurance on the entries in the financial statements to enable us to form our opinion and can consist of reliance on controls or on substantive testing of figures in the financial statements or on a combination of both. We have to ensure that our testing is sufficient to mitigate the risks of error identified in the previous steps.
- 8 Where we had obtained assurance that controls were working effectively in 2005/06, we were able to roll this assurance forward in accordance with ISA (UK&I) 330 unless more recent information contradicted this conclusion.
- 9 In accordance with ISA(UK&I) 240, we consider the risk of material fraud. Fraud encompasses both misappropriation of assets and intentional financial misreporting.
- 10 The systems that we identified as having a significant input into the financial statements were :
- General Ledger
 - Housing Rents
 - NNDR
 - Council Tax
 - Housing Benefits
 - Sundry Debtors
 - Payroll
 - Creditor Payments
 - Cash
 - Treasury Management
 - Budgetary Control and
 - Fixed Assets.

Post statements testing

- 11 Once we had received the draft Council Accounts and supporting working papers our testing consisted of:
- the agreement of balances in the financial statements to the general ledger;

- predictive analytical review of balances;
 - substantive testing, where necessary;
 - the identification and discussion of potential errors and omissions with officers; and
 - ensuring compliance with the SORP.
- 12 Our audit programme at final accounts is tailored to the assessed risks. If we have been able to conclude that material controls are working consistently our substantive testing at final accounts is reduced.

Main conclusions

Material Systems

- 13 Our work identified a number of specific system weaknesses which we have included in the action plan in the appendix to this report. For our opinion purposes we are either satisfied that there are compensating controls that would identify a material error arising in the accounts as a result of these weaknesses or we have increased our substantive testing at year end to address the risk. We are however reporting the weaknesses to you as significant control weaknesses which could allow fraud or error and which therefore need to be addressed. Some of the weaknesses identified have already been reported to you by Internal Audit but we are highlighting again in this report to emphasise the importance of addressing these control weaknesses.

Recommendations

R1 Issues already reported by Internal Audit:

- during 2006/07 there were instances where orders were being authorised by the same person who signed the invoice, in contravention of the Financial Regulations. The Council should ensure that Financial Regulations are fully complied with in purchasing to ensure that segregation of duties is maintained; and
- there were members of staff who had left the authority were still being paid. The Authority should ensure that Payroll is notified promptly when a member of staff leaves and that changes are processed promptly. In addition managers should retain evidence that they are checking staff being charged to their budgets.
- All journals should be signed, countersigned and be supported by an adequate narrative and supporting documentation where applicable.
- the payments bank reconciliation should be carried out on a regular basis.

Recommendations	
<i>R2</i>	<i>The Council should resolve the issue of unpresented cheques dating back as far as 2002 that are still included in the bank reconciliation. This issue has been raised in previous years and has been noted by internal audit.</i>
<i>R3</i>	<i>The Council should put in place a formal procedure for the back up of major IT systems.</i>
<i>R4</i>	<i>The Council should ensure that staff levels in the IT department are adequate and that controls are not compromised by the current recruitment difficulties</i>
<i>R5</i>	<i>The reconciliation of council tax refunds in Orbis to Cedar has not been carried out regularly due to a member of staff being on maternity leave. The Council should ensure that staff members are able to carry out each others duties in case of absence.</i>
<i>R6</i>	<i>The balance sheet value of the Council's Fixed Assets is in excess of £648,000,000. The Council should implement a more robust and secure fixed asset register that will enable the Council to implement the impending changes in capital accounting.</i>
<i>R7</i>	<i>The Council should retain evidence of the sample checks carried out on NNDR refunds.</i>

Financial Statements Approval and Opinion

- 14** The draft financial statements were approved by Council on 28 June 2007, ahead of the statutory deadline of 30 June 2007.
- 15** We have a duty under the International Auditing Standard (ISA) 260 to issue an Annual Governance Report to those charged with governance, in this case the Audit Committee, on any non-trivial errors and material adjustments. The Annual Governance report was presented to the Audit and Governance Committee on 13 September 2007. An unqualified opinion was issued on the financial statements on 20 September 2007.
- 16** The Annual Governance Report highlighted that the Council should seek advice on the way VAT had been accounted for following the sale of Wickfields. The Audit and Governance Committee asked officers to contact HM Revenue and Customs.

Recommendations

R8 Officers should ensure they seek HMRC advice on the VAT treatment applied to the sale of Wickfields.

Working Papers

- 17 A schedule of our working paper requirements for the post statements audit was provided to the Council.
- 18 The Council provided most of the working papers requested to support the accounts at the start of the audit. Where further working papers were required, or clarification was needed to explain those that were received, officers were able to provide them. Some delays were encountered in obtaining breakdowns for the sundry debtor and creditor balances to enable substantive testing of invoices. In future it is recommended that these should be provided in advance of the audit to enable the audit to progress more smoothly. There was an improvement in the audit trail from the accounts to the trial balance compared with previous years. Most reconciliations of feeder systems to the general ledger were provided on the working paper file but due to problems obtaining information from Anite, officers were unable to provide a reconciliation of council tax benefits until late in the audit.

The Recommendations

R9 The Council should ensure that a list of sundry debtor invoices and a list of sundry creditor invoices are included in the working papers provided for audit.

Amendments to the Financial Statements

- 19 No material amendments were required. A number of non-material amendments were made to the accounts as a result of the audit. These are listed below and included in the action plan in the appendix in order to ensure that the draft accounts presented for audit in 2007/08 incorporate all the improvements made this year:
- housing benefit overpayments which are being recovered from ongoing benefit payments were not included in the debtors figure. For 2006/07 this was £122,000;
 - there was no disclosure of a contingent liability for potential compensation or legal costs relating to the location of a mobile phone mast although this issue arose after the accounts had been approved;
 - no detailed breakdown of deferred charges was included in the accounts; and
 - there was no disclosure of the qualifications of the valuer or whether the valuer is internal or external to the organisation.

<i>The Recommendations</i>

<i>R10 The Council should ensure that the non-material errors highlighted by this year's audit and corrected are not repeated for the 2007/08 accounts as the identification and correction of errors takes additional officer and audit time.</i>
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Further improvements for the future

- 20 Some further matters arising during the audit which did not require an amendment to the accounts are listed below in order for the Council to make improvements for 2007/08:
- the guidance sent to officers and members on related party transactions is clear but does not explain that relevant transactions are those that are material to either the Council or the related party. Creditors and debtors with related parties should also be disclosed. This recommendation was made in the 2005/06 Final Accounts Memorandum and agreed but has not been implemented. Not all the declarations for 2006/07 had been returned to the Council at the time of the audit;
 - the valuer should confirm the estimated useful economic life of the Council assets; and
 - the 2005/06 Orbis report on NNDR credits carried forward differs to the 2006/07 Orbis report on NNDR credits brought forward by £54,000. The figures should match and the difference has not been explained by the Council, this should be resolved.

<i>Recommendations</i>

<i>R11 The Council should update the guidance circulated at the year end to ensure that officers and members are clear that they should declare related party transactions even if the amounts involved are relatively small. Creditors and debtors with related parties should also be disclosed.</i>
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<i>R12 The Council should request that the valuer provide an estimate of the remaining useful economic life of all assets revalued.</i>

<i>R13 The Council should ensure that a full explanation is provided for any differences between carried forward and brought forward balances on reconciliations.</i>

Whole of Government Accounts

- 21 The Council is required to submit a return to Central Government to enable Council Accounts to be consolidated into the Whole of Government Accounts (WGA). We are required to confirm that the return is consistent with the accounts.
- 22 There were two significant inconsistencies between the Council accounts and the WGA return which the Council adjusted before the final return was submitted. The Council should have a process in place to ensure the return is consistent with the accounts before being presented for audit.

Recommendations

R14 The Council should have a process in place to ensure the WGA return is consistent with the accounts prior to submitting it to audit.

Conclusion

- 23 We would like to thank the Council for their assistance with the final accounts audit. Working papers provided were significantly improved on previous years and most audit queries were dealt with quickly.
- 24 For 2007/08 onwards the Council's external auditor will change to PKF (LLP) following their appointment by the Audit Commission. As part of the transitional arrangements for the change of appointed auditor we will share this report with PKF (LLP) to inform their audit planning for 2007/08.

Appendix 1 – Action Plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date	
6	R1 Issues already reported by Internal Audit:	2	Directors	Yes	- A training programme is in place to ensure all relevant staff are aware of the requirements of financial regulations. Reminders are also sent out periodically by e-mail.	In place	
	- during 2006/07 there were instances where orders were being authorised by the same person who signed the invoice, in contravention of the Financial Regulations. The Council should ensure that Financial Regulations are fully complied with in purchasing to ensure that segregation of duties is maintained.						
	- there were members of staff who had left the authority but were still being paid. The Authority should ensure that Payroll is notified promptly when a member of staff leaves and that changes are processed promptly. In addition managers should retain evidence that they are checking staff being charged to their budgets.	2	Directors	Yes	- Managers have been reminded of their responsibilities and a process is now in place for regular verification of the establishment list.	In place	
	- all journals should be signed, countersigned and be supported by an adequate narrative and supporting documentation where applicable.	3	Director of Finance and ICT	Yes		Immediate	
	- the payments bank reconciliation should be carried out on a regular basis.	2	Assistant Head of Finance	Yes	- Procedures are now in place to cover absences more effectively.	December 2007	

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
7	R2 The Council should resolve the issue of unpresented cheques dating back as far as 2002 that are still included in the bank reconciliation. This issue has been raised in previous years and has been noted by internal audit.	2	Assistant Head of Finance	Yes	A new policy is being written to deal more promptly with unpresented cheques.	December 2007
7	R3 The Council should put in place a formal procedure for the back up of major IT systems.	2	Director of Finance and ICT	Yes	A corporate back up policy has now been written and was issued in September 2007.	In Place
7	R4 The Council should ensure that staff levels in the IT department are adequate and that controls are not compromised by the current recruitment difficulties	2	Director of Finance and ICT	Yes	Considerable resources have been devoted to IT recruitment but this has not always produced positive outcomes. Where staffing difficulties persist compensating controls are pursued to protect system integrity.	January 2008
7	R5 The reconciliation of council tax refunds in Orbis to Cedar has not been carried out regularly due to a member of staff being on maternity leave. The Council should ensure that staff members are able to carry out each others duties in case of absence.	2	Director of Finance and ICT	Yes	Additional cover arrangements will be put in place. The position in Revenues is currently complicated by several staff being seconded to work on the system conversion and implementation.	December 2007
7	R6 The balance sheet value of the Council's Fixed Assets is in excess of £648,000,000. The Council should implement a more robust and secure fixed asset register that will enable the Council to implement the impending changes in capital accounting.	3	Director of Finance and ICT	Yes	- A number of potential systems have been evaluated but so far none of these have adequately matched the Council's requirements.	February 2008
7	R7 The Council should retain evidence of the sample checks carried out on NNDR refunds.	2	Assistant Head of Finance	Yes		December 2007

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
8	R8 Officers should ensure they seek HMRC advice on the VAT treatment applied to the sale of Wickfields.	3	Director of Finance and ICT	Yes	Contact has been made with HMRC and their response is awaited.	December 2007
8	R9 The Council should ensure that an electronic list of sundry debtor invoices and a list of sundry creditor invoices are included in the working papers provided for audit.	1	Assistant Head of Finance	Yes	A note will be carried forward to the 0708 working paper file.	June 2008
9	R10 The Council should ensure that the non-material errors highlighted by this year's audit and corrected are not repeated for the 2007/08 accounts as the identification and correction of errors takes additional officer and audit time.	1	Director of Finance and ICT	Yes	One of the items referred to only came to light after the draft accounts had been presented to members.	June 2008
10	R11 The Council should update the guidance circulated at the year end to ensure that officers and members are clear that they should declare related party transactions even if the amounts involved are relatively small. Creditors and debtors with related parties should also be disclosed.	2	Assistant Head on Finance	Yes		April 2008
10	R12 The Council should request that the valuer provide an estimate of the remaining useful economic life of all assets revalued.	2	Assistant Head of Finance	Yes		April 2008
10	R13 The Council should ensure that a full explanation is provided for any differences between carried forward and brought forward balances on reconciliations.	2	Assistant Head of Finance	Yes		April 2008

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
10	R14 The Council should have a process in place to ensure the WGA return is consistent with the accounts prior to submitting it to audit.	2	Director of Finance and ICT	Yes	A greater priority will be given to the WGA return for 2007/08.	