
Chief Executive's Office

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Date: 15 January 2006

Chief Executive: Donna Hall

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Dear Councillor

AUDIT COMMITTEE - THURSDAY, 18TH JANUARY 2007

I am now able to enclose, for consideration at the above meeting of the Audit Committee, the following reports that were unavailable when the agenda was printed.

Agenda No Item

4. **Financial Statements Memorandum (Pages 11 - 22)**

Report of the Audit Commission (enclosed).

Yours sincerely



Chief Executive

Encs

Distribution

1. Agenda and reports to all Members of the Audit Committee for attendance (Councillor John Wilson (Chair), Councillor Anthony Gee (Vice Chair) and Councillors Magda Cullens, Keith Iddon, Geoffrey Russell, Shaun Smith, Mrs Joyce Snape and Mary Wilson)
2. Agenda and reports to Donna Hall (Chief Executive), Gary Hall (Director of Finance), Garry Barclay (Audit and Risk Manager), Andy Armstrong (Assistant Audit Manager) and Dianne Scambler (Trainee Democratic Services Officer) for attendance.

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આ માહિતીનો અનુવાદ આપની પોતાની ભાષામાં કરી શકાય છે. આ સેવા સરળતાથી મેળવવા માટે કૃપા કરી, આ નંબર પર ફોન કરો: 01257 515822

ان معلومات کا ترجمہ آپکی اپنی زبان میں بھی کیا جاسکتا ہے۔ یہ خدمت استعمال کرنے کیلئے براہ مہربانی اس نمبر پر ٹیلیفون
کیجئے: 01257 515823

Financial Statements Memorandum

Chorley Borough Council

Audit 2005/2006

External audit is an essential element in the process of accountability for public money and makes an important contribution to the stewardship of public resources and the corporate governance of public services.

Audit in the public sector is underpinned by three fundamental principles.

- Auditors are appointed independently from the bodies being audited.
- The scope of auditors' work is extended to cover not only the audit of financial statements but also value for money and the conduct of public business.
- Auditors may report aspects of their work widely to the public and other key stakeholders.

The duties and powers of auditors appointed by the Audit Commission are set out in the Audit Commission Act 1998, the Local Government Act 1999 and the Commission's statutory Code of Audit Practice. Under the Code of Audit Practice, appointed auditors are also required to comply with the current professional standards issued by the independent Auditing Practices Board.

Appointed auditors act quite separately from the Commission and in meeting their statutory responsibilities are required to exercise their professional judgement independently of both the Commission and the audited body.

Status of our reports

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.

Copies of this report

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Purpose of the report

- 1 Our annual governance report, which was presented to the Audit Committee on 26 September 2006, summarises the significant findings, conclusions and recommendations arising from the audit for the year ended 31 March 2006. This report sets out the detailed findings arising from the audit on:
 - material information systems;
 - financial statements; and
 - other audit related issues.
- 2 The report does not cover adjusted misstatements in the financial statements as reported in the annual governance report.

Scope of the report

- 3 In undertaking our audit we comply with the statutory requirements of the Audit Commission Act 1998 and the Code of Audit Practice. Auditors' responsibilities are to review and report on, to the extent required by the relevant legislation and the requirements of the Code:
 - the Authority's financial statements; and
 - whether the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.
- 4 Our risk assessment and planned response to the key audit risks was summarised in our 2005/06 Audit and Inspection Plan.

Key messages

Financial statements

- 5 Our work on the financial statements is now complete. We issued an unqualified opinion on 26 September 2006. Appendix 1 outlines the agreed action plan arising from the annual governance report.

Material information systems

- 6 ISA (UK and Ireland) 315 requires auditors to establish and evaluate controls for all material information systems. We found that the majority of expected controls were in place and were operating effectively. Table 1 shows the information systems reviewed and any significant issues arising.

Table 1 Material information systems

System reconciliations are not signed by the preparer and there is no evidence of review.

Information system	Finding
General ledger	Journals are not independently reviewed or authorised. The quality of journal narrative and supporting documentation is mixed.
NNDR, housing benefits, housing rents, payroll and council tax	The reconciliation of the financial system to the general ledger is not signed by the preparer and there is no evidence of review.
Cash	The bank reconciliation is not signed by the preparer and there is no evidence of review.
Debtors and creditors	The financial system is not reconciled to the general ledger until the end of the financial year. The reconciliation is not signed by the preparer and there is no evidence of review.
Asset register	The asset register from which the financial statements are prepared is not formally reconciled to the register maintained by property services.

Audit Commission

Budgetary control

- 7 Budget monitoring is a key control to prevent and detect material misstatement for a number of material entries in the financial statements. Consequently, it is important that the Authority has a robust system of budgetary control. Whilst overall controls are adequate, budget monitoring continues to be driven by the Finance Unit, rather than budget holders.
- 8 Appendix 2 outlines the action plan containing our recommendations, together with the Authority's response.

Financial statements

- 9 We are required to give an opinion on whether the Authority's financial statements present fairly the financial position of the Authority as at 31 March 2006 and its income and expenditure for the year then ended. The quality of the Authority's financial statements was high with only a few non-material but several significant misstatements identified through the audit. Following adjustment for these misstatements, we issued an unqualified opinion on 26 September 2006. More detailed findings from the audit are provided in Table 2 below.

Quality assurance arrangements

- 10 Whilst the quality of the Authority's financial statements indicate that robust quality assurance arrangements are in place, the working paper requirements checklist provided was not fully complete. The financial statements submitted for audit on 29 June 2006 contained a £12.5m error as a result of the benefits grants being netted off against related expenditure. As an example, the analytical review procedures included in the checklist would have identified this material misstatement prior to submission for audit.
- 11 There was also a good level of compliance with the disclosure requirements of CIPFAs 2005 Statement of Recommended Practice for Local Authority Accounting (SORP), although several amendments were made. As a result of the significant changes to the 2006 SORP, we recommend that the Authority completes CIPFAs SORP disclosure checklist as included in the working papers requirements checklist to ensure continuing compliance with the disclosure requirements of the SORP and FRS18 on Accounting Policies.
- 12 The Authority presented an early set of accounts for audit as approved by the Accounts Committee on 29 June 2006. A CD of electronic working papers was also provided, which greatly facilitated the smoother running of the opinion audit. However, all working papers were not available at the start of the audit, and although most were provided on a timely basis, there were some significant delays. We would like to work with the Authority to agree a timetable for next year's audit to further facilitate:
- earlier closedown of the financial statements;
 - correct treatment of new technical accounting and local issues;
 - a reduced opinion audit period; and
 - an agreed protocol for dealing with audit queries.

Other financial statement issues

- 13 Table 2 summarises other issues arising from the audit of the financial statements.

Table 2 Financial statement issues

Financial statement issues not raised in the annual governance report are listed below.

Area	Issue
Related party transactions	<p>The Authority did not review the register of interests to identify material related party transactions.</p> <p>Section P15 of module 4 of CIPFAs SORP guidance notes outlines the practical steps required for identifying material related party transactions, including reliance on the statutory register of interests.</p>
Cash flow statement	<p>Whilst detailed working papers were prepared to support the entries in the cash flow statement, an audit trail reconciling the cash position to the accruals position in the general ledger would help to link the audit of the cash flow statement to work done in other elements of the audit.</p>
Bad debt provision	<p>Where it is not practical to assess the probability of collection of individual debts, past experience and current knowledge should be applied to estimate the proportion of debt that will not be recoverable. The bad debt provisions for Authority tax, NNDR and housing rent arrears and benefit overpayments are not calculated on this basis. As an example of this, benefit overpayment bad debts written off are treated as collected.</p>

Source: Audit Commission

Other audit issues

Information technology controls

- 14 We have assessed whether the Authority has effective general IT controls and application controls. We found that the majority of expected policies and procedures are in place. However, the following issues were identified.
- Change control procedures documentation needs to be improved due to the lack of formal mechanisms for most IT system or programme changes.
 - An Internal Audit IT controls review found IT policies are not always fully put into practice with Audit Commission identified risk areas being access control, network security and manual intervention controls.
- 15 The Authority has also introduced an information management programme to identify and inventorise information held and consider information retention. This should be translated into an information strategy.

VAT

- 16 The partial exemption calculation is not up to date. Since the Housing Revenue Account provided a significant proportion of the Authority's standard VAT rated services, it is important that the Authority updates this calculation following the decision to transfer the Authority's housing stock to Chorley Community Housing to ensure that the partial exemption can continue to be applied.

Whole of Government Accounts

- 17 The Authority's audited Whole of Government Accounts (WGA) consolidation pack was submitted to the DCLG free from audit amendment, but over two months past 6 October deadline. The Authority needs to review the integration of the financial statements with the WGA return.

Appendix 1 – Annual governance report action plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
6	R1 Carry out an objective analytical review of the financial statements prior to their submission for approval.	2	Finance	Yes	Agree	For 2006/07 accounts December 2006
9	R2 Ensure change control procedures documentation has a formal mechanism for all IT system or programme changes.	2	IT section/Finance	Yes	Agree	December 2006
7	R3 Review registers and payments to outside bodies to establish if a related party disclosure is required.	2	Finance	Yes	Agree	For 2006/07 accounts April 2007
6	R4 Ensure future electronic working papers are supported by prompt responses on audit queries.	2	Finance	Yes	Agree	April 2007

Appendix 2 – Financial statements memorandum action plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
	Material information systems					
5	R1 Introduce guidance on journal preparation and arrangements to independently review and authorise journals.	2	Michael Jackson	Yes	Guidance to be prepared as part of the 2006/07 Closedown.	March 2007
5	R2 Ensure that reconciliations of all financial systems to the general ledger, including the bank reconciliation are signed by preparer and that there is evidence of review. Reconcile the debtors and creditors systems to the general ledger on a monthly basis.	2	Lee Hurst	Yes	To be completed during 2006/07 Closedown.	March 2007
5	R3 Reconcile the asset register from which the financial statements are prepared to the register maintained by property services at least annually. Ensure that the reconciliations are signed by preparer and that there is evidence of review.	2	Lee Hurst	Yes	To be completed during 2006/07 Closedown.	June 2007
	Budgetary control					
5	R4 Further develop the financial management skills of budget holders.	2	Gary Hall	Yes	Review to be undertaken jointly by Audit commission and ourselves as part of the 2006/07 Audit Plan.	TBC
	Financial statements					
6	R5 Complete the working papers requirements checklist, including analytical review procedures and the CIPFAs SORP disclosure checklist.	3	Lee Hurst	Yes	To be completed as part of the 2006/07 Closedown.	June 2007

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
6	R6 Consider a protocol for dealing with financial statement related audit queries.	3	Lee Hurst	Yes	To be jointly agreed.	Prior to 2006/07 Audit of Accounts
7	R7 Review the calculation of bad debt provisions where there is no assessment of the probability of collection of individual debts.	1	Lee Hurst	Yes	To be completed during the 2006/07 Closedown.	June 2007
7	R8 Provide an audit trail reconciling the entries in the cash flow statement, to the accruals position in the general ledger.	2	Lee Hurst	Agreed	To be completed as part of the 2006/07 Closedown.	June 2007
	Other audit issues					
8	R9 Develop an information strategy.	2	Tim Murphy	Agreed	To be completed in 2007/08.	TBC
8	R10 Review and update the VAT partial exemption calculation.	3	Lee Hurst	Agreed	In progress as part of stock transfer work.	March 2007
8	R11 Review integration arrangements for preparing the WGA consolidation pack from the financial statements to ensure timely submission.	2	Lee Hurst	Agreed	In progress as part of systems upgrade and 2006/07 Closedown.	June 2007

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