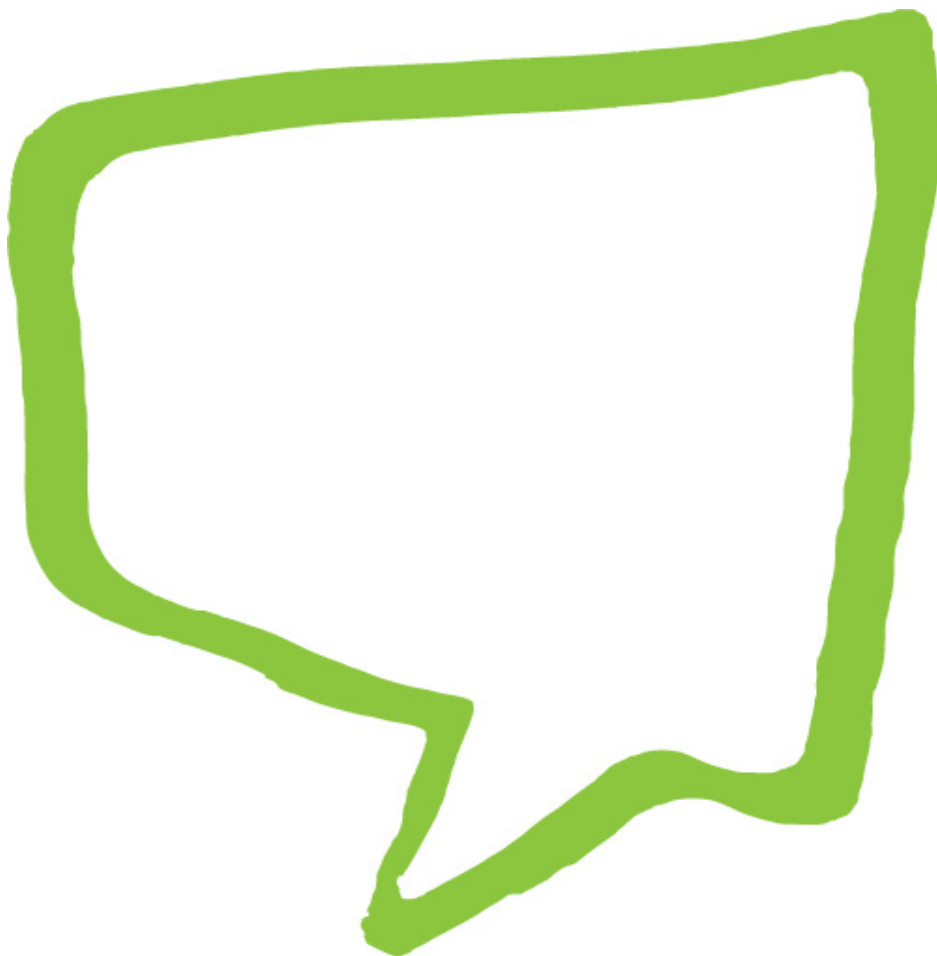


Interim Audit Report

Sedgefield Borough Council

Audit 2007/08

August 2008



Contents

Summary report	3
Appendix 1 – Action Plan	9

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.
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Summary report

Introduction

- 1 Our interim opinion audit involved a review of your material financial systems and the operation of key controls. This report summarises the results of our interim visit and the implication on our work at final accounts.
- 2 In performing this work, we work closely with Internal Audit and every three years we are required to review Internal Audit for compliance against the CIPFA Code for Internal Audit. This report also includes the findings of our triennial review of Internal Audit.

Background

- 3 The audit has been carried out to be ISA (International Standards on Auditing, United Kingdom and Ireland) compliant in accordance with the 2005 Code of Audit Practice. The ISA's were introduced by the Auditing Practices Board, applying to all accounting periods starting after 15 December 2004.
- 4 These ISA's place a greater emphasis on identifying information systems that lead to material balances in the financial statements, and evaluating and testing relevant key controls at the assertion level. In particular, ISA+315 requires us to demonstrate our understanding of the environment in which the Council operates and ISA+330 requires us to design procedures to mitigate risks. At the interim audit stage, these procedures are normally compliance tests in respect of key controls.

Audit approach

- 5 We have adopted a four stage approach to our interim audit:
 - stage 1: carry out a risk assessment of the general environment within which the Council's information systems operate;
 - stage 2: map the systems that provide material figures in the financial statements;
 - stage 3: document the processes and controls in place within each material system and undertake a walkthrough to ensure the system is operating as stated; and
 - stage 4: assess which are the key controls to ensure the integrity of the accounting entries and obtain evidence that they are operating as intended.

- 6 This work identifies the extent to which we can gain assurance from the controls the Council has put in place, and informed the testing strategy adopted for the final accounts audit, which started on 7 July 2008.
- 7 We carried out a detailed review of budgetary control and internal audit in order to assess the degree of assurance we could draw from the overall control environment. We then identified nine material financial systems and focused our work at stages 3 above on these areas:
 - general ledger;
 - payroll;
 - creditors;
 - benefits;
 - rents;
 - sundry debtors;
 - cash receipting;
 - council tax; and
 - NNDR.
- 8 Stage 4 was applied to the first 4 systems above this year in accordance with our cyclical plan.

Main conclusions

- 9 The Council has an effective control environment and strong budgetary control delivers considerable assurance that the accounts have not been materially misstated. The Council also has sound controls operating over the material financial systems that underpin the production of the 2007/08 financial statements. However, these controls could be better evidenced.
- 10 We confirmed that the Internal Audit Service provided at Sedgefield Borough Council, mostly complies with the requirements of CIPFA's Code of Practice for Internal Audit. However, again there were areas where compliance could have been better evidenced. We fed back our findings to the Audit and Resources Manager and Principal Auditor verbally earlier this year and remedial action was taken, which included improving the consistency of evidencing and recording internal audit work. Overall, IA are assessed as sufficiently compliant to ensure that the opinion given in their Annual Report is sound and IA can be relied upon where appropriate.

Detailed findings

Systems of Financial Management and Internal Control

- 11** Budgetary control is one of the Council's strengths. However, there is no audit trail to demonstrate that each budget holder reviews the monthly reports sent to them by Accountancy. The relevant portfolio accountant is in regular dialogue with budget holders in preparing reports to quarterly working groups, which discuss the issues arising in detail. Thus, it is unlikely that a failure to review budgetary control reports and investigate variances would fail to be detected. However, staff turnover and workload pressure in the run-up to LGR and LSVT increases this risk.
- 12** Although monthly bank reconciliations are properly performed by Accountancy there was no evidence that they had been independently reviewed. The reconciliations were not signed and dated either by the preparer or the reviewer.
- 13** Accountancy also perform various monthly or weekly reconciliations for all feeder systems to the general ledger to demonstrate that interfaces have transferred correctly, but again the reconciliations were not always clearly evidenced. In particular, we found:

 - some in-year reconciliations were recorded on tabulaions that were destroyed after a few weeks rather than retained to provide an audit trail;
 - rents, council tax and NNDR reconciliations were not always signed and dated by the compiler and reviewer; and
 - a control book summarising the interfaces made did not clearly indicate the balances transferred nor the officers responsible for the reconciliation.
- 14** The Council Tax Manager performs monthly reconciliations of schedules of alteration received from the Valuation Office but again these reconciliations are not evidenced.
- 15** The Accountancy Section does not have an authorised signatory list to check that departmental officers preparing journals and rechargeable works schedules are authorised to do so. Moreover, we found instances (eg journal 1306422 £750) where the department did not forward the rechargeable works form for over six months after the date the service was performed. This delay makes it harder to query the instructions and makes management information less up to date. However, as almost all significant journals (>£1,000) are prepared within Accountancy there is a low risk of this influencing decision making or leading to significant errors in financial reporting.

Internal Audit

- 16** The CIPFA Code on Internal Audit (2006) requires a risk based approach to be followed through which a system is first reviewed and controls documented, then key controls identified and finally compliance tests performed on those key controls. This approach is set out in the Audit Manual but there was insufficient evidence that this approach was followed in practice during 2007/08. The audit brief conveyed the misleading impression that the testing was pre-determined and not the result of an assessment of risk following the documentation of the system.
- 17** Internal Audit (IA) did not always perform compliance testing on key controls within the key financial systems. For example, a key control within benefits is the pre-notification check of claims performed by independent assessors on a sample basis. IA did not seek evidence that this control was being performed but instead went straight to checking the calculations themselves.
- 18** The presentation of IA working paper files could be improved. The files do not contain an index page and do not follow a consistent, logical sequence. Referencing is patchy and some key forms were left incomplete such as the audit work section of the job brief and the QM36 form or alternative list of key controls. One large file did not contain any dividers and many of the pages were unnumbered making it very difficult to follow. Consequently, two of the three files reviewed did not initially meet the CIPFA IA standard of being easy for an experienced, independent auditor to follow (standard 8.3.2). However, the third (payroll) was much better documented and the Audit and Resources Manager assured us that this was now the normal standard. The other two jobs had been started by staff that had left and new auditors had taken them over mid-audit.
- 19** The IA Manual needs updating in two respects:
- it includes a test summary form and says that it is mandatory for all testing but the form has not been used for several years and its contents are now covered on separate working papers; and
 - the new CIPFA IA standard introduced a requirement to document arrangements for respecting the confidentiality of data and the recent loss of child support data requested by the National Audit Office illustrates the risk of confidential data being handled carelessly and the need for robust procedures to mitigate the loss. However, the issue is not covered in Internal Audit's Audit Manual.
- 20** During 2007/08 IA had a procedure whereby no satisfaction survey was sent if there were no recommendations, but this made it difficult to confirm that surveys had been promptly issued when required and followed up when they were not returned. Moreover, there may be important feedback in areas where no recommendations are raised. The Audit and Resources Manager stated that satisfaction surveys are now requested electronically for all completed audits and this has improved the response rate in 2008/09.

Summary report

- 21** The 2007 Annual IA Report did not meet the LG standard on reporting in respect of:
- no explicit opinion on the control environment;
 - no PIs re satisfaction levels, acceptance of recommendations and timeliness of reporting;
 - no mention of the work being undertaken in accordance with the CIPFA Code for IA; and
 - no summary of QA procedures in place and results.
- 22** However, this appears to be a one-off as the 2008 Annual IA Report approved by the Audit Committee on 2 June 2008 does include these requirements. This report also includes a self-assessment of IA's compliance with the CIPFA Code of practice. Some additional areas of non-compliance or partial compliance are identified but overall IA assessed themselves as 90 per cent compliant and the Audit Committee and Section 151 Officer were satisfied that this was sufficient to make the opinion in the Annual Report reliable.

Recommendations

- | | |
|-----------|--|
| R1 | Develop a pro-forma for budget holders to complete and return to their portfolio accountant confirming that they have reviewed the budgetary control reports sent to them and noting any explanations for significant variances. |
| R2 | Ensure that bank reconciliations are signed and dated by both the compiler and an independent, senior reviewer. |
| R3 | Revise the control file of reconciliations between feeder systems and the ledger during the year to clarify which interfaces were checked, the responsible officers and what the balances on each system were. |
| R4 | Ensure that the Council Tax Manager signs and dates schedules of alteration received from the Valuation Officer to evidence the monthly reconciliation of property numbers to the council tax system. |
| R5 | Prepare an authorised signatory list to check the authorisation of journals and rechargeable works forms submitted by departments and instruct departments to ensure that they are submitted within one month. |
| R6 | Revise audit briefs to demonstrate compliance with the risk-based approach. The brief should require that each job starts with documentation of the system, followed by an evaluation of the system before the key controls to be tested are identified. |

Recommendations

- R7** Clarify in audit briefs that all key controls identified should be subject to compliance testing.
- R8** Agree at a team meeting a common file structure for IA working papers, which includes the testing headed by a QM36 form or equivalent list of key controls fully cross-referenced to the supporting tests.
- R9** Update the Internal Audit Manual to ensure that it reflects current practice and covers the confidentiality of data.

Appendix 1 – Action Plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Financial Management and Systems of Internal Control						
7	R1 Develop a pro-forma for budget holders to complete and return to their portfolio accountant confirming that they have reviewed the budgetary control reports sent to them and noting any explanations for significant variances.	3	Accountancy Services Manager	Not Agreed. Compensating Control agreed instead.	Democratic Services will be asked to expand minutes of quarterly strategic working groups to confirm that all budget holders received and reviewed their monthly budgetary control reports and also to explain significant variances and the action taken.	30 September 2008
7	R2 Ensure that bank reconciliations are signed and dated by both the compiler and an independent, senior reviewer.	3	Accountancy Services Manager	Agreed	Responsibility for bank reconciliations has now changed and this is being done.	31 August 2008
7	R3 Revise the control file of reconciliations between feeder systems and the ledger during the year to clarify which interfaces were checked, the responsible officers and what the balances on each system were.	2	Accountancy Services Manager	Agreed	Control book amended to reflect agreed changes of recording interfaces and reconciliations.	30 September 2008

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
7	R4 Ensure that the Council Tax Manager signs and dates schedules of alteration received from the Valuation Officer to evidence the monthly reconciliation of property numbers to the council tax system.	2	Revenue Services Manager	Agreed	The Total Page from the Schedules of Alteration and the supporting report from the council tax system will be printed down and the former signed to evidence the property numbers agree.	30 September 2008
7	R5 Prepare an authorised signatory list to check the authorisation of journals and rechargeable works forms submitted by departments and instruct departments to ensure that they are submitted within one month.	1	Accountancy Services Manager	Partially Agreed	Departmental journals are relatively rare and low value. In exceptional cases where they exceed £1,000 authority from a departmental head will be required to support the journal. Departments will be reminded to forward journals and recharge forms promptly.	30 September 2008
Internal Audit						
7	R6 Revise audit briefs to demonstrate compliance with the risk-based approach. The brief should require that each job starts with documentation of the system, followed by an evaluation of the system before the key controls to be tested are identified.	3	Audit and Resources Manager	Agreed	An extract from the Audit Manual describing the risk-based approach is now included in all audit briefs.	31 August 2008
8	R7 Clarify in audit briefs that all key controls identified should be subject to compliance testing.	3	Audit and Resources Manager	Agreed	IA always ensure that they are not part of the controls in the system they are auditing but recognise that at times substantive tests have been used when compliance testing was feasible.	31 August 2009

Summary report

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
8	R8 Agree at a team meeting a common file structure for IA working papers, which includes the testing headed by a QM36 form or equivalent list of key controls fully cross-referenced to the supporting tests.	2	Audit and Resources Manager	Agreed	The team will agree a consistent order for each file. Sections for documenting the system, assessing the key controls, testing the key controls and reporting will be clearly separated and indexed. The approach to page numbering will also be reviewed to improve cross-referencing.	30 September 2008
8	R9 Update the Internal Audit Manual to ensure that it reflects current practice and covers the confidentiality of data.	1	Audit and Resources Manager	Agreed	The vast majority of the Audit Manual is up to date and as a district council SBC handles lower volumes of sensitive data than single-tier authorities.	30 September 2008

The Audit Commission

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