

Audit Summary Report

January 2006



Final Accounts Memorandum

Salford City Council

Audit 2004-2005

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; and
- 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 and 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.

Status of our reports to the Council

Our reports are prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. Reports are prepared by appointed auditors and addressed to members or officers. They are prepared for the sole use of the audited body, and no responsibility is taken by auditors to any member or officer in their individual capacity, or to any third party.

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Introduction

- 1 The Audit Commission Act 1998 and the Code of Audit Practice require the external auditors to give an opinion as to whether the statement of accounts presents fairly the financial position of the Council and its income and expenditure for the year in question. In accordance with this requirement we gave an unqualified opinion on the 2004/05 accounts on 26 October 2005.
- 2 This report summarises the issues which arose from our audit of the financial statements.

Background

- 3 Members approved the Council's annual accounts on 14 July 2005 which is well within the deadline of 31 July 2005 required by the Whole of Government Accounts initiative. The Council is commended for its early closure.
- 4 Timeliness in producing the accounts will continue to be important as the deadline for completing the accounts is again being brought forward. In 2006, the accounts will need to be approved by members by the end of June 2006 and audited by the end of September 2006. We are aware that a closure programme has been produced which plans to fulfil these requirements.
- 5 Our review confirmed that the financial statements generally comply with good practice and that there is a good understanding of current technical accounting issues. Responses to queries and matters arising were dealt with expeditiously and working papers continue to be of a good standard and steps are being taken to improve these still further.
- 6 Financial reporting is one of the five elements that auditors have assessed as part of the new Comprehensive Performance Assessment which was introduced during 2005. Salford's financial reporting has been assessed as 'consistently above minimum requirements - performing well' (score 3).

Main issues arising

Adjusted misstatements

- 7 We are required by professional standards to report to 'those charged with governance' certain matters before we give an opinion on the accounts. In accordance with this requirement we reported the matters arising from our audit to the Accounts Committee on 24 October 2005.
- 8 The Strategic Director of Customer and Support Services issued a report in response to these issues and the Accounts Committee agreed with his recommendation to make several amendments to the accounts. These amendments did not impact on the reported balances in the Council's general fund reserve or the Housing Revenue Account.

Treasury management

- 9 Last year, we drew attention to an issue which is of national relevance and applies to other authorities as well as Salford, concerning the accounting treatment of LOBO interest and amortisation of premiums on debt rescheduling.
- 10 The Strategic Director of Customer and Support Services has presented a report to the Cabinet which explains the background to these issues and quantifies the financial effects and risks relating to the alternative accounting treatment that are currently being recommended. As indicated in the report, if the Audit Commission's favoured method of accounting treatment was used this would have resulted in an additional charge to the general fund of about £1.75 million in 2004/05. This is made up of the following:
 - £0.75 million additional interest on LOBO loans; and
 - approximately £1 million additional amortisation of premium.
- 11 In determining our opinion on the accounts, we adopt a concept of materiality and an unqualified opinion may not be given if there are material misstatements in the accounts. Our materiality levels for the general fund are currently set at £3.2 million (based on guidance from the Audit Commission). We are therefore satisfied that although there are differences of opinion in the favoured accounting treatment for LOBO interest and amortisation of premiums on debt rescheduling the Council's preferred method is within our materiality guidelines.
- 12 Looking ahead, it is not clear when the uncertainties relating to this issue will be resolved and we will keep this matter under review at our regular liaison meetings with the Strategic Director of Customer and Support Services.

Financial standing

- 13 We concluded from our review that the Council's overall financial position continues to be sound. The Council budgeted to contribute nearly £0.5 million from its general fund reserve to its spending in 2004/05. The outturn at 31 March 2005 showed a net underspend of £0.9 million for the year which arose due to a number of variances, including debt rescheduling savings and dividend income in excess of budget.
- 14 The £0.9 million underspend resulted in the general fund reserve increasing from £7 million at 31 March 2004 to £7.9 million at 31 March 2005. This level of balances is slightly higher than the minimum identified by the Council as part of its financial risk assessment.

Capital finance

- 15 Following changes in the capital finance and accounting regulations an adjustment (Adjustment A') was included in the formula for calculating the minimum revenue provision so that local authorities did not set aside less than that which they would have done under the previous capital finance controls.

- 16 The Council needs to be able to demonstrate that the component parts of Adjustment A explain the difference between the closing credit ceiling under the old capital finance regime as at 31 March 2004 and the opening capital financing requirement under the new capital finance regime as at 1 April 2004. The reconciliation is complex because it can entail understanding transactions which go back over several years and there can be valid reasons for differences arising. Initial attempts at completing this exercise have identified a difference of around £3 million (less than 1 per cent of the capital financing requirement) which needs to be further examined and explained.

Statement on internal control

- 17 The Accounts and Audit Regulations now require authorities to carry out an annual review of internal control arrangements together with the provision of a signed assurance statement in the published accounts. The Council fulfilled these requirements for 2004/05 and an appropriate Statement on Internal Control was included with its financial statements.
- 18 A matter which the Council could usefully further consider is the level of review which is given to the Statement on Internal Control by members. We recommend that an appropriate member group is given responsibility to scrutinise the arrangements for carrying out the annual review of internal control and to review the content of the Statement prior to it being approved as part of the financial statements by the Accounts Committee.

Pooled budgets

- 19 The Council and Salford Primary Care Trust have established partnership arrangements for several services, in accordance with section 31 of the Health Act 1999. Under such agreements the partners are required to follow certain requirements relating to the financial activities of the pooled budget and ensure that these accounts are incorporated as an additional disclosure note in each of the partners' statutory financial statements.
- 20 Last year, following our audit of the 'People with Learning Difficulties' pooled budget, we reported that:
- we had not been provided with evidence that the partnership agreement had been signed by both parties; and
 - that our review of the agreement which we were provided with concluded that it needed to be improved to ensure that all of the areas specified in the relevant Statutory Instrument had been met.

- 21 Following this year's audit we are pleased to report that these issues have been satisfactorily resolved. In 2004/05 two further pooled budgets have been established relating to the 'Integrated Equipment Services Pool' and the 'Adult National Treatment Allocation Drugs Pool'. Our audit of the Integrated Equipment Services Pool identified that:
- the arrangements for performance monitoring and financial management by the Partnership Board need to be strengthened; and
 - the partnership agreement needs to be improved to ensure all the areas specified in the relevant statutory instrument are met.
- 22 We will agree appropriate action with key officers to remedy these matters. There were no significant issues arising from the audit of the Drugs Pool.

Reserves, provisions, etc

- 23 The descriptions and purpose of some of the reserves and provisions need to be reviewed to ensure that these are being properly described in line with the Statement of Recommended Practice (SORP). There are also some balances included as receipts in advance (for example, development grants) which need to be reviewed to ensure that they are appropriately described.

Way forward

- 24 The action plan attached has been agreed for tackling the issues referred to above, together with some of the less significant matters arising from the audit.
- 25 Various matters also arose during the audit which we would like to consider and discuss further as part of our preparing the audit plan for 2006/07. These include the following:
- school deficit balances;
 - housing rent arrears; and
 - DSO trading position.

Appendix 1 – Action plan

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Treasury management					
R1 Take appropriate action when clarification is received on the outstanding issues relating to: <ul style="list-style-type: none"> • interest on LOBO loans; and • amortisation of premium on restructured loans. 	3	John Spink/ Chris Hesketh	Yes	Action to be taken if necessary when clear guidance is received.	Subject to further guidance.
Capital finance					
R2 The Council needs to be able to demonstrate that the component parts of Adjustment A explain the difference between the closing credit ceiling under the old capital finance regime as at 31 March 2004 and the opening capital financing requirement under the new capital finance regime as at 1 April 2004.	3	Chris Hesketh/ Tony Thompstone	Yes	The capital finance requirement is currently being reconciled to the credit ceiling calculation of the previous control regime.	25 February 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Statement on Internal Control					
R3 An appropriate member group should be responsible for scrutinising the arrangements for conducting the annual review of internal control and reviewing the content of the Statement on Internal Control, prior to it being approved as part of the financial statements by the Accounts Committee.	3	Alan Eastwood	Yes	These responsibilities were added to the Terms of Reference of the existing Audit Sub-Committee in September. However, a new full Audit Committee is being proposed which will take over responsibility for all corporate governance issues, such as the internal control environment and reviewing the content of the SIC.	28 February 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Pooled budgets					
R4 With regard to the Integrated Equipment Services Pool: <ul style="list-style-type: none"> • arrangements for performance monitoring and financial management by the Partnership Board should be strengthened; and • the partnership agreement needs to be improved to ensure all the areas specified in the relevant Statutory Instrument are met. 	3	Keith Darragh/ Andrew Tonge	Yes	(Bullet one) Both performance monitoring and financial management have now been strengthened. Performance reports are now a standing item on the Independent Living Board monthly meeting agenda. In June 2005, the Board received a report explaining the composition of the budget and outturn for 2004/05. In October 2005, the Board received a 2005/06 budgetary control report; future reports are planned quarterly. (Bullet two) Accountants and the Head of the IES Pool are to meet to update and amend the section 31 agreement. (General) Accountants are to meet with the auditor to discuss these and any further issues arising from the audit.	31 January 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Reserves, provisions, etc					
R5 The descriptions and purpose of some of the reserves and provisions need to be reviewed to ensure that these are being properly described in line with the Statement of Recommended Practice (SORP).	3	Chris Hesketh	Yes	The Corporate Accountancy Team will undertake a review of reserves, provisions and creditor items in preparation for the 2005/06 Statement of Accounts. Any findings will be considered in the Accountancy Development Group.	25 February 2006
R6 There are some balances included as receipts in advance (for example, development grants) which need to be reviewed to ensure that they are appropriately described.	3	Chris Hesketh	Yes	The Corporate Accountancy Team will undertake a review of reserves, provisions and creditor items in preparation for the 2005/06 Statement of Accounts. Any findings will be considered in the Accountancy Development Group.	25 February 2006
R7 The need for maintaining the Airport Loan Provision (£176,000) should be reviewed.	2	Chris Hesketh/ John Bilsborough	Yes	It had been intended that this provision be written off in 2004/05, however a doubt emerged that this was the correct treatment. The item will be reviewed in preparation for the 2005/06 Statement of Accounts.	25 February 2006

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Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
R8 The split between the reserve and the provision elements of the insurance fund need to be fully backed up by appropriate working papers.	2	Chris Hesketh/ Dave Noon	Yes	The format will be revised to make the distinction clear in the 2005/06 working papers.	30 June 2006
R9 The accounting treatment relating to the PFI capital reserve should be reviewed against further guidance which is anticipated will be forthcoming in the near future.	2	Phil Prady/ Chris Mee	Yes	Action to be taken if necessary when clear guidance is received.	Subject to further guidance.

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Accounting policies					
R10 The Council need to demonstrate that the exceptions to the SORP relating to the method of valuing some stock and non-accrual of energy bills are not material, as described.	2	Colin Gettins Chris Hesketh/ Colin Kay	Yes	Cityclean DSO salt stocks are now purchased as required and a zero balance is held. Highway Services DSO stocks are now held by UVPLtd. Social Services stocks are now valued in a new system in accordance with the SORP. Catering DSOs carry a value less than £100,000, so any difference from SSAP9 stock valuation is minimal. The non-accrual of energy bills will be reviewed in preparation for the 2005/06 Statement of Accounts.	No further action required. 25 February 2006
Fixed assets					
R11 Fixed assets should be reviewed to check if there are any intangible assets (for example, SAP software) which should be separately disclosed.	2	Phil Prady	Yes	The item will be reviewed in preparation for the 2005/06 Statement of Accounts.	30 June 2006

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Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Prudential indicators					
R12 Regular reporting to members on prudential indicators should be undertaken.	2	John Bilsborough/ Colin Kay	Yes	Key prudential indicators are currently included in weekly treasury management reports, the distribution of which includes the lead member. This reporting is to be widened by including key information in the monthly budgetary control reports to Budget and Audit Scrutiny Committee.	15 February 2006
Debtors/creditors					
R13 The analysis of debtors and creditors in the notes to the consolidated balance sheet needs to be carefully prepared to ensure that these are being reported as described.	2	Chris Hesketh/ Colin Kay	Yes	The analysis depends largely on the strength of working papers submitted by the various accountancy teams. The content and style of these working papers has been discussed in Accountancy Development Group meetings and Accountancy Briefing sessions. The Corporate Accountancy Team will review the working papers' analyses during the consolidation process.	30 June 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Creditors					
R14 The outstanding balance on the GR/IR account of £700,000 needs to be further investigated and cleared prior to the closure of the 2005/06 accounts.	2	Chris Hesketh/ Tony Brogan	Yes	All items in the GI/IR account will be cleared by reversal or transfer into a suitable creditor, provision or reserve account.	27 January 2006
Housing Revenue Account (HRA)					
R15 The accounting treatment of 'non-tenant' arrears within the HRA should be reviewed.	2	Nigel Dickens/ Joanne Hardman	Yes	The development of reports from the SAFFRON system has enabled greater analysis of arrears currently identified within the HRA. In preparation for the closure of the 2005/06 accounts, the Housing Accountancy Team will review treatment of arrears to ensure correct accounting procedures are in place.	25 February 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Working papers					
R16 Implement further improvements to the standard of working papers, including: <ul style="list-style-type: none"> • improving the audit trail from balances in the consolidated balance sheet to lead schedules in working papers; • improving comparative analysis of balances between years; and • improving explanations of significant variances between years and against estimates. 	2	Chris Hesketh/ Colin Kay	Yes	The content and style of working papers has been discussed in Accountancy Development Group meetings and Accountancy Briefing sessions. Revised standard forms will be devised and the advice given will be reinforced through the final accounts process. The Corporate Accountancy Team will also conduct sample checks of working papers during the consolidation process to ensure that they meet the requirements of this recommendation.	30 June 2006

Recommendations	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
Journals					
R17 The analysis of risks relating to journals needs to be demonstrated and further action taken, if appropriate. (See management response on this issue in last year's final accounts memorandum.)	2	Chris Hesketh/ John Bilsborough/ Mike Lyons	Yes	Reliance is placed on budget monitoring, cash reconciliation, and their supporting system to mitigate the risks. The ADG have considered this item and the general view is that the residual risk is minimal. The accountants identified will undertake a further analysis to identify any additional precautionary measures required; this is anticipated to focus on treasury management and journals moving sums into SAP from non-SAP systems.	25 January 2006