

Interim Report and Key Tasks Remaining

Salford City Council

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Introduction

It is the Council's responsibility to put in place 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. Our responsibilities and audit approach to this work are summarised in Appendix 1. Our approach is designed to focus on key risk areas identified as part of our audit planning process. Our work is integrated with that of Internal Audit with a view to avoiding duplication of effort and placing reliance on it, wherever possible.

It is against this background that this report summarises, for the consideration of the Budget and Audit Scrutiny, Audit sub-committee, the following:

- the main matters arising from our interim audit work, as part of undertaking our agreed audit and inspection plan for 2004/05, and
- an update on the key tasks that need to be completed by January 2006. This will bring the 2004/05 plan to conclusion and includes aspects of the 2005/06 plan which the Audit sub-committee received a copy of at its last meeting.

The issues and matters arising referred to in this report are monitored on an ongoing basis at our regular liaison meetings with the Strategic Director of Customer and Support Services and other senior officers in his directorate. We also have regular meetings with the Chief Executive.

Interim Report

Audit opinion on the financial statements

The Code of Audit Practice, approved by Parliament in March 2000, requires the external auditor to give, amongst other things, an independent assessment of whether the statement of accounts present fairly the financial position of the Council. We have, therefore, examined the processes which we consider are core to the production of the financial statements, namely

- the main accounting system
- the budgetary control system
- the accounts closedown procedures at the year end,

and established the extent to which we can rely on them in giving our opinion on those statements. Our overall conclusions from this work are that:

- we should be able to rely upon the main accounting and budgetary control systems to support the production of materially accurate figures for the accounts. This is subject to the completion of some further work at the final accounts audit to ensure that the results reported in the statement of accounts are in line with those reported through the budgetary control system and also further testing relating to reconciliations of the Council's various systems
- we are satisfied that the closedown plan produced for the 2004/05 accounts provided a sound basis for the preparation of this year's financial statements. The Council's accounts were approved by the Accounts Committee on 14 July 2005. This is within the timetable for meeting the requirements of the whole of government accounts which had a prescribed deadline of 31 July for 2004/05.

As reported last year the Audit Commission identifies risk areas relating to the closure of the accounts that auditors need to be alert to in completing their review of the financial statements. To help mitigate the potential impact that these risks might have we have again shared this information with senior finance staff from the Council at a joint presentation to auditors / accountants from the Greater Manchester area during April 2005.

It is important that the Council maintains its momentum for early closure because the deadline is being brought forward again to 30 June next year. We are aware that the Council is taking steps to ensure that it achieves this deadline. We will be pleased to discuss any proposals that the Council is considering on this matter.

Financial aspects of corporate governance

We have also carried out work towards the Code of Audit Practice objective relating to the financial aspects of corporate governance, which requires us to check the Council's arrangements for:

- ensuring that *financial standing* is soundly based
- ensuring that *systems of internal control* are adequate and effective
- ensuring proper standards of *financial conduct and preventing and detecting fraud and corruption*
- securing the *legality of transactions that have significant financial consequences*.

Based on the results of our interim work to date we are of the view that:

- the Council has continued to strengthen its *financial standing* in line with its medium term financial strategy and its risk assessment for requirement of reserves
- work on *systems of internal financial control* is being undertaken in line with what is set out in the Council's Statement on Internal Control and the actions which have been identified to make further improvements
- a responsible attitude continues to be displayed towards *financial conduct and prevention and detection of fraud and corruption*
- arrangements for identifying potential legal issues and the *legality of transactions that have significant financial consequences* remain satisfactory.

The current position on some of the more significant issues which we have reviewed is reported below.

Treasury management

Last year we reported that there are differences of professional opinion on the correct accounting treatment relating to the Council's LOBO (lender offer, borrower option) market loans. The Strategic Director of Customer and Support Services referred to these uncertainties in his report to the Accounts Committee on 14 July 2005 when the Committee approved the 2004/05 statement of accounts.

Whilst these uncertainties remain there is a risk that the Council's accounts are incorrectly stated and that additional charges could fall on its General Fund revenue account. We are currently quantifying the potential impact that this could have based on the latest advice which we have received from the Audit Commission. We will also need to carefully consider the impact that this may have on our opinion on the accounts. We will maintain our regular liaison with the Strategic Director of Customer and Support Services and we will update the Accounts Committee on the outcome when we report the results of our audit in late October 2005.

Partnership working

The Council currently delivers a wide range of services which often involve working in partnership with others, many of which involve considerable levels of funding. These practices are commended because of the potential for service improvement. However they need to be carefully managed due to the inherent legal and financial risks that can arise from such arrangements. It is against this background that we have been jointly reviewing the Council's partnership management arrangements with the Deputy Director of Customer and Support Services.

Our review found that the Council has embraced partnership working as a way of improving services and has acknowledged the risks which are inherent in such operations. Steps are being taken to improve the governance arrangements relating to partnership working. On the basis of our joint review to date it has been agreed that further action is needed on the following key issues:

- completing the compilation of a database of all partnerships that the Council is involved with
- drawing up a set of procedures / protocols to govern the process of establishing partnerships and the roles of partner bodies
- reviewing arrangements for routinely reporting back to the Council on partnership achievements and meeting objectives
- developing a competency framework for members and officers involved with partnerships and aligning this with an appropriate training programme, and
- embedding risk management arrangements at all levels of partnership activity.

Taking action on the areas identified above should considerably strengthen the Council's corporate governance arrangements relating to partnership working. For our part we will continue to monitor and review the Council's progress on these matters. It is important that the Council makes effective use of the partnerships database when it is completed. Sharing the information within the Council should help to strengthen its risk management arrangements. The data can also be used, for example, to help inform the statutory disclosures that the Authority makes in its financial statements and assist Internal Audit to prioritise its risk-based plans.

Looking ahead, the Council could also usefully develop a self regulatory framework whereby lead members / officers carry out a self-assessment of the risks faced by each of the partnerships with which they are involved. We will further discuss the potential for introducing such a framework with the Deputy Director of Customer and Support Services and the value this could add.

Review of Internal Audit

We are required as external auditors to utilise and rely on Internal Audit's work as far as possible. To this end we undertake an annual assessment of Internal Audit to determine the effect on our role and ensure that we co-ordinate the work we do for the Council. Periodically, our annual assessment is supported by a more detailed review of Internal Audit's work to ensure compliance with professional standards. We have recently completed such a review.

Our overall conclusion is that Internal Audit is meeting the CIPFA standards. A key strength identified is that Internal Audit is playing an increasingly significant role in the development of the Council's overall control environment and risk management arrangements. We summarised our assessment against each of the standards in our detailed report, a copy of which will be included on the Audit sub-committee's agenda for its meeting on 12 September.

Our conclusion drew significantly on the results from a clients' survey which were very encouraging. Positive comments were generally made with regard to all the operational issues, including the following:

- Professionalism and independence
- Reports, being evidence based and timely
- Recommendations, being clear and generally followed up
- Audit work is worthwhile and adds value.

We have agreed that Internal Audit could usefully feedback the summary of these results to clients with a view to identifying if there are any further opportunities for making improvements in its service. This could be done by exploring the relatively few negative comments that some respondents have made.

We have suggested a few areas where we feel Internal Audit could continue to strengthen its arrangements and appropriate action has been agreed with the Internal Audit Manager.

Internal Statement on Control

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. CIPFA has recognised that the review and statement included with the 2003/04 accounts was transitional towards a complete methodology which needed to be fully in place for the 2004/05 accounts.

In last year's Annual Letter we noted that the Council had recognised that much still needed to be done to fully comply with the requirements envisaged for 2004/05 and that a Management Group had been set up to take this forward. We have continued to monitor progress at our regular liaison meetings with the Strategic Director of Customer and Support Services and other key senior officers in his directorate. The Council's signed assurance statement for 2004/05 has been completed and included as required in its accounts, which are currently subject to audit.

The procedures and processes which are in place for producing the Internal Statement on Control are now an integral part of the Council's overall governance arrangements. We understand that the Audit sub-committee will receive a separate report on this topic at its September meeting and we will be pleased to further discuss this then.

Pooled budgets

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.

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.

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.

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.

Housing market renewal

Salford has been successful in securing, jointly with Manchester City Council, some £125m from the Housing Market Renewal fund for the initial three year period 2003/04 to 2005/06. This is a partnership arrangement in which Salford's share is about one-third and Manchester City Council is the designated accountable body. We have undertaken a review to ensure that the Council is accounting for its share of the spending correctly and, through limited testing at this stage, that the partnership's governance arrangements are sound. Based on our review to date we are of the view that:

- with regard to the accounting arrangements, we concluded that the partnership is considered to be a 'joint arrangement, non-entity' and that Salford should therefore account directly for its part of the assets, liabilities, income, expenditure and cash flows held within or arising from the arrangement, and
- with regard to the governance arrangements, the partnership is taking appropriate steps to strengthen its systems and protocols and thereby mitigate the inherent risks relating to this scheme.

Further work is planned as part of our final accounts programme and we will continue to liaise with Internal Audit who plan to carry out work in this area shortly and thereby avoid duplication of effort.

Capitalisation of expenditure

An issue on which we have previously raised concerns is the capitalisation of 'grey' areas of expenditure where there is some discretion as to whether this is classed as capital or revenue. The Council has continued with this practice in 2004/05 and has included £2.7m of expenditure which has been transferred from revenue to capital to help ease pressure on the revenue budget. We are satisfied that this is in line with Council's medium term financial strategy and understand that 2005/06 (budgeted at £2m) is the final year that the Council plans to rely on this arrangement. It remains essential to the Council's overall financial stability that this strategy is successfully implemented.

Last year, we noted that the Council has not yet determined a 'de minimis' level for capital expenditure. The Code of Practice on Local Authority Accounting states that "authorities are expected to have a firm de minimis policy but this may involve different levels for different asset types and for the different purposes for which information is required". We understand that steps are being taken to action this by making an appropriate amendment to the Council's financial regulations.

National fraud initiative

The National Fraud Initiative (NFI) is the Audit Commission's data matching exercise which brings together data from local authorities, NHS bodies, government departments and other agencies to detect a wide range of frauds against the public sector. The NFI is carried out every two years.

The Commission's exercise this year has again collected data on payroll, pensions, housing benefits, student loans and housing rents. In addition, the Commission have been piloting a number of other initiatives which are focused on risk areas highlighted by authorities and include payments made to privately run care homes, abuse of blue badge parking permits and duplicate payments to suppliers.

The Council is committed to playing its part in this initiative and is currently actively investigating its data matches. We feel that this is an area which the Audit sub-committee could usefully receive further information and we understand that the Strategic Director of Customer and Support Services plans to do this at a future meeting.

Grant claim control

Staff in Customer and Support Services actively monitor that the Council's grant claims, (which are submitted to government departments), are being sent on time and are being forwarded for audit certification. Steps have also been taken over the past couple of years to strengthen the quality of working papers and to this end we have maintained a regular liaison with key staff to provide feedback on where we feel improvements can be made. Taking appropriate action can help to reduce the number of claims on which problems arise.

It is against this background that we are pleased to report that all the outstanding claims for 2002/03 have now been cleared and it is indicative of the actions that the Council is taking to improve its arrangements that there are no remaining claims outstanding for 2003/04 for which it is responsible. The Audit Commission monitors 'stragglers' on a regular basis and as at the end of July 2005 there were nearly 200 claims outstanding at English authorities. It is therefore commendable that Salford is reported as 'nil'.

Key tasks remaining

The Table below summarises the key pieces of work and deadlines which are planned up to January 2006. This will bring to a conclusion the work which was set out in our audit and inspection plan for 2004/05 and includes some aspects that are included in our agreed plan for 2005/06.

SUMMARY OF WORK REMAINING AND KEY DATES TO JANUARY 2006	
Work planned	Key dates / deadlines
Final accounts	
• Audit fieldwork	July to October 2005
• Auditor's report to members (SAS610)	Late October 2005
• Audit opinion	By 30 October 2005
Use of resources assessments*	
• Audit fieldwork	August to September 2005
• Audit Commission quality assurance and moderation	October 2005
• Notification of scores to the Council	November 2005
Best value performance plan (BVPP) / performance indicator (PI) audit	
• Auditor's return to the Audit Commission on mandatory PI work	5 September 2005
• Auditor's report on the BVPP	By 31 December 2005
Direction of travel statement*	
Comprehensive performance assessment* - update	Mid December 2005
Annual audit and inspection letter	By 31 January 2006
Corporate assessment (CA)	
• Self assessment	21 November 2005
• CA review	January – March 2006

* Further information on these is provided below.

Comprehensive performance assessment (CPA)

At previous meetings we have kept the Audit sub-committee advised of the changes which the Audit Commission is making to the CPA framework for 2005. The new CPA is a harder

test and a council will have to attain a higher standard to achieve a particular category or rating, such as 'good' or 'excellent'. This is essential if CPA is to continue to galvanise councils into raising the quality of their work. In summary, the overall CPA framework for single tier and county councils will comprise:

- annual use of resources assessments by the Commission, based on work by appointed auditors, (this is further explained below)
- annual service assessments by the Commission or provided to the Commission by Ofsted, the Commission for Social Care Inspection and the Benefits Fraud Inspectorate
- periodic corporate assessments by the Commission, which in Salford's case is scheduled for the first quarter of 2006, and
- direction of travel statements, with straightforward labels, reported by the Commission, (this is further explained below).

Use of resources assessment

The use of resources assessment evaluates how well the Council manages and uses its financial resources. It is a more stringent test of performance than the auditor scored judgements that have formed part of the CPA framework up until 2004. It focuses on the importance of having sound and strategic financial management to ensure that resources are available to support the Council's priorities and improve services. It has five themes covering:

- Financial reporting
- Financial management
- Financial standing
- Internal control, and
- Value for money.

For single tier councils, the use of resources assessment will carry more weight in determining the overall CPA category as it is designated as a 'level 1' element. For example, a use of resources score of 2 or less will prevent a council being 'excellent'. In addition, the scope of the assessment has been widened and the standards of performance required have been raised. Previously, 'adequate arrangements' were sufficient to score 3, but under the new approach meeting 'adequate performance' will score 2.

The Audit Commission will determine the overall use of resources score by combining the auditor's separate scores for each of the themes covered, using a set of rules. The score will be on the following scale:

- 1 = below minimum requirements – inadequate performance
- 2 = only at minimum requirements – adequate performance
- 3 = consistently above minimum requirements – performing well
- 4 = well above minimum requirements – performing strongly.

Each judgement area consists of a number of key lines of enquiry and areas of audit focus and evidence. There are also descriptions of performance against each key line of enquiry showing performance levels 2, 3 and 4.

As indicated in the Table above we are currently undertaking our fieldwork on these assessments, which is due to be completed by the end of September 2005, and following the Audit Commission's consistency checks during October 2005 we will notify the Council of its scores in November 2005.

Direction of travel statement

Direction of travel statements will be published when CPA categories are updated and will have clear labels to indicate the progress being made in achieving improvement. These labels will be:

- Significant improvement
- Some improvement
- No improvement, or
- Weakening.

The next direction of travel statement for Salford is planned for December 2005. However the Commission is still considering whether these will be issued where an authority is scheduled for a corporate assessment in the following quarter, as is the case at Salford. We will update the Audit sub-committee at its meeting if this matter is clarified in the meantime.

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 non-Executive Directors/Members or officers. They are prepared for the sole use of the audited body, and no responsibility is taken by auditors to any Director/Member or officer in their individual capacity, or to any third party.

Audit Approach

Opinion audit

Responsibilities

Auditors are required to audit the financial statements and to give an opinion, including:

- whether they present fairly the financial position of the audited body and its expenditure and income for the year in question
- whether they have been prepared properly in accordance with relevant legislation and applicable accounting standards.

Audit approach

Opinion audit (Statement of accounts)	<p>Assess the strength and reliability of the control environment by undertaking a review of the processes we consider core to the production of the financial statements:</p> <ul style="list-style-type: none"> • the main accounting system • the budgetary control process • closedown procedures. <p>Identify the elements that can only be tested as part of the full review of the financial statements at the final accounts audit.</p>
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Financial aspects of corporate governance

Responsibilities

Auditors have a responsibility to review and, where appropriate, report on the financial aspects of the audited body's corporate governance arrangements.

Audit approach

Internal financial controls	<p>An assessment of the arrangements put in place by the Council to satisfy itself that its systems of internal financial control are both adequate and effective in practice. This includes reviewing:</p> <ul style="list-style-type: none"> • standing orders and standing financial instructions • internal audit • IT strategy and control procedures • procedures in place to control business-critical systems and the collection of major sources of income • tax-related management arrangements • risk management arrangements. <p>Detailed work in risk areas not already addressed by the Council or Internal Audit.</p>
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Standards of financial conduct and prevention and detection of fraud and corruption	<p>An assessment of the Council's overall arrangements for maintaining proper standards of financial conduct and the prevention and detection of fraud and corruption.</p> <p>Detailed work in risk areas not already addressed by the Council or Internal Audit.</p>
Financial standing	<p>Assessment of the Council's arrangements for ensuring it is able to meet its financial obligations, including statutory requirements. This includes reviewing:</p> <ul style="list-style-type: none"> • budget setting procedures • budget monitoring procedures at all levels • responses to financial hotspots, major developments and liabilities. <p>We monitor the Council's financial standing with key staff throughout the audit year.</p>
Legality	<p>Assessment of the arrangements in place to ensure the Council:</p> <ul style="list-style-type: none"> • acts within its legal powers especially in relation to local transactions that might have a significant financial consequence • responds effectively to new legislation and national legal issues. <p>We monitor and review any potential legal issues that might have a significant financial consequence by discussions with key staff throughout the audit year.</p>