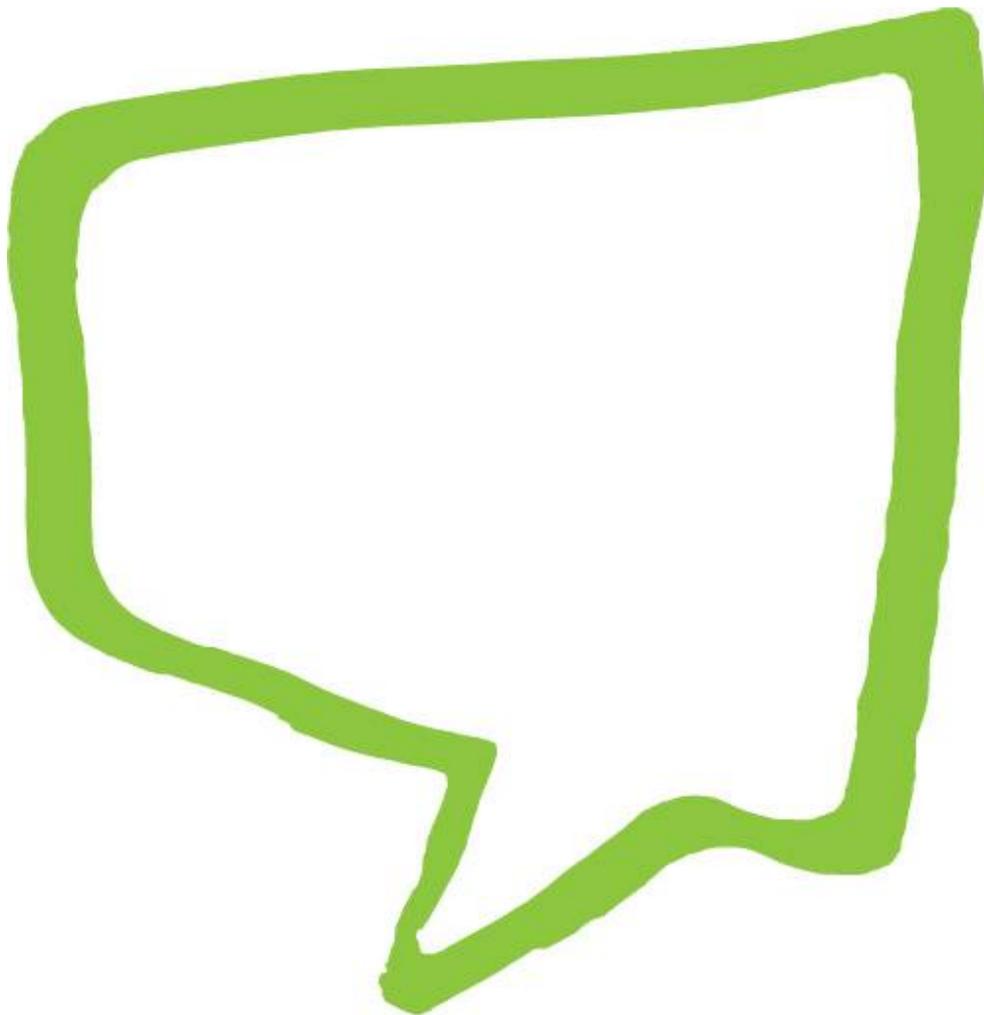


# Interim Audit Memorandum

Guildford Borough Council

Audit 2008-2009

June 2009



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## **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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# Introduction

- 1 The purpose of this report is to summarise our work to date on Guildford Borough Council's (the Council's) 2008/09 accounts. Our interim work was carried out as required by the International Standards of Auditing (ISAs) and can be summarised as:
  - identifying audit risks for 2008/09 accounts;
  - testing of material financial systems; and
  - Information Technology risk assessment (ITRA).
- 2 As part of our work we also carried out a review of Internal Audit. This is a review we are required to carry out every three years, and the results of that review are summarised in this report.
- 3 We use the findings of this stage of our audit to inform the focus and amount of work that we will carry out on the financial statements. At appendix 1 we attach a supplementary audit fees letter, which summarises the opinion audit risks which we have identified and considers the impact on our audit fee. The supplementary audit fees letter is required under ISA 300.
- 4 As part of our work we also followed up the recommendations from the Audit Commission's national report 'Risk and Return', which dealt with issues arising from the collapse of Icelandic banks and, more generally, Treasury Management arrangements in local government.
- 5 Key findings of this report are as follows.
  - There are a number of risks to our audit opinion which arise as a consequence of the current economic downturn. We plan to follow-up these potential issues as part of our audit visit.
  - On the whole, key controls in financial systems are in place and operating effectively. However there were some issues with the operation of housing benefits controls. As a result we do not plan to place reliance on those controls this year and we have brought forward our certification work on the housing benefits claim.
  - We have assessed the Council's IT environment as 'low risk'. The Council has addressed our prior year recommendations on IT security and achieved government 'Code of Connect' status in August 2008.
  - The Council's in-house internal audit service complies with CIPFA internal audit standards. However it has lacked capacity this year and there were issues with quality control arrangements over work which was contracted out to other auditors.
  - The Council adopts a prudent approach to Treasury Management and was not affected by the failure of Icelandic banks. The subject of Treasury Management has become more high-risk and consequently more high-profile over recent months. In our view it is timely for the Council to review its controls and reporting arrangements.

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# Main conclusions

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## Technical Accounting Issues

- 6 As part of our pre-statement work we have considered the potential risks to our opinion on the 2008/09 statements. A number of risks affecting the accounts of all local government bodies arise as a result of the current recession.
- 7 We have discussed accounting issues with the Council on an ongoing basis. In addition, the Audit Commission hosted a final accounts seminar in January 2009, which the Head of Financial Services attended.
- 8 Our supplementary fees letter at appendix 1 gives further detail of the specific audit risks which we plan to follow up as part of our audit. These are:
  - asset valuations;
  - income and expenditure position;
  - impairment of financial assets;
  - accounting treatment of the new Civic Hall;
  - events after the balance sheet date; and
  - collection fund deficit.

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## Financial systems

- 9 We confirmed our understanding of the Council's key financial systems by documenting and carrying out walkthroughs of each system. We identified the main financial controls in each system, and we tested controls for a number of systems as part of our cyclical plan, those systems being:
  - payroll;
  - accounts receivable; and
  - housing benefits.
- 10 Within the limited scope of our work we concluded that key controls were in place in the payroll and accounts receivable processes and that those controls were operating as intended.

- 11 From our sample of housing benefits cases there was one key control where we were unable to obtain the assurance we were seeking for our audit opinion. We plan to gain our assurance on housing benefits disclosures in the accounts by certifying the housing and council tax benefits grant claim before we give our opinion. We have discussed this with the Head of Revenues and Benefits and we plan to carry out our certification work from the week commencing 27 July. We may also carry out additional substantive testing of benefits.

### Recommendation

- R1 Review the operating effectiveness of controls to confirm the accuracy of payments to housing benefits claimants.

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### Triennial review of Internal Audit

- 12 As part of our 'managed audit' approach we aim to place reliance on Internal Audit for aspects of our review of financial systems. We do this to minimise duplication and to carry out our audit in an efficient way.
- 13 We are also required by auditing standards to carry out a full review of internal audit arrangements every three years. We have carried out this review in 2008/09.
- 14 We assessed the Council's internal audit arrangements, compared with CIPFA internal audit standards. Our conclusion was that the Council's internal audit service does comply with internal audit standards. The Council made a decision last year to contract out significant parts of the audit programme to another audit provider, because of a lack of capacity within the audit function.
- 15 We carried out a detailed review of a small sample of Internal Audit's work, with the aim of placing reliance on those files as part of our managed audit approach. Our sample included work carried out by the in house team as well as work which had been contracted out to an external provider.
- 16 Within the limited scope of our work we noted a difference in quality between work carried out in house and work done by the external provider. The in house files were timely and well documented and we were able to place reliance on them in all areas where we had planned to do so.
- 17 However there were some issues with the quality of the small sample of files we reviewed that were produced by the external provider. The issues were that the files:
- were not provided on a timely basis;
  - did not cover the expected scope; and
  - were sometimes not adequately documented to support the conclusions reached.

- 18 We discussed these issues with the Audit and Performance Manager and the Head of Corporate Development, who were aware of the issues. We understand the Council has taken steps to address this and is increasing capacity within the internal department.
- 19 We recommend that where the Council does contract out its work in future, that it ensures that robust quality control arrangements are in place for that work.

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**Recommendation**

**R2** Ensure that appropriate quality control measures are in place for the ICT and general audit contracts planned for 2009/10.

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**Information Technology Risk Assessment (ITRA)**

- 20 ISA+315 emphasises that the Information Technology (IT) element of internal control is an important part of the general control environment. The ISA requires the completion of an annual risk assessment (the ITRA) of the IT control environment.
- 21 A detailed ITRA was undertaken by our computer audit team with the objective of identifying any key risks at the pre-statements audit. In our previous two audit visits we assessed arrangements as 'high risk' because of earlier concerns around IT security. This year we reviewed the action taken by the Council following the recommendations we made in previous years. As a result of the progress which the Council has made, we have re-assessed the Council's IT control environment as 'low risk.'
- 22 Guildford Borough Council was one of the first Councils in Surrey to be given sign off on the Government Connect Secure Extranet Code of Connection. This was achieved in August 2008. This external sign off provides us with assurance that IT controls in a number of areas, such as access control and network control, are of sufficient quality to minimise the risk of material misstatement in the Council's statement of accounts.
- 23 We identified one area where control could be strengthened. There is no systematic process to ensure that all material financial systems are restored from back up over an acceptable period. In the absence of regular testing, there is a risk that failures in the back up process may not be identified.

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**Recommendation**

**R3** Draw up a cyclical plan for test-restoring systems from back up, ensuring that all material financial applications are test restored from back up in an acceptable period.

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## Review of Treasury Management arrangements

- 24 In March 2009 the Audit Commission published its national report 'Risk and Return'. The report was issued in the aftermath of the failure of Icelandic banks. It reports specifically on Icelandic banks and more generally on Treasury Management arrangements in local government. It contained nine key recommendations for all councils to benchmark their own arrangements against best practice.
- 25 These recommendations formed the basis of our discussions with council officers, in which we discussed the investments which the Council holds and the Council's approach and arrangements for managing its investment portfolio. The Council has a large portfolio for a council of its size, and receives significant income from its investments.
- 26 The Council adopts a prudent and risk averse approach to its investments. Its Treasury Management strategy document is presented to the Executive each year. The Council appears to have a relationship of trust with its financial advisers and part of the advisers' remit is to keep the Council informed of developments in the wider economy. The Council had no investments in Icelandic banks. During the worst part of the credit crunch the Council restricted its new investment to a narrow range of safe investments with the Debt Management Office.
- 27 In our view it is timely for the Council to revisit some its Treasury Management arrangements. There is scope for Members to be better engaged in Treasury Management. At present the Finance portfolio holder is involved in Treasury Management decisions, where appropriate, and each year the Executive receives a report and a Treasury Management strategy. We would consider it best practice for more frequent reports to be considered by a Committee with specialist knowledge and training in Treasury Management, in order to be able to provide more meaningful direction and challenge.
- 28 Day to day investment decisions are delegated to a qualified accountant in the Finance department. At the time of our review written procedure notes were in the process of being updated, in readiness for the role to be handed over to another member of staff. The officer is able to make investments in line with the written policy, which includes pre-approved amounts and institutions but does not require any independent authorisation when making the investment. The Council's view is that appropriate checks and balances are in place.

### Recommendation

Review Treasury Management arrangements, including reporting to Members, using the Commission's 'Risk and Return' report and the revised CIPFA Code of Practice as a benchmark.

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## The way forward

- 29 Our action plan at appendix 2 sets out the recommendations arising from this report. We have discussed this with Council officers and used the findings from this report to inform the scope of our work in our final accounts audit, which will take place from July 2008.
- 30 We would like to thank the finance team and Internal Audit for their support and co-operation during this audit.

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# Appendix 1 – Supplementary fees letter

21 May 2009		
Sue Sturgeon Director of Finance Guildford Borough Council Millmead Guildford Surrey GU2 4BB	Direct line	01483 243346
	Email	p-grady@audit-commission.gov.uk
Dear Sue		

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## Supplementary opinion audit plan 2008/09

You will recall that I issued the initial audit plan for 2008/09 in March 2008, which set out the work that I proposed to satisfy my responsibilities under the Audit Commission's Code of Audit Practice. As this plan was produced at the start of the financial year to give you an indication of the proposed fee, I was not able at that time to specify the detailed risks that I would need to consider as part of my audit opinion work.

I am now in a position to do this as the opinion work is about to commence. This letter represents my supplementary opinion plan under International Standard on Auditing (United Kingdom and Ireland) 300.

The above standard requires me to:

- identify the risk of material misstatements in your accounts;
- plan audit procedures to address these risks; and
- ensure that the audit complies with all relevant auditing standards.

I have therefore considered the additional risks that are appropriate to the current opinion audit and I have set these out overleaf.

<b>Risk</b>	<b>Residual risk</b>	<b>Audit response</b>
The economic downturn has resulted in significant reductions in the values of land and buildings. There were errors in the values shown for fixed assets in last year's accounts. There is a risk the value of assets may be materially misstated in the accounts.	Yes	We will consider the appropriateness of valuations and the accounting treatment the Council applies to fixed assets.
The economic downturn has led to reduced income and increased demand for services. There is a risk that the income and expenditure position may be mis-stated.	Yes	We will focus on the reported financial performance in the financial statements.
We were unable to fully rely on the controls which we tested in the Housing Benefits system, due to two controls failures. There is a risk that we have insufficient assurance that benefits expenditure is materially correctly stated.	Yes	We will carry out our audit of the housing benefits claim early, starting July 2009 and we plan to place reliance on assurance obtained as part of benefits certification for our opinion on the accounts.
The Council has a major capital development for a new Civic Hall. As this is a complex and significant capital project, there is a risk that the accounting treatment adopted may be inaccurate.	Yes	We will consider the appropriateness of amounts capitalised, for consistency with FRS15 and the Statement of Recommended Practice.
Due to the ongoing economic downturn there is an increased potential for Events after the balance sheet date to have an impact on the 2008/09 accounts. There is a risk that events taking place after the balance sheet day may not be appropriately reflected as a Post Balance Sheet Event.	Yes	We will consider the relevance of events up to the date of signing the opinion.
The economic downturn creates an increased risk of reduction in the value of financial assets. There is a risk this reduction in value may not be fully reflected in the value of the financial assets disclosed in the accounts.	Yes	We will review the values disclosed for financial assets and bad debts, for consistency with accounting standards and we will consider whether the Council has followed an appropriate process in identifying impairments.

Risk	Residual risk	Audit response
<p>In 2007/08 the collection fund was in deficit by around £1 million.</p> <p>In the 2007/08 annual governance report we made a recommendation that the Council take action to bring the Collection Fund back into balance.</p>	Yes	We will revisit the financial position of the collection fund as part of our audit.

In my original audit plan, the estimated fee for the opinion audit was based on my best estimate at the time and agreed at £71,125 as part of a total audit fee of £107,276.

I am satisfied that the original fee estimate for the opinion audit was appropriate and no adjustment is therefore required to the fee at this stage. However, I will keep the fee under review as the opinion audit progresses. If I need to amend the fee subsequently, I will first discuss it with you.

Yours sincerely

**Paul Grady**  
**District Auditor**

## Appendix 2 – Action Plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
5	R1 Review the operating effectiveness of controls to confirm the accuracy of payments to housing benefits claimants.	2	SW	Yes		December 2009
6	R2 Ensure that appropriate quality control measures are in place for the ICT and general audit contracts planned for 2009/10.	2	MB	Yes		September 2009
6	R3 Draw up a cyclical plan for test-restoring systems from back up, ensuring that all material financial applications are test restored from back up in an acceptable period.	2	SW-M	Yes		September 2009
7	R4 Review Treasury Management arrangements, including reporting to Members, using the Commission's 'Risk and Return' report and the revised CIPFA Code of Practice as a benchmark.	2	SR	Yes		December 2009

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