



INFRASTRUCTURE, GOVERNMENT
AND HEALTHCARE

Annual Audit Letter 2008/09

Surrey Heath Borough
Council

January 2010

AUDIT

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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Greg McIntosh, who is the engagement director to the Authority, telephone 02703116430, email greg.mcintosh@kpmg.co.uk who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 236 4000, email trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Investigation Officer, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by e mail to: complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421

Executive Summary

Purpose

This Annual Audit Letter (the letter) summarises the key issues arising from our 2008/09 audit at Surrey Heath Borough Council (the Council). Although this letter is addressed to the Members of the Council, it is also intended to communicate these issues to key external stakeholders, including members of the public. The letter will also be published on the Audit Commission website at www.audit-commission.gov.uk. It is the responsibility of the Council to publish the letter on its website at www.surreyheath.gov.uk. Throughout our audit we have highlighted areas of good performance and also provided recommendations to help you improve performance. A summary of our key recommendations is summarised in Appendix 1. We have reported all the conclusions in this letter to you throughout the year and a list of all reports we have issued is provided in Appendix 2.

Scope of our audit

The statutory responsibilities and powers of appointed auditors are set out in the Audit Commission Act 1998. Our main responsibility is to carry out an audit that meets the requirements of the Audit Commission's *Code of Audit Practice* (the *Code*) which requires us to review and report on your:

- *use of resources* - whether you have made proper arrangements for securing economy, efficiency and effectiveness ('value for money') in your use of resources (UoR). Our work in this area is summarised in section 2; and
- *accounts* – the Financial Statements and the Annual Governance Statement, summarised in section 3.

Key Messages

The key areas which we draw to your attention to are:

- Our use of resources assessment, the first under the Audit Commission's new UoR regime, demonstrated that the Council has got sound processes in place and is achieving positive outcomes in managing resources where the Council was assessed as level 3. In managing finances and governing the business the Council scored a level two as although processes were found to be adequate, areas for development were noted. Overall the Council has been assessed as level 2 (performing adequately).
- We identified no issues in the course of the financial statements audit that have not been revised by the Council and which are considered to be material and we issued unqualified audit opinions on the Council's financial statements and on its arrangements for securing value for money conclusion in 2008/09.

Fees

Our fee for the audit is £94,000. This fee was in line with the fee agreed with you in our 2008/09 audit plan.

Future Issues

- From 2010/11 local government bodies are required to prepare their financial statements under International Financial Reporting Standards (IFRS) and therefore the Council will need to be preparing for this transition.
- Those Local Authorities in the Carbon Reduction Commitment scheme will need to start reporting their usage from 1 April 2010 and recording these transactions within their financial statements with effect from 1 April 2011. There will be implications for cash flow, energy bills, and investment decisions and these could be significant. There are huge opportunities in addressing sustainability with clear cost reduction opportunities from saving energy which will become more and more significant over time. There are also opportunities to use the sustainability agenda to support the achievement of business challenges. It puts carbon reduction firmly amongst your corporate priorities.
- Sustainability performance - The Treasury is developing guidance for 2010/2011 which will require all public sector bodies to report publicly on sustainability performance in annual reports. CIPFA is in discussion with the Treasury about when and in what form this requirement will be formalised for local authorities. The reported information will be subject to audit and scrutiny. Sustainability reporting will be difficult to implement and many organisations will need to act now to implement new information gathering processes.

Executive Summary (continued)

Future Issues (continued)

- Public expenditure forecasts indicate that there will be significant pressure on local authorities' funding in the medium term. Future financial settlements will be extremely tight, increasing the need for local authorities to have comprehensive efficiency programmes supported by sound financial management arrangements. It is likely that bold measures will be required to generate sufficient savings to mitigate the impact on priority services. More than ever before, officers and Members will need to focus on identifying these significant savings measures and ensuring that robust arrangements are in place to monitor their delivery to ensure they are realised. The Council has a good track record in delivering such efficiency and savings targets. It will, however, be necessary to revisit and update the Council's plans to ensure that they can deliver the levels of savings required for the future.

Acknowledgement

This has been KPMG's second year as the Council's external auditor following our appointment by the Audit Commission in 2007. We would like to thank the Council's management and staff for the help, support and co-operation they have provided throughout our audit. We have agreed our audit plan for our 2009/10 audit and look forward to working closely with the Council in the coming year to deliver this programme of work.

Use of resources

The main elements of our use of resources work are:

- *Use of Resources* - from 2008/09, the Audit Commission introduced a new UoR assessment framework which forms part of the Comprehensive Area Assessment (CAA). This replaced the former UoR assessment which was predominantly focused on processes – the scope of the new regime is wider as it also considers whether public bodies have achieved significant and sustainable outcomes. UoR assessment comprises three themes which consider:
 - Managing finances – focusing on sound and strategic financial management;
 - Governing the business – focusing on strategic commissioning and good governance; and
 - Managing resources – focusing on the management of natural resources, assets and people.
- *Value for money conclusion* – we issue a conclusion on whether we are satisfied that you have put in place proper arrangements for securing economy, efficiency and effectiveness in your use of resources. This is based on the UoR assessment.

The findings from this work are summarised below.

Element of work	Key findings								
Use of Resources	<p>Our assessment of Surrey Heath Borough Council against the three themes resulted in the following scores on a scale of one (inadequate) to four (performing strongly):</p> <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th style="background-color: #003366; color: white;">Area</th> <th style="background-color: #003366; color: white;">Score</th> </tr> </thead> <tbody> <tr> <td style="background-color: #d9e1f2;">Managing finances</td> <td style="background-color: #d9e1f2;">2</td> </tr> <tr> <td style="background-color: #d9e1f2;">Governing the business</td> <td style="background-color: #d9e1f2;">2</td> </tr> <tr> <td style="background-color: #d9e1f2;">Managing resources</td> <td style="background-color: #d9e1f2;">3</td> </tr> </tbody> </table> <p>These scores build on last year's UoR assessment when the Council scored level 2 (performing adequately) overall with scores of 2 for financial reporting, financial standing and value for money and 3 (performing well) for financial management and internal control themes. It should be noted, however, that direct comparisons cannot be made between the previous UoR scores and those awarded this year due to the differences in each assessment framework.</p> <p>In achieving level 2 overall the Council is getting the basics right in managing its finances and governing its business. It is performing well in its approach to managing its workforce. It is conscious of the challenges it faces in the short- and medium- term and has responded positively, undertaking a series of service reviews to identify £850k of recurrent, sustainable savings. It shares data with other authorities to enable benchmarking and continues to develop its understanding of its cost base. It is progressing a number of partnerships to help it meet its strategic objectives. Performance reporting has been updated and provides clear information for Members to understand and challenge performance..</p>	Area	Score	Managing finances	2	Governing the business	2	Managing resources	3
Area	Score								
Managing finances	2								
Governing the business	2								
Managing resources	3								
Value for money conclusion	<p>We issued an unqualified value for money conclusion for 2008/09.</p> <p>This means that we are satisfied that you put in place proper arrangements for securing economy, efficiency and effectiveness in your use of resources.</p>								

Financial statements

Audit opinion

We issued an unqualified opinion on your accounts on 30 September 2009. This means that we believe the accounts give a true and fair view of the financial affairs of the Council and of the income and expenditure recorded during the year.

Before we give our opinion on the accounts, we are required to report to 'those charged with governance' any significant matters identified. We did this in our report to the Policy and Audit Scrutiny Committee meeting on the 23 September 2009 and the key issues are summarised here.

Accounts production and adjustments to the accounts

- We received a complete set of draft accounts by the 30th June deadline supported by some good quality working papers.
- Our audit identified two audit adjustments which were material in nature to the financial statements. Both of these adjustments were made by the Council and had no impact on the Income and Expenditure account outturn. We also identified various presentational audit differences which were corrected by the Council.
- Our audit resulted in twelve recommendations regarding financial controls, which the Council have agreed to implement.

There were no other issues raised for the attention of the Policy and Audit Scrutiny Committee.

Future issues

There is one key developments which the Council will need to manage effectively in order to continue its good track record in producing timely, complete and materially accurate financial statements:

- From 2010/11 local government bodies are required to prepare their financial statements under IFRS. There is a transitional process that needs to be followed, starting with assessing the areas where IFRS will require re-statement of aspects of the Council's accounts to comply with IFRS. The Council will need to prepare for this transition and ensure that its financial systems and other arrangements have been reviewed and updated as necessary, and that finance staff receive necessary training.

Appendix 1: Key recommendations

This appendix summarises the main high priority recommendations that we have identified during 2008/09, along with your response to them.

Issue/ Recommendation	Management Response
<p><u>Issue</u></p> <p>We noted that the Council does not perform a reconciliation of council tax benefits as per iworld (council tax system) with its Oracle financial ledger. We noted that there is some confusion over the frequency of reconciliation. Consequently, the benefits expenditure as per council tax record and as per financial services are not in agreement. <u>Recommendation</u></p> <p>It is recommended that a monthly reconciliation should be performed between council tax system and the financial ledger. Any reconciling items should be investigated.</p>	<p>The cash element of Council Tax and Benefits is reconciled monthly with the Oracle Financials system however the non cash elements are only posted once a year. In the light of your recommendation we have agreed to post these non cash elements on a quarterly basis.</p>
<p><u>Issue</u></p> <p>In our ISA 260 report for 2007-08, we raised a recommendation that a process needs to be in place to obtain confirmation from members and staff regarding their interests. During interim audit, we noted that the Council does not obtain confirmation from members and staff regarding their interests, gifts and hospitality received..</p> <p><u>Recommendation</u></p> <p>It is suggested that the Council should obtain confirmation from all members and staff of any interests in other entities, gifts and hospitality received during the year 2008-09. In addition, the Council needs to review the register of interests on a periodic basis. We will review the steps taken by the Council during our accounts audit stage.</p>	<p>The Council does maintain a register of hospitality and gifts, which is kept by the Chief Executive Secretary, which staff are required to complete as appropriate. The Assistant Head of Legal Services, Miss Sophia Nartey, will be asking all staff and members to complete a formal declaration of interests form between now and the final audit visit</p>
<p><u>Issue</u></p> <p>We understand that the finance department is working with the IT department to incorporate a new supplier form on the procurement system, but this is not yet in place. Consequently, there is a risk of fraud that orders are placed to new suppliers without obtaining relevant details and credit checks.</p> <p><u>Recommendation</u></p> <p>The online form should be put in place as soon as possible, and the finance department should not make payments to suppliers if the form is not in place, to mitigate this risk of fraud.</p>	<p>Finance will be informing service managers that forms need to be completed when ordering from new suppliers.</p> <p>The form has been put on the intranet in e-form to make it more accessible and we are also expecting suppliers to complete this form in the first instance otherwise payment may be delayed.</p>
<p><u>Issue</u></p> <p>The Council is aware of the requirement to prepare its accounts based on IFRS from 2010-11. Staff have attended various IFRS courses and the Council is in the process of collating data for staff annual leave accruals. We noticed that there is no formal work plan in place which identify tasks, timeframe and task owner. Due to the absence of a work plan, there is a risk that the Council's accounts may not be IFRS ready for 2010-11.</p> <p><u>Recommendation</u></p> <p>It is suggested that the Council should prepare a IFRS readiness work plan (in accordance with LAAP 80), which defines tasks, milestones, task owner and deadlines.</p>	<p>A briefing paper has been prepared on the main challenges of IFRS and has been presented to Management Board and the Audit Scrutiny Panel. In addition all accounts staff have been on presentations on IFRS to increase awareness of this issue. An outline work plan has been prepared and is included within the report but has not been worked up in to any detail at the moment as suggested by LAAP 80. This will be done in the next few months.</p>

Appendix 1: Key recommendations (continued)

Issue/ Recommendation	Management Response
<p><u>Issue</u></p> <p>The National Fraud Initiative exercise for 2008-09 has identified 11 cases for the Council, 8 of which are payroll related and 3 are pension fund related. We understand that the Council has not started investigating these cases and there is no time frame in place to resolve these. <u>Recommendation</u></p> <p>It is suggested that the Council should investigate these 11 cases in an agreed timeframe and identify the core reasons for such errors. The Council needs to consider modifying its procedures over payroll and pension based on the result of that investigation.</p>	<p>These matches are being investigated by payroll and will be completed by the final audit visit</p>
<p><u>Issue</u></p> <p>We noted that bank reconciliations for all accounts are not performed on a monthly basis. The reconciliations for August, October and November were performed in January 2009 upon identification by internal audit. Consequently, the financial ledger was not in agreement with the bank information.</p> <p><u>Recommendation</u></p> <p>It is recommended that financial services should perform bank reconciliations for all accounts on a monthly basis. This will ensure that bank accounts are agreed with the financial ledger and any reconciling items are investigated on a timely manner.</p>	<p>We endeavour to perform bank reconciliations on a monthly basis however due to pressure of work this is not always done as quickly as possible. We will endeavour to ensure this is done more rapidly in future.</p>
<p><u>Issue</u></p> <p>The Council does not prepare exception reports for payments made to new suppliers. Consequently, there are no process in place to ensure that payments above £10k made to new suppliers are approved in accordance with financial regulations and any duplicate payments are investigated. Due to this, there is a possibility that duplicate payments or unapproved payments are made to new suppliers.</p> <p><u>Recommendation</u></p> <p>It is recommended that a monthly exception report should be generated for payments to new suppliers. This report needs to be reviewed by senior management to ensure that all such transactions are executed as per financial regulations.</p>	<p>Controls do exist regarding payments to all suppliers whether existing or new. However as an additional control Internal Audit will be given the facility to run a report to list all suppliers created for a particular date range for review.</p>
<p><u>Issue</u></p> <p>The Council generates monthly exception reports from its benefit system to identify un-presented cheques. We understand that management performs a review of such exception reports. However, the audit trail for such review are not maintained. Consequently, it is not evident what actions are taken to resolve the items identified in such reports.</p> <p><u>Recommendation</u></p> <p>It is recommended that the evidence of review and actions taken relating to all exception reports should be maintained by the Council.</p>	<p>Finance will send this list monthly to benefits for them to check and action</p>

Appendix 1: Key recommendations (continued)

Issue/ Recommendation	Management Response
<p><u>Issue</u></p> <p>The exceptions reports to monitor the ledger are produced on an adhoc basis. Consequently, there are no controls in place to monitor inactive user profiles and ledger use at unusual times.</p> <p><u>Recommendation</u></p> <p>It is suggested that the Council should run ledger monitoring exception reports on a monthly basis. This will ensure that strict monitoring processes are in place to check the irregular use of the ledger and any issue identified are investigated in a timely manner.</p>	<p>Typically many staff have read only access to the financial system yet choose not to use it. However they are not normally removed. Any member of staff that leaves the Council has their main log in details cancelled which means they no longer have access to the financial system. The system can only be accessed internally and then only in working hours. However the systems accountant will run these reports on a quarterly basis for review by the Financial Accountant. This is supplemented by an audit recommendation in the 08/09 main accounting audit which is still to be finalised where it is recommended that dormant accounts over a certain period should be suspended.</p>
<p><u>Issue</u></p> <p>Review of the Fixed Asset Register identified two categories of assets 'de-minimis' and 'not owned by the Council'. Both categories of assets had been subject to valuations in year. Assets 'not owned' by the Council do not appear on the Council's balance sheet.</p> <p>It is unclear why these assets are recorded alongside those disclosed within the balance sheet.</p> <p><u>Recommendation</u></p> <p>We recommend that dates are set for review of policies, and these are monitored centrally and enforced where necessary. In addition the policies should then go to the relevant committee for approval.</p>	<p>The asset register includes all of the Councils Land and Buildings whatever their value so as to provide a complete list of the Council's holdings.</p> <p>The "deminimis" assets are revalued to ensure that they remain "de minimis" . The new asset system will be able to make a distinction in respect of "deminimis" assets.</p>

Appendix 2: Audit reports issued

A summary of the reports issued in the year to date is set out below.

Report	Date issued
Audit and Inspection Plan 2008/09	June 2008
Annual Audit Fee letter 2009/10	April 2009
Interim Audit Report	June 2009
Report to those charged with governance 2008/09	September 2009