

# Interim Opinion Report

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**Sunderland City Council**

**Audit 2010/11**

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**We also help public bodies manage the financial challenges they face by providing authoritative, unbiased, evidence-based analysis and advice.**

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# Introduction

**1** This report sets out the results of our interim opinion audit work for 2010/11, which we concluded in June 2011.

**2** The Code of Audit Practice requires review and reporting on the Council's financial statements and the Annual Governance Statement. The work at the interim stage informs the opinion process.

**3** The requirements of the International Standards on Auditing United Kingdom and Ireland (ISA UK&I) require auditors to gain an understanding and test the systems which inform the material entries in the financial statements.

# Background

**4** 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.

**5** The duties and powers of auditors appointed by the Audit Commission are set out in the Audit Commission Act 1998 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.

**6** Appointed auditors act quite separately from the Commission and in meeting their statutory responsibilities are required to exercise their professional judgement independently of both the Commission and the audited body.

# Audit approach

**7** The work we have completed to satisfy the requirements set out in the Introduction consists of:

- mapping the financial and information systems that provide material figures in the financial statements. The material financial and information systems identified are as follows:
  - General ledger
  - Bank reconciliation
  - Loans
  - Investments
  - Accounts payable (Creditors)
  - Accounts receivable (Debtors)
  - Payroll
  - Social care payment system (SWIFT)
  - National Non-Domestic Rates (NNDR)
  - Council Tax
  - Housing and Council Tax Benefits
  - Cash receipting
  - Capital accounting
  - Periodic income
- documenting the processes and controls in place within each system and undertaking walkthrough tests (these follow a transaction through each part of the system) to ensure the system is operating as stated; and
- testing key controls within the systems to ensure that they are operating effectively (these are detailed sample tests covering the full financial year). We have a three year cyclical programme for testing system controls where we seek to place reliance on controls for our opinion audit. This year we carried out controls testing on the following systems:
  - General ledger.
  - Cash receipting.
  - Social care payment system (SWIFT).

**8** In addition to the interim financial systems work, we have completed our review of Internal Audit, an IT risk assessment, a tax risk assessment and some early work on Sunderland City Council's compliance with IFRS. These are briefly summarised in this report.

# Main conclusions and findings

## Interim Systems Work

**9** We have concluded that, in general, the key controls within the Council's main financial systems are operating as designed. There is some scope for improvement in the areas of the social care payment system (SWIFT), National Non-Domestic Rates (NNDR), Housing and Council Tax Benefit, Council Tax and Periodic Income. Details are given below. Our recommendations made to address the issues raised and comments from officers are summarised in the Action Plan in Appendix 1. We will follow up the agreed action plan in future audit work to ensure that the actions have been fully implemented by officers.

### Journal entries

**10** We discussed with officers last year whether there should be independent authorisation of all journal entries, including online journals and all high value journals. A new process was agreed to carry out a review of all journals over £500k as part of the annual closedown of accounts process.

**11** To obtain the assurance we need to give our audit opinion on the financial statements, our response to this is that we will increase our sample sizes when substantively testing journals. We will also consider the review of all journals over £500k undertaken by officers.

### Social care payment system (SWIFT)

**12** Within the SWIFT process a weekly sample check of 10 payments to SAP and copy remittance advices is undertaken. For the week selected in our walkthrough of the SWIFT process, this check had not been undertaken.

## Recommendation

**R1** Consider whether this check of SWIFT contracts is required. If it is required we recommend that it is carried out consistently as designed.

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### National Non Domestic Rates (NNDR)

**13** It was noted in our walkthrough testing that the daily reconciliation between the cash receipting system and the NNDR system had only been completed up to July 2010 (as at 25 January 2011). However, a separate reconciliation is undertaken between cash receipting and SAP as part of the bank reconciliation process and this was kept up to date.

14 There is a small risk of misallocation of cash postings between council feeder systems without timely and prompt reconciliations.

15 We will ensure that a year end reconciliation has been completed as part of our post statements work.

### Recommendation

R2 Daily NNDR reconciliations with the cash receipting system should be undertaken on a timely basis.

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### Bank Reconciliation

16 The monthly bank reconciliation reviewed during our walkthrough test showed that 7 out of the 15 individual code reconciliations had been signed by only one officer (4 occasions no preparer signature and 3 occasions no reviewer). We do note that the bank reconciliation had been prepared correctly. There is, however, a risk that if the agreed process of preparation and review is not followed, errors may not be highlighted...

17 We will ensure that a year end bank reconciliation has been completed, and we will test this as part of our post statements work.

### Recommendation

R3 All bank reconciliations should be signed by the preparing and reviewing officers.

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### Housing and Council Tax Benefits

18 During our walkthrough test we found there was a lack of documentary evidence that system parameters are checked following uprating. There is a risk that inaccurate data is entered, causing incorrect benefit calculations.

19 Our certification work on the Housing and Council Tax Benefit Subsidy return will include checking the accuracy of 2010/11 Housing Benefits parameters.

### Recommendation

R4 Implement a procedure of recording the check on Housing and Council Tax Benefit parameters input during uprating.

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## Council Tax

**20** A monthly report of all property changes is sent to the Valuations Office (VO) from Council Tax; in previous years this was being checked monthly to the VO schedules received to ensure the change had been actioned. During the walkthrough test there was no up-to-date documentation of this control. Review showed that 3 out of 12 months were held on file for 2010/11, but these had little or no annotation to show a check of the changes had taken place.

**21** There is a risk that changes may not be processed. This weakness would not have a material impact on the accounts and will not impact on our audit approach.

### Recommendation

**R5** Monthly review of property amendments with the Valuations Office is undertaken and documentation retained as evidence of the process.

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**22** Our walkthrough of Council Tax exemptions highlighted an out of date student exemption. The Student Certificate held on file had an expected end date of January 2011. However, the Council Tax account had an exemption into 2011/12 and no review date entered on the system.

**23** A weekly review of exemptions takes place based on a report which picks up the review dates entered on the system, therefore this student was not reviewed.

**24** There is an annual review of all student exemptions each October which would have highlighted the case. However, there is a risk that arrears are built up resulting in an increased risk of uncollectable tax.

### Recommendation

**R6** Ensure that student exemptions that have no review date are highlighted on a timely basis.

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## Periodic Income

**25** Our walkthrough highlighted that there was no formal process of checking updates to system parameters. There is a risk that incorrect charges are raised based on an error in the parameters entered.

## Recommendation

**R7** Periodic Income parameters should be entered by one officer and checked by another officer, and this process should be documented.

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**26** We were unable to ascertain a common control that ensured all periodic income requested by a department had been billed. Once a request has been sent to the PI team for input, confirmation e-mails were sent to some departments showing the account number set up.

**27** Reviewing a few of the processes within initiating departments, showed that monitoring of periodic income was inconsistent between departments. Some departments would follow up the set up of periodic income and maintain spreadsheets of the accounts set up and monitor the invoices sent out. Others stated that there was no formal process for monitoring that all PI requests had been actioned.

## Recommendation

**R8** Each department should ensure that all periodic income requests are implemented.

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## Review of Internal Audit

**28** We completed our annual review of Internal Audit against the CIPFA Code of Practice for Internal Audit in Local Government, and this included a detailed review of audit files.

**29** Our review identified that Internal Audit continues to meet its professional and statutory duties. Processes in place are driven by an effective Quality System. Our detailed review of files did not highlight any significant non-compliance with the Quality System or the Code.

**30** A separate report was agreed with officers.

## IT risk assessment

**31** As part of our work to support the opinion that we give on your accounts, we undertake an annual Information Technology (IT) risk assessment of your arrangements.

**32** The scope of our review was to complete an IT Risk Assessment that included testing some general IT controls surrounding the operation of the main financial systems and associated infrastructure.

**33** Overall, we concluded that the IT arrangements for the key financial systems present a low risk of material error in the 2010/11 accounts. However, we have identified some weaknesses in general IT controls where there is scope for improvement.

**34** A separate report has been discussed with officers and an action plan agreed with the Head of Corporate ICT. The completed action plan will be used to monitor progress in implementing the agreed actions.

## **Tax risk assessment**

**35** Our specialist tax auditor carried out a tax risk assessment focused on VAT, PAYE and NIC. We concluded that appropriate arrangements are in place, and we did not identify any risks of material misstatement for our opinion audit.

## **Implementation of IFRS**

**36** Throughout the year we have worked closely with officers on the impact of International Financial Reporting Standards (IFRS). Officers have been keen to share their early work with us in order to smooth the workload at the draft accounts stage.

**37** Progress on the approach to componentisation of plant, property and equipment has been agreed with us regularly. This included the identification of a suitable minimum asset value for assessment and clarification of which components would be separately depreciated. Appropriate input on these issues has been obtained from the Council's valuer.

**38** IFRS compliant restated accounts were provided by officers and our audit work has been focused on the:

- restated 2008/09 Balance Sheet
- restated 2009/10 Balance Sheet
- restated 2009/10 Income and Expenditure Account (now the Comprehensive Income and Expenditure Statement), and
- the new Movement in Reserves Statement

**39** This process of ongoing discussion and agreement with officers has helped both with accounts production and the audit. We recognise the considerable efforts undertaken by officers to ensure that the Council complies with the new requirements and the expertise that has been established through this process.

**40** We did identify some relatively minor errors in the calculation and presentation of the following:

- accruals for unused leave;
- property lease accounting entries did not take account of up-front contributions to leases; and
- adjustments for lease hire vehicles had been omitted.

41 However, because these issues have been identified in a timely way, officers were able to rectify these errors in the financial statements that were produced before the end of June.

## Appendix 1 Action Plan

### Recommendations

#### Recommendation 1

Consider whether this check of SWIFT contracts is required. If it is required we recommend that it is carried out consistently as designed.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Not applicable   |
| <b>Priority</b>       | Low  |
| <b>Date</b>           | Not applicable   |
| <b>Comments</b>       | The checks were all up to date and being maintained. However, a review of this task has shown that this is no longer required, because all SWIFT feeder uploads are controlled and reconciled centrally to SAP on a daily basis. |

#### Recommendation 2

Daily NNDR reconciliations with the cash receipting system should be undertaken on a timely basis.

|                       |   |
|-----------------------|---|
| <b>Responsibility</b> | Non Domestic Rates Specialist   |
| <b>Priority</b>       | Medium  |
| <b>Date</b>           | 1 July 2011   |
| <b>Comments</b>       | Agreed - all 2010/2011 have been completed since and new process for 2011/2012 to reflect the new income management system that has been implemented. |

#### Recommendation 3

All bank reconciliations should be signed by the preparing and reviewing officers.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Principal Accountant   |
| <b>Priority</b>       | Low  |
| <b>Date</b>           | 1 July 2011  |
| <b>Comments</b>       | All bank reconciliations for 2010/2011 had been completed, the most important fact, although some signatures were missing. Management have since streamlined the sign off protocol to make the process less onerous. |

#### Recommendation 4

Implement a procedure of recording the check on Housing and Council Tax Benefit parameters input during uprating.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Revenue Systems Team Manager   |
| <b>Priority</b>       | Low  |
| <b>Date</b>           | 1 July 2011  |
| <b>Comments</b>       | All of the necessary checks and segregation of duties had been carried out but no formal evidence could support this activity. A flow chart of this task is available and was followed, but the Manager is to maintain formal records in future showing signatures of staff entering and checking the input. |

#### Recommendation 5

Monthly review of property amendments with the Valuations Office is undertaken and documentation retained as evidence of the process.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Council Tax & Business Rates Officer   |
| <b>Priority</b>       | Low  |
| <b>Date</b>           | 1 July 2011  |
| <b>Comments</b>       | Recognised that no formal sign off of each document is carried out although the Manager confirmed that all VO documentation is fully and regularly checked. The fact that few narrative comments were present reflected the fact that only new properties and those with errors can be amended immediately per the regulations. Other changes can only be actioned once a property changes ownership through sale usually and these are kept on file with little or no comment. The Officer however is to ensure all VO documentation is appropriately signed off in future. |

#### Recommendation 6

Ensure that student exemptions that have no review date are highlighted on a timely basis.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Council Tax & Business Rates Officer                                       |
| <b>Priority</b>       | Medium   |
| <b>Date</b>           | 1 July 2011  |
| <b>Comments</b>       | Agreed - will introduce regular quarterly reviews to avoid this in future. |

### Recommendation 7

Periodic Income parameters should be entered by one officer and checked by another officer, and this process should be documented.

|                       |  |
|-----------------------|--|
| <b>Responsibility</b> | Transactional Finance Processing Manager   |
| <b>Priority</b>       | Low  |
| <b>Date</b>           | 1 July 2011  |
| <b>Comments</b>       | Agreed - checks are carried out on the system parameters but agreed to formally separate out this duty and incorporate within year end procedures to be able to evidence this in future. |

### Recommendation 8

Each department should ensure that all periodic income requests are implemented.

|                       |   |
|-----------------------|---|
| <b>Responsibility</b> | Transactional Finance Processing Manager  |
| <b>Priority</b>       | Low   |
| <b>Date</b>           | 1 July 2011   |
| <b>Comments</b>       | Agreed - all requests will be responded to by e-mail once set up as part of the new way of working process. A mitigating factor would be that the budget manager should identify any income that has not been raised properly through budget monitoring procedures. |

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