

# Interim report

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Uttlesford District Council

Audit 2009/10

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# Contents

<b>Introduction .....</b>	<b>2</b>
<b>Audit approach.....</b>	<b>3</b>
Main conclusions .....	4
<b>Detailed report.....</b>	<b>5</b>
Internal Audit.....	5
Material systems.....	6
The way forward .....	8
<b>Appendix 1 Action plan .....</b>	<b>9</b>

# Introduction

1 The Audit Commission's Code of Audit Practice requires that I give an opinion on the Authority's annual financial statements. I am required to plan and perform my work in accordance with International Standards on Auditing (UK and Ireland) (ISAs) and to meet this requirement I undertook a pre-statement audit at the Council.

2 My pre-statement audit work was undertaken in order to comply with ISA(UK&I) 315 which requires that:

**The auditor should obtain an understanding of the entity and its environment, including its internal control, sufficient to identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, and sufficient to design and perform further audit procedures.**

3 I also undertook a programme of testing of certain controls upon which I decided I would seek to place reliance for the audit opinion. As part of this work, I reviewed the work of Internal Audit where this was available. Where Internal Audit concluded effective controls were in place I sought to place reliance on their work.

4 This report summarises our findings from the pre-statement audit.

# Audit approach

5 My interim audit was structured as follows.

- Identifying the risk of material error in the financial statements at the audited body level. This included an assessment of external and internal factors, business risks, financial performance, internal control and any other identified risks. This work was performed on existing knowledge and recent Audit Commission work carried out at the Council.
- Identifying the risks of material error in the financial statements at the systems level. I have sought to understand and document all the significant financial systems relevant to financial reporting. This consists of the procedures and records that are established to initiate record, process and report the transactions and to maintain accountability for the related assets and liabilities.
- Determining a testing strategy. The testing strategy is the way in which I seek to obtain sufficient assurance on the entries in the financial statements to enable me to form my opinion. This work can consist of reliance on controls or on substantive testing of figures in the financial statements or on a combination of both.
- Pre-statement testing. Where my understanding of the system indicated that I could obtain assurance on the financial statements from controls then these were tested on a sample basis. If I concluded that substantive testing would be required early testing was completed wherever possible.
- Under ISA(UK&I) 240, I am also required to consider and identify if there is any risk of material fraud. Fraud encompasses both misappropriation of assets and intentional misstatements within the financial statements (ie deliberate error).

6 The systems that I identified as having a significant input into the financial statements were:

- general ledger;
- cash and bank;
- debtors;
- creditors;
- fixed assets;
- payroll;
- housing rents;
- business rates/NNDR;
- housing benefits;
- council tax;
- treasury management;
- pension costs/FRS17; and
- housing repairs and maintenance.

## Main conclusions

**7** I was able to gain assurance from controls operating within most financial systems, with the exception of creditors where my testing identified that creditor invoices were not always formally agreed to their respective purchase orders and delivery notes. This resulted in additional substantive testing for the final accounts audit.

**8** For all other systems, minor weaknesses were identified, which if addressed, would improve internal control and reduce the risk to the Council of a material error in the accounts. The detailed section of this report includes more information on these issues.

**9** Fully effective controls in all areas would reduce the amount of testing we are required to do as part of our final accounts audit and could potentially reduce the audit fee.

**10** The action plan at Appendix 1 summarises the recommendations made as a result of our interim work and the Council's response.

# Detailed report

## Internal Audit

**11** In order to document and test material systems I review the work of Internal Audit and seek to place reliance on it wherever possible.

**12** The Audit Commission's Code of Audit Practice requires that I give an opinion on the Council's annual financial statements. I am required to plan and perform my work in accordance with International Standards on Auditing (UK and Ireland) (ISAs) and to meet this requirement I undertook a pre-statement audit at the Council.

**13** My pre-statement audit work was undertaken in order to comply with ISA(UK&I) 315 which requires that:

**The auditor should obtain an understanding of the entity and its environment, including its internal control, sufficient to identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, and sufficient to design and perform further audit procedures.**

**14** I also undertook a programme of testing of certain controls upon which I sought to place reliance for the audit opinion. As part of this work, I planned to review the work of Internal Audit, where this was available, with a view to placing reliance on it wherever possible.

**15** Internal Audit is a key governance tool that gives senior management of the Council assurance that the internal controls are operating effectively. They also act as a detector of, and deterrent against, fraud.

**16** As part of my audit approach I planned to maximise the reliance placed on Internal Audit's work and reduce the amount of testing I needed to carry out. As noted in my previous audit fee report to Performance Select Committee in July 2010, I was not able to fully utilise the work performed by Internal Audit in 2009/10. This was mainly due to the fact that the controls tested by Internal Audit did not match those I considered to be key for opinion purposes. I therefore had to undertake testing on these controls.

**17** As part of planning for 2010/11, I have ensured that Internal Audit is aware of the controls I consider to be key before starting its audit work. I have also agreed when this work needs to be completed by in order for me to be able to place reliance on it for my audit opinion. This has been included within the updated protocol for liaison between internal and external audit. I would suggest that work on the main financial systems is completed in quarter 3 to ensure it is available on a timely basis. This

should result in a reduction in the amount of external audit work required and associated fee.

**18** I will continue to liaise with Internal Audit to agree the systems and the respective key controls where I may be able to place reliance on their work.

## Material systems

**19** Overall, I was able to obtain a good level of assurance from our systems work, with the majority of controls found to be working effectively.

**20** However, my work identified a small number of specific system weaknesses which are detailed below. For my opinion purposes I am satisfied that there are either compensating controls that would identify a material error arising in the accounts as a result of these weaknesses or I have increased our substantive testing at year end to address the risk. I am however reporting these control weaknesses to you as they could allow fraud or error and therefore need to be addressed.

## General ledger

**21** Standard new user and user removal forms for two employees could not be located by IT. This was due to the fact that the requests were made electronically and no audit trail was kept on file. Maintaining a complete audit trail of IT users is an important control as it ensures the Council has an up-to-date record of those users who have access to IT systems, and whether the access rights granted are appropriate for their role.

### Recommendation

**R1** Ensure that all new staff and leavers complete an appropriate IT form and this is retained on file.

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## Debtors

**22** Sales invoices which are in the process of being queried are not subject to the Council's invoice recovery procedures until the query is resolved. The department which first raised the invoice is responsible for resolving the dispute. However there are no formal controls in place for managing and monitoring the status of queries or processes in place to escalate the urgency of the queries if required. As a result there are some unpaid invoices that are over three years old which are still being disputed.

**23** There is a risk that the Council could lose control of disputed invoices or that an invoice could be held in dispute indefinitely and the payments not recovered.

### Recommendation

**R2** Put in place arrangements for formally tracking and monitoring all disputed debtor invoices.

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**24** Work on debtors also identified that although the aged debtors report is printed monthly, there is no evidence that it is reviewed. There is an expectation that it is the responsibility of the officer who raised the respective debtor to ensure that the money is collected in a timely manner. At the time of our review, there were several outstanding debts of more than 144 days old which have not been collected or written off.

**25** The review of the aged debtors report is an important control which the Council should implement more regularly as it aids the management of debt collection and determining the likely recovery of outstanding debt. This should be performed by one individual to ensure that an overall view of total outstanding debt is obtained.

### Recommendation

**R3** Review the aged debtors report on a monthly basis with a view to supporting the Council's debt collection arrangements and informing the recoverability of debt and associated year end doubtful debt provision.

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### Creditors

**26** Testing of creditors noted that for three purchase orders from a sample of 20, the purchase order was not formally agreed to the invoice and/or the delivery note. In addition, a number of delivery notes were missing or had not been signed as reviewed.

**27** Agreement of invoices to purchase orders and delivery notes is an important control as, when performed correctly, it ensures that the Council only pays for goods and services that it has received and ordered. It also ensures that correct amounts are coded to the right supplier.

**28** We also noted that for one sample, the invoice for a particular supplier had been coded to the wrong purchase order, despite being signed off as reviewed.

**29** The failures in this control have resulted in the need for additional substantive audit work on creditors as part of my final accounts audit. There is an opportunity for the Council to reduce fees in future by ensuring that such controls are in place and working effectively. This would reduce the substantive audit work required to compensate for control failures.

### Recommendation

**R4** Ensure that invoices agree to the respective purchase order and delivery note and that this check is evidenced through retention of a signed copy of the delivery notes.

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**30** For some suppliers we also noted that, due to the high number of orders that can be raised in a day, purchase orders are not raised on a per order basis through marketplace. Instead, a quarterly order is raised and authorised through marketplace as an estimate for the value of orders in the coming three months. However there are currently no procedures for reconciling the actual number of orders placed with suppliers during the quarter and the purchase order raised at the start of the quarter. Such a control will help to provide better estimates for future quarterly purchase orders and will provide management with an overview of how much money is actually being spent in a quarter and whether this is higher or lower than the estimate. Identification of such variances will also help to identify any unauthorised orders being placed.

### Recommendation

**R5** For those suppliers where a quarterly estimated purchase order has been raised, the Council should reconcile the actual number of orders placed with the original purchase order estimate and investigate any large variations.

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**31** Testing also noted that a works order for housing repairs was raised and authorised by the same officer, with no subsequent review of the works order by a separate senior officer. We acknowledge that this may occur in the rare case where the work required is sufficiently urgent and there are no senior officers available to review and authorise the order. Where this occurs in future, the Council must ensure that these work orders are reviewed and re-authorised by a senior officer at the first available opportunity.

### Recommendation

**R6** Ensure that a senior officer reviews and re-authorises work orders which have previously been raised and authorised by the same individual.

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## The way forward

**32** The Council should consider the recommendations set out in the action plan and take action to identify the weaknesses identified.

## Appendix 1 Action plan

### Recommendations

#### Recommendation 1

Ensure that all new staff and leavers complete an appropriate IT form and this is retained on file.

<b>Responsibility</b>	N/A
<b>Priority</b>	Medium
<b>Date</b>	N/A
<b>Agreed</b>	Agreed in principle
<b>Comments</b>	The Council has moved away from manual forms and adopted an electronic approach to IT requests. However, there are practical difficulties associated with keeping an audit trail of changes. In practice the risk is extremely low because of the small number of users and the ease of demonstrating that all access to the finance system is authorised.

#### Recommendation 2

Put in place arrangements for formally tracking and monitoring all disputed debtor invoices.

<b>Responsibility</b>	Assistant Chief Executive – Finance
<b>Priority</b>	Medium
<b>Date</b>	From September 2010
<b>Agreed</b>	Agreed
<b>Comments</b>	The monthly aged debtors review (referred to below) is the means by which this will be controlled.

#### Recommendation 3

Review the aged debtors report on a monthly basis with a view to supporting the Council's debt collection arrangements and informing the recoverability of debt and associated year end doubtful debt provision.

<b>Responsibility</b>	Assistant Chief Executive – Finance
<b>Priority</b>	Medium
<b>Date</b>	From September 2010
<b>Agreed</b>	Agreed
<b>Comments</b>	The aged debtors report is reviewed by the ACE-F every month. Evidence of this review will be retained.

#### Recommendation 4

Ensure that invoices agree to the respective purchase order and delivery note and that this check is evidenced through retention of a signed copy of the delivery notes.

<b>Responsibility</b>	N/A
<b>Priority</b>	High
<b>Date</b>	N/A
<b>Agreed</b>	Agreed in principle
<b>Comments</b>	Only a small proportion of transactions use Marketplace so the evidence sought by the auditors simply doesn't exist in most cases. The recommendation is not practical to implement until such time as a corporate procurement system has been implemented. Meanwhile there is adequate compensating control via the invoice certification process which requires a minimum of two officers to certify that the goods/services have been received.

#### Recommendation 5

For those suppliers where a quarterly estimated purchase order has been raised, the Council should reconcile the actual number of orders placed with the original purchase order estimate and investigate any large variations.

<b>Responsibility</b>	N/A
<b>Priority</b>	Low
<b>Date</b>	N/A
<b>Agreed</b>	Not agreed
<b>Comments</b>	The recommendation is not practical to implement and in any case the risk perceived by the auditors and the benefits arising from the recommendation are not considered to be significant. There is adequate compensating control through the budget monitoring process.

#### Recommendation 6

Ensure that a senior officer reviews and re-authorises work orders which have previously been raised and authorised by the same individual.

<b>Responsibility</b>	N/A
<b>Priority</b>	Medium
<b>Date</b>	N/A
<b>Agreed</b>	Not agreed
<b>Comments</b>	No payments are made without an invoice that has been properly certified by an independent officer. This provides adequate compensating control.

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