Colney Heath Parish Council

Internal Audit Report 2002-03 & 2003-04

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Background and Scope

Under the revised Accounts and Audit Arrangements implemented with effect from the financial year commencing 1 April 2001, all Parish Councils were required to implement an independent internal audit examination of their Accounts and accounting processes annually.

The Council appointed its former external auditors to undertake the review in 2001-02, but has not had any subsequent coverage, nor has a Statement of Accounts for 2002-03 or 2003-04 been prepared until the present time (November 2004). This has primarily been the result of work pressures on the former clerk, who has been replaced in recent months.

The newly appointed clerk approached us to undertake the internal audit review for both years and the following detailed report sets out our conclusions on areas examined as part of the internal audit certification process for both 2002-03 and 2003-04. Our review has included an examination of sample of transactions throughout the two years in order to gain sufficient assurance to 'sign-off' the Internal Audit Certificates in the Annual Return for both. That for 2003-04 will be "signed-off" at a later date, once the external auditors (Lubbock Fine) have signed off the 2002-03 Return.

Internal Audit Approach

In undertaking our review, we have and will continue to have regard to the materiality of transactions and their susceptibility to potential mis-recording or misrepresentation in the year-end Statement of Accounts. We will, once the adequacy of systems has bee subjected to initial review and confirmation as sound, employ selective sampling techniques, focusing on those areas where the Statement of Accounts indicates significant or material changes in income or expenditure levels between 2000-01 and 2003-04. All such variances have been discussed with the new Parish Clerk and suitable explanations been obtained wherever possible: we shall update our analytical review annually and apply the results in planning the audit approach.

The detailed report includes recommendations, where necessary, in each area of coverage required by the Annual Return. These are then summarised in an Action Plan at the end of the report and we recommend that the Clerk and members consider detail contained therein and, where deemed necessary, take appropriate steps to remedy any weaknesses or concerns identified.

The report is also available for presentation to Lubbock Fine, the Council's external auditors, who may also have access to our working paper file on request.

Overall Conclusion

We have identified a number of areas of significant concern with the manner in which the Statements of Accounts have been prepared in previous years, which indicate that the cumulative balance of funds available to the Council at the year-end have been understated in 2001-02 and previously.

Similarly, we have identified concerns with the manner in which accounting records have been maintained in previous years and also in 2002-03 and 2003-04.

Detailed Report

Maintenance of Accounting Records & Bank Reconciliations

The former clerk maintained the Council's accounting records in spreadsheet format, recording detail of transactions only on the Current bank account. No record detailing transactions on the Reserve Account, Capital Reserve Account, Wages Account or either of the two Map Accounts appear to have been formally recorded. Furthermore, the current account spreadsheets do not record detail of the opening balance for 2001-02.

The recently appointed clerk has prepared a revised current account cashbook, also preparing a cashbook for the Reserve and Capital Reserve Accounts for 2002-03 and 2003-04. We have checked the detail of these cashbooks for both 2002-03 and 2003-04 to the respective bank account statements and have identified a number of anomalies that have required amendment before the Statement of Accounts for either 2002-03 or 2003-04 can be finally prepared and submitted to the Council for adoption. Detail of the errors identified and amendments required have been provided to the clerk for his necessary action.

We note that the clerk intends to implement Sage accounting software for 2004-05, once the 2003-04 Statement of Accounts has been prepared and detail been finally agreed. We commend this approach, which should also provide the Clerk and Council with regular information on the financial position of the Council throughout the year, together with comparative budgetary information identifying the actual spend against the planned budget.

No movement has occurred on the two Map accounts in the past two years, other than the addition of £3.24 and £7.27 interest on the Map Reserve Account in 2002/03 and 2003/04 respectively. The wages bank account has been funded generally each month by cheques drawn on the current account to the value of the cheques drawn on the wages account for non-office staff: this has not however always been the case and in both years some wages expenditure has been met from the balance held in the wages account.

We do not consider that there is any need to retain any of these three accounts and would suggest that the Council transfers the residual balances on the each of the accounts back into the current account: any future cheques required being drawn from that account. Similarly, members should consider the ongoing need for retention of both the Reserve and Capital Reserve accounts.

The overall cash balance held in the Council's bank accounts exceeds £80,000 at the end of each of the last three financial years, combined balances on the two Reserve Accounts alone being in excess of £100,000 for significant periods of each of the last two financial years. Interest totalling marginally in excess of £2,000 has been obtained in each of the past two years, which equates to a return of only some 2% on the average balance on the two Reserve Accounts in each year. Experience at other councils, has shown that higher interest rates can in most cases be obtained by placing surplus funds in Treasury term-deposit accounts where, with the balances available for most of the year, interest rates of 4% and above would be obtainable on monthly deposits: a higher return may well be obtained by placing sums in term deposits for lengthier periods.

In verifying the true cashbook balances and reconciling them to bank accounts at the start of the 2001-02 financial year, we noted that the Balance Sheet recorded on the Statement of Accounts for 2001-02 (and comparative information for 1999/00) included neither the Wages Account nor two Map Account balances, thereby understating both the cash at bank and general fund balances available to the Council. We note that this had also been identified by the external auditors and referred to on the Annual Return certificate for 2001-02.

The present clerk has, in entering detail on the Excel spreadsheet not made full use of the spreadsheet's potential, entering financial detail in "text" format rather than numerical. Consequently, the spreadsheets in use have not provided total information at the close of each quarter or at the year-end.

We have checked and agreed detail of the cashbook entries for the two years to both bank statements and invoices held on the invoice-processing file. In carrying out this check, we have identified a number of transposition errors in the detail as recorded. The manner in which the detail has been entered has resulted in our working with the clerk to re-enter all financial detail to ensure that the information recorded agrees with the detail of actual payments charged to the Council's accounts by the bank and also, are supported by appropriate invoices or other form of supporting documentation (see "Review of Payments" below.

One issue we would draw specific attention to relates to the manner in which direct debits have been entered in the cashbooks. Our experience at other councils has shown that service companies do not always charge clients' accounts with the same values as identified on the invoices sent out in advance of the due date for debiting funds from councils' account. Similar situations have been identified in both 2001-02 and 2002-03 for the Council and we would therefore suggest that direct debits (and any Standing Orders) are only entered in cashbooks once bank statements have been received and the actual amount charged can be identified and matched to the invoice received.

Having verified the accuracy of the transactions in the cashbooks prepared by the clerk for both financial years, we have prepared a summary bank reconciliation at each financial year-end including detail of opening balances, receipts and payments during both years: these have been successfully agreed to the Council's bank statements.

Recommendations

R1. Standard accounting practice requires that a formal cashbook be maintained for each bank account in operation, identifying the opening balance on each account, together with detail of all receipts payments and inter account transfers.

R2. *In order to ensure that transactions are entered accurately, the spreadsheet cashbook should be entered in numerical, not text format, with totals and check totals being calculated using the spreadsheet's full capacity.*

R3. *Consideration should be given to the rationalisation of the Council's bank accounts, as there appears to only be a need for a current and high interest earning account.*

R4. *Consideration should also be given to placing surplus funds in high interest monthly (or longer) Treasury term deposit accounts, thereby increasing the income received from bank interest.*

R5. *In order to ensure the accuracy of entry of transactions during the course of the year, we would suggest that the spreadsheets are balanced at the end of each quarter (as a minimum), although ideally they should be balanced at the end of each calendar month.*

R6. *Following on from R5, a formal reconciliation of the quarter/month-end cashbook balances to the bank statements should be prepared.*

Review of Regulatory Framework

We understand from the clerk that the Council's Standing Orders have not been reviewed or revised recently. There has been a wealth of legislative changes in the last couple of years including, inter alia, the revised Members Code of Conduct, Freedom of Information Act and revisions to the Accounts and Audit Arrangements in recent years. NALC has produced a model format for Standing Orders and we would commend this document as a suitable baseline for the Council to review and update its extant documentation.

Similarly, good accounting practice suggests that all bodies, including councils, should develop and adopt a formalised approach to management of their financial affairs. As with the Standing Orders, NALC has developed a model set of Financial Regulations for councils and we would suggest that these are used by the Council as the basis for development of their own financial regulatory framework.

In order to assist the Council and clerk, we have provided the clerk with an electronic copy of the NALC model documents and would urge the Council to apply these documents to meet their own requirements.

We have examined the Council's minutes for both 2002-03 and 2003-04 to ensure that no issues exist or are developing that may have an adverse affect on the Council's financial stability either currently or in the foreseeable future. We are pleased to record that no significant issues appear to exist at present, although we note that the Council does not appear to consider the relevant powers applying for approval of each grant and donation payment made. The S.137 "free resource" can only be applied when the Council has no specific powers to provide assistance to groups or local bodies and should only then be used for the benefit of the local population.

Recommendations

R7. *The Council should re-examine its extant regulatory framework and update it in line with the model Standing Orders and Financial Regulations issued recently by NALC.*

R8. *When considering applications for payment of grant aid and donations, the Council should satisfy itself that the relevant powers exist, those powers being formally identified in the minutes for each approval granted.*

Review of Payments

We have reviewed all payments made throughout 2002-03 and 2003-04 to ensure that the following criteria were met: -

- Payments were supported by a trade invoice or acknowledgement of receipt. ***A number of payments in the two years were not supported by either trade invoices or proformas certified by the Council's Chairman approving the payment. Whilst appreciating that the clerk has experienced a number of difficulties in finding and identifying all appropriate supporting documentation, we would expect to see an appropriately certified invoice or other form of supporting document in respect of each and every payment made during the course of the financial year.***
- VAT has been calculated correctly and is recovered at appropriate intervals. ***A number of errors were identified in the value of VAT identified on the cashbooks prepared by the clerk and no reclaim appears to have been submitted covering either 2002-03 or 2003-04, although we note that the clerk has deferred submission pending completion of our audit review.***
- The Council at a Council meeting approved each payment. ***We note that the new clerk has introduced (in January 2004) a system for reporting payments for each month to the Council for ratification.***
- Payments have been correctly analysed in preparation of the year-end Statement of Accounts. ***Following our revisions to the cashbook detail (see "Maintenance of Accounting Records" above), the clerk has prepared a full analysis of payments for the two years. We have reviewed the detail and, subject to one or two minor amendments have agreed the detail).***
- Purchases have been correctly analysed as capital or revenue acquisitions in the year. ***As above.***
- Section 137 payments have been identified in the cashbook and are within the Council's spending limit. ***A separate column has been used to identify Section 137 grants and donations, etc. Detail has been agreed.***

Recommendations

R9. *All payments should be fully supported by either a traders invoice or a proforma invoice certified by the Chairman approving the payment.*

R10. Care should be taken to ensure that, where invoices for services paid for by direct debit are received, the actual payment matches the invoice detail: any anomalies should be followed up with the supplier.

Assessment and Management of Risk

We note that the minutes make regular references to the completion of risk assessments at the Council's various sites. We also note the production of a risk assessment by the Council in early 2003. This provides a suitable initial basis on which the Council can further develop its approach to risk assessment and management.

In order to further assist the process, we have provided the clerk with a risk assessment format produced by another council, which may also be of assistance in developing the Council's own formalised document. Additionally, the Council may be interested to note the existence of specific risk software developed by a company in the north of England – DMH Solutions Ltd. A number of our clients, including Kings Langley PC, have purchased the software and we would commend it as a suitable medium for use by the Council in developing their own formalised approach to risk assessment and management.

Zurich Municipal Insurers provide the Council with insurance cover: examination of the policy documents and schedule indicates that an appropriate level of cover generally exists for the Council's needs. We note the current level of Fidelity Guarantee cover (£100,000), which we consider appropriate given the Council's average cash at bank balance over the two years under review.

However, whilst no precise formula exists for the calculation of the appropriate level of fidelity cover, we consider that good practice would be represented by assessing the likely average cash balance for the following year and setting cover at that level: this should be subject to annual review and adjustment in order to ensure that the Council is neither over nor under-insured.

Recommendations

R11. The Council should undertake a regular review of its risk assessments to ensure that all potential risks have been identified and that they are subjected to routine examination and re-evaluation. We would also suggest that, given the number of Council managed sites and diversity of service provision, consideration be given to the acquisition of the bespoke software referred to in the body of our report.

R12. The current level of fidelity guarantee cover should be reviewed annually and be adjusted to provide cover in line with the anticipated average cash balance during the course of the following year.

Budgetary Control and Reserves

The Council's minutes confirm that the budget and precept for 2004-05 have been formally discussed and agreed by the Council, following consideration of a detailed assessment of the Council's spending requirements for the forthcoming year. We note that the Council agreed a precept level of £114,500 for 2004-05.

Examination of the minutes indicates that members receive no information detailing actual spending against that planned for the year, although we note that the new clerk has started to report bank balances to the monthly meetings. In order to ensure that members are kept aware of the Council's full financial position and actual spending against that planned, a regular update setting out the actual spend to date in the financial year against the approved budget should be provided: this should, as a minimum be reported at quarterly intervals.

The Council minutes provide no indication that the Council has established specific earmarked reserves to provide funding for items such as equipment replacement; election costs; building repairs or other potential development areas that will require future funding. However, we understand from the clerk that "Common" and "Building" funds have been established: we would suggest that the level of these funds should be examined annually to ensure that an appropriate amount is held in the reserves to meet the Council's planned areas of spending.

The year-end 2003-04 General Fund balance of £69,000 equates to some six month's net revenue spending and, as such, is considered adequate to meet the Council's routine spending requirements, especially given the availability of additional funds in the above mentioned reserve funds.

Recommendations

R13. The Council should receive regular financial reports identifying actual spending during the course of the financial year compared with the approved budget.

Review of Income

The Council receives income from a variety of sources annually. Due to difficulties experienced with the accuracy of accounting records, we have not had an opportunity to examine the detail systems of control over the various sources in existence. We shall include an examination of this detail as a priority area for our first interim visit in 2004-05.

We have however undertaken an analytical analysis of the various income sources, no significant anomalies being identified.

We did however notice that the Accounts for 2001-02 make reference to a capital receipt of £14,190 in 2000-01, presumably from the sale of land, a building or Council owned equipment. Local Government accounting requires that all such capital receipts may only be applied on future capital spending or repayment of loan debt: they may not be used to meet routine revenue spending.

It is not apparent from the Council's Accounts for 2001-02 and subsequently whether or not a specific Capital receipts Reserve has been established to control this income and ensure that it is only applied in accordance with extant legislation.

Recommendation

R14. The Council should ensure that a Capital receipts Reserve is established based on the original capital receipt in 2000-01, reduced by any subsequent permissible capital spending.

Petty Cash Account

We note that a petty cash account is in operation, although no formal records detailing the nature of spending have been maintained. Monthly cash of £100 is drawn from the current bank account to provide funding for all ad hoc expenditure.

It is essential that a formal record is maintained identifying the nature of all petty cash expenditure incurred and that till receipts, trade invoices, etc. are retained for audit inspection. We would also suggest that in order to simplify the process of analysing expenditure accurately, rather than just regard it as "petty cash expenses", the petty cash account is operated on an imprest system with a fixed balance of say £100. As and when required, the actual expenditure incurred should then be reimbursed exactly by cheque drawn on the bank account.

Recommendations

R15. A formal record identifying the nature of expenditure from petty cash should be maintained, also detailing the cash advances received from the bank account.

R16. Appropriate documentation should be obtained and retained to support all expenditure from the petty cash account.

R17. In order to simplify accounting and ensure that petty cash expenditure is correctly analysed to the appropriate budget heading, we recommend that the account be operated on an imprest basis, which is then topped up to the agreed level by cheque equating to the exact amount expended in the period.

Salaries and Wages

We have not had an opportunity to look at the payroll documentation in any great detail due to time constraints arising from the need to ensure that a formal and meaningful Statement of Accounts was prepared for both 2002-03 and 2003-04 for adoption by the Council and completion of and submission to external audit of the Annual Returns for both years.

Notwithstanding that, we note that the new clerk has undertaken a full review of the payrolls for both years and identified a number of anomalies that he has either already addressed or is in the process of addressing. We have additionally carried out a perfunctory review of the documentation available for 2003-40 and noted a number of anomalies ourselves where tax deductions have been made, but the total deduction for the year does not appear to correlate to the total tax due applying the tax code detail that we have been provided with. Additionally one member of staff (RP) appears to have been paid for 54 weeks work in 2003-04.

We have provided the clerk with detail of these anomalies and would suggest that the clerk needs to re-examine the tax position in greater detail to ensure that the annual return detail provided to Inland Revenue is accurate and that the appropriate tax deductions have been made for each employee.

We also noted some apparent anomalies on the National insurance deductions and contributions made for certain employees and would suggest that the detail of these is re-examined.

We also note the Clerk's intention to use the Sage payroll software in future to prepare the necessary payroll documentation: Sage is an acknowledged leader in the preparation of payrolls and we see this as a positive step forwards, which should, provided the correct baseline information is input when the system is set-up, ensure that the payroll calculations are effected more accurately than appears t have been the case hitherto.

We shall undertake a more detailed review of the payroll system and detailed calculations as part of our 2004-05 internal audit coverage in order to ensure that the system is now working effectively and accurate detail is being produced, with the resultant payment of the correct salaries and wages to staff.

Recommendations

R18. The clerk should revisit the payroll calculation detail for 2003-04 (and, if time permits, 2002-03) to ensure that the detail is accurate and that the appropriate tax and national insurance deductions and contributions have been calculated and paid over to Inland Revenue.

R19. The Council should proceed with the implementation of the Sage payroll system as soon as is practicable and physically possible.

R20. The clerk and Council should identify the true extent of any overpayments that may have occurred in 2002-03 and 2003-04and take appropriate action to either write off or recover any that are identified.

Asset Registers

No formal asset register is in place despite the fact that, we understand from the clerk, the Council has a wide range of assets for which it is responsible. The 1996 Accounts and Audit Regulations required all councils to establish and maintain a formal asset register.

Such an asset register should serve as a record of **all** land, premises, property and equipment owned by the Council. Ideally, it should also identify the following basic information and would best be recorded on a spreadsheet, so that the annual movement in values as recorded on the insurance schedule may be revised accordingly on the register:

- Date of acquisition
- Detail of item
- Position where item is stored or fixed
- Serial number
- Purchase cost
- Current year insurance value (if insured)
- Disposal date

By inclusion of this detail in the register for all assets owned, including land, buildings, plant, machinery, furniture and equipment, the Council has a permanent record, which serves as a sound source for provision of information to the insurance company and/or police in the event of any need to make an insurance claim. It also provides the Council and us with an easy source for verifying the accuracy and completeness of the insurance schedule detail.

We would also suggest that, in order to assist in the pursuance of any insurance claim that may arise, a photograph (ideally in digital format) of all the assets owned should be taken and held to support any claims that may be necessary.

Recommendation

R21. The Council should comply with the terms of the 1996 Accounts and Audit Regulations and ensure that a formal register identifying ***all*** *fixed assets is established and maintained: the register should provide full detail (where available) as outlined in the body of the report.*

R22. The Asset Register should be reviewed and updated annually to include detail of new assets acquired and also of those disposed.

Investments and Loans

The Council currently holds surplus funds in Business and Capital Reserve accounts with its bankers. These do not attract a particularly high interest rate and, given the level of funds available for possible "short-term investment", we would suggest that the Council discusses the best potions available with its bankers. Based on our experience at other councils, we would anticipate that a return in excess of 3.5% should be available on investment of say £50,000 in monthly Treasury term-deposits through the bank.

Recommendations

R23. The Council should investigate the best form of investment for surplus funds to ensure that interest earned is maximised.

Statement of Accounts and Annual Return

We have indicated earlier in this report the level of support that we have provided to the new clerk in clarifying the detail of transactions during 2002-03 and 2003-04 in order to produce a meaningful and accurate set of Account s Statements for both years.

Consequently, no issues have arisen from our work on the Statements that have not been referred to previously. We have also assisted the clerk in identifying the appropriate detail for entry onto each year's Annual Return.

We note that the clerk is intending to enter the 2004-05 transactions onto Sage accounting software, which should assist in the process of preparing the year-end Statement of Accounts.

We shall review progress on the implementation of the software at our interim visit for 2004-05 and report our conclusions accordingly.

No specific issues arise on the 2002-03 or 2003-04 Statement of Accounts and Annual Returns not mentioned earlier in this report.

Action Plan

Rec. No.	Recommendation	Response
Review of Accounting Arrangements and Bank Reconciliations		
R1	Standard accounting practice requires that a formal cashbook be maintained for each bank account in operation, identifying the opening balance on each account, together with detail of all receipts payments and inter account transfers.	
R2	In order to ensure that transactions are entered accurately, the spreadsheet cashbook should be entered in numerical, not text format, with totals and check totals being calculated using the spreadsheet's full capacity.	
R3	Consideration should be given to the rationalisation of the Council's bank accounts, as there appears to only be a need for a current and high interest earning account.	
R4	Consideration should also be given to placing surplus funds in high interest monthly (or longer) Treasury term deposit accounts, thereby increasing the income received from bank interest.	
R5	In order to ensure the accuracy of entry of transactions during the course of the year, we would suggest that the spreadsheets are balanced at the end of each quarter (as a minimum), although ideally they should be balanced at the end of each calendar month.	
R6	Following on from R5, a formal reconciliation of the quarter/month-end cashbook balances to the bank statements should be prepared.	
Review of Regulatory Framework		
R7	The Council should re-examine its extant regulatory framework and update it in line with the model Standing Orders and Financial Regulations issued recently by NALC.	
R8	When considering applications for payment of grant aid and donations, the Council should satisfy itself that the relevant powers exist, those powers being formally identified in the minutes for each approval granted.	

Rec. No.	Recommendation	Response
Review of Payments		
R9	All payments should be fully supported by either a traders invoice or a proforma invoice certified by the Chairman approving the payment.	
R10	Care should be taken to ensure that, where invoices for services paid for by direct debit are received, the actual payment matches the invoice detail: any anomalies should be followed up with the supplier.	
Assessment and Management of Risk		
R11	The Council should undertake a regular review of its risk assessments to ensure that all potential risks have been identified and that they are subjected to routine examination and re-evaluation. We would also suggest that, given the number of Council managed sites and diversity of service provision, consideration be given to the acquisition of the bespoke software referred to in the body of our report.	
R12	The current level of fidelity guarantee cover should be reviewed annually and be adjusted to provide cover in line with the anticipated average cash balance during the course of the following year.	
Budgetary Control & Reserves		
R13	The Council should receive regular financial reports identifying actual spending during the course of the financial year compared with the approved budget.	
Review of Income		
R14	The Council should ensure that a Capital receipts Reserve is established based on the original capital receipt in 2000-01, reduced by any subsequent permissible capital spending.	

Rec. No.	Recommendation	Response
Petty Cash Account		
R15	A formal record identifying the nature of expenditure from petty cash should be maintained, also detailing the cash advances received from the bank account.	
R16	Appropriate documentation should be obtained and retained to support all expenditure from the petty cash account.	
R17	In order to simplify accounting and ensure that petty cash expenditure is correctly analysed to the appropriate budget heading, we recommend that the account be operated on an imprest basis, which is then topped up to the agreed level by cheque equating to the exact amount expended in the period.	
Salaries and wages		
R18	The clerk should revisit the payroll calculation detail for 2003-04 (and, if time permits, 2002-03) to ensure that the detail is accurate and that the appropriate tax and national insurance deductions and contributions have been calculated and paid over to Inland Revenue.	
R19	The Council should proceed with the implementation of the Sage payroll system as soon as is practicable and physically possible.	
R20	The clerk and Council should identify the true extent of any overpayments that may have occurred in 2002-03 and 2003-04and take appropriate action to either write off or recover any that are identified.	
Asset Registers		
R21	The Council should comply with the terms of the 1996 Accounts and Audit Regulations and ensure that a formal register identifying <u>**all**</u> fixed assets is established and maintained: the register should provide full detail (where available) as outlined in the body of the report.	
R22	The Asset Register should be reviewed and updated annually to include detail of new assets acquired and also of those disposed.	
Investments and Loans		
R23	The Council should investigate the best form of investment for surplus funds to ensure that interest earned is maximised.	