

CARLISLE CITY COUNCIL

Report to:- **The Mayor and Members of The City Council**

Date of Meeting:- **27 April 2004**

Agenda Item No:-

Public

Policy

Delegated Yes

Accompanying Comments and Statements

Required

Included

Environmental Impact Statement:

No

No

Corporate Management Team Comments:

No

No

Financial Comments:

Yes

Yes

Legal Comments:

No

No

Personnel Comments:

No

No

Impact on Customers:

No

No

Title:-

SAS 610 STATEMENT (FINAL ACCOUNTS 2002/03)

Report of:-

The Head of Finance

Report reference:-

FS3/04

Summary:-

There is a new requirement that the Audit Commission is required to prepare a report following the end of the annual audit in accordance with the Statement of Auditing Standard (SAS) 610. The SAS 610 report, which must be considered by those charged with Corporate Governance, is attached and details the unadjusted misstatements for 2002/03.

Once the SAS 610 has been approved the next step is to approve the amended Statement of Accounts for 2002/03, which is considered next on the Council agenda.

Recommendation:-

Council is requested to approve the SAS 610 report.

Contact Officer: Angela Brown

Ext: 7299

Note: in compliance with section 100d of the Local Government (Access to Information) Act 1985 the report has been prepared in part from the following papers: None

CITY OF CARLISLE

To: The Mayor and Members of
The City Council
27 April 2004

FS3/04

SAS 610 STATEMENT
(FINAL ACCOUNTS 2002/03)

1. INTRODUCTION

- 1.1 There is a new requirement that the Audit Commission is required to prepare a report following the end of the annual audit in accordance with the Statement of Auditing Standard (SAS) 610. The SAS 610 report, which must be considered by those charged with Corporate Governance, is attached and details the unadjusted misstatements for 2002/03. Council must approve this report before the Audit Commission can sign off the accounts and issue their Audit certificate and opinion.
- 1.2 Corporate Resources Overview and Scrutiny Committee received a presentation on the SAS 610 statement on 1 April 2004 from the Audit Commission and, following a number of queries, they referred the approval of the statement to full Council to be considered alongside the amended Statement of Accounts for 2002/03.

2. SAS 610 STATEMENT – MAIN ISSUES ARISING

- 2.1 The summary of unadjusted errors listed in Appendix 2 of the SAS 610 statement which I have recommended are not adjusted in the Statement of Accounts for 2002/03 relate to the treatment of costs associated with the LSVT transfer. Following discussions between the Audit Commission, the ODPM and ourselves, the Audit Commission have accepted the Council's position regarding these costs.

3. NEXT STEPS

If the Council approve the non-adjusted errors contained within the SAS 610 statement then the next step is to approve the final Statement of Accounts for 2002/03 which is considered next on the Agenda. This incorporates all of the material misstatements that have been agreed to be adjusted between the Head of Finance and the Audit Commission.

4. RECOMMENDATION

Council is requested to approve the SAS 610 report.

ANGELA BROWN
Head of Finance

Contact Officer: Angela Brown

Ext: 7299

Communication concerning
financial statements to those
charged with governance

Carlisle City Council

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- Summary of unadjusted misstatements

Reference:	SAS 610 Carlisle City Council
Date:	April 2004

Introduction

The Council is responsible for the preparation of financial statements that present fairly its financial position as at 31 March 2003 and its income and expenditure in the year then ended. We are responsible for undertaking an audit and reporting whether in our opinion the Council's financial statements do present fairly its financial position and income and expenditure.

The Council is responsible for the preparation of a Statement of Internal Control in accordance with the provisions of the Code of Practice on Local Authority Accounting in the United Kingdom: a Statement of Recommended Practice. We are required to report where we become aware in the course of our audit of inconsistencies with the disclosures made by the Council.

The Council submitted draft financial statements to us on 10 September 2003 and we have now substantially completed our audit of those statements. This report details key matters arising from our audit that we must communicate to those charged with governance prior to giving an opinion on those financial statements.

Background

A revised Statement of Auditing Standards (SAS), SAS 610 Reporting to those charged with governance – is applicable for the first time to the audit of the Council's accounts. It requires auditors to report to those charged with governance (as distinct from management) certain matters before they give an opinion on the financial statements:

Auditors should communicate to those charged with governance:

- a. expected modifications to the auditors' report;*
- b. unadjusted misstatements;*
- c. material weaknesses in the accounting and internal control systems identified during the audit;*
- d. their views about the qualitative aspects of the entity's accounting practices and financial reporting;*
- e. matters specifically required by other Auditing Standards to be communicated to those charged with governance; and*
- f. any other relevant matters relating to the audit.*

We agreed with the Council that the communications required by SAS 610 in advance of issuing our report on the annual financial statements of the Council would be with the Corporate Resources Overview and Scrutiny Committee.

We have considered each of the areas listed above and our views are set out below together in this first year with explanations of the issues that we are responding to.

Auditor's report

The standard requires that we report to those charged with governance any proposed modifications to our report on the financial statements. The standard explains the reasons for this requirement:

Auditors discuss expected modifications to the auditors' report on the financial statements with those charged with governance to ensure that:

- *those charged with governance are aware of the proposed modification and the reasons for it before the report is finalised;*
- *there are no disputed facts in respect of the matter(s) giving rise to the proposed modification (or that matters of disagreement are confirmed as such); and*
- *those charged with governance have an opportunity, where appropriate, to provide the auditors with further information and explanations in respect of the matter(s) giving rise to the proposed modification.*

On the basis of our audit work we do not currently intend to issue a non-standard report on the Council's financial statements. A draft report is attached at Appendix 1.

Delayed Opinion

Our annual audit letter drew attention to our decision to delay our opinion on the Authority's 2002/03 statement of accounts in order to allow officers more time to respond to matters raised in connection with the accounting treatment of income and costs associated with the transfer of the Authority's housing stock to Carlisle Housing Association Limited.

Central to these issues were our concerns over the extent to which the capital receipt generated by the transfer could, under existing statutory provisions and guidelines, be applied to meet revenue expenditure associated with the transfer. Specifically the items of expenditure concerned were those relating to:

- the accounting treatment afforded to contributions made by the Authority in respect of the accrued pension fund deficit attributable to staff transferring to Carlisle Housing Association; and
- the Authority's administrative costs of and incidental to the transfer.

Following further communications between the ODPM, the Authority and ourselves we have accepted the treatment of the main deductions from the capital receipt and the accounts have been amended to properly reflect the capital nature of the transactions. However, whilst we have accepted the overall position is materially correct, members should be aware of the need to ensure proper compliance with the capital finance regulations in order to avoid future delays in the certification of the accounts or potential qualification.

Unadjusted misstatements

We are required to report to you all misstatements other than those of a clearly trifling nature. A trifling error is an entirely inconsequential error, whether taken individually or in aggregate and whether judged by any quantitative and/or qualitative criteria.

Our audit identified a number of misstatements in the financial statements which management has decided not to adjust. We have included as Appendix 2 to this report

the list of unadjusted misstatements. These relate to less significant items and presentational issues which will be addressed in the 2003/04 financial statements.

Material weaknesses in accounting and internal control systems

We have limited responsibilities to report to you weaknesses in accounting systems and systems of internal control identified in the course of our audit. SAS 610 provides:

A material weakness in the accounting and internal control systems is a deficiency in design or operation which could adversely affect the entity's ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements. Auditors normally do not need to communicate information concerning a material weakness of which those charged with governance are aware and in respect of which, in the view of the auditors, appropriate corrective action has been taken, unless the weakness is symptomatic of broader weaknesses in the overall control environment and there is a risk that other material weaknesses may occur. Material weaknesses of which the auditors are aware are communicated where they have been corrected by management without the knowledge of those charged with governance.

We have a duty to report adjusted errors in financial statements where they are relevant to your wider governance responsibilities.

Our audit did not identify any weaknesses in accounting and internal control systems other than those of which you are aware and in respect of which appropriate corrective action is being taken.

You should be aware that we do not provide a comprehensive statement of all weaknesses that may exist in the accounting and internal control systems or of all improvements that may be made, but have addressed only those matters that have come to our attention as a result of the audit procedures performed.

Qualitative aspects of accounting practices and financial reporting

SAS 610 places specific duties on auditors to report their assessment of qualitative aspects of accounting practices and financial reporting to those charged with governance:

In the course of their audit of the financial statements, auditors consider the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the financial statements. Auditors discuss in an open and frank manner with those charged with governance the auditors' views on the quality and acceptability of the entity's accounting practices and financial reporting. Such discussions may include:

- *the appropriateness of the accounting policies to the particular circumstances of the entity, judged against the objectives of relevance, reliability, comparability and understandability but having regard also to the need to balance the different objectives and the need to balance the cost of providing information with the likely benefit to users of the entity's financial statements;*

- *auditors explain to those charged with governance why they consider any accounting policy not to be the most appropriate, and request those charged with governance to make appropriate changes. If those charged with governance decline to make the changes on the grounds that the effect is not material, the auditors inform them that they will consider qualifying the auditors' report as soon as the effect of not using the most appropriate policy can reasonably be expected to influence the economic decisions of users of the financial statements.*
- *the timing of transactions and the period in which they are recorded;*
- *the appropriateness of accounting estimates and judgments, for example in relation to provisions, including the consistency of assumptions and degree of prudence reflected in the recorded amounts;*
- *the potential effect on the financial statements of any uncertainties including significant risks and exposures, such as pending litigation, that are required to be disclosed in the financial statements;*
- *material uncertainties related to events and conditions that may cast significant doubt on the entity's ability to continue as a going concern;*
- *the extent to which the financial statements are affected by any unusual transactions including non-recurring profits and losses recognised during the period and the extent to which such transactions are separately disclosed in the financial statements;*
- *apparent misstatements in the other information in the document containing the audited financial statements or material inconsistencies between it and the audited financial statements;*
- *the overall balance and clarity of the information contained in the annual report;*
- *disagreements about matters that, individually or in aggregate, could be significant to the entity's financial statements or the auditors' report. These communications include consideration of whether the matters have, or have not, been resolved and the significance of the matters.*

We have carefully considered the qualitative aspects of the Council's accounting practices and financial reporting. No matters have come to our attention that we would wish to draw to the attention of those charged with governance.

Matters required by other auditing standards to be reported to those charged with governance

Other auditing standards require us to communicate with you in other specific circumstances including:

- where we suspect or detect fraud, even if the potential effect is not material to our audit of the financial statements
- in respect of the conclusion that the Council is a going concern
- where there is an inconsistency between the Council's financial statements and other information in documents containing the financial statements.

We have identified no such matters in the course of our audit.

Other matters

There are no other matters that we wish to draw to your attention.

Next steps

You need to determine whether or not you will adjust the financial statements of the Council in respect of the misstatements and/or the qualitative aspects of financial reporting identified above.

Should you chose not to do so, we are required by SAS 610 to request from you a letter of representation explaining why you are not going to adjust the financial statements. We ask that the letter specifically details the misstatements and/or qualitative aspects of reporting to which it relates, either in the body of the letter or in a document appended to it.

Status of this report to the Council

This report is prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. It is prepared by appointed auditors and addressed to Members of the Council. It is prepared for the sole use of the audited body, and no responsibility is taken by auditors to any Director or officer in their individual capacity, or to any third party.

Draft auditor's report

Draft Independent Auditor's Report to Carlisle City Council

I have audited the financial statements on pages 1 to 55 which have been prepared in accordance with the accounting policies applicable to local authorities as set out on pages 11 to 16. This report is made solely to Carlisle City Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 54 of the Statement of Responsibilities of Auditors and of Audited Bodies, prepared by the Audit Commission.

Respective Responsibilities of the Chief Financial Officer and Auditor

As described on page 56 the Chief Financial Officer is responsible for the preparation of the financial statements in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2002: A Statement of Recommended Practice. My responsibilities, as independent auditor, are established by statute, the Code of Audit Practice issued by the Audit Commission and my profession's ethical guidance.

I report to you my opinion as to whether the financial statements present fairly the financial position of the Council and its income and expenditure for the year

I review whether the statement on page 57 reflects compliance with the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom 2002: A Statement of Recommended Practice. I report if it does not meet the requirements specified by CIPFA/LASAAC or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider whether the statement on internal financial control covers all risks and controls, or to form an opinion on the effectiveness of the authority's system of internal financial control. My review is not performed for any purpose connected with any specific transaction and should not be relied upon for any such purpose.

I read the other information published with the statement of accounts and consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the statement of accounts.

Basis of audit opinion

I conducted my audit in accordance with the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission, which requires compliance with relevant auditing standards issued by the Auditing Practices Board.

An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the council in the preparation of the financial statements, and of whether the accounting policies are appropriate to the council's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion, I evaluated the overall adequacy of the presentation of the information in the financial statements.

Opinion

In my opinion the financial statements present fairly the financial position of Carlisle City Council as at 31 March 2003 and its income and expenditure for the year then ended.

Certificate

I certify that I have completed the audit of the accounts in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

Summary of Unadjusted Errors:- Consolidated Revenue Account, Balance Sheet and Collection Fund.

Our audit has identified the following misstatements in the financial statements which management has decided not to adjust

Consolidated Revenue Account (CRA)/ General Fund Balances

- (A) £166,818cr - transfer from Housing Revenue Account (HRA) to General Fund (GF) *Careline* income attributable to GF user groups
- Less
- (B) £151,472dr - transfer from HRA to GF *Careline* costs attributable to GF user groups
 - (C) £446,287dr - overstatement of costs financed from the LSVT receipt, relating to items reported as earmarked reserves as at 31 March 2004, but which have not yet been defrayed or incurred either by way of a cash payment, accrual or appropriately recognised provision. Of this amount £292,000 relates to amounts set aside to meet the cost of environmental warranties insurance (insurance premium for years 13 to 25) with the balance of £154,287 represented by amounts set aside from the capital receipt to meet possible future costs associated with non environmental warranties, included in the transfer contract, but not covered by existing insurance arrangements. This potential overstatement of the General Fund balance is matched by a corresponding understatement in value of reserved capital receipts (capital financing reserve)

Net impact of non trivial unadjusted errors £430,941 (GF balance overstated). The net impact of all identified unadjusted errors on the General Fund balances is £404,372 (overstatement of balance carried forward at 31 March 2003).

Other adjustments to the Consolidated Revenue Account not impacting on General Fund Balances

Net Cost of Services

- (D) HRA Income - £70,465dr - overstatement of HRA subsidy income (overstatement of Major Repairs Allowance (MRA) element)
- (D) Housing General Fund Expenditure - £70,465dr - write-off of deferred charges expenditure associated with the excess of the Major Repairs Reserve balance paid to Carlisle Housing Association (CHA) over the actual MRA receivable for 2002/03
- (E) Cultural, Environmental and Planning Services - £400,027cr - overstatement of capital charges in respect of Tullie House Museum and the Millennium Gallery
- (F) Service Expenditure (various) - £120,505cr - estimated overstatement of depreciation (overstatement of expenditure) arising from inclusion of non depreciable land within depreciation calculations

Transfers to/from the Major Repairs Reserve

- (D) £70,465cr - adjustment to appropriations to/from the CRA (HRA) in respect of adjustments made to HRA subsidy receivable

Asset Management Revenue Account

- (E) £400,027dr - overstatement of capital charges (notional interest) relating to Tullie House/Millennium Gallery
- (F) £120,505dr /£120,505cr - potential overstatement of depreciation arising from the inclusion of non depreciable land in depreciation calculations (estimate based on assumption of 20% of valuations being attributable to land)

Less

- (G) £89,488cr - overstatement of depreciation on Tullie House/Millennium Gallery

Contributions to/from CFR

- (G) £89,488dr - overstatement of depreciation on Tullie House/Millennium Gallery
- (F) £120,505dr - estimated overstatement of depreciation arising from inclusion of non depreciable land in depreciation calculations

Less

- (D) £70,465cr - reversal of amounts written off to the CRA in respect of deferred charges expenditure associated with the excess of the amounts paid to Carlisle Housing Association in respect of the residual balance on the Major Repairs Reserve over the value of Major Repairs Allowance (MRA) receivable in 2002/03

Balance Sheet**Other Land and Buildings**

- (G) £89,488dr - overstatement of depreciation on Tullie House/Millennium Gallery
- (F) £120,505dr - estimated overstatement of depreciation arising from inclusion of non depreciable land in depreciation calculations

Capital Financing Reserve

- (G) £89,488cr - overstatement of depreciation on Tullie House/Millennium Gallery
- (F) £120,505cr - estimated overstatement of depreciation charged to service revenue accounts
- (C) £446,287cr - potential overstatement of costs financed from the LSVT receipt

Government Department Creditors

- (D) £70,465cr - overstatement of the MRA element of HRA subsidy income credited to the HRA in 2002/03

Useable Capital Receipts balance

- (D) £70,465dr - application of capital receipts to fund amounts paid to CHA in respect of the residual Major Repairs Reserve balance after adjusting for the identified overstatement of the MRA credited to the HRA in 2002/03

Housing Revenue Account / HRA Reserve

- (B) £151,472cr - transfer from HRA to GF *Careline* costs attributable to GF user groups

Less

- (A) £166,818dr - transfer from Housing Revenue Account (HRA) to General Fund (GF) *Careline* income attributable to GF user groups

The net impact of unadjusted errors (all identified items) on the HRA balance carried forward at 31 March 2003 is £47,264 (overstatement of balance).

**EXCERPT FROM THE MINUTES OF THE
CORPORATE RESOURCES
OVERVIEW AND SCRUTINY COMMITTEE
HELD ON 1 APRIL 2004**

**CROS.37/04 STATEMENT OF AUDITING STANDARDS (SAS) 610 –
AUDIT COMMISSION REPORT ON THE 2002/03 FINAL
ACCOUNTS**

There was submitted report of the Head of Finance F S.02/04 attaching the SAS 610 Statement for 2002-03, which detailed the unadjusted misstatements during that period, together with the draft Independent Auditor's Report.

The Head of Finance introduced Mr Richard McGahon who was in attendance at the meeting.

Mr McGahon began by advising that he was an Audit Manager with the Audit Commission, but had previously held the post of Audit Manager with the City Council. He also introduced Mr Barry Lennox who worked in Carlisle Audit and submitted apologies on behalf of Ms Fiona Daley (District Auditor and Relationship Manager) who was unable to be present today.

Mr McGahon outlined the key points and next steps for the benefit of Members. Before the Audit Commission could sign off the accounts and issue their Audit Certificate and Opinion this Committee must approve the report. Subject to the Committee's approval to the unadjusted misstatements, the amended Statement of Accounts for 2002-03 would be finalised and considered by Council on 27 April 2004. The amended Statements would incorporate any material misstatements agreed with the Auditors.

In response to a Member's question, Mrs Brown advised that because this was a new requirement and bearing in mind the time constraints involved, it had not been possible to report to this Committee on adjustments made. She hoped that next year it would be possible to submit the entire statement to this Committee in order that Members may have the opportunity to consider the whole picture.

It was noted that none of the amendments agreed would have an impact on the overall financial position of the Council.

A Member queried whether any of the unadjusted misstatements would impact on the future financial position of the Council.

In response, Mr McGahon explained the manner by which the audit had been undertaken and the judgements made in respect thereof. Ms Daley was satisfied that the unadjusted misstatements related to less significant items

and presentational issues which would be addressed in the 2003/04 financial statements.

Members then suggested that consideration of the matter should be deferred to the City Council, at which time a short covering report should be submitted detailing the background to the matter. Mrs Brown indicated that that course of action was acceptable.

RESOLVED – That the SAS 610 Statement 2002-03 be referred to the City Council for approval and that the Head of Finance be requested to provide a short covering report appraising Members of the background to the matter.