

December 2008

# Darlington Borough Council

## Report on Internal Control and Accounting Recommendations

2007/2008

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# 1. Introduction

## **Introduction**

As part of our 2007/08 external audit work, we have examined certain aspects of the Council's system of internal control. The matters raised in this report are only those that came to our attention during our normal audit work, which is primarily concerned with enabling us to provide an opinion on the Council's financial statements. Our findings may not, therefore, include all of the possible improvements in internal control that a more extensive examination might reveal.

During our audit, we carried out a review of a range of financial systems. Our work included:

- a review of the overall control environment;
- a review of monitoring controls in place over all systems within the Council; and

Our main findings are set out in section 3 of this report.




## **Acknowledgements**

We would like to take this opportunity to thank the officers at the Council, for the co-operation we received during the course of the audit.

# 2. Executive Summary




## Introduction

This section summarises the high level findings following our audit of the 2007/08 financial statements. Our review highlighted 11 main areas where controls should be improved. We have prioritised each of our recommendations according to the following categories:



Risk Rating	Assessment Rationale
 H	<b>High level risk:</b> These are significant weaknesses that require immediate action by management.
 M	<b>Medium level risk:</b> These are weaknesses that require management action in the near future.
 L	<b>Low level risk:</b> Other weaknesses where findings are less important but implementation of our recommendations will improve overall control.



### Summary of findings




Our detailed findings and recommendations are set out in section three of this report. The table below summarises the actual number of findings raised and the relative risk ratings.

Risk Rating	Number of findings
	0
	9
	2


### 3. Findings and Recommendations




Finding	Risk	Recommendations	Management response
<p><b>Building Control Operations</b></p> <p>The Building Control (Local Authority Charges) Regulations 1998 require that the Authority at least covers its costs on its fee earning activities over a three year rolling programme.</p> <p>Over the past three years, Darlington Borough Council has made a loss on chargeable activities of £108k.</p>		<p>Whilst the quantum of the loss is relatively low, the Council should consider the level of fees charged to enable an improvement of the financial position in future years.</p>	<p>Agreed – The council had built up a reserve over a number of years which offset any losses incurred without having to increase fees and hence keeping the council competitive. The service has been reviewed with a view to reducing costs rather than increasing fees.</p>
<p><b>Late Submission of VAT Returns</b></p> <p>VAT returns are not being routinely submitted on time. Our testing identified that only two monthly returns had been submitted before the due date. This was a result of the member of staff responsible having conflicting commitments, as he was also working on the new general ledger Aggresso system at the time.</p> <p>As the returns were for money owed to DBC no interest was charged for the late submissions. However, there remains the risk of financial penalties for late submission as well as cash flow disadvantage to the Council.</p>		<p>The Council should ensure that the returns are prepared promptly and reviewed by an appropriate member of staff in order that they can then be submitted to HMRC on time. There should be a process of review each month to check for accuracy and timeliness.</p>	<p>Agreed - The implementation last year of Aggresso impacted on the completions of the VAT returns. All vat returns are now completed within scheduled timescales.</p>

Finding	Risk	Recommendations	Management response
<p><b>Assets Carried at Nil Net Book Value</b></p> <p>In our review of the fixed asset register, we found that there were a number of assets included which had a net book value of nil as at 31/03/08. Of these, items with a gross book value of £2.5m had a nil net book value in previous years.</p> <p>Per discussion with Council officials, the IPS system does not remove assets from the register unless they are manually removed. No listing is maintained which would show whether these assets are still in use within the council or not.</p> <p>The implication of this is that the fixed asset register is not up to date resulting in an overstated gross book value of properties.</p>		<p>We recommend that a clean up of the FAR is performed and all assets no longer held or in use removed.</p>	<p>Agreed - This clean up will be completed before the end of this financial year.</p>
<p><b>Timing of Council Dwelling Revaluations</b></p> <p>The revaluations for council dwellings are carried out in July every year and therefore the valuation in the accounts has always been nine months behind the correct position.</p> <p>The accounts may therefore not be reflecting significant valuation adjustments relevant to the appropriate year end.</p>		<p>Management should ensure that valuations for council dwellings are carried out at a time where they can be reflected in the year end accounts to which they relate.</p>	<p>Agreed - A desk top valuation is required for 2008/09. This is scheduled for February 2009 for inclusion in the 2008/09 accounts.</p>

Finding	Risk	Recommendations	Management response
<p><b>Control Account Reconciliations</b></p> <p>The purchase and sales ledger control account reconciliations are produced electronically and are not held as paper records. The reconciliations are not reviewed or authorised.</p> <p>This presents the risk that any errors in the reconciliations may not be noticed and corrected promptly.</p>		<p>Purchase and sales ledger control account reconciliations should be printed, signed and dated by the preparer and then reviewed by another member of the team.</p>	<p>Agreed – the reconciliations have always been done electronically but have not been printed off.</p>
<p><b>Loss on Disposal of Fixed Assets</b></p> <p>The council recognised a loss on the disposal of fixed assets for General Fund assets of £715,150 being the payment of sale proceeds due to One North East. This loss should have been recognised as at the date of disposal (i.e. 2006/07) and not at the time the proceeds were paid across to ONE.</p>		<p>Although no prior period adjustment was recommended in the accounts due to the immaterial nature of the balance, the Council should ensure that appropriate monitoring procedures are in place to ensure that disposals are correctly accounted for as they occur.</p> <p>This will avoid potential issues should a material transaction occur in the future.</p>	<p>Agreed - In future any items such as this will be recognised in the year of disposal.</p>
<p><b>Government Grant Deferred Account</b></p> <p>In the year the Council wrote out a significant balance from the Government Grant Deferred Account due it not having associated assets on the balance sheet and therefore no depreciation to set the grant against.</p>		<p>The Council needs to ensure that all government grants are directly attributed to assets and are written down to the Income and Expenditure account in line with the treatment of the asset itself.</p>	<p>Agreed - Grants are now being directly attributed to assets</p>



Finding	Risk	Recommendations	Management response
<p><b>Impairments</b></p> <p>DBC have £14m in impairments for 2007/08 which relate to the write off of enhancement works which have not added value. This treatment has arisen because management recognise that the buildings in question will have deteriorated, however no impairment assessment has been made. Instead, the enhancement works correcting any deterioration are impaired as they occur to maintain an accurate carrying value of the asset.</p> <p>Properties may therefore not always have been carried at the appropriate carrying value as demonstrated by the need for periodic impairment for consumption of economic benefit.</p> <p>In addition, enhancement works run the risk of not being treated as capital when they have the characteristics of capital spend, ie the distinction between revenue and capital works is blurred.</p>		<p>As part of the rolling programme of revaluations we recommend that management bring forward the assessment process, so that they regularly consider condition of properties, altering asset lives or making impairments as appropriate, so that when enhancement work is undertaken, a decision can be taken on whether value has been added and work capitalised where appropriate.</p>	<p>Agreed - Although it may be difficult to comply for 2008/09 as much of the work ie revaluations cannot be completed at this stage in the financial year.</p>

Finding	Risk	Recommendations	Management response
<p><b>Cash Flow Statement</b></p> <p>During our review of the Cash Flow Statement we found that the Council was unable to fully substantiate one balance that balanced the cash flow to the movement in cash in the year. This line was as follows:</p> <ul style="list-style-type: none"> <li>○ Accrual adjustment – within the Cash Flow notes with a total value of £727k.</li> </ul>		<p>The Council should review this figure for next year in order to try and fully substantiate all balances in the cash flow statement.</p>	<p>Agree in principle – the problem in the past was that the old Financial Management System (FMS) did not produce the detail required to substantiate every balance. With the introduction of the new FMS the production of the cash flow statement will be reviewed with a view to being able to produce reports to substantiate all balances.</p>
<p><b>Significant Contracts</b></p> <p>When reviewing significant contracts at the Council we noted a number of issues:</p> <ul style="list-style-type: none"> <li>○ A small number of contracts had been signed after the provision of services had begun, including a contract with Apetito for the provision of food services.</li> <li>○ Three separate contracts with NPower were amalgamated on the contract register.</li> </ul>		<p>We recommend that the Council ensure all contracts are in place and signed prior to the commencement of service provision. This would offer the Council a sound legal footing should there be any disputes over service or cost.</p> <p>In addition, the contract register should be split down to individual contracts so that it more accurately reflects the underlying records.</p>	<p>Agreed – The Head of Strategic Procurement in conjunction with Legal Services to remind managers of this requirement.</p> <p>Agreed.</p>
<p><b>Bad Debt Write-Offs</b></p> <p>Bad debt write-offs of £45k had not been authorised as at the time of our audit visit.</p> <p>The Council were therefore open to the risk that inappropriate write-offs may have been included in the accounts.</p>		<p>Bad debt write-offs should be authorised on a timely basis and in advance of the final submission of the year end accounts.</p>	<p>Agreed – The write-offs were authorised by Cabinet on 9<sup>th</sup> September, which was later than normal due to the transition period of the Darlington and Stockton Partnership.</p>

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