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Report to those charged with governance (ISA 260) 2010/11

Cheltenham Borough Council

September 2011

Contents

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This report is addressed to the Council and has been prepared for the sole use of the Council . We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Ian Pennington, the appointed engagement lead to the Council , who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by email to complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421.

Section one

Introduction

This report summarises:

- **the key issues identified during our audit of Cheltenham Borough Council's ('the Council's) financial statements for the year ended 31 March 2011; and**
- **our assessment of the Council's arrangements to secure value for money (VFM) in its use of resources.**

We do not repeat matters we have previously communicated to you. In particular, we draw your attention to our I*nterim Audit Report 2010/11*, presented to you in June 2011, which summarised our planning and interim audit work

Financial statements

Our audit of the financial statements can be split into four phases:

Planning → Control Evaluation → Substantive Procedures → Completion

We previously reported on our work on the first two stages in our *Interim Audit Report 2010/11* issued in June 2011

This report focuses on the final two stages: substantive procedures and completion. It also includes any additional findings in respect of our control evaluation that we have identified since we issued our *Interim Audit Report 2010/11.*

Our final accounts visit on site took place between 4th July and 22nd July 2011. During this period, we carried out the following work:

Substantive Procedures

- Planning and performing substantive audit procedures.
- Concluding on critical accounting matters.
- Identifying audit adjustments.
- Reviewing the Annual Governance Statement.

We are now in the final phase of the audit. Some aspects are also discharged through this report:

Completion

- Declaring our independence and objectivity.
- Obtaining management representations.
- Reporting matters of governance interest.
- Forming our audit opinion.

VFM conclusion

We have also now completed our work in respect of the 2010/11 VFM conclusion. This included work to address the specific risk areas identified in our *Audit Fee Letter 2010/11*.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out the key findings from our audit work in relation to the 2010/11 financial statements.
- Section 4 outlines the key findings from our work on the VFM conclusion.

Our recommendations are included in Appendix 1. We have also reviewed your progress in implementing prior year recommendations and this is detailed in Appendix 2.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

Headlines

This table summarises the headline messages. The remainder of this report provides further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion by 30 September 2011. We will also report that the wording of your Annual Governance Statement accords with our understanding.
Audit adjustments	Our audit has identified only two potential audit adjustments. Both adjustments were in relation to classification and as such has no impact on the net assets reported or the council's net expenditure. This result demonstrates the high level of care and resource that the finance team put into preparing the financial statements and the working papers for audit. We have included details of the above audit adjustments at Appendix 3. These were adjusted by the Council.
Critical accounting matters	We have worked with officers throughout the year to discuss specific risk areas. The Council addressed the issues appropriately.
Accounts production and audit process	The quality of the accounts and the supporting working papers provided to us was again excellent. Officers dealt efficiently with audit queries and the audit process has been completed to the planned timescales. It should be noted that this has been achieved whilst coping with the transition to the International Financial Reporting Standards (IFRS), which resulted in a significant amount of additional work for officers, who were also preparing for 'GO'. The Council has implemented the recommendations in our *ISA 260 Report 2009/10* relating to the financial statements.
Completion	At the date of this report our audit of the financial statements is complete. Before we can issue our opinion we require a signed management representation letter and to confirm there are no events after the balance sheet date that require to be included within the accounts. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.
VFM conclusion	We have concluded that the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.
VFM risk areas	We have considered the specific VFM risks we set out in our Audit Fee Letter 2009/10 namely: • Follow up of the Public Interest Report • GO partnership

Proposed opinion and audit differences

We have identified no issues in the course of the audit that are considered to be material.

The wording of your Annual Governance Statement accords with our understanding.

Proposed audit opinion

We anticipate issuing an unqualified audit opinion by 30 September 2011.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

We did not identify any material misstatements. We identified two issues that have been adjusted by management, these are detailed in appendix 3.

The tables on the right shows the Authority's movements on the general fund for 2010/11 and the balance sheet as at 31 March 2011 as the same for both pre and post audit.

Annual Governance Statement

We have reviewed the Annual Governance Statement and confirmed that:

- it complies with *Delivering Good Governance in Local Government: A Framework* published by CIPFA/SOLACE in June 2007; and
- it is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Movements on the General Fund 2010/11	£m
	Pre and Post-audit
Surplus or (deficit) on the provision of services	11.3
Adjustments between accounting basis & funding basis under regulations	(10.3)
Transfers to/ from earmarked reserves	(0.8)
Increase/(decrease) in General Fund	**0.2**

Balance Sheet as at 31 March 2011	£m
	Pre and Post-audit
Property, plant and equipment	231.1
Other long term assets	26.7
Current assets	21.1
Current liabilities	(23.7)
Long term liabilities	(65.1)
Net assets	**190.1**
General Fund	2.6
Other reserves	187.5
Total reserves	**190.1**

Critical accounting matters

We have worked with officers throughout the year to discuss specific risk areas. The Council addressed the issues appropriately.

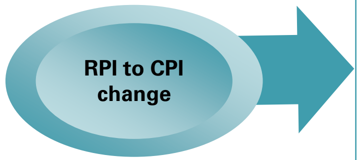
In our Financial Statements Audit Plan 2010/11, presented to you in January, we identified the key risks affecting the Council's 2010/11 financial statements.

We have now completed our testing of these areas and set out our final evaluation following our substantive work.

The table below sets out our detailed findings for each risk.

Key audit risk	Issue	Findings
IFRS Conversion Process	**IFRS Conversion process** • The transition to IFRS represents the largest change in accounting for a number of years. The Council will require a lot of planning and resources to ensure a smooth and successful transition to IFRS.	• Following on from our work carried out at interim we reviewed the Council's approach to component accounting and disclosures around less complex areas such as provisions and leases. • We did not identify any issues. • The Council provided detailed working papers to explain the transition.
Valuation of Investments	**Valuation of Investments** • We will review the CBC valuation to ensure that it is consistent with LAAP 82 'Guidance on the Impairment of Icelandic Banks'. • We will assess valuation assumptions for appropriateness.	• We note that the valuation of Icelandic Investments has been undertaken in line with LAAP 82 update 4 'Guidance on the impairment of investment banks'. • Latest indications are that councils will be treated as priority creditors of Landsbanki and Glitnir Bank Hf. As a result the council has reversed £2.7 million of previous impairments. • As a matter of prudence, the council has transferred £2.5 million to an earmarked reserve to manage the risk of the investment not being repaid and so at the current time the Council are maintaining their capitalisation directive. • We have reviewed this accounting treatment and we are satisfied with its accounting appropriateness.

Critical accounting matters (continued)

Key audit risk	Issue	Findings
	**RPI to CPI pension change** • In its June 2010 budget, the government announced that it intended for future increases in public sector pension schemes to be linked to changes in the Consumer Prices Index (CPI) rather than, as previously, the Retail Price Index (RPI). • As CPI is generally expected to be lower than RPI in the long term this should in turn lead to lower pension increases in deferment as well as payment. Furthermore the cost of benefit accrual will also be correspondingly lower. • The Urgent Issues Task Force (UITF) issued Abstract 48 on 20 December which provides additional guidance on the accounting treatment. The Abstract states that an entity must identify whether its existing obligation is to pay benefit increases based on RPI ("an RPI obligation") or more generally inflation-linked increases. An RPI obligation may be within the formal terms of the scheme or a constructive obligation arising from a public statement or past practice which has created a valid expectation in members of RPI increases.	• If an entity has an RPI obligation and changes it, this is a benefit change and any reduction in scheme liabilities is accounted for as a past service cost in accordance with IAS 19. • We have confirmed that this is how the actuary has treated the move from RPI to CPI. We have also confirmed with Gloucestershire County Council (the pension fund administrator) that the inflation rate of RPI was not referred to in the scheme terms and conditions however RPI has been referred/inferred to in the past in correspondence with members. • Therefore we agree with the treatment of the change from RPI to CPI as a change in assumed benefits and for the negative past service cost of £12m in Non distributable costs . • The year end pension liability has reduced from £70m to £38m.

Critical accounting matters (continued)

Key audit risk	Issue	Findings
	**Local taxes/rent arrears** • We will review the Council's processes for collecting and recovering outstanding balances in relation to council tax, national non-domestic rates (NNDR) and rent arrears. • We will critically review the level of bad debt provisioning at the year end. We will perform a trend analysis of the level of balances over the last financial year.	• We reviewed the levels of tax and rent arrears and bad debt provisioning at year-end and there do not appear to be any significant issues with recoverability of debt or with the completeness of bad debt provision.

Accounts production and audit process

We have noted that the accounts and the supporting working papers were well prepared and of an excellent standard.

Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.

The Council has implemented all of the recommendations in our *ISA 260 Report 2009/10* relating to the financial statements.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the qualitative aspects of the Council's accounting practices and financial reporting.

We also assessed the Council's process for preparing the accounts and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Council has a structured financial reporting process which provides reasonable assurance that the accounts are prepared to a strong standard. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30th June 2011.
Quality of supporting working papers	Our *Accounts Audit Protocol*, which we issued on 19th April 2011 and discussed with Sarah Didcote, set out our working paper requirements for the audit. The quality of the working papers provided was excellent. The working papers requested by KPMG as part of the accounts audit protocol were all provided by Finance on time. The working papers were clearly referenced and a good trail existed.
Response to audit queries	Staff were available when required throughout the audit. All additional audit queries were resolved in a reasonable time.

Prior year recommendations

In our *Interim Audit Report 2010/11* we commented on the Council's progress in addressing the recommendations in our ISA 260 Report 2009/10.

The Council has now implemented all of the recommendations in our ISA 260 Report 2009/10 relating to the financial statements.

Appendix 2 provides further details.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Cheltenham Borough Council for the year ending 31 March 2011, we confirm that there were no relationships between KPMG LLP and Cheltenham Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 4 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have included a copy of a representation letter as Appendix 5. We have provided a template to Mark Sheldon (the Section 151 Officer). We require a signed copy of your management representations before we issue our audit opinion.

Other matters

ISA 260 requires us to communicate 'audit matters of governance interest that arise from the audit of the financial statements' to you which includes:

- material weaknesses in internal control identified during the audit;
- matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. Issue's relating to fraud, compliance with laws and regulations, subsequent events etc.);
- other audit matters of governance interest.

There are no others matters which we wish to draw to your attention.

New VFM audit approach

We followed a new VFM audit approach this year.

Our VFM conclusion considered how the Council secures financial resilience and challenges how it secures economy, efficiency and effectiveness.

We have concluded that the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Overview of the new VFM audit approach

For 2010/11, auditors are required to give their statutory VFM conclusion based on two criteria specified by the Audit Commission. These consider whether the Council has proper arrangements in place for:

- securing financial resilience: looking at the Council's financial governance, financial planning and financial control processes; and
- challenging how it secures economy, efficiency and effectiveness: looking at how the Council is prioritising resources and improving efficiency and productivity.

We follow a risk based approach to target audit effort on the areas of greatest audit risk. We consider the arrangements put in place by the Council to mitigate these risks and plan our work accordingly.

Our VFM audit draws heavily on other audit work which is relevant to our VFM responsibilities and the results of last year's VFM audit.

The key elements of the VFM audit approach are summarised in the diagram below.

Conclusion

We have concluded that the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

VFM criterion	Met
Securing financial resilience	✓
Securing economy, efficiency and effectiveness	✓

Appendix 1: New issues and recommendations

We included a number of recommendations in our June 2011 interim report. This appendix includes recommendations we have identified since then.

We have given each recommendation a risk rating and agreed what action management will need to take.

The Council should closely monitor progress in addressing specific risks and implementing our recommendations.

We will formally follow up these recommendations next year.

Priority rating for recommendations		
Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	***Priority two***: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	***Priority three***: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

No.	Risk	Issue and recommendation	Management response/ responsible officer/ due date
1	(two)	**Issue – access to Live Environment not restricted for Open Revenues and Icon** When organisations develop and test new IT applications, they usually do so in a part of the system ("the Development Environment") that can only be accessed by the IT development team. When the development team has checked the new application for errors and bugs, they release the application for general use by council staff in "the Live Environment". Staff should not be able to make changes to applications in the Live Environment, or there is a risk of programming errors creating errors in transactions. We identified that all users have the ability to access network folders containing the Open Revenues and Icon live environment files, which increases the risk of the application files being accidentally or otherwise overwritten or deleted. **Recommendation** The Council should review access rights to live environment folders and ensure that they are restricted appropriately for all systems including the new Agresso system when it is introduced in 2012.	**Responsible officer** – Paul Woolcock, ICT Infrastructure Manager Applications may require access to the program files held on a shared drives. Permissions are being checked on shared and folders, as some applications will only run with 'full control' access. ICT will get clarification with the Agresso suppliers on folder and file permissions prior to going live in 2012.

Appendix 1: New issues and recommendations (continued)

No.	Risk	Issue and recommendation	Management response/ responsible officer/ due date
2	(two)	**Issue – Lack of evidence of review of Benefits payments run.** The Benefits System automatically generates a list of payments due each week. Benefits Officers have the ability to suspend payments to individuals for a range of reasons for example if it is suspected that the individual is not entitled to the benefit they are claiming. As part of the control process, the system produces a Suspended Payment Report and these reports are reviewed. However the reports are not printed out and therefore no audit trail exists of the management review which is an important part of the control process. **Recommendation** The suspended payments reports are signed and dated as evidence of the review process.	Responsible officer - Paul Aldridge, Housing Benefit Manager The Benefit service have put into place processes for staff to ensure the printing, checking and validating of reports (signature and date) before payments are made. Hard copies will be kept on file

Appendix 1: New issues and recommendations (continued)

No.	Risk	Issue and recommendation	Management response/ responsible officer/ due date
3	● (three)	**Issue – Lack of evidence of review of journals** A journal is a mechanism used in accounting systems for making adjustments and corrections. If not used carefully, there is a risk that they can create errors. In order to control this risk, it is best practice that journals should be reviewed and signed off by a more senior staff member. The higher the financial value on the journal, the more senior should the sign off be. We noted that currently there is no formal review of journals. A system of secondary authorisation/approval at least for higher value journals would provide assurance that only genuine journals are being posted. We recognise that the Council has high level budgetary controls in place as a compensating control but do no feel that this is at the right level to pick up journal errors. Currently the Council has a proven and trusted finance team in place however in moving forwards to GO shared services the secondary authorisation of journals will become more imperative. **Recommendation** Higher value journals are authorised and evidence of this authorisation is maintained.	**Responsible officer** - Paul Jones, Head of Financial services In 2011/12 it is agreed that all Journals exceeding £100,000 are countersigned by the Head of Financial Services or the Director of Resources. All journal entries into the new Financial Management system (Agresso) which is due to go 'live' on 1st April 2012, may only be processed by authorised employees with the approval of the Section 151 Officer. The Head(s) of Finance for GO Shared Services will be responsible for ensuring that a daily report of all journals raised on the new finance system is produced and retained for audit purposes. This report will be checked and signed as agreed by a delegated senior officer within GO Shared Services.

Appendix 2: Follow up of prior year recommendations

The Council has implemented all of the recommendations in our *ISA 260 Report 2009/10.*

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2009/10* and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	4
Implemented in year or superseded	4
Remain outstanding (re-iterated below)	0

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at August 2011
1	(two)	**Lack of evidence of review of bank reconciliation** The monthly bank reconciliation review is currently not evidenced by a signature and date and therefore no audit trail exists of the management review which is an important part of the control processes. **Recommendation** The bank reconciliations are signed and dated as evidence of the monthly review process.	Paul Jones September 2010	**Completed** All bank reconciliations are now signed and dated.
2	(two)	**Lack of high level monthly payroll review** We noted that currently there is no high level review of the payroll before authorisation and payment each month. There is limited payroll exception reporting with the current payroll system and this high level overview would provided added assurance until a new payroll system is introduced. **Recommendation** A monthly high level review examining any significant monthly variances would give additional assurances of the completeness and accuracy of the payroll payment which is one of the most significant costs of the council.	Paul Jones September 2010	**Completed** The payroll and BACS authorisation form and supporting papers are now reviewed and signed off by a manager independent of the payroll input team.

Appendix 2: Follow up of prior year recommendations (continued)

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at August 2011
3	● (two)	**Lack of evidence of review of income reconciliations** There was a lack of evidence of the review of the income reconciliation of the debtors system to the cash receipting system using the daily ASH reports, as the reconciliation is not signed or dated. **Recommendation** The income reconciliations are signed and dated as evidence of review which leaves a clear audit trail of the completion of the control.	Revenues Manager September 2010	**Completed** Income reconciliations are now initialled and dated to evidence the monthly review.
4	● (two)	**Lack of documentation of the NNDR reconciliation** There was a lack of evidence of the review of the reconciliation between the NNDR and the IBS reports. **Recommendation** The reconciliations between the NNDR and IBS reports are signed and dated to evidence that the control is operating effectively.	Revenues Manager September 2010	**Completed** A spreadsheet is completed which documents the reconciliation, this file is initialled and dated as prepared and reviewed on a monthly basis.

Appendix 3: Audit differences

No significant audit adjustments were identified during the course of the audit.

Only two immaterial adjustments were identified.

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in the Council's case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Corrected audit differences

The following table sets out the significant audit differences identified by our audit of Cheltenham Borough Council's financial statements for the year ended 31 March 2011. These have been adjusted in the final set of financial statements.

Uncorrected audit differences

There are no uncorrected audit differences.

Impact					Basis of audit difference
Income and expenditure statement	Adjustments accounting basis & statute	Assets	Liabilities	Reserves	
		Dr Assets held for sale £1,314k			Council dwellings disposed of during the year have been disclosed as assets held for sale at year end and then removed from fixed assets as part of the revaluation. They should have been disclosed as an in year disposal. This is a classification adjustment and therefore has no impact on the total of fixed assets.
		Cr Disposals £1,314k			
No net impact on the reported outturn	-	-	-	-	On the 1st April the concessionary fares function was transferred to the control of Gloucestershire County Council. This was disclosed as an event after the balance sheet date however this should have been separately disclosed on the face of the Income and expenditure statement. This is a classification adjustment and therefore has no impact on the reported outturn.
£0	-	**£0**	-	-	**Total impact of adjustments**

Appendix 4: Declaration of independence and objectivity

The Code of Audit Practice requires us to exercise our professional judgement and act independently of both the Commission and the Council .

Requirements

Auditors appointed by the Audit Commission must comply with the *Code of Audit Practice* (the Code) which states that:

"Auditors and their staff should exercise their professional judgement and act independently of both the Commission and the audited body. Auditors, or any firm with which an auditor is associated, should not carry out work for an audited body that does not relate directly to the discharge of auditors' functions, if it would impair the auditors' independence or might give rise to a reasonable perception that their independence could be impaired."

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Audit Commission's Standing guidance for local government auditors (Audit Commission Guidance) and the requirements of APB Ethical Standard 1 *Integrity, Objectivity and Independence* (Ethical Standards).

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Audit Commission Guidance requires appointed auditors to follow the provisions of ISA (UK &I) 260 Communication of *Audit Matters with Those Charged with Governance*' that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor's objectivity and independence.
- The related safeguards that are in place.
- The total amount of fees that the auditor and the auditor's network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor's professional judgement, the auditor is independent and the auditor's objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor's objectivity and independence may be compromised and explaining the actions which necessarily follow from his. These matters should be discussed with the Audit Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Audit Director and the audit team.

General procedures to safeguard independence and objectivity

KPMG's reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

Appendix 4: Declaration of independence and objectivity (continued)

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the Ethics and Independence Manual ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual Ethics and Independence Confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of Cheltenham Borough Council for the financial year ending 31 March 2011, we confirm that there were no relationships between KPMG LLP and the Cheltenham Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.

Appendix 5: Management representation letter

We ask you to provide us with representations on specific matters such as whether the transactions within the accounts are legal and unaffected by fraud.

The wording for these representations is prescribed by auditing standards.

We require a signed copy of your management representations before we issue our audit opinion.

Dear Sirs

This representation letter is provided in connection with your audit of the financial statements of Cheltenham Borough Council ("the Council"), for the year ended 31 March 2011, for the purpose of expressing an opinion as to whether these:

i) give a true and fair view of the financial position of the Group and of the Council as at 31 March 2011 and of the Group's and the Council's expenditure and income for the year then ended; and

ii) have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

These financial statements comprise the Council and Group Movement in Reserves Statements, the Council and Group Comprehensive Income and Expenditure Statements, the Council and Group Balance Sheets, the Council and Group Cash Flow Statements, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement and the Collection Fund and the related notes.

The Council confirms that the representations it makes in this letter are in accordance with the definitions set out in the Appendix to this letter.

The Council confirms that, to the best of its knowledge and belief, having made such inquiries as it considered necessary for the purpose of appropriately informing itself:

Financial statements

1. The Council has fulfilled its responsibilities, as set out in regulation 8 of the Accounts and Audit (England) Regulations 2011, for the preparation of financial statements that:

- give a true and fair view of the financial position of the Group and of the Council as at 31 March 2011 and of the Group's and the Council's expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11.

The financial statements have been prepared on a going concern basis.

2. Measurement methods and significant assumptions used by the Council in making accounting estimates, including those measured at fair value, are reasonable.

3. All events subsequent to the date of the financial statements and for which the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11 require adjustment or disclosure have been adjusted or disclosed.

Information provided

4. The Council has provided you with:

- access to all information of which it is aware, that is relevant to the preparation of the financial statements, such as records, documentation and other matters;
- additional information that you have requested from the Council for the purpose of the audit; and
- unrestricted access to persons within the Council and Group from whom you determined it necessary to obtain audit evidence.

5. All transactions have been recorded in the accounting records and are reflected in the financial statements.

6. The Council acknowledges its responsibility for such internal control as it determines necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error. In particular, the Council acknowledges its responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

   The Council has disclosed to you the results of its assessment of the risk that the financial statements may be materially misstated as a result of fraud. Included in the Appendix to this letter are the definitions of fraud, including misstatements arising from fraudulent financial reporting and from misappropriation of assets.

Appendix 5: Draft management representation letter

7. The Council has disclosed to you all information in relation to:

(a) Fraud or suspected fraud that it is aware of and that affects the Council and its Group and involves:

- management;
- employees who have significant roles in internal control; or
- others where the fraud could have a material effect on the financial statements; and

(b) allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, analysts, regulators or others.

8. The Council has disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements. Further, the Council has disclosed to you and has appropriately accounted for and/or disclosed in the financial statements in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11 all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.

9. The Council has disclosed to you the identity of the Council's and its Group's related parties and all the related party relationships and transactions of which it is aware and all related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11.

Included in the Appendix to this letter are the definitions of both a related party and a related party transaction as the Council understands them and as defined in IAS 24, except where interpretations or adaptations to fit the public sector are detailed in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11.

10. On the basis of the process established by the Council and having made appropriate enquiries, the Council is satisfied that the actuarial assumptions underlying the valuation of pension scheme liabilities are consistent with its knowledge of the business.

11. The Council further confirms that:

a) all significant retirement benefits, including any arrangements that:

- are statutory, contractual or implicit in the employer's actions;
- arise in the UK and the Republic of Ireland or overseas;
- are funded or unfunded; and
- are approved or unapproved,

have been identified and properly accounted for; and

b) all settlements and curtailments have been identified and properly accounted for.

This letter was tabled and agreed at the meeting of the Audit Committee on 21 September 2011.

Yours faithfully,

Councillor A Wall.

Chair of the Audit Committee

Mark Sheldon

Director of Resources

Appendix 5: Draft management representation letter

Appendix A to the Management Representation Letter of Cheltenham Borough Council: Definitions

Financial Statements

A complete set of financial statements comprises:

- Movement in Reserves Statement for the period
- Comprehensive Income and Expenditure Statement for the period
- Balance Sheet as at the end of the period
- Cash Flow Statement for the period
- Notes, comprising a summary of significant accounting policies and other explanatory information, and
- Balance Sheet as at the beginning of the earliest comparative period (ie a third Balance Sheet) when a Council applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.

A local Council is required to present group accounts in addition to its single entity accounts where required by chapter nine of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11.

A housing authority shall present:

- a HRA Income and Expenditure Statement; and
- a Movement on the Housing Revenue Account Statement.

A billing authority shall present a Collection Fund Statement for the period showing amounts required by statute to be debited and credited to the Collection Fund

Material Matters

Certain representations in this letter are described as being limited to matters that are material.

Omissions or misstatements of items are material if they could, individually or collectively, influence the decisions or assessments of users made on the basis of the financial statements. Materiality depends on the nature or size of the omission or misstatement judged in the surrounding circumstances. The nature or size of the item, or a combination of both, could be the determining factor.

Fraud

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users.

Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorisation.

Error

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

a) was available when financial statements for those periods were authorised for issue, and

b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Management

For the purposes of this letter, references to "management" should be read as "management and, where appropriate, those charged with governance".

Appendix 5: Draft management representation letter

Related party

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions or if the related party entity and another entity are subject to common control.

Related parties include:

a) entities that directly, or indirectly through one or more intermediaries, control, or are controlled by the Council (ie subsidiaries);

b) associates;

c) joint ventures in which the Council is a venture;

d) an entity that has an interest in the Council that gives it significant influence over the Council;

e) key management personnel, and close members of the family of key management personnel; and

f) post-employment benefit plan (pension fund) for the benefit of employees of the Council, or of any entity that is a related party of the Council.

Key management personnel are all chief officers (or equivalent), elected members, chief executive of the Council and other persons having the Council and responsibility for planning, directing and controlling the activities of the Council, including the oversight of these activities.

The following are deemed not to be related parties by the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11:

a) providers of finance in the course of their business in that regard and trade unions in the course of their normal dealings with an Council by virtue only of those dealings; and

b) an entity with which the relationship is solely that of an agency.

Related party transaction

Related party transaction is a transfer of resources or obligations between related parties, regardless of whether a price is charged. Related party transactions exclude transactions with any other entity that is a related party solely because of its economic dependence on the Council or the government of which it forms part.

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