Governance and Accountability for Smaller Authorities in England

Section 5: Supporting information and practical examples

June 2016

The Practitioners' Guide is issued by the Joint Practitioners' Advisory Group (JPAG), and jointly published by the Society of Local Council Clerks, the National Association of Local Councils and the Association of Drainage Authorities.

JPAG is responsible for issuing proper practices in relation to the accounts of smaller authorities. Its membership consists of sector representatives from the Society of Local Council Clerks, the National Association of Local Councils and the Association of Drainage Authorities, together with stakeholder partners representing the Department of Communities and Local Government, the Department of Environment, Food and Rural Affairs, the Chartered Institute of Public Finance and Accountancy, the National Audit Office, and a representative of the external audit firms appointed to smaller authorities.

Contents

Introduction

5.1. Sections 1, 2 and 3 of the Practitioners' Guide (the Guide) issued by the Joint Practitioners' Advisory Group represent the proper accounting and governance practices *('proper practices')* referred to in statute. They set out for responsible financial officers (RFOs) the appropriate standard of financial and governance reporting for smaller authorities and are mandatory.

5.2. Section 4 of the Guide sets out the non-statutory guidance relating to internal audit which smaller authorities are required to take into account.

5.3. This section of the Guide contains supporting information and practical examples to support practitioners in complying with proper practices as set out in Sections 1 and 2 of the Guide. As Section 5 is not part of proper practices, it cannot and does not set any mandatory requirements in respect of the annual return. It does however include references to statutory requirements where appropriate, such as the requirements around making provision for the exercise of public rights.

5.4. This section of the Guide follows the order of Sections 1 and 2, with supporting information relating to the annual governance statement preceding supporting information on the accounting statements.

5.5. General information about smaller authorities and their responsibilities can be found on the following websites:

National Association of Local Councils

Society of Local Council Clerks

Association of Drainage Authorities

5.6. In accordance with Section 6 of the Local Audit and Accountability Act 2014, an authority is a 'smaller authority' for a financial year if the higher of the authority's gross income for the year and its gross expenditure for the year does not exceed £6.5 million for that year or either of the two previous years. This section of the Guide uses the term 'authority' to refer to all types of smaller authority.

Annual governance statement

AGS assertion 1: Financial management and preparation of accounting statements

Budgeting

5.7. The preparation of an annual budget is one of the key statutory tasks to be undertaken by an authority, irrespective of its size. The budget has three main purposes:

- it results in the authority setting the precept for the year (or rates and special levies for IDBs);
- subject to the authority's Financial Regulations, it gives the clerk and other officers overall authority to make spending commitments in accordance with the plans approved by members; and
- it provides a basis for monitoring progress during the year by comparing actual spending against planned spending.

5.8. It is essential that authority members understand how the budget is put together and how it should be used in the running of the authority. Reviewing the budget against actual expenditure regularly gives members early warning about the likelihood of a shortfall (or surplus) and helps them to decide what responsive action to take.

5.9. The key stages in the budgeting process are:

- decide the form and level of detail of the budget;
- review the current year budget and spending;
- determine the cost of spending plans;
- assess levels of income;
- bring together spending and income plans;
- provide for contingencies and consider the need for reserves;
- approve the budget;
- confirm the precept or rates and special levies; and
- review progress against the budget regularly throughout the year.

Accounting records and supporting documents

5.10. All authorities, including parish meetings where there is no parish council, need to appoint an officer, the RFO, to be responsible for the financial administration of the authority in accordance with section 151 of the Local Government Act 1972. The clerk to the authority is often also appointed as the RFO, but this is not automatically the case. The authority should formally determine in whom the responsibility vests, recognising that there are particular risks that arise in the unusual circumstances where an elected member is appointed (unpaid) as the RFO. Decisions about appointing the RFO should always be the subject of a full risk assessment and consideration evidenced in the minutes. The proper segregation of duties means that the Chairman of the authority or of the Finance Committee should never be appointed (even on a short-term basis) either as Clerk or as RFO.

5.11. The appointment of an RFO does not mean that members then have no responsibility for the financial health of the authority. On the contrary, members continue to be accountable for ensuring that the authority does not live beyond its means, but the RFO takes on the duty of designing and implementing the accounting arrangements that will assure members that finances are being properly managed.

5.12. Regulation 4 of the Accounts and Audit Regulations 2015 sets out the duties of the RFO and requirements relating to accounting records and financial control systems.

5.13. The RFO is responsible for determining, on behalf of the authority, the form of its accounting records and supporting records and its financial control systems. The RFO must also ensure, on behalf of the authority, that the financial control systems are observed and that the accounting records of the authority are kept up to date.

5.14. The accounting records must contain:

- entries from day to day of all sums of money received and expended by the authority and the matters to which its income and expenditure or receipts and payments relate; and
- a record of the assets and liabilities of the authority.

5.15. It is also good practice for the accounting records to contain a record of income and expenditure by the authority in relation to claims made for contribution, grant or subsidy from a government department or other public body.

5.16. The financial control systems must include:

- measures to ensure that the financial transactions of the authority are recorded as soon as, and as accurately as, reasonably practicable;
- measures to enable the prevention and the detection of inaccuracies and fraud, and the reconstitution of any lost records;
- measures to ensure that risk is appropriately managed; and
- identification of the duties of officers dealing with financial transactions and division of responsibilities of those officers.

5.17. It is also good practice for the financial control systems to include procedures for uncollectable amounts, including bad debts, only to be written off with the approval of members or, under delegated authority, the RFO and for the approval to be disclosed in the accounting records.

5.18. The basic record of receipts and payments is always the starting point of an accounting system and the majority of internal controls will work back to that record. A successful accounting system requires that the basic cash book is kept up to date and balances are regularly verified against a bank statement or the actual cash in the petty cash tin. This record will also agree with the supporting vouchers, invoices or receipts. Even though the arithmetic may be automatic on a computer based system it is necessary to check that the additions and balancing are correct. Where there is a computer based system, the reliability of information reported by the system depends on the quality and accuracy of data input, and how it is then processed, and so tests of the integrity of data input and processing should be considered. A member or officer may do the checking or verification.

5.19. Manually kept books of account, or an effective computerised accounting system, should provide the basis for the accounting statements, in that the accounting statements are compiled from the information recorded in the books. But the books of account are important in themselves in the running of the authority throughout the year. A good set of books will allow an authority to appreciate at any time:

- the amounts that it has spent in the year, the income it has received and its financial commitments;
- whether, in the light of this information, its spending plans for the rest of the year are still affordable; and
- the assets that it owns (for example, land, buildings, vehicles, investments, cash) and the liabilities that it owes (for example, outstanding payments for goods and services, borrowings).

5.20. The record of the assets and liabilities of the authority required by Regulation means in practice the asset and investment register and record of loans and other debts.

Bank reconciliation

5.21. The most important accounting record maintained by authorities will be the cash book which is a register of all the payments made and receipts taken in by the authority. There may be a temptation to rely on the bank statement as a record of cash transactions. However, a cash book is essential because the statements provided by the bank will not necessarily be a reliable record of the authority's cash balances because:

- the bank can make errors and omissions in processing transactions – the authority needs its own records to provide a check on the bank statement;
- while electronic payments and receipts are instant, there can be considerable timing differences between, say, writing cheques to other parties and their being cashed by the bank, and between receiving income and it being credited to the authority's account once paid in; and
- the bank statement takes time to catch up with the actual cash flows of the authority and does not provide an up-to-date position.

5.22. The up to date cash book, therefore, provides the most accurate record of all income received and payments made, including cheques drawn.

5.23. Bank statements are important documents as they are evidence provided by an independent party of the state of the authority's cash balances. They contrast with the cash book, which is the authority's own record of its cash position. It is consequently an invaluable exercise to compare the balances on the bank statement with the balance in the cash book at any particular date and understand the reasons for any differences between them. This will reveal whether there are any errors, omissions or discrepancies in either the bank records or the cash book (for example, cheques drawn properly have been known to be altered by recipients before being banked).

5.24. The bank reconciliation is a key tool for management as it assists with the regular monitoring of cash flows which aids decision-making, particularly when there are competing priorities. The year-end bank reconciliation is particularly important as it will provide evidence to support the total cash and short-term investments balance shown in Line 8 in Section 2 of the authority’s annual return. As bank statements may be made up to different dates in the month, care should be taken, particularly at year-end, to ensure that the statement being reconciled includes balances as at 31 March.

5.25. Bank reconciliations should be performed on a regular basis and cover each of the authority's bank accounts. Most commonly, authorities will operate a current account through which most transactions are made, and possibly one or more deposit accounts. Some authorities will carry out a reconciliation every time they receive a bank statement, which is good practice as it identifies bank errors early on. It is for each authority to decide how regularly it wants to receive the assurance that a successful reconciliation can provide. Reconciling the cash book to bank statements should be reported to members, and the full reconciliation made available for their scrutiny each time it is done. Approval of the bank reconciliation by the authority or the chair of finance or another authority nominee is not only good practice but it is also a safeguard for the RFO and may fulfil one of the authority's internal control objectives.

5.26. There is a limited number of reasons for differences between bank statements and the cashbook, and most authorities will be able to use a standard layout for the bank reconciliation. The common reasons are:

- transactions in the bank statement that are not recorded in the cash book – this may include interest payable and bank charges, direct debits, standing orders and other automated payments that have been omitted from the cash book. None of these is an item for the reconciliation. Instead, the cash book should be updated to record all of these transactions, and the resulting balance is then brought into the reconciliation.
- unpresented cheques – payments are recorded in the cash book when the authority commits itself to making them, usually by handing over a cheque, putting a cheque in the post or completing the instructions for an automated payment; the balance on the bank account will not reduce until several days later when the cheque or instruction is received by the bank and processed. Unpresented cheques therefore need to be deducted from the bank statement balance in the reconciliation.
- payments into the bank which are outstanding (sometimes referred to as 'cash in transit') - receipts are recorded in the cash book when they come into the possession of the authority; however, they will not be recognised on the bank statement until after cash is banked or cheques are cleared. Payments into the bank which are outstanding from the bank statement therefore need to be added to the bank statement balance in the reconciliation.

5.27. A standard layout for a financial year-end bank reconciliation can be found in Appendix 1 on page 33.

Investments

5.28. It is unusual for an authority to hold its reserves other than in the form of easily accessible bank deposits or other short-term investments (see paragraph 2.21 in Section 2 of the Guide for a definition). Occasionally, circumstances require authorities to consider making other types of investments, for example when saving for a future capital project or while deciding how to apply the proceeds of an asset sale or a donation.

5.29. In deciding whether it is appropriate to make long-term investments, the authority should follow the [Guidance on local government investments issued by DCLG in 2010].

5.30. The authority's investment strategy will set out management arrangements for the investments held and procedures for determining the maximum periods for which funds may prudently be committed. The strategy should ensure and demonstrate that the authority has properly assessed the risk of committing funds to longer term investments and complies with legislative requirements. Long-term investments in assets whose capital values may fluctuate carry considerable risks and require active management. Investment management is a specialist area. Authorities may wish to seek independent professional assistance when developing their investment strategy.

AGS assertion 2: Internal Control

Standing Orders and Financial Regulations

5.31. The first step in establishing a financial system is to identify the general rules applicable at authority or committee meetings and in carrying out the authority's business. These are set out in the authority's Standing Orders, Financial Regulations and other internal instructions. Model versions of Standing Orders and Financial Regulations are provided by NALC and ADA.

5.32. Standing Orders must include provisions for securing competition and regulating the manner in which tenders are invited. To comply with these requirements, authorities should set within their Financial Regulations a limit for the purchase of goods and services above which three estimates or quotes should be invited from persons or firms competent to do the work. Standing Orders will state a higher value above which competitive tenders in sealed envelopes should be invited. It is the responsibility of authorities to determine their own limits that are most appropriate to local circumstances.

5.33. As far as possible, a fully priced official order should be sent to suppliers in advance of delivery of goods. Official orders both commit a supplier to a price and help prevent unauthorised credit being granted in the authority's name. On receipt of invoices, verification that the relevant goods or services have been received should be obtained and invoices checked to ensure that the arithmetic is correct, agreed discounts have been deducted and everything is acceptable regarding reclaiming the VAT. Practitioners should keep up to date with VAT Guidance issued by HM Revenue and Customs.

5.34. Procedures for the management of capital projects should also be covered by Standing Orders which should require payments only against certified completions under a planned and approved programme of works governed by a properly negotiated contract supervised by a named authority officer.

Safe and efficient arrangements to safeguard public money

Accounts for payment

5.35. The payments process should always be carried out in accordance with the authority's Financial Regulations. Cheques and other payments should only be released once confirmation has been obtained that adequate funds are available. All payments made since the last meeting should be reported to the next authority meeting. Members should never sign blank cheques or authorise funds transfers which are presented to them unsupported by the appropriate documentation.

5.36. The authority should develop specific control procedures for any payments by bank transfer, or other electronic means, taking into account the risks brought about by the ease and speed of these transactions and the difficulties faced in unravelling them should they go wrong.

5.37. If there is any doubt as to how much the authority owes to one of its regular suppliers, the supplier should be asked to send a statement of the authority's account. It would be appropriate to request statements as at 31 March each year to assist with the preparation of the annual return.

Receipts

5.38. Cash and cheques should be entered into the cash book on the date of receipt and banked promptly and intact (i.e. without any of the cash being kept back for spending).

Practitioners should be aware that some receipts may require VAT to be accounted for and paid over by the authority, particularly where sales of items are involved and certain thresholds have been reached. Once again, the RFO should be familiar and up to date with the rules governing such transactions. These are published by HM Revenue and Customs and accompanied by guidance for practitioners.

Cash

5.39. Before finalising and adopting procedures and internal control systems involving cash, the RFO should always check the requirements of insurers under Fidelity Guarantee insurance cover arrangements, which may well specify the amount, location and minimum security arrangements required regarding the handling of cash or bank balances.

5.40. The number of petty cash floats should be kept to a minimum and should not be used when an official order is more appropriate. The floats should be adequate in size to meet small items of expenditure and should not require reimbursement more frequently than once a month. Adequate records of the receipts and payments should be maintained for each float, including a VAT analysis, and regular reconciliation performed, usually with such regularity that successful reconciliation can be reported at each authority meeting.

Debt collection

5.41. Effective debt collection is an essential part of proper financial management. Authorities should ensure that invoices raised are paid promptly or that appropriate recovery action has been taken.

5.42. Debt monitoring arrangements should be in place covering all activities of the authority which involve receiving payment. For example, if the authority rents out a number of allotments, a separate record may be appropriate for that purpose. The record would need to include details of the person who owes the debt, the amount, any arrears brought forward at the start of the accounting period, amounts due in the year, amounts paid in the year, any debts written off, and a note of the current state of any recovery action taken.

5.43. At the end of each year, the record will need to be reconciled to ensure that the figures for arrears brought forward plus new amounts due, less new receipts and write-offs, balances to the total arrears to be carried forward.

5.44. Irrecoverable debts should be written off, after full consideration of the possibilities for, and the likely costs of, pursuing the debt. Uncollectible amounts, including bad debts, should only be written off with the approval of members, or under delegated authority, by the RFO. The approval should be shown in the accounting records.

Employment

5.45. Authorities with any employees are, by definition, employers and are required to apply Pay as You Earn (PAYE). PAYE taxes and employee and employer National Insurance contributions (NIC) should be calculated and recorded for every employee. Deductions should be paid to HMRC on or before the date prescribed. In addition, the general requirements of employment law apply but are not within the scope of this Guide.

5.46. HMRC guidance setting out the correct income tax and NIC treatment of parish clerks is set out in the HMRC Employment Income Manual. This guidance confirms that a parish clerk is an office holder and that all office holders are subject to PAYE. This means that parish clerks:

- can never be considered as self-employed for tax or NIC purposes;
- cannot be paid 'gross'; and
- fall to be taxed under PAYE.

5.47. HMRC guidance confirms that where the RFO is a separate appointment, the RFO is also an office holder and is subject to the same income tax and NIC rules as the clerk.

5.48. Authorities should pay particular attention to situations where contractors are engaged to carry out the authority's services. Occasions may arise when contractors cease to be self-employed and become employees for tax purposes. Authorities should refer to HMRC's Employment Status Indicator Tool for further information.

5.49. As part of risk management arrangements, written confirmation should be sought from HMRC to ensure that payments for services are being correctly treated; otherwise authorities may find themselves with unexpected and significant liabilities to pay income tax and employers NIC. Care should also be taken when making any payments of expenses or allowances to non-employees, for example authority members, which should also be considered as falling within the scope of PAYE.

5.50. All employers are required by law to take out employers' liability insurance and decide the appropriate level of fidelity guarantee insurance. All cover should be risk based and kept under constant review to make sure it adequately reflects changes in circumstances.

5.51. Authorities should have regard to guidance on employment matters issued jointly by NALC and SLCC, or by ADA.

VAT

5.52. This can be a complex area and authorities are advised to refer to guidance issued by HMRC.

5.53. Information on how to account for VAT in Section 2 of the annual return can be found at paragraphs 5.129 and 5.130 below.

Fixed assets and equipment

5.54. If the assets it owns or for which it is responsible are not being managed properly the authority is exposed to the risk of financial loss relating to:

- improper asset management – without the right management information, outdated patterns of use may run on unchallenged or unnoticed;
- improper asset usage and maintenance – assets may not be fit for purpose, be underused or so out-of-date as to be incapable of satisfactory modernisation. Equally they may be capable of alternative, additional or more intensive use or be readily saleable. These opportunities may be missed where no comprehensive information on assets is available; and
- asset ownership – the continued ownership of assets may be overlooked altogether and risks unmanaged.

5.55. These risks are most likely to be realised when information is poor. In particular where information about assets is not available or is out-of-date. The risk of financial loss can be greatly reduced by setting up an asset register which holds all the information needed.

5.56. An asset register is the starting point for any system of financial control over assets as it:

- facilitates the effective physical control over assets;

- provides the information that enables the authority to make the most cost effective use of its capital resources;
- ensures that no asset is overlooked or underutilised and is therefore used most efficiently;
- pools all the information available about each asset from across the authority and makes it available to every part of the authority;
- provides a record of the sources of evidence used to support the existence and valuation of assets to be covered by insurance;
- supports the annual return entry for capital assets by collecting the information on the cost or value of assets held; and
- forms a record of assets held for insurance purposes.

5.57. The key information needed in the asset register is:

- dates of acquisition, upgrade and disposal (it is useful to keep a record of disposed assets as an asset management tool);
- costs of acquisition and any expenditure which increases the life of the asset;
- if proxy cost is used for first valuation, a note of the method used for valuation and details of any professional advice received;
- useful life estimate;
- location;
- responsibility (it may be appropriate to assign responsibility for each asset to members of staff);
- present use and capacity, for example in terms of site area, internal floor areas, and measures of occupancy and/or usage;
- corresponding periodic measures of usage or occupation;
- any available indications of asset value and condition; and
- any regular charges for usage or occupancy.

5.58. Most assets should be first recorded in the asset register at their actual purchase cost. In some cases the purchase cost may not be known at acquisition or first recording and so a proxy cost may be substituted. A proxy cost is a value for the asset which is an estimate of its value by the authority which is based on external professional advice. Authorities may apply the insurance value of the asset at the time of first recording as a proxy. A proxy cost may be applied at the time of acquisition or first recording of an asset in the asset register only where the cost/value is not known.

5.59. In the special case where an authority receives an asset as a gift at zero cost, for example by transfer from a principal authority under a community asset transfer scheme, the asset should be included in the asset register with a nominal one pound (£1) value as a proxy for the zero cost. The use of the £1 proxy is particularly important in cases where an authority operates an asset registration system that requires a positive value for every asset. Any costs of bringing gifted assets into productive use should be expensed as revenue items.

5.60. Many authorities own assets that do not have a functional purpose or any intrinsic resale value (for example, a village pond or war memorial). These assets are often referred to as 'community assets'. Authorities should record community assets in the assets register in the same way as gifted assets.

5.61. The total value of an authority's assets recorded on the asset register as at 31 March each year is reported at Line 9 on the authority's annual return (see paragraphs 2.24 to 2.28 in Section 2 of the Guide and 5.137-5.141 below). It follows that users of the annual return may ask for details of the assets whose total value is reported at Line 9, including about the method of valuation applied and about any changes in value to previously recorded assets. Authorities should be able to track and explain fully any changes in the asset register from year to year.

Loans and long term liabilities

5.62. Authorities may borrow money temporarily for cash flow purposes to fund payments in advance of receiving money from precepts, rates and special levies, or other sources during the year. Such loans will normally be in the form of arranged overdraft facilities and will be repaid as the anticipated receipts materialise.

5.63. Long-term loans will normally be associated with capital projects and these require borrowing approval before they can be arranged. For local councils, this is obtained by applying to the relevant Association of Local Councils, which act for the government in this regard. For IDBs, this is obtained from the Secretary of State for Environment, Food and Rural Affairs, in accordance with section 55 of the Land Drainage Act 1991.

5.64. Capital projects need to be managed carefully and authorities should ensure that accurate forecasts are made of the amounts and timings of future payments and receipts so that cash flow can be managed and the authority can be confident that the project can be afforded both in the short and longer term. Full financial appraisals are likely to be required before any borrowing or public grant approval is given.

5.65. Traditionally loans are obtained from the Public Works Loans Board (PWLB). Where other lenders or alternative forms of financing are being considered, authorities need to seek professional advice to ensure that they are properly informed of the risks and benefits and aware of all the implications.

AGS assertion 3: Compliance with laws, regulations and proper practices

Acting within its powers

5.66. Authorities in England operate within a legal framework which provides them with the necessary statutory powers and authority to deliver local public services. Authorities and their clerks/chief executives/RFOs should always be aware of, and have regard to, the legal power they are exercising when deciding on any action including to spend public money.

5.67. The clerk/chief executive is the authority's Proper Officer and the primary source of advice to the authority as they prepare to make decisions requiring the exercise of their legal powers. It would be unreasonable for an authority to make a decision when it as an entity does not, or members individually do not, understand what legal power they are exercising, or whether the power is current, applicable and correct.

5.68. To assist authorities and their clerks/chief executives/RFOs NALC, SLCC and ADA publish information on their websites.

Regulations and proper practices

5.69. Authorities are subject to a range of regulations, which can change more frequently than primary legislation. It is important, therefore, to be aware of new regulations that are issued as well as keeping up to date with the latest versions of existing ones. NALC, SLCC and ADA provide updates and training on developments in this area.

5.70. Of particular importance in relation to financial practices and procedures are the Accounts and Audit Regulations which cover the procedures authorities must follow in relation to the issuing of notices about the accounts and the exercise of public rights of inspection.

5.71. Also relevant to publication of financial information is the Transparency Code for Smaller Authorities. This requires parish councils, internal drainage boards, charter trustees and port health authorities with an annual turnover not exceeding £25,000 to publish certain information set out in the Code. This enables local electors and local taxpayers to access relevant information about the authority's accounts and governance.

5.72. Parish and town councils with annual turnover in excess of £200,000 should comply with the Local Government Transparency Code 2015.

5.73. Monitoring an authority's compliance with the relevant Transparency Code is not part of the external auditor's limited assurance review of the annual return.

Actions during the year

5.74. As part of its annual governance review to prepare its annual governance statement (see Section 1 of the Guide), an authority needs to scrutinise the actions it has taken during the year, and the decisions that it has made, and satisfy itself that it has acted properly within its powers and in accordance with any relevant Regulations.

AGS assertion 4: Exercise of public rights

5.75. Sections 25 to 27 of the Local Audit and Accountability Act 2014 contain provisions giving interested persons and local government electors certain rights of inspection of the accounts and accounting records. Local government electors may also question the auditor about the accounting records and make an objection to the auditor.

5.76. The rights in Sections 26 and 27 must be exercised within a period of 30 working days, during which period the authority must make the accounts and all supporting records available for inspection on reasonable notice and at all reasonable times.

5.77. In accordance with Regulation 12(3) of the Accounts and Audit Regulations 2015, the authority's RFO is responsible for commencing the 30 working day period as soon as possible after the statement of accounts has been approved by the authority and signed and dated by the person presiding at the meeting at which that approval is given. The RFO must also notify the local auditor of the date on which the period was commenced.

5.78. In accordance with Regulation 15(1), the RFO must ensure that the 30 working day period includes the first 10 working days of July following the end of the financial year to which the accounts relate.

5.79. In accordance with Regulation 15(2), the RFO must publish (including publication on the authority's website):

- the statement of accounts (Section 2 of the annual return) accompanied by:
  - a declaration, signed by the RFO, to the effect that the statement has not yet been reviewed by the external auditor and thus may be subject to change;
- the annual governance statement (Section 1 of the Annual Return); and
- a statement that sets out:
  - the period for the exercise of public rights;
  - details of how a notice should be given of an intention to inspect the accounting records and other documents;
  - the name and address of the local auditor; and
  - the provisions contained in sections 26 and 27 of the Local Audit and Accountability Act 2014 concerning the exercise of public rights.

5.80. In accordance with Regulation 15(3), the period for the exercise of public rights is treated as being commenced on the day after all of these obligations have been fulfilled.

5.81. Where an authority does not have its own website, publication may be on any website, provided that the information is accessible by any member of the public without registration or payment. A parish meeting may instead display the information in question in a conspicuous place in the area of the authority for at least 14 days.

5.82. Assertion 4 in the annual governance statement relates to the exercise of public rights 'during the year' which means in relation to the annual return for the previous financial year. For example, when completing the 2016/17 annual return, assertion 4 refers to the exercise of public rights for the 2015/16 annual return taking place in June/July 2016. The common period of inspection for the 2015/16 annual return is 1 to 14 July 2016. The earliest commencement date of the 30 working day inspection period is 3 June 2016 and the latest commencement date is 1 July 2016.

5.83. Information on the rights of interested persons and local government electors in respect of the accounts of their authority can be found in Council Accounts – a guide to your rights published by the National Audit Office.

Limited assurance review by the external auditor

5.84. In accordance with Regulation 13, after the conclusion of the period for the exercise of public rights, but no later than 30 September, the authority must publish (including on its website) the annual governance statement, statement of accounts and the external auditor's certificate and report – Sections 1, 2, and 3 of the annual return. Authorities must keep copies of these documents for purchase by any person at a reasonable sum and ensure that they remain available for public access for 5 years.

5.85. In accordance with Regulation 16, as soon as reasonably practicable after the conclusion of the external auditor's review, an authority must publish (including on its website):

- a statement:
  - that the review has been concluded and that the statement of accounts has been published; and
  - of the rights of inspection conferred by section 25 of the Local Audit and Accountability Act 2014 in relation to the statement of accounts, auditor's opinion, public interest report and auditor's recommendations;
- the address at which, and the hours during which, those rights may be exercised.

5.86. Where, following completion of the external auditor's review, an authority receives a letter or further report from the external auditor, such as a letter containing statutory recommendations or a Public Interest Report, the members must meet to consider it as soon as practicable. Following this consideration, the authority must publish the letter or report (including on its website) and make copies available for purchase on payment of a reasonable sum.

AGS assertion 5: Risk management

Background

5.87. Risk is an uncertain event or condition that, if it occurs, will have an effect on the achievement of an authority's objectives. Risk management is the process whereby authorities methodically address the risks associated with what they do and the services which they provide. The focus of risk management is to identify what can go wrong and take proportionate steps to avoid this or successfully manage the consequences. Good risk management allows stakeholders to have increased confidence in the authority's corporate governance arrangements and its ability to deliver its priorities.

5.88. Risk management is not just about financial management; it is about protecting the achievement of objectives set by the authority to deliver high quality public services. The failure to manage risks effectively can be expensive in terms of litigation and reputation, and can impact on the ability to achieve desired outcomes. The authority generally and members individually are responsible for risk management.

5.89. Risk management is an ongoing activity that comprises four elements:

- identifying risks;
- assessing risks;
- addressing risks; and
- reviewing and reporting.

Identifying risks

5.90. In order to manage risk, an authority needs to know what risks it faces. Identifying risks is therefore the first step in the risk management process.

5.91. It is not possible to present a suggested list of the specific risks which authorities face as the range, nature, complexity and scale of the business of authorities vary. Similarly, the priorities and service delivery objectives of one authority will differ from those of others. For this reason each authority should identify, for itself, the key risks to achieving successfully its priorities and service objectives. However, there are some typical categories of risks that might help in the process of risk identification:

- financial – loss of money;
- security – fraud, theft, embezzlement;
- property – damage to property;
- legal – breaking the law or being sued;
- IT – failure of IT systems or misuse; and
- reputational – actions taken could harm the authority's public reputation.

Assessing risks

5.92. Once the authority has identified its key risks, the next step is to assess the potential consequences of a risk occurring (impact) and consider how likely this is (likelihood).

5.93. The assessment of potential impact and likelihood need not be any more complex than assigning a simple numerical score, say 1 – 3, and multiplying the two scores to arrive at a risk assessment for each risk of high, medium or low. The risk assessment enables the authority to decide which risks it should pay most attention to when considering what measures to take to manage them.

5.94. Authorities could use a simple risk assessment matrix as follows:

Likelihood				
	Highly likely (3)	Medium (3)	High (6)	High (9)
	Possible (2)	Low (2)	Medium (4)	High (6)
	Unlikely (1)	Low (1)	Low (2)	Medium (3)
		Negligible (1)	Moderate (2)	Severe (3)
			Impact	

Addressing risks

5.95. Risk is unavoidable, and every organisation needs to take action to manage risk in a way which it can justify to a level which is tolerable. The response to risk, which is initiated within the organisation, is called ‘internal control’ and may involve one or more of the following standard responses:

- **Tolerate** the risk - for risks where the downside is containable with appropriate contingency plans; for some where the possible controls cannot be justified (e.g. because they would be disproportionate); and for unavoidable risks, e.g. terrorism.
- **Treat** the risk - a common response which can mean imposing controls so that the organisation can continue to operate; or setting up prevention techniques.
- **Transfer** the risk – buying in a service from a specialist external body or taking out insurance. Some risks cannot be transferred, especially reputational risk.
- **Terminate** the activity giving rise to the risk - it may be best to stop (or not to start) activities which involve intolerable risks or those where no response can bring the risk to a tolerable level.

5.96. Areas where there may be scope to use insurance to help manage risk include the following:

- The protection of physical assets owned by the authority – buildings, furniture, equipment, etc. (loss or damage).
- The risk of damage to third party property or individuals as a consequence of the authority providing services or amenities to the public (public liability).
- The risk of consequential loss of income or the need to provide essential services following critical damage, loss or non-performance by a third party (consequential loss).
- Loss of cash through theft or dishonesty (fidelity guarantee).
- Legal liability as a consequence of asset ownership (public liability).

5.97. The limited nature of internal resources in most authorities means that those wishing to provide services often buy them in from specialist external bodies. Areas where there may be scope to work with others to help manage risk include the following:

- Security for vulnerable buildings, amenities or equipment.
- Maintenance for vulnerable buildings, amenities or equipment.
- The provision of services being carried out under agency/partnership agreements with principal authorities.
- Banking arrangements, including borrowing or lending.
- Ad hoc provision of amenities/ facilities for events to local community groups.
- Markets management.
- Vehicle or equipment lease or hire.
- Trading units (leisure centres, playing fields, burial grounds, etc.).
- Professional services (planning, architects, accountancy, design, etc.).

Reviewing and reporting

5.98. Once the key risks have been identified and assessed they should be recorded, for example in a risk register. Members should review the risk register on a regular basis. This could be achieved by risk management being a standing item at authority or committee meetings.

5.99. An example of a simple risk register can be found in Appendix 1 on page 34.

5.100. Support for authorities wishing to improve their risk management arrangements, over and above that provided by this guidance, is available through training that may be requested from NALC, SLCC and ADA, or from other training providers. In identifying training needs, parish and town councils may wish to seek the professional input of their insurance provider and refer to various elements of the National Training Strategy for town and parish councils in England.

AGS assertion 6: Internal audit

5.101. Section 4 of the Guide sets out the non-statutory 'guidance' referred to in Regulation 5(1) of the Accounts and Audit Regulations 2015, and needs to be taken into account by smaller authorities in undertaking an effective internal audit.

5.102. In addition to the information in Section 4, authorities may wish to consider the following list of the key systems and processes they can ask internal audit to review from time to time as part of its work:

- proper book-keeping including the cash book;
- standing orders and financial regulations;
- payment controls;
- income controls;
- budgetary controls;
- petty cash procedure;
- payroll controls;
- asset control;
- bank reconciliations;
- year-end procedures; and
- risk management arrangements.

5.103. This is not an exhaustive list and each authority will need to agree a specific programme of work with its internal audit provider each year.

5.104. Authorities should note that it is not part of internal audit's responsibility to review or 'sign off' the completed annual return. Internal audit report(s) should inform the authority's responses to assertions 2 and 6 in the annual governance statement. Internal audit reports should therefore be made available to support and inform members considering the authority's approval of the annual governance statement.

AGS assertion 7: Reports from auditors

5.105. Authorities will receive reports from both their internal and external auditors. An authority should consider the matters included in these reports and decide what action it needs to take to prevent recurrence of the issues raised. The consideration and decisions should be included in formal minutes.

5.106. Information regarding internal audit reporting is provided in paragraphs 4.18 to 4.20 of Section 4 of the Guide.

5.107. External auditors are required to carry out their work in accordance with the Code of Audit Practice and supporting guidance issued by the National Audit Office. Auditor Guidance Note 2 (AGN02) provides the specified procedures that auditors follow when undertaking limited assurance engagements at smaller authorities.

5.108. The formal terms of engagement between external auditors and authorities are set out in the Statement of responsibilities of auditors and audited bodies issued by Public Sector Audit Appointments Limited. It summarises where the different responsibilities of auditors and of the authority body begin and end, and what is to be expected of the authority in certain areas.

AGS assertion 8: Significant events

5.109. The authority needs to have considered if any events that occurred during the financial year (or after the year-end), have consequences, or potential consequences, on the authority's finances. If any such events are identified, the authority then needs to determine whether the financial consequences need to be reflected in the statement of accounts.

5.110. For authorities accounting on a receipts and payments basis, the review of significant events should cover events that occurred during the financial year to ensure that they have been included in the accounting statements where appropriate.

5.111. For authorities accounting on an income and expenditure basis, the review of significant events should also cover events that occurred after the financial year-end but before the accounting statements are approved by the authority.

AGS assertion 9: Trust funds (local councils only)

5.112. Certain local authorities have powers to be appointed as trustee of local, usually charitable, trusts and fulfil this role as either custodian or managing trustee.

5.113. Charitable trusts in England are regulated by the Charity Commission which sets out minimum standards of accounting and audit requirements where these are not covered by the Trust Deed. The Charity Commission also requires annual reporting by registered charities.

5.114. Larger authorities meet this requirement via disclosure in the notes to the accounts which are covered by an audit opinion. For smaller bodies preparing an annual return there are no provisions for notes and so the required disclosure is achieved through a simple disclosure in the annual return.

5.115. If the authority has disclosed that it is a sole managing trustee it must also complete the associated assertion in the annual governance statement. In this way, small bodies meet the legal requirement to disclose each 'account of the body'. Auditors plan work around these disclosures as required.

5.116. Authorities should ensure that a separate bank account operates to receive income for each trust to which it is a managing trustee. If, exceptionally, the authority's bank account is used to receive monies intended for the trust or to pay for any expenditure on behalf of a trust (prior to recovery from the trust account), then these transactions, including any VAT, must be included in the annual return of the authority as being its own expenditure and income during the year and to the extent that they are yet to be recovered or paid over reconciled as debtor and creditor amounts. However, to simplify accounting and ensure separation, a separate bank account should be established for any trust as soon as possible and funds should never or only exceptionally mixed. The reserves of the authority should not include those belonging to any trust.

5.117. Meetings of the authority when it is acting as charity trustee must take place separately from those of the authority acting as the authority. Separate minutes must be kept. In order to avoid confusion, trust business should always be minuted separately from authority business. Separate notices and agendas for meetings should be issued.

5.118. The clerk should take responsibility for guiding the authority regarding the capacity, either as the authority or as trustees for a charity, in which members are meeting. The chairman should make clear to the meeting, at the outset and throughout, the capacity in which it is meeting, particularly if authority and trust meetings are held one after the other or where confusion around capacity is possible.

5.119. The value of trust property must not be shown in the authority's books of account and on the annual return as authority property. Trust assets held by the authority as custodian or managing trustee should, however, be recorded in the authority's asset register and identified there as 'charity assets held by the authority as trustee' with their value excluded from the total.

Accounting statements[1]

Reporting on an income and expenditure basis

5.120. Current rules require authorities where the gross income or expenditure for the year (whichever is the higher) has exceeded the threshold of £200,000 for a period of three continuous years, to report their financial details on an income and expenditure basis, from the third year onwards. Authorities operating below the £200,000 threshold have the option to report either on an income and expenditure basis or on a receipts and payments basis.

5.121. The receipts and payments basis requires authorities only to consider their actual bank and cash transactions. The entries for the annual return will usually be taken straight from the summary totals in the cash book.

5.122. For authorities with annual turnovers between £200,000 and £6.5 million the annual return has to be prepared on an 'income and expenditure' basis. In income and expenditure accounts, the transactions for the year comprise all those instances in the twelve months where the authority has received economic benefits or given others economic benefits (irrespective of the year in which they are paid for).

5.123. For example, suppose an authority has its offices re-roofed in March but the builders do not issue an invoice until April and the authority does not settle the bill until May. The cash book will record a bank outgoing in May of the new financial year. However, the authority will have received the benefit of the works before the end of the financial year in March and have an obligation to pay the builders, even though their invoice has not arrived to confirm the exact amount due. In order to show the proper financial position of the authority for the previous financial year, expenditure should be recognised in March.

5.124. In contrast, someone might put down a refundable deposit in February on a booking for the hall in June. The cash book would record a cash receipt in February. However, the authority will not be providing any economic benefits to the booker (i.e. use of the hall) until June of the new financial year, and would be unwise to spend the cash receipt until the event takes place. The receipt would not then count as income in the previous financial year and would be treated as a prepayment to be accounted for in the new financial year.

5.125. Income and expenditure accounting thus gives a more sophisticated presentation of an authority's true financial position, focusing on the balance of economic benefits that it has under its control, rather than just its bank balance.

5.126. Very few authorities will actually maintain their books of account on an income and expenditure basis. The cash book will be the main focus for day-to-day accounting and

[1] Accounting statements for joint arrangements, which may include joint committees, are no longer required under legislation and so the proper practices, supporting information and examples contained in the Guide do not apply to joint arrangements. Authorities should, however, understand the risks associated with how their share of the assets and liabilities is used by any joint arrangement in which they participate, as well as their share of annual income and expenditure employed in delivering the service managed by a joint arrangement. Authorities should also make sure that the appropriate shares of income, expenditure, assets and liabilities (including any year-end balances), are included as necessary within their own accounts. Joint arrangements are not bodies corporate and may not own assets, hold bank accounts in their own name, have employees or enter into any form of contract.

balancing off and reconciliation to the bank statement, and remains the most important control over the accounting system. Subsidiary records will be kept of the authority's debtors (people who owe the authority) and creditors (people the authority owes) based on invoices, but transactions will be made in the cash book for this activity only when cheques and cash are actually received or payments are made. This means that there will need to be a special exercise at the end of each financial year to convert the receipts and payments record represented by the cash book into the income and expenditure account required by section 2 of the annual return.

5.127. The exercise is a little complicated because care has to be taken to make adjustments for both ends of the financial year. For example, as well as adding in amounts owed at the end of the year that are not in the cash book, payments that are in the cash book but relate to amounts owed at the end of the previous year have to be taken out. The adjustments required comprise the following:

- **Debtors:** situations where the authority has provided goods or services before the end of the year, but has not yet been paid for them by 31 March. To convert 'receipts' into 'income' take the cash book totals for receipts and deduct the amount of debtors brought into the calculation of income for the previous year and add the amount of debtors outstanding at the end of this year.
- **Receipts in advance:** situations where the authority has received cash before the year end, but has not yet provided the relevant goods and services by 31 March. To convert 'receipts' into 'income' take the cash book totals for receipts and add the amount of receipts in advance excluded from the calculation of income for the previous year and deduct the amount of receipts in advance held at the end of this year.
- **Creditors:** situations where the authority has received goods or services before the end of the year, but has not yet paid for them by 31 March. To convert 'payments' into 'expenditure' take the cash book totals for payments and deduct the amount of creditors brought into the calculation of expenditure for the previous year and add the amount of creditors outstanding at the end of this year.
- **Deferred Grant:** arises only in situations where the authority receives a grant before the year end but some or all of the grant has not been spent by 31 March and the grant conditions require repayment of any balance not spent on the specified purpose for which the grant was given. To convert 'receipts' into 'income' take the cash book total of receipts and add the amount of deferred grant excluded from the calculation of income for the previous year and deduct the amount of grant held at the end of this year.
- **Prepayments:** situations where the authority has paid cash before the year end, but has not yet received the relevant goods or services by 31 March. To convert 'payments' into 'expenditure' take the cash book totals for payments and add the amount of prepayments excluded from the calculation of expenditure for the previous year and deduct the amount of prepayments made at the end of this year.
- **Stock:** consumable goods (for example bar supplies) purchased before the end of the year but which have not been used by 31 March. To adjust for stock in expenditure take the cash book totals for payments and add the amount of stock brought forward as an asset from the previous year and deduct the amount of stock held at the end of this year.

- **Provisions:** any other situation in which the authority has an obligation to make a payment, but it is uncertain when the payment will be due (for example, a claim has been made for compensation against the authority that is likely eventually to result in the authority making recompense). This is only likely to occur in rare circumstances. To adjust for provisions in expenditure take the cash book totals for payments and add the value of any provision that needs to be made for events taking place in this year and deduct the value of any provisions made in previous financial years and brought forward, to this financial year and where payment has been made to settle the obligation and those no longer required.

5.128. Authorities will need to have effective arrangements in place to identify and calculate the adjustments needed. These will include:

- deciding on a level of materiality for adjustments – income and expenditure needs to be shown fairly, but excessive accuracy is not beneficial. For instance, most authorities will have utilities bills that include prepayments for standing charges and payments in arrears for energy consumption that strictly should be adjusted for into their appropriate years. As this is a regular item of expenditure it is not usually worth apportioning individual bills across financial years, but just ensuring that four bills (if payable quarterly) are charged each year;
- making sure that a record is retained of the adjustments that were made in preparing the income and expenditure accounts for the previous financial year;
- examining entries in the cash book before 31 March for possible receipts in advance and prepayments and entries after 31 March for possible debtors and creditors;
- examining invoices after 31 March for possible debtors and creditors; and
- considering whether the authority has any other obligations arising from events that took place before 31 March that mean it will not be able to avoid making a payment at some time after 31 March.

5.129. For authorities reporting on the receipts and payments basis, the amount of VAT charged to customers and the VAT refund made by HMRC will be included in Line 3 (total other receipts); the amount of VAT paid to suppliers and any paid to HMRC will be included in Line 6 (all other payments).

5.130. For authorities reporting on an income and expenditure basis the amounts of VAT collected from customers, paid to suppliers, and payable to, or repayable by, HMRC will be posted to a Creditor Account which will result in a balance due to, or from, HMRC. This balance will be included in Creditors or Debtors as appropriate – i.e. in this case the only value of VAT to be included in the annual return figures will be any that is to be written off as irrecoverable (usually due to a partial exempt position on VAT).

Total other receipts (Line 3)

5.131. Proceeds from the disposal of fixed assets are known as capital receipts and are subject to statutory controls[2]. Such proceeds cannot be used for revenue purposes and can only be used for capital purposes - that is the purchase of fixed assets, the making of capital grants, or the repayment of long-term loans. Authorities should keep separate records so that they can demonstrate compliance with this requirement. Where the total proceeds from the

[2] The Local Authorities (Capital Finance and Accounting)(England) Regulations 2003 apply only in relation to local authorities in England so do not apply to IDBs.

sale of a fixed asset is below a specified amount, currently £10,000, it is deemed to be *de minimis* and these requirements do not apply.

5.132. This does not affect the requirement to include such amounts in Line 3 when they are received, but is necessary to ensure that the authority complies with the appropriate statutory provisions.

Loan interest/capital repayments (Line 5)

5.133. Many authorities will not have any borrowings and will not therefore have interest or capital payment transactions. For those that have borrowed from the PWLB, the figure will be the payments made in the year in accordance with the PWLB repayment schedule.

5.134. If an authority goes overdrawn at the bank, then any interest or charges paid as a result of the overdraft should be included in this line. Bank charges other than those arising as a result of temporary borrowing should be included in Line 6.

Total value of cash and short-term investments (Line 8)

5.135. Short-term investments are defined in paragraph 2.21 of Section 2 of the Guide.

5.136. Where an authority holds short-term investments such as deposit or savings accounts, all year-end balances must be reported in detail within the bank reconciliation and be included in the sum of Line 8. Auditors may seek to confirm these account balances from time to time.

Total fixed assets plus long-term investments and assets (Line 9)

Fixed assets

5.137. The term fixed assets means property, plant and equipment with a useful life of more than one year used by the authority to deliver its services. Fixed assets are also known as non-current assets.

5.138. Fixed assets acquired in any year should be added to the asset register for management purposes (see paragraphs 5.54 – 5.61 for information about managing fixed assets). For accounting purposes, acquisitions and disposals of fixed assets should be treated as any other purchase or sale and recorded as part of annual payments or receipts, expenditure or income.

5.139. Proper practices in Section 2 of the Guide state that the value of the cell at Line 9 is taken from the authority's asset register which is up to date at 31 March and includes all capital acquisition and disposal transactions recorded in the cash-book during the year. A particular method of asset valuation is not specified in proper practices so authorities may use any reasonable approach to be applied consistently from year to year. The method of asset valuation adopted should be set out in a policy approved by the authority and recorded in the asset register.

5.140. For authorities covered by this Guide, an appropriate and commonly used method of fixed asset valuation for first registration on the asset register is at acquisition cost. This means that in most circumstances once recorded in the asset register, the recorded value of the asset will not change from year to year until disposal. Commercial concepts of depreciation, impairment adjustments, and revaluation are not required or appropriate for this method of asset valuation. For reporting purposes therefore, the original value of fixed assets will stay constant throughout their life until disposal.

5.141. If for some reason the authority decides that the basis of valuation should be changed, the change must be applied consistently to all relevant classes of fixed assets. In such an event, the value shown in Line 9 for the previous year should also be changed to the new basis and clearly marked as 'RESTATED'. The authority should provide a justification and explanation for the change.

Long-term investments

5.142. An authority may also hold assets in the form of long-term investments. Long-term investments are defined in paragraph 2.24 of Section 2 of the Guide. On acquisition, long-term investments should be recorded in the cash book as expenditure and therefore appear as part of the total in Line 6 (all other payments). Any asset created in this way should also be recorded on the asset register at its purchase cost. At year-end the asset will also appear within the sum at Line 9.

5.143. Where an authority acquires an investment with a fixed maturity date (for example, a three year savings bond), the investment should be accounted for as expenditure in the year (Line 6) and also as an increase in assets and long-term investment (Line 9) until its maturity. At maturity, the total (gross) proceeds should be recorded as income in Line 3 (total other receipts).

5.144. Any transaction costs should be recorded as other expenditure in Line 6. At maturity, the original acquisition value of the investment asset (which will remain unchanged over its term for the purposes of the annual return) should be removed from the total in Line 9.

5.145. Long-term investments should be recorded in the asset and investments register at original cost at acquisition (the purchase price) which for accounting purposes will remain unchanged until disposal. It is recognised that the market value of long-term investments may change over time; therefore, at each year end, the RFO should make a note in the asset register of the notional market value of each investment as at 31 March to inform readers. However, any real gain or loss compared to purchase cost will only ever be accounted for at the time of disposal when the total proceeds from the investment will be included in Line 3.

5.146. Any dividend or interest payments received during the year from investments should be recorded as income and reported in Line 3. Where the authority has made a contract to the effect that any dividends or interest receivable from an investment are 'rolled up' and only paid to the authority on the maturity of the investment (for example, as may be the case with certain fixed-term bonds), the 'rolled up' dividend and/or interest should only be reported in Line 3 if it has actually been received, that is, on the maturity of the investment.

5.147. When the authority has incurred expenditure by making a loan, grant or other financial assistance to a third party this transaction should be recorded as an expenditure item in the cash book. Any loan or other repayable amount should be added to the asset and investments register. The outstanding amount of any third party loan at 31 March each year, excluding interest, falls to be reported in the sum of Line 9. Any repayment of a loan or part of it, or any interest received should be recorded as an income item in the cash book when received and reported in annual return Line 3. This receipt will also be reflected as an increase in Line 7 (balances carried forward). Any repayments of loan principal must also be applied to reduce the amount of the loan outstanding on the asset and investments register.

5.148. When an authority receives shares following a de-mutualisation of a building society or similar institution this also creates a long-term asset.

Total borrowings (Line 10)

5.149. This figure will be the total amount outstanding at 31 March. If an authority has borrowings, they will usually be in the form of long-term loans from the PWLB. The capital value of instalment finance, including HP or leases which have not been classed as borrowing by DCLG, should not be included here. The total borrowings at 31 March should be easily calculated by reference to official loan schedules. The total borrowings figure in Line 10 should include the current portion of long-term debt.

Accompanying information

5.150. Authorities are required to provide to the external auditor certain supporting documentation for the accounting statements in section 2 of the annual return. These documents are the year-end bank reconciliation and an explanation of significant variances. These are minimum requirements and the auditor may ask for other information which the authority should provide. However, authorities should only send to the auditor the information that has been specifically requested.

Bank Reconciliation

5.151. The most important document to be provided is the bank reconciliation as it confirms the authority's books of account are supported by the bank's records. Because of its importance, the reconciliation should be prepared in sufficient detail so that it is clear what the year-end cash book and bank account balances are, and the nature of the items that reconcile the difference can be seen. The authority should carry out a separate reconciliation for each bank account operated by the authority although the results may then be summarised. The bank reconciliation should agree to the figure in Line 8 of Section 2 of the annual return.

5.152. See paragraphs 5.21 to 5.26 for more information about bank reconciliations. A standard layout for a financial year-end bank reconciliation can be found at Appendix 1 on page 33.

Explanation of significant variances

5.153. The other supporting documentation required to accompany the annual return is a brief explanation of significant variations from year to year between the figures in Section 2 of the annual return. 'Significant' is defined as being worthy of attention. A significant variance is one that would be of interest to the authority and to the public when looking at the figures in Section 2 of the annual return.

5.154. The purpose of showing comparative values in financial statements is so that the reader can observe and note any changes in levels of activity from one year to the next. The absence of significant variances from one year to the next implies that the authority has continued to provide expected services at the same level and approximately at the same cost as previously. Readers are therefore drawn to any items which are significantly different or unusual, as representing a possible change in the scope or level or cost of services they have come to expect.

5.155. The reason for providing the explanation of significant variances to the external auditor is to support the auditor's review of the figures in Section 2 of the annual return and to demonstrate the authority's understanding of its accounts and their movements. The auditor will compare the current year's figures to the previous year's figures to identify any differences. Where there are significant differences, the auditor may be concerned that the figures for the current year could be incorrect. Authorities will be able to remove this doubt by providing clear and complete explanations for the differences.

5.156. For example, a reasonable expectation may be that staff costs should rise each year only by the level of wage inflation. Thus, if the clerk's remuneration had risen, from £2,500 in the previous year to £2,575 (3 per cent), this could reasonably be assumed to be attributable to a cost of living increase. However, if the remuneration had risen to £2,900, i.e. by 16 per cent, then the authority would need to explain the reason for the increase, to demonstrate that a mistake had not been made in recording staff costs. If the explanation was that the authority had implemented tighter new financial procedures that required the clerk to work more hours a week, this should be set out in a note which can be provided to the auditor.

5.157. Any change, or even the absence of change when one might be expected, can be considered as significant and the RFO should be prepared to explain any figure presented in the accounting statements. Generally, changes (either up or down) of 10 to 15 per cent and greater will almost certainly require a formal explanation. If the external auditor states a percentage figure in their letter accompanying the annual return, authorities should comply with it.

5.158. Where the value in Line 7 of Section 2 of the annual return does not equal the value in Line 8, this difference should be explained. This difference should only occur in cases where the authority's accounts are presented on an income and expenditure basis, and the most common explanation is the effect of debtors and creditors in the authority's statement of balances. It should be possible to provide the auditor with details of the year-end debtors and creditors showing how the net difference between them is equal to the difference between Lines 7 and 8.

5.159. In deciding what needs to be explained, authorities should think about noting the following:

- one-off items of spending or income from last year and this year;
- regular items of spending and income where the relevant activity (for example the number of hall bookings) has risen or fallen between the two years or where prices have not changed in line with inflation (for example a price freeze on charges for hall rentals);
- items of spending and income that used to be regular but which were made for the last time last year and do not feature in the current year (for example a grant to a sporting association that went out of existence); and
- items of spending and income that were made for the first time in the current year and will be made regularly in future years (for example running expenses for a newly opened one stop shop facility).

5.160. As authorities have no legal powers to hold revenue reserves other than those for reasonable working capital needs, or for specifically earmarked purposes, whenever an authority's year-end general reserve is significantly higher than the annual precept or rates and special levies, an explanation should be provided to the auditor.

Appendix 1: Example documents

Bank reconciliation

A standard layout for financial year-end bank reconciliation might look something like this. The model can be applied for reconciliations carried out at any time of the year.

Bank Reconciliation	**Financial year ending 31 March 20XX**	
Authority Name		
Prepared by__________________ (Name and role (Clerk/RFO etc)) Date_____________		
Approved by__________________ (Name and role (RFO/Chair of Finance etc)) Date_____________		
Balance per bank statements as at 31 March 20XX	**£**	**£**
eg Current account	1,000.00	
High interest account	3,000.00	
Building society premium a/c	10,000.00	
Petty cash balance	10.00	
		14,010.00
Less: any un-presented cheques at 31 March (normally only current account)		
Cheque number 000154 000157 000158	(60.00) (18.00) (2.00)	 (80.00)
Add any unbanked cash at 31 March		
eg Allotment rents banked 31 March (but not credited until 1 April)	50.00	50.00
Net bank balances as at 31 March 20XX		**13,980.00**
The net balances reconcile to the Cash Book (receipts and payments account) for the year, as follows		
CASH BOOK Opening Balance Add: Receipts in the year Less: Payments in the year	 15,280.00 6,500.00 (7,800.00)	
Closing balance per cash book [receipts and payments book] as at 31 March 20XX (must equal net bank balances above and Section 2, line 8)	**13,980.00**	

Risk register

A simple risk register might look something like this:

Risk no.	Description (The risk is that…)	Impact (The impact on the authority would be…)	Likelihood score (1-3)	Impact score (1-3)	Risk rating (High, medium, low)	Response (What actions have been taken)
1	Items from the village hall may be damaged or stolen.	The cost of repair and replacement.	2	2	Medium (4)	Security arrangements reviewed and insurance in place.
2						
3						
4						