Manchester City Council

Audit of Accounts 2010/11
Annual Report to those Charged with Governance

16 September 2011

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1 Executive Summary

Purpose of the report

ISA 260 requires communication of:
- relationships that have a bearing on the independence of the audit firm and the objectivity of the engagement team
- nature and scope of the audit work
- the form of reports expected.

1.1 This report has been prepared for the benefit of discussion between Grant Thornton UK LLP and the Audit Committee of Manchester City Council (the Council). The purpose of this report is to highlight the key issues arising from the audit of the Council's financial statements for the year ending 31 March 2011.

1.2 This report meets the mandatory requirements of International Standard on Auditing 260 (ISA 260) to report the outcome of the audit to 'those charged with governance', designated as the Audit Committee. The requirements of ISA260, and how we have discharged them, are set out in more detail at Appendix A.

1.3 The Council is responsible for the preparation of financial statements which record its financial position as at 31 March 2011, and its income and expenditure for the year then ended. We are responsible for undertaking an audit and reporting whether, in our opinion, the Council's financial statements present a true and fair view of the financial position.

1.4 Under the Audit Commission's Code of Audit Practice we are also required to reach a formal conclusion on whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Audit conclusions

Financial Statements Opinion

1.5 This year presented significant challenges to the Council's finance team as, for the first time, the Council was required to produce its accounts under the International Financial Reporting Standards (IFRS) based CIPFA Code of Practice ('the Code') which came into effect from 1 April 2010.

1.6 The Council performed well in producing a good draft set of accounts which were certified by the City Treasurer on 29 June 2011. Although member approval of draft accounts is no longer a formal requirement, the Council demonstrated good engagement with members by presenting the accounts and discussing key issues at a member briefing.

1.7 As in previous years, the draft accounts were of a high quality and the accompanying working papers were of a good standard. The Council's finance team has worked proactively with us to resolve issues as they have emerged, which has helped the audit to progress smoothly, representing a significant achievement in the first year of IFRS.

1.8 The quality of the accounts is reflected in the small number of audit adjustments required which are largely presentational in nature and do not impact on the Council's General Fund. The most significant adjustments we have discussed and agreed with management relate to:

- the removal of the Wright Robinson School (a PFI funded school) from the balance sheet to ensure consistency with accounting policies as the school became a Foundation School on 1 March 2010. The 2009/10 comparative figures have also therefore been amended

- separating payments made to the contractors for two of the Council's housing PFI schemes, which are not included within the PFI agreements, from those included within the financial models

- improvements to the presentation of the Group accounts and a number of amendments to ensure the accurate consolidation of group entities.

1.9 The Council remains in dispute with Manchester Teaching Primary Care Trust in relation to the amount of overspend attributable to the Council from 2009/10 and the amount of contributions to be paid for 2010/11. This is an issue that we have referred to in several previous audit reports and the Council should, as a matter of urgency, resolve the dispute.

1.10 Looking to the future, following inconsistency in the accounting treatment for schools across Local Government nationally, CIPFA has issued a consultation document, with a response deadline at the end of September. For 2011/12, the Council should ensure its accounting policies are in accordance with the final guidance issued.

1.11 We anticipate providing an unqualified opinion on the Council’s financial statements, following approval of the accounts by the Audit Committee on 29 September 2011.

1.12 Further details of the outcome of our financial statements audit are given in Section Two and Appendix B and C (adjustments to the financial statements and action plan).

Value for Money Conclusion

1.13 In providing our opinion on the financial statements, we are required to reach a conclusion on the adequacy of the Council's arrangements for ensuring economy, efficiency and effectiveness in its use of resources (the Value for Money conclusion). We are pleased to report that we propose to issue an unqualified Value for Money conclusion.

1.14 The key messages arising from our review of the Council's arrangements will be discussed with the Council's senior management team and will be summarised in our 2010-11 Annual Audit Letter, which will be issued to management in October 2011 and is due to be presented to the Audit Committee on 3 November 2011. We will also issue a separate 'Financial Resilience' report to management in September 2011 summarising our key findings and this will be presented to the Audit Committee on 3 November 2011.

Action required by the Audit Committee

1.15 The Audit Committee is asked to:

- confirm that it is not aware of any risks, including fraud risks, that may have a material impact on the accounts
- confirm the proposed audit adjustments (Appendices B)
- note the attached Action Plan to address the identified procedural issues (Appendix C)
- note the attached Letter of Representation for approval by the Council (Appendix D).

The way forward

1.16 Matters arising from our audit have been discussed with the City Treasurer. Proposed audit adjustments are set out at Appendices B and recommendations made to address procedural issues are summarised at Appendix C.

Use of this report

1.17 This report has been prepared solely for use by the Council to discharge our responsibilities under ISA260, and should not be used for any other purpose. We assume no responsibility to any other person. This report should be read in conjunction with the Statement of Responsibilities and the Council's Letter of Representation, included at appendix D.

Acknowledgements

1.18 We would like to record our appreciation for the assistance and co-operation provided to us during our audit by the Council’s staff.

Grant Thornton UK LLP

16 September 2011

2 Detailed Findings

Introduction

2.1 This section provides a summary of findings arising from our audit of the financial statements.

Status of the audit

2.2 We carried out our audit in accordance with our Accounts Audit Plan, which was presented to the Audit Committee on 27 January 2011. Our audit is substantially complete, subject to the following finalisation procedures:

- review of the final version of the financial statements
- auditing the Council's Whole of Government Accounts return
- obtaining and reviewing the Council's Letter of Representation
- updating our post balance sheet events review, to the date of signing the accounts.

2.3 We anticipate providing an unqualified opinion on the Council’s financial statements and group accounts, following approval of the accounts by the Audit Committee on 29 September 2011.

Accounts Preparation

2.4 The Council produced its draft 2010/11 accounts in accordance with the Accounts and Audit (England) Regulation 2011, which came into effect from 31 March 2011. The accounts were produced and certified by the City Treasurer on 29 June 2011 and presented for audit in advance of the 30 June 2011 statutory deadline.

2.5 The accounts are compiled under the the International Financial Reporting Standards (IFRS) based CIPFA Code of Practice ('the Code') for the first time and training with members of the Audit Committee took place on 30 June 2011. The accounts were formally presented to the Audit Committee on 7 July 2011, which is in accordance with best practice.

2.6 In our interim report we identified slippage in the Council's restatement timetable and made recommendations to ensure appropriate accounting. We are pleased to report that the Council completed the IFRS restatement exercise to a good standard reflecting early resolution of emerging accounting issues through regular liaison meetings in advance of the compilation of the accounts. As in previous years, the working papers were of a good standard and were presented for audit through an electronic working papers library and our requests for additional audit evidence were responded to in a timely manner by Council officers.

2.7 We have identified several improvements that can be made to the Council's audit trail supporting some entries in the accounts and we will discuss these with the finance team to assist with the preparation of the 2011/12 accounts.

Financial Position

2.8 The Council has reported a £1,876,000 overall underspend against budgets, with a decrease of general reserves during the year of £1,366,000 against a budgeted reduction of £3,242,000. The Council's levels of reserves continues to underpin a strong financial position, as demonstrated in 2010/11 by the Council being able to fund the £39m unbudgeted costs of Voluntary Early Retirement and Voluntary Severance schemes with further costs to be funded during 2011/12.

2.9 The current economic climate has placed significant pressure on the public sector, and local government in particular to generate efficiencies and operate within reduced resources. The Council is well placed to deal with these challenges having a strong record of managing its budget outturn and has established appropriate planning and governance arrangements to plan and monitor delivery of required savings going forward.

Key risks

2.10 Our 2010/11 Accounts Audit Plan set out the key risks relating to the audit of the financial statements. As part of our interim audit, we completed work in a number of areas to consider the audit risks identified and reported our findings in our Interim Audit Report, presented to the Audit Committee in June 2011.

2.11 Our work at that time enabled us to conclude on a number of key risk areas and identified emerging accounting issues. As part of our final accounts audit, we reviewed the remaining audit risks and emerging accounting issues and have set out in Exhibit One the outcome of work completed. Our review of the risks facing the Council has not identified any additional risk areas.

Exhibit One: Key findings arising from our review of IFRS restatement

Accounting requirement	Council's position
Accounting for Schools	
In our interim report we highlighted the national inconsistencies across authorities in accounting for schools, with some types of school accounted for within the Council's balance sheet (such as community and voluntary controlled schools) and others excluded (such as voluntary aided and foundation schools). Following the interim audit, CIPFA issued a Consultation document in July on the future accounting for different types of school. The Consultation is currently open for comment and is expected to be finalised in time to	The Council's accounting policy is to account for foundation schools as off balance sheet. However, Wright Robinson College has been accounted for as on balance sheet as it was funded through PFI, which is not consistent with the Council's accounting policy. The Council has agreed with our recommendation to remove the school from the accounts at the date it obtained foundation status. This reduces assets on the balance sheet by £42.1m, with the PFI liability remaining. Upon receiving support for the change in status the Council identified that Wright Robinson College actually obtained

Accounting requirement	Council's position
impact on the 2011-12 accounts. In summary, the Consultation proposes taking all voluntary aided, voluntary controlled and foundation schools off the balance sheet from 2011-12, including any PFI financed schools of these types.	Foundation status on 1 March 2010. As such the Council has amended the accounts through restating the 2009/10 balances. The Council has also performed a review to ensure no other school has changed status. We have recommended further disclosures to the accounts and accounting policies to reflect the accounting treatment of schools within the accounts. The Council has updated the accounts to reflect these recommendations. Once finalised and published, we will be discussing the CIPFA guidance for accounting for schools with the finance team as part of our 2011-12 audit.
Recognition of grants	
The Code requires capital and revenue grants to be recognised fully when grant conditions are met and removes previous accounting treatments for deferred government grants.	The Council has undertaken a detailed review of grants against the Code requirements. We have reviewed the methodology used by the Council and sample tested significant grants and conclude the Council has recognised grants in accordance with the Code.
Accounting for leases, embedded derivatives and service concessions	
The Code requires the Council to assess the treatment of all leases and service concessions to identify whether these should be recognised on the Council's balance sheet. A significant element of this review was undertaken for the 2009/10 accounts, because of the early adoption of these requirements for PFI schemes. Our 2009/10 audit confirmed the accounting treatment for PFI schemes was in accordance with the Code.	The Council has now completed the exercise to identify all leases and potential service concessions. Our review and sample testing confirmed the Council has accounted for leases and potential service concessions in accordance with the Code, following some presentational amendments to the disclosure notes. However, we identified, as in the prior year, that the Council does not maintain copies of all schools leases and recommend that copies are maintained centrally to support the accounts (**recommendation 1**).
Accounting for employee benefits	
The Code requires employee benefits to be accounted for as they are earned by the employee requiring accruals for items such as holiday pay. Additional guidance has been issued by CIPFA to enable the Council to calculate the accrual relating to teachers' holiday pay.	We have reviewed the Council's methodology and calculations and conclude that the accrual for teachers' holiday pay has been calculated in accordance with the CIPFA guidance. Following our recommendation in the interim report, the Council has reviewed

Accounting requirement	Council's position
	the appropriateness of the calculation against the employee benefit policy and confirmed no material change has occurred. Narrative is included within note 5.6 detailing the basis for the estimate included within the accounts.
Assets held for sale	
The Code introduces a new classification of 'non-current assets held for sale' if its carrying amount will be recovered principally through a sale transaction rather than through continued use.	We have agreed the approach adopted by the Council to identify and account for assets held for sale. Our audit identified two assets totalling £10,716,000 included within surplus assets which meet the accounting definition of an asset held for sale as plans are in place to transfer the assets. The Council has amended the accounts to correctly classify these assets.
Segmental reporting	
The Code requires the Council to present information on reportable segments, based on the Council's internal management reporting, within the notes to the accounts. An authority need not report all operating segments, however, should include all segments where expenditure or income is more than 10% of gross expenditure or income in the net cost of services.	We have reviewed the Council's working paper to support the segmental reporting disclosure note and confirm that this is in accordance with the requirements.
Component accounting	
The Code places greater emphasis on reporting components of assets and derecognising parts of an asset that are replaced. This accounting treatment is applicable to expenditure which is incurred from 1 April 2010 that enhances the value of assets.	The Council has complied with the Code requirements for component accounting. We recommended enhanced disclosures to the notes to the accounts and accounting policies, which the Council has processed.
Accounting policies	
Following the adoption of the Code and introduction of IFRS, the Council is required to review and update its accounting policies.	We have reviewed the accounting policies adopted by the Council and agreed some amendments to ensure they are consistent with the Code. The Audit Committee approved the draft accounting policies in June 2011 and should approve the final accounting policies included in the final accounts.
'Clarified' International Standards on Auditing	
There are increased expectations on	We have reviewed the Council's

Accounting requirement	Council's position
auditors arising from the 'Clarified' International Standards of Auditing (Clarified ISAs) in determining the material accuracy of accounting estimates and judgements and increased involvement throughout the audit process of group subsidiaries.	disclosure note in relation to Key Sources of Estimation and Uncertainty and confirm that this is in accordance with the accounting policies adopted by the Council. We recommended further disclosures, which the Council has included in the final accounts. In undertaking the audit of the Group Accounts, we have reviewed the responses to the Group Instructions received from the auditors of Manchester Airport Group and concluded that no revision was required to our planned audit procedures.
Accounting for Town Hall Extension	
The Town Hall extension and central library are currently being refurbished as part of the Council's transformation programme. During this period of refurbishment staff and facilities have been temporarily relocated to a leased property at One First Street. The Council need to determine how these assets will be categorised and valued within the accounts during the refurbishment.	The Council has disclosed the Town Hall extension and central library as 'Assets Under Construction'. We have reviewed this accounting treatment and confirm that this is in accordance with the Code.
Accounting for PFI schemes	
The Council brought its PFI schemes onto balance sheet for the first time in 2009/10. To support its PFI expenditure the Council receives PFI grant, which in 2009/10 was accounted for partly as a specific grant and partly as a general grant. The 2010 Code revised this treatment and requires PFI grant to be treated as a general grant. Additionally, in last year's accounts audit report we recommended that the Council should consider whether its treatment of lifecycle costs associated with PFI schemes is appropriate and consistent with the Code.	The Council has reviewed its treatment of PFI grant against the Code and revised the accounting treatment in accordance with the requirements. We have concluded that the Council has appropriately accounted for PFI grant within 'Non Specific Grant Income' and updated the accounting policy appropriately. The Council has adopted component accounting and reviewed its treatment of lifecycle costs to determine whether any revision is required. As the PFI schemes are still in their early stages, components have not yet been replaced and therefore the Council has maintained the existing accounting treatment. However, we recommend the Council continues to monitor the treatment of lifecycle costs against the requirements of the Code (**recommendation 2**).

Accounting requirement	Council's position
Follow up of 2009/10 accounts audit findings	
We reported on follow up of the 2009/10 accounts audit findings in our interim report presented to the Audit Committee on 2 June 2011. We raised a further recommendation that the Council should urgently resolve the dispute with Manchester Teaching Primary Care Trust (the PCT) in relation to the amount of 2009/10 overspend attributable to the Council and the amount of 2010/11 contribution to be paid.	The dispute remains unresolved and we have reviewed correspondence between the Council and the PCT detailing the proposed settlement. However, the Council should now, as a matter of urgency, reach agreement and formal resolution with the PCT (**recommendation 3**).

2.12 The focus of our audit was to address the key issues identified in our Accounts Audit Plan. In addition to this, our accounts audit planning procedures identified key risk areas where we determined a material misstatement in the accounts may be most likely to occur. These key risk areas, our work performed and our conclusions are set out in Exhibit Two:

Exhibit Two: 2010-11 Key risk areas

Key risk areas	Work completed and conclusions
Grant Revenues There is a risk that recorded levels of grant funding are not valid and grant funding may not be recognised in accordance with the IFRS based Code requirements.	We have reviewed significant grant funding, agreed to funding notifications and reviewed revenue recognition for consistency against Code requirements. We have concluded that Grant Revenues have been appropriately accounted for.
NNDR Revenues There is a risk that income and receivables may be overstated.	We have tested the adequacy of controls and placed reliance on the Academy system. We have reviewed the NNDR return in line with the certification instruction and reconciled amounts from the system to the accounts. We have concluded that NNDR Revenues have been appropriately accounted for. However, as in the prior year, our review of the reconciliation of NNDR debtors between SAP and Academy identified minor variances between the two systems. Whilst these variances are immaterial for the 2010/11 accounts, the Council should fully reconcile the two systems (**recommendation 4**).
Council Tax Revenues There is a risk that income and receivables may be overstated.	We have tested the adequacy of controls and placed reliance on the Academy system. We have reviewed the system and reconciled to the accounts. We have concluded that Council Tax Revenues have been appropriately accounted for.

Key risk areas	Work completed and conclusions
Operating expenses There is a risk that payables are understated or not recorded in the correct period.	We sample tested payables and accrued expenditure, including reviewing post year end invoices and payments to ensure that there were no significant liabilities that the Council had not recorded in its accounts. There are no issues to bring to the Council's attention.
Property, plant and equipment There is a risk that activity is not valid, revaluation measurements are not correct and assets may be impaired.	Our review of capitalised expenditure included sample testing additions to assets in the year and we concluded that expenditure has been capitalised appropriately. Our overall review of expenditure capitalised identified expenditure relating to repairs and maintenance, which, whilst the amount is clearly trivial to the accounts, should be accounted for as revenue expenditure and the Council should reiterate the policy on capitalising expenditure to all departments and perform a review of capitalised expenditure to ensure this is in accordance with the policy (**recommendation 5**). We have reviewed the basis of asset revaluations and concluded that the reviews undertaken by the valuation officers have been performed appropriately and consistently with prior periods, based on accurate information from the Council's fixed asset register. We have reviewed the accounting treatment for impairments included within the accounts and confirm these are in accordance with the requirements of the Code.

Matters arising from the financial statements audit

2.13 A number of matters arose during the course of the audit which, whilst not considered material to the reported financial performance, should be considered by the Audit Committee. These are set out in Exhibit Three, together with the associated recommendations for improvement, which are also set out in the agreed Action Plan at Appendix C.

Exhibit Three: Issues arising from the audit and resulting recommendations

Audit issue	Recommendation
Accounting for PFI In 2009/10 the Council brought six PFI schemes on balance sheet, accounting for transactions generated from financial models. In 2010/11, the Council updated the financial models to reflect actual payments made to contractors. Amending the models changed the implicit interest rates and	**Recommendation 6** The Council has amended the accounts for two of the housing PFI schemes as the impact was significant to the accounts. This reduces total deferred liabilities and the Capital Adjustment Account by £932,000. However, as there were only clearly trivial differences on the other schemes, the Council has agreed to use the original models for 2011/12 and not

Audit issue	Recommendation
entries required in the accounts. However, review of these payments identified they should be accounted for outside of the models.	processed any amendments. We recommend the Council uses the original models for the accounting disclosures within the accounts and process any additional payments separately through the accounts.
Journal entry controls Whilst the Council's key control over the raising of journals is restricting access to appropriate individuals, we identified that journals were raised at times which were 'outside of the normal hours of business' due to the increased use of flexible working. No review is undertaken of journals raised for appropriateness and the raising of journals 'outside the normal course of business' poses a potential fraudulent reporting risk to the Council.	**Recommendation 7** Whilst we did not identify any specific issues, we recommend the Council implement exception reporting to identify significant journals raised to mitigate against the risk of fraudulent activity in financial reporting.
Calculation of Depreciation Depreciation on HRA assets, when assets have been revalued below historic cost, has to be calculated manually as SAP currently is unable to automatically calculate this. This increases the risk of input error and misstatement within the accounts.	**Recommendation 8** The Council should implement improvements to SAP to enable the depreciation charge to be calculated automatically to reduce the risk of misstatement.

Group Accounts

2.14 Following our recommendation in the prior year, the Council has reviewed the organisations included within the Group Accounts and updated its policy for consolidation. We have reviewed the Council's assessment, which considers the materiality of organisations and impact disclosure would have on the readers understanding of the Group accounts, and confirm the Council has implemented appropriate procedures for implementing group entities.

2.15 We have identified some improvements to the overall presentation of the Group Accounts to ensure compliance with the Code. Our audit identified some consolidation amendments, which have been processed by the Council. The amendments increase the 2009/10 deficit by £1.4m and reduce the 2010/11 surplus by £1m following the accounting for dividends paid and changes in shareholders' funds.

Adjusted items

2.16 Our audit identified three adjustments which impact on the Council's surplus, increasing the 2010/11 surplus by £1.7m and reducing the 2009/10 surplus by

£42.1m, with no impact on general fund reserve. These adjustments have been processed by management and are detailed in Appendix B. There are no unadjusted items.

2.17 In addition, there were a number of other minor presentational and disclosure changes that arose during the course of our audit and these have been made to the accounts.

Evaluation of key controls

2.18 We have undertaken sufficient work on key financial controls for the purpose of designing our programme of work for the financial statements audit. Our evaluation of the Council's key financial control systems did not identify any control issues that present a material risk to the accuracy of the financial statements. However, as shown in exhibit three we have raised recommendations to improve controls in relation to journal entry, calculation of depreciation and SAP reconciliation procedures.

2.19 We performed a high level review of the general IT control environment as part of the overall review of the internal control system and concluded that there were no material weaknesses within the IT arrangements that could adversely impact on our audit of the accounts. We reported our findings in our Interim Report to the Audit Committee in June 2011 and we will follow up the Council's response to these recommendations during 2011/12.

2.20 We have reviewed the work of internal audit and concluded that the scope and conduct of internal audit work was appropriate to provide adequate assurance on the effective operation of controls. We have therefore taken assurance from the work of internal audit in our evaluation of controls. Our review of internal audit was reported in our interim report to the Audit Committee in June 2011.

Whole of Government Accounts

2.21 The Council met the 2010/11 WGA submission deadline, providing the WGA consolidation packs for audit on 29 July 2011. The Council has put in place an effective structure within the ledger to efficiently prepare the required figures for the consolidation exercise.

2.22 The audit of the WGA consolidation pack is ongoing and will be completed in accordance with the deadline of 30 September 2011. We will provide a verbal update of our findings to the Audit Committee.

2010/11 Annual Governance Statement

2.23 The Council's arrangements for preparing the Annual Governance Statement (AGS) continue to be effective. The assurance processes required to prepare the 2011-12 AGS have been co-ordinated and reviewed by an AGS working group, which has ensured that evidence supporting assurances gained through business planning governance questionnaires is robust and timetables have been adhered to.

2.24 Internal Audit carried out a review of the AGS process and provided 'substantial' assurance over the process. They concluded that there was adequate supporting evidence for the AGS and our year-end review has confirmed this view. Assurance was also given that there had been appropriate levels of challenge and review from officers and Members.

2.25 The CIPFA/SOLACE 'Delivering Good Governance in Local Government' framework states that the AGS should be "an open and honest self-assessment of the organisation's performance across all of its activities, with a clear statement of the actions being taken or required to address areas of concern". The Council's AGS is a very comprehensive and balanced self-assessment covering all significant aspects of the Council's governance processes. The AGS also includes a detailed programme of improvement for 'significant governance issues' and articulates to readers the actions taken against prior year issues.

2.26 The AGS has been prepared in accordance with the CIPFA/SOLACE framework and we are satisfied that the areas identified for future improvement are consistent with our knowledge of the Council. Due to the Council providing detailed information on emerging context, the AGS is a lengthy document and far more detailed than at most other local authorities. The Council's informative and transparent approach is welcome, however, the Council may wish to consider whether some of the narrative currently in the AGS would be more appropriately included in the Annual Report. This would reduce the length of the Council's accounts and focus the AGS on the Council's core governance issues and sources of assurance (**recommendation 9**).

Local Government Elector Queries

2.27 During 2010/11 we received correspondence from a member of the public regarding items of expenditure included in the Council's Licensing Accounts, specifically in relation to taxi licensing. The Council's Licensing Unit Accounts include income and expenditure relating to the entirety of the licensing function such as premises and street trading as well as hackney carriage and private hire licensing. It is therefore not possible to separately identify income and expenditure relating only to taxi licensing. We agreed that the Council will in future maintain a separate account for the purposes of recording only taxi and hackney carriage licensing income and expenditure (recommendation 10).

Next steps

2.28 The Audit Committee is required to approve the financial statements for the year ended 2010/11. In forming its conclusions the Committee's attention is drawn to the adjustments to the accounts and the required Letter of Representation.

A Reporting Requirements of ISA 260

The principal purpose of the ISA 260 report is:

To reach a mutual understanding of the scope of the audit and the respective responsibilities of the auditor and those charged with governance.
To share information to assist both the auditor and those charged with governance fulfil their respective responsibilities.
To provide to those charged with governance constructive observations arising from the audit process.

ISA260 reporting requirement	Key messages
Independence	We are able to confirm our independence and objectivity as auditors and draw attention to the following points: • We are independently appointed by the Audit Commission. • The firm has been assessed by the Audit Commission as complying with its required quality standards. • The appointed auditor and client service manager are subject to rotation in line with the Audit Commission's requirements. • We comply with the Auditing Practices Board's Ethical Standards. • We have not provided any non-audit services in 2010/11.
Audit Approach	Our approach to the audit was set out in our 2010/11 audit plan. We have planned our audit in accordance with auditing standards and the Audit Commission's Code of Audit Practice. Other key factors to highlight include: • We consider the materiality of items in the financial statements in determining the audit approach and in determining the impact of any errors. • We have been able to place appropriate reliance on the key accounting systems operating at the Council for financial statement audit purposes. • In 2010/11 we have been able to take assurance from the work of internal audit in respect of the key accounting systems.

ISA260 reporting requirement	Key messages
Accounting Policies	The Council has adopted appropriate accounting policies in the areas covered by our testing. Accounting policies are in accordance with the 2010 Code. The Audit Committee should confirm that it is satisfied that the accounting policies adopted are the most appropriate, as required by IAS 8. We have considered the Council's financial plans and consider it appropriate for the Council to continue to account on a going concern basis.
Material Risks	The Audit Committee should confirm that it is not aware of any additional material risk areas facing the Council, including significant fraud risks. We have requested from the Council a Letter of Representation, to state that there are no additional material risks and exposures as at 29 September 2011, which should be reflected in the financial statements. This is included at Appendix D. We will also perform our own audit procedures to ensure that all significant risks and exposures to the Council have been recognised in the accounts as at 29 September 2011. We will focus on accounting provisions and cash flow forecasting over the next 12 months.
Audit Adjustments	We have discussed with management the adjustment to the accounts, primarily to improve the fair presentation of the financial statements, as well as the clarity and presentation of disclosure notes. These adjustments are summarised at Appendix B.
Unadjusted Errors	As at 29 September 2011, there were no unadjusted misstatements in the financial statements.
Other Matters	We have made recommendations in respect of some areas for improvement in internal control. Recommendations and agreed action are listed in the Action Plan at Appendix C.

Appendix A

B Adjustments to the Financial Statements

The table below lists all significant audit adjustments which have been processed and agreed with the City Treasurer.

Adjustment Type

Misstatement - A change to the value of a balance presented in the financial statements.
Classification - The movement of a balance from one location in the accounts to another.
Disclosure - A change to the way in which a balance is disclosed or presented in an explanatory note.

Adjustment type	£000	Accounts balance	Impact on financial statements
Misstatement	400 (2010/11) 42,069 (2009/10)	Property, Plant and Equipment/Capital Adjustment Account	Wright Robinson College became a Foundation school on 1 March 2010. The Council's accounting policy is to account for Foundation schools as off balance sheet as these are not controlled by the Council. The College has therefore been derecognised from the Council's accounts through restating the 2009/10 balance sheet, reducing assets, increasing the 2009/10 deficit and the Capital Adjustment Account by £42.1m and removing 2010/11 accounts entries, leading to an increased 2010/11 surplus of £400,000.
Misstatement	932	Deferred liabilities/Capital Adjustment Account	The Council updated PFI models in 2010/11 instead of accounting for additional payments separately. Accounting should be in accordance with the original models and additional payments processed separately. Amendment increases the surplus and reduces deferred liabilities and Capital Adjustment Account.
Misstatement	409	Comprehensive Income and Expenditure Statement/Usable Reserves	The Council, in 2009/10, included capital receipts from preserved right to buy properties, which should be excluded from the amount pooled. The Department for Communities and Local Government agreed to reimburse the

Adjustment type	£000	Accounts balance	Impact on financial statements
			Council after the draft accounts were submitted for audit. The amendment reduces the amount paid to the housing capital receipts pool within the Comprehensive Income and Expenditure Statement, increasing the surplus, and increases usable capital reserves.
Classification	10,716	Property, Plant and Equipment – Surplus Assets/Assets Held for Sale	A reclassification of two properties which are due to transfer to other bodies in 2011/12 which had been accounted for as surplus assets rather than as Asset Held for Sale. These assets meet the criteria as held for sale as they are available for sale in their current state and the transfer is highly probable.
Disclosure	500	Cash equivalents/Bank overdraft	St Matthew's RC High School invested funds within a Guaranteed Investment Account, which matures within 3 months and therefore meets the definition of cash equivalents.
Disclosure	6,573	Contractual capital commitments	A disclosure adjustment to recognise additional capital commitments identified after the draft accounts were prepared.
Disclosure	1,101	Related party transaction	Interest received from Destination Manchester Limited was omitted from the related party disclosure note in error.
Housing Revenue Accounts			
Disclosure	200	Housing Revenue Account	The Council has overstated receipts for Other Land and Buildings within HRA disclosure note (d) due to an error when inputting the figure into the accounts file. The amendment reduces the figure reported for receipts.
Group Accounts			
Misstatement	1,023 (2010/11) 1,436 (2009/10)	Other Group Losses/Group Income and Expenditure Account	An amendment to include the consolidation of dividends paid and changes in shareholders' funds omitted from the accounts in error.

Appendix B

Adjustment type	£000	Accounts balance	Impact on financial statements
Classification	400	Gross Expenditure (Highways and Transport Services)/loss on disposal of assets	In consolidating Manchester Airport Groups' accounts, the Council incorrectly duplicated the amount for loss on disposal of assets due to an input error.

C Action Plan

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council response	Implementation date and responsibility
1	As in the prior year, the Council does not maintain copies of all schools leases.	Copies of all school leases should be maintained centrally to support the accounts.	M	Copies of school leases will be requested at the end of October and at the end of March. Any outstanding leases will be chased up by Children's Services finance staff.	October 2011 and March 2012 Rachel Rosewell Head of Children's Services Finance
2	The Council has adopted component accounting and reviewed its treatment of lifecycle costs to determine whether any revision is required. As the PFI schemes are still in their early stages, components have not yet been replaced and therefore the Council has maintained the existing accounting treatment.	The Council should continue to monitor the treatment of lifecycle costs against the requirements of the Code.	M	The treatment of lifecycle costs will continue to be monitored against the requirements of the code.	April 2012 (for financial year 2011/12) Ceri Taylor Head of Capital Finance, Projects and VAT
3	The Council is still in dispute with Manchester Teaching Primary Care Trust in relation to the amount of 2009/10 overspend attributable to the Council and the	The Council should, as a matter of urgency, reach agreement and formal resolution.	H	The City Treasurer and the Director of Adults are to meet with the PCT on 27 September to attempt to move the matter to a conclusion.	Ongoing Richard Paver, City Treasurer and Liz Bruce, Director of Adults

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council response	Implementation date and responsibility
	amount of 2010/11 contribution to be paid.				
4	As in the prior year, our review of the reconciliation of NNDR debtors between SAP and Academy identified minor variances between the two systems.	Whilst these variances are immaterial for the 2010/11 accounts, the Council should fully reconcile the two systems.	M	A considerable amount of work has been undertaken during 2010/11 to identify the reasons for the variations between the two systems. An issue with the way the NNDR system deals with suspended receipts has been identified as one of the reasons for the differences. This has been raised with the system supplier for resolution.	March 2012 Charles Metcalfe Revenues Manager
5	Our overall review of capitalised expenditure identified expenditure relating to repairs and maintenance, which, whilst the amount is clearly trivial to the accounts, should be accounted for as revenue expenditure.	The Council should reiterate the policy on capitalising expenditure to all departments and perform a review of capitalised expenditure to ensure this is in accordance with the policy.	M	The policy on capitalisation of expenditure will be reiterated to all departments and a review of capitalised expenditure will be undertaken to ensure expenditure is in accordance with this policy.	Policy will be reiterated by October 2011 and the review undertaken throughout 2011/12. Karen Gilfoy Head of Financial Accountancy
6	In 2010/11, the Council updated	We recommend the Council uses	M	The original models will be used	April 2012

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council response	Implementation date and responsibility
	the PFI financial models to reflect actual payments made to contractors. Amending the models changed the implicit interest rates and entries required in the accounts. However, review of these payments identified they should be accounted for outside of the models.	the original models for the accounting disclosures within the accounts and process any additional payments separately through the accounts.		to produce the disclosures in the 2011/12 accounts. Any additional payments will be accounted for separately.	Ceri Taylor Head of Capital Finance, Projects and VAT
7	No review is undertaken of the appropriateness of journals raised Those journals raised 'outside the normal course of business' poses a potential fraudulent reporting risk to the Council.	The Council should implement exception reporting to identify significant journals raised to mitigate against the risk of fraudulent activity in financial reporting.	M	A review of significant journals will be undertaken on a monthly basis.	Ongoing to April 2012 (for financial year 2011/12) Karen Gilfoy Head of Financial Accountancy
8	Depreciation on HRA assets, when assets are revalued below their historic cost, has to be calculated manually as SAP currently is unable to automatically calculate this. This increases the risk of input error and misstatement within the accounts.	The Council should implement improvements to SAP to enable the depreciation charge to be calculated automatically to reduce the risk of misstatement.	M	Due to the SAP upgrade taking place this enhancement will not be possible before the end of the current financial year. However this will be discussed with the implementation partner.	Discussions with implementation partner to take place by March 2012. SAP Manager, ICT
9	Due to the Council providing	The Council may wish to consider	L	Consideration will be given to	June 2012

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council response	Implementation date and responsibility
	detailed information on emerging context, the AGS is a lengthy document and far more detailed than at most other local authorities.	whether some of the narrative currently in the AGS would be more appropriately included in the Annual Report. This would reduce the length of the Council's accounts and focus the AGS on the Council's core governance issues and sources of assurance.		this suggestion during the preparation of the AGS for 2011/12.	Sean Davies Head of Finance (Governance and Corporate Support)
10	The Council's Licensing Unit Accounts include income and expenditure relating to the entirety of the licensing function such as premises and street trading as well as hackney carriage and private hire licensing. It is therefore not possible to separately identify income and expenditure relating only to taxi licensing.	The Council should maintain a separate account for the purposes of recording only taxi and hackney carriage licensing income and expenditure.	H	A separate account has been maintained from the start of the 2011/12 financial year.	Completed. Matthew Bennett Head of Neighbourhood Services Finance

D Draft Letter of Representation

{****Prepare on Council letterhead****}

Grant Thornton UK LLP
No 1 Whitehall Riverside
LEEDS
LS1 4BN

29 September 2011

Dear Sirs

Manchester City Council
Financial Statements for the Year Ended 31 March 2011

This representation letter is provided in connection with the audit of the financial statements of Manchester City Council for the year ended 31 March 2011 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view in accordance with International Financial Reporting Standards.

We confirm to the best of our knowledge and belief that the following representations are made on the basis of appropriate enquiries of other officers and members with relevant knowledge and experience (and, where appropriate, of inspection of supporting documentation) sufficient to satisfy ourselves that we can properly make each of the following representations to you in respect of your audit of the above financial statements.

Financial Statements

i We have fulfilled our responsibilities for the preparation of the financial statements in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in Great Britain ("the Code") as adapted for International Financial Reporting Standards; in particular the financial statements give a true and fair view in accordance therewith.

ii We have complied with the requirements of all statutory directions and these matters have been appropriately reflected and disclosed in the financial statements.

iii We acknowledge our responsibility for the design and implementation of internal control to prevent and detect error and fraud.

iv Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

v We are satisfied that the material judgements used by us in the preparation of the financial statements are soundly based, in accordance with the Code, and adequately disclosed in the financial statements. There are no further material judgements that need to be disclosed.

vi We confirm that we are satisfied that the actuarial assumptions underlying the valuation of pension scheme liabilities for IAS19 disclosures are consistent with our knowledge. We confirm that all settlements and curtailments have been identified and properly accounted for. We also confirm that all significant retirement benefits have been identified and properly accounted for (including any arrangements that are statutory, contractual or implicit in the employer's actions, that arise in the UK or overseas, that are funded or unfunded).

vii Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of the Code.

viii All events subsequent to the date of the financial statements and for which the Code requires adjustment or disclosure have been adjusted or disclosed.

ix There are no unadjusted misstatements that were brought to our attention through the course of the audit, and the financial statements are free of material misstatements, including omissions.

x Except as stated in the financial statements:

a. there are no unrecorded liabilities, actual or contingent
b. none of the assets of the Council have been assigned, pledged or mortgaged
c. there are no material prior year charges or credits, nor exceptional or non-recurring items requiring separate disclosure that are not already disclosed in the financial statements.

xi We have no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

xii We believe that the Council's financial statements should be prepared on a going concern basis on the grounds that current and future sources of funding or support will be more than adequate for the Council's needs. We believe that no further disclosures relating to the Council's ability to continue as a going concern need to be made in the financial statements.

xiii Valuations of investments in companies included in the accounts are based on appropriate estimation techniques. Where the Council has not been able to determine valuations with sufficient reliability this has been disclosed in the financial statements.

xiv All known liabilities in respect of equal pay/ single status have been recognised in the accounts.

xv The split of the Unitary Charge for the Council's PFI schemes have been determined using appropriate modelling based on our best estimate of the charges for capital, service and lifecycle costs from the Operator's model

xvi We consider the assumptions within the financial models regarding operator's returns on the Council's PFI schemes to be appropriate.

xvii We confirm the position of the Mental Health Pooled Budget and amounts owed to Manchester Teaching Primary Care Trust are appropriately included in the financial statements.

Information Provided

xviii We have provided you with:

a. access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters
b. additional information that you have requested from us for the purpose of your audit
c. unrestricted access to persons within the entity from whom you determine it necessary to obtain audit evidence.

xix We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

xx We have communicated to you all deficiencies in internal control of which management is aware.

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

xxii We have disclosed to you our knowledge of fraud or suspected fraud affecting the entity involving:

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

xxiii We have disclosed to you our knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

xxiv We have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing financial statements.

xxv We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware.

Other statements

xxvi We are satisfied that the Annual Governance Statement (AGS) fairly reflects the Council's risk assurance and governance framework and we confirm that we are not aware of any significant risks that are not disclosed within the AGS.

Approval

The approval of this letter of representation was minuted by the Audit Committee at its meeting on 29 September 2011.

Signed on behalf of Manchester City Council.

Name ....

Position ....

Date ....

Grant Thornton