

ARCHBISHOPS' COUNCIL

ANNUAL REPORT OF THE AUDIT COMMITTEE FOR THE YEAR TO 31 MAY 2004

1. Introduction

The Audit Committee has a duty to oversee the discharge of the Council's responsibilities, both in its own right and in its capacity as the Central Board of Finance, relating to the financial statements, internal control systems and internal and external audit. It reports to the Council (normally by submission of its minutes) with recommendations as appropriate and is required, under the terms of its constitution, to publish each year a report on the discharge of its functions, which shall be laid before the Council and the General Synod.

2. Meetings

The Committee has met twice during the year, on 5 November 2003 and 28 April 2004 and held a telephone conference on 18 May, to discuss and recommend the financial statements, which had not been completed at the time of their meeting in April.

3. Committee Membership

I have been Chairman for the whole of the last twelve months.

The other members who served during the year were:

Mr Tony Hesselwood	Vice Chairman (appointed by the Archbishops' Council for a period of five years to 31 May 2006)
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Mr Ian Garden	Archbishops' Council Member and appointed by them. (term of office to expire on 13 December 2005)
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Mr Harry Marsh	Elected by the General Synod for five years to 31 May 2006.
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Revd. Simon Stokes	Elected by the General Synod in November 2002, with his term of office expiring on 31 May 2006.
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Mrs Jane Bisson was appointed as an observer/consultant to the Committee in June 2001. This appointment remains effective until 31 July 2004.

Shaun Farrell, the Council's Financial Secretary and Director of Central Services, acted as secretary to the Committee.

My term of office as Chairman comes to an end on 31 July 2004. Looking ahead, I am pleased to report that the Appointments Committee have agreed with the Archbishops' choice of Tony Hesselwood to be my successor as Chairman of the Audit Committee for a five year term, although this is subject to approval by Synod in July. If appointed, Tony's term will run for five years from 1 August 2004.

4. Reporting

The Committee's report has to be laid before both the Archbishops' Council and General Synod annually. Current Committee practice is for the report to be debated every three years (next year's report is scheduled for debate), unless there is a specific request from the Committee in the intervening years to debate something. There is however no automatic right for a Synod member to request a debate. The Business Committee has recommended that this omission be rectified by the report being presented to Synod for deemed approval, but with the right for Synod members to request debate. The Standing Orders Committee will be considering the precise mechanism later this year.

Furthermore, if the Committee Chairman is not a Synod member, he may be invited to present the report to Synod, but is unable to deal directly with any questions which might arise in debate. The Standing Orders Committee have been asked also to look at this issue .

The Committee has also asked that a brief summary of its business feature in the Archbishops' Council's annual report under its *Governance* section.

5. Constitution

A revised constitution was placed before the Archbishops' Council and agreed in October 2002.

In the light of the quinquennial review of all committee constitutions taking place at the moment, the Committee will be reconsidering its terms of reference later in the year. At the same time, the Committee will be mindful of the provisions of the *Combined Code on Corporate Governance* published in July 2003 relating to audit committees and auditors.

6. “In relation to the external auditor, to consider the appointment, the audit fee and any questions of rotation, resignation or dismissal.”¹”

6.1 Appointment of External Auditors

Deloitte & Touche continue to serve the Archbishops’ Council as external auditors. In line with other leading accountancy firms in the United Kingdom, Deloitte & Touche transferred its business from its general partnership to a limited liability partnership, Deloitte & Touche LLP, with effect from 1 August 2003. The Council accepted the resignation of Deloitte & Touche as auditors and agreed to novate the audit appointment to the successor firm, Deloitte & Touche LLP, noting as they did that the audit approach would be no different with the successor firm.

6.2 Audit Fee

Against an originally agreed figure of £29,000, the outturn for the 2002 audit was £29,500. The fee has been increased by inflation to £30,500 for the 2003 audit, on the basis of a defined scope and that full draft financial statements and supporting schedules would be available in line with an agreed timetable.

6.3 Conflicts of Interest

To avoid any conflict of interests that might arise from carrying out audits of both the Archbishops’ Council and the Church Commissioners, Deloitte & Touche continued to provide a second partner for their 2003 work.

7. “To discuss with the external auditors before the audit begins the nature and scope of the audit.”

The Audit Partner and other representatives of Deloitte & Touche attended the meeting of the Audit Committee on 5 November 2003 at which they detailed their approach for the 2003 audit. They also drew attention to a number of matters arising from their 2002 audit (see 9.1 below).

¹ The headings for sections 6-13 take as points of reference the Committee’s main duties.

Deloitte & Touche also noted that following the formation of a common services Accounts department for the NCIs on 1 November 2003, matters of governance concerning the new department will fall to the Committee as the body charged with looking after common services departments.

As part of their 2003 audit work Deloitte & Touche would continue to direct their attention to understanding and analysing the Council's operations. They would focus upon areas which had been reported on in their 2002 post-audit report. They would also take into consideration the review of trust funds being undertaken by staff and any findings arising from the work of Internal Audit..

8. “To review the annual accounts in the light of their consideration by the Finance Committee (before their formal submission to the Archbishops' Council) with particular reference to:

- (i) Any changes in accounting policies and practices.**
- (ii) Major judgmental areas.**
- (iii) Any significant adjustments resulting from the audit.**
- (iv) Compliance with accounting standards.**
- (v) Compliance with legal requirements.”**

8.1 Financial Statements for 2003

The Committee has considered the financial statements for the Council, CBF and Central Church Fund.

8.2 Changes in accounting policies and practices

Accounting policies have remained unchanged.

8.3 Major judgmental areas

As reported last year, the Council is currently involved in a number of complex transactions involving the relocation of Whitelands College, owned by the CBF, and leased to the University of Surrey at Roehampton through the Whitelands College Foundation. Completion in stages of the sale of the West Hill site takes place in 2004 and 2005, with the funds, under a Memorandum of Understanding signed by the CBF and the Foundation being committed to help finance the development of a new site, Parkstead.

During 2003, the residential part of the Parkstead site was acquired by the CBF and leased back to the Foundation. When the sale of the West Hill site is sold, the CBF will acquire the remainder of the Parkstead site, for academic purposes, and this too will be leased to the Foundation.

The external auditors have confirmed that they are content with the proposed accounting treatment of the transactions contained within the CBF's 2003 financial statements, and the Committee has endorsed their view, subject to notes being included enabling the transactions to be seen as a whole and to ensure transparency.

The Committee noted that it has been customary in previous years for the CBF to pass any legacy income directly to the Central Church Fund. However, for legal reasons in 2003, legacies have been reflected in the CBF's own financial statements. A decision on their application consistent with the wishes of the testators will be taken in 2004 by the Archbishops' Council meeting as the CBF, which will receive a recommendation from the Finance Committee, acting as the CBF's executive committee.

8.4 Format and Contents of Annual Report

The Committee reviewed the draft annual report of the Archbishops' Council which accompanied the financial statements and made a small number of drafting suggestions, mainly to those sections covering *Governance*.

9. "To keep under review the effectiveness of internal control systems and in particular to review the external auditors' management letter and the management response."

9.1 External Auditor's Post-Audit Report for the 2002 Year End

As noted in last year's report, following the 2002 end of year, Deloitte & Touche issued a post-audit report of their main findings, which was circulated to members of the Committee for comment. The final version of this report, together with management responses was considered by the Committee at their meeting on 5 November.

Key issues covered the structure and functions of the Central Board of Finance and the use of designated and restricted funds.

CBF: Deloitte & Touche recommended a thorough review of the continuing requirement for the CBF, given that the Council had now become fully established. This recommendation has been accepted, and the review is ongoing. For 2003 the Committee was provided with separate financial statements for the Council, CBF and the Central Church Fund.

Designated Funds: Designated funds provide trustees with the ability to set aside unrestricted funds for future charitable use. Normal practice for charities is to earmark unrestricted fund surpluses as designated, with expenditure then matching those funds as incurred. The Council's practice however has led to designated funds attracting income in the year.

Consequently, Deloitte & Touche recommended a review of designated funds to determine if the existing designations meet the requirements of the Council's charitable objectives. In addition, they recommended some streamlining, especially where there was no movement within the year, to aid efficiency and control, and reduce staff time.

This recommendation was accepted and designated funds were reviewed towards the end of 2003. The number of designated funds has been reduced and will be kept under active review. Consideration will continue to be given to ways of streamlining accounting procedures in the future.

Restricted Funds: Deloitte & Touche also recommended a review of the Council's restricted funds, the principal ones being the Central Church Fund, the Training for Ministry Fund and the Church Colleges of Education Fund. The need for restrictions should be challenged so that it might be possible to expand their terms or abolish them altogether. In some cases it might be more appropriate for some restricted funds to become designated funds.

The status of restricted funds for the main General Synod activities covered by Votes 1-4 remain unchanged.

A review of the remaining restricted funds is planned for 2004 following the completion of the 2003 year end exercise. The results of the review should be reflected in the Council's 2004 financial statements.

A number of other recommendations, largely of a "housekeeping" nature, were recommended by Deloitte & Touche. These are being addressed as part of the ongoing development of the Accounts department.

9.2 CBF Investment Funds/CCLA Ltd

As stated last year, the Committee was pleased to learn that a working group had been set up, in part because of its concerns, which would look closely at the existing organisational structures.

At its meeting in November, the Committee reiterated its concerns about the current governance arrangements, and asked that their resolution be treated as a high priority. In so doing, it received an interim report from the working group, noting a number of actions that had already been put in place, pending the outcome of the review. These were the appointment of the Royal Bank of Scotland to provide an oversight of CCLA's management; the establishment of an ad-hoc committee drawn from both the Finance and Investment Committees to consider structural changes; and steps taken to appoint an independent member to the Investment Committee's Audit Sub-Committee.

Further consideration of structural change is deferred for the time being, because the Charity Commission are conducting their own wide ranging review into the regulatory framework governing common investment funds and other pooling schemes of the sort that CCLA use to manage church investments. No date has yet been fixed for the publication of the Charity Commission report.

On the question of membership of the Audit Sub-Committee, the Committee noted that the need for independent membership is under review. We will report further on this in due course.

9.3 Internal Audit report on Risk Management

The Charities SORP 2000 requires that the Council's Annual Report contains a statement "confirming that the major risks to which the charity is exposed, as identified by trustees, have been reviewed and systems have been established to mitigate those risks". As a consequence a Risk Register was established in 2001 and papers were presented to both the Finance Committee and Council later that year. Revisions were presented in 2002.

For 2003, risks were identified from a Church-wide perspective and interviews took place with heads of division and others to help quantify these wider risks, before discussion at the Senior Management Group and Council. Because of their responsibility to oversee common service functions, the Joint Employer & Common Services Board subsequently considered the way in which the common service departments managed and mitigated their own risks, suggesting that only the largest should be a focus for their oversight.

The Senior Management Group have been advised of suggested improvements to the risk management process such as training and control and risk self assessment.

In accepting the report, the Committee have noted the need for the risk register to be a part of the process, and not an end in itself. They will be examining the revised divisional registers across the Council later this year.

9.4 Internal Audit Department's Review of Research and Statistics

The Committee considered and accepted a report covering the research and statistics functions undertaken within the Council. The key finding was that the system for collecting data via annual membership and finance returns from dioceses is robust and reasonable assurance may be placed upon it.

The Head of Research and Statistics has accepted one high and seven medium priority recommendations made within the report, whilst two low level recommendations will not be implemented.

The Committee discussed the high priority recommendation identified, namely the setting up of a User Forum. There was concern that this could be resource heavy, but the group would meet only once a year, would be solely internal and would not impact on staff time.

9.5 Internal Audit Department's Follow up of Treasury Functions and Payments and Receipts Audits

The Committee examined and accepted these two reviews together, and noted that the findings would be addressed as part of the development of the new common services Accounts department.

A brief examination of the Council's Treasury functions had been undertaken in 2001, although this was not a full audit with no formal recommendations made. Its principal findings were then taken into account with the subsequent appointment of a cashier. The review found that the issues identified earlier were being addressed, although there was scope for better reconciliation processes, which again would be addressed during the development of the Accounts department, and long term deposits should be reviewed from time to time.

The payments and receipts audit in 2001 made four recommendations which were either accepted in full or in part by the then Chief Accountant. The review found them still to be valid, but that the follow up action had been mixed. Nevertheless the development of the Accounts department should address these points.

9.6 Internal Audit Plan for 2004

The Internal Audit plan for 2004, examined and approved by the Committee in November 2003, was drawn down from the audit needs assessment and long term plan that the Committee approved in 2002.

The plan included reviewing the interim functions of the new common services Accounts department, as well as work on the NCI staff payroll function, due to start in 2003, and a review of I.T. policy and implementation. In part this was a follow up to the I.T. security review that had been conducted in 2000.

10. “To develop an understanding of the financial policies and processes of the Archbishops' Council and the bodies answerable to the Synod through the Archbishops' Council in order to identify omissions or weaknesses in their functions and to review the timing and methods of implementation of those policies and processes.”

Paragraphs 9.1 to 9.6 indicate that the Committee has received and considered reports on the Council's financial policies and processes from both the external and internal auditors. It has also considered the Council's accounting policies as outlined in paragraph 8.1–8.4.

11. “To consider representations which may be made to the Audit Committee by members of the Archbishops' Council, members of the Council's staff, General Synod members or other persons.”

No representations were received.

12. “To liaise from time to time with the Audit Committees of the Church Commissioners and the Church of England Pensions Board to discuss any issues of mutual concern.”

12.1 National Institutions of the Church of England Audit Committees Meeting of Chairmen and Secretaries

I represented the Committee at a joint meeting with the chairmen and secretaries of the other NCI audit committees in February. The meeting majored on the work of Internal Audit, covering their performance and allocation of service across the NCIs, service level agreement, risk register and the external quality assurance of the function. It also

examined the question of the audit committees working more closely together (see 12.2).

12.2 Committee Observers from the Church Commissioners' and Pensions Board's Audit Committees

Whilst there are no plans at present for a single audit committee, the Church Commissioners asked for a common meeting of the three committees. The Committee were content to use one of their existing dates in 2004 for such a meeting, which would major on common service issues, but felt the decision should be left to the chairmen and secretaries. As an alternative, the chairmen and secretaries asked the committees to consider sending observers to attend the Council's audit committee when common service items are on the agenda. This has received the support of all three committees and observers will be invited to attend a meeting later this year. Areas of common training across the committees has also been endorsed.

13. "To consider such other topics as either the Audit Committee or the Archbishops' Council may from time to time consider appropriate."

13.1 Central Church Fund

The Committee considered an "annual review" document produced for the first time in 2003 by the Central Church Fund and circulated widely to Synod members and to dioceses, purporting to contain summary financial statements for the CCF, approved by the external auditors. A statement added that the full accounts were available on request and had received an unqualified opinion.

Although the financial statements have now been signed off by the CCF and the auditors, this occurred sometime after the circulation of the review document. The CCF and auditors have reviewed the problems encountered with the timing of the documents and the premature release of incomplete information. Assurances have been received from the CCF's trustees that greater care will be taken in future to ensure that information is not released prematurely.

Church House
London
13 May 2004

(signed) Ian McNeil
Chairman of the Audit
Committee