

Hertsmere Borough Council

Audit of Accounts 2008/09.

Annual report to those Charged with Governance 2008/09

September 2009

Contents		Page
1	Executive Summary	2
2	Detailed findings	5

Appendices

- A Reporting requirements of ISA 260**
- B Action Plan: Accounts Audit**

1 Executive Summary

ISAUK 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 Purpose of report

This report has been prepared for the benefit of discussion between Grant Thornton UK LLP and the Audit Committee of Hertsmere Borough Council ('the Authority'). The purpose of this report is to highlight the key issues arising from the audit of the Authority's statement of accounts for the year ending 31 March 2009.

The document is used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) (ISAUK) 260, and to report audit findings to "those charged with governance", designated as the Audit Committee.

The Authority is responsible for the preparation of a statement of accounts which records its financial position as at 31 March 2009 and its income and expenditure for the year then ended. We as auditors are responsible for undertaking an audit and reporting whether, in our opinion, the statement of accounts presents fairly the Authority's financial position.

Under the Audit Commission's Code of Audit Practice ('the Code') we are also required to reach a formal conclusion on whether the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('VFM conclusion'). The pieces of work that have informed our VFM conclusion, and our detailed findings, are set out in this report.

1.2 Status of audit

We were presented with the draft statement of accounts on 24 June 2009. We have performed our final accounts audit in accordance with the Audit Commission's Code of Audit Practice and applicable auditing standards.

At the time of writing this report the audit of the Hertfordshire County Council Pension Scheme is yet to be completed by the Audit Commission. This may impact upon the Authority's pension liability and disclosures in the accounts. Further the audit of Elstree Film Studios Ltd has not been completed and as a result our work on the group accounts is not finalised.

1.3 Overall conclusions

As was the case in 2007/08, the Authority continues to prepare good quality accounts that are free from material misstatements and are supported by good quality working papers.

The key highlights from the audit are:

- The Authority held a £1m investment with Heritable Bank which went into administration in the week commencing 6 October 2008. Both FRS 26 and the Statement of Recommended Practice (SORP) require authorities to make their best estimate of any impairment of financial assets. The Authority has calculated the impairment of its asset in accordance with guidance issued by CIPFA in its Local Authority Accounting Panel (LAAP) bulletins 78, 79 and 82. LAAP bulletin 82 stated that it would be 'appropriate for authorities to recognise impairment based on an 80% recovery of the invested amount. This is the approach that the Authority has followed and has recognised a net impairment of £315k in 2008/09.
- A classification adjustment of £2m has been processed between short and long term investments.
- The auditors of the pension fund noted that the net assets used by the actuary to calculate the pensions liability was significantly less than that recorded in the Hertfordshire County Council pension fund. This has led to a reduction in the pensions liability and reserve of £903k. The Authority was notified of this amendment after the date of approval of the accounts.

None of the adjustments above have had an impact on the Income and Expenditure account deficit or on the General Fund balance. This is consistent with prior year performance on the number and nature of audit adjustments identified. The Authority continues to provide good quality working papers for the audit and to respond promptly to audit queries.

Statement of accounts opinion

We anticipate providing an unqualified opinion on the Authority's statement of accounts, prior to the statutory deadline of 30 September 2009.

Value for Money conclusion

In providing our opinion on the statement of accounts, we are required to reach a conclusion on the adequacy of the Authority's arrangements for ensuring economy, efficiency and effectiveness in its use of resources ('the Value for Money conclusion').

Our Value for Money conclusion is informed by our work on Use of Resources. In order for us to provide an unqualified conclusion, the Authority needs to achieve a score of at least 2 for each Key Line of Enquiry ('KLOE'). We are pleased to report that the Authority has met the requirements for all the scored KLOE. This is a good achievement given the new Use of Resources assessment in 2008/09 represents a much harder test, particularly for District Councils.

We anticipate providing an unqualified Value for Money conclusion.

Further information on the outcome of our Use of Resources audit is contained in Section Two.

1.4 Way forward

We will continue to work with the Authority to ensure that outstanding finalisation issues are completed in time for the accounts opinion to be formally signed in accordance with the statutory deadline of 30 September 2009.

We are required to provide an audit opinion on the consolidation pack that is to be completed as part of the Whole of Government Accounts. This work is not covered by our opinion on the Authority's accounts. We will complete this work once the accounts audit has been finalised and in time for the 1 October deadline.

1.5 Acknowledgements

We would like to record our appreciation for the positive co-operation and assistance provided to us by the finance department and other staff at the Authority during the course of our audit.

Grant Thornton UK LLP

8 September 2009

2 Detailed findings

2.1 Introduction

This section provides a summary of our findings arising from the audit of the statement of accounts, including matters arising from our evaluation of key controls and comment on the Authority's overall financial position.

2.2 Status of the audit

We carried out our audit in accordance with the audit plan presented to the Audit Committee in March 2008. Our audit is substantially complete.

The following finalisation procedures are outstanding:

- review of the final version of the statement of accounts, including the Annual Governance Statement;
- review of the assurances provided by the auditors of the Hertfordshire County Council Pension Fund in respect of the pensions liability, associated reserve and disclosures included in the Authority's statement of accounts;
- completion of our work on the Authority's group accounts. This cannot be completed until the auditors of Elstree Film Studios Ltd have issued their audit opinion for the year ended 31 March 2009.
- obtaining and reviewing the Authority's letter of management representation; and
- updating our post balance sheet events review to the date of signing the accounts.

2.3 Audit opinion

Statement of accounts Opinion

We expect to issue an unqualified audit opinion on the Authority's statement of accounts. This is subject to the approval of the statement of accounts by the Audit Committee on 29 September 2009 and completion of our finalisation procedures.

A number of issues 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 sections 2.4 to 2.6 below.

Value for Money Conclusion

Our Value for Money conclusion is drawn from our work on UoR. In order for us to provide an unqualified conclusion, the Authority needs to achieve a score of at least 2 for each Key Line of Enquiry ('KLOE'). Our proposed assessment for the Authority is summarised overleaf. Please note that these scores are subject to national quality assurance processes and are not final.

Scoring scale:

- 1 - Below minimum requirements - inadequate performance
- 2 - Only at minimum requirements – adequate performance
- 3 - Consistently above minimum requirements – performing well
- 4 - Well above minimum requirements – performing strongly

Table 1: Provisional UoR scores

Theme	2009
1 Managing Finances	3
2 Governing the Business	2
3 Managing Other Resources	2

We would like to emphasise that the Authority has performed well to achieve scores of level 2 and 3 and an overall score of 2, as this is a new assessment which represents a much harder test, particularly for District Councils. We understand that 2 is the prevailing score nationally for district councils.

Based on the Use of Resources assessment above, we propose to provide an unqualified value for Money conclusion.

The outcome of our Use of Resources audit will be reported in full in a separate report to be presented to the Audit Committee in January 2010.

2.4 Matters arising from the statement of accounts audit

Matters arising from the statement of accounts audit are set out below. Where appropriate, we have made recommendations for improvement, as set out in the agreed action plan at Appendix B.

The Authority held a £1m investment with Heritable Bank which went into administration in the week commencing 6 October 2008. Both FRS 26 and the SORP require authorities to make their best estimate of any impairment of financial assets. The Authority has calculated the impairment of its asset in accordance with guidance issued by CIPFA in its Local Authority Accounting Panel (LAAP) bulletins 78, 79 and 82. LAAP bulletin 82 stated that it would be 'appropriate for authorities to recognise impairment based on an 80% recovery of the invested amount. This is the approach that the Authority has followed and has recognised a net impairment of £315k in 2008/09.

The Authority did not undertake an impairment review of its land and buildings and investment properties. The Authority has confirmed through its Estates Valuer that a review of the asset register was undertaken and it was considered that no properties required revaluing on the basis of significant impairment having taken place. Our audit experience in other sectors identified that land values had fallen by around 25% in the 2008/09 financial year. The Authority should monitor land and building prices in the current year and determine whether an impairment review in 2009/10 is appropriate to ensure the value of its land and building assets are not misstated.

Further, the Authority should ensure that it has appropriate arrangements in place to meet the valuation requirements for fixed assets under International Financial Reporting Standards which will apply from 2010/11.

We have undertaken sufficient work on key financial controls for the purpose of designing our programme of work for the statement of accounts audit. Our evaluation of the Authority's key financial control systems did not identify any control issues presenting a material risk to the accuracy of the statement of accounts. However a number of issues have been identified in relation to system controls in place at the Authority. Our review of the Council's Members register of interests identified that only new Members had completed a declaration of interests during the year, six of 38 entries reviewed. An annual return should be completed by all Members to ensure that this register is kept up to date. This issue, and others identified, has been included in an action plan included at Appendix B to this report along with recommendations to address the weaknesses.

We have reviewed the work of Internal Audit and concluded that the scope and conduct of the testing was appropriate for us to rely on in understanding key financial systems of the Authority. We have therefore taken assurance from the work of internal audit to support our responsibilities in documenting and understanding material systems used to prepare the statement of accounts. There were no significant issues that would impact on our planned audit strategy as reported to the Audit Committee in June 2009.

However we are concerned to note that the Internal Audit Programme has again not been delivered for the financial year 2008/09 with 368.3 days of chargeable time delivered against a plan of 580 days. Further we note from review of the annual internal audit report that only two of the nine planned Key Financial Systems audits have a final report issued. The Authority should take appropriate steps to ensure that Internal Audit is adequately resourced to meet its annual plans.

We performed a high level review of the general IT control environments as part of the overall review of the internal control system and concluded that there were no material weaknesses within the IT arrangements that would adversely impact on our audit of the accounts.

The Authority continue to provide good quality working papers for the audit and continue to respond promptly to audit queries.

2.5 Adjusted misstatements

There were no misstatements identified by the management team during the course of the audit.

Our audit identified only two adjustments, which have been processed by management:

- Investments - £2m of investments were reclassified from short term investments to long term investments as they fall due over 12 months.
- The auditors of the pension fund noted that the net assets used by the actuary to calculate the pensions liability was significantly less than that recorded in the Hertfordshire County Council pension fund. This has led to a reduction in the pensions liability and reserve of £903k. The Authority was notified of this amendment after the date of approval of the accounts.

The aggregate of these adjustments has not impacted on the Income and Expenditure account deficit or on General Fund balances. This is consistent with prior year performance on the number and nature of audit adjustments identified.

2.6 Unadjusted misstatements

There is one unadjusted error. Rents for industrial lettings which related to 2009/10 had been included within sundry debtors. Our audit procedures indicated that up to £189k of these debtors should have been classified as deferred income. The Authority has decided not to adjust for this error as the same adjustment would be required to be made for 2007/8 leaving a minimal effect on the income and expenditure account. The Authority does not consider the impact on the balance significant enough to warrant an adjustment.

2.7 Financial Performance

The Council added £14,000 to its Council Fund balance in 2008/09. The SORP requires that the Council produces an Income and Expenditure account that is UK GAAP compliant. This requires the Council to include items such as depreciation, pension fund adjustments (FRS17) and other reserve movements within its Income and Expenditure Account. Under this basis the Council has reported a deficit of £4,283,000; however these items are not required by statute when determining the council fund for the year, and are added back on the Statement of Movement on the Council Fund. Excluding these items, which amount to £4,297,000, result in a surplus for the Council of £14,000 for council tax purposes.

The Authority over spent against the budget by £124,000 (2007/08 £2,714,000). Included within this over spend are a number of positive and negative variances, the most significant of which are included in the table below:

Table 2: Most significant variances against budget

Budget area	Performance against budget
Planning and Development	£397k adverse
Housing Services	£229k favourable
Central Services	£237k adverse

As stated in section 2.4 above, the Authority held a £1m investment in Heritable Bank at the time of its collapse. As a response to the collapse of the Icelandic Banks, Internal Audit undertook a review on Treasury Management and gave substantial assurance that risks material to the achievement of the objectives for the system are adequately managed and controlled. The Authority has also revised its Treasury Management Strategy to enable it to respond to changes in the market and as a response to the Audit Commission report on Icelandic investments. Officers continue to closely monitor credit ratings and future prospects of financial institutions that the Authority is authorised to invest in to minimise the risk of losses, whilst securing competitive returns.

The Audit Commission required us to complete a review of Treasury Management arrangements at the Authority and we are due to report back to the Audit

Commission on our findings in October 2009. There are no significant issues arising from this work which we wish to bring to your attention at this time.

2.7 Annual Governance Statement ('AGS')

We have examined the Authority's arrangements and process for compiling the AGS. In addition, we read the AGS and consider whether the statement is in accordance with our knowledge of the Authority. Our audit has not identified any proposed adjustments.

The Audit Commission has requested that all auditors of local Authorities review the policies and arrangements for members' allowances and expenses. Should we identify any significant issues we will report these to the Audit Committee.

The Authority has reflected on arrangements in place to manage risks in respect of treasury management and members' allowances in the AGS.

2.8 Next Steps

The Audit Committee is required to approve the annual accounts of the Authority for the year ended 31 March 2009.

The Audit Committee should monitor the implementation of the recommendations included in this report.

Finally, we would like to draw to the attention of those charged with governance further significant changes that will happen to the statement of accounts in future years. The most significant of which is the full implementation of International Financial Reporting Standards ("IFRS") in 2010/11. Although this may seem a long way off, it is important that authorities start planning now, as there will be significant changes to the accounts. Our experience in other sectors shows that audited bodies that are well planned for the transition to IFRS have fewer amendments to their accounts and are less likely to be charged additional audit fees, than those who are not well prepared. We would be happy to share our experiences of working with CIPFA in this area, as well as involving our Financial Reporting Advisory Group who are specialists in planning for IFRS.

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.

Matters Reported under ISA 260

Area	Key Messages
Independence	<p>We are able to confirm our independence and objectivity as auditors and draw attention to the following points:</p> <ul style="list-style-type: none"> • 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 every 5 years • We comply with the Auditing Practices Board's Ethical Standards. • We have not provided any non-audit services.

Area	Key Messages
Audit Approach	<p>Our approach to the audit was set out in our 2008/09 audit plan and our audit strategy document for the year ending 31 March 2009. 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:</p> <ul style="list-style-type: none"> • We consider the materiality of items in the statement of accounts 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 Authority for final accounts audit purposes. • In 2008/09 we have been able to place reliance on the work of internal audit in respect of understanding and documenting key accounting systems.
Accounting Policies	<p>We consider that the Authority has adopted appropriate accounting policies in the areas covered by our testing. Accounting policies were in accordance with the 2008 Local Government SORP.</p> <p>The Audit Committee should confirm that it is satisfied that the accounting policies adopted are the most appropriate, as required by FRS 18.</p> <p>We have considered the Authority's financial plans and consider it appropriate to account on a going concern basis.</p>
Material Risks	<p>We have requested from the Authority a letter of management representations, to state that there are no additional material risks and exposures as at the date of the audit report which should be reflected in the statement of accounts.</p> <p>We will also perform our own audit procedures to ensure that all significant risks and exposures to the Authority have been recognised in the accounts as at the date of the audit report.</p>

Area	Key Messages
Audit Adjustments	<p>We have discussed with management two adjustments to the accounts. These are in respect of the classification of investments and a reduction in the pensions liability and reserve. Details are included in section 2.5 above.</p> <p>A number of disclosure adjustments have been agreed to improve clarity and presentation of the accounts which do not affect the reported financial position</p>
Unadjusted Errors	There is an unadjusted error relating to the classification and disclosure of deferred income. This is detailed in section 2.6 above.
Other Matters	There have been a number of control issues that have been noted as a result of our audit. These are detailed in the action plan at Appendix B.

B Action Plan: Accounts Audit

The following table presents a list of recommendations which require action on the part of the Authority. These relate to weaknesses in the systems of financial control and other issues associated with the accounts process.

Issue Noted	Priority	Recommendation	Management Response	Officer Responsible	Implementation Date
Declaration of Interests We identified that not all Members of the Council have submitted an annual declaration of interests return.	High	All Members should be reminded of their responsibility to submit an annual declaration of their interests and missing declarations should be obtained from existing Members.	Agreed	Head of Legal & Democratic Services	Immediate
Journal Entry Controls Officers can prepare, input and authorise their own journals as there are no system controls to prevent this from happening. There is therefore an increased risk of errors or other misstatement arising from journal processing.	Medium	All journal entries should be reviewed and signed off by an independent officer prior to processing.	Agreed	Finance Manager	Immediate

Issue Noted	Priority	Recommendation	Management Response	Officer Responsible	Implementation Date
<p>Fixed Asset: Additions Our testing of additions to fixed assets identified one instance where an invoice had not been authorised for payment.</p>	Medium	All invoices should be signed as authorised prior to being processed for payment.	Agreed	Finance Manager	Immediate
<p>Creditors System Officers can both request and authorise the purchase of goods within the Orbit procurement software. This indicates a lack of segregation of duties.</p>	Medium	The Authority should review authorisation controls in place on its procurement software to ensure that there is adequate separation of duties in place so that officers cannot both raise and authorise the same purchase.	Agreed	Head of Financial Services	31 December 2009.
<p>Bank Account It has been noted that one of the Authority's bank accounts has not been used since 2005. There is currently a small debit on the account.</p>	Low	The Authority should consider whether this bank accounts should be closed if it is not intended to be used.	Agreed. Will review all accounts and decide on closure if necessary.	Head of Financial Services	31 March 2010.

Issue Noted	Priority	Recommendation	Management Response	Officer Responsible	Implementation Date
<p>Valuations under IFRS The accounting requirements and valuation methods for fixed assets will change significantly under International Financial Reporting Standards from 2010/11.</p>	High	The Authority should ensure that it has appropriate arrangements in place to meet the valuation requirements for fixed assets under International Financial Reporting Standards which will apply from 2010/11.	Agreed. Arrangements are in place and reviewed in light of further guidance.	Finance Manager	On going.
<p>Internal audit delivery We are concerned to note that the internal audit plan has not been delivered in 2008/09.</p>	High	The Authority should take appropriate steps to ensure that Internal Audit is adequately resourced to meet its annual plans.	Agreed. It is anticipated that the impact of previous reactive work on the timing of planned audit work will permit delivery of this year's annual plan.	Audit Manager	Ongoing



www.grant-thornton.co.uk

© 2009 Grant Thornton UK LLP. All rights reserved.

"Grant Thornton" means Grant Thornton UK LLP, a limited liability partnership.

Grant Thornton UK LLP is a member firm within Grant Thornton International Ltd ('Grant Thornton International'). Grant Thornton International and the member firms are not a worldwide partnership. Services are delivered by the member firms independently.

This publication has been prepared only as a guide. No responsibility can be accepted by us for loss occasioned to any person acting or refraining from acting as a result of any material in this publication