

Watford Borough Council

Audit of Accounts 2008/09.

Annual report to those Charged with Governance 2008/09

September 2009

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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 Watford 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 Authority's statement of accounts represents a true and fair view of the 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 the course of this report.

1.2 Status of audit

We were presented with the draft statement of accounts on 30 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 impairment charge to the fixed assets is yet to be completed with regard to a current assessment of rent levels for both the Harlequin and Charter Place. Confirmation is expected by 30 September 2009. There were a number of other minor completion points outstanding at this point, which are detailed in Section 2.2.

The fieldwork supporting the VFM conclusion is based on our Use of Resources (UoR) audit. This work has been completed sufficiently for us to provide our conclusion.

The appointed day for electors to ask the auditor questions on the accounts this year was 10 August 2009. However, we did not receive questions from the public on this date.

1.3 Overall conclusions

The Authority continues to prepare good quality accounts that are free from material misstatements and which are supported by good quality working papers. The accounts required a small number of changes to disclosures in the notes as a result of matters identified during the audit process and there are also a small number of minor misstatements which were not-adjusted on grounds of materiality. These are detailed in Section 2 of this report. We have also made a number of recommendations which are set out in Section 2 and summarised in Appendix D.

The key highlights from the audit are:

- The Pension Fund auditors for Hertfordshire County Council identified a difference between the actuary's estimate and the year end actual return from the pension funds which resulted in the Council's pension assets being understated by £1.5million. This issue affects all District Councils within the Hertfordshire pension fund. The accounts have been adjusted to reflect the actual position.
- The Council assets have been impaired in the year, to reflect the downturn in the economic conditions. The value of one class of assets rose in the year by £20million regarding investment assets, which reflects the fact that the assets are valued on a quinquennial basis.
- Our review of Treasury Management arrangements, using the standard workbook issued by the Audit Commission, demonstrates that the Council has sound arrangements in place and has taken positive and appropriate action to deal with the fall out from the Icelandic banking crisis.

Statement of accounts opinion

We anticipate providing an unqualified opinion on the Authority's statement of accounts, by 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. Therefore, we propose to give an unqualified Value for Money conclusion. Further details of the assessment are set out in Section 3 of this report.

1.4 The Way forward

We will continue to work with the Authority to ensure that outstanding 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

18 September 2009

2 The Accounts Opinion

2.1 Introduction

This section provides a summary of our findings arising from the audit of the statement of accounts. This includes 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:

- Confirmation of the impairment amounts on fixed assets
- Obtain and review the Authority's letter of management representation.
- Update our post balance sheet events review, to the date of signing the accounts.
- Review of the final version of the statement of accounts, including the Annual Governance Statement, to ensure that agreed adjustments have been made.
- We are awaiting receipt of bank confirmation letters from Britannia Building Society & West Bromwich Building Society.

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 30 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 below.

Where appropriate, we have made recommendations for improvement, as set out in the agreed action plan at Appendix C.

2.4 Financial Performance

The Authority has reported an Income and Expenditure account deficit of £7.08 million which is in line with the revised medium term financial plan. In 2007/08 the Authority reported a deficit of £370.75 million, which was exceptionally large due to the transfer of housing stock that took place in that year.

The Statement of Movement on the General Fund Balance adjusts the I&E deficit to exclude specific costs, which are determined by statute, in order to calculate the

impact on the Council's General Fund. This statement shows that the Authority has delivered a net surplus which increases the general fund by £359,000 to a closing general fund balance of £1.696m.

The Authority managed revenue expenditure within the budget for the year. The capital budget recorded a £1m underspend against the original budget of £9.357m. Capital expenditure in the year includes a £436,000 adjustment to the General Fund to capitalise costs previously charged to revenue, which were of a capital nature. This increases the actual variance between budget and actual to around £1.5million with the main reason being slippage in capital schemes programmed for 2008/09 including slippage on works to the Woodside all weather pitch of £291,000, and refurbishment of the Town Hall and Colosseum totalling £216,000.

2.5 Issues Arising in the Year

There are a number of matters arising in the year which should be considered by those charged with governance when approving the financial statements. These are set out below:

Fixed Assets Valuation

The Council's current revaluation policy for fixed assets is to undertake a complete revaluation every 5 years with approximately 20% of the fixed assets subject to revaluation annually. Due to the prevailing economic conditions, the Council took the view that it would be more prudent to value a larger percentage of the assets in 2008/09, a view that is not uncommon amongst Councils this year, and valued a total of 62% of the total fixed assets. This helped to ensure that asset values reflected the downward movement in prices as a result of the economic downturn. We would like to draw to the attention of the committee that the revaluations were mainly downward, there was one significant valuation movement upwards with regard to Investment properties which have increased by £20million to a closing balance of £106.9million. The increase was as a result of prices being higher in 2008/09 than they were 5 years ago, as investment properties are valued on a quinquennial basis.

The impairment charge is currently still being audited and a verbal update on the position will be delivered to the audit committee members on 30th September 2009.

Pension Fund adjustment

The auditors of Hertfordshire County Council Pension fund found that the actuary's estimate of net pension fund assets was £39.6million less than the outturn position per the pension fund statements for the year ended 31st March 2009. The auditor has determined that this has resulted in a £1.5million understatement of the pension fund assets for the Council. As the amount is above the materiality limit, the limit above which any adjustment identified has to be processed, the adjustment has been processed through the financial statements.

Treasury management

Local Authority investment management practices have come under close scrutiny following the collapse of the Icelandic Banks. The Authority's investment policy is to invest in domestic banks and building societies, Officers continue to monitor

credit ratings and future prospects of the financial institutions with which the Authority is authorised to invest, in order to minimise the risk of losses, whilst securing competitive returns. The Audit Commission has required us to complete a review of Treasury Management arrangements at the Authority, which will incorporate the work undertaken by the Council as appropriate. We are due to report back to the Audit Commission on our findings in October 2009.

Member and Officer expenses

Following Audit Commission guidance, we have also reviewed members and officers expense claims and have performed testing where appropriate. The application of expenses and allowances was found to be consistent with accepted practice and the policies set out in the Council procedures.

Outstanding 2006/07 Grant claims

We noted that the Council has not been in a position to apply to the Secretary of State for Communities and Local Government (DCLG) for permission to close the Housing Revenue Account [HRA], following the transfer of its Housing Stock in September 2007. The HRA cannot be closed until the 2008-09 Housing subsidy advanced claim and the 2007-08 Housing subsidy claim have been audited. Grant Thornton can only audit these claims once the 2006-07 Housing subsidy claim has been audited by the Audit Commission, which is still outstanding.

Recommendation: Contact the Audit Commission to arrange a date for a member of the Audit Commission to complete the 2006/07 housing subsidy claim.

Journal processing

The process for the raising and posting journal entries in the accounts is not considered robust, as there is currently no segregation of duties between the originating and the posting of journals. In practice Nigel Kennedy will review most journals over £50,000.

Recommendation: The journal entries are originated and posted by different officers.

Building Control account

The Building control account has recorded a deficit for the 2008/09 financial year. Building control accounts are set up to administer the charges of the building control function for the Council. The Building control regulations require building control accounts to break even.

Recommendation: Plans are to be put in place to return the building control account to a surplus position.

Capitalisation of staff costs

The current process employed by the Council of recording staff costs against projects based on a annual canvassing of officers to estimate the time spent per individual capital project. This is not as accurate as a time recording system for identifying officer time per project. This point was raised last year.

Recommendation: A robust process is put in place to accurately record the officer time capitalised per capital project.

2.6 Internal Control Issues

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.

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.

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 could adversely impact our audit of the accounts.

2.7 Adjusted Misstatements

Other than the pension adjustment there were no material misstatements identified during the course of the audit.

We identified the following non-material adjustments which finance officers have agreed to amend:

- The accumulated depreciation brought forward on investment assets did not agree to the prior year accounts, it had been restated from £232,000 to £0 with the value of the investment assets falling by the same amount. The change was processed to record investment assets at their correct brought forward value.
- It was found that in note 13, officer remuneration, one officer had been recorded in the incorrect banding. The officer has received redundancy payments, which were not reflected in the note, and we have requested that the officer is shown in the correct banding of £120,000 - £129,000 band.

All adjusted misstatements are scheduled at Appendix B. 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.

2.8 Unadjusted Misstatements

There were no unadjusted misstatements to report to the Audit committee, all adjustments identified were processed by management.

2.9 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.

2.10 Next Steps

The Audit Committee is required to approve the annual accounts of the Authority for the year ended 2008/09.

Finally, we would like to draw to the attention of those charged with governance further significant changes to the basis on which the statement of accounts will be prepared in future years. The most significant of which is the full implementation of International Financial Reporting Standards ("IFRS") into the 2010/11 accounts. It is important that authorities start planning now, as there will be significant changes to the accounts under IFRS. Our experience in other sectors shows that audited bodies that are well prepared for the transition to IFRS have fewer amendments to their accounts than those who are not. 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.

3 The Value for Money Conclusion

Scoring scale:

- 1 - Below minimum requirements - inadequate performance
- 2 - Meets the basic requirements - in line with national expectations
- 3 - Consistently above expected requirements – performing well
- 4 - Well above minimum requirements – performing strongly

3.1 Introduction

This section sets out the basis for our Value for Money conclusion and summarises our work on Use of Resources (UoR) to date. In 2008/09 a new basis for the assessment was introduced for the UoR Assessment. It is important to note that the basis for the assessment has changed and therefore the scores are not directly comparable with prior years.

3.2 Our Conclusion

Based on the Use of Resources assessment, we propose to give an unqualified value for Money conclusion. A score of 2 is the prevailing score nationally for organisations subject to the assessment and this score is in line with most other district councils within the County of Hertfordshire.

3.3 Provisional Scores

In order for us to provide an unqualified conclusion, the Authority needed to achieve a score of at least 2 for each Key Line of Enquiry (KLOE). This criteria has been achieved and our proposed assessment for the Authority is summarised by KLOE 'Theme' in table 1.

Please note that the scores set out in table 1 are provisional at this stage as they are subject to national moderation by the Audit Commission. Also note that KLOE within Theme 3 will be assessed on a 3 year cycle for district councils and therefore KLOE 3.1 and 3.2 were not assessed in 2008/09.

Table 1: Provisional UoR Scores

1. Managing Finances	2009
1.1 Financial Planning & Delivering Priorities	2
1.2 Understanding Costs	2
1.3 Reporting Finances & Performance	2
<i>Theme Score</i>	2
2. Governing the Business	2009
2.1 Commissioning & Procurement	3
2.2 Data Quality	2
2.3 Principles of Governance	3
2.4 Risk & Internal Control	2
<i>Theme Score</i>	2

3. Managing Other Resources	2009
3.1 Use of Natural Resources	Not Assessed
3.2 Asset Management	Not Assessed
3.3 Managing People	2
<i>Theme Score</i>	2
<hr/>	
Overall UoR Score	2009
	2

3.4 The Way forward

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. This will include guidance on the level 3 requirements across all three KLOE themes.

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	Detail
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 charged fees for additional services in excess of the main audit fee (£107,000 excluding VAT).

Area	Detail
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 Statement of Recommended Practice.</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 in regard to the appropriateness for the Authority to account on a going concern basis and find this to have been appropriate.</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	Detail
Audit Adjustments	We have discussed with management a number of adjustments to the accounts primarily to improve the fair presentation of the statement of accounts as well as the clarity and presentation of disclosure notes. These adjustments are summarised in Appendix B.
Unadjusted Errors	From the audit results mentioned previously we have identified no unadjusted errors.
Other Matters	No other matters have been noted.

B Appendix: Adjustments to the Statement of Accounts

The following table presents all significant adjustments made to the accounts arising from the audit process which have been processed and agreed with Officers in the Authority.

Adjustment Type

- **Misstatement** - A change to the value of a balance presented in the statement of accounts.
- **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	Accounts balance	Impact on statement of accounts
Misstatement	Balance Sheet	Understatement of pension fund net assets by £1.5million, which has resulted in the liability to the defined benefit pension scheme and the pension reserve both reducing by £1.5million.
Disclosure	Note 19b Fixed Asset movements	The accumulated depreciation brought forward on investment assets did not agree to the prior year accounts, it had been restated from £232,000 to £0 with the value of the investment assets falling by the same amount. The change was processed to record investment assets at their correct brought forward value.
Disclosure	Note 13 Officer remuneration	It was found that one officer had been recorded in the incorrect banding. The officer has received redundancy payments, which were not reflected in the note, and we have requested that the officer is shown in the correct banding of £120,000 - £129,000 band.

Adjustment type	Accounts balance	Impact on statement of accounts
Disclosure	All	A number of disclosure adjustments have been agreed to improve clarity and presentation of the accounts which do not affect the reported financial position.

C Appendix: Summary of Unadjusted Misstatements

The following table presents errors arising from the audit process which have not been adjusted on the grounds of Materiality.

Adjustment type	Accounts balance	Impact on statement of accounts
		None noted.

D Appendix: Audit Recommendations

The following table presents recommendations arising from the audit.

Recommendation	Priority	Management Response	Responsible Officer	Action Date
<p>Capitalisation of staff costs</p> <p>A robust process is put in place to accurately record the officer time capitalised per capital project.</p>	Medium	Agreed, procedures have now been put in place for 2009/10 to identify officer time charged to individual capital schemes	Nigel Kennedy	Immediate
<p>Grant claims</p> <p>Contact the Audit Commission to arrange a date for a member of the Audit Commission to complete the 2006/07 housing subsidy claim.</p>	High	Officers have been in contact with the Audit Commission for several months regarding the finalisation of these claims. Officers will continue to pursue this issue	Nigel Kennedy	Immediate

Recommendation	Priority	Management Response	Responsible Officer	Action Date
<p>Journal entries</p> <p>The journal entries are originated and posted by different officers.</p>	Low	<p>Journal entries, are generally posted by the accountant responsible for monitoring the service area and in all cases by staff within the Finance Department. The new financial management system to be implemented in April 2010, will enable journals to be prepared by budget holders and posted by accountants hence achieving the required division of duties required by the external auditor</p>	Alan Power	April 2010
<p>Building control account</p> <p>Plans are to be put in place to return the building control account to a surplus position.</p>	Medium	<p>This issue is currently being looked at in the review of fees and charges for 2009/10</p>	Jane Custance	March 2010



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