

Darlington Borough Council

2008/09 Report to those charged with governance



The Audit Committee
Darlington Borough Council
Town Hall
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Ladies and Gentlemen

2008/09 Report to those charged with governance

We are pleased to present our report on the results of our audit work for 2008/09. We hope that the information contained in this report provides a useful source of reference for members.

Yours faithfully

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Code of Audit Practice and Statement of Responsibilities of Auditors and of Audited Bodies

In April 2008 the Audit Commission issued a revised version of the ‘Statement of responsibilities of auditors and of audited bodies’ which applies to the 2008/09 audit. It is available from the Chief Executive of each audited body. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas. Our reports and management letters are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.

Executive summary

The purpose of this report

This report summarises the results of the work we have conducted in our 2008/09 audit of accounts.

It includes the issues arising from our audit of the financial statements and those issues which we are formally required to report to you under the Audit Commission's Code of Audit Practice and International Standard of Auditing (UK & Ireland) (ISA(UK&I)) 260 - "Communication of audit matters with those charged with governance".

Our work during the year was performed in line with the Audit Plan that we presented to you in June 2009.

We have set out below the most important issues and recommendations that we have discussed with management in the course of our work.

Status of our work

We are pleased to report that our programme of detailed audit work as set out in our plan is nearing completion. The detailed findings of this work are described below and the audit adjustments identified are shown in the tables attached. The main areas where we still have work to complete are:

- Ensure that changes to the pension disclosures, recently provided by the Council's actuaries, have been properly reflected in the accounts; and

- Conduct a review of post balance sheet events up to the date that the accounts are signed.

Financial Statements

At the time of writing, our audit of the financial statements is nearing completion. This report sets out the findings up to 16 September 2009. Any significant issues arising after this date but before the conclusion of the audit will be raised with the Council as appropriate.

Our audit work has identified a small number of proposed adjustments to the draft financial statements approved by Members on 26 June 2009. A number of these adjustments have been agreed with officers in Finance and will be reflected in the final, audited, financial statements. There remain a small number of unadjusted misstatements which should be considered by the Audit Committee. These misstatements are set out in Appendix B to this report.

The following key issues have been discussed further in this report:

- The basis of valuation of shares held in Durham Tees Valley Airport;
- The Building Control Account has not covered its costs on its fee earning activities over a three year rolling timescale. Over the past three years, the Council has made a loss on chargeable activities of £206k.

- There are two trading operations, Catering and School Meals-Best Value, which have been in deficit in recent years.

Use of Resources

We have completed the work on our Use of Resources assessment leading to an overall score of 3 for the Council. Further information on our assessment is included on pages 8 and 9 with detailed scores for each key line of enquiry set out in Appendix D. We will issue a separate report on our Use of Resources assessment that includes detailed findings.

Electors' queries on the accounts

To date there have been no formal objections to the 2008/09 accounts. However, we are currently working on an issue raised by an elector in relation to the redevelopment of a school in the borough.

Financial statements

Accounts

We have completed the audit of the Authority's accounts in line with the Code of Audit Practice and Auditing Standards. We anticipate issuing an unqualified audit opinion on the financial statements.

Accounting Issues

We bring to your attention, in Appendix B, the misstatements which we have identified in the course of our audit and which have not been adjusted in the financial statements. All remaining misstatements identified by audit were agreed with management and concluded during our clearance meeting on 10 August 2009. These have been adjusted in the revised version of the Statement of Accounts. Significant adjusted misstatements can be found in Appendix C. The key adjustments and accounting issues arising from our audit are:

- There were some accounting and disclosure errors noted in the entries for revaluations and impairments. The main issue is that the balance (£165k) in the revaluation reserve for assets disposed of had not been written out to the Capital Adjustment Account following the disposal of those assets.
- An equal pay provision amounting to £248k has been included in the current year. This had been estimated using past settlements, however, the estimated liability excluded the associated tax and National Insurance impact. This element amounts to £64k.

- The Council's actuaries generate the pension scheme disclosures in advance of the year-end. This approach is used to facilitate prompt closure of the accounts. In previous years, changes in the scheme liability between the date of the actuarial valuation and the financial year-end have been insignificant. However, in 2008/09, because of volatility in the financial markets, the value of Darlington's assets underpinning the pension scheme increased by £2,270k during this period. The resulting decrease in the net pension liability, and associated disclosures, have been processed as an audit adjustment.

Systems of internal control

We are required to report to you any material weaknesses in the accounting and internal control systems identified during the audit. We have set out below details of control weaknesses that we have identified as part of our audit.

The most significant internal control recommendations arising from our work are as follows:

- As the Buildings Control Account has made a deficit for three consecutive years, the Council should consider reviewing the level of fees charged and the cost base to improve the financial position in future years;
- Two trading operations, Catering and School Meals-Best Value, are in

deficit positions at the year-end. These should be closely monitored and operations reviewed in order to improve the financial position in future.

- Valuations of Housing Stock were carried out in January 2009. The Council should ensure that any material movements between the valuation date and the year-end are reflected in the accounts. We are satisfied that no such material movements have occurred this year.
- The contract for Working for Wellbeing has now been signed by both parties; however, this was not signed promptly and was not dated. The Council should ensure that contracts are signed and dated promptly in order that contract terms can be enforced.
- The fixed asset register had not been updated regularly throughout the year due to software problems. In future, the Council should ensure the register is updated on a timely basis to ensure that all transactions are recorded and depreciation is correctly applied.
- Following the introduction of shared services with Stockton Borough Council, payment authorisation policies are not being consistently applied. This results in some duplication of authorisation procedures. For example, within Community Services, when invoices are received by Housing Services, they are signed by the line manager to authorise payment. This control is not used across other departments and Xentrall does not formally recognise this authorisation procedure.

There were some issues earlier in the year relating to the timely preparation of bank reconciliations within Xentrall that have already been reported to Audit Committee. We are pleased to report that these issues had been resolved as at the year-end.

A detailed report including all of our Internal Control Recommendations will be issued in October 2009.

Accounting practices

We are also required to report to you our view on qualitative aspects of the Authority's accounting practices and financial reporting and have set out

below our observations on key issues affecting the Authority.

- The Fixed Asset Register includes a number of assets which have been fully depreciated. For the purposes of maintaining up to date accounting records, the Council should ensure that any assets which are fully depreciated and no longer in use are removed from the register. The Council has already begun a review of the register and assets to the value of approximately £4m have been removed;
- One balance in the Cash Flow statement, 'Accruals Adjustment' cannot be fully substantiated by the Council. The Council should introduce procedures to ensure all balances can be substantiated in future;
- The investment in Durham Tees Valley Airport has suffered an impairment of approximately £69k calculated on a net assets basis. The method of valuation should be assessed for reasonableness and closely monitored in future given the current economic climate.

Value for Money in the Use of Resources

Work performed

We have performed audit work to conclude on the Authority's arrangements for achieving economy, efficiency and effectiveness in its use of resources. Our work comprised the following elements:

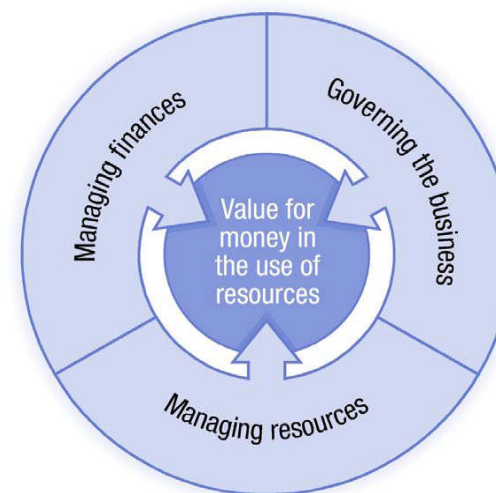
- Use of Resources assessment, supported by our conclusions on the key lines of enquiry (KLoEs) as specified by the Audit Commission, including:
 - review of evidence provided by management;
 - meetings held with officers responsible for the individual KLoEs; and
 - data quality assessment including a review of selected National Indicators.
- Review of the Annual Governance Statement

Use of resources

From April 2009, the Audit Commission has been implementing comprehensive area assessment (CAA), jointly with the other public service inspectorates. The audit year 2008/09 is a year of transition to CAA. Our use of resources judgements in 2008/09 will therefore input into the first results of CAA on which the Audit Commission will report in autumn 2009, as well as acting as the basis for our value for money conclusion. The Audit Commission have therefore issued new KLoEs for auditors to assess Local Authorities' arrangements against.

We have assessed the Authority's arrangements against a series of KLoEs grouped into three themes which form the Use of Resources framework. The assessment has changed to focus on the Authority's achievements, outputs and outcomes rather than the Authority's processes. Auditors are

therefore considering the Authority's strategies and outcomes rather than the detailed processes that the Authority has put in place.



KLoEs are scored as follows:

- 1 – Failure to meet minimum requirements – inadequate performance;
- 2 – Meets only minimum requirements – performs adequately;
- 3 – Exceeds minimum requirements – performs well; or
- 4 – Significantly exceeds minimum requirements – performs excellently.

Scores for each key line of enquiry are set out in Appendix D. In aggregate, we assessed Darlington Borough Council as 3 out of 4. This equates to “performs well”.

Value for Money Conclusion

Under the Code of Audit Practice we are required to provide a conclusion on the Authority’s arrangements for securing economy, efficiency and effectiveness in its use of resources. This conclusion is reached by assessing the Authority’s arrangements against a set of criteria issued by the Audit Commission. From 2008/09 the Key Lines of Enquiry for the scored use of resources assessment also form the criteria for the Use of Resources conclusion. They are listed in Appendix D. A score of Level 2 or higher under the KLoEs will usually result in an assessment of ‘adequate’ arrangements for the purposes of the Code criteria. In reaching our conclusions, we also consider whether the KLoE scores should be adjusted for other factors such as whether the arrangements have been in place for the whole financial year.

We intend to issue an unqualified value for money conclusion. Additional detail on the basis for this conclusion is included within our separate Use of Resources report.

Annual Governance Statement

Local Authorities are required to produce an Annual Governance Statement (AGS) which is consistent with guidance issued by CIPFA / SOLACE. The AGS was included in the financial statements.

We reviewed the AGS to consider whether it complied with the CIPFA / SOLACE guidance and whether it is misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

Audit fee update

Audit Plan

We issued our Audit Plan for 2008/09 and presented it to Members in June 2009. We have performed appropriate procedures for each of the risks identified in the plan. In this report we comment only on those areas where we believe we need to communicate with those charged with governance.

Audit fees update for 2008/09

We reported our fee proposals as part of the Audit Plan for 2008/09. Our actual fees are in line with these proposals (all stated excluding VAT):

	2008/09 Outturn	2008/09 Fee proposal
Accounts:		
Main authority accounts	£139,000	£139,000
Use of Resources/VfM conclusion	£68,800	£68,800
Total	£207,800	£207,800

Our fee for Use of Resources work includes the following:

- Assessment of the Council against the Use of Resources criteria contained within the Code of Audit Practice;

- Audit of your 2008/09 BVPP and validation of selected performance indicators; and
- Follow up of previous work.

Other work

We are in the process of responding to an issue raised by an elector. This work has been conducted under the Code of Audit Practice and the costs incurred will be charged separately to the Council and notified to the Audit Committee.

We have also provided advice to the Council on data security and facilitated fraud awareness workshops for officers. The fees arising from these additional services were less than £5,000 in aggregate.

Independence considerations

We have made enquiries of all PricewaterhouseCoopers' teams providing services to you and of those responsible in the UK Firm for compliance matters.

At the date of this report we confirm that, in our professional judgement, we are independent accountants with respect to the Council, within the meaning of UK regulatory and professional requirements and that the objectivity of the audit team is not impaired.

Appendix A: Accounting and Audit Matters

As part of the planning process we identified significant risks which were reported to you as part of our External Audit Plan. We have set out below the work undertaken as part of the external audit in relation to the risks identified as well as a number of other accounting and audit matters which we consider of interest to management and members of the Audit Committee.

Matters Identified in Audit Plan	Work Performed
<p>Strategic Partnership with Stockton Borough Council</p> <p>Darlington Borough Council has entered into a strategic partnership with Stockton Borough Council to provide a range of back-office functions to both authorities. The Council needs to ensure that appropriate governance arrangements are in place for the partnership and that controls operating over Darlington's transactions are robust.</p>	<p>We have worked closely with officers involved with the partnership, as well as with internal audit at both authorities, to gain an understanding of governance arrangements in place and to determine whether controls over transactional finance are operating effectively.</p> <p>We have raised an internal control recommendation in relation to the expenditure authorisation process (see section above).</p> <p>The Audit Commission, as auditors of Stockton Borough Council, has reviewed the effectiveness of IT general controls in operation in Xentrall.</p>

Matters Identified in Audit Plan	Work Performed
<p>New General Ledger System</p> <p>A new General Ledger system was implemented by the Council on 1 April 2008. There is a risk that data from the old ledger may not have been transferred accurately or completely to the new system resulting in errors in the 2008/09 accounts.</p>	<p>We have reviewed the data transfer arrangements adopted during the implementation and have considered the Council's own assurance procedures on the completeness and accuracy of data transfer.</p> <p>We have not identified any audit issues that are a direct result of the implementation.</p>
<p>Financial Standing</p> <p>In common with many authorities in the current economic climate, Darlington Borough Council is expecting to face increasing budgetary pressures in future. The Council's Revenue Medium Term Financial Plan for 2009/10 to 2012/13 relies on the achievement of challenging efficiency savings and requires the use of some £2.8m in revenue reserves over the four years of the Plan to balance expenditure.</p>	<p>We monitor the financial position of the Council to ensure that financial standing is not compromised. Efficiency savings have already been achieved in 2008/09 with the result that reserve balances have not been utilised to the extent expected.</p>

Appendix B: Summary of Unadjusted Misstatements

We have identified the following errors during our audit of the financial statements that have not been adjusted by management. The Audit Committee are requested formally to consider the listed unadjusted errors and determine whether the accounts should be amended. If the errors are not adjusted we will require a written representation from you explaining your reasons for not making the adjustments.

Unadjusted Misstatement	Income and Expenditure Account		Balance Sheet	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Overstatement of debtors due to credit note not being accrued into the correct period.	Income 32			Debtors 32
2009/10 expenditure has been charged to the 2008/09 accounts. This should be classed as a prepayment.		Expenditure 8	Prepayment 8	
2009/10 expenditure has been charged to the 2008/09 accounts. This should be classed as a prepayment.		Expenditure 2	Prepayment 2	
Accumulated depreciation missed in relation to Darlington FC (land and buildings) - related to adjustment 7 above.	Depreciation Expense 11			Accumulated Depreciation 11

Unadjusted Misstatement	Income and Expenditure Account		Balance Sheet	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Increase in equal pay provision to reflect tax and NI impact.	Net Cost of Services 64			Provisions 64
Net effect	107	10	10	107

Appendix C: Summary of significant adjusted misstatements

We have identified the following errors over £100k during our audit of the financial statements that have been adjusted by management, but which we consider should be communicated to you to assist you in fulfilling your governance responsibilities.

Unadjusted Misstatement	Income and Expenditure Account		Balance Sheet	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Overstatement of Income within Central Services to the Public.	Income 2,666	Expenditure 2,666		
Overstatement of Income within Cultural, Environmental and Planning Services.	Income 738	Expenditure 738		
Overstatement of Income within Children's and Education Services.	Income 652	Expenditure 652		
Understatement of Income within Housing Services.	Expenditure 123	Income 123		
Overstatement of Income within Highways.	Income 295	Expenditure 295		

Unadjusted Misstatement	Income and Expenditure Account		Balance Sheet	
	Dr £'000	Cr £'000	Dr £'000	Cr £'000
Reclassification of Assets Under Construction to Land and Buildings (Playing for Success - Darlington FC).			Land and Buildings 111	Assets Under Construction 111
Transfer revaluation reserve balance for disposed assets to CAA (HRA).			Revaluation Reserve 165	Capital Adjustment Account 165
Adjustment to the net pension liability arising from changes in fund assets values arising between the date of the actuarial valuation and the year-end.			Net Pension Liability 2,270	Pension Reserve 2,270
Net effect	4,474	4,474	2,546	2,546

Appendix D: Value for Money Conclusion

The Audit Commission publishes Code of Practice criteria on which auditors are required to reach a conclusion on the adequacy of an audited body's arrangements for economy, efficiency and effectiveness in its use of resources.

These code criteria are linked to the scored use of resources Key Lines of Enquiry (KLoEs). A score of Level 2 or higher under the KLoEs will result in an assessment of adequate for the purposes of the Code criteria. The Code criteria and the linked KLoEs are shown in the table below and the scoring for the 2009 assessment are provided. We have carried out sufficient work to confirm that a minimum Level 2 (adequate) will be reached for each KLoE and that the overall score for the Council under the 2009 use of resources assessment will be a 3.

The use of resources assessment considers how well organisations are managing and using their resources to deliver value for money and better and sustainable outcomes for local people. The assessment comprises three themes that focus on:

- sound and strategic financial management;
- strategic commissioning and good governance; and
- the management of natural resources, assets and people.

Managing Finances

Key Lines of Enquiry		Score
1.1	Does the organisation plan its finances effectively to deliver its strategic priorities and secure sound financial health?	3
1.2	Does the organisation have a sound understanding of its costs and performance and achieve efficiencies in its activities?	2
1.3	Is the organisation's financial reporting timely, reliable and does it meet the needs of internal users, stakeholders and local people?	3

Governing the Business

Key Lines of Enquiry		Score
2.1	Does the organisation commission and procure quality services and supplies, tailored to local needs, to deliver sustainable outcomes and value for money?	2
2.2	Does the organisation produce relevant and reliable data and information to support decision making and manage performance?	3
2.3	Does the organisation promote and demonstrate the principles and values of good governance?	3
2.4	Does the organisation manage its risks and maintain a sound system of internal control?	3

Managing Resources

Key Lines of Enquiry		Score
3.1	Is the organisation making effective use of natural resources?	2
3.2	Does the organisation manage its assets effectively to help deliver its strategic priorities and service needs?	2
3.3	Does the organisation plan, organise and develop its workforce effectively to support the achievement of its strategic priorities?	N/A

A detailed summary of our conclusions under each KLoE and how we have scored the Council against each assessment criterion will be included a separate Use of Resources report.

