



Clerk: Lisa Warrillow
Telephone: 01803 207013
E-mail address: democratic.services@torbay.gov.uk
Date: Thursday, 15 September 2011

Democratic Services
Town Hall
Castle Circus
Torquay
TQ1 3DR

Dear Member

AUDIT COMMITTEE - TUESDAY, 20 SEPTEMBER 2011

I am now able to enclose, for consideration at the Tuesday, 20 September 2011 meeting of the Audit Committee, the following report that was unavailable when the agenda was printed.

Agenda No	Item	Page
6.	Annual Governance Report	(Pages 175 - 200)

Yours sincerely

Lisa Warrillow
Clerk

This page is intentionally left blank

Annual governance

report

Torbay Council

Audit 2010/11



Contents

Key messages	3
Audit opinion and financial statements	3
Value for money	3
Before I complete my audit	4
Financial statements	5
Opinion on the financial statements	5
Errors in the financial statements	5
Value for money	12
Appendix 1 – Draft audit report	14
Appendix 2 – Amendments to the draft financial statements	17
Appendix 3 – Unadjusted misstatements to the financial statements	20
Appendix 4 – Glossary	22

Key messages

This report summarises the findings from the 2010/11 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.

	Our findings
Unqualified audit opinion	●
Proper arrangements to secure value for money	●

Page 177

Audit opinion and financial statements

Subject to satisfactory clearance of outstanding matters, I propose to issue an unqualified opinion on the financial statements.

My audit identified one material error, three material disclosure errors and a number of non-trivial errors in the financial statements. None of these has an effect on Council balances.

- The Authority plans to amend the material errors and most of the non-trivial errors. These are set out in Appendix 2.
- The details of the remaining potential misstatements, which the Council does not plan to amend in the 2010/11 accounts, are set out in Appendix 3. In each of these cases the Council will review the issue I have raised and amend if necessary.

In addition I identified a significant number of minor errors, omissions and/or inconsistencies in the text, which the Council is correcting.

Value for money

I intend to issue an unqualified conclusion stating that the Authority had adequate arrangements to secure economy, efficiency and effectiveness in the use of resources.

I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against criteria specified by the Audit Commission:

- Financial resilience
- Securing economy, efficiency and effectiveness

I have shown my conclusions for both of these on page 10.

Appendix 1 contains a draft version of my audit report, including my opinion on the financial statements and my value for money conclusion.

BW symbol key: Red ■ Amber ◆ Green ●

Before I complete my audit

I confirm to you

My report includes only matters of governance interest that have come to my attention in performing my audit. My audit is not designed to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) - Integrity, Objectivity and Independence. I can also confirm there were no relationships resulting in a threat to independence, objectivity and integrity.

The Audit Commission's Audit Practice has not undertaken any non-audit work for the Council during 2010/11.

I ask you to confirm to me

I ask the audit committee to:

- take note of the adjustments to the financial statements which are set out in this report (Appendix 2);
- agree your response to the errors identified which management are proposing not to amend (Appendix 3) and include this in the letter of representation; and
- approve the letter of representation provided alongside this report, on behalf of the Council, before I issue my opinion and conclusion.

Financial statements

I propose to issue an unqualified opinion on the financial statements. Appendix 1 includes a draft version of my audit report, including my opinion on the financial statements.

Opinion on the financial statements

Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the financial statements. Appendix 1 contains a copy of my draft report.

Errors in the financial statements

I have identified the following errors that the Council has adjusted in the 2010/11 accounts:

- One material error relating to the way that changes in pension liabilities are shown in the accounts and three material disclosure errors that affect the relevant disclosure note only. (Appendix 2). None of these has an effect on Council balances
- A number of non trivial errors (Appendix 2); and
- A significant number of minor wording errors, omissions and/or inconsistencies in the text (page 8)

I identified a further three potential non-trivial misstatements that the Council does not plan to adjust in the 2010/11 accounts but will investigate and, if necessary, adjust in 2011/12. (Appendix 3).

Recommendation

I recommend that the Council takes action to address the issues I have raised in relation to:

- Weakness in internal control (page 7)
- Financial statement quality issues (page 8).

Financial statements

The Council's financial statements and annual governance statement are important means by which the Council accounts for its stewardship of public funds. As Council members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.

In planning my audit I identified specific risks and areas of judgement that I have considered as part of my audit.

Key audit risk and our findings

Key audit risk

1. First time adoption of the International Standards on Financial Reporting (IFRS)
The Council is required to implement new International Financial Reporting Standards in 2010/11.

Finding

- I reviewed the Council's plans for implementing and accounting for the new Standards and liaised with the Council's finance team to review the principles that had been applied in adopting IFRS for the 2010/11 accounts.
- I carried out audit procedures to ensure that the Authority have made appropriate disclosures in accordance with adopted accounting policies and the requirements of the Code and IFRS.
- I carried out appropriate audit tests on the IFRS compliant accounts to ensure that they are materially correct.
- As a result I am proposing to give an unqualified opinion on the 2010/11 accounts.

2. Foundation schools accounting under IFRS.

- I have reviewed the council's accounting for foundation schools under IFRS to ensure that it is correct.

3. Changes in borrowing relating to pre 1998 debt and financing of capital programme.

- I have reviewed the accounting for these significant transactions and am satisfied that they are materially correct
-

Key audit risk

4. Possibility that group accounts may be required under IFRS
5. Payroll controls - During 2010/11, although some existence checks on payroll payments were made, confirmations were not carried out and followed up systematically across the payroll.

Finding

- The council has carried out an assessment to quantify the value of group transactions and has concluded that they are not material. I have reviewed the assessment and confirmed that group accounts need not be produced.
- In agreement with the Chief Financial Officer, a 100% check was carried out at the end of the year. Internal audit have reviewed the arrangements and I have verified that the checks provide the assurance needed.

Financial statements

Significant weaknesses in internal control

I have not identified any significant weaknesses in internal controls for which I have not been able to place reliance upon alternative controls or testing. However, the control weakness referred to below relating to payroll should be addressed.

This weakness is only that which I identified during the course of the audit that is relevant to preparing the financial statements. I am not expressing an opinion on the overall effectiveness of internal control.

Internal control issues and our findings

Description of weakness	Potential effect	Management action
1. Payroll controls - A key payroll control is the verification of employees charged to budgets by Service Heads. During 2010/11 this control was not operated consistently (see above under Audit Risks).	The absence of this control meant that the Council had less assurance over the integrity of its payroll.	As noted above, a 100% check was carried out at the end of the year. Internal audit reviewed the arrangements and I verified that the checks provide the assurance needed. Management should ensure that this control is operated effectively in the current and future years.

Financial statements

Quality of your financial statements

I consider aspects of your accounting practices, accounting policies, accounting estimates and financial statements disclosures.

These are the issues I want to raise with you:

Accounting practices, policies, estimates and financial closures

Issue

1. Wording and disclosure amendments

A significant number of amendments have been agreed arising from the audit.

Findings and recommendations

The areas where the main changes occurred were:

- Annual governance statement compliance and consistency issues
- Foreword and notes to the accounts – minor errors, omissions and inconsistencies
- Typing errors and incorrect cross references etc

The Council is making these amendments.

For the future Quality Assurance arrangements should be put in place to ensure that accounts presented for audit do not contain errors.

2. Valuation reporting

Valuation practice does not accord with the CIPFA code for valuations.

The Asset Management Team in Torbay Development Agency undertakes valuations of the Council's properties on the basis of instructions issued by the Council. My review of the valuation report identified that it did not meet the requirements of the CIPFA valuation code. It did not include the valuer's estimate of the remaining useful life of individual properties, the valuer's proposed strategy for the rolling programme of valuation reviews, the arrangements for implementing the rolling programme, or proposals for carrying out additional ad hoc valuations. Future arrangements should be strengthened to ensure that instructions are issued in accordance with the code and that valuation report meets these requirements.

In the current year the remaining useful life of individual assets has been identified and entered directly by the asset registrar. I have agreed these as part of our sample testing and am satisfied that these are properly recorded on the asset register

3. Bad debt provisions

The process for setting provisions should be more evidence-based.

The provision for bad debts for Council Tax and NNDR are set at 75% and 50% of outstanding debt respectively. This is not best practice. The Council should improve the evidence base for its bad debt provisions, using, for example, aged debt analysis to assess the adequacy of provisions.

4 Related parties

The process for collecting details of members' interests should be reviewed.

My review of related party transactions and, in particular, members' interests, identified some that had not been declared. The council should review the process for collecting details of members' interests to ensure that it obtains all relevant interests.

5. Quality of working papers

IFRS implementation has been very demanding and this has impacted upon the quality of working papers. A number were only constructed at the audit when requested and others did not agree to figures in the accounts.

There is scope to improve the quality of working papers.

For the future Quality Assurance arrangements should be put in place to ensure that working papers are sufficient to support figures in the statements.

Financial statements

Letter of representation

Before I issue my opinion, auditing standards require me to ask you and management for written representations about your financial statements and governance arrangements.

The letter of representation will be presented for your approval at the meeting where the Annual Governance Report is received.

Value for money

I am required to conclude whether the Council put in place proper corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money conclusion.

I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against two criteria specified by the Audit Commission. My conclusion on each of the two areas is set out below.

I intend to issue an unqualified conclusion stating that the Council had proper arrangements to secure economy, efficiency and effectiveness in your use of resources.

Value for money criteria and our findings

Criterion	Findings
1. Financial resilience The organisation has proper arrangements in place to secure financial resilience.	The criterion is met. <ul style="list-style-type: none">The Council agreed a well-evidenced and balanced budget for 2011/12 in February 2011 following a rigorous review of spendingThe Medium Term Financial Plan was agreed in December 2011, but officers have updated it subsequently and an updated version will be agreed shortly.The Council's reserves have been maintained and are adequate. Their robustness has been confirmed by the s151 officer.Although the first quarter outturn in the current year projected significant overspends in Adult and Children's Services, officers and members are working together to revise recovery plans and to ensure that spending stays within budget.

Focus for 2010/11:

The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

2. Securing economy efficiency and effectiveness

The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

Focus for 2010/11:

The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

The criterion is met.

- The 2011/12 budget prioritised resources to meet realistic tighter budget constraints. Arrangements are in place to ensure that the Council can continue to drive out efficiencies.
- The Council's Annual Governance Statement confirms that underlying performance management systems continue to operate effectively.
- The Council has been able to respond with valid reasons for variances identified by the Audit Commission's VFM profiles.
- The management of Adult and Children's services continues to be challenging as demand pushes up costs but the Council is committed to driving up standards in Childrens' Services and delivering priorities in Adult Services and is actively managing these issues.

Appendix 1 – Draft audit report

Independent Auditor's Report to the Members of Torbay Council

Opinion on the Authority's accounting statements

I have audited the accounting statements of Torbay Council for the year ended 31 March 2011 under the Audit Commission Act 1998. The accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Collection Fund, and the related notes. These accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of Torbay Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Chief Financial Officer and auditor

As explained more fully in the Statement of the Chief Financial Officer's Responsibilities, the Chief Financial Officer is responsible for the preparation of the Authority's Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAC Code of Practice on Local Authority Accounting in the United Kingdom. My responsibility is to audit the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements sufficient to give reasonable assurance that the accounting statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Authority; and the overall presentation of the accounting statements. I read all the information in the explanatory foreword to identify material inconsistencies with the audited accounting statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on accounting statements

In my opinion the accounting statements:

- give a true and fair view of the state of Torbay Council's affairs as at 31 March 2011 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the accounting statements are prepared is consistent with the accounting statements.

Matters on which I report by exception

I have nothing to report in respect of the governance statement on which I report to you if, in my opinion the governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007.

Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

Auditor's responsibilities

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Basis of conclusion

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2010, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2011.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2010, I am satisfied that, in all significant respects, Torbay Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2011.

Certificate

I certify that I have completed the audit of the accounts of Torbay Council in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

Alun Williams
District Auditor

Audit Commission
3-4 Blenheim Court
Lustleigh Close
Matford Business Park
Exeter EX2 8PW

September 2011

Appendix 2 – Amendments to the draft financial statements

I identified the following misstatements during my audit and management have adjusted the financial statements. I bring them to your attention to aid you in fulfilling your governance responsibilities.

Adjusted misstatement	Nature of adjustment	Comprehensive income and expenditure statement		Balance sheet	
		Dr £000s	Cr £000s	Dr £000s	Cr £000s
Reduction in pension liability (CIES)	The £28 million reduction in pension liability arising from the government's announcement that pension increases will be linked to the (lower) CPI index rather than the RPI should be shown as Exceptional in the CIES. This was originally shown under Non Distributed Costs in the CIES. There is no overall impact on cost of services.	28,000	28,000		
Pension liability estimates (Note 4)	A note explaining the estimation uncertainty will be added for clarity				N/A

Comprehensive income and expenditure statement	Balance sheet
<p>Property, plant and equipment – Infrastructure (Balance sheet)</p> <p>De-recognition of £757k of capital expenditure relating to the South Devon Link Road was incorrectly shown within the 'Other Movements in Cost or Valuation' line, rather than under 'De-recognition on Disposal', in Note 12.</p>	<p>Affects note 12 only</p>
<p>Revaluation reserve (Balance sheet and note 26)</p> <p>The revaluation reserve contains 2 incorrect entries: The surplus/deficit on revaluation included should be (£0.7m), originally, due to typo, shown as £0.7m, and the difference between fair value and historical cost on depreciation should be (£0.7m) rather than £0.7m. The year end value should be £31.4m (£32.8m shown in the statements).</p>	<p>1400</p> <p>1400</p>
<p>Council tax debtors (Note 21)</p> <p>Council tax debtors are misstated: Debtors are described as including Liability orders and are incorrectly shown gross of other precepting authorities £500k. The net effect is £200k and 'Other entities and individuals should be increased by this amount. Total debtors are correct.</p>	<p>Affects Note 21 only</p>

Collection fund	Comprehensive income and expenditure statement	Balance sheet
<p>Collection fund</p>	<p>The distribution of the 2009/10 surplus has been shown double counted within the collection fund. This has resulted in a £700k misstatement in the year end surplus.</p>	<p>Affects collection fund only</p>
<p>Adjustments between accounting basis and funding basis under regulations 2010/11 (Note 7)</p>	<p>Adjustments involving the Capital Adjustment Account - A new separate line should be included for capital grants and contributions applied £4.7m – originally included elsewhere in this note.</p>	<p>Affects disclosure only</p>
<p>Adjustments between accounting basis and funding basis under regulations 2009/10 (Note 7)</p>	<p>Audit of the 2009/10 material balances in this note identified a £5.4m disclosure error which impacts upon 3 entries in the note.</p>	<p>Affects disclosure only</p>
<p>Cash Flow Statement</p>	<p>£9m of grant income has been included in the investing and financing adjustment lines (following contradictory advice from CIPFA) The opposite entry is in adjustments for non-cash movements. The overall net decrease in cash and cash equivalents is not affected.</p>	<p>Affects cash flow only</p>
<p>Dedicated schools grant (Note 37)</p>	<p>The total final DSG shown is misstated – it includes £2.1m grant relating to academies. The value should be £71.1m</p>	<p>Affects Note 37 only</p>

Appendix 3 – Unadjusted misstatements to the financial statements

I identified the following misstatements during my audit, but management has not adjusted the financial statements. I bring them to your attention to help you in fulfilling your governance responsibilities and ask you to correct these misstatements.

If you decide not to amend, please tell me why in the representation letter. If you believe the effect of the uncorrected errors, individually and collectively, is immaterial, please reflect this in the representation letter. Please attach a schedule of the uncorrected errors to the representation letter.

Unadjusted misstatement	Nature of required adjustment	Comprehensive income and expenditure statement		Balance sheet	
		Dr £000s	Cr £000s	Dr £000s	Cr £000s
Property, plant and equipment – Land and buildings (Balance sheet)	7 pieces of land and property with a value of £218k have been included in the asset register and balance sheet where the Council does not have title				218
Property, plant and equipment – Land and buildings (Balance sheet)	The ledger balance does not reconcile to the asset register. The former exceeds the latter by £80k				80

	Comprehensive income and expenditure statement	Balance sheet
<p>Ellacombe school (Balance sheet)</p> <p>Ellacombe school has been leased for 99 years at a notional £5 pa since 1932. The school is included in the Council's asset register at a gross value of £2.2m. The lease is disclosed as an operating lease and therefore the school should not be included on the balance sheet.</p> <p>The Council plans to review and sort out this anomaly in 2011/12.</p>		2,000

Appendix 4 – Glossary

Annual governance statement

A statement of internal control prepared by an audited body and published with the financial statements.

Audit closure certificate

A certificate that I have completed the audit following statutory requirements. This marks the point when I have completed my responsibilities for the audit of the period covered by the financial statements.

Page 19 of 20

Audit opinion

On completion of the audit of the financial statements, I must give my opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Opinion

If I agree that the financial statements give a true and fair view, I issue an unqualified opinion. I issue a qualified opinion if:

- I find the statements do not give a true and fair view; or
- I cannot confirm that the statements give a true and fair view.

Materiality and significance

The Auditing Practices Board (APB) defines this concept as ‘an expression of the relative significance or importance of a particular matter for the financial statements as a whole. A matter is material if its omission would reasonably influence users of the financial statements, such as the addressees of the auditor’s report; also a misstatement is material if it would have a similar influence. Materiality may also be considered for any individual primary statement within the financial statements or of individual items included in them. We cannot define materiality mathematically, as it has both numerical and non-numerical aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

‘Significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

Weaknesses in internal control

A weakness in internal control exists when:

- a control is designed, set up or used in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements quickly; or
- a control necessary to prevent, or detect and correct, misstatements in the financial statements quickly is missing.

An important weakness in internal control is a weakness, or a combination of weaknesses that, in my professional judgement, are important enough that I should report them to you.

Value for money conclusion

The auditor’s conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources based on criteria specified by the Audit Commission.

The Code of Audit Practice defines proper arrangements as corporate performance management and financial management arrangements that form a key part of the system of internal control. These comprise the arrangements for:

- planning finances effectively to deliver strategic priorities and secure sound financial health;
- having a sound understanding of costs and performance and achieving efficiencies in activities;
- reliable and timely financial reporting that meets the needs of internal users, stakeholders and local people;
- commissioning and buying quality services and supplies that are tailored to local needs and deliver sustainable outcomes and value for money;

- producing relevant and reliable data and information to support decision making and manage performance;
- promoting and displaying the principles and values of good governance;
- managing risks and maintaining a sound system of internal control;
- making effective use of natural resources;
- managing assets effectively to help deliver strategic priorities and service needs; and
- planning, organising and developing the workforce effectively to support the achievement of strategic priorities.

If I find that the audited body had adequate arrangements, I issue an unqualified conclusion. If I find that it did not, I issue a qualified conclusion.

If you require a copy of this document in an alternative format or in a language other than English, please call:
0844 798 7070

© Audit Commission 2011.
Design and production by the Audit Commission Publishing Team.
Image copyright © Audit Commission.

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors, members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.



This page is intentionally left blank