

## Luton Borough Council

Audit of Accounts 2009-10

Annual report to those Charged with Governance 2009-10

September 2010

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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.

## Purpose of Report

- 1.1 This report has been prepared for the benefit of discussion between Grant Thornton UK LLP and the Audit Committee of Luton Borough Council (the Council). The purpose of this report is to highlight the key issues arising from the audit of the Council's statement of accounts (including its Group Accounts) for the year ending 31 March 2010.
- 1.2 The document is used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) (ISA UK) 260, and to report audit findings to "those charged with governance", designated as the Audit Committee. These requirements are set out in Appendix A.
- 1.3 The Council is responsible for the preparation of a statement of accounts, which records its financial position as at 31 March 2010 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 Council's statement of accounts represents a true and fair view of the financial position.
- 1.4 Under the Audit Commission's Code of Audit Practice ('the Code'), we are also required to reach a formal conclusion on whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, the Value for Money (VFM) conclusion. This is primarily based on the work carried out for our Use of Resources (UoR) assessment.

## Status of Audit

- 1.5 We were presented with the draft statement of accounts on 21 June 2010. We have performed our final accounts audit in accordance with the Audit Commission's Code of Audit Practice and applicable auditing standards.
- 1.6 There are a small number of completion points outstanding at the date at which this report was issued, detailed in section 2, paragraph 2.3, which we expect to clear in time for approval by the Audit Committee on 22 September 2010.
- 1.7 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 this conclusion.
- 1.8 The appointed day for electors to ask the auditor questions on the accounts this year was 18 August 2010. However, we did not receive questions from the public on this date, and there have been no formal objections to the 2009-10 accounts. Correspondence was received from a member of the public but did not impact on our statutory responsibilities in respect of 2009/10.

## Overall Conclusions

- 1.9 The Council has provided timely accounts and sound working papers, however during the course of our audit we identified a number of material misstatements, which required adjustment before we could issue an unqualified opinion.
- 1.10 In addition, the accounts required a small number of changes to disclosures in the notes as a result of matters identified during the audit process as well as a small number of minor adjustments which were not adjusted on grounds of materiality. These are detailed in Section 2 of this report, and are summarised in Appendices B and C.
- 1.11 We have also made a number of recommendations to improve the accounts process which are set out in Section 2 and summarised in Appendix D of this report.

### *Statement of Accounts Opinion*

- 1.12 We anticipate providing an unqualified opinion on the Council's statement of accounts, prior to the statutory deadline of 30 September 2010.

### *Use of Resources Conclusion*

- 1.13 In providing our opinion on the statement of accounts, we are also required to reach a conclusion on the adequacy of the Council's arrangements for ensuring economy, efficiency and effectiveness in its use of resources. We anticipate providing an unqualified (Use of Resource) conclusion for 2009-10.

## Use of Resources

- 1.14 Our Value for Money conclusion is informed by our work on the Use of Resources (UoR) assessment. The Use of Resources framework assesses the Council's performance against a range of Key Lines of Enquiry (KLOE). In order for us to provide an unqualified conclusion, the Council needed to be assessed as 'adequate' or better for each Key Line of Enquiry ('KLOE') prescribed by the Audit Commission. This was accomplished by the Council in our 2009/10 assessment. A high level summary of findings from this work is set out in Section 3 of this report. A more detailed report on the Use of Resources assessment for 2009-10 will be presented to the Audit Committee in December 2010, following completion of the process.

## Whole of Government Accounts

- 1.15 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 (WGA). This work is not covered by our opinion on the Council's accounts. We will complete this work once the material adjustments to the Council's statement of accounts have been processed and the WGA consolidation pack has been updated in time for the 1 October deadline.

### Summary of audit fees

- 1.16 We have provided a summary of our audit fees for 2009-10 in Appendix E. Our actual fee was the same as quoted in our Audit Plan.

### The Way forward

- 1.17 We will continue to work with the Council 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 2010.

### Acknowledgements

- 1.18 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 Council during the course of our audit. The Council has worked extremely pro-actively with us throughout the year to help deliver both the accounts and Use of Resources audits in an effective manner.

**Grant Thornton UK LLP**

**September 2010**

## 2 The Accounts Opinion

### Introduction

- 2.1 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 comments on the Council's overall financial position.

### Status of the audit

- 2.2 We carried out our audit in accordance with the audit plan presented to the Audit Committee in June 2009. Our audit is substantially complete.
- 2.3 The following finalisation procedures are outstanding:
- obtaining the outstanding invoice from our fixed asset additions testing;
  - obtaining the outstanding Barclays loan confirmation;
  - obtaining the Valuations Report;- this is key to ensuring we can sign off the accounts in accordance with the statutory timetable.
  - review of the final version of the statement of accounts, including the Annual Governance Statement;
  - obtaining and reviewing the Council's letter of management representation; and
  - updating our post balance sheet events review, to the date of signing the accounts.

### Audit Opinion

#### Statement of accounts Opinion

- 2.4 We expect to issue an unqualified audit opinion on the Council's statement of accounts. This is subject to the approval of the final statement of accounts by the Audit Committee on 22 September 2010, and completion of our finalisation procedures.
- 2.5 A number of issues arose during the course of the audit, some of which are considered material to the reported financial performance, and others which although not material should be considered by the Audit Committee. These are set out in paragraphs 2.7 to 2.35 below.
- 2.6 Where appropriate, we have made recommendations for improvement, as set out in the agreed action plan at Appendix D.

## Audit Risk

- 2.7 We identified the following transaction cycles that were classed as critical to the Council and subject to more detailed testing:
- Fixed assets
  - Investments
  - Grant Revenue
  - Expenditure
- 2.8 We identified the following areas of the accounts that required increased audit assurance procedures, as they were either high risk or the figure was not in line with expectation:
- Fixed assets valuation and impairments
  - Recoverability of debts including age profiling of debts
  - Group accounts, including review of the valuation of London Luton Airport Limited.
- 2.9 All issues related to our audit of these areas have been set out in this Report and there are no further issues which we need to mention.

## Financial Performance

- 2.10 The Council has produced good financial results for the year, including the decrease of a substantial net deficit, which are broadly in line with medium term financial plans. The Council's financial performance in the year can be measured in terms of the net increase in the General Fund Balance.
- 2.11 The General Fund exists to finance the Council's day to day costs of providing services. All expenditure, other than that relating to capital and the Housing Revenue Account (HRA) is charged to the General Fund through the Income and Expenditure (I&E) account.
- 2.12 The Council has reported an I&E account deficit of £43.64 million (2008-09 £66.83 million). This is after taking into account an impairment of £18.43 million on tangible fixed assets [
- 2.13 The Statement of Movement on the General Fund Balance adjusts the reported I&E account deficit to exclude specific costs, which are determined by statute and include transfers to Earmarked Reserves, in order to calculate the net impact on the Council's General Fund. This statement shows that the Council has increased the General Fund by £1.206 million in year, bringing the total General Fund balance at year end to £6.803 million (excluding a further £8.877 million allocated to schools).

## Issues Arising in the Year

- 2.14 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:

### Accounting Policies and Practices

- 2.15 We consider that the Council has largely adopted appropriate accounting policies in the areas covered by our testing. Accounting policies adopted are in accordance with the 2009 SoRP. However, our testing has identified an area where the policies have not been consistently applied. The departures are set out below.
- 2.16 The Council's accounting policy note on depreciation states that all tangible fixed assets are depreciated on a straight-line basis over their estimated useful lives (with certain exceptions). During the course of our audit it was discovered that depreciation is calculated by dividing the opening net book value of the fixed assets by the remaining useful life of the asset. This is effectively the reducing balance method of calculating depreciation and is therefore not according to the method stated in the accounting policy notes. An adjustment has not been proposed as we have calculated that the potential error is not material to the 2009-10 statement of accounts. We are aware that the Council is in the process of developing an asset management system that will help eliminate possible material misstatement in future.

### Recommendations:

- The Council should review its depreciation process, to ensure that depreciation is accounted for in line with its accounting policy.
- The Council should prioritise the development of the asset management system, to ensure that on-going issues with the accuracy of the fixed asset register are addressed.

### Fixed Asset Valuations

- 2.17 According to the SoRP, the valuer is required to produce two documents; the valuation certificate and the valuation report. The valuation report is a separate report, in addition to the valuation certificate, which is required to cover such matters as; 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 and the proposals for carrying out additional and ad hoc valuations. As at 31 August 2010, the valuation report had not yet been drafted by the Council's valuers and as a result we have been unable to form a view on the adequacy of the work of the valuer as required by auditing standards. Receipt of this report and audit review of the assumptions contained within it are a pre-requisite for us to be able to sign off by 30 September.
- 2.18 Halyard School valued at £5.8 million is to be demolished in order to make way for the construction of an Academy. The buildings element has been valued at £220,000 and should be subject to impairment. As this amount is not material to the accounts, we have not proposed an adjustment to impair the school's building value to £nil, but intend to include this in the schedule of unadjusted errors.



- 2.19 SSAP 19 requires investment properties to be included in the balance sheet at open market value. One investment property, is currently valued at £100,000 in the accounts at historic cost. The potential increase in value is unlikely to be material to the financial statements.

**Recommendations:**

- Valuation reports should accompany valuation certificates for all valuations carried out on the Council's assets to ensure compliance with the SORP.
- A review for impairment of a fixed asset should be carried out if events or changes in circumstances indicate that the carrying amount of the fixed asset or goodwill may not be recoverable.
- Investment properties should be included in the balance sheet at open market value.

**Fixed Asset Completeness**

- 2.20 Housing Revenue Account Investment Properties were revalued as part of the 01/04/10 Valuation Certificate, however the Valuation Certificate was not received until after the accounts had been prepared and the Capital Accountant was therefore unable to process the upward revaluation adjustment £0.58 million.
- 2.21 According to FRS15 (Tangible Fixed Assets), where an asset has been revalued the current period's depreciation charge is based on the revalued amount and the remaining useful economic life. The Council's current depreciation charge for the year for assets that have been revalued in year is not based on the revalued amount does not comply with of FRS15.

**Recommendations:**

- All revaluations should be recorded in the year to which they relate.
- Depreciation should be calculated on the assets revalued amount.

**Capital Expenditure**

- 2.22 During our audit we identified capital expenditure amounting to £5.59 million which had not been capitalised or recognised as a capital creditor in the accounts. As a result of this omission, fixed assets and creditors for the year were understated. Due to the material amount involved, the Council has agreed to adjust the accounts.
- 2.23 We have also identified that £1.205 million of capital expenditure recorded in 2009-10 that actually relates to 2008-09, but was not accrued for in 2008-09.

**Recommendation:**

The Council should review the nature and frequency with which the service departments communicate with Corporate Finance to identify any areas which should be strengthened.

### **Leases**

- 2.24 During our audit the Council identified a previous lease arrangement which had not been disclosed as a finance lease under SSAP21. This lease is related to the rental of the Registrars Premises on George Street West. The fair value of the premises amounts to £544,000 and has been added to our summary of unadjusted errors.

#### **Recommendation:**

A central leases register should be maintained by the finance department and reviewed regularly to ensure the completeness and accuracy of records. The leases in the register should be assessed when preparing the year end accounts to ensure appropriate classification and disclosures are made.

### **Investment Properties**

- 2.25 A car park valued at £3.75 million has been included in investment properties despite being leased to London Luton Airport, a subsidiary of the Council. SSAP 19 states that a property let to and occupied by another group company is not an investment property for the purposes of its own accounts or the group accounts. The car park should therefore be reclassified as an operational fixed asset and depreciated accordingly.
- 2.26 South Luton School valued at £7.615 million has been included in investment properties despite being leased at peppercorn rates. For the purposes of SSAP 19, an investment property is an interest in land and/or buildings, which is held for its investment potential, any rental income being negotiated at arm's length. Although this amount is material to the accounts, we have agreed that it will not be adjusted on the basis that it is only a reclassification entry from investment properties into operational fixed assets and the resulting depreciation would be significantly below materiality. We expect that this issue will be addressed in the 2010-11 accounts when the Council will be required to comply with International Financial Reporting Standards.

#### **Recommendation:**

The Council should ensure that all investment properties are assessed against the requirements of SSAP 19.

### **Housing Benefits GIRO Account**

- 2.27 In the prior year it was found that the Housing Benefits payment bank account could not be reconciled to the ledger and that the reconciling difference was £111,130. In 2009-10, this difference has more than doubled to £255,241. An adjustment has been proposed but is not material to the 2009-10 statement of accounts.

#### **Recommendation:**

The Council should review and resolve differences to ensure the correct amounts are reconciled between the associated systems.

### **Housing Rents Bad Debt Provision**

- 2.28 Due to an error in the Council's calculation, the Housing Rents Bad Debt provision has been understated by £220,000.

#### **Recommendation:**

The Council should that robust arrangements are in place to ensure spreadsheets used to provide provisions data are correct..

### **Completeness of Creditors**

- 2.29 During our audit we identified a trade creditor's invoice amounting to £185,000, that related to 2009-10 but which had not been accrued for in the accounts.
- 2.30 There were also a number of debit balances on the trade creditors ledger, amounting to £75,000, which should have been reclassified to debtors.

#### **Recommendation:**

The Council should review their cut-off arrangements to ensure that all income and expenditure relating to the financial year end in question is accounted for correctly.

### **Deferred Capital Grants**

- 2.31 Our 2008-09 audit of capital grants deferred highlighted an area of control weakness. The SORP requires these grants to be matched to individual assets, with the assets depreciation charge effectively cancelled out by releasing the equivalent value from the grant over the useful economic life of the asset. Our audit testing of deferred grants found that a majority of the deferred grant expenditure could not be matched to the specific education assets they were intended to finance.
- 2.32 This year it was found that some Capital Grants are being amortised over 40 years despite being used to purchase IT equipment. SSAP 4 (Revised) Accounting for Government Grants provides that grants related to capital expenditure should be credited to revenue over the expected useful life of the assets. An adjustment has not been proposed as we have calculated that the potential error is not material to the 2009-10 statement of accounts.

#### **Recommendation:**

A review should be undertaken against deferred grants to, where possible, trace to an individual asset and amortised over the life of the asset they relate to. All amounts which can not be traced should be written off. Such grants cannot be carried forward under IFRS.

### **Financial Instruments (London Luton Airport Valuation)**

- 2.33 The Council has reflected the investment in London Luton Airport within the financial instrument note, which was identified as an issue in the prior year ISA260 report, as an unquoted investment valued at cost on the basis that a fair value cannot be attributed to the asset. In order for the asset to be valued at fair value the

financial asset must fall into one of two categories and those are loans or receivables or assets available for sale.

- 2.34 Loans or receivables are defined as financial assets that have fixed or determinable payments and are not quoted in an active market. However, as we did not consider the investments in the Airport and the related dividends and debentures interest to be fixed or determinable, we are of the view that strict application of accounting standards would mean that the Airport could be classified, in accounting terms, as available for sale. Discussions with the Head of Corporate Finance have indicated that there is no intention by the Council to sell this asset.
- 2.35 We have considered this argument against the provisions of the SoRP which indicate that this type of financial asset could be classified as an asset available for sale and given the context and nature of the Airport investment for the Council we are satisfied with the Council's treatment in the accounts.

### **Pension Fund Assets**

- 2.36 There is a difference between the value of the fund per the actuary and the pension fund accounts as at 31 March 2010 resulting in an estimated understatement of pension fund assets at the Council of £1.421 million

### **Internal Control Issues**

- 2.37 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 Council's key financial control systems did not identify any fundamental control issues presenting a material risk to the accuracy of the statement of accounts.

### **Information Technology**

- 2.38 We performed a high level review of the general IT control environment as part of the overall review of the internal control system and did not identify any issues that require immediate action. However, we have identified an area that requires improvement:

#### ***Acknowledgement of the ICT Security Policy***

- 2.39 An ICT security policy has been formally documented and is available on the Council's Intranet. There is currently no process of ensuring that users confirm that they consent to comply with the Council's Security policy. User sign off is currently sought for the Internet policy. There are plans to deploy a tool to manage this process.
- 2.40 Without formal acceptance of the security policy staff may not be aware of their responsibilities in respect of Information Security. Additionally, where a breach occurs IT management may be unable to refer to the policy as part of a disciplinary process.

#### **Recommendation:**

We recommend that a process of obtaining staff acknowledgement of their responsibility to comply with the ICT security policy is implemented as planned.

### **Internal Audit**

- 2.41 Where appropriate, we have been able to use the work completed by Internal Audit to support our audit in documenting and understanding material systems used to produce the statement of accounts. There were no fundamental control issues, arising from the work of Internal Audit.

### **Other Audit Issues**

- 2.42 A number of more detailed systems and internal control issues arose from our audit, which are set out below:

#### ***Statement of Movement on the General Fund Balance (SMGFB)***

- 2.43 When agreeing the Revenue Expenditure Funded from Capital Under Statute (REFCUS) per Capital Monitoring Schedule to the REFCUS per the SMGFB, there was a difference of £867k, which has been caused by deducting the Disabled Facilities Grant and Decent Homes Grant from the REFCUS before including it in the SMGFB. There is no reason for this treatment other than it is the way it has been done in the past.

#### **Recommendation:**

The Council should revise its treatment of Disabled Facilities Grant and Decent Homes Grant and ensure that they are included in the SMGFB in 2010-11 .

#### ***Statement of Recognised Gains & Losses (STRGL)***

- 2.44 The Council has made progress in clearing balancing items from the STRGL since 2008-09. However, there remains a small 'Other' balance of £224,000 which should be cleared during 2010-11.

#### **Recommendation:**

The Council should ensure that residual balancing items are removed from the STRGL in 2010-11.

#### ***Schools Reserves***

- 2.45 Putteridge High School Reserve of £168k could not be agreed to a signed confirmation as the school had not yet returned this to the Council.

#### **Recommendation:**

The Council should ensure that all confirmations due from schools are signed and returned before the school closes for the summer holiday.

## Adjusted Misstatements

- 2.46 There were a number of material misstatements identified during the course of the audit, which finance officers have agreed to amend:
- Capital expenditure of £5.59 million not accrued for at year end
  - Reclassification of a car park valued at £3.75 million from investment properties to operational fixed assets.
- 2.47 We have also identified the following non-material adjustments, which finance officers have agreed to amend:
- Capital Commitments: The Capital Commitments note was understated and has increased from £43.6 million to £45.9 million.
  - HRA Rent and Arrears: The rent arrears at 31 March 2010 was understated and has been increased from £2.159 million to £2.164 million.
  - Pensions Liability and Reserve: Council to include disclosure on best employer estimate of contributions expected to be paid to the pension fund in the next accounting period.
- 2.48 At the time of this Report, a number of other minor adjustments were to be processed through the Accounts by the Borough's finance team.
- 2.49 A number of disclosure adjustments have also been agreed to improve clarity and presentation of the accounts which do not affect the reported financial position.
- 2.50 All adjusted misstatements are scheduled at Appendix B. The aggregate of these adjustments has impacted on the Income and Expenditure account deficit and on General Fund balances.

## Unadjusted Misstatements

- 2.51 There were a number of unadjusted misstatements which were not processed by management on grounds of materiality. We do not consider these to have a significant bearing on the validity of the reported accounts, but it is important that those charged with governance satisfy themselves that these misstatements do not warrant adjustment prior to approving the financial statements. These are scheduled at Appendix C.

## Annual Governance Statement ('AGS')

- 2.52 We have examined the Council'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 Council. The AGS is a comprehensive and well structured assessment of the Council's governance arrangements and areas requiring further attention.
- 2.53 The Council have agreed to update the AGS, in the context of the proposed adjustments and control issues identified during the audit. Areas include:

- The Financial Statements Audit has revealed some capital accounting weaknesses, including a material error in capital accruals. This may be worthy of inclusion under key control weaknesses (for example, capital accruals and depreciation policy).
- The AGS needs to be updated to reflect recent developments in Government grant cuts and particularly, the impact of BSF cuts on financial and service plans.
- One of the key issues highlighted in our UoR work was high levels of sickness absence. This is likely to be significant in the context of the control framework and should be covered by the AGS.

### Next Steps

- 2.54 The Audit Committee should approve the final annual accounts of the Council for the year ended 2009-10, and consider the issues raised in this report.
- 2.55 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 these is the full implementation of International Financial Reporting Standards (IFRS) in the 2010/11 accounts. It is important that the Council continues to progress its IFRS implementation plans as a matter of priority, including a restatement of the 2009/10 accounts, in order to ensure that it is fully prepared for the transition. 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. Working with the finance team, we are already sharing our experiences of working with CIPFA in implementing IFRS and this will continue over the next year.

### 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

- Introduction**
- 3.1 This section sets out the basis for our value for money conclusion and summarises our work on Use of resources (UoR) to date.
- Our Conclusion**
- 3.2 Based on the Use of Resources assessment, we propose to give an unqualified value for Money conclusion.
- Overall conclusion**
- 3.3 The Council has been assessed as adequate overall, in regard to the criteria for assessing Use of Resources and Value for Money. This is in line with the prevailing level of performance nationally for organisations subject to the assessment.
- 3.4 In order for us to provide an unqualified conclusion, the Council needed to achieve an 'adequate' level of performance for each Key Line of Enquiry (KLOE). This requirement has been achieved by the Council for 2009/10.
- 3.5 Our assessment for the Council is summarised by KLOE 'Theme' in table 1. Please note that, following the termination of the CAA process, we are no longer permitted to publish numerical scores, as has been the case in prior years and can only conclude whether or not the Council's arrangements are adequate. When compared to 2009 the Council has strengthened its performance in Managing Finances.

**Table 1: UoR Conclusions**

#### 1. Managing Finances

	2010	Score 2009
1.1 Financial Planning & Delivering Priorities	At least adequate	Adequate
1.2 Understanding Costs	At least adequate	Adequate
1.3 Reporting Finances & Performance	Adequate	Adequate
<b>Theme</b>	<b>at least Adequate</b>	<b>Adequate</b>

#### 2. Governing the Business

2.1 Commissioning & Procurement	Adequate	Adequate
2.2 Data Quality	Adequate	Adequate
2.3 Principles of Governance	Adequate	Adequate
2.4 Risk & Internal Control	<b>Adequate</b>	<b>Adequate</b>



### 3. Managing Other Resources

	2010	Score 2009
3.1 Use of Natural Resources	Adequate	Adequate
3.2 Asset Management	Adequate	Adequate
3.3 Managing People	Adequate	Not Assessed
<b><i>Theme</i></b>	<b>Adequate</b>	<b>Adequate</b>
<b>Overall UoR assessment</b>	<b>Adequate</b>	<b>Adequate</b>

#### The Way Forward

- 3.6 The detailed outcomes of our Use of Resources audit will be reported in full in a separate report to be presented to the Audit Committee in December 2010.

## 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 to 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
<b>Independence</b>	<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"><li>• We are independently appointed by the Audit Commission.</li><li>• The firm has been assessed by the Audit Commission as complying with its required quality standards.</li><li>• The appointed auditor and client service manager are subject to rotation every 5 years</li><li>• We comply with the Auditing Practices Board's Ethical Standards.</li><li>• We have not charged fees for additional services in excess of the main audit fee (£287,000 excluding VAT).</li></ul>

Area	Key Messages
<b>Audit Approach</b>	<p>Our approach to the audit was set out in our 2009/10 audit plan and our audit strategy document for the year ending 31 March 2010. 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"> <li>• We consider the materiality of items in the statement of accounts in determining the audit approach and in determining the impact of any errors.</li> <li>• We have been able to place appropriate reliance on the key accounting systems operating at the Council for final accounts audit purposes.</li> <li>• In 2009/10, we have been able to place reliance on the work of internal audit in respect of understanding and documenting key accounting systems.</li> </ul>
<b>Accounting Policies</b>	<p>We consider that the Council has adopted appropriate accounting policies in the areas covered by our testing. Accounting policies were in accordance with the 2009 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 Council's financial plans in regard to the appropriateness for the Council to account on a going concern basis and find this to have been appropriate.</p>
<b>Material Risks</b>	<p>We have requested from the Council 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 Council have been recognised in the accounts as at the date of the audit report.</p>

Area	Key Messages
<b>Audit Adjustments</b>	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.
<b>Unadjusted Errors</b>	From the audit results mentioned previously we have identified no unadjusted errors. These are disclosed in Appendix C.
<b>Other Matters</b>	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 Council.

### 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	£'000	Accounts balance	Impact on statement of accounts
<b>Misstatement</b>	£5,552	Capital expenditure which has not been capitalised or recognised as a capital creditor in the accounts. As a result of this omission, fixed assets and creditors for the year were understated.	<b>The financial impact would be as follows:</b>  <b>Increase Fixed asset by £5,552k</b> <b>Increase Capital creditors by £5,552k</b>

Adjustment type	£'000	Accounts balance	Impact on statement of accounts
<b>Classification</b>	£3,750	A car park (40 acres of land) has been included in investment properties despite being leased to London Luton Airport, a subsidiary of the Council. SSAP 19 states that a property let to and occupied by another group company is not an investment property for the purposes of its own accounts or the group accounts. The car park should therefore be reclassified as an operational fixed asset.	<b>The financial impact would be as follows:</b>  <b>Increase Operational fixed assets by £3,750k</b> <b>Decrease Investment properties by £3,750k</b>
<b>Classification</b>	£1,265	The split between Dwellings and Land and Buildings is correct within note 15 (Tangible Fixed Assets) however the split between these classes of assets on the face of the balance sheet is incorrect.  This is simply a classification error with nil effect on overall assets, and will only effect the face of the balance sheet.	<b>An amendment is required to the face of the Balance Sheet only:</b>  <b>Increase Council Dwellings by £1,265k</b> <b>Decrease Land and Buildings by £1,265k</b>
<b>Disclosure</b>	£45,900	Note 28 (Significant Commitments under Capital Contracts) The amount for capital commitments has been understated by £2,300k.  Capital commitments should read £45,900k. This is to adjust the existing figure of £43,600k.	<b>No impact upon the financial statements only the amount stated in note 28 for 2009-10 capital commitments required updating.</b>

Adjustment type	£'000	Accounts balance	Impact on statement of accounts
<b>Disclosure</b>	£2,164	HRA Note 11 (Rent and Arrears) narrative requires updating from £2,159k to £2,164k.	<b>No impact upon the financial statements only the amount stated in HRA note 11 for 2009-10 rent arrears required updating.</b>
<b>Disclosure</b>	£17,173	Note 23 (Pensions Liability and Pensions Scheme) requires disclosure of best employer estimate of contributions expected to be paid to the pension plan in the next accounting period.	<b>No impact upon the financial statements only the disclosure of employer estimate of future pension plan contributions.</b>
<b>Disclosure</b>		All	<b>A number of disclosure adjustments have been agreed to improve clarity and presentation of the accounts which do not affect the reported financial position.</b>

## 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	£'000	Accounts balance	Impact on statement of accounts
<b>Misstatement</b>	£185	During our audit we identified a trade creditor's invoice amounting to £185k, that related to 2009-10 but which had not been accrued for in the accounts.	<b>The financial impact would be as follows:</b>  <b>Increase Trade Creditors by £185k</b> <b>Increase in Income and Expenditure deficit by £185k</b>
<b>Misstatement</b>	£578	Housing Revenue Account Investment Properties were revalued as part of the 01/04/10 Valuation Certificate, however the Valuation Certificate was not received until after the accounts had been prepared and the Capital Accountant was therefore unable to process the upward revaluation adjustment £578k.	<b>The financial impact would be as follows:</b>  <b>Increase Investment Properties by £578k</b> <b>Increase in Revaluation Reserve by £578k</b>
<b>Misstatement</b>	£220	Halyard School valued at £0.22 million is to be demolished in order to make way for the construction of an Academy, however no impairment has been recognised in the accounts.	<b>The financial impact would be as follows:</b>  <b>Decrease Investment Properties by £220k</b> <b>Increase in Income and Expenditure deficit by £220k</b>



Adjustment type	£'000	Accounts balance	Impact on statement of accounts
<b>Misstatement</b>	£255	The Housing Benefits payment bank account could not be reconciled to the ledger. The reconciling difference is £255k.	<b>The financial impact would be as follows:</b>  <b>Decrease Bank and Cash by £255k</b> <b>Increase in Income and Expenditure deficit by £255k</b>
<b>Misstatement</b>	£220	Due to an error in the Council's calculation, the Housing Rents Bad Debt provision has been understated by £220k.	<b>The financial impact would be as follows:</b>  <b>Decrease Debtors by £220k</b> <b>Increase in Income and Expenditure deficit by £220k</b>
<b>Misstatement</b>	£1,421	There is a difference between the value of the fund per the actuary and the pension fund accounts as at 31 March 2010 resulting in an estimated understatement of pension fund assets at the Council of £1.421 million.	<b>The financial impact would be as follows:</b>  <b>Decrease Pension Fund liability by £1,421k</b> <b>Increase in Pensions Reserves by £1,421k</b>
<b>Misstatement</b>	£1,205	We have identified that £1.205 million of capital expenditure recorded in 2009-10 that actually relates to 2008-09, but was not accrued for in 2008-09.	<b>The financial impact would be as follows:</b>  <b>Decrease Income and Expenditure deficit by £1,205k</b> <b>Decrease in General fund balance by £1,205k</b>

Adjustment type	£'000	Accounts balance	Impact on statement of accounts
<b>Misstatement</b>	£544	The operating lease for the rental of George Street West (Registrars Office) should actually be recorded as a finance lease in the accounts as it would seem that the Council bears a greater share of the risks and rewards of the premises and the at the inception of the lease the present value of the minimum lease payments amounts to substantially all (94%) of the fair value of the leased asset.	<p><b>The financial impact would be as follows:</b></p> <p><b>Increase Fixed Assets by £544k*</b></p> <p><b>Decrease in Loan Creditor liability by £544k*</b></p>
<b>Classification</b>	£75	We identified a number of debit balances on the trade creditors ledger, amounting to £75k, which should have been reclassified to debtors.	<p><b>The financial impact would be as follows:</b></p> <p><b>Increase Trade Creditors by £75k</b></p> <p><b>Increase in Debtors by £75k</b></p>
<b>Classification</b>	£7,615	South Luton School valued at £7,615k has been included in investment properties despite being leased at peppercorn rates. For the purposes of SSAP 19, an investment property is an interest in land and/or buildings, which is held for its investment potential, any rental income being negotiated at arm's length. Although this amount is material to the accounts, we have agreed that it will not be adjusted on the basis that it is only a reclassification entry from investment properties into operational fixed assets and the resulting depreciation would be significantly below materiality.	<p><b>The financial impact would be as follows:</b></p> <p><b>Decrease Investment Properties by £7,615k</b></p> <p><b>Increase in Operational fixed assets by £7,615k</b></p>

**\* Subject to the calculation of accumulated depreciation and the loan payments to date.**

## D Appendix: Audit Recommendations

The following table presents recommendations arising from the audit.

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council Response	Implementation date and responsibility
1	2.16	The Council should review its depreciation process, to ensure that depreciation is accounted for in line with its accounting policy.	High	The processes are already under review.	March 2011 Senior Accountant (Capital & Technical)
2	2.16	The Council should prioritise the development of the asset management system, to ensure that on-going issues with the accuracy of the fixed asset register are addressed.	High	Plans are in place to procure a module of the existing finance system which will provide this functionality. The system is still being developed by the software supplier, but is expected to be released in December 2010.	By March 2011 Chief Accountant
3	2.17	Valuation reports should accompany valuation certificates for all valuations carried out on the Council's assets to ensure compliance with the SoRP.	High	Agreed	Spring 2011 Head of Capital & Asset Management

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council Response	Implementation date and responsibility
4	2.18	A review for impairment of a fixed asset should be carried out if events or changes in circumstances indicate that the carrying amount of the fixed asset or goodwill may not be recoverable.	Medium	This is already done as a matter of course. The property referred to had been reviewed and impaired.	
5	2.19	Investment properties should be included in the balance sheet at open market value.	Medium	The one investment property not valued at open market value will be investigated.	Immediate Senior Accountant (Capital & Technical)
6	2.20	All revaluations should be recorded in the year to which they relate.	Medium	The Capital & Asset Management Division will be reminded of the need to provide information on a timely basis.	Immediate Head of Corporate Finance
7	2.21	Depreciation should be calculated on the assets revalued amount.	Medium	The depreciation processes will be reviewed as part of the IFRS work and the introduction of Fixed Asset software.	Winter 2010 Senior Accountant (Capital & Technical)
8	2.23	The Council should review the nature and frequency with which the service departments communicate with Corporate Finance to identify any areas which should be strengthened.	Medium	New procedures will be implemented to ensure that capital creditors are identified and accrued properly, especially where more than one service department is involved with the capital project.	March 2011 Chief Accountant

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council Response	Implementation date and responsibility
9	2.24	A central leases register should be maintained by the finance department and reviewed regularly to ensure the completeness and accuracy of records. The leases in the register should be assessed when preparing the year end accounts to ensure appropriate classification and disclosures are made.	Medium	This will be implemented as part of the work around IFRS.	March 2011 Senior Accountant (Capital & Technical)
10	2.26	The Council should ensure that all investment properties are assessed against the requirements of SSAP 19.	Medium	The council will be reviewing all investment properties under the relevant International Standard as part of their IFRS work.	Winter 2010 Chief Accountant & Senior Accountant (Capital & Technical)
11	2.27	The Council should review and resolve differences to ensure the correct amounts are reconciled between the associated systems.	Medium	The bank account referred to is in the process of being closed. Accountants will have this recommendation drawn to their attention.	Autumn 2010 Chief Accountant
12	2.28	The Council should ensure that all formulae in prior year Excel workbooks, which are carried forward, are correct.	Low	All Accountants will be reminded to check formulae.	Ongoing Chief Accountant
13	2.30	The Council should review their cut-off arrangements to ensure that all income and expenditure relating to the financial year end in question is accounted for correctly.	Medium	A system of reviewing payments and receipts for the first weeks of the new financial year will be implemented for future years.	April 2011 Chief Accountant

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council Response	Implementation date and responsibility
14	2.32	A review should be undertaken against deferred grants to, where possible, trace to an individual asset and amortised over the life of the asset they relate to. All amounts which can not be traced should be written off.	High	The 2010/11 Code of Practice will require all deferred grants to be written out to the Income and Expenditure Statement and all future grants will not be deferred.	March 2011 Senior Accountant (Capital & Technical)
15	2.40	We recommend that a process of obtaining staff acknowledgement of their responsibility to comply with the ICT security policy is implemented as planned.	Low	This recommendation will be drawn to the attention of the Head of HR who would provide the resource to manage the Net Consent project.	Immediate Head of Corporate Finance
16	2.43	The Council should revise its treatment of Disabled Facilities Grant and Decent Homes Grant and ensure that they are included in the SMGFB in 2010-11	Low	The Council will review its accounting entries and will include the appropriate entries in the new Movement in Reserves Statement.	April 2011 Senior Accountant (Capital & Technical)
17	2.44	The Council should ensure that residual balancing items are removed from the STRGL in 2010-11.	Low	This is not a required statement in the 2010/11 Code of Practice. However, the council will continue to eliminate any changes in the net worth that do not pass through the Income & Expenditure Statement	March 2011 Chief Accountant

Rec. No.	Para Ref	Recommendation	Priority H/M/L	Council Response	Implementation date and responsibility
18	2.45	The Council should ensure that all confirmations due from schools are signed and returned before the school closes for the summer holiday.	Low	The council will remind all schools of the need to return their signed confirmations.	April 2011 Group Accountant (Schools)



## E Summary of Audit Fees

Audit area	Planned fee 2009/10	Actual fee 2009/10
Financial Statements	£140,000	£140,000
Use of Resources, including Data Quality	£147,000	£147,000
<b>Total</b>	<b>£287,000</b>	<b>£287,000</b>



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