

# Annual Governance Report

Test Valley Borough Council

Audit 2007/08

Date **17 September 2008**

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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.

# Summary

## Purpose

- 1 This report summarises the findings from our 2007/08 audit. It identifies the key issues that you should consider before we issue our opinion, conclusion and certificate.
- 2 This report includes only those matters of governance interest that have come to our attention in performing our audit. Our audit is not designed to identify all matters that might be relevant to you.

## Financial statements

- 3 We have completed our audit work and have concluded that the financial statements submitted for audit were complete and contained only a few non-material errors. We therefore propose to issue an unqualified opinion on your financial statements shortly.

## Value for Money

- 4 The Council's system of internal control was satisfactory during the 2007/08 financial year. We therefore propose to issue an unqualified conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in the use of resources.

## Main issues

- 5 We have suggested that the assurance you have over cash could be further strengthened by introducing a formal process for the monthly bank reconciliations to be formally reviewed and signed-off by a senior manager.
- 6 We have also pointed to a small number of areas where financial reporting could be improved to comply more closely with CIPFA requirements.

## Next steps

- 7 We ask the General Purposes Committee to:
  - consider the matters raised in the report before approving the financial statements for publication;
  - approve the representation letter on behalf of the Council before we issue our opinion, conclusion and certificate; and
  - agree the proposed action plan.

# Financial statements and Annual Governance Statement

- 8 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 the financial statements and Annual Governance Statement. It is therefore important that you consider our findings before you adopt the financial statements and the Annual Governance Statement.
- 9 In planning our audit we identified specific risks and areas of judgement that we have focused on during our audit. We report to you the findings of our work in those areas.
- 10 In addition, auditing standards require us to report to you:
- the draft representation letter which we are asking management and you to sign;
  - our views about the Council’s accounting practices and financial reporting;
  - errors in the financial statements;
  - any expected modification to our report;
  - weaknesses in internal control; and
  - certain other matters.

## Key areas of judgement and audit risk

- 11 In planning our audit we identified key areas of judgement and audit risk that we have considered as part of our audit. Our findings are set out in Table 1.

**Table 1 Key areas of judgement and audit risk**

| Issue or risk   | Finding  |
|---|--|
| Changes to accounting requirements, including those relating to capital assets and financial instruments  | The accounts are fully compliant with the new requirements |
| Capital transactions relating to the major development in Andover   | The transactions did not take place until 2008/09          |
| Issues reported following our audit of your 2006/07 accounts. In particular: <ul style="list-style-type: none"> <li>• Valuing and accounting for fixed assets; and</li> <li>• Accounting for housing benefit overpayments.</li> </ul> | We are satisfied that the issues have been addressed       |

## Financial statements and Annual Governance Statement

### Draft representation letter

- 12** Before we issue our opinion, auditing standards require us to obtain from you and management, written representations that:
- you acknowledge your collective responsibility for preparing financial statements in accordance with the applicable financial reporting framework;
  - you have approved the financial statements;
  - you acknowledge your responsibility for the design and implementation of internal controls to prevent and detect fraud and error;
  - you have told me the results of your assessment of the risk that the financial statements might be materially misstated because of fraud;
  - you have told me any actual or suspected fraud by management, employees with significant roles in internal control or others (where the fraud could have a material impact on the financial statements);
  - you have told me of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others;
  - you have told me about all known actual or possible non-compliance with laws and regulations whose effects should be considered when preparing financial statements;
  - you have assessed the reasonableness of significant assumptions, including whether they appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the Council where relevant to the fair value measurements or disclosures;
  - you are satisfied that all related parties requiring disclosure in the financial statements have been disclosed and that the disclosure is adequate;
  - you are satisfied that the individual or collective impact of errors we have identified, but that you have not corrected, is not material; and
  - cover areas where other sufficient appropriate evidence cannot reasonably be expected to exist, for example the completeness of the disclosure of contingent liabilities.
- 13** We have sought specific representations from you about the funding of vehicles purchased for £250,000 in February 2008. These have been accounted for on the assumption that they are to be funded from the draw-down of leasing finance, but no such finance has yet been arranged. We understand that arrangements are now to be made, but we need your formal confirmation of this, as no other evidence is available to us.
- 14** Appendix 1 contains the draft of the letter of representation we seek from you.

### Accounting policies and financial reporting

- 15** We considered the qualitative aspects of your financial reporting and have not identified any significant issues to raise with you.

**Errors in the financial statements**

- 16 We identified a small number of errors in the financial statements (other than those of a trivial nature) and reported these to management.
- 17 Management has agreed to adjust the financial statements for the errors identified in Appendix 2. We are reporting these to you because they impact upon figures on the face of your financial statements.
- 18 We have not identified any errors (other than those of a trivial nature) that management has declined to correct.

**The audit report**

- 19 We plan to issue an unmodified report including an unqualified opinion on the financial statements. Appendix 3 contains a copy of our draft report.

**Material weaknesses in internal control**

- 20 We have identified weaknesses in the operation of internal controls that could result in material errors in your financial statements, and which has not been previously reported to you. These are set out in Table 2.

**Table 2 Weaknesses in internal control**

| Issue or risk   | Finding  |
|---|--|
| Bank reconciliations - risk of misstatement and fraud | There is no formal process for a senior manager to check and sign-off the monthly bank reconciliation. This increases the risk that errors go undetected and the opportunity for fraud.  |
| Council Tax system - risk of errors in billing        | The Council Tax bandings for each parish are loaded onto the Council Tax system each year and the Local Taxation Manager checks the entries are correct before billing is started. However, assurance on the operation of this key process would be strengthened if it were formally signed-off by the Local Taxation Manager and authorised by the Head of Revenues and Benefits. |

**Recommendation**

- R1** Strengthen controls over cash by requiring that monthly bank reconciliations are reviewed and signed-off by a senior manager.

**R2** Provide additional assurance that the correct parish council tax bandings have been loaded onto the system by evidencing sign-off by the Local Taxation Manager and authorisation by the Head of Revenues and Benefits.

**21** We have not provided a comprehensive statement of all weaknesses which may exist in internal control, nor of all improvements which may be made. We have reported only those matters which have come to our attention because of the audit procedures we have performed.

### Other matters

**22** There are no other matters that auditing standards require me to report to you.

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# Value for money

- 23 We are required to conclude whether the Council has put in place adequate corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. We assess your arrangements against 12 criteria specified by the Commission. Our conclusion is informed by our work on Use of Resources, a scored judgement reported to the Audit Commission.
- 24 We have assessed the arrangements of the Council as adequate in all 12 areas and we therefore propose to issue an unqualified conclusion.

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# Formal audit powers

25 We have:

- a power to issue a public interest report. We do so where we believe this is necessary to draw a matter to your attention, or to that of the public;
- a power to apply to court for a declaration that an item in the Council's accounts is contrary to law;
- a power to issue an advisory notice. An advisory notice requires the Council to meet and consider the notice before:
  - making a decision that might give rise to unlawful expenditure; or
  - taking an unlawful course of action that would give rise to a loss; or
  - making unlawful entry in the accounts; and
- a power to seek judicial review of a decision of the Council.

26 We have not and do not propose to exercise these powers.

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# Independence

- 27** The Code of Audit Practice and the APB's Ethical Standards with which auditors must comply require that auditors act, and are seen to act, with integrity, objectivity and independence.
- 28** We confirm that we comply with the APB's Ethical Standards, that we are independent and that our objectivity is not compromised.
- 29** We communicate to you:
- any relationships between us and the Council, its members and senior management that might affect our objectivity and independence and any safeguards put in place;
  - total fees charged to you for audit and non-audit services; and
  - our arrangements to ensure independence and objectivity.

## Relationships with the Council

- 30** We have identified no relationships that might affect objectivity and independence.

## Audit fees

- 31** We reported our fee proposals as part of the Audit Plan for 2007/08. The table below reports the outturn fee against that plan.

**Table 3      Audit fees**

|  | <b>Plan 2007/08</b> | <b>Actual 2007/08</b> |
|--|---------------------|-----------------------|
| Financial statements and Annual Governance Statement | £59,457             | £59,457               |
| Value for Money                                      | £26,409             | £26,409               |
| Whole of Government accounts                         | £ 1,819             | £ 1,819               |
| National Fraud Initiative                            | £ 575               | £ 575                 |
| <b>Total Audit Fees</b>                              | <b>£88,260</b>      | <b>£88,260</b>        |
| Other work   | Nil                 | Nil                   |

- 32** The analysis above shows that we contained our audit fee within the totals you have already agreed.

## Independence

### Our arrangements to ensure independence and objectivity

33 We have comprehensive procedures to ensure independence and objectivity. These are outlined in Table 5.

**Table 4 Arrangements to ensure independence and objectivity**

| Area                  | Arrangements  |
|-----------------------|---|
| Independence policies | <p>Our policies and procedures ensure that professional staff or an immediate family member:</p> <ul style="list-style-type: none"><li>• do not hold a financial interest in any of our audit clients;</li><li>• may not work on assignments if they have a financial interest in the client or a party to the transaction or if they have a beneficial interest in a trust holding a financial position in the client; and</li><li>• may not enter into business relationships with UK audit clients or their affiliates.</li></ul> <p>Our procedures also cover the following topics and can be provided to you on request:</p> <ul style="list-style-type: none"><li>• the general requirement to carry out work independently and objectively;</li><li>• safeguarding against potential conflicts of interest;</li><li>• acceptance of additional (non-audit) work;</li><li>• rotation of key staff;</li><li>• other links with audited bodies;</li><li>• secondments;</li><li>• membership of audited bodies;</li><li>• employment by audited bodies;</li><li>• political activity; and</li><li>• gifts and hospitality.</li></ul> |
| Code of Conduct       | <p>The Code of Conduct forms part of the terms and conditions of all Audit Commission employees. The Code of Conduct states that staff have to comply with ethical guidance issued by their relevant professional bodies.</p>   |
| Confidentiality       | <p>All staff are required to sign an annual undertaking of confidentiality as a condition of employment.</p>  |

# Appendix 1 – Letter of management representations

To: Patrick Jarvis  
District Auditor  
The Audit Commission  
Collins House  
Bishopstoke Road  
Eastleigh  
Hampshire SO50 6AD

Dear Patrick

## **Test Valley Borough Council – Audit for the year ended 31 March 2008**

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Test Valley Borough Council, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2008.

### **Compliance with the statutory authorities**

I acknowledge my responsibility under the relevant statutory authorities for preparing the financial statements, in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom: A Statement of Recommended Practice, which present fairly the financial position and financial performance of the council and for making accurate representations to you.

### **Supporting records**

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the council have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Council and Committee meetings, have been made available to you.

### **Irregularities**

I acknowledge my responsibility for the design and implementation of internal control systems to prevent and detect fraud or error.

There have been no:

- irregularities involving management or employees who have significant roles in the system of internal accounting control;

## Appendix 1 – Letter of management representations

- irregularities involving other employees that could have a material effect on the financial statements; or
- communications from regulatory agencies concerning non-compliance with, or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements; and
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

### Law, regulations, contractual arrangements and codes of practice

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the council.

The council has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

### Fair Values

I confirm the reasonableness of the significant assumptions on fair value within the financial statements

### Assets

The following have been properly recorded and, where appropriate, adequately disclosed in the financial statements:

- losses arising from sale & purchase commitments;
- agreements & options to buy back assets previously sold; and
- assets pledged as collateral.

### Compensating arrangements

There are no formal or informal compensating balancing arrangements with any of our cash and investment accounts and we have no undisclosed credit arrangements.

### Contingent liabilities

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;

## Appendix 1 – Letter of management representations

- there are no material commitments or contractual issues, other than those already disclosed in the financial statements; and
- no financial guarantees have been given to third parties.

### Related party transactions

I confirm the completeness of the information disclosed regarding the identification of related parties.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements

### Post balance sheet events

Since the date of approval of the financial statements by the Council, no additional significant post balance sheet events that have occurred which would require additional adjustment or disclosure in the financial statements.

The council has no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

### Specific representations:

Vehicles and equipment to the value of £250,000 purchased in February 2008 are to be fully funded by drawdown of equivalent funds from a leasing company and the items remain unfunded at this time only because of delays in arranging drawdown.

### Signed on behalf of Test Valley Borough Council

I confirm that the this letter has been discussed and agreed on behalf of the Council by the General Purposes Committee on 24 September 2008

Signed

William Fullbrook, Head of Finance

Councillor I Carr, Chair of General Purposes Committee and Leader of the Council

Date

## Appendix 2 – Errors adjusted

The following errors were identified during our audit and the Council has made adjustments to correct them in its financial statements.

| Accounting Item   | Adjustment  |
|---|---|
| Balance Sheet sums inappropriately classified as Provisions                 | Your balance sheet provisions included a sum of £136,000 described as a provision for 'all risks loss', and six other items totalling £58,000 that had not changed in value for several years. These items did not meet the definition of a provision in the Financial Reporting Standards (FRS12), as they did not relate to specific obligations to make payment within 12 months. Adjustments have now been made, with most items being re-classified as earmarked reserves. |
| External trading account disclosures in the Income and Expenditure account. | The line in the Council's Income and Expenditure Account for external trading services showed the net deficit of £0.06 million. This has now been replaced with the gross income and expenditure figures of £6.77 million and £6.83 million respectively, in accordance with accounting standards.  |
| Debtor and Creditor balances in the balance sheet                           | An adjustment made to correct an error in the sums due from and to the national non-domestic rate pool was itself incorrect. This led to an overstatement of both balances by £173,256 which has now been corrected.  |
| Earmarked Reserves  | Balances totalling £151,000 on three earmarked reserves in the financial statements did not agree individually with the Council's ledger, although they agreed in total. The figures have been adjusted so that they are consistent with the ledger.  |
| Categorisation of Tangible Fixed Assets in the balance sheet                | CIPFA's Statement of Recommended Practice (SORP) on local authority accounting requires that fixed assets are analysed by category in the balance sheet, but the Council's balance sheet shows only a single figure.  |

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# Appendix 3 – Auditor's report

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## Independent auditor's report to the Members of Test Valley Borough Council

### Opinion on the financial statements

I have audited the Authority accounting statements and related notes of Test Valley Borough Council for the year ended 31 March 2008 under the Audit Commission Act 1998. The Authority accounting statements comprise the Authority Income and Expenditure Account, the Authority Statement of the Movement on the General Fund Balance, the Authority Balance Sheet, the Authority Statement of Total Recognised Gains and Losses, the Authority 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 Test Valley Borough Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 36 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by the Audit Commission.

### Respective responsibilities of the Head of Finance and auditor

The Head of Finance's responsibilities for preparing the financial statements in accordance with relevant legal and regulatory requirements and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2007 are set out in the Statement of Responsibilities for the Statement of Accounts.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the Authority accounting statements present fairly, in accordance with relevant legal and regulatory requirements and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2007 the financial position of the Authority and its income and expenditure for the year.

I review whether the governance statement reflects compliance with 'Delivering Good Governance in Local Government: A Framework' published by CIPFA/SOLACE in June 2007. I report if it does not comply with proper practices specified by CIPFA/SOLACE or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered, whether the governance statement covers all risks and controls. Neither am I required to form an opinion on the effectiveness of the Authority's corporate governance procedures or its risk and control procedures

I read other information published with the Authority accounting statements, and consider whether it is consistent with the audited Authority accounting statements. This other information comprises the Explanatory Foreword. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies

## Appendix 3 – Auditor's report

with the Authority accounting statements. My responsibilities do not extend to any other information.

### Basis of audit opinion

I conducted my audit in accordance with the Audit Commission Act 1998, the Code of Audit Practice issued by the Audit Commission and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the Authority accounting statements and related notes. It also includes an assessment of the significant estimates and judgments made by the Authority in the preparation of the Authority accounting statements and related notes, and of whether the accounting policies are appropriate to the Authority's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the Authority accounting statements and related notes are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the Authority accounting statements and related notes.

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### Opinion

In my opinion, the Authority's financial statements present fairly, in accordance with relevant legal and regulatory requirements and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2007, the financial position of the Authority as at 31 March 2008 and its income and expenditure for the year then ended.

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### Conclusion on 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 regularly to review the adequacy and effectiveness of these arrangements.

#### Auditor's Responsibilities

I am required by the Audit Commission Act 1998 to be satisfied that proper arrangements have been made by the Authority 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 in relation to proper arrangements, having regard to relevant criteria specified by the Audit Commission for principal local authorities. I report if significant matters have come to my attention which prevent me from concluding that the Authority has made such proper

arrangements. 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.

### Conclusion

I have undertaken my audit in accordance with the Code of Audit Practice and having regard to the criteria for principal local authorities specified by the Audit Commission and published in December 2006, I am satisfied that, in all significant respects, Test Valley Borough Council made proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2008.

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### Best Value Performance Plan

I have issued our statutory report on the audit of the authority's best value performance plan for the financial year 2006/07 on 31 December 2007. I did not identify any matters to be reported to the authority and did not make any recommendations on procedures in relation to the plan.

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### Certificate

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

Patrick Jarvis

District Auditor

Audit Commission  
Collins House  
Bishopstoke Road  
Eastleigh  
Hampshire  
SO50 6AD

September 2008