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Argyll and Bute Council
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15 September 2011

SUPPLEMENTARY PACK 3

AUDIT COMMITTEE – FRIDAY 16 SEPTEMBER 2011 AT 11.15 AM

I enclose herewith item 12 **(EXTERNAL AUDIT 2010/11 ACCOUNTS AUDIT)** which was marked "to follow" on the above agenda.

Please note item 11 **(EXTERNAL AUDIT ISA 260 REPORT)** is now incorporated within item 12 and is no longer a separate report on the agenda.

Douglas Hendry
Executive Director - Customer Services

BUSINESS

12. EXTERNAL AUDIT 2010/11 ACCOUNTS AUDIT
Report by Grant Thornton UK LLP, External Auditors (Pages 1 - 18)

AUDIT COMMITTEE

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Grant Thornton

Argyll and Bute Council

Report on the 2010-11 Accounts Audit

31 March 2011

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The purpose of this memorandum is to highlight the key issues affecting the results of the Council and the preparation of the Council's financial statements for the year ending 31 March 1. It is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We take responsibility for this memorandum, which has been prepared on the basis of the limitations set out in 'The small print' (Appendix A).

This is the final year of our appointment as external auditors to the Council. We would like to take this opportunity to record our appreciation for the kind support and assistance provided by the audit committee, finance team and other staff during our audit.

Grant Thornton UK LLP

9 September 2011

Contents

1 Executive summary

1.1 Introduction
This report has been prepared for the benefit of discussion between Grant Thornton UK LLP and the Audit Committee of Argyll and Bute Council (the Council). The purpose of this report is to highlight the key issues arising from the audit of the Council's financial statements for the year ending 31 March 2011.

This report meets the mandatory requirements of International Standard on Auditing 260 (ISA 260) to report the outcome of the audit to 'those charged with governance', designated as the Audit Committee. The requirements of ISA260, and how we have discharged them, are set out in more detail at Appendix A.

The Council is responsible for the preparation of financial statements which record its financial position as at 31 March 2011, and its income and expenditure for the year then ended. We are responsible for undertaking an audit and reporting whether, in our opinion, the Council's financial statements present a true and fair view of the financial position.

1.2 Financial Results
The Council reported a surplus on the Statement of Comprehensive Income and Expenditure for 2010-11 of £101.5 million (2010 restated: deficit £50.7 million). The net decrease on the general fund was £47,000.

The total net worth of the Council at 31 March 2011was £212.5 million (2010 restated: £111.5 million). The significant increase in the net worth position is due to a decrease in the Council's pension liability of £81.7 million due to the Consumer Price Index (CPI) replacing the Retail Price Index (RPI) as the measure of pension inflation, and a reduction in the assumptions in the future rate of wage inflation.

For the year ending 31 March 2011, the Council had a total general fund reserve balance of £32.9 million, of which £29.1 million was earmarked for specific purposes. The unallocated general fund balance is £3.8 million, 1.5% of the Council's budgeted net expenditure for 2011-12, which is in line with the Council's reserves policy.

1.3 Financial Statements
We expect to give an unqualified opinion on the Council's 2010-11 financial statements and conclude that the financial statements are prepared in accordance with Part VII of the Local Government (Scotland) Act 1973 and the Code.

The main change to the financial statements this year has been the transition to IFRS. This has resulted in the restatement of the 2010 and 2009 financial statements.

1.4 Audit Adjustments
The financial statements and supporting working papers presented for audit were generally of good quality. Our audit has, however, identified a small number of adjustments that have been processed by management. The adjustments relate to:

- to correct the valuation methodology for the former Hermitage Academy site
- to update the equal pay provision following receipt of post balance sheet information from the Council's solicitors
- a requirement to recognise the police capital grant as income, with an equivalent amount of expenditure, in both 2010 and 2011

- to release provisions previously made that no longer meet the definition of a provision under IAS 36.
- increase the bad debt provision for aged debts over one year

There is one identified unadjusted misstatement. The Council has not adjusted this misstatement on the basis of materiality.

In addition there was significant adjustments to correct the group accounts following changes in the recognition of the pension costs of injury benefits at two associates

The impact of the audit adjustments on the financial statements is explained in Section 4.

1.5 Design effectiveness of internal controls

We have applied our risk methodology to the audit, which allows us to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

Our audit identified three findings:

- bank reconciliations for the deposit bank accounts not completed during the year

- transactions in 2010-11 relating to the CT/NDR and income bank accounts were not originally included in the general ledger for the year or on the original year end bank reconciliations.

- the bad debt provision methodology should be reviewed on an annual basis, including a review of significant individual debtors for impairment.

Our detailed findings are contained at Section 5 of this report.

2 Financial results

2.1 Statement of Comprehensive Income and Expenditure

The Council reported total comprehensive income and expenditure for 2010-11 of £101.5 million (2010 deficit: £50.7 million). Net cost of services was £209.3 million (2010: £242.4 million).

Table 1: Financial results for 2010-11

	2011 £'000	2010 £'000
Net Cost of Services	209,324	242,450
Other operating income and expenditure	1,453	1,501
Financing and investment income and expenditure	15,670	20,934
Taxation and non-specific grant income	(279,925)	(277,497)
Surplus on the provision of services	**(53,478)**	**(12,612)**
Other comprehensive income and expenditure	(47,572)	63,326
Total Comprehensive Income and Expenditure	**(101,050)**	**50,714**

Source: Argyll and Bute Council 2010-11 financial statements

The main movements in the Comprehensive Income and Expenditure Account relate to pension movements resulting from two changes to the actuarial assumptions used to calculate the Council's liabilities in the Strathclyde Pension Fund.

The first change has arisen as a result of the change in the index used to measure pension inflation from the Retail Price Index (RPI) to the Consumer Price Index (CPI). Although both indices measure the average change in the cost of a basket of retail goods and services, CPI is calculated using the geometric average whereas RPI is calculated using the arithmetic average. As such CPI is generally lower than RPI and by switching to CPI for measuring pension inflation, the value of pension liabilities is reduced. The impact of the change is that a past service gain of £42.2 million is recognised in the 2010-11 accounts and this has been credited to Non-Distributed Costs within Net Cost of Services.

The assumption for salary increases has also changed in 2010-11 to take into account the Government's public sector pay freeze for all but those earning less than £21,000 per annum. This change to the salary increase assumption has led to a reduction in the value of active members' liabilities in the year. This has contributed to actuarial gains on the Council's share of the Fund of £38.9 million (2010: an actuarial loss of £74 million resulting from a change in the discount rate).

2.2 Balance Sheet

The total net worth of the Council at 31 March 2011 was £212.5 million (2010 restated: £111.5 million). The significant increase in the net worth position is due to a decrease in the changes in the pension liability arising from the two actuarial changes noted in section 2.1. The total pension liability as at 31 March 2011 was £26.2 million (2010: £107.9 million).

Short term provisions have increased significantly from £1 million to £4.6 million. The increase relates to the provision of £3.1 million from obligations arising from the Council's restructuring scheme. In addition, a provision of £0.6 million has been recognised to settle equal pay claims.

2.3 General Fund

For the year ending 31 March 2011, the Council has a total general fund reserve balance of £32.9 million, of which £29.1 million was earmarked for specific purposes and £3.8 million was unallocated.

The Council agreed the allocations of the earmarked general fund at their meeting on 23 June 2011. The amount of the general fund to be earmarked by the Council at the meeting was agreed to be £26.7 million, which included a £3.1 million allocation from the PPP Smoothing Fund to meet future severance costs. Following audit adjustments, the amount that is required to be borrowed from the PPP Smoothing Funds has reduced to £0.7 million.

The unallocated general fund balance is £3.8 million, 1.5% of the Council's budgeted net expenditure for 2011-12, which is in line with the Council's reserves policy. The increase on the general fund in the year is £47,000.

3 Financial statements

3.1 Matters identified at the planning stage

In the conduct of our audit, we have not had to alter or change our audit plan, which we communicated to you in our Audit Approach Memorandum.

IFRS

Local authorities are required to comply with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). From 2010/11 this Code is based on International Financial Reporting Standards (IFRS) rather than a UK GAAP based Statement of Recommended Practice (SORP). The Code requires a restated balance sheet at 1 April 2009, restated 2009/10 accounts and full published IFRS accounts for 2010/11. During the year, we performed an arrangements review to provide feedback on the Council's approach to restatement with detailed work on the restated figures taking place during the 2010/11 final accounts audit.

Our report, *Review of arrangements for implementation of International Financial Reporting Standards (IFRS)*, was presented to the audit committee in June 2011 and summarised our review. Overall we found that the Council had made good progress in the transition to IFRS, with further work required in the areas of:

- fixed asset re-categorisation
- group accounts

We also recommended that the Council investigate methods of improving data collection for the holiday pay accrual.

Significant matters relating to IFRS transition noted during the financial statements audit are listed at section 3.2 below.

3.2 Matters identified during the course of the audit

Remuneration Report

During the year, Scottish Ministers approved an amendment to the Local Authority Accounts (Scotland) Regulations 1985 to publish a remuneration report as part of their annual accounts. The report is similar to that produced for listed companies and public sector bodies that report under the Government Financial Reporting Manual.

The amendments to the Regulations require the Council to disclose:

- remuneration policies for senior members and senior officers
- remuneration paid to senior members and senior officers for 2009-10 and 2010-11
- pension benefits including pension contributions paid by the Council and the value of accrued pension benefits at the balance sheet date
- information of the number of employees earning in excess of £50,000 per year.

In future years, the Council will also be required to disclose summary information in relation to exit packages, including compulsory and voluntary redundancy costs, ex-gratia payments and other departure costs.

Our review of the Council's Remuneration Report found that the Report was compiled in accordance with the Regulations and presented in line with guidance issued by the Scottish Government.

Valuation of Hermitage Academy site

The Council holds land relating to the former Hermitage Academy site in Helensburgh, and it is intended that this asset will be sold at some point in the future. The Academy was last used as a school in 2008, and became surplus when a new school estate was built under the NPDO scheme. The Academy was then moved to the available for sale category as negotiations where at an advanced stage with a property developer to acquire the site. However, negotiations ended when the developer entered administration following the downturn in the property market. In the 2011 draft accounts the Academy was valued at £5.5 million in the surplus assets category within property, plant and equipment (PPE) as it no longer met the definition of an asset held for sale.

The Code requires that surplus assets held with PPE are tvalued at existing use at the last time the asset was being used to provide services. The Council's valuer has confirmed this value to be £8.5 million when the asset was last used to provide services as a school. The Council has processed an adjustment to return the asset to its value when last used to provide services to comply with the requirements of the Code.

Equal pay

In 1999, local authorities in Scotland agreed that a new pay and grading system would be introduced (single status), which would ensure equality in pay structures across employee grades. The Council implemented its new pay and grading model in 2007-08.

Under the Equal Pay Act 1970, employees are entitled to make claims for equal pay settlements for a period up to six years. As at 31 March 2010, the Council recognised a provision of £163,000 relating to the claims received, with a contingent liability for those claims it could not quantify at that time.

During 2010-11, the Council was nearing agreement of the settlement of all outstanding claims and the provision was increased to £2.4 million in the draft accounts. Post balance sheet correspondence with the Council's solicitors, however, highlighted that the status of the claims was not as advanced as previously thought, and the Council revised the provision to £0.6 million to match the project settlement amounts provided by its solicitors. the Council has recognised a contingent liability for those claims where a final settlement figure is not yet known.

Holiday pay accrual

A new requirement under the Code relates to the treatment of short-term accumulating compensated absences that can be carried forward where the current entitlement is not used e.g. annual leave and flexitime balances, as authorities are required to recognise a liability for the untaken element at the year end. Authorities are required to measure the additional amount that they expect to pay as a result of unused entitlement that has accumulated at the balance sheet date. This is required even where employees are not entitled to a cash payment for unused entitlement on leaving. Authorities are required to gather information on the number of days of untaken leave as at 31 March to allow them to identify the liability. The liability should represent the proportion of the annual salary which relates to the number of days of untaken leave.

During the IFRS conversion process, the Council found practical difficulties in obtaining the information required to calculate an accurate holiday pay accrual, mainly due to a lack of central computerised records in relation to holiday balances for all grades of staff as this information is held locally by line managers. Accordingly the Council has adopted a methodology using a sample of 5% of employees. The sample is selected across a wide range of employees to ensure it includes all relevant grades and geographical locations. Additional work has been completed on teacher's holiday pay, and on staff groups where holiday balances are likely to be significant (eg those staff on maternity leave).

We have considered the Council's methodology and considered it to be sufficient for the purposes of calculating the holiday pay accruals. During the audit, we reviewed the sample chosen by the Council to confirm the accuracy of the calculation. The results of our audits found a number of errors between the information supplied by HR and the data used by the Council in the accrual calculation. The value of the errors, even if extrapolated across the population, is not considered material to the financial statements and we have not proposed an adjustment in this regards.

We previously recommended that the Council investigate methods of obtaining more accurate information for accumulated absences. The Council hopes that the problem will be solved by a new HR system which will track holidays and flexitime leave and allow this information to be extracted centrally for accounting purposes.

Strathclyde Police Capital Grant

Where an element of the General Capital Grant (GCG) is used to fund third party capital expenditure, it should be recognised as both income and expenditure in the relevant line of the Comprehensive Income and Expenditure Statement in accordance with the Scottish Government's guidance on the 2010-11 GCG,.

The Council originally did not recognise the element of the GCG relating to Police Capital in either 2010 or 2011 as this was received and then paid out to Strathclyde Police. Adjustments have been processed in both 2010 and 2011 to recognise £424,000 and £399,000 as expenditure in the Comprehensive Income and Expenditure Statement under the Strathclyde Police Joint Board heading and as income in Government Capital Grants and other Capital Contributions. These adjustments have no effect on the reported surplus in either of the two years.

Debtors

Recoverability and improvements in process

The gross amount of debtor accounts at 31 March 2011 was £2.5 million. This is compared with a gross amount of £6.2 million at 31 March 2010, a decrease of £3.7 million (60%). This decrease has been facilitated by the implementation of the new debtors system in March 2009. Invoices are now printed from the system and posted or emailed on the same day and statements are issued automatically when amounts are due. Also as part of the process of migration to the new debtors system, the Council transferred as many debtor accounts as possible to payment by either BACS or Direct Debit. This revised approach has had a significant impact on improving overall cash management within the Council.

Table 2 below highlights the aged debt balances, the bad debt provision and the net debtor for each aged category, split into the debtors on the old and new systems.

Table 2: Summary of sundry debtors by age

Age	Debtors balance- new system	Debtors balance- old system	Provision	Net Debtor	BDP %
0-1 month	1,215	0	0	1,215	0%
1-2 months	118	0	7	110	10%
2-3 months	91	0	13	78	20%
3-4 months	8	0	2	6	30%
4-6 months	71	0	21	50	30%
6-9 months	36	0	13	23	40%
9-12 months	36	0	14	22	40%
12-24 months	308	0	158	149	55%
24-36 months	102	99	138	63	70%
36-60 months	0	335	268	67	80%
>60 months	0	289	289	0	100%
TOTAL	**1,983**	**723**	**924**	**1,783**	

The Code requires that authorities should consider the impairment risk of debtor balances and provide for bad and doubtful debts by considering such things as future cashflows and history of default for groups of similar debtors.

Table 2 highlights that there is £279,000 of aged debt over one year that has not been provided for. The Council has reported that, to the end of August 2011, they received £51,000 in relation to aged debts over one year and did not consider that a further provision was required for debtors on the new system.

We noted that there were £96,000 of debtors over one year on the old system that had not been provided for. Given the evidence on debtor recovery and default for these debts, we have concluded that this balance should also be provided for and the Council have processed this adjustment.

Group accounts

The Council's group accounts consolidate the following bodies:

- Strathclyde Police Joint Board
- Strathclyde Fire and Rescue Joint Board
- Strathclyde Partnership for Transport Concessionary Fares
- Dunbartonshire Argyll and Bute Valuation Joint Board
- Oban Common Good Fund
- Campbeltown Common Good Fund.

The joint boards are all audited by external auditors appointed by the Accounts Commission for Scotland. Consolidation is based on the Council's contributions to the joint board's budgets.

The net worth of the Group is £18.8 million (2010: deficit of £113 million) compared to the Council's individual net worth of £212 million (2010: £112 million). The difference reflects the Council's share of deficits in the pension schemes of the Strathclyde Police Joint Board and the Strathclyde Fire and Rescue Joint Board, both of which are unfunded schemes. The schemes are effectively underwritten by the Scottish Government from funding provided to local authorities.

During the audits of Strathclyde Police Joint Board and Strathclyde Fire and Rescue Joint Board, a significant issue was noted with regards to the pension costs associated with injury benefits. Previously, the information supplied by the actuaries under FRS 17, *Retirement Benefits*, excluded an estimate for the service based element of potential future awards. This information is now provided by the actuary under IAS 19, *Employee benefits*, and both associates have determined that this represents a change in accounting policy and as such the 2011 and 2010 group accounts have been amended to reflect the Council's share of the increase in liabilities.

4 Audit adjustments

4.1 Misstatements

Misstatements with a total impact of £92,000 on the Statement of Comprehensive Income and Expenditure were identified by the Council team during the course of the audit and subsequently adjusted, increasing the reported surplus and the general fund for the year.

The following misstatements noted in table 4.2 were identified by Grant Thornton and have been adjusted for.

The net impact of the adjusted misstatements are to increase the surplus on the provision of services in 2010-11 by £2.4 million, and increase the general fund balance by £2.4 million. There is no impact on reported results in the 2009-10 financial statements.

The auditor is required to communicate all uncorrected misstatements, other than those considered to be clearly trivial, to the entity's management and to request that management corrects them. There is one identified unadjusted misstatement as set out in section 4.3.

In addition, there is a number of significant misstatements in the Group accounts arising from audit adjustments in two associates: Strathclyde Police Board and Strathclyde Fire and Rescue Joint Board. These are detailed in section 4.4

4.2 Adjusted misstatements to the Council's financial statements

	Statement of Comprehensive Income and Expenditure		Balance sheet	
	Dr £000	Cr £000	Dr £000	Cr £000
Valuation of Hermitage Academy	Impairment	SOMR	PPE	CAA
Revaluation of Hermitage Academy from to value in use when the asset was last used to provide services in line with Code requirements for surplus assets held within Property, Plant and Equipment.	2,960	2,960	2,960	2,960
Equal pay provision		Net costs of services	Provisions	
Recalculation of the provision following further information provided by the Council's solicitors after the balance sheet date		1,823	1,823	

	Statement of Comprehensive Income and Expenditure		Balance sheet	
	Dr £000	Cr £000	Dr £000	Cr £000
Strathclyde Police capital grant	Net cost of services	Capital grants		
Recognition of grant income regarding police capital grant in accordance with Distribution of Capital Grant schedule in 2011	399	399		
Recognition of grant income regarding police capital grant in accordance with Distribution of Capital Grant schedule in 2010	424	424		
Provisions		Net costs of services	Provisions (short term)	
To release provisions made by the Operational Services department which no longer meet the definitions of a provision under International Accounting Standard 37, *Provisions, Contingent Liabilities and Contingent Assets.*		573	573	
Provision for bad and doubtful debts To provide for doubtful debts over 1 year.	Net cost of services 97			Sundry debtors 97

4.3 Unadjusted misstatements

There is one identified unadjusted misstatements.

	Statement of Comprehensive Income and Expenditure		Balance sheet	
	Dr £000	Cr £000	Dr £000	Cr £000
Debit balances in the creditors listing	-	-	67	67
Reclassification of credit notes within creditors to debtors				
TOTAL	**-**	**-**	**67**	**67**

The Council has declined to adjust this misstatement on the basis of materiality. Where these misstatements to be adjusted, there would be no impact on the reported surplus on the provision of services or the general fund. The audit committee should confirm that it is content for this adjustments not to be processed.

4.4 Adjusted misstatements to the Group accounts

There was a significant adjustment to the Group accounts as a result of the impact of audit adjustments to the accounts of two associates: Strathclyde Police Board and Strathclyde Fire and Rescue Joint Board.

	Group Statement of Comprehensive Income and Expenditure		Group Balance sheet	
	Dr £000	Cr £000	Dr £000	Cr £000
Group accounts To reflect a change in accounting policy by Strathclyde Police Joint Board and Strathclyde Fire and Rescue Joint Board to account for pension costs associated with injury benefits for 2009-10	NCS 382 SOMR 1765	SOMR 382 Actuarial Gains 1,765	Pension Reserve (01/04/09) 4,000	Pension Liability (01/04/09) 4,000
To reflect a change in accounting policy by Strathclyde Police Joint Board and Strathclyde Fire and Rescue Joint Board to account for pension costs associated with injury benefits for 2010-11	NCS 538 SOMR 5,622	SOMR 538 Actuarial Gains 5,622	Pension Reserve (31/03/10) 6,160	Pension Liability (31/03/10) 6,160

The Council adjusted the group accounts upon receipt of the information on the misstatements from the associates as part of the consolidation process.

5 Design effectiveness of internal controls

5.1 Accounting system and internal control

We have applied our risk methodology to your audit. This approach allows us to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

We have previously documented our findings at the interim stage with regard to key internal controls, and those findings are not duplicated here.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you. See 'The small print' for further details of our approach.

Key to assessment of internal control deficiencies

● (red)	Material weakness - risk of material misstatement
● (yellow)	Significant deficiency - risk of significant misstatement
● (green)	Deficiency - risk of inconsequential misstatement

	Assessment	Issue and risk	Recommendation
1	● (yellow)	**Bank reconciliations** Deposit account bank reconciliations were not prepared on a monthly basis throughout 2010-11 or for the first quarter of 2011-12. The 2010-11 reconciliation was only prepared when requested by the audit team during fieldwork.	The Council should review the processes for completing the reconciliation of the deposit bank accounts, including: • ensuring all bank accounts are reconciled on a monthly basis • all bank account reconciliations have an identified preparer and reviewer • reconciliations are performed in a timely basis to ensure any errors or inappropriate transactions are identified. **Management response:** We accept this issue and will ensure that the Deposit Bank Accounts are reconciled and reviewed monthly. To be actioned immediately.

	Assessment	Issue and risk	Recommendation
2	●	**Council tax/NDR and Income Bank Account Reconciliations** We noted the following issues: • The council tax and non-domestic rates bank reconciliation did not agree to the ledger as at 31 March 2011. There was a difference of £38,000 relating to cash posted to the ledger on 1 April 2011 which was received on 31 March 2011. The difference was not material to the financial statements. • The income account bank reconciliation did not agree to the ledger as at 31 March 2011. A net adjustment of £159,000 was made to the bank reconciliation and to the general ledger to decrease the adjusted bank balance. This was to reflect the impact of items that cleared the bank on 31 March 2011 but were not posted to the general ledger until after the year end. The gross effect on the accounts was an increase in income of £3.7 million and in expenditure of £3.6 million. The Council did post the corrections, but the bank reconciliation had not been updated and did not reflect the actual ledger balances. In the cases above the differences were either not material or the differences were subsequently posted but not updated on the bank reconciliation. However, there remains a risk of misstatement if the bank reconciliation is not performed against the final ledger balance for the relevant period/year end.	For the reconciliations of these bank accounts, the Council should ensure that these are performed from the bank balance to the final period or year end ledger balance to ensure all postings are correctly identified and posted in a timely manner. **Management response:** At the moment our view is we do not recognise this as a medium risk. We accept there are areas of presentation that could be improved but these are minor and there are no substantive issues with the underlying bank reconciliation. Both these bank reconciliations were done promptly within a few days of the year end. The reconciling items were noted on them and the subsequent journals were processed. The only thing that was not done at the time was to re-do the bank reconciliations after the journals had been posted to the final closing ledger balances. This has now been done. The bank reconciliations at the time were signed off on the basis that the journals had been prepared and were being posted
3	●	**Bad debt review procedures** The bad debt provision methodology for sundry debtors has not been reviewed for some time. The methodology should be regularly reviewed to ensure general provision levels are appropriate, based on historical trends of debt defaults.	Management should review the methodology for providing for sundry debtors to ensure that the level of provision is appropriate for the likelihood of recoverability of significantly aged debts.

	Assessment	Issue and risk	Recommendation
		At the audit date there was £97,000 of debtors from the old system which were at least two years old at the year-end. Following our audit, these have now been provided for. A further £159,000 of debtors from the new system that were at least one year old at the year-end have not been received or provided for.	**Management response:** The old system debts over one year have now been fully provided for. New system debt aged over 12 months at year end amounted to £409,092 and had a provision of £226,986 leaving a net debt of £182,106 of which we have already recovered £51,471 in 5 months. This rate of recovery suggests we could receive all of this within 18 months or so, so this level of provision seems reasonable. We review the level of the provision each year to ensure that it remains appropriate, and we also write off old unrecoverable debts on a regular basis.

A The small print

Purpose of memorandum

This Report has been prepared for the benefit of discussions between Grant Thornton and the Audit Committee of Argyll and Bute Council.

The purpose of this memorandum is to highlight the key issues affecting the results of the Group and the preparation of the Council's financial statements for the year ending 31 March 1.

This document is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We would point out that the matters dealt with in this report came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements of the Council.

Responsibilities of the Council and auditors

The Council is responsible for the preparation of the financial statements and for making available to us all of the information and explanations we consider necessary. Therefore, it is essential that the council confirm that our understanding of all the matters in this memorandum is appropriate, having regard to their knowledge of the particular circumstances.

Clarification of roles and responsibilities with respect to internal controls

The Council is responsible for the identification, assessment, management and monitoring of risk, for developing, operating and monitoring the system of internal control and for providing assurance to the Audit Committee that it has done so.

The Audit Committee is required to review the Council's internal financial controls. In addition, the Audit Committee is required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk.

The Audit Committee should receive reports from management as to the effectiveness of the systems they have established as well as the conclusions of any testing conducted by internal audit or ourselves.

The Audit Committee are required to review the Council's internal financial controls. In addition, the Audit Committee is required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk.

The Audit Committee should receive reports from management as to the effectiveness of the systems they have established as well as the conclusions of any testing conducted by internal audit or ourselves.

We have applied our audit approach to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you.

In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify.

We would be pleased to discuss any further work in this regard with the Audit Committee.

Independence and robustness

Ethical standards require us to give you full and fair disclosure of matters relating to our independence.

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opnion on the financial statements.

In accordance with best practice, we analyse our fees below:

	£
Grant Thornton	205,000
Audit Scotland fixed charge	81,500
Total audit	286,500

Our Fee includes VAT and all travel and subsistence

ISAUK 260 requires communication of:

- relationships that have a bearing on the independence of the audit firm and the integrity and objectivity of the engagement team
- nature and scope of the audit work
- the form of reports expected