

# Argyll and Bute Council

## Report to those charged with governance on the 2011/12 audit



Prepared for the members of Argyll and Bute Council  
September 2012

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. It provides services to the Auditor General for Scotland and the Accounts Commission. Together they ensure that the Scottish Government and public sector bodies in Scotland are held to account for the proper, efficient and effective use of public funds.

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# Summary

## Introduction

1. International Standard on Auditing (ISA) 260 requires auditors to report certain matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action.
2. ISA 260 requires us to highlight:
  - relationships that may bear on our independence and the integrity and objectivity of the appointed auditor and audit staff
  - the overall scope and approach to the audit, including any expected limitations, or additional requirements
  - expected modifications to the audit report
  - management representations requested by us
  - unadjusted misstatements, other than those that are clearly trivial
  - material weaknesses in internal control identified during the audit
  - qualitative aspects of accounting practice and financial reporting, including accounting policies
  - matters specifically required by other auditing standards to be communicated to those charged with governance and any other matters that are relevant to the audit.
3. This report sets out for the Audit Committee's consideration the matters arising from the audit of the financial statements for 2011/12 that require reporting under ISA 260. We are drawing to your attention those matters we think are worthy of note, so that you can consider them before the financial statements are approved and certified. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. This report has been prepared for the use of Argyll and Bute Council and no responsibility to any third party is accepted.

## Status of the Audit

4. Our work on the financial statements is now substantially complete. The issues arising from the audit were included in a matters arising schedule issued to the Finance Manager - Corporate Support over the course of the audit. This schedule was finalised and agreed on the 27 August 2012. The more significant issues arising were discussed with the Head of Strategic Finance at a meeting on 10 September 2012.

## Matters to be reported to those charged with governance

### Conduct and scope of the audit

5. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Audit Plan presented to the Audit Committee on 16 March 2012, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.

### Audit opinion & representations

6. Subject to the satisfactory conclusion of any outstanding matters and receipt of a revised set of accounts for final review, we anticipate being able to issue an unqualified auditor's report on 21 September 2012. (The proposed report is attached at [Appendix A](#)). There are no anticipated modifications to the audit report.
7. Several errors were identified during the audit, where if adjustments were made these would have a net effect of reducing the net assets on the balance sheet by £0.102 million and reducing the surplus on provision of services by the same amount, with a corresponding impact on the general fund balance. Officers in finance propose not to adjust the accounts for these errors and we concur on this. The effect of these unadjusted errors is detailed in [Appendix B](#).
8. In addition, there were a few presentational adjustments required to the unaudited accounts that the council have now amended. These were mainly minor adjustments that form part of the normal audit process. The most significant of the changes was to amend the remuneration report to include the total cost to the council of added years pension costs relating to non-teaching staff retiring early in 2011/12. This is now reflected in the updated financial statements.
9. As part of the completion of our audit we seek written assurances from the Accountable Officer on aspects of the accounts and judgements and estimates made. A draft letter of representation under ISA 580 will be provided to the Accountable Officer on receipt of a final agreed set of accounts. This should be signed and returned by the Accountable Officer with the signed accounts prior to the independent auditor's opinion being certified.
10. ISA600 'Using the work of another auditor' requires us to consider a number of matters relating to the audit of group entities included within the financial statements of the council. As part of this process we obtain confirmation of the audit opinion for all associates within the council's Group. We are currently awaiting assurances regarding the audited accounts for these entities.

### Accounting and internal control systems

11. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the accounts.

## Matters arising

12. In our view, the following matters require to be brought to your attention regarding the appropriateness of accounting policies or accounting estimates and judgements, the timing of transactions, the existence of material unusual transactions or the potential effect on the financial statements of any uncertainties.
13. **Refuse Disposal Sites:** Valuations provided after the accounts had been prepared in respect of three landfill sites on Mull, Islay and Tiree included significant liabilities for future expenditure on restoration and aftercare, resulting in negative asset valuations for two of the three sites. Following discussion with officers and consideration of accounting guidance in this area, it was agreed that the sites should be impaired to the land and buildings asset values provided by the Valuation Office Agency. With regard to estimated future expenditure for restoration and aftercare, we agreed that the treatment will be kept under review going forward.

**Resolution:** The impairments are now reflected in the updated financial statements.

14. **Equal Pay Provision:** The Equal Pay Act 1970 makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work, work rated as equivalent, or work of equal value. Employees who consider that they have been discriminated against in terms of pay can put forward claims to an employment tribunal. The ultimate cost to the council remains uncertain and it is likely that resolution of the issue will take some time. As the tribunal process unfolds the extent of the council's eventual liability will become clearer. The council's equal pay provision at 31 March 2012 of £0.191million is based on full provision for all known claims against the council. The council have disclosed a contingent liability for any additional future claims that may potentially arise.

**Resolution:** The equal pay provision will be reviewed on an annual basis.

15. **Reduction in net assets - due to changes in assumptions about Employee Benefits - Pension fund liabilities:** The net assets on the council's balance sheet have decreased from £212.980 million in 2010/11 to £180.177 million in 2011/12, a reduction of £32.803 million. The principal reason for this decrease is due to the £52.865 million increase in the pension liability from £26.227 million to £79.092 million. This is also reflected in the balance sheet for the group. The pension liability represents the difference between the expected future payments to be made to former employees of the council and their spouse in the form of pension payments and the underlying value of pension fund assets to meet this cost. The calculation of the liability is assessed by professional actuaries each year and is an estimated figure.
16. The large increase in the pension liability in 2011/12 is due to financial assumptions about the cost of pension payments being less favourable at March 2012 than they were at March 2011 which has the effect of increasing the overall cost of pensions. In addition, the level of assumptions applied by the Actuary to the expected return on pension fund assets was more

favourable than actual returns in most cases. Both these factors have contributed to the increase in the net liability faced by the council.

**Resolution:** Assurance is obtained from the triennial valuations of the pension fund carried out by Strathclyde Pension Fund, which assures that the pension fund remains adequately funded. The financial statements have been prepared on the basis of these assumptions.

17. **Trade Receivables:** In their report on the 2010/11 Audit, the auditors recommended that the bad debt provision (BDP) methodology should be reviewed on an annual basis, including a review of significant individual debtors for impairment. Our follow-up review identified
- That for 2011/12 there was a specific write off of bad debt of £305,000
  - All debt on the “old” debtors system has a full 100% BDP
  - The BDP for debt over one year old varies from 55% (12-24 months) to 70% (24 to 36 months) and 80% to 100% (36 to 60 months) and these are the same percentages applied in 2010/11.
  - Currently there are debtor balances of £159,390 over 12 months old that have not been fully provided for.
18. Our experience of the level of BDP in other councils suggests the percentage provisions for bad debt are lower than other councils. Taking all of this into account there is a risk that the BDP is understated but not by a material amount.

**Resolution:** The basis of calculating the BDP will be reviewed annually.

19. **Trade Payables:** Trade payables included within the financial statements include £214,083 relating to capital creditors brought forward from previous years and for which no supporting documentation is available. Following discussion with officers, we are advised that these brought forward creditors relate primarily to retentions for work carried out. We have also established that all capital creditors raised in 2011/12 can be agreed to listings of individual projects which split the amounts between retentions, fees and final payments. We are however unable to confirm that the brought forward capital creditors are valid entries in the financial statements and £214,083 has been included in the total of Unadjusted Errors at Appendix B.

**Resolution:** For 2012/13 the capital creditors balance brought forward will be reviewed at an early date.

## Acknowledgements

20. We would like to express our thanks to the staff of Argyll and Bute Council for their help and assistance during the audit of this year’s financial statements which has enabled us to provide an audit report within the agreed timetable.

# APPENDIX A: Proposed Independent Auditor's Report

## **Independent auditor's report to the members of Argyll and Bute Council and the Accounts Commission for Scotland**

I certify that I have audited the financial statements of Argyll and Bute Council and its group for the year ended 31 March 2012 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the group and authority-only Statements of Movement in Reserves, Statements of Comprehensive Income and Expenditure, and Balance Sheets, the Cash-Flow Statement, the Council Tax Income Account, the Non Domestic Rate Income Account, the Common Good Funds, the Trust Funds and Other Third Party Funds and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2011/12 (the 2011/12 Code).

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Accounts Commission for Scotland, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

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

As explained more fully in the Statement of Responsibilities, the Head of Strategic Finance is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the group's and the body's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Head of Strategic Finance; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the statement of accounts to identify material inconsistencies with the audited financial statements. If I become



aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

### **Opinion on financial statements**

In my opinion the financial statements:

- give a true and fair view in accordance with applicable law and the 2011/12 Code of the state of the affairs of the group and of the body as at 31 March 2012 and of the income and expenditure of the group and the body for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2011/12 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973 and the Local Government in Scotland Act 2003.

### **Opinion on other prescribed matters**

In my opinion:

- the part of the Remuneration Report to be audited has been properly prepared in accordance with The Local Authority Accounts (Scotland) Regulations 1985; and
- the information given in the Explanatory Foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which I am required to report by exception**

I am required to report to you if, in my opinion:

- adequate accounting records have not been kept; or
- the financial statements and the part of the Remuneration Report to be audited are not in agreement with the accounting records; or
- I have not received all the information and explanations I require for my audit; or
- the Statement of Governance and Internal Control does not comply with Delivering Good Governance in Local Government; or
- there has been a failure to achieve a prescribed financial objective.

I have nothing to report in respect of these matters.

Fiona Mitchell-Knight FCA  
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21 September 2012

# Appendix B

## Non-Adjusted Errors within the 2011/12 Annual Accounts

Below is a summary of the non-adjusted errors which have not been processed in the 2011/12 Annual Accounts.

Narrative	DR £000	CR £000
<b>Income &amp; Expenditure Account/General Fund Balance</b>		
Debtors invoice not accrued		8
Common Good/Trusts understated	101	
Imprest balance overstated	9	
<b>Balance Sheet</b>		
Capital Creditors overstated	214	
Fixed assets (PPE) overstated		214
Debtors invoice not accrued	8	
Common Good/Trusts understated		101
Imprest balance overstated		9
<b>Totals</b>	<b>332</b>	<b>332</b>