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**Audit Committee – 25th September 2008**

**Report of the Director of Finance**

**Auditor's Annual Governance Report 2007/08**

**Purpose of Report**

1. To present the auditor's Annual Governance Report to the Audit Committee for consideration and approval, and to invite the Audit Committee to approve the formal Management Representation Letter to the Auditor.

**Background**

2. The Audit Commission's Code of Audit Practice 2005 requires external auditors to report to those charged with governance on the results of their work. The Council has delegated the responsibility for the approval of the Statement of Accounts, and all audit matters, to the Audit Committee.
3. The Accounts and Audit Regulations 2003 (as amended) formalised the responsibility of members of local authorities for the adequacy of financial management.
4. Towards the end of each audit of the annual accounts, the Director of Finance provides a management representation letter (sometimes known as a letter of comfort), confirming the completeness and reliability of the information and records supplied to the auditors. The Audit Commission have requested that this letter should also be signed by the Chairman of this meeting, to evidence members' acknowledgment of responsibility for financial management. A copy of this letter is attached to the Annual Governance Report.

**Annual Governance Report 2007**

5. The Report is attached, and will be presented by the District Auditor, Mr. Tony Corcoran. It includes findings from the audit of the 2007/08 accounts, and opinions on the Council's arrangements for securing value for money.

**Finance**

6. This report refers to various aspects of financial management, but does not give rise to any direct costs.

## **Law**

7. Legislation appertaining to Local Authority Audit and Accounts is contained in the Local Government Act 1972, part 2 of the Audit Commission Act, 1998, and regulations made thereunder.

## **Equality Impact**

8. The proposal takes account of the Council's policy in relation to equal opportunities.
9. With regard to children and young people:
- There is no direct effect of the proposals on children and young people.
  - There has been no specific consultation with children and young people.
  - There has been no direct involvement of children and young people in developing the proposals.

## **Recommendation**

10. It is recommended that:-
- the Committee considers the Annual Governance Report, and the auditor's comments.
  - the Committee approves the Letter of Representation.
  - the Chairman of the Committee signs and dates the Letter of Representation to give evidence of the approval above.



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**Mike Williams**  
**Director of Finance**

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# Annual Governance Report

Dudley MBC

Audit 2007/08

Date **25 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, which are substantially complete. It identifies the key issues that you should consider before we issue our opinion, conclusion and certificate.
- 2 This report includes only 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 During the audit, management agreed to a number of adjustments to the financial statements submitted for audit. Most of these adjustments are in respect of disclosures made in the notes to the accounts. The most significant adjustments are in respect of fixed assets and deferred capital grants. These adjustments do not have any effect on the deficit reported in the Income and Expenditure Account or the revenue reserves available to the Council.

## Value for Money

- 4 We are required to conclude whether the Council put in place adequate corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. We assess your arrangements against twelve criteria specified by the Commission. We have assessed the arrangements of the Council as adequate in all twelve areas and we therefore propose to issue an unqualified conclusion.

## Next steps

- 5 We ask the Audit Committee to:
  - consider the matters raised in the report before approving the financial statements;
  - 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

- 6 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.
- 7 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.
- 8 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

- 9 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
Accounting for equal pay settlements	The entries in the financial statements in respect of equal pay settlements are fairly stated
The 2007 SORP includes a number of changes to accounting requirements such as changes in accounting for financial instruments and the introduction of the revaluation reserve	The entries in the financial statements in respect of financial instruments and the revaluation reserve are fairly stated

## Draft representation letter

- 10 Before we issue our opinion, auditing standards require us to obtain from you and management, written representations that:

## Financial statements and Annual Governance Statement

- 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.

11 Appendix 1 contains the draft of the letter of representation we seek from you.

### Accounting policies and financial reporting

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

### Adjustments to the financial statements

13 We identified adjustments that needed to be made to the financial statements (other than those of a trivial nature) and reported these to management. Management has agreed to adjust the financial statements for the items identified in Appendix 3. However, because of the value and nature of the adjustments, we are reporting these to you.

**The audit report**

14 We plan to issue an unmodified report including an unqualified opinion on the financial statements. Appendix 2 contains a copy of our draft report.

**Material weaknesses in internal control**

- 15 We have not identified any weakness in the design or operation of an internal control that might result in a material error in your financial statements of which you are not aware. However, you should be aware that section 5 of the Council's Annual Governance Statement reports that there has been unbudgeted expenditure on the Leaps and Bounds Project, the reasons for which are currently being reviewed.
- 16 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**

17 We have identified the following matters that we require you to consider.

**Table 2 Other matters**

Issue	Finding
Financial reporting	Financial Management Outturn Reports are prepared at Directorate level and are published in the Council's 'Quarterly Corporate Performance Monitoring Report'. These reports disclose the projected year end net expenditure but do not report actual expenditure as at the end of the financial period which is being reported on. In addition, these reports disclose only the projected net expenditure and not the Council's projected gross income and expenditure. The quality of the Council's financial reporting could be enhanced if this additional information was disclosed.
Fixed asset records	Two adjustments to the financial statements in respect of fixed assets are reported in Appendix 3. These issues came to light on the transition to more complex rules for accounting for fixed assets in 2007/08. They do not have any effect on the deficit reported in the Income and Expenditure Account or the revenue reserves available



## Financial statements and Annual Governance Statement

Issue	Finding
	to the Council. We recommend that the Council's officers review the level of record keeping for fixed assets and consider the option of acquiring and implementing specialised fixed assets IT software to address the complexity of the new rules.

<b>Recommendations</b>	
<b>R1</b>	Financial Management Outturn Reports, as published in the Council's 'Quarterly Corporate Performance Monitoring Report', should report: <ul style="list-style-type: none"><li data-bbox="218 754 1399 822">• actual gross income and expenditure as at the end of the financial period which is being reported on</li><li data-bbox="218 844 984 878">• projected year end gross income and expenditure.</li></ul>
<b>R2</b>	The acquisition and implementation of specialised fixed assets IT software should be considered

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# Value for money

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

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# Formal audit powers

20 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.

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

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# Independence

- 22** 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.
- 23** We confirm that we comply with the APB's Ethical Standards, that we are independent and that our objectivity is not compromised.
- 24** 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

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

## Audit fees

- 26** 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	191,083	191,083
Value for Money	89,216	89,216
National Fraud Initiative	1,200	1,200
<b>Total Audit Fees</b>	<b>281,499</b>	<b>281,499</b>

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

## Our arrangements to ensure independence and objectivity

- 28** We have comprehensive procedures to ensure independence and objectivity. These are outlined in Table 6.

**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>

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# Appendix 1 – Letter of representation

To:

Tony Corcoran  
District Auditor  
Audit Commission  
Ground Floor, Suite 1,  
Observer House  
Horsefair,  
Abbey Forgate  
Shrewsbury,  
SY2 6BL

## **Dudley MBC - 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 Dudley MBC, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2008. All representations cover the Council's accounts included within the financial statements.

## **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 relevant Council 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:

## Appendix 1 – Letter of representation

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

### 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. Except as disclosed in Note 28 to the financial statements we have no other lines of 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;
- 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 Audit Committee, no additional significant post balance sheet events 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.

Signed on behalf of Dudley MBC

I confirm that the this letter has been discussed and agreed by the Audit Committee on 25 September 2008

Signed

Mike Williams  
Director of Finance  
25 September 2008

Councillor Alan Taylor  
Chair of the Audit Committee  
25 September 2008



# Appendix 2 – Independent auditor's report to the Members of Dudley Metropolitan Borough Council

## Opinion on the financial statements

I have audited the Authority accounting statements and related notes of Dudley Metropolitan Borough Council for the year ended 31 March 2008 under the Audit Commission Act 1998. The Authority accounting statements comprise the 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 Housing Revenue Account, 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 Dudley Metropolitan 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 Director of Finance and auditor

The Director 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 by the Director of Finance and the Summary of the 2007/08 Financial Year. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies 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.

### **Opinion**

In my opinion:

The Authority 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; and

### **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

## Appendix 2 – Independent auditor's report to the Members of Dudley Metropolitan Borough Council

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, Dudley Metropolitan Borough Council made proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2008.

### 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 2007/08 on 14 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.

### 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.

Tony Corcoran  
District Auditor  
Audit Commission  
Ground Floor, Suite 1,  
Observer House  
Horsefair,  
Abbey Forge  
Shrewsbury,  
SY2 6BL

X September 2008

# Appendix 3 – Adjustments made to the financial statements

**Table 5 Adjustments made to the financial statements**

This table lists the most significant adjustments made to the financial statements during the audit

Items of account	Adjustment required
Fixed assets (note 17 to the core statements)	The gross book value of fixed assets at 1 April 2007 has been reduced by £7.9m from £1,671.4m to £1,663.5m. There is no effect on the net book value of these assets as accumulated depreciation has also been reduced by £7.9m This adjustment was made because the Council was unable to reconcile its detailed asset records to the gross book value of assets brought forward from the previous set of financial statements. The adjustment ensures that the gross book value in the financial statements now agrees to the Council's detailed asset records. This adjustment does not have any effect on the deficit reported in the Income and Expenditure Account or the revenue reserves available to the Council. We have recommended earlier in this report that the Council's officers review the record keeping for fixed assets, potentially by the acquisition and implementation of specialised fixed assets IT software
Grants deferred account	This account holds various capital grants which are written off to revenue over the life of the relevant assets. The value of these grants has been reduced by £28.1m from £139.9m to £111.8m. This resulted from an exercise by officers to assess whether the Council could readily identify the assets to which the grants relate. The reduction of £28.1m is in respect of grants deferred balances for which the Council not readily identify the relevant asset. This

### Appendix 3 – Adjustments made to the financial statements

Items of account	Adjustment required
	adjustment does not have any effect on the deficit reported in the Income and Expenditure Account or the revenue reserves available to the Council. We have recommended earlier in this report that the Council's officers review the record keeping for fixed assets, potentially by the acquisition and implementation of specialised fixed assets IT software

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# Appendix 4 – Action Plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
7	R1 Financial Management Outturn Reports, as published in the Council's 'Quarterly Corporate Performance Monitoring Report', should report: <ul style="list-style-type: none"> <li>• actual gross income and expenditure as at the end of the financial period which is being reported on</li> <li>• projected year end gross income and expenditure.</li> </ul>	3				
7	R2 The acquisition and implementation of specialised fixed assets IT software should be considered	3				