Falkirk Council

Report to those charged with governance on the 2009/10 audit

September 2010

AUDIT SCOTLAND

Contents

Key Issues

Introduction

1. International Standard on Auditing 260 (ISA 260) requires auditors to communicate matters relating to the audit of the financial statements to those charged with governance of a body in 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 audit engagement lead and audit staff
   - the overall scope and approach to the audit, including any expected limitations, and the form of reports expected to be made
   - expected modifications to the audit report
   - management representations requested by us
   - unadjusted misstatements
   - material weaknesses in internal control identified during the audit
   - views about the qualitative aspects of accounting practices and financial reporting, including accounting policies
   - matters specifically required by other auditing standards to be communicated and any other matters that are relevant to the audit.

3. This report sets out for the Council's consideration the relevant matters arising from the audit of Falkirk Council financial statements for 2009/10 that require reporting under ISA 260. The contents should be brought to the attention of the Director of Finance, Chief Executive and Leader so that they can consider them before they sign the relevant pages of the financial statements. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. The report has been prepared for the use of Falkirk Council and no responsibility to any third party is accepted.

Status of the audit

4. Our work on the financial statements is now complete and the matters identified during the audit have been discussed with the Director of Finance.

Matters to be reported to those charged with governance

Conduct and scope of the audit

5. Information on the integrity and objectivity of the audit engagement lead and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan submitted to management in March 2010 and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in March 2007.

Audit opinion & representations

6. Our anticipated auditor's report (appendix A) is unqualified.

7. The financial statements have not been adjusted to correct five financial misstatements as detailed in appendix B. The net impact of these is to increase the deficit on the income and expenditure account by £3.767 million and to decrease the general fund and the net assets in the balance sheet by the same amount and to increase the pension fund net assets by £0.41 million. The impact of these misstatements is not material, individually or in aggregate, to the financial statements.

8. As part of the completion of our audit we seek written assurances from the Director of Finance on aspects of the accounts and judgements and estimates made. We have received the formal representations from the Director of Finance that we require.

Accounting and internal control systems

9. 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

10. In our view, the following issues require to be brought to your attention regarding the appropriateness of the council's accounting policies or accounting estimates and judgements, the timing of transactions, the existence of any material unusual transactions or the potential effect on the financial statements of any uncertainties:

11. **Equal pay compensation costs**: We have requested and received a specific representation from the Director of Finance that actual and potential claims in relation to equal pay legislation have been reviewed and the amount recognised as a provision (£5.0 million) is the best estimate of the expenditure likely to be required to settle the present obligation at the balance sheet date. A contingent liability is also disclosed in the accounts, highlighting that recent legal judgements may mean that the council is at risk in respect of further categories of claims. The Council has further disclosed that it has applied for and received borrowing consent in relation to equal pay costs under the terms of Finance Circular No. 11/2009.

12. Having considered the requirements of the SORP and FRS 12, reviewed the details reported by the Directors of Finance and Corporate & Neighbourhood Services to the council in June 2010 and considered the terms of related borrowing consent, our view is that the council should provide for a additional £3.4 million of expenditure in 2009/10 in relation to equal pay costs.

13. The Director of Finance has disagreed with this, taking the view that recognising the expenditure without matching it to the corresponding funding through application of borrowing under consent would understate the general fund. While we understand the argument presented, we do not agree with this view given the accounting rules that apply.

14. While there remain uncertainties over the actual costs that will be incurred, we are satisfied that in all other respects the council's approach is reasonable. We have also agreed with the Director of Finance that it is not appropriate to recognise funding until the point that the borrowing under the consent is made.

15. The disputed amount is not considered material to our opinion on the audit, but we consider that the disagreement on accounting approach is significant enough to be highlighted in this report. The amount involved is included in the overall unadjusted financial misstatements summarised in paragraph 7.

***Resolution*:** The accounts have not been amended, but this is not considered material for our audit opinion. The circumstances and nature of the disagreement will be highlighted in the annual report to members and the controller of audit.

16. **Non-depreciation of council house dwellings**: the Council has not charged depreciation on its council housing stock on the grounds that the amount involved would not be material. We have requested and received a specific representation from the Director of Finance that in his view this treatment is appropriate on the grounds that the impact of depreciation would not be material. We are satisfied that the approach adopted does not have a material impact on the accounts.

***Resolution*:** No depreciation has been charged on council dwellings and we have accepted the Director of Finance's representation that depreciation of these assets is not material in 2009/10.

17. **Going Concern (Group Accounts)**: The Group Balance Sheet at 31 March 2010 has an excess of liabilities over assets of £166.198 million due to the accrual of FRS17 pension liabilities in accordance with Financial Reporting Standard 17 (retirement benefits). The Group net worth reflects both the FRS 17 liability for the council and for the unfunded pension schemes in its associate bodies, Central Scotland Joint Police Board and Central Scotland Fire & Rescue Joint Board. The Council and its group have adopted a 'going concern' basis for the preparation of the financial statements as future actuarial valuations of the pension fund will consider the appropriate employer's rate to meet the funds' commitments.

***Resolution*:** We are satisfied that the process which the Council and its group has undertaken to consider the group's ability to continue as a going concern is reasonable.

Acknowledgements

18. We would like to express our thanks to the staff of Falkirk Council for their help and assistance during the audit of this year's Accounts which has enabled the appointed auditor to certify the Accounts by the Controller of Audit's target date.

AUDIT SCOTLAND

September 2010

Appendix A

Proposed Independent Auditor's Report

Independent auditor's report to the members of Falkirk Council and the Accounts Commission for Scotland

I certify that I have audited the financial statements of Falkirk Council for the year ended 31 March 2010 under Part VII of the Local Government (Scotland) Act 1973. The financial statements comprise the Income and Expenditure Account, Statement of Movement on the General Fund Balance, Statement of Total Recognised Gains and Losses, Balance Sheet and Cash Flow Statement, the Housing Revenue Account Income and Expenditure Account, Statement of Movement on the Housing Revenue Account Balance, the Council Tax Income Account, the Non-Domestic Rate Income Account, Common Good Funds Account, Pension Fund Accounts and the related notes and the Statement of Accounting Policies together with the Group Accounts. These financial statements have been prepared under the accounting policies set out within them.

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 123 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 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 Code of Practice on Local Authority Accounting in the United Kingdom 2009 - A Statement of Recommended Practice (the 2009 SORP) 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) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland.

I report my opinion as to whether the financial statements give a true and fair view, in accordance with relevant legal and regulatory requirements and the 2009 SORP, and have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

In addition, I report to you if, in my opinion, the Council has not kept proper accounting records, or if I have not received all the information and explanations I require for my audit.

I review whether the Annual Governance Statement reflects compliance with the SORP, and I report if, in my opinion, it does not. I am not required to consider whether this statement covers all risk and controls, or form an opinion on the effectiveness of the local government body's corporate governance procedures or its risk and control procedures.

I read the other information published with the financial statements, and consider whether it is consistent with the audited financial statements. This other information comprises the Introduction to the Accounts and the Foreword by the Director of Finance. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

Basis of audit opinion

I conducted my audit in accordance with Part VII of the Local Government (Scotland) Act 1973 and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board as required by the Code of Audit Practice approved by the Accounts Commission. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Director of Finance in the preparation of the financial statements, and of whether the accounting policies are most appropriate to the Falkirk Council and its group'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 financial statements 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 financial statements.

Opinion

In my opinion the financial statements

- give a true and fair view, in accordance with relevant legal and regulatory requirements and the 2009 SORP, of the financial position of Falkirk Council and its group as at 31 March 2010 and the income and expenditure of Falkirk Council and its group for the year then ended; and

- have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

Mark Taylor CPFA, Assistant Director
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Osborne House, 1/5 Osborne Terrace
Edinburgh, EH12 5HG

30 September 2010

Appendix B

Non-Adjusted Errors within the 2009/10 Annual Accounts

Below is a summary of the non-adjusted errors which have not been processed in the accounts, with an explanation of their impact on the general fund, balance sheet and pension fund accounts:

General Fund and Balance Sheet errors	**General Fund/ I&E**		**Balance Sheet**	
	Dr	**Cr**	**Dr**	**Cr**
	£000	**£000**	**£000**	**£000**
General Fund	605			
Creditors *Under accrual in respect of 2009/10 payroll costs.*				605
Debtors			238	
General Fund		238		
HSG income for 2007/08 not received until after 2009/10 but not accrued.				
General Fund: Non-Distributed Costs	29			
General Fund: Net Cost of Services		29		
Depreciation on surplus assets charged to Community Services instead of Non-Distributed Costs.				
General Fund	3,400			
Provisions *Insufficient provision made for equal pay liabilities.*				3,400
Totals	**4,034**	**267**	**238**	**4,005**
Net Total	**3,767**			**3,767**

Pension Fund Account error	**Pension Fund A/C**		**PF Net Asset Statement**	
	Dr	**Cr**	**Dr**	**Cr**
	£000	**£000**	**£000**	**£000**
Current Liabilities: Unpaid Benefits			41	
Benefits payable		41		
Benefits wrongly accrued to 2009/10 for a beneficiary who retired in 2010/11.				
Totals		**41**	**41**	
Net Total		**41**	**41**	

It can be seen that the net effect of the above transactions would be to:

- reduce the general fund balance carried forward and decrease the net worth shown in the balance sheet by £3,767(000)
- increase the closing net assets in the Pension Fund Accounts by £41 (000).