

East Ayrshire Council

Draft Report to those charged with governance on the 2008/09
audit

September 2009



 AUDIT SCOTLAND

Contents

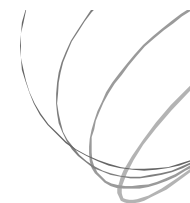
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Key Issues

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 East Ayrshire Council financial statements for 2008/09 that require reporting under ISA 260. The contents should be brought to the attention of the Leader of the Council, the Chief Executive and the Executive Head of Finance and Asset Management 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 East Ayrshire Council and no responsibility to any third party is accepted. In line with good practice, this report is also considered by the Governance and Scrutiny Committee on 25 September 2009, before the audit is concluded.



Status of the audit

4. Our work on the financial statements is now complete and matters arising during the audit have been discussed with the Executive Head of Finance and Asset Management.

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 January 2009 and follow the requirements of the Code of Audit Practice issued by Audit Scotland in March 2007.

Audit opinion & representations

6. Our anticipated auditor's report (appendix A) is unqualified.
7. The issues arising from the investigation into the operation of the Building and Works trading organisation have been well aired in previous reports to Cabinet and the Governance and Scrutiny Committee. An explanatory paragraph has been included in the independent auditor's report. This is not a qualification but draws attention to the limitation of the reliability of the evidence in support of income credited to the Building and Works trading organisation.
8. All errors identified during the audit have been corrected in the accounts and therefore there are no unadjusted misstatements to bring to your attention.
9. As part of the completion of our audit we seek written assurances from the Executive Head of Finance and Asset Management on aspects of the accounts and judgements and estimates made. A draft letter of representation under ISA 580 has been provided to the Executive Head of Finance and Asset Management. This should be signed and returned by the Executive Head of Finance and Asset Management prior to the independent auditor's opinion being certified.

Accounting and internal control systems

10. 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

11. 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:

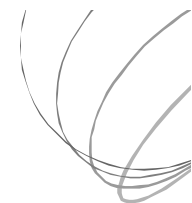
12. **Group financial statements:** In the council's the group financial statements Strathclyde Police Joint Board and Strathclyde Fire and Rescue Joint Board are consolidated as associates. An issue has arisen concerning the treatment of pension costs in the financial statements of these associates. The matter is of a technical nature concerning the proper treatment in respect of pension costs. In essence, the absence of regulations requiring the restoration of the actual charge in respect of pension schemes established after 6 April 2006 has left the associates' financial statements in breach of financial reporting standard 17 (Retirement benefits). At the time of writing the treasurers of the joint boards have declined to make the necessary adjustment and this is likely to lead to a technical qualification of the joint boards' accounts. As the council consolidate the net worth of associates there is no impact on the council's group accounts. The council have agreed to include a disclosure note within the group accounts concerning the qualification in the audit certificate of these associates.

Resolution: As the council consolidate the net worth of associates there is no impact on the council's group accounts. The matter has no impact on our opinion on the council's group accounts. The council have agreed to include a disclosure note concerning the qualification of the audit opinion on the joint boards' accounts. The Scottish Government intend to amend the relevant regulations to include the new schemes, this will be effective for 2009/10.

13. **Building and Works STO:** The report on the investigation into allegations made against the ex-Head of the Building and Works STO during 2008/09 was submitted to Cabinet and the Governance and Scrutiny Committee in June of this year. The investigation uncovered issues in relation to charging and internal controls, which in our view, limits the reliability of the evidence available to us to provide an opinion as to whether the STO has achieved its statutory financial objective.

Resolution: The inclusion of an explanatory paragraph in the independent auditor's report stating that we are unable to confirm the achievement of the statutory financial objective.

14. **Equal pay:** 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. In common



with other UK councils the ultimate cost to the council of claims in respect of equal pay remains uncertain. It is likely that resolution of the issue will take some time. The picture will become clearer as tribunal claims are decided. It is known that at least one council is seeking to reach a negotiated settlement with claimants, however, even if this is successful the outlook for East Ayrshire Council will, at least in the short term, remain uncertain. What is highly probable, based on previously decided cases and advice we have received from legal and human resource practitioners, is that East Ayrshire Council will be required to pay compensation to a proportion of claimants.

Resolution: The Executive Director of Finance and Asset Management has provided for a sum in anticipation of a proportion of the claims being successful. This estimate has been prepared using information and assessments of likely outcomes provided by the council's Legal Service and Personnel Service. In addition a note to the accounts indicates the existence of a contingent liability in the event of further claims arising.

15. **Common Good assets:** Nationally, this area continues to produce a significant amount of correspondence and complaints. In December 2007, the Local Authority (Scotland) Accounts Advisory Committee (LASAAC) issued a guidance note for practitioners. The guidance recognised the legal distinction of the common good as a separate fund, requiring separate disclosure within local authority financial statements and common good asset registers to be in place by March 2009.

Resolution: The council recognises that this issue is both live and controversial. In terms of the LASAAC action plan, the council considers itself to be making progress against the first two of the three stages, which is reviewing the arrangements in place and establishing a common good asset register. The council plans to have an asset register in place for 2009/10. The council also recognises that this may result in issues in terms of any income and expenditure in relation to assets confirmed as common good assets and is to seek further guidance on how this should be dealt with.

16. **Community assets:** A review of the assets listed as community assets on the asset register suggests that there are a number of items which could be considered, at least partially, as operational operational assets.

Resolution: The council will, for 2009/10, review the community assets category on the assets register and ensure that these are categorised in accordance with the SORP guidance notes.



17. **Icelandic banks:** In the week beginning 6 October 2008, a number of Icelandic banks went into administration. The council have three separate deposits totalling £5 million with the UK subsidiaries of two of these banks. The Local Authority Accounting Panel (LAAP) has issued advice in how to account for the loans, impairment and loss of interest in the 2008/09 accounts. The council has taken advantage of the capital finance regulations made by the Scottish Government. For 2008/09 only the loss of interest has been taken into account. Any loss of principal will be accounted for in the financial year 2010/11.

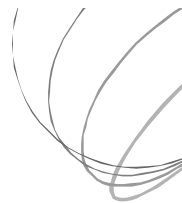
Resolution: The council have accounted for the Icelandic banks losses in accordance with LAAP guidance and regulations. No further action is required.

18. **Removal of ring fenced funding:** The introduction of the Concordat with the Scottish Government resulted in the consolidation of some specific grant funding into the revenue support grant for 2008/09. When compared to the previous year, this has the effect of giving the appearance of a substantial increase in funding from revenue support grant and service net expenditure. This change in the structure of funding has a significant impact on the comparability of income and expenditure with the previous year.

Resolution: The council have prepared the accounts in accordance with the 2008 SORP. No further action is required.

Acknowledgements

19. We would like to express our thanks to the staff of East Ayrshire Council for their assistance during the audit of this year's financial statements which has enabled the appointed auditor to certify the statements by the Controller of Audit's target date.



Appendix A

Proposed Independent Auditor's Report

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

I certify that I have audited the financial statements of East Ayrshire Council and its group for the year ended 31 March 2009 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 HRA Balance, the Council Tax Income Account, the Non-Domestic Rate Income Account, the Trust Fund accounts, the Common Good 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 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 Executive Director of Finance and Asset Management and auditor

The Executive Director of Finance and Asset Management'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 2008 - A Statement of Recommended Practice (the 2008 SORP) are set out in the Statement of Responsibilities for the financial statements.

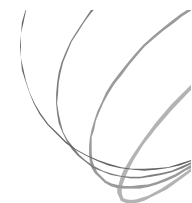
My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland) as required by the Code of Audit Practice approved by the Accounts Commission.

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 2008 SORP, of the financial position of East Ayrshire Council and its group and its income and expenditure for the year, and have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

I also report to you if, in my opinion, East Ayrshire 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 Statement on the System of Internal Financial Control 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 East Ayrshire Council'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 Explanatory Foreword by the Executive Director of Finance and Asset Management and the Corporate Governance Assurance Statement by the Leader of the Council and the Chief Executive. 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. My 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 Executive Director of Finance and Asset Management in the preparation of the financial statements, and of whether the accounting policies are most appropriate to East Ayrshire Council and its group 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 2008 SORP, of the financial position of East Ayrshire Council and its group as at 31 March 2009 and its income and expenditure for the year then ended
- have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

Failure to comply with a statutory requirement

It has not been necessary to qualify my opinion in respect of the following matter.

(FINAL WORDING TO BE AGREED)

Peter Tait CPFA
Assistant Director of Audit (Local Government)
Audit Scotland
7th Floor
Plaza Tower
East Kilbride
G74 1LW

September 2009

Appendix A

Proposed Independent Auditor's Report

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

I certify that I have audited the financial statements of East Ayrshire Council and its group for the year ended 31 March 2009 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 HRA Balance, the Council Tax Income Account, the Non-Domestic Rate Income Account, the Trust Fund accounts, the Common Good 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 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 Executive Director of Finance and Asset Management and auditor

The Executive Director of Finance and Asset Management'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 2008 - A Statement of Recommended Practice (the 2008 SORP) are set out in the Statement of Responsibilities for the financial statements.

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.

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 2008 SORP, of the financial position of East Ayrshire Council and its group and its income and expenditure for the year, and have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

I also report to you if, in my opinion, East Ayrshire 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 Statement on the System of Internal Financial Control 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 East Ayrshire Council'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 Explanatory Foreword by the Executive Director of Finance and Asset Management and the

Corporate Governance Assurance Statement by the Leader of the Council and the Chief Executive. 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. My 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 Executive Director of Finance and Asset Management in the preparation of the financial statements, and of whether the accounting policies are most appropriate to East Ayrshire Council and its group 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 2008 SORP, of the financial position of East Ayrshire Council and its group as at 31 March 2009 and its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Local Government (Scotland) Act 1973.

Failure to comply with a statutory requirement

It has not been necessary to qualify my opinion in respect of the following matter.

Local authorities have a duty under section 10 of the Local Government in Scotland Act 2003 to conduct each of their significant trading operations so that income is not less than expenditure over each three year period. In respect of the Building and Works Significant Trading Operation I am unable to form an opinion on whether the financial objective been met due to the lack of reliable evidence supporting the income credited to this trading account.

Peter Tait CPFA
Assistant Director of Audit (Local Government)

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September 2009