

Annual governance report

Durham County Council

Audit 2011/12



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Key messages

This report summarises the findings from the 2011/12 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.

Financial statements

As at 18 September 2012 I expect to issue an unqualified audit opinion. My audit of Durham County Council's Annual Statement of Accounts for the year ended 31 March 2012 is nearing completion. However, there are a number of audit procedures that are not yet complete and several queries remain to be answered.

During the year the Council again faced a number of significant challenges, particular on implementing new financial systems and preparing a new single asset register. This has again stretched resources within the finance function. Despite this, the financial statements were produced on time and to a much higher standard than last year. As last year however, a full set of working papers was not available by the date agreed but were provided progressively over subsequent weeks.

My audit identified no material errors in the financial statements. There were several adjustments to disclosure notes and some significant, but immaterial, uncorrected errors which would impact on the reported outturn and reserves. This reflects the work the finance team has undertaken to improve the quality of the financial statements this year. My team will discuss with officers on completion of the audit how we can continue to improve the process next year.

Value for money (VFM)

I expect to conclude that you have made proper arrangements to secure economy, efficiency and effectiveness in your use of resources.

Overall, the Council understands the financial challenges and risks it faces and has worked hard to deliver a sustainable Medium Term Financial Plan (MTFP) for 2012/13 and beyond. It is also aware of the challenges that lie ahead. It has successfully delivered planned savings and efficiencies and is aware that achieving sustainable efficiencies will become harder and require some difficult and bold decisions in the future.

Certificate

The audit certificate serves to formally close my audit. I cannot issue this until our work on Whole of Government Accounts (WGA) has been completed and I have reported to the National Audit Office (NAO). I expect to complete this work and report my findings to management by the deadline of 5 October 2012. I will then issue my certificate on the same day.

Before I give my opinion and conclusion

My report includes only matters of governance interest that have come to my attention in performing my audit. I have not designed my audit to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) - Integrity, Objectivity and Independence.

I am not aware of any relationships that may affect the independence and objectivity of the Audit Commission, the audit team or me, that I am required by auditing and ethical standards to report to you.

The Audit Commission's Audit Practice has not undertaken any non-audit work for the Council during 2011/12.

I ask the Audit Committee to:

- take note of the adjustments to the financial statements included in this report (Appendices 2 and 3);
- approve the letter of representation (Appendix 4), on behalf of the Council before I issue my opinion and conclusion; and
- agree your response to the proposed action plan (Appendix 6).

Financial statements

The Council's financial statements and annual governance statement are important means by which the Council accounts for its stewardship of public funds. As elected Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.

Opinion on the financial statements

Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the financial statements. Table 1 summarises the outstanding areas of work. I will provide further updates on progress in each area.

Table 1: **Audit work outstanding as at 18 September 2012**

Area of work	Comments
Review of post balance sheet events.	We will undertake a final review immediately prior to giving the audit opinion.
Final review of the amended financial statements	Officers have agreed to make a number of amendments to the draft financial statements. Once made, we will review these to ensure they are in accordance with expectations. We also need to ensure that the final set of financial statements is cross checked to testing and working papers.
Letter of Representation	We need to issue this to the Council and receive signed copies back after the meeting on 27 September 2012.
Additional specific tests outstanding: ■ Complete sufficient work for opinion purposes on	This section will be updated as work is completed.

Area of work

Comments

material grant claims including Teachers Pensions (PEN05), Housing Benefits (BEN01) and Housing Subsidy (HOU01).

- Complete work on reconciliations between the General Ledger and the benefits system(s).
- Complete work on exit packages (Note 34).
- Complete work on termination benefits (Note 43.)
- Complete review of provisions (landfill) (Note 22).
- Complete our analytical review of balances.
- Complete work on the physical verification of property, plant and equipment.

Appendix 1 contains my proposed unqualified audit report. I commenced my audit on 2 July 2012 following receipt of the Council's draft financial statements by the deadline on 29 June 2012. The financial statements I received for audit were better than last year. However, working papers to support the financial statements were not available at the start of the audit. This has led to delays in completing our audit work while working papers were prepared or retrieved from officer's files.

My team held regular meetings with key officers to discuss issues which helped to raise the profile of audit queries and receive information back for audit to enable the audit to progress.

Uncorrected errors

I have detailed the errors at Appendix 2 that officers have chosen not to amend. The most significant uncorrected errors are set out in table 2.

Table 2: **Uncorrected errors**

Issue	Finding
Municipal Mutual Insurance (MMI)	MMI encountered financial difficulties some years ago and since it ceased taking in any new business it has been trying to achieve a solvent run-off. However its balance sheet as at the end of June 2011, showed a net liability of £72m, and a judgement in March 2012 by the

Supreme Court, relating to the liability for asbestos claims, increases the risk that MMI will not be able to achieve a solvent run-off. Councils, including Durham County Council, that are the 'owners' of MMI as a mutual organisation are ultimately responsible for MMI's liabilities.

The Council has explained the factors behind the accounting treatment in the Contingent Liabilities note (Note 46) in the accounts. The Corporate Director Resources has made the judgement that the information provided so far by MMI does not:

- show that the Council will be liable for additional costs; and
- enable a reliable accounting estimate of any liability to be calculated.

The Council's judgement is therefore that the £5.5m shown in the Contingent Liabilities note 46 should not be accounted for as a provision. Creating a provision would increase the cost of services in the Comprehensive Income & Expenditure Statement, and correspondingly reduce the amount available to add to earmarked reserves.

Our view is that a proportion of this £5.5m should be shown as a provision. A reliable estimate of the liability can be made based on MMI's latest accounts and the level of claims which would be subject to claw-back. For Durham that equates to between £0.55m and £1.375m (10% to 25%). Some councils have included a provision in their accounts for 2011/12, but there are different views amongst Directors of Finance and auditors about the robustness of the information available. I have no evidence to suggest that the Corporate Director Resources has not taken all relevant information into account in reaching his judgement on the accounting treatment for 2011/12. However in discharging my responsibilities for the 2011/12 audit, I need to ensure that the Council is aware that it will likely face liabilities that are not fully reflected in its 2011/12 accounts if MMI cannot achieve a solvent run-off.

Revaluations - schools

The Council had only valued half of the schools in 2011/12. Paragraph 4.1.2.35 of the Code: requires an entire class of property to be revalued if an item within that class is revalued. It allows the use of rolling basis but only if revaluations for a class of assets are completed within a short period and provided that revaluations are kept up-to-date (eg. by the use of indices). Had a full revaluation of schools been undertaken we do not believe the impact of any changes to the accounts would be material.

The Council Valuer will need to consider what is revalued in 2012/13 to avoid any problems with part valuation of schools. DCC should ensure that changes in valuations as at April and at year end (31 March) are fully considered by finance as well as estates before deciding whether to account for these in the financial statements. A full valuation of schools should be completed as at 1 April 2012.

Revaluations - Part owned assets

Our testing of revaluations included one asset which the Council does not own. It is owned by Nomad Housing and is included at 60% of its value because the Council will obtain 60% of the capital receipts should it ever be sold within 80 years. The Council has not explained at this point that this complies with the Code. The Council has a number of 'part owned' assets (total value £2.4m) and these would need to be reviewed if it is agreed that the accounting treatment is in correct. The impact if incorrect would be to remove these assets from the Council's balance sheet.

Corrected errors

The errors and disclosure errors identified during my audit and corrected by management in the revised financial statements are summarised at Appendix 3. The corrected errors have no impact on the general fund balance or earmarked reserves. Officers are due to take a full schedule of all corrected errors to the audit committee on 27 September 2012.

Significant risks and my findings

My audit plan, dated February 2012, set out the significant risks that I expected to give particular attention to as part of my audit. In addition, following the planning phase of this year's audit we identified the need to report explicitly our work on the areas where management bias could impact on the accounts. Table 3 sets out my findings in these areas:

Table 3: **Significant risks and findings**

Significant risk	Finding
CIVICA and EBS Oracle	
The Council introduced new Revenues and Benefits and	I reviewed and tested arrangements in place to ensure that closing balances had been

Significant risk	Finding
<p>Accounts receivable systems in 2011/12. Migration from the seven former district systems to CIVICA and EBS Oracle increases the risk of material errors in housing and council tax benefits, council tax and business rates and income recognition in the financial statements.</p>	<p>successfully transferred as opening balances in the new system. My testing has not identified any significant issues to bring to your attention.</p>
<p>Property, Plant and Equipment (PPE)</p> <p>The Council introduced a new Single Asset register in 2011/12. Migration from the seven former district asset registers increases the risk of material errors in the property, plant and equipment balance in the accounting statements.</p>	<p>I reviewed and tested arrangements in place to ensure that closing balances had been successfully transferred as opening balances in the new system. A complete audit trail was not readily available for all adjustments made on conversion. My testing has however not identified any significant issues to bring to your attention.</p>
<p>Schools/Academies</p> <p>The Council had 16 schools transferring to Academy status in 2011/12. The Council may materially misstate property, plant and equipment in the balance sheet.</p>	<p>I have evaluated the Council's consideration of schools and the IAS 16 recognition criteria and consistency with the accounting policy. I also tested the detailed accounting treatment of a sample of schools held on the balance sheet and a sample of schools not recognised on the balance sheet against the IAS 16 recognition criteria.</p> <p>My testing has not identified any significant issues to bring to your attention.</p>
<p>Housing Revenue Account (HRA) Reform</p> <p>The government reformed local Council housing finance by adopting a self-financing model from 1 April 2012. This was through a one-off settlement payment to central government on 28 March 2012 that impacted on the HRA debt of the Council. Because of the complexity, scale and timing of the HRA reform, there is a risk of material errors in the accounting statements.</p>	<p>I have evaluated management's oversight of HRA reforms and the transactions required by the Council. I have agreed the detail on the settlement payment to the DCLG notification.</p> <p>My testing has not identified any significant issues to bring to your attention.</p>
<p>Group Accounts</p> <p>During 2011/12 there were changes to the Council's group interests in Premier Waste. Wrong inclusion or</p>	<p>I reviewed management's assessment of the need for group accounts. Our work this year identified that there was no requirement to produce group accounts. My testing has</p>

Significant risk

omission of group accounts is a risk.

IAS19 and Pensions

The Council must include pension assets at fair value using the revaluation method as described in IAS 19. Pension assets can be subject to significant volatility and are valued each year. The disclosures in the accounting statements involve the use of the scheme Actuary, as the Council's expert, and include significant estimates.

Management bias and/or override of journal controls

In any organisation, management may be in a position to override the financial controls it has put in place. This does not imply that I suspect actual or intended manipulation but that I approach the audit with professional scepticism.

Officers do not authorise all journals. This may result in the non-detection of material errors.

Finding

not identified any significant issues to bring to your attention.

I evaluated the management controls in place to assess the reasonableness of the figures provided by the Actuary.

I assessed the controls over the estimation uncertainties.

I also agreed the pension figures from the Actuary's report to the accounting statements and checked the disclosures are consistent with requirements.

My testing has not identified any significant issues to bring to your attention.

I evaluated the design and implementation of controls to mitigate the risk of manipulation and performed procedures to satisfy myself that, taking account of materiality, no manipulation has occurred. In particular, I tested:

- material year end adjustment journals;
- recognition of income and expenditure;
- the reasonableness of estimations and liabilities; and
- the basis for capitalising expenditure.

My audit has not identified any material issues beyond those that are reflected in the proposed adjustments to the draft accounts.

Other risks and my findings

My audit plan, dated February 2012, also set out a small number of other risks that would be considered as part of this year's audit. Table 4 describes my findings in these areas:

Table 4: **Other risks and findings**

Other risk

Finding

Other risk

Finding

Revenues and Benefits Reconciliations

The Council began implementing the new revenues and benefits system (CIVICA) in 2011. Reconciliations to the general ledger and relevant sub-systems (including housing and council tax benefits, Council Tax, NNDR and Housing Rents) are key controls.

I am in the process of reviewing all revenues and benefits reconciliations.
My testing so far has not identified any significant issues to bring to your attention.

Job Evaluation and Equal Pay

The Council has set aside amounts for equal pay and job evaluation. The risk is the accounting treatment will not be correct.

I am in the process of reviewing and testing transactions for job evaluation and equal pay including any potential omissions.
My testing so far has not identified any significant issues to bring to your attention, but there are a few amendments which need to be made to the note.

Heritage Assets

New Code requirements will result in a new accounting policy and may require disclosures in the financial statements.

I reviewed the process for identifying heritage assets for completeness and performed procedures to satisfy myself that you have recognised, valued and disclosed material heritage assets in your financial statements.
My testing has not identified any significant issues to bring to your attention.

Significant weaknesses in internal control

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. My responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

I have tested the controls of the Council only to the extent necessary for me to complete my audit. I am not expressing an opinion on the overall effectiveness of internal control.

In my interim governance report to members in April 2012 I highlighted that the large number of material information systems (53) in use during 2011/12 continued to perpetuate control weaknesses during 2011/12. I also noted that officers were aware of this position and were reporting regularly to Members on progress.

My review of the material information systems again identified weaknesses in controls over journals that could lead to a material misstatement of the financial statements. During my early testing I also noted weaknesses in the testing of opening balances and weaknesses in internal controls in several systems including accounts payable, accounts receivable, council tax, NNDR, benefits and rents. I do not intend to repeat those weaknesses in this document. As a result, I have again planned a substantive testing strategy for my review of the key financial statements. Subsequent to the early testing, officers have done a considerable amount of work reconciling systems ready for year end, which we have reviewed as part of our year end work.

One weakness which I did identify during the course of the audit that is relevant to preparing the financial statements is regarding the reconciliation of asset registers to the ledger. Officers have prepared these reconciliations but only to the total Gross Book Value, Accumulated Depreciation, Accumulated Impairment and Net Book Value amounts shown in Note 12 and not to each individual amounts shown in the note. Reconciliations of all of the figures in the note should be completed and be supported by working papers. Also the asset register should be updated regularly throughout the year (including in year additions).

I have reviewed the Annual Governance Statement and can confirm that:

- it complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
- it is consistent with other information that I am aware of from my audit of the financial statements.

Other matters

I am required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Authority’s financial reporting process including the following.

- Qualitative aspects of your accounting practices, including accounting policies, accounting estimates and financial statement disclosures.
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions.
- Other audit matters of governance interest.

Table 5 sets out those matters I need to report to you.

Table 5: **Other matters**

Issue	Finding
Working papers	Working papers to support the financial statements need to improve significantly in 2012/13. A full set of working papers is not provided at the start of the audit and are often incomplete

and require further requests to officers. Although placed on a shared folder, they are not organised by relevant heading in the accounts which means that it is more difficult to find them and agree them to the accounts. On occasions, officers appear to produce working papers for audit when they should be preparing them for their own internal assurance.

The impact on the audit is that our work takes longer than it should and the number of audit queries is significantly higher than it should be which puts pressure on officers. The risk of error increases. Next year the Council needs to ensure final accounts working papers are prepared by officers as part of the closedown arrangements. There should be a clear audit trail to the figures in the statements and notes.

This process will involve considerable effort but I am confident that the number of audit queries will reduce and more importantly so will the demands on officers' time.

HRA

Officers were unable to provide a detailed breakdown of the weekly rent income figure, for the week 02/01/2012 - 08/01/2012, from the Durham City Homes rents system. This was because only one individual who is not permanently based in Durham has the appropriate knowledge to interrogate the system to provide a full breakdown of the income value selected. The request for this additional work would have incurred extra expense and a response would have taken considerable time. We have been able to obtain assurance that the value is free from material misstatement through other audit testing. However, officers should ensure that in the future they have the appropriate knowledge within the council to enable them to complete this task.

HRA Arms Length Management Organisations (ALMOs)

For the two ALMOs the monthly invoices for management fees are not split between 'Supervision and Management' and 'Repairs and Maintenance' but are billed as a single amount. This split is done for accounts purposes at the year end by finance officers. For East Durham Homes (EDH) it was based on budget amounts and for Dale and Valley Homes (DVH) on some prior year DVH management figures.

I recommend that both EDH and DVH specifically show a charge for 'Supervision and Management' and 'Repairs and Maintenance' on their periodic management fee invoices to provide a more robust method for finance officers to the classification needed for accounts.

Disclosure requirements

The Movement in Reserves Statement (MiRs) or the notes should show an analysis of the

amounts included in each line of the classification of reserves, presenting amounts held for capital purposes separately from those held for revenue purposes, and separately identifying the total reserves held by schools. The MiRs and Note 8 provides some of the required disclosures including separate disclosure on schools in Note 8. However, Note 8 did not provide prior year comparatives as required. This has since been amended.

There should also be a description of the nature and purpose of each reserve. Disclosure in Note 24 provides this information for all unusable reserves. However, neither Note 8 nor Note 23 provides this information for usable reserves. The accounts have been amended.

Whole of Government Accounts

Alongside my work on the financial statements, I also review and report to the National Audit Office on your Whole of Government Accounts return. As at 18 September 2012 I have not completed the procedures specified by the National Audit Office. I expect to complete my work and report by the 5 October 2012 deadline.

Value for money

I am required to conclude whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is the value for money conclusion.

I assess your arrangements against the two criteria specified by the Commission. In my Audit Plan I reported to you that I was not aware of any significant risks that were relevant to my conclusion. I have set out below my conclusions on the two criteria and I intend to issue an unqualified conclusion stating that the Council has proper arrangements to secure economy, efficiency and effectiveness in the use of its resources. I include my draft conclusion in Appendix 1.

Table 6: **Value for money conclusion criteria and my findings**

Criteria	Findings
<p>1. Financial resilience</p> <p>The organisation has proper arrangements in place to secure financial resilience.</p> <p>Focus for 2011/12:</p> <p>The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.</p>	<p>Criterion met.</p> <p>The Council understands the financial challenges and risks it faces and has worked hard to deliver a sustainable Medium Term Financial Plan (MTFP) for 2012/13 and beyond and is aware of the challenges ahead.</p> <p>Senior officers and members provide constructive scrutiny on financial matters and there is an effective Audit Committee in place. The Council has updated its medium term financial plan to reflect the savings required over the next four years. Senior officers receive regular finance reports that provide a clear link between budget, in-year forecasts and the year-end forecast.</p> <p>A net contribution to reserves of £12.3 million was recorded for 2011/12. As at 31 March 2012, the Council has usable reserves of £132.7million, with earmarked reserves of £100.4 million and General Fund balances of £21.9 million.</p>

Criteria	Findings
	<p>The positive financial out-turn for 2011/12 means the Council has positioned itself well for future challenges.</p> <p>In the short-term, the Council is facing existing challenges of dealing with:</p> <ul style="list-style-type: none"> ■ changes to welfare reform; ■ business rates localisation; ■ new public health responsibilities from April 2013; and ■ the further savings and efficiencies required along with any agreed tri-borough collaboration arrangements. <p>Members and officers recognise the need to continue to work together to maintain momentum on achieving the wider-reaching changes needed to address the required efficiency savings.</p>
<p>2. Securing economy efficiency and effectiveness</p> <p>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p> <p>Focus for 2011/12:</p> <p>The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.</p>	<p>Criterion met.</p> <p>The Council has put proper arrangements in place to challenge how it secures economy, efficiency and effectiveness.</p> <p>The medium term financial plan (MTFP) covers the four year period 2012/13 to 2015/16. The main objective of the programme is to achieve budget savings of up to £79.3 million by 2015/16 while maintaining focus on its vision and priorities for the county which were developed with partners.</p> <p>The Council is continuing to ensure that sufficient capacity is provided to deliver the programme effectively. Accurately monitoring savings from these projects will continue be important if budget savings are to be achieved as planned.</p> <p>In the context of considering efficiencies, the Council remains aware that its costs are high in some areas. It is addressing this by service reviews and wider benchmarking against others. Looking ahead, the Council is aware that achieving sustainable efficiencies will become harder and require some difficult and bold decisions.</p>

Fees

I reported my planned audit fee in the 2011/12 Audit Plan (issued February 2012).

I will complete the audit within the planned fee.

Table 7: Fees

	Planned fee 2011/12 (£)	Expected fee 2011/12 (£)
Audit	555,300	555,300
Claims and returns ⁱ	90,000	90,000
Non-audit work	0	0
Total	645,000	645,000

The Audit Commission has paid a rebate of £44,424 to reflect attaining internal efficiency savings, reducing the net audit fee amount payable to the Audit Commission to £510,876.

ⁱ This represents an estimate as work on grant claims and returns will not be completed until 31 October 2012.

Appendix 1 – Draft independent auditor’s report

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF DURHAM COUNTY COUNCIL

Opinion on the Authority financial statements

I have audited the financial statements of Durham County Council for the year ended 31 March 2012 under the Audit Commission Act 1998. The financial statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement and Collection Fund and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Durham County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Corporate Director Resources and auditor

As explained more fully in the Statement of the Corporate Director Resources’ Responsibilities, the Corporate Director Resources is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, 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). 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 Authority’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Director Resources; and the overall presentation of the financial statements. In addition, I

read all the financial and non-financial information in the explanatory foreword 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 of the financial position of Durham County Council as at 31 March 2012 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

Opinion on other matters

In my opinion, 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 report by exception

I report to you if:

- in my opinion the annual governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007;
- I issue a report in the public interest under section 8 of the Audit Commission Act 1998;
- I designate under section 11 of the Audit Commission Act 1998 any recommendation as one that requires the Authority to consider it at a public meeting and to decide what action to take in response; or
- I exercise any other special powers of the auditor under the Audit Commission Act 1998.

I have nothing to report in these respects

Opinion on the pension fund financial statements

I have audited the pension fund financial statements for the year ended 31 March 2012 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Durham County Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Corporate Director Resources and auditor

As explained more fully in the Statement of the Corporate Director Resources' Responsibilities, the Corporate Director Resources is responsible for the preparation of the Authority's Statement of Accounts, which includes the pension fund financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, 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). 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 fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Director Resources; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the explanatory foreword 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 pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2012 and the amount and disposition of the fund's assets and liabilities as at 31 March 2012; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources

Respective responsibilities of the Authority and the auditor

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 to review regularly the adequacy and effectiveness of these arrangements.

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. 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.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2011, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2011, I am satisfied that, in all significant respects, Durham County Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

Delay in certification of completion of the audit

I cannot formally conclude the audit and issue an audit certificate until I have completed the work necessary to issue my assurance statement in respect of the authority's Whole of Government Accounts consolidation pack. I am satisfied that this work does not have a material effect on the financial statements or on my value for money conclusion.

Cameron Waddell
District Auditor
Nickalls House
Metro Centre
GATESHEAD
NE11 9NH
September 2012

Appendix 2 – Uncorrected errors

I identified the following errors during the audit which management have not addressed in the revised financial statements.

		Statement of comprehensive income and expenditure		Balance sheet	
Item of account	Nature of error	Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
Short term debtors	£369k Reconciling difference on the Council Tax Ratepayer Account due to system migration errors [mainly from City of Durham and some for Sedgefield - old Northgate systems]	369			369
Short term debtors	Debit balance in creditors of £547,664 and credit balances in debtors of £596,415.			596	547
Short term creditors				547	596
CIES	Courts and Probation costs incorrectly shown separately. This is historic. No requirement under SeRCOP for this to be included as a separate line.	-	-	-	-
Expenditure - Environment	Extrapolated error £5.9 million - a classification error of £2,970 Environmental Services line. Expenditure related to a Community Centre which should have been classified as Culture. Error caused by a mapping problem from	5931	5931		

		Statement of comprehensive income and expenditure		Balance sheet	
	CORAM which was not corrected during the year.				
Expenditure Central Services to public	Debt recovery costs are not recorded separately but netted off income so understating both net income and expenditure as only the net transaction is recorded. The total value of debt recovery fees during the year not recognised in the gross expenditure is £295k.	295	295		
Other Housing services	Extrapolated error £385k. A classification error of £220 was identified which relates to CCTV licence fees. Supporting People undertake all CCTV operations hence all CCTV licence fees are included in the Supporting People line. Per SeRCOP guidance CCTV expenditure relates to Community Safety and should be classified as Central Services to the Public	385	385		
Environmental services	Extrapolated error of £2.37 million. An employee tested works in Adult training and was incorrectly classified to Environmental Services for 5 months due to the restructure of the Adults section. During the year, cost centres were rationalised resulting in this individual being coded to an Environment cost centre as this is their managers cost centre.	2370	2370		
REFCUS ABFAB	Extrapolated error £584k. Environmental improvement scheme value £11.4k has not been classified correctly. Thought to be work at		584	584 PPE 584 Mirs	584 CAA

		Statement of comprehensive income and expenditure	Balance sheet
	a play area (at Hallgarth aka Whinney Hill) that was owned by a third party, but on investigation it is an asset that belongs to the Council and should have been added to the asset register.		
Provisions	Extrapolated amount. Testing of non schools and schools payments of equal pay in 2011/12 and comparing with provision made previously indicated that the provision calculation potentially understated by some £220k.	220	220
Short term creditors CIES various services	Invalid auto accruals	1900	1900

As well as the numerical errors within the primary statements highlighted above, there were a number disclosure notes which were not amended. Only the most significant ones have been summarised in the next table.

Not Amended in primary statements and disclosure notes		
Disclosure	Nature of adjustment	Amendment
Future minimum lease payments	Extrapolated error £3.55 million - several leases per the lease register testing identified that the leases had expired and should not be included in the minimum lease note. The error has been extrapolated.	Note has not been amended.

Appendix 3 – Corrected errors

I identified the following errors during the audit which management have addressed in the revised financial statements. Officers have taken a full schedule of all corrected errors to members of the audit committee on 27 September.

		Statement of comprehensive income and expenditure		Balance sheet	
Item of account	Nature of error	Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
Short term debtors Short term creditors	Debtor balance for purchasing cards £3,176k is included in "Other entities and individuals" category in short term debtors. The debtor is in effect a contra with a corresponding credit in the year end AP Ledger. Both debtors and creditors overstated.			3176	3176
Short term creditors Short term debtors	Post ledger adjustment £1,836k related to timing difference between debt income being received in ICON and the corresponding debt clearing in Oracle. The £1,836k is debtors cash and should be offset against short term debtors at the year end and not included in short term creditors.			1836	1836
Provisions creditors	The year end provision for equal pay [£16,048k] includes items that relate to amounts owing to staff and HMRC			5549	5549

	Statement of comprehensive income and expenditure	Balance sheet
	with regard to the settlement for the period 1/1/09 to 31/12/10. These items should be in short term creditors and not in provisions. The amounts are: a) £2,563k Non Schools b) £2,986k Schools total £5,549k	
Capital grants long term	£37,226k Capital Grants – Receipts in Advance is currently shown as Long Term in the Balance Sheet. £32,175k will be used in 2012/13 and therefore should be Short Term.	32,175
Capital grants short term		32,175

As well as the numerical errors within the primary statements highlighted above, there were a number of amendments to disclosure notes. Only the most significant ones have been summarised in the next table.

Amendments to primary statements and disclosure notes		
Disclosure	Nature of adjustment	Amendment
Note 7 Abfab	The use of major repairs allowance £11,696k to fund new capital expenditure is shown in the wrong column in note 7.	Note has been amended.
Officer remuneration Note 34 bandings	Band £50,000-£54,999 incorrectly included an individual who is not an officer of Durham County. Note also added to the senior officer remuneration note to state why comparatives have been amended. Overall total in	Note has been amended.

	10/11 509 but comparative in 11/12 is 599. The note also explains a number of differences in the individual bandings.	
Related party transactions note 38	The note has been amended to reflect the value of transactions for VISIT County Durham (£413,066) and Durham Villages Regeneration Company Limited (£nil).	Note has been amended.
Exit packages note 34 Termination benefits note 43	<p>Amendment to note to explain what these disclosures relate to and the difference between the two notes. Accounting policy updated to refer to both termination benefits and exit packages.</p> <p>Termination benefits note needs to include all payments including pension enhancements.</p> <p>Exit package some bandings need to be amended and certain individuals originally excluded from the note officers have found approvals so need to be included.</p> <p>Service departments did not have all the documentation required for authorisations and officers are working to improve systems across the council.</p>	Note has been amended.
HRA	The Vacant Possession valuation disclosed in the HRA note 2 has been amended from £1,336.210 million to £1,218.213 million. The note has also been amended to show the previous years Vacant Possession valuation for 2010/11 which was £1,326.230 million but now amended to £1,285.092 million.	Note has been amended.
HRA	£11,696k major repairs allowance should be shown separately in the analysis of the movement on the HRA statement.	Note has been amended
Financial instruments note	Debtors balances includes £13,030k net of Council Tax related debtors. Debtors and creditors arising from non-exchange transactions which do not have a contractual basis (e.g. non-domestic rates, council tax) do not specifically meet	Note has been amended

	the definition of financial instrument. The creditors £5.2m net balance includes amounts relating to NNDR which should also be excluded from the FI disclosures.	
Collection fund	No comparatives were shown for notes 2 and 3.	Note has been amended.

Appendix 4 – Draft letter of management representation

To: Cameron Waddell
District Auditor
Audit Commission

Durham County Council - Audit for the year ended 31 March 2012

We confirm to the best of our knowledge and belief, having made appropriate enquiries of other officers of Durham County Council, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2011 and the associated financial statements of its pension fund.

Compliance with the statutory authorities

We have fulfilled our responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Council, for the completeness of the information provided to you, and for making accurate representations to you.

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.

Uncorrected misstatements

The effects of uncorrected financial statements misstatements summarised in the attached schedule are not material to the financial statements, either individually or in aggregate. These misstatements have been discussed with those charged with governance within the Council and the reasons for not correcting these items are detailed in the appendix [to be added by Council].

- reason 1 etc;

- reason 2]

Supporting records

We have made available all relevant information and access to persons within the Council for the purpose of your audit. I have properly reflected and recorded in the financial statements all the transactions undertaken by the Council.

Irregularities

We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

There have been no:

- 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;
- communications from regulatory agencies concerning non-compliance with, or
- deficiencies on, financial reporting practices which could have a material effect on the financial statements.

We also confirm that we have disclosed:

- our 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;
- our knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk the financial statements may be materially misstated as a result of fraud.

Law, regulations, contractual arrangements and codes of practice

We have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. 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.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates including fair values

We confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

We confirm:

- the appropriateness of the measurement method, including related assumptions and models, and the consistency in application of the method;
- the assumptions appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the Council, where relevant to the accounting estimates and disclosures;
- the disclosures relating to the accounting estimate are complete and appropriate under the Code; and
- that no subsequent event requires the Council to adjust the accounting estimate and related disclosures included in the financial statements.

Related party transactions

We confirm that we have disclosed the identity of the Council's related parties and all the related party relationships and transactions of which I am aware. We have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the Code.

Unfunded pension liabilities

I confirm that all unfunded pension liabilities e.g. discretionary added years awarded to staff in the LGPS and discretionary benefits awarded to teachers under the Teachers Pension scheme are included within the IAS 19 liability figures.

Subsequent events

We have adjusted for or disclosed in the financial statements all relevant events subsequent to the date of the financial statements.

Single Asset Register

There have been a number of large and material adjustments/assumptions made as part of the single asset project. We confirm that the Dingle asset register as at 31 March 2012 is free from material misstatement.

Provisions

We confirm that provisions made are comprehensive and complete at 31 March 2102.

Property, Plant and Equipment

We confirm that property, plant and equipment have been appropriately and adequately disclosed in the financial statements and this value is not materially misstated. In particular, we confirm that there are no material misstatements due to:

- omissions of property, plant and equipment from the asset records of the Council;
- the lack of up-to-date historic cost records relating to land and buildings;

- significant weakness in controls: in particular, no reconciliations being undertaken between the general ledger and asset registers
- the lack of working papers to support some of the figures included in the property, plant and equipment in note 12; and
- any other information which we are not currently aware of that may have a material impact on property, plant and equipment.

We confirm that this letter has been discussed and agreed by the Audit Committee on 27 September 2012

Signed

Name: Don McLure

Signed

Name: Eddie Bell

Appendix 5 – Glossary

Annual Audit Letter

Letter issued by the auditor to the Authority after the completion of the audit that summarises the audit work carried out in the period and significant issues arising from auditors' work.

Annual Governance Report

The auditor's report on matters arising from the audit of the financial statements presented to those charged with governance before the auditor issues their opinion [and conclusion].

Annual Governance Statement

The annual report on the Authority's systems of internal control that supports the achievement of the Authority's policies aims and objectives.

Audit of the accounts

The audit of the accounts of an audited body comprises all work carried out by an auditor under the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

Audited body

A body to which the Audit Commission is responsible for appointing the external auditor.

Auditing Practices Board (APB)

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

Auditing standards

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

Auditor(s)

Auditors appointed by the Audit Commission.

Code (the)

The Code of Audit Practice for local government bodies issued by the Audit Commission and approved by Parliament.

Commission (the)

The Audit Commission for Local Authorities and the National Health Service in England.

Ethical Standards

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

Financial statements

The annual statement of accounts that the Authority is required to prepare, which report the financial performance and financial position of the Authority in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

Group accounts

Consolidated financial statements of an Authority and its subsidiaries, associates and jointly controlled entities.

Internal control

The whole system of controls, financial and otherwise, that the Authority establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

Materiality

The APB defines this concept as 'an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement

within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

Significance

The concept of ‘significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit of the financial statements. Significance has both qualitative and quantitative aspects.

Those charged with governance

Those entrusted with the supervision, control and direction of the Authority. This term includes the members of the Authority and its Audit Committee.

Whole of Government Accounts

A project leading to a set of consolidated accounts for the entire UK public sector on commercial accounting principles. The Authority must submit a consolidation pack to the department for Communities and Local Government which is based on, but separate from, its financial statements.

Appendix 6 – Action plan

Recommendations

Recommendation 1 Revaluations - schools

The Council Valuer will need to consider which assets are revalued in 2012/13 to avoid any problems with part valuation of schools. The Council should ensure that changes in valuations as at April and at the year end (31 March) are fully considered by finance as well as estates before deciding whether to account for these in the financial statements. A full valuation of schools should be completed as at 1 April 2012.

Responsibility	Service Finance
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Priority	High
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Recommendation 2 Asset register reconciliation to ledger

.Reconciliations between the fixed asset register and the general ledger should be completed as part of the closedown period and must reconcile to all figures in the PPE note in the accounts. This should be supported by working papers and be completed prior to submission of the draft statements. The asset register should be updated regularly throughout the year (including additions).

Responsibility	Service Finance
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Priority	High
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Recommendation 3 Asset register - migration of housing dwellings

Easington Council Dwellings records are held on a village basis and not on an individual asset basis. The Council should look to migrate all three housing asset registers for council dwellings onto the IPF Asset Manager as soon as is practicable to address this issue.

Responsibility	Service Finance
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Priority	High
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Recommendation 4 Working papers

The Council needs to ensure that final accounts working papers are prepared by officers as part of the closedown arrangements and a full set available for the beginning of the audit. There should be a clear audit trail to the figures in the statements and notes. This process will involve

considerable effort but I am confident that the number of audit queries will reduce and more importantly so will the demands on officers' time.

Responsibility Service Finance

Priority High

Recommendation 5 HRA rents

Officers were unable to provide a detailed breakdown of the weekly rent income figure, for the week 02/01/2012 - 08/01/2012, from the Durham City Homes rents system because only one individual who works offsite has the appropriate knowledge to allow an interrogation of the system. Officers should ensure that they have the appropriate knowledge within the council to enable them to complete this task.

Responsibility Service Finance

Priority High

Recommendation 6 HRA ALMOs

Both East Durham Homes and Dale and Valley Homes should be requested to specifically show a charge for 'Supervision and Management' and 'Repairs and Maintenance' on their periodic management fee invoices to provide a more robust method for finance officers to be able to prepare the classification needed for the accounts.

Responsibility Service Finance

Priority High

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