

Lothian Valuation Joint Board

Report to Members and the Controller of Audit on the 2007/08
Audit



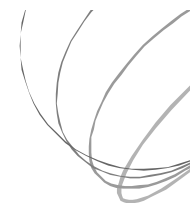
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Introduction

1. This report summarises the findings from our 2007/08 audit of the Lothian Valuation Joint Board. The scope of the audit is set out in our Annual Audit Plan (AAP), which was submitted to the board in March 2008.
2. The financial statements of the board are the means by which it accounts for its stewardship of the resources made available and its financial performance in the use of these resources. It is the responsibility of the board to prepare financial statements that present fairly its financial position and the income and expenditure for the year.
3. The members and officers of the board are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
 - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed
 - the board's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests
 - the board has adequate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability
 - the systems of internal control provide an appropriate means of preventing or detecting material misstatement, error, fraud or corruption
 - the board has proper arrangements for securing best value in its use of resources.



Financial statements

Introduction

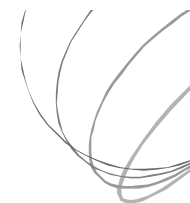
4. In this section we summarise key outcomes from our audit of the board's financial statements for 2007/08. We also summarise key aspects of the board's reported financial position and performance to 31 March 2008.
5. We audit the financial statements and give an opinion on:
 - whether they present fairly the financial position of the board and its expenditure and income for the year
 - whether they have been prepared properly in accordance with relevant legislation, applicable accounting standards and other reporting requirements.
6. We also review the statement on the system of internal financial control by considering the adequacy of the process put in place by the board to obtain assurances on systems of internal financial control and assessing whether disclosures in the statement are consistent with our knowledge of the board.

Overall conclusion

7. We have given an **unqualified** opinion on the financial statements of the Lothian Valuation Joint Board for 2007/08.
8. The board's unaudited financial statements were submitted to the Controller of Audit prior to the deadline of 30 June. A number of presentational changes were made to the draft accounts made available for public inspection to reflect the disclosure requirements set out in the SORP and for typographical errors. We would recommend that the draft accounts are subject to a full review by management prior to submission for audit.
9. Audited accounts were finalised by the target date of 30 September 2008 and are now available for presentation to the board and publication.

Financial position

10. The surplus or deficit on the income and expenditure account measures the board's financial result for the year, recognising the resources that have been consumed and generated in accordance with Generally Accepted Accounting Principles. The board's net operating expenditure in 2007/08 was



£5.579 million. This was met by constituent authorities' contributions of £5.965 million, resulting in an income and expenditure account surplus of £0.386 million.

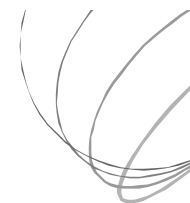
11. The movement on the general fund balance is also an important aspect of the board's stewardship as the main budget reference point, the main differences being:
 - capital investment is accounted for as it is financed, rather than when fixed assets are consumed
 - retirement benefits are charged as amounts become payable to pension funds and pensioners, rather than as future benefits are earned.
12. After adjusting for these items, the board broke even for the year.
13. Within these figures, the board made savings of £0.229 million arising from underspends in employee costs, and supplies and services costs. The net underspend will be returned to constituent councils.

Going concern

14. The board's balance sheet shows a net liability of £0.803 million. The negative balance reflects the pension liabilities falling due in future years. Auditing standards require auditors to consider an organisation's ability to continue as a going concern when forming an opinion on financial statements. One of the indications that may give rise to going concern considerations is an excess of liabilities over assets.
15. The board's statement of accounting policies confirms that it has been considered appropriate to adopt a going concern basis for the preparation of the financial statements as the constituent councils have a legal obligation to fund the net expense of the board. Future pension liabilities will therefore be met as they fall due by constituent authorities and government grant in the normal way. We are satisfied that the process the board has undertaken to consider going concern is reasonable.

Accounting practice

16. Local authorities in Scotland are required to follow the *Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice* (the 'SORP'). The 2007 SORP required a number of significant changes to be made to the 2007/08 financial statements to make them more consistent with the accounts of other public and private sector entities. The major changes include:
 - accounting for financial instruments based on FRS 25, FRS 26 and FRS 29;

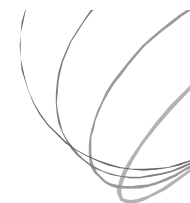


- replacement of the fixed asset restatement account and capital financing account by a revaluation reserve and capital adjustment account.
17. Overall, we were satisfied that the board had prepared the accounts in accordance with the revised SORP.
 18. The board adjusted the financial statements to reflect our audit findings. A significant change to the accounts was the introduction of fixed asset accounting. This was a result of the board moving to the new premises at the Gyle and acquiring a number of assets that will provide economic benefit over more than one accounting period.
 19. Capital expenditure in 2007/08 totalled £0.102 million which was financed from current revenue. A prior year adjustment of £0.540 was required to reflect assets previously acquired. The board must now ensure that it recognises all capital expenditure appropriately and reflects it in the balance sheet in accordance with accounting convention. Maintaining a fixed asset register would greatly enhance this process.

Key Risk Area 1

Legality

20. Each year we request written confirmation from the Treasurer that the board's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of the Assessor and the Senior Management Team, the financial transactions of the board were in accordance with the relevant legislation and regulations governing its activities.
21. The board moved to larger premises at the Gyle in 2007. Subsequently unused accommodation within the new premises has been made available for hire as conference facilities. This generated income of approximately £10K in 2007/08. Whilst the extent of this activity was limited and we are advised it has now ceased we would suggest that the board considers its position carefully prior to undertaking any such activities in the future.
22. The Valuation Joint Boards (Scotland) Order 1995 under which the board was created is quite specific in the functions that Valuation Joint Boards have been given and we would suggest that it would be appropriate to seek legal advice before extending the range of the board's activities further than those described in that legislation.



23. Where such activities may be considered allowable the board should ensure that they are demonstrably charged with their full share of appropriate overhead costs and are accounted for separately from the board's valuation functions to ensure that constituent councils do not bear any costs.

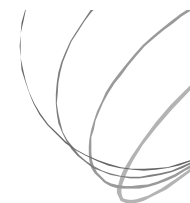
Key Risk Area 2

24. There are no additional legality issues arising from our audit which require to be brought to members' attention.

Financial outlook

Pension liabilities

25. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. In accounting for pensions, Financial Reporting Standard 17 (Retirement Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in very large future liabilities being recognised in the annual accounts.
26. The board's estimated pension scheme liabilities at 31 March 2008 exceeded its share of the assets in the Lothian Pension Fund by £1.400 million, reducing from £5.372 million in the previous year. Budgeted contributions are to be 325% of employee contributions in 2007/08 and 2008/09, reflecting the actuarial valuation as at 31 March 2005. The next full actuarial valuation will assess the position at 31 March 2008. Recent changes to the Local Government Pension Scheme regulations are expected to release some future financial benefits, while providing additional flexibility to future pensioners.



Governance

Introduction

27. In this section we comment on key aspects of the board's governance arrangements during 2007/08. We also provide an outlook on future governance issues, including our views on potential risks.

Overview of arrangements in 2007/08

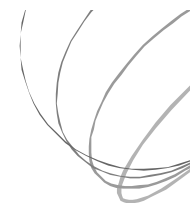
28. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. The board has a responsibility to put in place arrangements for the conduct of the affairs of the organisation, ensure the legality of activities and transactions, and to monitor the adequacy and effectiveness of those arrangements in place.

Audit Committee

29. Effective scrutiny is central to good governance, with a significant role for members to scrutinise performance and hold management to account. Due to the size of the organisation, the board does not have an established audit committee. That said, the board considers reports by internal and external audit. In addition, the Chief Internal Auditor provides an annual report, including a statement on the adequacy and effectiveness of the board's internal control system. In accordance with CIPFA's good practice principles for audit committees, the remit of the board should be reviewed to include the review of the ISA 260 letter.

Internal Audit

30. Internal audit provides a key role in the board's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. The board's internal audit service is provided by the City of Edinburgh Council's Chief Internal Auditor. From our review of the service, we found that the work is conducted in accordance with CIPFA's Code of Practice for Internal Audit in Local Government, that the audit plan was sufficient and that all work on which we placed reliance was completed and the relevant assurances obtained.



Service level agreements

31. A range of support functions are provided by the City of Edinburgh Council to the Lothian Valuation Joint Board, this includes payroll, accounts payable and accounts receivable. In addition, the City of Edinburgh Council's finance function prepares the annual financial statements for the board. Currently these activities have not been formalised and service provision would benefit from the introduction of a service level agreement defining the relationship between the board and City of Edinburgh Council.

Key Risk Area 3

Systems of internal control

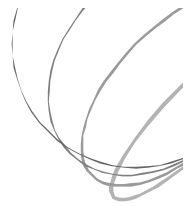
32. A Statement on the System of Internal Financial Control for the board was included within the financial statements. Following receipt of the Assessor's assurance certificate on financial controls, the work of managers, internal and external auditors, the Treasurer concluded that he was satisfied that reasonable assurance could be placed on the adequacy and effectiveness of the systems of internal control operated by the board.
33. In accordance with good practice, the statement was reviewed by the board in June 2008 prior to signature by the Treasurer and is supported by a high level review of the adequacy and effectiveness of internal financial controls undertaken by Internal Audit. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.

Prevention and detection of fraud and irregularities

34. The board has arrangements in place to prevent and detect fraud, inappropriate conduct and corruption. These arrangements include standing orders and financial regulations, a whistle blowing policy, an anti-fraud and corruption policy and codes of conduct for elected members and staff. We are pleased to note that the board continues to have appropriate arrangements in place to minimise the risk of fraud and corruption. Each year, Audit Scotland gathers information on such cases of fraud identified by audited bodies. In 2007/08, there were no cases reported for the Lothian Valuation Joint Board.

Performance

35. The board approved the Performance Management Policy in March 2007 and aims to achieve a corporate approach to managing performance through this Policy. The board has identified five core components for managing performance:



- aims, values, contributions to the joint board's strategic objectives and service plans
- pyramid performance monitoring
- a management information system
- annual appraisal and employee development plans
- structured communication.

36. The Annual Report 2007/08 produced by the board indicates an improvement in performance in relation to their locally determined performance indicators. The percentage of amendments dealt with within 3 months has improved significantly from 74.90% in 2006/07 to 83.26% in 2007/08.

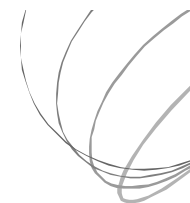
Governance outlook

37. Overall, the board is well placed to ensure that it operates appropriate corporate governance arrangements in the coming years. It will need to keep these under review to ensure that they remain up-to-date and are subject to continuous improvement.



Final Remarks

38. Attached to this report is an action plan setting out the key risks identified by the audit which we are highlighting for the attention of members. In response, officers have considered the issues and have agreed to take the specific steps set out in the column headed 'planned management action'. On occasion, officers may choose to accept the risk and take no action. Alternatively, there may be no further action that can be taken to minimise the risk. Where appropriate, the action plan clearly sets out management's response to the identified risks.
39. Appropriate mechanisms should be considered and agreed by members for monitoring the effectiveness of planned action by officers. We will review the operation of the agreed mechanism as part of the 2008/09 audit.
40. The co-operation and assistance given to us by the officers of the board and the City of Edinburgh Council is gratefully acknowledged.



Appendix A: Action Plan

Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1.	19	<p>Fixed Asset Accounting</p> <p>The board must now ensure that it recognises all capital expenditure appropriately and reflects it in the balance sheet in accordance with accounting convention. Maintaining a fixed asset register would greatly enhance this process.</p> <p><i>Risk: the board may fail to exercise appropriate stewardship over its assets.</i></p>	A fixed asset register shall be created and maintained. While commencing from 1 st April 2008 it shall reflect expenditure established under the audit for 2007/2008.	Graeme Strachan, Depute Assessor	Current
2.	21-23	<p>Trading Activity</p> <p>If the board continues to provide conference facilities, it should first establish that it has the power to do this and account for this activity separately.</p> <p><i>Risk: the board provides a service that is not within its statutory powers. The costs of this service are met by constituent authority contributions.</i></p>	The Board has ceased to promote or provide conference facilities.	N/A	N/A
3.	31	<p>Service Level Agreements</p> <p>A service level agreement between the Lothian Valuation Joint Board and the City of Edinburgh Council should be formalised and presented to the board for their approval.</p> <p><i>Risk: the board cannot monitor the performance of services provided by the City of Edinburgh Council.</i></p>	A work programme leading to an agreed SLA shall be established between client (LVJB) and service provider (CEC).	Assessor/ Treasurer	31 st March 2009