

North Hertfordshire District Council

**Report to Those Charged With Governance (ISA 260)**

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For the year ended 31 March 2012

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# 1 Executive summary

## 1.1 Purpose of this report

The purpose of this report is to highlight the key issues affecting the results of North Hertfordshire District Council (the Council) and the preparation of the Council's financial statements for the year ended 31 March 2012. It is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

Under the Audit Commission's Code of Audit Practice we are required to report whether, in our opinion, the Council's financial statements present a true and fair view of the financial position. We are also required to reach a formal conclusion on whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources (the Value for Money Conclusion).

We take responsibility for this report, which has been prepared on the basis of the limitations set out in 'The small print' (Appendix B).

## 1.2 Introduction

In the conduct of our audit we have not had to alter or change our audit plan, which we communicated to you in our Audit Approach Memorandum dated June 2012.

Our audit is substantially complete although we are finalising our procedures in the following area:

- updating our past balance sheet events review, to the date of signing of the accounts.

We received draft financial statements in accordance with the national deadline and the majority of accompanying working papers at the commencement of our work.

Through consultation with management, we have identified a number of areas for potential improvement in the accounts close down process, mainly relating to 'account mapping' and documentation of support for estimates and judgements. We intend to hold a de-brief meeting with the finance team following the completion of the audit to ensure that any revised arrangements are incorporated into next year's audit preparation, in accordance with other recommendations raised in this report (Appendix A).

## 1.3 Key audit and financial reporting issues

### Financial statements opinion

A small number of misstatements were identified that impact on the Council's income and expenditure position (statement of comprehensive income) and balance sheet (statement of financial position). Other audit adjustments processed to the accounts were relatively minor in nature and predominantly of a presentational nature only, with no overall net effect on the Council's reported assets and liabilities.

The key messages arising from our audit of the Council's financial statements are:

- the need to maintain appropriate non-current asset accounting records separate from those maintained for estates management purposes, supported by a monthly or quarterly reconciliation process;

- the need to ensure that appropriate formal arrangements are put in place to maintain an appropriate schedule of non-current asset revaluation exercises to support the ongoing valuation basis of the Council estate, in accordance with the requirements of IAS 16 and as per the Council's stated accounting policy; and
- the need to evaluate and maintain the documented basis for any significant accounting treatments that have been applied, in particular where these impact on the Council's income and expenditure position and relate to areas of significant accounting judgement or estimates, such as provisions, assets-held-for-sale or redevelopment, and grant income recognition.

Further details are set out in sections 2 and 3.

#### **Value for money conclusion**

We are pleased to report that, based on our review of the Council's arrangements, we propose to issue an unqualified opinion.

Our detailed findings will be reported to the Council separately in our report 'Review of the Council's arrangements for securing value for money - September 2012.'

Further details are set out in section 6.

#### **1.4 Controls**

##### **Roles and responsibilities**

The Council's management is responsible for the identification, assessment, management and monitoring of risk, and for developing, operating and monitoring the system of internal control.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to the Council.

##### **Findings**

We draw your attention in particular to potential weaknesses in internal control identified in relation to controls over journal postings.

Management should continue to keep the system of controls under review.

Section 4 contains further commentary in this regard.

#### **1.5 The way forward**

Matters arising from the financial statements audit and review of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources have been discussed with the Strategic Director of Finance, Policy and Governance.

We have made a number of recommendations, which are set out in an action plan within Appendix A. Recommendations have been discussed and agreed with the Strategic Director of Finance, Policy and Governance and the finance team.

#### **1.6 Acknowledgement**

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

**Grant Thornton UK LLP**

**6 September 2012**

## 2 Key audit issues

In this section we present our findings in respect of matters and risks identified at the planning stage of the audit and we provide details of additional matters that arose during the course of our work.

Issue	Audit areas affected	Work completed	Assurances gained
Accounting for property, plant and equipment	Non-current assets and income and expenditure	<ul style="list-style-type: none"> <li>We have communicated directly with the Council's internal valuer and evaluated the reasonableness and relevance of the key assumptions applied.</li> <li>Our testing specifically considered the instructions and data provided to the valuer by the finance team and all associated accounting entries recorded in the accounts.</li> <li>We have inspected and considered the results of the specific exercise undertaken by the Council to review the recorded measured internal floor spaces of all specialised assets, in order to identify any further potential discrepancies in addition to those identified during the 2011 audit.</li> </ul>	<ul style="list-style-type: none"> <li>Significant valuation movements were reviewed individually due to the lack of a covering report by the valuer detailing the basis of valuation and any specific valuation considerations applied.</li> <li>The results of the specific exercise undertaken in respect of recorded floor spaces was not presented separately from other valuation movements or changes to recorded asset detail and therefore this needed to be considered alongside all such movements recorded throughout the year.</li> <li>Evaluation of the individual assumptions applied by the valuer, and any separate considerations or judgements performed by the finance team, confirmed them to be reasonable, appropriate and in accordance with accepted RICs standards as relevant to the valuation of public sector assets.</li> <li>A number of 'reconciling' differences between asset records were identified by the finance team during the course of our testing which result in audit adjustments. (Matters identified during the course of the audit are discussed below, with audit adjustments detailed in section 3).</li> </ul>

Issue	Audit areas affected	Work completed	Assurances gained
Financial performance pressures	All areas of the financial statements	<ul style="list-style-type: none"> <li>Regular liaison meetings were held with the Director of Finance, Policy and Governance and ongoing reviews were carried out of internal financial reporting in order to maintain our understanding of the Council's underlying financial position.</li> <li>Our Financial Resilience Review II considered progress against recommendations raised in our prior year review, as well as the Council's own progress against its medium term financial plans.</li> </ul>	<ul style="list-style-type: none"> <li>A number of issues were identified during the course of the audit that, whilst not resulting in quantified audit adjustments impacting on the Council's reported financial position for the year ended 31 March 2012, should be subject to further consideration by the Council to ensure that any potential impacts are appropriately managed and accounted for in future periods. (Matters identified during the course of the audit are discussed below).</li> <li>The Council's arrangements for securing financial resilience and securing economy, efficiency and effectiveness in the use of its resources are otherwise considered to remain sufficiently robust. (Further details are set out in section 6).</li> </ul>
Control weaknesses in the Council's IT systems	All areas of the financial statements	<ul style="list-style-type: none"> <li>Our information systems specialist undertook a review of network controls and the main accounting system (Integra) in March 2012, which included follow up on the implementation status of any previous recommendations.</li> </ul>	<ul style="list-style-type: none"> <li>We concluded that, from the work undertaken to date there were no material weaknesses that were likely to impact on the Council's financial statements for the year ended 31 March 2012.</li> <li>Detailed findings and recommendations have been communicated to management during the year, as reported in our Audit Approach Memorandum dated June 2012. Recommendations are included in Appendix A of this report.</li> </ul>

## 2.1 Matters identified during the course of the audit

The following findings are presented to the Council for consideration of its responsibilities in the context of overall financial reporting.

### Valuation of non-current assets and accounting records

Management have identified a number of misstatements to non-current assets as a result of errors or omissions within reconciliations to the GVAS system.

The GVAS system is an estates management system which is used to record detailed asset information including the full location address, floor space measurements and other considerations that may be relevant to valuation. Information is updated by the estates management team throughout the year for a variety of different purposes, which includes valuations. The iterative use of this system in recording valuation changes appears to be to the detriment of the traditional main accounting record, the fixed asset register (FAR), which should act as the means by which management both identify the need for, and record the results of, asset valuations. The GVAS system is periodically reconciled to the FAR, which currently takes the form of an excel spreadsheet, although there are plans to implement the fixed asset module available as part of the main ledger system (Integra) as soon as possible.

In our opinion, use is not currently made of an appropriate accounting record, within a suitable IT control environment, that efficiently and accurately supports a programme of valuation exercises, which should originate from a documented annual management decision.

Our testing continues to highlight a number of concerns regarding the engagement with, and recording the results of the work of, the Council's valuer and other potential contributors to the financial statements.

In addition to the misstatements identified by management, our testing identified a number of instances whereby changes in both underlying asset data and movements in valuation and their basis were unclear from the work performed by the valuer, changes in asset data or valuation were recorded in the incorrect accounting period, the basis of valuations applied on individual assets by management differed from those applied by the valuer, and unnecessary market based valuations had been

performed for several years against assets from which the Council derives no operational use. These findings support that the current use of the GVAS system does not provide a suitable audit trail for asset valuations.

To ensure ongoing compliance with the requirements of IAS 16 (Property, Plant and Equipment), which states that the frequency of valuations should be determined based on the significance and volatility of changes in fair value of a class of assets, the Council should ensure that a documented annual review is undertaken by management to identify and support decisions as to when professional valuation is required. Some classes of asset may necessitate annual revaluation, whereas such frequent revaluations are unnecessary for items of property, plant and equipment with only insignificant changes in fair value. Instead, it may be necessary to revalue such items only every three or five years.

The Council should establish and undertake a documented annual assessment of the requirement to undertake any in-year revaluation exercises by assessing each class of asset. Instructions should then be formally communicated to the valuer, which include the requirement for the valuer to present their finding in an appropriate report detailing the basis of the valuation performed, any specific valuation considerations and supported by a detailed schedule of results. This schedule should then be used to update the FAR, as the accounting record, as part of a specifically dated exercise.

### Assets held-for-sale

The Council continues to record a comparatively high, and unchanged, balance of non-current assets as 'held-for-sale.'

	2010/11	2011/12
Assets held for sale as at 31 March	£3,750k	£3,750k

In accordance with the Council's accounting policies and relevant GAAP (IFRS 5), in order for an asset to be classified as 'held-for-sale' it must be available for immediate sale in its present condition and its sale must be highly probable, whereby there is an active programme committed to the sale of the asset. Events or circumstances may extend the period to

complete the sale beyond one year if the delay is caused by events or circumstances beyond the entity's control and there is sufficient evidence that the entity remains committed to its plan to sell the asset.

Our testing highlighted a significant lack of documented support for the commitment to the disposal of these assets by sale, with some support extending back more than one year, despite managements ongoing consideration of market conditions and interaction with prospective purchasers. The valuation basis for assets 'held-for-sale' can be considerably different to the valuation that would otherwise be held for their ongoing operational use, especially in a reduced capacity, or disposal by a means other than sale.

Whilst we are satisfied that there is no requirement for either adjustment or further work in respect of the current year, we highlight to those charged with governance that a degree of judgement has been made by management in both the stated ongoing commitment to sale and in determining the carrying value of these assets. In order to ensure ongoing compliance with relevant GAAP, the Council should seek to document the basis of all significant judgements, and the basis of valuation, to ensure that such judgement is applied consistently.

### **Provisions and contingent liabilities**

Municipal Mutual Insurance Ltd (MMI) was the predominant insurer of public sector bodies prior to ceasing its underwriting operations in September 1992 having suffered substantial losses. Although MMI directors are committed to run-off with full payments of agreed claims, the companies liabilities have increased in recent years. In addition, on 28 March 2012 the Supreme Court reached a judgement on the 'mesothelioma trigger litigation' which means that some cases previously rejected by MMI will now need to be paid.

The Council participates in the 'Scheme of Arrangements' and is therefore effectively a 'Scheme Creditor', which means that it may have to pay back part of all claims for which it has received settlements since 1993 in the event of the Scheme of Arrangements being triggered. As at 31 March 2012 the Scheme of Arrangements had not been triggered, however, many

commentators believe that it will be triggered in the next twelve months, resulting in claw-backs of 10-25%.

The Council currently has a provision of £40k and an earmarked 'insurance' reserve of £90k against existing potential claw-back arrangements up to £453k, which have been maintained at this level for several years. Management support their decision to continue to maintain the existing arrangements for the year ended 31 March 2012 based on the certainty of known events as at the balance sheet date.

In 2004, the Council tendered and won the Leisure Management contract for Hitchin and Royston leisure centres. The Council has since placed £118k aside each year as a provision against the costs of compensating one of the Leisure Management contractors for any potential future employment cost as specified within the contract if they fall due. The provision currently held now totals £600k as at the balance sheet date.

Our review highlighted that the current basis and documented support for these provisions and the amounts set aside appears to be insufficient under the requirements of accounting standards.

IAS 37 (Provisions, Contingent Liabilities and Contingent Assets) requires that the amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. As such, assumptions and discount rates should be considered on an annual basis against the latest available data and any relevant in-year transactions.

The Council should revisit the estimation basis of its major provisions to ensure that any potential over or under provision is appropriately addressed in subsequent accounting periods.

We understand that management have committed to a review of the basis of calculation of its significant provisions and the key underlying assumptions applied during 2012/13, with the assistance of its legal department.



**Recognition of grant and contribution income**

Where previously amounts received would have been deferred and offset against associated expenses as they were incurred, since 2010/11 the revised requirements of the Code now require the recognition of grant and contribution income within the comprehensive income and expenditure position as soon as any conditions attached to these amounts by the granting body or individual can be evidenced to have been met.

Our review of the conditions attached to significant grants and contributions, and amounts still recorded as 'receipts in advance' or yet to be recorded as receivable, highlighted a degree of inconsistency in the judgements made by management in applying the Council's accounting policies.

Whilst no significant misstatements have been identified as part of our testing, the Council should establish, apply and communicate a consistent treatment of income received in the form of grants and contributions from other parties, in order to reduce the potential for such misstatements in future periods.

## 3 Audit adjustments

### 3.1 Misstatements

We are required to communicate all uncorrected misstatements to you, other than those considered to be clearly trivial. We have requested that management correct these misstatements and have included (where applicable) the reasons given by them as to why the misstatements remain uncorrected.

### 3.2 Impact of misstatements

All adjusted misstatements are set out in detail in section 3.5 below. In summary, the impact of adjustments is:

<b>Comprehensive income and expenditure statement</b>	<b>Increase/ (Decrease) in surplus</b>
	<b>£'000</b>
Deficit per draft accounts	(11,987)
Management adjustments posted	(423)
<b>Final deficit per adjusted financial statements</b>	<b>(12,410)</b>

The aggregate impact of unadjusted misstatements on the comprehensive income and expenditure statement, were they to be processed, would result in a decrease in the deficit by £19k. There is no impact on the audit report as a result of these unadjusted misstatements.

### 3.3 Misclassifications and disclosure omissions

Tests of detail identified a small number of misclassification and disclosure errors within the supporting notes. These misclassifications did not impact on the statement of comprehensive income and expenditure or the balance sheet.

The supporting notes have been adjusted by management in accordance with our findings, to ensure consistency with underlying accounting records and allow meaningful year-on-year comparison by readers of the accounts.

### 3.4 Unadjusted misstatements

	Detail	Balance sheet £000	Comprehensive Inc & Exp statement £000	Reason for not adjusting
1	Our review of provisions identified that a provision still exists for the rebuilding of Baldock Pavilion, which burnt down 10 years ago. This amount is not considered to continue to meet the recognition requirements of IAS 37 (Provisions, Contingent Liabilities and Contingent Assets) and should be released back to the general fund. - Management have been advised that amounts could be more appropriately recognised as 'earmarked reserves.'	£19	(£19)	Management have stated an intention to review these amounts in the current financial year.
<b>Impact</b>		<b>£19</b>	<b>(£19)</b>	

### 3.5 Adjusted misstatements

	Detail	Balance sheet £000	Comprehensive Inc & Exp statement £000
1	'Middlefields Pelican Pub' (an investment asset) was disposed of in the prior year, but not removed from the balance sheet.	(36)	36
2	'Lairage Depot' was identified to have been recorded as a separate asset as well as being correctly included as part of the Hitchin multi-storey car park, thereby double counting this asset.	(30)	30
3	'Burford Way' and 'West Avenue Store' were identified as having been omitted from the balance sheet in error and have therefore been recognised in year, with an appropriate depreciation charge applied.	108	(108)
4	'Howard Park' public convenience was demolished during the year, but had not been derecognised from the balance sheet.	(280)	280
5	The impact of the downward revaluation of 'Old Hale Way' had not been reflected on the balance sheet.	(185)	185
<b>Impact</b>		<b>(£423)</b>	<b>£423</b>

## 4 Design effectiveness of internal controls

### 4.1 Accounting system and internal control

Our audit is not designed to identify all significant weaknesses in the Council's internal controls but is designed primarily for the purpose of expressing our opinion on the financial statements of the Council.

However, where, as part of our testing, we identify any control weaknesses, we will report these to you.

In consequence, our work did not encompass a detailed review of all aspects of the internal controls and cannot be relied upon necessarily to disclose all defalcations or other irregularities or to include all possible improvements in internal control.

See 'The small print' for further details of our approach in respect of internal controls.

### 4.2 Review of information technology controls

Our information systems specialist performed a review of the general IT control environment in March 2012, as part of our overall review of the internal controls system. We also performed a follow up of the issues that have been raised in the previous year.

We concluded that, from the work undertaken to date there are no material weaknesses that are likely to impact on the Council's financial statements for the year ended 31 March 2012.

We have, however, reiterated areas for improvement identified during the course of our work relating to change management, remote backup and recovery testing and regular review of firewall logs.

Detailed findings and recommendations have been communicated to management during the year as reported in our Audit Approach Memorandum dated June 2012. Recommendations are included in Appendix A of this report.

### 4.3 Key findings

The following findings are presented to the Council for consideration of its responsibilities in the context of the overall internal control environment and potential weaknesses.

#### Controls over journal postings

During testing of in-year journals, it was identified that the journal posters user ID is not a mandatory field when uploading journals, whilst for two journals selected, there were no physical records evidencing the sign-off by the preparer and authoriser. Further substantive testing did not identify evidence of inappropriate journals having been posted.

Poorly-controlled journal posting processes mean that both errors or fraud can occur and go undetected. With the heightened risk of fraud caused by the current economic conditions, improving controls over journals should be an area of focus for the Council.

## 5 Other reporting matters

### 5.1 Other assurance reviews

To support our audit opinion the following additional reviews have been undertaken as communicated as part of our audit planning:

#### VAT

Our VAT specialist undertook a review of the Council's arrangements in April 2012, with specific consideration of the following:

- overall compliance, including assurance processes and controls;
- reclaim on expenditure and contracted out services;
- sales/business income; and
- partial exemption and VAT return preparation.

#### PAYE

As part our 2011/12 audit plan we stated our intention to undertake a review of the arrangements in place regarding taxation associated with payroll, including National Insurance and PAYE. The objectives of this work were to:

- provide additional assurance that the figures recorded within the financial statements are true and fair and calculated appropriately and in accordance with current legislation; and
- assess employment taxes compliance for weaknesses and identify any potential material risk of exposure to tax/NIC, penalties and interest.

From the information available during the course of these reviews, there did not appear to be any material issues that we need to bring to your attention.

### 5.2 Annual governance statement

The Council is required to produce an Annual Governance Statement (AGS), which is consistent with the Code and other guidance issued by CIPFA. The AGS is published alongside the financial statements with the annual accounts.

We have reviewed the Council's arrangements and processes for compiling the AGS and considered whether the draft statement, as submitted to audit, is either misleading or inconsistent with other information known to us from our audit work.

Our review highlighted only minor adjustments to the overall structure and content of the statement. We have shared our findings with the Performance and Risk Manager and will review the narrative content of the revised statement to ensure that all agreed audit findings are appropriately reflected prior to signing of our audit opinion.

### 5.3 Public challenge matters

At the time of writing we have received no questions or objections in respect of the financial statements for the year ended 31 March 2012 that will prevent us from issuing our audit certificate.

## 6 Value for Money

### 6.1 Value for money conclusion

The Code of Audit Practice 2010 (the Code) describes the Council's responsibilities to put in place proper arrangements to:

- secure economy, efficiency and effectiveness in its use of resources;
- ensure proper stewardship and governance; and
- review regularly the adequacy and effectiveness of these arrangements.

We are required to give our conclusion based on the following two criteria specified by the Audit Commission:

#### **The Council has proper arrangements in place for securing financial resilience.**

The Council 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.

#### **The Council has proper arrangements for challenging how it secures economy, efficiency and effectiveness.**

The Council is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

### 6.2 Programme of work

#### **Securing financial resilience**

To support our conclusion against this criteria we have undertaken a follow up review to our work performed in the prior year, which considered the Council's performance against a series of key performance indicators and the arrangements in place against the three expected characteristics of proper arrangements as defined by the Audit Commission:

- Financial governance;
- Financial planning; and
- Financial control

Our 2011/12 review considers the Council's current performance against the same series of key performance indicators before focusing on the following specific areas of the characteristics listed above where the Council was rated as amber in the prior year review:

- The adequacy of planning assumptions within the medium term financial plan (MTFP);
- responsiveness of the MTFP; and
- performance management of savings plans

Our detailed findings will be reported to the Council separately in our report 'Review of the Councils arrangements for securing value for money - September 2012.'

### **Challenging economy, efficiency and effectiveness**

To support our conclusion against this criteria we have reviewed whether the Council has prioritised its resources to take account of the tighter constraints it is required to operate within by achieving cost reductions and improved productivity and efficiencies. In addition to considering the Council's savings plans as part of the review detailed above we have also undertaken separate reviews in the following areas:

- Review of the proposed business case for ICT shared service; and
- Comparison of anticipated versus actual reductions in the daily rate of internal audit provided under the Shared Internal Audit Service (SIAS)

### **6.3 Key findings**

There are no significant concerns arising from our follow up review of financial resilience, however, the Council faces increasing challenges from ongoing reform to local government funding. Localisation of non-domestic rates and support for council tax are expected to have a profound effect on local authority finances and the level of funding risk that individual councils will face.

Our review of the plans for developing a detailed business case for ICT shared services with Stevenage Borough Council and East Hertfordshire Council is ongoing and we intend to provide a draft report of our findings, to discuss with Management, in September. We have reviewed and challenged the risk assessment that the councils are performing. Although we have not performed any financial assessment of the business case itself, we have suggested guidance around what the councils should consider if they make a decision to pursue a shared service. The councils have engaged the services of an independent third party, SOCITM, to review the technical arrangements for the proposed hosting data centre, for any shared service that is pursued.

To date we have met with key staff at both the operational and senior management level, to gain an understanding of the governance structures in place to oversee the business case development process. In addition, we have reviewed key documents that support the processes in place for risk management and governance activities and controls, to assess how well current and future needs and investment decisions are made, and whether they are at the appropriate level

### **6.4 Overall conclusion**

On the basis of our work, having regard to the guidance on the specified criteria published by the Audit Commission, we are satisfied that in all significant respects the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2012.

## A Recommendations

### Key to priority rating of recommendations

- ▲ High – significant effect on control system
- Medium – effect on control system
- Low – best practice

	Assessment	Issue and risk	Recommendation
1	<p>■ Medium</p>	<p><b>Review of information technology controls</b> No documented Change Management policies and procedures have been presented during this audit or previous audits.</p> <p>In addition, we noted the following in relation to Change Management:</p> <ul style="list-style-type: none"> <li>• change requests are initiated and authorised through a Job Request form, which is used to request any job from ICT. It was, however, observed that routine patches from vendors on Integra do not adhere to this process; and</li> <li>• no formal emergency procedure is in place.</li> </ul> <p>Change control is not consistently applied across the ICT department and business systems, due to a lack of formal guidance.</p>	<p>We reiterate our original recommendation to implement a formal Change Management policy and related procedures.</p> <p><b>Management response: *</b> Since the last review the ICT Department have had to change its priorities to meet corporate demands such as Office Accommodation and moving between Buildings, Server Relocation, Server Virtualisation Project, New WIFI Services, and the ICT Restructure with 5 post being removed from the establishment.</p> <p>The programme to have Change Control developed is within the 2012-13 ICT Service Business Plan and this will commence within the next couple of months and in place by July 2012.</p>



	Assessment	Issue and risk	Recommendation
2	<p style="text-align: center;">■</p> <p>Medium</p>	<p><b>Review of information technology controls</b></p> <p>The Council utilises two new backup solutions to backup data and system to disk (via PHD backup) and then to tape (via BackupExec). However, as noted in prior years, formal backup restoration only happens during the Disaster Recovery testing, which is on a yearly basis. The last test was performed with HP in January 2012.</p> <p>Additionally, there is no off-site back-up storage to secure backup tapes. All backup tapes are kept onsite in a fire-proof safe. Without offsite backup facilities, essential business information, data and software may not be recovered following a media failure or disaster onsite.</p>	<p>We reiterate our original recommendation for management to develop and implement formal procedures over backup recovery testing. With consideration of the limited resources of ICT, we recommend that this exercise be done on an at least bi-annual basis.</p> <p>We further recommend that management should keep copies of backup tapes in an offsite backup location that is:</p> <ul style="list-style-type: none"> <li>• a safe distance from the Council office that will not be subjected by the same disruptive or destructive elements that can affect the office area; and</li> <li>• secure and has appropriate level of environmental protection.</li> </ul> <p><b>Management response: *</b></p> <p>The issue of storing all backup tapes off site to another building will be looked at within the next couple of weeks and tapes will be stored in a safe, protected, environmentally location as directed. Target date – end of May 2012.</p> <p>The ICT Manager and his Technical Services Manager are currently reviewing the HP Business Continuity Contract and we will discuss a bi-annual recovering testing project at HP’s Business Continuity offices.</p>

	Assessment	Issue and risk	Recommendation
3	<p style="text-align: center;">■ Medium</p>	<p><b>Review of information technology controls</b> As of September 2010, the firewalls have been configured, tested and implemented, with the logs kept by the GFI Events Manager, who retains 6 months' worth of data. However, there is still no reporting and investigation or reviewing is being carried out to identify any suspicious activities that the firewalls have detected.</p>	<p>We recommend that management should perform a regular review of firewall logs.</p> <p><b>Management response: *</b> Currently the GFI Events Manager does keep the 6 months of logs but the Technical Team have not had the spare capacity to look at the logs albeit we have passed our External PEN Testing this year.</p> <p>The appointment of the additional Senior Technical Support Officer will aid the workloads within this area and this piece of work will be factored in and started by May 2012.</p>
4	<p style="text-align: center;">● Low</p>	<p><b>Controls over journal postings</b> During testing of in-year journals, it was identified that the journal posters user ID is not a mandatory field when uploading journals, whilst for two journals selected, there were no physical records evidencing the sign-off by the preparer and authoriser. Further substantive testing did not identify evidence of inappropriate journals having been posted.</p> <p>Poorly-controlled journal posting processes mean that both errors or fraud can occur and go undetected. With the heightened risk of fraud caused by the current economic conditions, improving controls over journals should be an area of focus for the Council.</p>	<p>We reiterate our prior year recommendation that journal input processes and controls should be reviewed to ensure the accurate recording of journal inputters and authorisers and the minimisation of potential unauthorised manual changes to journal amounts.</p> <p><b>Management response:</b> We are satisfied that the current controls over journal postings are proportionate. A workflow solution would be better, but would also come at a cost. The current process requires segregation of duties via an inputter and an authoriser. The number of personnel with access to journal postings is also very limited. A journal is a transaction between accounting codes within the Council which would make it difficult to commit fraud without a failure in other controls.</p>

	Assessment	Issue and risk	Recommendation
5	<p style="text-align: center;">■</p> <p>Medium</p>	<p><b>Valuation of non-current assets</b></p> <p>Management have identified a number of misstatements to non-current assets as a result of errors or omissions within reconciliations to the GVAS system, whilst our testing continues to highlight a number of concerns regarding the engagement with, and recording the results of the work of, the Council's valuer and other potential contributors to the financial statements.</p> <p>The iterative use of an inappropriate accounting record, coupled with a lack of clear instructions or clearly scheduled results, increases the risk of potentially material introduced errors.</p>	<p>We reiterate our prior year recommendation that formal arrangements should be put in place regarding the issue of instructions to qualified professionals responsible for providing valuation information for inclusion in the Councils accounts and financial statements. Arrangements should include the receipt of a signed two part report comprising detail of the assumptions and methodologies applied, accompanied by a detailed schedule of results from the work performed, that can then be used to update the FAR as an appropriate accounting record in the form of a single documented exercise.</p> <p><b>Management response:</b></p> <p>We will continue to improve the regularity of communication between the Council's valuer and the accountancy team to ensure ongoing reconciliations of systems and the appropriate programme of valuations. This will include formal meetings during the year. However, given the Council's valuer and accountancy team work within the same Directorate we do not consider it necessary to go as far as producing a signed two part report, although would do so in the event of any valuations being contracted out. This would create additional work in an area where there is scarce free capacity and the use of formalised internal reporting between staff within the same Directorate is not considered effective use of resources.</p>

	Assessment	Issue and risk	Recommendation
6	<p style="text-align: center;">■ Medium</p>	<p><b>Estimates and judgements</b> Relevant GAAP and the Code requires management to disclose in the accounts, both the significant judgements that it has made in the process of applying the Council's accounting policies and information about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.</p> <p>Management should ensure that they maintain documented support for significant judgements and estimates made at the end of each accounting period.</p>	<p>That management review and put in place suitable arrangements to ensure that significant judgements and estimates are supported and documented to the same extent as all other significant transactions and accounting treatments recorded at the end of each financial year.</p> <p><b>Management response:</b> The significant changes in accounting regulations which came into force from April 2010 have required the collation of additional evidence and production of additional disclosures for the statement of accounts. We will continue to strive to meet all of these requirements and the additional documentation will be built into the closure process for 2012/13.</p>

\* response provided by Vic Godfrey (ICT Manager) April 2012

## B The small print

ISAUK 260 requires communication of:

- relationships that have a bearing on the independence of the audit firm and the integrity and objectivity of the engagement team
- nature and scope of the audit work
- significant findings from the audit

### Purpose of report

This report has been prepared for the benefit of discussions between Grant Thornton, the Audit Committee of North Hertfordshire District Council and the Board (Council).

The purpose of this report is to highlight the key issues affecting the results of the Council and the preparation of the Council's financial statements for the year ended 31 March 2012.

This document is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK & Ireland) 260.

We would point out that the matters dealt with in this report came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements of the Council.

This report is strictly confidential and although it has been made available to management to facilitate discussions, it may not be taken as altering our responsibilities to the Council arising under the terms of our audit engagement.

The contents of this report should not be disclosed to third parties without our prior written consent.

### Responsibilities of the directors and auditors

The directors are responsible for the preparation of the financial statements and for making available to us all of the information and explanations we consider necessary. Therefore, it is essential that the directors confirm that our understanding of all the matters in this memorandum is appropriate, having regard to their knowledge of the particular circumstances.

### Clarification of roles and responsibilities with respect to internal controls

The Council's management is responsible for the identification, assessment, management and monitoring of risk, for developing, operating and monitoring the system of internal control and for providing assurance to the Council that it has done so.

The Audit Committee is required to review the Council's internal financial controls. In addition, the Audit Committee is required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk.

The Audit Committee should receive reports from management as to the effectiveness of the systems they have established as well as the conclusions of any testing conducted by internal audit or ourselves.

We have applied our audit approach to document, evaluate and assess your internal controls over the financial reporting process in line with the requirements of auditing standards.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you.

In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify.

We would be pleased to discuss any further work in this regard with the Audit Committee.

### Independence

Ethical standards require us to give you full and fair disclosure of matters relating to our independence. In this context, we disclose the following to you:

- the appointed engagement lead and audit manager are subject to rotation every seven years;
- Grant Thornton, its partners and directors and the audit team have no family, financial employment, investment or business relationship with the Council; and
- our fees paid by the Council do not represent an inappropriate proportion of total fee income for either the firm, office or individual engagement lead.

In accordance with best practice, we analyse our fees below:

Statutory audit	£114,136
Certification of claims and returns	£25,000*
<b>Total</b>	<b>£139,136</b>

\* the quoted fee for certification work is an estimate only and will be charged at published hourly rates.

### Audit quality assurance

Grant Thornton's audit and assurance practice is currently monitored by the Audit Inspection Unit, an arm of the Financial Reporting Council, which has responsibility for monitoring the firm's public interest audit engagements.

The audit and assurance practice is also monitored by the Quality Assurance Directorate of the ICAEW and Grant Thornton conducts internal quality reviews of engagements.

Furthermore, audits of public interest bodies are subject to the Audit Commission's quality review process.



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