

Annual Governance Report Addendum

London Borough of Tower Hamlets

Audit 2009/10

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Addendum AGR

Introduction

1 My work on the audit of the Council's financial statements has continued since I drafted my Annual Governance Report. This work has identified matters I need to bring to your attention. This addendum should be read in conjunction with my Annual Governance Report delivered to the Audit Committee on 21 September 2010. The attached appendices show the final position on amendments made to the accounts and unadjusted mis-statements.

2 My work is now complete and I intend to give an unqualified opinion on the accounts on 6 October 2010.

Main conclusions

Income and expenditure

3 My testing of Income found internal recharges that were incorrectly included in the accounts. Further work undertaken by officers identified that Income and Expenditure were both overstated by £12,484k. Management has corrected the accounts for this error.

Barkantine combined heat and power plant

4 The Council has not recognised the Barkantine Combined Heat and Power plant on its balance sheet. The scheme was identified as falling under IFRIC 12 in the report prepared by the Council's PFI advisors, suggesting that it should be brought on balance sheet in 2009/10.

5 I accept that there is uncertainty surrounding the treatment of this asset and I have assurance that the amount involved is not material in 2009/10. Moving forward, the Council should review this agreement and provide working papers for audit review to support the treatment adopted in the 2010/11 accounts.

Uncertainties

6 I found differences between the general ledger and the supporting debtors systems:

- the debtors ledger includes £758k which is not on the general ledger and has not been included in the debtors figure in the accounts and
- the housing benefit overpayment debtor included in the accounts is £2,456k more than the value reported by the Council's housing benefit system. Debtors may be overstated by this amount. Council officers are liaising with the system provider to establish the reason for the difference.

7 My testing of payroll expenditure at outsourced schools identified a difference of £55k between the Council's general ledger and the data provided by the school's payroll provider. I have extrapolated this error across the other schools with outsourced payroll providers and the possible error value is £337k.

8 These are uncertainties therefore no adjustments have been made to the accounts for these items. Reconciliations are key controls which give assurance over the integrity of the data in financial systems. Officers should investigate and resolve all reconciliation differences as part of the closedown process.

Recommendation

R1 As part of the 2010/11 closedown process, ensure that internal recharges are excluded from the financial statements.

R2 Review the accounting treatment of the Barkantine Combined Heat and Power plant for the 2010/11 financial statements.

R3 Ensure all reconciliations between underlying systems and the general ledger are completed at the year end and investigate any differences.

Appendix 1 Amendments to the draft accounts

I identified the following misstatements during my audit and officers have made the necessary adjustments. I bring them to your attention to aid you in fulfilling your governance responsibilities.

Table 1:

Description of adjustment	Income & Expenditure		Balance Sheet	
	Dr £k	Cr £k	Dr £k	Cr £k
Correctly account for two assets which are not owned by the Council but were on the balance sheet. The assets were revalued in year and then removed as disposals from the balance sheet.			700	
		700		
Post the impact of a schools valuation adjustment to the income and expenditure account.	3,717			3,717
Remove a prior period adjustment made in error.			2,710	
				2,710
Post movements on earmarked reserves to the income and expenditure account.	329			329
Include the pre-service transfer element of the pension liability of Tower Hamlets Homes within the balance sheet.	17,959			17,959
Correct an error in the calculation of Council Tax receivable in the year.	598			598
Income and expenditure were overstated due to the inclusion of internal re-charges	12,484			
		12,484		

Other adjustments to the notes to the accounts	£k
Note 20 - Fixed Assets	
The write down of assets demolished was accounted for as a disposal instead of as an impairment.	10,718
Land which had previously held HRA dwellings was not reclassified to other land and buildings when the HRA dwellings were demolished.	4,594
The write down of the value of assets included in a stock transfer was treated as a disposal instead of as an impairment.	6,842
Revaluations and impairments were shown net in note 20 instead of gross as required by SORP:	
impairments	54,004
revaluations	54,004
(Since we reported to the Audit Committee on the 21st September, the Council has undertaken further work on the impairments and revaluations. As a result the amendments made to the accounts have changed. This table has been updated to reflect the revised amendments.)	
Note 31 - Financial Instruments	
The following balance sheet financial instruments were omitted from the financial instruments note:	
Debtors	15,879
Creditors	44,314
Cash	37,010
The credit risk section of the financial instruments note has been amended:	
Debtors	17,240
Debtors past due but not impaired	3,028
Note 57 - Prior Period Adjustments	
A reclassification of borrowing from long term to short term was incorrectly included as a PPA.	2,710
Note 48 - Capital Adjustment Account	
Revenue expenditure financed by capital under statute (REFCUS) and amortisation were shown net as opposed to gross as required by the SORP:	
REFCUS	15,045
Amortisation	1,374
Statement of Total Recognised Gains	
surplus/ deficit on the income and expenditure account	2,790
surplus/ deficit arising from revaluations	2,303
other gains and losses	598

Note 47 - Pension Schemes

The actuarial losses in this note did not agree to the statement of total recognised gains and losses. 16,693

Appendix 2 Unadjusted misstatements in the accounts

I identified the following misstatements during my audit, but management has not adjusted the financial statements. I bring them to your attention to help you in fulfilling your governance responsibilities. If you decide not to amend, please tell us why in the representation letter. If you believe the affect of the uncorrected errors, individually and collectively, is immaterial, please reflect this in the representation letter. Please attach a schedule of the uncorrected errors to the representation letter.

Description of error	Accounts affected	Value of error £ '000
As part of a reconciliation exercise the Council has identified a number of assets not currently included within the balance sheet fixed assets figure. A provisional valuation provided by the Council's internal valuer indicates that the value of these assets is £4.2m.	Balance Sheet: - Fixed Assets - Revaluation Reserve	4,515
The Council have guaranteed to pay £1.3m of pension liabilities relating to the post-transfer service of Tower Hamlets Homes. This should be accounted for as a provision under FRS12. The Council have chosen to account for this as a pension liability under FRS17, along with the pre transfer service amount.	Balance Sheet: - Pension Liability - Pension Reserve - Provisions Income and Expenditure Account: - Net Cost of Services	1,300
The Council employed external consultants to review their leases. The consultants identified finance lease liabilities which the Council has accounted for as operating leases.	Balance Sheet: - Fixed Assets - Short Term Borrowing - Long Term Borrowing Income and	188

Description of error	Accounts affected	Value of error £ '000
	Expenditure Account: - Net Cost of Services - Interest Payable	
<hr/> Note 10 - Private Finance Initiative Schemes	- Short term liability overstated	321
	-Long term liability understated	321

Appendix 3 Draft letter of representation

Jon Hayes
District Auditor
Audit Commission
1st Floor,
Millbank Tower,
Millbank, London,
SW1P 4HQ
X October 2010

London Borough of Tower Hamlets - Audit for the year ended 31 March 2010

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of the London Borough of Tower Hamlets, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2010. All representations cover the Council's Accounts, Group Accounts and Pension Fund Accounts included within the financial statements.

Compliance with the statutory authorities

I acknowledge my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom: A Statement of Recommended Practice which give a true and fair view of the financial position and financial performance of the Council and for making accurate representations to you.

Uncorrected misstatements

I confirm that I believe that the effects of the uncorrected financial statements are not material to the financial statements, either individually or in aggregate. These misstatements have been discussed with those charged with governance within the Audit Committee and the reasons for not correcting the items are as follows;

- We have not recognised the value of 13 assets identified in year on our balance sheet. We do not regard this decision as having a material impact on our financial statements.

- We recognise that we have accounted for three finance leases as operating leases. We do not regard this decision as having a material impact on our financial statements.
- £1.3m of provisions relating to a guarantee arrangement with Tower Hamlets Homes have been accounted for as pension liabilities under FRS17, rather than under FRS12. We do not regard this decision as having a material impact on our financial statements.
- We have not accounted for the Barkantine combined heat and power plant on balance sheet. We will review the accounting treatment of this asset in 2010/11. We do not regard this decision as having a material impact on our financial statements.
- The long and short term liabilities for the Private Finance Initiatives are misclassified. We do not regard this decision as having a material impact on our financial statements.

Supporting records

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Council have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Council meetings, have been made available to you.

Irregularities

I acknowledge my responsibility for the design and implementation of internal control systems 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; or
- communications from regulatory agencies concerning non-compliance with, or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

I also confirm that I have disclosed:

- my 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; and
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

Law, regulations, contractual arrangements and codes of practice

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the Council.

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. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

Fair Values

I confirm the reasonableness of the significant assumptions within the financial statements.

Assets

The following have been properly recorded and, where appropriate, adequately disclosed in the financial statements:

- losses arising from sale & purchase commitments;
- agreements & options to buy back assets previously sold; and
- assets pledged as collateral.

Compensating arrangements

There are no formal or informal compensating balancing arrangements with any of our cash and investment accounts. Except as disclosed in notes 31 and 32 to the financial statements we have no other lines of credit arrangements.

Contingent liabilities

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements; and
- no financial guarantees have been given to third parties other than the guarantee already disclosed in the financial statements.

Related party transactions

I confirm the completeness of the information disclosed regarding the identification of related parties.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements

Post balance sheet events

Since the date of approval of the financial statements by the Council, no additional significant post balance sheet events have occurred, other than the disclosure relating to pension liabilities, which would require additional

adjustment or disclosure in the financial statements other than those items already disclosed.

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.

Specific representations

I have considered the Council's long-term contracts in line with IFRIC 12 and other relevant financial reporting standards and confirm that, other than those already disclosed in the accounts, these are not considered to include leases, service concession arrangements or any embedded derivatives that would require separation from the host contract.

Signed on behalf of the London Borough of Tower Hamlets.

I confirm that the this letter has been discussed and agreed by the Council on [date]

Signed

Name

Position

Appendix 4 Action Plan

Recommendations

Recommendation 1

As part of the 2010/11 closedown process, ensure that internal recharges are excluded from the financial statements.

Responsibility	Chief Accountant
Priority	Medium
Date	By 30 June 2011
Comments	Transactions will be reviewed to ensure that internal recharges do not gross up expenditure or income.

Recommendation 2

Review the accounting treatment of the Barkantine Combined Heat and Power plant for the 2010/11 financial statements.

Responsibility	Chief Accountant
Priority	Medium
Date	By 30 June 2011
Comments	Accounting treatment will be reviewed and approach agreed with auditors prior to closing accounts.

Recommendation 3

Ensure all reconciliations between underlying systems and the general ledger are completed at the year end and investigate any differences.

Responsibility	Chief Accountant
Priority	High
Date	By 30 June 2011
Comments	Systems reconciliations will be reviewed during the year to ensure differences are investigated and corrected.

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