

## BABERGH DISTRICT COUNCIL

<b>From: Director of Finance</b>	<b>Report Number: L69</b>
<b>To: Overview and Scrutiny (Stewardship) Committee</b>	<b>Date of meeting: 22 September 2011</b>

### STATEMENT OF ACCOUNTS 2010/11 AND AUDITOR'S GOVERNANCE REPORT

#### 1. Purpose of Report

- 1.1 To advise Members on the position on the Statement of Accounts for 2010/11 and consider the external auditor's Annual Governance Report.
- 1.2 To note the changes that have been made since the draft accounts were produced and that the final audited Statement of Accounts will be presented to Council on 27 September 2011 for approval.

#### 2. Recommendations

- 2.1 That the Committee considers and notes the external auditor's Annual Governance Report for 2010/11, as attached at Appendix A.
- 2.2 That the Committee notes the main changes since the draft accounts were completed in June, as set out in Appendix B and the revised core financial statements that have been produced following the completion of the audit, as set out in Appendix C.

The views and comments of the Committee will be reported to Council on 27 September 2011.

#### 3. Financial Implications

- 3.1 None, other than the revenue budget outturn position is confirmed, which is very similar to that reported to the Committee in July 2011:

General Fund - £421k saving compared to the budget

Council Housing (HRA) - £209k saving compared to the budget

- 3.2 In addition and as also reported in July 2011, there are a number of budgets that have been carried forward into this year and these are being monitored as part of the quarterly performance and finance reports to Members.

#### 4. Risk Management

- 4.1 This report is most closely linked with the Council's Corporate / Significant Business Risk No. 6, Performance and Cost Management. Key risks are set out below:

Risk Description	Likelihood	Impact	Mitigation Measures
Material misstatements in the accounts or non-compliance with accounting requirements, resulting in a possible 'qualified' audit opinion or unfavourable audit report.	Low	Marginal	Unqualified 'true and fair' opinion from the external auditors as a result of: <ul style="list-style-type: none"> <li>• Clear arrangements in place for ensuring compliance with other accounting requirements.</li> <li>• Analytical review of 2010/11 outturn against previous year and the Budget.</li> <li>• Discussion on key issues with the auditors.</li> </ul>
Issues or concerns raised by the public from the right to inspect the accounts	Low	Marginal	Open and transparent arrangements and publication of the public's right to inspect the accounts. No issues have arisen.

## 5. Consultations

5.1 None.

## 6. Equality and Diversity Impact

6.1 None.

## 7. Shared Service / Partnership Implications

7.1 None.

## 8. Key Information

8.1 The draft Statement of Accounts for 2010/11, subject to audit, was presented to the Committee in July 2011.

8.2 The audit has now been completed by PKF, the Council's external auditors and their Annual Governance Report is attached at Appendix A. this covers their:

- opinion on the accounts
- view on the Council's key financial systems and annual governance statement
- conclusion on the council's arrangements to achieve value for money

- 8.3 Richard Bint, Senior Partner from PKF, will present the report and answer Members questions.
- 8.4 In terms of the Statement of Accounts, officers have discussed the various changes and matters arising from the audit with PKF and agree with the findings in their report.
- 8.5 The changes to the accounts largely arise from the complexities of the transition to IFRS, which the auditors believe the Council has effectively managed.
- 8.6 The final core financial statements and the revised explanatory foreword to the accounts are attached in Appendix B and details of the main changes that are included are set out in Appendix C.
- 8.7 The full audited Statement of Accounts for 2010/11 will be presented to Council on 27 September 2011 for approval.

**9. Appendices**

Title	Location
A - Annual Governance Report for 2010/11	Attached
B - Main Changes to Core Financial Statements	Attached
C - Revised Core Financial Statements 2010/11 and additional note 2	Attached
D – Revised Explanatory Foreword	Attached

**10. Background Documents**

10.1 None.

**Authorship:**

Name Barry Hunter  
 Job Title Director of Finance

Tel. 01473 825819  
 Email:  
 barry.hunter@babergh.gov.uk

Name Sue Smith  
 Job Title Acting Corporate Finance Manager

Tel. 01473 825816  
 Email:  
 sue.smith@babergh.gov.uk



Accountants &  
business advisers

**Babergh District Council**

**Annual Governance Report**

**2010/11**

September 2011

## Contents

1	Executive summary .....	1
2	Introduction.....	2
3	Financial statements.....	4
4	Value for Money conclusion .....	15

## Appendices

- A Action plan
- B Draft letter of representation
- C Uncorrected misstatements
- D Draft independent auditors' report

### **Code of Audit Practice and Statement of Responsibilities of Auditors and Audited Bodies**

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission contains an explanation of the respective responsibilities of auditors and of the audited body. Reports and letters prepared by appointed auditors are addressed to members or officers. They are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.

# 1 Executive summary

- 1.1 This report sets out our findings from the audit of Babergh District Council ('the Council'). Auditing standards and the *Code of Audit Practice* require that we report to those responsible for financial governance and financial reporting (those charged with governance) the key findings of our audit of the accounts and use of resources prior to issuing our opinion on the financial statements and value for money conclusion.

## Findings and conclusions

- 1.2 A summary of the audit findings and conclusions is included in the table below:

Area of audit	Findings & Conclusion
<b>Financial statements</b>	
<b>Financial statements</b>	<p>No material errors were identified as a result of audit work.</p> <p>Some non-trivial but not material errors have been identified and these are detailed in Appendix C.</p> <p>The Council has effectively managed the transition to financial reporting under International Financial Reporting Standards (IFRS) and correctly restated comparative figures in the financial statements.</p> <p><b>Some areas of work are still outstanding at the time of drafting this report.</b> Should these result in any significant issues, we will give an oral update to the Overview and Scrutiny (Stewardship) Committee.</p> <p><b>Subject to satisfactory completion of the outstanding work, we anticipate issuing an unqualified "true and fair" opinion.</b></p>
<b>Annual governance statement</b>	We are satisfied that the Annual Governance Statement (AGS) is not inconsistent or misleading with other information we are aware of from our audit of the financial statements.
<b>Key financial systems</b>	<p>Overall, no significant control deficiencies were identified during the course of our audit. We noted an area where deficiencies in internal controls should be improved or where the control environment could be strengthened, for example:</p> <ul style="list-style-type: none"> <li>National Non-Domestic Rate (NNDR) refunds were authorised by staff outside of their delegated limit.</li> </ul>
<b>Value for Money conclusion</b>	
<b>Value For Money conclusion</b>	<p>We are satisfied that, in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2011. This is based upon the following two Audit Commission criteria:</p> <ul style="list-style-type: none"> <li>The organisation has proper arrangements in place for securing financial resilience;</li> <li>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</li> </ul> <p><b>We anticipate issuing an unqualified value for money conclusion.</b></p>

## Acknowledgement

- 1.3 We would like to thank Council staff for their co-operation and assistance during the audit and throughout the period.

## 2 Introduction

- 2.1 This report summarises the results of our audit work completed to date in respect of the financial statements and arrangements to secure economy, efficiency and effectiveness in the use of resources for the year ending 31 March 2011.
- 2.2 Our report is presented to the Members in accordance with the provisions of International Auditing Standard 260 (“ISA 260”), which requires us to report key findings from the audit to “those charged with governance”, prior to issuing our opinion on the financial statements.
- 2.3 The contents of this report have been discussed and agreed with the Director of Finance.
- 2.4 We have reported verbally to management other non-significant findings from our audit in accordance with ISA (UK & Ireland) 265 Communicating deficiencies in internal control to those charged with governance and management.

### Findings

- 2.5 Recommendations in response to the key findings identified by our audit of the financial statements are provided in the action plan at Appendix A. These recommendations have been discussed with appropriate officers and responses are included in the action plan where appropriate.
- 2.6 We would highlight that in this report we do not provide a comprehensive statement of all weaknesses that may exist in the financial and operational systems, but only those matters which have come to our attention as a result of the audit procedures performed. We have not restated weaknesses already reported by Internal Audit unless these are significant weaknesses.

### Fee outturn

- 2.7 The Audit Commission’s *Standing Guidance for Auditors* requires us to report the outturn fee position for the year against the budgeted fee included within your Audit Plan. The table below sets out this analysis:

Audit plan 2010/11	Planned fees £	Actual fees £
Financial statements	67,950	67,950*
Value for Money conclusion	33,300	33,300
Planning and reporting	11,350	11,350
<b>Subtotal audit</b>	<b>112,600</b>	<b>112,600</b>
Grants	36,000	36,000
<b>Total</b>	<b>148,600</b>	<b>148,600</b>

\* At the time of drafting our audit is not complete. Should any additional fees arise, we will discuss the matter with management and issue an updated fee outturn to the Overview and Scrutiny (Stewardship) Committee.

- 2.8 A number of the grant claim audits are currently in progress or do not require certification until 31 December 2011 and therefore the actual fee remains an estimate of the expected final position. The final position will be reported in our grants report to be issued in February 2012.

## Independence

- 2.9 We confirm that we are not aware of any relationships that may bear on our independence and objectivity as auditors and that our independence declaration, included in the Audit Plan for 2010/11, has remained valid throughout the period of the audit.



## 3 Financial statements

### Requirements

- 3.1 We are required to provide an opinion on whether your financial statements give a true and fair view of your financial position and income and expenditure and whether they have been prepared properly, in accordance with appropriate legislation and relevant accounting guidance.
- 3.2 We carry out procedures designed to obtain sufficient appropriate audit evidence to determine with reasonable confidence whether the financial statements are free from material misstatement and evaluate the overall presentation in order to ascertain whether they have been prepared in accordance with relevant legislation and accounting standards.
- 3.3 We identify the principal areas of risk of material misstatement from our knowledge of the Council, of the environment in which it operates and from discussions with management. We address these risks by carrying out appropriate audit procedures.
- 3.4 In carrying out our work we determine and apply a level of materiality. Consequently the audit cannot be relied upon to identify *all* risks or potential and actual misstatements. Materiality is the expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole, or specific individual elements of the financial statements as appropriate, such as the senior officer remuneration report.
- 3.5 We are also required to set a second level of materiality (known as “performance materiality”) which is to be used when planning and performing the audit. This has to be set at a level lower than the materiality for the financial statements as a whole so as to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole.
- 3.6 We are required to report to you all uncorrected misstatements that relate to the current financial year (including those arising in previous periods that have an effect on the current year financial statements) and the effect that they have individually, or in aggregate, on the auditors’ report, except for those that are clearly trivial. For reporting purposes, we consider misstatements of less than £15,000 to be trivial to the financial statements, unless the misstatement is indicative of fraud. We will request that any non-trivial uncorrected misstatements be corrected.

### Reporting to those charged with governance

- 3.7 We will report to you:
- our assessment of and response to **significant risks** in the financial statements
  - significant qualitative aspects of **accounting practices** including the application of the applicable financial reporting framework
  - significant difficulties that we have encountered during the course of the audit
  - significant matters discussed, or subject to correspondence with management or other employees
  - **written representations** that we are requesting from you which includes the final draft letter of representation to be agreed by management and those charged with governance
  - **material misstatements** that have been corrected by management
  - **uncorrected misstatements**
  - expected modifications to the **audit report**
  - significant deficiencies in **accounting and internal control systems** identified during our work
  - **matters required to be reported by other auditing standards**

- any **other audit matters of governance interest** relevant to the financial reporting process.

3.8 Our comments in these areas are set out in order below.

### ***Significant risks of material misstatement in the financial statements***

3.9 Auditing standards require that we bring to your attention areas that require additional or special audit consideration and are, therefore, considered a significant risk. These may include weaknesses in controls or areas requiring a higher degree of judgement by management.

3.10 We reported to you our updated risk assessment in the 2010/11 Annual Audit Plan issued in December 2010. We have since undertaken a more detailed assessment of risk following our completion of the interim review of financial controls and review of the Council's draft financial statements, and concluded that there are no changes to the significant risks previously reported.

3.11 The findings from our review of financial statements risks and other areas of audit focus identified in our Audit Plan are summarised below:

#### **Management override**

3.12 Management override refers to the ability of management to manipulate accounting records and prepare fraudulent financial statements by overriding what might appear to be effective internal controls. Management is in a unique position to perpetrate or conceal the effects of fraud through recording fictitious journal entries, inappropriately adjusting assumptions and changing judgments used to estimate account balances, engaging in complex transactions that are structured to misrepresent the financial position, and altering records and terms related to significant and unusual transactions. Therefore, we are required to consider management override of controls to be a significant risk in all audit engagements under auditing standards as discussed in our Audit Plan.

3.13 Our review of management journals and accounting estimates did not indicate any material management bias or override of controls in preparing the financial statements.

3.14 We have reviewed material accounting estimates identified as having high estimation uncertainty or subject to a significant degree of judgement and further detail is provided in the section on Appropriateness of management accounting estimates below.

#### **Implementation of International Financial Reporting Standards (IFRS)**

3.15 The introduction of IFRS as the financial reporting framework for local authorities is both a significant change in terms of accounting treatment and in the overall presentation of the financial statements. It requires a review of material classes of transactions, balances and disclosures where the accounting treatment differs from that previously recognised under the UK GAAP based SORP. This requires restatement of the opening balances at 1 April 2009, restatement of the 2009/10 accounts and review of the correct accounting treatment of transactions in 2010/11.

3.16 The Council has put in place appropriate arrangements to adopt IFRS and to restate its previous UK GAAP based accounts. Our review confirmed that it has appropriately applied IFRSs in the production of its financial statements, including changes in accounting standards, new format of the financial statements, additional disclosure requirements and restated comparative information, although some amendments to the draft financial statements have been made during the course of the audit.

3.17 The Council has not disclosed the 1 April 2009 balances within the notes to the financial statements as required by IFRS 1. There are some notes such as property, plant and equipment where this information is disclosed to reconcile opening and closing balances, but

there are other notes such as debtors and creditors where this information has not been disclosed. No amendments have been made to the financial statements for this omission, however, this non-compliance does not impact on our audit opinion.

### **Group accounting**

- 3.18 IFRS places greater emphasis on the ability to control rather than actual control in deciding whether entities should be included in group accounts of a parent entity.
- 3.19 The Council has reviewed its interests in other entities and concluded that it does not have significant influence over any other organisation by way of power to participate in their financial and operating policies that would have a material impact on its financial statements.
- 3.20 We are satisfied that there is no requirement for group financial statements to be prepared after a detailed review of the documentation relating to the the South Suffolk Leisure Trust.

### **Government grants and other contributions under IPSAS23**

- 3.21 Grants and contributions for revenue and capital purposes are now required to be recognised as income immediately rather than being deferred and released to revenue to match expenditure or depreciation, where grant conditions have been met or there is a reasonable assurance that grant conditions will be met.
- 3.22 The Council has reviewed its grants income and balances previously held in a 'Government grants deferred account' and an 'Unapplied grants and contributions account' balance under UK GAAP and has reversed amounts that do not qualify for recognition as receipts in advance to the Capital Adjustment Account.
- 3.23 Our work on this area remains on-going at the time of drafting this report and an oral update will be given to the Overview and Scrutiny (Stewardship) Committee should any matters arise.

### **Municipal Mutual Insurance (MMI) case**

- 3.24 Recent developments regarding the MMI case, which resulted in the Courts ruling against the Council in the appeal, could expose the Council to potentially significant additional costs. This issue is currently disclosed as a contingent liability within the statement of accounts, but the accounting treatment is determined on the likelihood of success or failure of the Council's future legal hearing.
- 3.25 A provision of £76,500 has been included within the financial statements as at the year end to cover the legal costs of this legal case. There are is also a receipt in advance balance for the costs already awarded and received by the Council in relation to the first in the likelihood they will have to be repaid. An earmarked reserve has also been established within reserves should further costs arise.
- 3.26 As part of our audit work we have reviewed the legal correspondence and reports produced by the Council. Our conclusion on this matter is outstanding awaiting further information from the Council's legal Counsel and an oral update will be given to the Overview and Scrutiny (Stewardship) Committee.
- 3.27 Additional comments have been added to the contingent liability note in the draft financial statements to highlight that if the Council loses the forthcoming appeal case then it will be uninsured for claims made against the Council with an unquantifiable liability.

## **Accounting practices**

### **Application of accounting policies**

- 3.28 The key change introduced by the 2010 Code of Practice on Local Authority Accounting in the United Kingdom was the introduction of an IFRS based set of financial statements, resulting in a number of significant changes in accounting practice:

- Grants and contributions for capital purposes will be recognised as income immediately rather than being deferred and released to revenue to match depreciation, where grant conditions have been met
- The main financial statements have changed, and there are additional requirements regarding segmental reporting
- There is a greater emphasis on component accounting, and a greater emphasis on derecognising parts of an asset that are replaced
- Property leases are classified and accounted for as separate leases of land and buildings. Local Councils will also need to assess whether other arrangements contain the substance of a lease
- Impairment losses will be taken initially to the revaluation reserve to the extent that there is a balance on that reserve relating to the specific asset
- The Code introduces a new classification of non-current assets held for sale. Specific criteria apply to this classification
- All employee benefits are accounted for as they are earned by the employee. This will require accruals for items such as holiday pay
- The definition of associates is based on the ability to control rather than actual control, and may lead to a change in the group boundary.

3.29 Complications arose in the following areas:

#### **Cashflow statement**

3.30 The presentation of the cashflow statement has changed significantly since the prior year. We were unable to audit the re-statement of the 2009/10 comparative in advance and working papers were provided during the course of the audit. The Council themselves identified that there were errors in the original draft accounts and provided updated information for audit review. This work is outstanding and there remains a £700k balancing figure within the 2010/11 cashflow that requires further investigation. Should any issues arise an oral update will be given to the Overview and Scrutiny (Stewardship) Committee.

#### **Leases under IFRIC 4 (lease type arrangements) and IAS 17 (leases)**

3.31 IAS 17 increases the qualitative criteria to be applied in assessing whether a lease is a finance lease or an operating lease and requires that land and buildings are considered separately for the purposes of the lease calculations. IFRIC 4 requires arrangements or a series of transactions that convey the right to use an asset to be reviewed to assess whether they meet the definition of a lease in IAS 17 (and subsequent inclusion as a finance lease or operating lease).

3.32 The Council has reviewed its leases and other contractual arrangements and originally recognised the SERCO waste contract as falling within the scope of these types of arrangements. However, upon review of the contract and vehicle purchasing arrangements it was concluded that the waste vehicles are assets of the Council and therefore no change in accounting treatment was required as a result of the transition to IFRS.

#### **The financial statements preparation process**

3.33 The requirement for Members to approve the draft financial statements by 30 June was removed by the Accounts and Audit Regulations 2011, however these regulations did introduce the requirement for the Responsible Financial Officer to sign and present the financial statements for audit by 30 June 2011. The financial statements were signed on 30 June 2011 and presented for audit on 6 July 2011.

3.34 As part of our planning for the audit, we prepared a detailed document request which outlined the information that we would require to complete the audit. The Council provided us with files of working papers on 8 August 2011, in line with the agreed timetable, however

there were a number of key working papers omitted including the cash flow workings. The IFRS restatement note was not included in original draft financial statements and a copy not provided until 31 August 2011, this delayed the completion of the IFRS restatement audit work.

- 3.35 We appreciate all the help and assistance we have received during the audit given that there were unforeseen absences within the finance team and staff departures that put strain on the resources available to deal with audit queries. We will work with officers to ensure requirements are clear going forward and a process is in place to ensure timely clearance of queries raised.

### Testing of transactions and balances

- 3.36 As part of our audit approach, all material balances were subject to audit testing and agreement, on a sample basis, to supporting documentation. Issues arose in respect of the following matters, which we bring to your attention:

#### Amortisation of intangible fixed assets

- 3.37 Our testing of intangible fixed assets, which are assets such as software, found that two assets (out of ninety-two total assets held) were not being amortised (written down) over useful economic lives in accordance with the Council's accounting policy.
- 3.38 The accounting policy for intangible assets is to amortise assets on a straight line basis for a period of 5-7 years. The two assets chosen for testing were being written down over 11 years and it was confirmed with appropriate officers that the accounting policy accurately reflected the life of the Council's intangible assets.
- 3.39 This has resulted in an overstatement of intangible assets as at 31 March 2011 of £40,000 which is included as an unadjusted error within Appendix B. We recommend that the Council reviews all its intangible assets to ensure the carrying value is appropriate.

#### De-recognition of replaced components

- 3.40 Assets are valued on a Beacon basis which assumes a certain standard of condition. The Council had a depreciation policy of 44 years, now revised to 50 years, for dwellings though kitchens and bathrooms have a more frequent replacement cycle.
- 3.41 The Council replaced a number of kitchens and bathrooms during the financial year in its Council dwellings as part of on-going replacement programmes. No value has been de-recognised within the financial statements to show the accounting write out of the old component. The consequence is an overstatement of the asset value in the balance sheet, and an understatement of the deficit in the CIES.
- 3.42 A number of authorities have experienced difficulties with applying this particular principle of de-recognition and have adopted various approaches. The Council's view is that those assets replaced had no value because they were effectively scrapped. Whilst this maybe the economic reality, in accounting terms the Council are still carrying those components at a carrying value within the whole asset value and therefore an appropriate amount should be de-recognised.
- 3.43 An approximate value of £225,000 has been included within the unadjusted errors schedule at Appendix B.

#### Holiday pay accrual

- 3.44 IAS 19 requires that all employee benefits are accounted for as they are earned by the employee, which results in the recognition of employee accumulating compensated absences, such as untaken holiday pay, as an accrual in the financial statements.
- 3.45 The Council has accrued for short term accumulating compensated absences of £77,000 at 31 March 2011 and comparatives have also been restated to include estimated accruals.

- 3.46 We are satisfied that the Council has applied a reasonable approach for determining the value of untaken holiday pay and that the calculations and assumptions applied follow guidance issued by CIPFA.
- 3.47 However, the draft financial statements had initially included this amount in provisions and it should correctly be included in creditors as the amount is certain and earned. This has been amended within the revised financial statements.

## **Appropriateness of management accounting estimates**

### **Valuation of fixed assets**

- 3.48 Land and buildings are required to be carried at fair value which is either existing use value, depreciated replacement cost for specialised properties or open market value. The Council revalue Housing Revenue Account dwellings every five years using Beacon valuations and revalue other land and buildings on a five year cycle.
- 3.49 The Department for Communities and Local Government issued updated guidance in January 2011 that affected the value of the Council's dwelling stock. The social housing adjustment factor was revised from 46% to 39%, and is therefore significantly lower than the 2005 adjustment factor applied. The Council applied the new guidance as at 31 March 2011 as part of its annual impairment review for the updated valuation of Council dwellings and there was an overall reduction in the dwelling stock value of £28.2 million. The net effect after reversal of previous revaluation gains has been separately identified on the face of the Comprehensive Income and Expenditure Statement (CIES) due to the material nature of the adjustment.
- 3.50 The Council does not adjust for price indices on other land and buildings between formal valuations, which is accepted practice in the Code unless there has been a significant change in values.
- 3.51 The Council undertook a review of the useful economic life (UEL) of council dwellings, consulting with both the Council's valuers and other authorities. As a result the accounting policy has been revised from 44 years as at 31 March 2010 to 50 years as at 31 March 2011 thereby reducing the depreciation charge to the CIES.
- 3.52 The revised UEL being applied is considered to be appropriate and is within the average range being used by other authorities of 40-80 years. The Council should continue to keep this under review
- 3.53 It was identified during testing that the UEL of garage blocks have not had separate consideration. The UEL of garages has been amended in line with the council dwellings; this is not considered to be an appropriate method. Whilst the assets are similar, separate consideration should be given in the future to ensure the UEL is appropriate given the condition of the Council's assets.
- 3.54 Equipment assets, such as vehicles and information technology, are reasonably short-life assets and the depreciated carrying value is assumed to be a reasonable proxy for their fair value, without requiring any regular market valuation adjustments. We have reviewed the useful economic lives allocated to classes of equipment assets and are satisfied that they are not unreasonable.

### **Componentisation of fixed assets**

- 3.55 The implementation of IFRS also introduced the principle of componentisation of fixed assets. Each part of an item of property, plant and equipment that has a cost that is significant in relation to the cost of the whole item should be depreciated separately. This is so that that the depreciation charge reflects the potentially different economic lives of the main asset and its components. There is no definition of 'significant' within the guidance.
- 3.56 The Council has presently concluded that there are no significant components apart from leased heating within the Council dwellings though as no full valuation has taken place



componentisation does not yet apply to these assets under the Code. The accounting policy wording has been amended to show that this position is to be kept under review.

- 3.57 General Fund assets over £500k have been subject to componentisation and the Council have adopted a proactive approach to this area with early engagement with us on their proposals. No issues have been identified from our work in this area.

#### **Recoverability of debtor balances**

- 3.58 The Council makes allowance for the impairment of debtors based on an assessment of their recoverability. Management reviews all debts, and specific amounts that are considered to be unlikely to be recovered are included in the allowance for doubtful debts. We have reviewed the level of provision set aside for non-recovery of debt and the methodology applied by management for each type of debtor and are satisfied that these are reasonable and in line with the current collection rates and recoverability in the current economic conditions.
- 3.59 The previous year was the first year the Council provided for bad debts within sundry debtors. In the current year sundry debtors have again been included within the recoverability review undertaken by the Council and the provision has increased further from £33,000 to £54,000.

#### **Actuarial assumptions for the pension fund liability**

- 3.60 The pension fund liability attributable to the Council is subject to significant estimation based on expected rates of inflation, salary increases, pension increases, appropriate discount rates, option for retiring members to convert an element of pension into a lump sum, and mortality tables for life expectancy.
- 3.61 An actuarial estimate of the pension fund liability is calculated by an independent firm of actuaries with specialist knowledge and experience. The estimate has regard to local factors such as mortality rates and expected pay rises along with other assumptions around inflation.
- 3.62 Management has agreed the assumptions made by the actuary and these are included in the financial statements. We have requested written representations from the Council to confirm that the assumptions applied by the actuary are reasonable and consistent with the Council's knowledge of the business.
- 3.63 We are satisfied that the actuary is suitably independent of the Council, objective and experienced in undertaking this work. Our review of the assumptions applied in estimating the pension liability suggest that these are not significantly different from those being applied by the actuaries of other local authorities.
- 3.64 The Government in its budget on 22 June 2010 announced a move to using the Consumer Price Index (CPI) from the Retail Price Index (RPI) as the measure of price inflation for public sector pension schemes. This change has affected the valuation of the pension liability as CPI increases have generally been lower, and are anticipated to be lower, than RPI increases. The impact has in part led to the Past Service Gain which has been separately disclosed on the face of the Comprehensive Income and Expenditure Statement as an exceptional item.

#### **Adequacy of disclosures**

- 3.65 We identified a small number of departures from the expected presentation of the financial statements or where notes and other disclosures had not been presented in accordance with the Code. These have been amended by the Council.

#### **Written representations**

- 3.66 We are required by ISAs to obtain written confirmation from you of certain representations that have been made during the course of our audit. The draft letter of representation has

been attached as Appendix C. We do not anticipate any changes being required before providing our opinion on the financial statements.

### ***Identified misstatements***

3.67 As part of our audit approach, all material balances were subject to audit testing and agreement, on a sample basis, to supporting documentation. To assist you in fulfilling your governance responsibilities, which include maintaining oversight of the financial reporting process and the system of internal control we have set out below the misstatements identified during our audit.

### **Material misstatements corrected by management**

3.68 We did not identify any material misstatements during the course of our audit.

### **Uncorrected non-trivial misstatements**

3.69 We set out at Appendix B all of the non-trivial misstatements which we noted during the course of our audit and which management do not intend to adjust. We will provide an update at the Overview and Scrutiny (Stewardship) Committee meeting should we identify any additional items during the final clearance of outstanding issues.

3.70 We will obtain written representation from the Overview and Scrutiny (Stewardship) Committee of the reasons for not making these adjustments as noted in Appendix C.

### ***Audit report***

3.71 Subject to satisfactory resolution of the following outstanding issues and final clearance of the audit, we anticipate issuing an unqualified audit opinion on the accounts:

- Copies of documents from Legal Counsel on the MMI case
- Review of the cashflow balancing figure
- Clearance of outstanding queries with officers
- Clearance of Manager and Partner review points.

3.72 We will provide an oral update on these outstanding issues at the Overview and Scrutiny (Stewardship) Committee.

### ***Accounting and internal control systems***

3.73 We have reviewed the key financial systems, which contribute to the preparation of materially accurate financial statements, to assess the extent to which we can place reliance on them for this purpose. In carrying out this work we consider:

- the extent to which your accounting and internal control systems are a reliable basis from which to prepare the financial statements
- the robustness of your accounts preparation processes.

3.74 In assessing the reliability of systems as a basis for providing financial information that is free from material misstatement, we prepared systems notes for each financial system and we evaluated the controls within those systems, with particular focus on assessing whether the controls in place to mitigate significant risks are suitably designed and operating as intended to meet their objective.



3.75 Your key financial systems are:

- Main accounting
- Cash and bank
- Payments and creditors
- Non-contracting income and debtors
- Payroll and employment costs
- Information technology
- Council tax
- Housing and council tax benefits
- National Non Domestic Rates
- Housing rents income
- Investments and investment income

3.76 We also have a responsibility to give specific consideration to the potential risk of material misstatement of your financial statements due to fraud and error, including the risk of fraudulent financial reporting. This requires us to:

- review internal controls that are designed to prevent, or detect and correct, misstatements in the accounts
- review the arrangements for preparing the financial statements
- select and test transactions and balances, including review of significant balances against expectations and substantiate individual items
- assess the significant estimates and judgements made by officers in preparing the accounts
- consider the adequacy of presentation and disclosures included in the financial statements.

3.77 The primary responsibility for ensuring that your internal control frameworks are robust enough to prevent and detect material fraud and corrupt practices lies with management and those charged with governance.

### **Risks of material misstatement due to fraud**

3.78 In order to identify the fraud risks, and the controls you have put in place to mitigate those risks, we have:

- discussed your anti fraud and corruption arrangements with officers, and those charged with governance
- considered the extent to which the work of Internal Audit is designed to detect material misstatements in the accounts arising through fraud
- made enquiries regarding instances of actual fraud you have brought to our attention.

3.79 We did not identify any significant fraud risks that affected our audit programme for the financial statements.

### **Internal audit**

3.80 Where possible, we have sought to use Internal Audit's work and thereby avoided unnecessary duplication of audit effort. To ensure this approach was valid, we have undertaken the following:

- reviewed Internal Audit's working papers and reports
- considered the robustness of the key financial systems on the evidence of this work
- re-performed Internal Audit's evaluation of controls and a sample of its testing of the effectiveness of controls, to ensure that its conclusions are soundly based.

3.81 We were able to place reliance on Internal Audit's work for the testing of the effectiveness of specific controls.

### **Deficiencies identified**

3.82 We would like to draw to your attention the following matters arising from our review of the key financial and operational systems that we consider indicate the existence of deficiencies in the system of internal control.

3.83 In this respect please note that:

- the purpose of the audit was for us to express an opinion on the financial statements. Our audit is not designed to identify all deficiencies in the system of internal control nor to identify all improvements which might be necessary to address the deficiencies identified
- the audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control; and
- we report only those deficiencies that have come to our attention as a result of our audit work and that we have concluded are of sufficient importance to merit your attention.

### **Conclusions**

3.84 As a result of our work, we have concluded that the key financial systems are generally adequate as a basis for preparing the financial statements. No significant control deficiencies were identified as a result of our audit. We have included in Appendix A any recommendations arising from issues identified during our work.

3.85 We did not identify any significant fraud risks that affected our audit programme for the financial statements.

3.86 The following internal control issues have been identified and reported by Internal Audit during 2010/11:

#### ***National non-domestic rates (NNDR) empty property relief***

3.87 It was identified that empty/partially unoccupied properties are not being visited on an annual basis to confirm their status. There is the potential that the Council is not receiving NNDR income to which it is entitled. It was noted during our review of the testing that time constraints and lack of resources play a part in this control not being fully implemented.

3.88 It is recommended that the Council implement a policy that a sample properties claiming this relief are visited on a regular basis throughout the year. This has been previously reported by Internal Audit. We are aware that positive action has been taken in response to Internal Audit's recommendation with canvassing of empty properties and inspections being undertaken where no response has been received.

#### ***NNDR refund authorisation***

3.89 Internal Audit's testing highlighted that a member of staff was authorising NNDR refunds above their approved limit. We undertook additional testing on these breaches as part of our accounts audit and identified no issues.

3.90 It is acknowledged that high value refunds, including the refunds authorised above, are checked and evidenced as such by another officer prior to authorisation.

3.91 The Council has already reminded staff to adhere to authorised limits.

***Segregation of duties***

- 3.92 It was established during Internal Audit's review of key controls that back office staff who can update NNDR liability details are occasionally involved in front office duties such as receiving cash payments. There is the potential for staff to be able to raise NNDR liabilities on the system and receive the payment, leaving the process open to fraud.
- 3.93 It is recommended that a stricter segregation of duties is maintained in order to mitigate the risk of fraud. This has been previously reported by Internal Audit but is seen as low risk by the Council.

***Data security***

- 3.94 It has been identified there is a lack of clear understanding from managers as to what constitutes protected data and if Data Transfer Registers are being kept up to date. The potential is that the council could release protected data to an external source and give rise to litigation for a breach.
- 3.95 This has been previously reported by Internal Audit who have recommended that Managers either be provided with a simple guide as to their responsibilities or the matter be discussed and a way forward agreed collectively by them. See recommendation in Appendix A.
- 3.96 This is currently work in progress as part of the Babergh and Mid Suffolk Integration (BMI) process to align policies and procedures. In addition, measures are to be identified to better track use of Data Transfers.

***Matters required to be reported by other auditing standards***

- 3.97 There are no other matters arising from our work that we are required by other auditing standards to bring to the attention of those charged with governance.

***Other audit matters of governance interest******Annual governance statement***

- 3.98 The Council has a responsibility to publish an Annual Governance Statement, including the outcome of a review of its effectiveness, with its 2010/11 financial statements.
- 3.99 We have reviewed the Annual Governance Statement and the supporting review of effectiveness that has been undertaken and we are satisfied that the Statement is not inconsistent with the evidence provided in the review of effectiveness and our knowledge of the Council.

## 4 Value for Money conclusion

- 4.1 We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (value for money, or “VFM”).

### VFM risks

- 4.2 The findings from our review of use of resources risks identified in our Annual Audit Plan are summarised as follows:

#### *Financial pressure*

##### **Financial resilience**

- 4.3 Along with all other Councils, Babergh District Council was notified of a reduction in central government revenue funding of 11% (or £703,000) in 2011/12<sup>1</sup>, a 14% reduction in 2012/13 and further reductions in subsequent years. Saving and efficiency initiatives have been identified to fund the gap in 2011/12, partly through greater integration with Mid Suffolk District Council and operating a shared management team and through a review of discretionary funding areas. The Council has a track record of achievement with significant savings being achieved in 2010/11 through vacancy management arrangements, which remain on-going in 2011/12, as well as other initiatives.
- 4.4 Forecast spending reductions are 7.9% or £1.1m in 2011/12<sup>2</sup> which is in line with other District Councils across the Country as all local authorities are facing similar financial pressures. The Council applied for capitalisation in order to fund redundancies for the 2010/11 financial year and this was utilised against the outgoing Chief Executive’s additional pension strain costs. A further £750k request has been approved for 2011/12 to fund pension elements of redundancy costs from the next phase of integration with Mid Suffolk District Council.

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

- 4.5 The savings required for 2012/13 is forecast at £1.3m and the Council are consulting with the public to identify priority and non-priority areas of spend to inform savings plans. The total savings required over the three year period for Babergh alone are forecast at £3.5m compared to the 2011/12 budget. This is a significant amount in the context of the Council’s annual budget.
- 4.6 Members have a clear understanding of the Council’s financial challenge and are supportive of officers in the budgetary process and on-going financial management. 2011/12 is very much seen as a year of consolidation by both members and officers to prepare for the medium term and focus on the integration and transformation programme with Mid Suffolk.

#### *Integration with Mid Suffolk District Council*

- 4.7 We have been reviewing the plans and proposals surrounding the integration with Mid Suffolk District Council throughout the financial year. Progress has been monitored through our regular liaison with key officers, review of Committee papers and also contact has been maintained with the Auditor of Mid Suffolk District Council.
- 4.8 The Council produced a Detailed Business Case (DBC) in September 2010 covering both integration of staff and services, and merger. The plan was updated particularly for financial information in March 2011.
- 4.9 Independent external advisors were appointed by the Council to carry out a review of the DBC and their report was produced at the same time as the updated DBC. They were asked

---

<sup>1</sup> Source: CLG – RA and SSG returns 2010/11 and 2011/12

<sup>2</sup> Source: Audit Commisison Financial Resillience Survey

to validate the key assumptions costs and savings in the DBC, and assess the key risks, and applied their own financial model to the data to validate it.

- 4.10 We reviewed both the DBC and the external validation report and identified no issues with the DBC. The report, whilst finding the DBC robust made a number of comments regarding the plans, the key ones being:
- they saw scope for additional cost savings over those in the DBC;
  - they saw IT integration as a significant risk;
  - the Housing Revenue Accounts should be integrated.

The Council should ensure the comments are pursued.

- 4.11 The Council appointed a Joint Chief Executive with Mid Suffolk District Council in May 2011. We have reviewed the redundancy costs relating to Babergh’s out-going Chief Executive from the perspectives of Use of Resources consideration and lawfulness. The costs were shared on a straight 50/50 basis with Mid Suffolk, though the costs in relation to each Chief Executive were not significantly dissimilar. Further consideration is being undertaken as to whether this principle will apply to savings and costs going forward including the next phase of integration where costs (and savings) will be significantly higher.
- 4.12 The next phase is to integrate management teams and services and a number of Service Integration and other workstreams have been established to meet this desired end. The proposal is to reduce the Senior Management Team from eight to five, however, the original timetable has slipped slightly on this phase with the process now due to be concluded late Autumn.
- 4.13 To further support the integration plans, both councils invited staff to apply for voluntary redundancy to contribute towards the joint integration savings that are being sought of around £1m a year. A number of applications were approved in August 2011. The overall business case for integration and transformation is currently being reviewed and this will be submitted to Members later this year.
- 4.14 The new Chief Executive has set out a vision to be “The best of the best” to support the new joint management team and integration/transformation proposals. The principles behind the proposals are to create a joint management team that has the capacity and flexibility to meet the challenges facing local authorities, facilitate wider partnership working and transforming how the council operates. Changes are expected to be made quickly to maximise savings and ensure innovation and best practice is applied across both authorities through shared knowledge and expertise.

### VFM conclusion

- 4.15 Our VFM conclusion is based on considering our preliminary judgements from the review of arrangements to deliver against the Code criterion and the results of risk based audit work, as well as consideration of the processes underpinning your review of the effectiveness of your controls as described in your Annual Governance Statement.
- 4.16 The table below sets out our conclusions for each of the VFM Code criteria:

	Code criterion	Criterion met
1	The organisation has proper arrangements in place for securing financial resilience.	Yes
2	The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.	Yes

***Overall conclusion***

- 4.17 Our overall conclusion is that adequate arrangements are in place to secure value for money.

## Appendix A: Action Plan

Conclusions from work	Recommendations	Priority	Management response	Responsibility	Timing
<b>Financial statements</b>					
An incomplete set of working papers was available at the start of the audit.	<ol style="list-style-type: none"> <li>1. Ensure all the documents requested within the Records Required Listing are provided at the start of the audit.</li> <li>2. Ensure that there is a breakdown of debtors and creditors balances held at the year end that make up the value of the balance included within the financial statements</li> </ol>	Medium	<p>Acknowledged</p> <p>Determine whether a separate environment can be created to isolate year end information</p>	Corporate Finance Manager/ Finance Operations Manager	Q4 2011/12
Intangible assets were not being amortised in accordance with the Council's accounting policy.	<ol style="list-style-type: none"> <li>3. The Council should review all intangible assets to confirm they are in use and the carrying value is appropriate.</li> </ol>	Medium	2 assets (out of 92 intangible assets) relating to long term projects were previously amortised correctly over a longer period. The remaining life should have been reviewed in 2010/11 due to organisational changes and the assets will be relifed in 2011/12 to reflect a more realistic remaining life	Corporate Finance Manager/ Corporate Accountant	September 2011
The Council has not attributed any value to the components such as kitchens and bathrooms replaced during the financial year and therefore the assets are potentially overstated.	<ol style="list-style-type: none"> <li>4. The Council should determine an appropriate derecognition policy and ensure that amounts are removed from the financial statements.</li> </ol>	High	To be investigated and evaluated in conjunction with PKF	Corporate Finance Manager/ PKF	Q3/4 2011/12
<b>Financial systems</b>					
All issues were raised by Internal Audit therefore recommendations have not been re-raised other than that relating to data security.	<ol style="list-style-type: none"> <li>5. We recommended that Managers either be provided with a simple guide as to their responsibilities or the matter be discussed and a way forward agreed collectively by them.</li> </ol>	High	This is currently work in progress as part of the BMI process to align policies and procedures. In addition, measures are to be identified to better track use of Data Transfers.	Kevin Peck	Q4 2011/12

## Appendix B: Uncorrected misstatements

The table below details the potential differences recorded during the audit that have not been adjusted for within the financial statements:

Uncorrected misstatements	Income Over/ (Under) £'000	Expenses (Over)/ Under £'000	Assets (Over)/ Under £'000	Liabilities Over/ (Under) £'000	Reserves Over/ (Under) £'000
<b>Factual misstatements</b> Being the understatement of amortisation for intangible assets being written down over the incorrect period.		40	(40)		
<b>Judgemental misstatements</b> Being the approximate overstatement of Council dwelling value for the non de-recognition of kitchens and bathrooms replaced in the year.		225	(225)		
<b>Projected misstatements (extrapolation of errors)</b>					
<b>Total net misstatements</b>		265	(265)		
- Net understatement of costs					
- Net overstatement of net assets					



## Appendix C: Draft letter of representation

PKF (UK) LLP  
16 The Havens  
Ransomes Europark  
Ipswich  
Suffolk  
IP3 9SJ

XX September 2011

Dear Sirs

### Financial statements of Babergh District Council for the year ended 31 March 2011

This representation letter is provided in connection with your audit of the financial statements of Babergh District Council for the year ended 31 March 2011 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view, have been properly prepared in accordance with the relevant financial reporting framework and have been prepared in accordance with the requirements of applicable law.

I confirm to the best of my knowledge and belief, and having made appropriate enquiries of directors and management of the Council, the following representations given to you in connection with your audit of the Council's financial statements:

#### FINANCIAL STATEMENTS

##### Responsibility for the financial statements

I acknowledge as the Director of Finance and s151 Officer my responsibilities for the financial statements and for ensuring that these are prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom.

##### Accounting policies

I confirm that the selection and application of the accounting policies used in the preparation of the financial statements are appropriate.

##### Significant assumptions

The following significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable:

- See pension fund assumption below.

##### Completeness of information

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 management and committee meetings (held during the year and up to the date of this letter) have been made available to you.

##### Internal control

I acknowledge my responsibility for the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that are free from misstatement, whether arising from fraud or error.

##### Fraud

I have disclosed to you the results of my assessment of the risk that the financial statements could be materially misstated as a result of fraud.

I am not aware of any fraud or suspected fraud affecting the financial statements, nor have any allegations of fraud or suspected fraud affecting the financial statements been communicated to me by employees, former employees, councillors, regulators or others.

#### **Compliance with law and regulations**

I am not aware of any possible or actual instances of non-compliance with laws or regulations whose effects should be considered when preparing financial statements of the Council.

#### **Transactions with related parties**

I confirm that I have put in place appropriate arrangements to identify related party transactions.

I am satisfied that the disclosure in the financial statements of related party transactions is appropriate and complete and contains all the elements necessary for an understanding of the financial statements.

#### **Contingent liabilities**

I am not aware of any significant contingent liabilities, including pending claims, proceedings or litigation involving the Council.

#### **Pension fund assumptions**

I confirm that the actuarial assumptions underlying the valuation of the Local Government Pension Scheme (LGPS) scheme liabilities, as applied by the scheme actuary, are reasonable and consistent with my knowledge of the business.

These assumptions include:

- |  |       |
|--|-------|
| • Rate of inflation (RPI)  | N/A   |
| • Rate of inflation (CPI)  | 2.8%  |
| • Rate of increase in salaries                                       | 5.1%  |
| • Rate of increase in pensions                                       | 6.7%  |
| • Rate for discounting scheme liabilities                            | 5.5%  |
| • Take up option to convert the annual pension into retirement grant | 25.0% |

I also confirm that the actuary has applied up-to-date mortality tables for life expectancy of scheme members in calculating scheme liabilities.

#### **Valuation of housing stock**

The useful economic lives of the housing stock and its constituent components, used in the valuation of the housing stock and the calculation of the depreciation charge for the year are consistent with those advised to us by the expert valuer appointed by the Council to provide this information.

#### **Uncorrected misstatements**

You have brought to my attention uncorrected misstatements in the financial statements as listed in Appendix 1 to this letter. I do not wish to correct these misstatements as I consider them to be immaterial to the view given by the financial statements.

**Subsequent events**

There have been no events since the balance sheet date which necessitate revision of the figures included in the financial statements or inclusion of a note thereto. Should any material events occur, which may necessitate revision of the figures included in the financial statements or inclusion of a note thereto, I will advise you accordingly.

Yours faithfully

**Barry Hunter**  
**Director of Finance**

***Representations of the Council***

We confirm to the best of our knowledge and belief, and having made appropriate enquiries of other officers and members of the Council, the following representations given to you in connection with your audit of the Council's financial statements.

**Responsibility for the financial statements**

We acknowledge our responsibilities to make arrangements for the proper administration of the Council's financial affairs and to approve the financial statements. The Director of Finance is responsible for the preparation of the financial statements in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom.

**Uncorrected misstatements**

We have considered the uncorrected misstatements in the financial statements as listed in Appendix 1 to this letter together with the explanations provided by the Director of Finance for not correcting these misstatements, and we consider them to be immaterial to the view given by the financial statements.

**Annual Governance Statement**

We confirm that the Council has conducted a review during the year of the effectiveness of its system of internal control. We are satisfied that the Annual Governance Statement appropriately reflects the circumstances of the Council and includes an outline of the actions taken, or proposed, to deal with significant internal control issues.

Yours faithfully

**Cllr Busby**  
**Overview and Scrutiny (Stewardship) Chair**

Signed on behalf of the Council

**Note: Appendix 1 referred to in this letter relates to Appendix B in this report**

## Appendix D: Draft independent auditors' report

### Independent auditor's report to the Members of Babergh District Council

#### *Opinion on the accounting statements*

#### **Opinion on the Council's accounting statements**

We have audited the accounting statements of Babergh District Council for the year ended 31 March 2011 under the Audit Commission Act 1998. The accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Housing Revenue Account, 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 2010/11 (based on International Financial Reporting Standards).

This report is made solely to the members of Babergh District 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. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Council and the Council's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### **Respective responsibilities of the Director of Finance and auditor**

As explained more fully in the Director of Finance Responsibilities Statement, Director of Finance is responsible for the preparation of the Council's Statement of Accounts, that include the accounting 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. Our responsibility is to audit and express an opinion on the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practice's Board's Ethical Standards for Auditors.

#### **Scope of the audit of the accounting statements**

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements sufficient to give reasonable assurance that the accounting 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 Council's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the accounting statements. In addition, we read all the financial and non-financial information in the explanatory foreword and the Statement of Accounts to identify material inconsistencies with the audited accounting statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### **Opinion on accounting statements**

In our opinion the accounting statements:

- give a true and fair view of the state of Babergh District Council's affairs as at 31 March 2011 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2010/11.

**Matters on which we are required to report by exception**

We have nothing to report in respect of the governance statement on which we report to you if, in our opinion the governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007.

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

We are required under Section 5 of the Audit Commission Act 1998 to satisfy ourselves that the Council 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 us to report to you our conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

**Respective responsibilities of the Council and auditor**

The Council 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.

Our responsibility requires us to review and, where appropriate, examine evidence that is relevant to the Council's corporate performance and financial management arrangements. It therefore excludes arrangements relating specifically to the delivery of front-line services, unless we have identified a significant risk with implications for corporate arrangements.

We report if significant matters have come to our attention which prevent us from concluding that the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Council'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**

We have undertaken our 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 2010, as to whether the Council 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 us to consider under the Code of Audit Practice in satisfying ourselves whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2011.

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

**Conclusion**

On the basis of our work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2010, we are satisfied that, in all significant respects, Babergh District Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2011.

***Certificate***

We certify that we have completed the audit of the accounts of Babergh District Council in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

Richard Bint  
for and on behalf of PKF (UK) LLP

London, UK

X September 2011

**CHANGES TO DRAFT CORE STATEMENTS REPORTED TO OVERVIEW  
AND SCRUTINY (STEWARDSHIP) COMMITTEE ON 7<sup>TH</sup> JULY 2011**

**Comprehensive Income & Expenditure Statement**

	<b>EXPENDITURE £000</b>	<b>INCOME £000</b>
Changes to Income and Expenditure to reflect corrections to the treatment of grant income under IFRS and other adjustments– Net reduction in expenditure Net reduction in income	(170)	49
Increase in expenditure relating to Housing Benefit	86	
2 lines for exceptional items shown separately –  Housing Revenue Account - Impairment due to the reduction in Social Housing Discount factor from 46% to 39% Change in the Pension Obligation for the change in inflation assumptions from RPI to CPI (moved from expenditure to income)	28,181	(6,334)
Reduction in Taxation and Non Specific Grant Income to correctly reflect treatment of grant income and expenditure previously omitted		769
Changes to the movement in net worth – Correction of the surplus on revaluation and derecognition of fixed assets Other adjustments	15	(226)

Movement in Net Worth – decrease of £523k.

**Balance Sheet**

Correction to usable reserves to reflect the correct treatment of grant income and expenditure under IFRS (including movement to earmarked reserves) as above.

Some adjustments to debtors and creditors.

Borrowing reanalysed between short and long term.

**Movement in Reserves Statement**

Correction to usable reserves to reflect the correct treatment of grant income and expenditure under IFRS (including movement to earmarked reserves).



## **Cash Flow Statement**

A number of changes to the core statement and notes 9 – 12 to reflect correct treatment of cash and non cash items relating to income and expenditure including grants.

## **Notes**

An additional note has been added (now note 2) to explain the changes to the Balance Sheet and the Comprehensive Income & Expenditure Statement as a result of the introduction of International Financial Reporting Standards.

Other notes have been updated as required to reflect the changes to the core statements including an update on Contingent Liabilities (note 30) and related party transactions (note 18).

H:\DOCS\Committee\REPORTS\Overview&Scrutiny\Stewardship\2011\220911-Main changes to core statements  
App B.doc

**COMPREHENSIVE INCOME AND EXPENDITURE STATEMENT**

2009/10			2010/11		
Gross Expenditure £'000	Restated Gross Income £'000	Net Expenditure £'000	Gross Expenditure £'000	Gross Income £'000	Net Expenditure £'000
7,058	(5,884)	1,174	7,492	(6,136)	1,356
10,676	(3,360)	7,316	9,719	(3,464)	6,255
1,061	(293)	768	1,056	(195)	861
920	(13,932)	(13,012)	12,960	(14,109)	(1,149)
18,736	(17,820)	916	19,384	(18,719)	665
2,244	(4)	2,240	2,578	(28)	2,550
		-	(15)	-	(15)
			28,181	-	28,181
			-	(6,334)	(6,334)
40,695	(41,293)	(598)	81,355	(48,985)	32,370
3,216	-	3,216	3,287	-	3,287
1,229	(93)	1,136	906	(54)	852
	(13,032)	(13,032)		(13,147)	(13,147)
			<b>(Surplus) or Deficit on Provision of Services (note 13) -</b>		
			<b>(9,278) A</b>		
			(771) (Surplus) or deficit on revaluation of fixed assets (note 8a)		
			(116) Net Movement on Collection Fund Balance		
			106 Derecognition of Fixed Asset (note 23)		
			16,900 Actuarial (gains)/losses on pension assets/liabilities (note 17)		
			<b>16,119 Other Comprehensive Income and Expenditure - B</b>		
			<b>(13,416)</b>		

BABERGH DISTRICT COUNCIL - STATEMENT OF ACCOUNTS 2010/11

6,841	<b>Total Comprehensive Income and Expenditure (A+B)</b>	<b>9,946</b>
-------	---	--------------

**MOVEMENT IN RESERVES STATEMENT**

	General Fund Balance £'000	Earmarked General Fund Reserves £'000	HRA Balance £'000	Major Repairs Reserve £'000	Capital Receipts Reserve £'000	Capital Grants Unapplied Reserve £'000	Total Usable Reserves £'000	Unusable Reserves £'000	Total Authority Reserves £'000
<b>Balance at 31 March 2009 Restated</b>	<b>(2,342)</b>	<b>(1,277)</b>	<b>(1,060)</b>	<b>(520)</b>	<b>(1,180)</b>	<b>(140)</b>	<b>(6,519)</b>	<b>(175,742)</b>	<b>(182,261)</b>
<b><u>Movement in reserves during 2009/10</u></b>									
(Surplus) or deficit on provision of services	2,483	-	(11,761)	-	-	-	(9,278)	-	(9,278)
Other Comprehensive Expenditure and Income							-	16,119	16,119
<b>Total Comprehensive Expenditure and Income</b>	<b>2,483</b>	<b>-</b>	<b>(11,761)</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>(9,278)</b>	<b>16,119</b>	<b>6,841</b>
Adjustments between accounting basis and funding basis under regulations (note 4)	(1,955)	-	11,607	334	871	(10)	10,847	(10,847)	-
<b>Net (Increase)/Decrease before Transfers to Earmarked Reserves</b>	<b>528</b>	<b>-</b>	<b>(154)</b>	<b>334</b>	<b>871</b>	<b>(10)</b>	<b>1,569</b>	<b>5,272</b>	<b>6,841</b>
Transfer to/(from) Earmarked Reserves (note 5)	190	(190)	-	-	-	-	-	-	-
<b>(Increase)/Decrease in 2009/10</b>	<b>718</b>	<b>(190)</b>	<b>(154)</b>	<b>334</b>	<b>871</b>	<b>(10)</b>	<b>1,569</b>	<b>5,272</b>	<b>6,841</b>
<b>Balance at 31 March 2010 Restated</b>	<b>(1,624)</b>	<b>(1,467)</b>	<b>(1,214)</b>	<b>(186)</b>	<b>(309)</b>	<b>(150)</b>	<b>(4,950)</b>	<b>(170,470)</b>	<b>(175,420)</b>
<b><u>Movement in reserves during 2010/11</u></b>									
(Surplus) or deficit on provision of services	(5,241)	-	28,603	-	-	-	23,362	-	23,362
Other Comprehensive Expenditure and Income							-	(13,416)	(13,416)
<b>Total Comprehensive Expenditure and Income</b>	<b>(5,241)</b>	<b>-</b>	<b>28,603</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>23,362</b>	<b>(13,416)</b>	<b>9,946</b>
Adjustments between accounting basis and funding basis under regulations (note 4)	5,298	-	(28,812)	(100)	(89)	43	(23,660)	23,660	-
<b>Net (Increase)/Decrease before Transfers to Earmarked Reserves</b>	<b>57</b>	<b>-</b>	<b>(209)</b>	<b>(100)</b>	<b>(89)</b>	<b>43</b>	<b>(298)</b>	<b>10,244</b>	<b>9,946</b>
Transfer to/(from) Earmarked Reserves (note 5)	(478)	478	-	-	-	-	-	-	-
<b>(Increase)/Decrease in Year</b>	<b>(421)</b>	<b>478</b>	<b>(209)</b>	<b>(100)</b>	<b>(89)</b>	<b>43</b>	<b>(298)</b>	<b>10,244</b>	<b>9,946</b>
<b>Balance at 31 March 2011 carried forward</b>	<b>(2,045)</b>	<b>(989)</b>	<b>(1,423)</b>	<b>(286)</b>	<b>(398)</b>	<b>(107)</b>	<b>(5,248)</b>	<b>(160,226)</b>	<b>(165,474)</b>

BABERGH DISTRICT COUNCIL - STATEMENT OF ACCOUNTS 2010/11

**CASH FLOW STATEMENT**

<b>2009/10</b>		<b>2010/11</b>
<b>£'000</b>		<b>£'000</b>
<b>Restated</b>		
(9,278)	Net (surplus) or deficit on the provision of services	<b>23,362</b>
9,148	Adjust net surplus or deficit on the provision of services for non cash movements	<b>(26,401)</b>
	Adjust for items included in the net surplus or deficit on the provision of services that are investing and financing activities	(579)
(924)		(3,618)
(1,054)	Net cash flows from Operating Activities (note 9)	40
(77)	Investing Activities (note 10)	4,738
4,589	Financing Activities (note 11)	<b>(725)</b>
(825)		435
2,633	Net (increase) or decrease in cash and cash equivalents	
	Cash and cash equivalents at the beginning of the reporting period	<b>(799)</b>
(3,432)		(364)
(799)	<b>Cash and cash equivalents at the end of the reporting period (note 12)</b>	(364)

## 2 Prior Period Adjustments

The adoption of International Financial Reporting Standards (IFRS) as part of the CIPFA Code of Practice for 2010/11 has resulted in a number of changes in Accounting Policies and accounting entries.

Adoption of the IFRS based Code has resulted in the restatement of various balances and transactions related to prior year financial information as though the new accounting policies had always been applied, unless the Code stipulates specific transitional arrangements. The following tables explain the material differences between the amounts presented in the 2009/10 financial statements and the equivalent restated figures shown in the 2010/11 financial statements.

### Grants and Contributions

Under the code, grants and contributions for capital schemes are recognised as income when they become receivable. Previously, grants were held in a grants deferred account and recognised as income over the life of the assets which they were used to fund. As a consequence of adopting the Code, the financial statements have been amended as follows:

- The balance on the Government Grants Deferred Account at 31 March 2009 has been transferred to the Capital Adjustment Account in the opening 1 April 2009 Balance Sheet
- Portions of government grants deferred were previously recognised as income in 2009/10 and these have been removed from the Comprehensive Income and Expenditure Statement (CIES) in the comparative figures
- Capital grants and contributions (including section 106 contributions) that have not satisfied the grant conditions at the Balance Sheet date have been reflected as Receipts in Advance in the Liabilities section of the Balance Sheet
- Capital grants and contributions received that have no conditions attached have been included in the CIES as income from Non-specific grants. There is no change to the General Fund Balance as capital grant income is transferred out of the General Fund under both the previous and current accounting policies
- Revenue grants that were previously recognised as receipts in advance in the Balance Sheet have been transferred to the CIES and if no conditions are attached the unspent balances have been transferred to an earmarked reserve. Where conditions are attached to revenue grants at the balance sheet date, the unspent balances have been reflected as Receipts in Advance in the Liabilities section of the Balance Sheet, as previously.

### Fixed Assets (now Property, Plant and Equipment)

The main changes in the Code relate to changes in terminology, the clarification of the definition of Investment Properties, the introduction of a new asset category 'Assets Held for Sale' and an increased focus on the recognition of component assets. Most fixed assets now fall under the heading 'Property, Plant and Equipment'.

Following a review of all assets, no assets satisfied the revised definition of Investment Properties and one council dwelling was transferred to Assets Held for Sale as the legal process was nearing completion. The recognition of components within General Fund properties does not require a prior period adjustment.

### Short term accumulating compensated absences

Short term accumulating compensated absences relate to benefits that employees receive as part of their contract of employment. Entitlement to this accrues as employees provide services to the Council and the most significant of these is holiday pay. Under IFRS the cost of this is required to be recognised as employees render services that increase their entitlement to future compensated absences. The Council is required to accrue for any annual leave earned but not taken at the year end, 31 March.

The government has issued regulations that mean local authorities are only required to fund holiday pay and similar benefits when they are used rather than when the

#### Other Items

Other minor presentation changes were also required:

- Cash Equivalents: Short-term investments meet the Code's definition of Cash Equivalents which are monies held on deposit in instant access call accounts. These monies are shown with cash balances and have been restated for 2009/10 in the Balance Sheet
- Provisions: Previously shown in Long-term Liabilities in the Balance Sheet. Provisions anticipated to be called on within one year are now recognised as part of Current Liabilities

## SUMMARY OF IFRS RESTATEMENT - BALANCE SHEET

BABERGH DISTRICT COUNCIL - STATEMENT OF ACCOUNTS 2010/11

1st April 2009 SORP £'000	Grants & Contributions £'000	Fixed Assets £'000	Other Items £'000	1st April 2009 IFRS £'000		31st March 2010 SORP £'000	Grants & Contributions £'000	Fixed Assets £'000	Other Items £'000	31st March 2010 IFRS £'000
192,210		2,490		194,700	Property, Plant and Equipment	204,902		2,616		207,518
2,539		(2,539)		-	- Investment Property	2,665		(2,665)		-
1,626				1,626	Intangible Assets	1,747				1,747
-		124		124	Assets held for sale	-				-
386				386	Long Term Debtors	370				370
<u>196,761</u>				<u>196,836</u>	<b>Long Term Assets</b>	<u>209,684</u>				<u>209,635</u>
6,342			(3,804)	2,538	Short Term Investments	2,852			(345)	2,507
75				75	Inventories	53				53
2,558			3	2,561	Short Term Debtors	3,120			8	3,128
-			3,432	3,432	Cash and Cash Equivalents	462			337	799
-				-	- Assets held for sale	-		124		124
<u>8,975</u>				<u>8,606</u>	<b>Current Assets</b>	<u>6,487</u>				<u>6,611</u>
(369)			369	-	- Cash and Cash Equivalents	-				-
(7)				(7)	Short Term Borrowing	(1,008)				(1,008)
(6,761)	4			(6,757)	Short Term Creditors	(6,736)	31			(6,705)
(76)				(76)	Provisions	(76)			(77)	(153)
(167)	167			-	- Capital Grants / Contributions Received in Advance	(267)	267			-
<u>(7,380)</u>				<u>(6,840)</u>	<b>Current Liabilities</b>	<u>(8,087)</u>				<u>(7,866)</u>
(1,100)				(1,100)	Long Term Borrowing	(1,100)				(1,100)
(46)				(46)	Other Long Term Liabilities	(23)				(23)
(918)	918			-	- Government Grants Deferred	(762)	762			-
(1,431)	1,431			-	- Capital Contributions Deferred	(1,595)	1,595			-
(543)				(543)	Deferred Liabilities	(368)				(368)
(14,652)				(14,652)	Defined Benefit Pension Scheme Liability	(31,469)				(31,469)
<u>(18,690)</u>				<u>(16,341)</u>	<b>Long Term Liabilities</b>	<u>(35,317)</u>				<u>(32,960)</u>
<u>179,666</u>				<u>182,261</u>	<b>Net Assets</b>	<u>172,767</u>				<u>175,420</u>
989		66		1,055	Revaluation reserve	1,685		66		1,751
187,915	2,349	9		190,273	Capital Adjustment Account	198,485	2,357	9		200,851
-				-	- Accumulated Absences Account	-			(77)	(77)
(15,586)				(15,586)	Other Unusable Reserves	(32,055)				(32,055)
-	140			140	Capital Grants Unapplied	-	150			150
2,359	(17)			2,342	General Fund Balance	1,685	(60)			1,625
1,229	48			1,277	Earmarked Reserves	-	208			208
2,760				2,760	Other Usable reserves	2,967				2,967
<u>179,666</u>				<u>182,261</u>		<u>172,767</u>				<u>175,420</u>



**SUMMARY OF IFRS RESTATEMENT COMPREHENSIVE INCOME AND EXPENDITURE STATEMENT**

	SORP Net Expenditure 2009/10 £'000	Grants & Contributions £'000	Accumulating Compensated Absences £'000	IFRS Net Expenditure 2009/10 £'000
Central services to the public	1,102	70	2	1,174
Cultural, environmental, regulatory and planning services	7,208	73	35	7,316
Highways and transport services	765		3	768
Local Authority Housing (HRA)	(13,067)	41	14	(13,012)
Other housing services	895	9	12	916
Corporate and democratic core	2,214	15	11	2,240
Non distributed costs	-			-
<b>Cost of Services</b>	<b>(883)</b>	<b>208</b>	<b>77</b>	<b>(598)</b>
Other Operating Expenditure (note 6)	3,216			3,216
Financing and Investment Income and Expenditure (note 7)	1,136			1,136
Taxation and Non-Specific Grant Income (note 32)	(12,689)	(343)		(13,032)
<b>(Surplus) or Deficit on Provision of Services (note 13) - A</b>	<b>(9,220)</b>	<b>(135)</b>	<b>77</b>	<b>(9,278)</b>
Surplus or deficit on revaluation of fixed assets	(771)			(771)
Net Movement on Collection Fund Balance	(116)			(116)
Derecognition of Fixed Asset	106			106
Actuarial gains/losses on pension assets/liabilities	16,900			16,900
<b>Other Comprehensive Income and Expenditure - B</b>	<b>16,119</b>			<b>16,119</b>
<b>Total Comprehensive Income and Expenditure (A+B)</b>	<b>6,899</b>	<b>(135)</b>	<b>77</b>	<b>6,841</b>

# **STATEMENT OF ACCOUNTS 2010/11**

## **Explanatory Foreword**

	<b>Page</b>
1. Introduction/Background .....	1
2. Audit Opinion .....	1
3. Accounting and Disclosure Changes.....	1
4. Statements Included .....	2
5. Net Revenue Expenditure .....	5
6. Capital Investment (incl. Treasury Management) .....	7
7. Pensions .....	9
8. Funds/Reserves.....	10
9. Future Plans and Challenges .....	10
10. Further Information .....	11

### **1. Introduction/Background**

This foreword provides an explanation of the most significant matters affecting the Council's accounts in 2010/11, including a comparison of actual income and expenditure against the budget and the Council's overall financial position. The aim is to assist readers in understanding key aspects of the Council's finances for the year and the detailed accounting statements.

The Statement of Accounts have to be produced in accordance with the Code of Practice on Local Authority Accounting 2010 (The Code) published by the Chartered Institute of Public Finance and Accountancy (CIPFA) and, for the first time this is based on International Financial Reporting Standards (IFRS).

The Code specifies the principles and practices of accounting required to prepare a Statement of Accounts which presents a true and fair view of the financial position of the Authority at the 31 March 2011. It also prescribes the accounting treatment and minimum requirements for disclosures.

### **2. Audit Opinion**

The accounts are published subject to audit.

### **3. Accounting and Disclosure Changes**

As a result of the transition to IFRS the following accounting policies have been changed. A full explanation is shown within the Accounting Policies.

- Property, plant and equipment
- Intangible assets

- Non-current assets and liabilities classified as held for sale
- Grants and contributions received
- Leasing

The 2010/11 Accounts reflect a number of significant changes to reflect IFRS including the restatement of the 2009/10 core financial statements. The Council's first IFRS-based financial statements include three statements of the financial position, two statements of comprehensive income and expenditure, two statements of cashflows and two statements of changes in equity (Movement in Reserves Statements).

#### **4. Statements Included**

As specified under the Code the following accounting statements have been prepared:

**(i) Statement of Accounting Policies**

Policies adopted in compiling the Accounts for the year are set out.

**(ii) Statement of Responsibilities for the Statement of Accounts**

Sets out the respective responsibilities of the Council and the Director of Finance.

**(iii) The four Core Financial Statements - required to be given equal prominence:**

**(a) Comprehensive Income and Expenditure Statement**

This Statement shows the accounting cost in the year of providing services in accordance with generally accepted accounting practices, rather than the amount to be funded from taxation. The total reported net expenditure for 2010/11 of £9.653m reconciles to the Segmental Reporting Note (Page 50 Note 13) which provides a comparison between the way financial information is reported and monitored in the Council's budget as opposed to the statutory financial statement. The taxation position is shown in the Movement in Reserves Statement.

This reported 'deficit' largely results from 'negative' movements on unusable reserves of, which largely result from technical accounting requirements. Discounting these, there was a small increase in usable reserves relating to the General Fund, the HRA and capital reserves.

**(b) Movement in Reserves Statement**

This statement shows the movement in the year on the different reserves held by the authority. Not all of these reserves can be used to deliver services or to reduce local taxation and the Code reflects this by reporting in two groups – 'usable' reserves and 'unusable' reserves. The Surplus or Deficit on the Provision of Services line shows the true economic cost of providing the authority's services, more details of which are shown in the Comprehensive Income and Expenditure Statement. These are different from the statutory amounts required to be charged to the General Fund Balance for council tax setting and the Housing Revenue Account for rent setting purposes.

The Net Increase/Decrease before transfers to Earmarked Reserves line shows the actual General Fund Balance and Housing Revenue Account Balance before any discretionary transfers to or from earmarked reserves.

### **(c) Balance Sheet**

The Balance Sheet shows the value as at the Balance Sheet date of the assets and liabilities recognised by the authority. The net assets of the authority (assets less liabilities) are matched by the reserves held by the authority. Reserves are reported in two categories. The 'usable' reserves can be used to provide services Members can, therefore, exercise control over these. They are subject to the need to maintain a prudent level of reserves and any statutory limitation on their use (e.g the Capital Receipts Reserve may only be used to fund capital expenditure or repay debt).

The 'unusable' reserves, are not available to use to provide services. These include reserves that hold unrealised gains and losses (e.g. the Revaluation Reserve), where amounts would only become available to provide services if the assets are sold; and reserves that will become a charge against the revenue account or 'usable' reserves – over time. These timing differences are shown in the Movement in Reserves Statement line 'Adjustments between accounting basis and funding basis under regulations'.

Net assets stood at just over £165m as at the 31 March 2011, a fall of around £10m during the year, largely as a result of impairment (i.e, reduction in value) of Council Housing assets but also reflecting the significant reduction in the Pension Scheme liability.

### **(d) Cash Flow Statement**

The Cash Flow Statement shows the changes in cash and cash equivalents of the authority during the reporting period. The statement shows how the authority generates and uses cash and cash equivalents by classifying cash flows as operating, investing and financing activities. The amount of net cash flows arising from operating activities is a key indicator of the extent to which the operations of the authority are funded by way of taxation and grant income or from the recipients of services provided by the authority. Investing activities represent the extent to which cash outflows have been made for resources which are intended to contribute to the authority's future service delivery. Cash flows arising from financing activities are useful in predicting claims on future cash flows by providers of capital (ie borrowing) to the authority.

### **(iv) Notes to the Core Financial Statements**

The Code requires certain information to be disclosed in notes to the core financial statements. These are intended to add to and explain the content of individual statements, and provide more analysis where matters of financial significance cannot adequately be set out in the statements themselves.

**(v) Supplementary Financial Statements:**

**(a) Housing Revenue Account (HRA)**

The HRA records all income and expenditure on the Council's statutory function with regard to the provision of housing accommodation and associated services. Authorities charge rents to cover expenditure in accordance with regulations and this may differ from the accounting cost. The reconciliation between the surplus or deficit on the HRA and the amounts that are required by statute and by non-statutory proper practices to be disclosed are shown in the Movement in the HRA Statement.

**(b) Notes to the HRA**

The Code requires certain information to be disclosed in notes to the HRA. These are intended to add to and explain the content of individual statements, and provide more analysis where matters of financial significance cannot adequately be set out in the statements themselves.

**(c) Collection Fund**

This account reflects the statutory requirement for billing authorities to maintain a separate Collection Fund, which shows the transactions in relation to non-domestic rates and the council tax, and illustrates the way in which these have been distributed to preceptors and the General Fund.

**(d) Notes to the Collection Fund**

The Code requires certain information to be disclosed in notes to the Collection Fund. These are intended to add to and explain the content of individual statements, and provide more analysis where matters of financial significance cannot adequately be set out in the statements themselves.

**(vi) Accompanying Statements**

**(a) Audit Report**

The accounts signed by the Council's Chief Financial Officer (the Director of Finance) are subject to audit.

The external Auditor's responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing. The auditor's opinion is given on whether the financial statements present true and fair view, in accordance with applicable laws and regulations and the SORP and this will be provided in September 2011.

**Glossary of Terms**

Explanations are given to help the reader understand some of the terms used.

## 5. Net Revenue Expenditure

The Comprehensive Income and Expenditure (CI & E) Account includes all expenditure on services including Council Housing, interest payable and other operating costs, income from grants, local taxpayers and other sources.

### The General Fund

The Comprehensive Income and Expenditure (CI & E) Account also includes changes resulting from the revaluation of assets, which impacts both on the HRA in relation to Council Housing, but also affects the reported costs of General Fund services (i.e. those services paid for by Council Tax and general Government Formula grant). A comparison of the overall position in 2010/11 compared with 2009/10 is given below, removing these items, to arrive at the resulting General Fund position:

	<b>2009/10</b>	<b>2010/11</b>
	<b>Restated</b>	
	<b>£000</b>	<b>£000</b>
Reported I&E deficit/(surplus) for the year	(9,273)	<b>23,362</b>
Adjust for:		
Revaluation of assets (impairment/changes in value)	11,737	<b>(27,896)</b>
Other Changes	<u>(894)</u>	<u><b>4,113</b></u>
Actual deficit/(surplus) for the year in General Fund balance	<u><b>1,570</b></u>	<u><b>(421)</b></u>

The following table compares the actual position on General Fund income and expenditure with the original and revised budget for the year. This covers all services excluding Council Housing:

	<b>Original Budget</b>	<b>Revised Budget</b>	<b>Actual</b>	<b>Variance</b>
	<b>£000</b>	<b>£000</b>	<b>£000</b>	<b>£000</b>
Net Expenditure (excl. items below)	11,113	11,066	10,322	(744)
Revenue Financing - Capital Investment	-	1,120	573	(547)
Transfer to (from) Earmarked Reserves	<u>(175)</u>	<u>(1,175)</u>	<u>(478)</u>	<u>697</u>
Net Revenue Expenditure	10,938	11,011	10,417	(594)
Less: Government Formula Grant and Council Tax	<u>(10,838)</u>	<u>(10,838)</u>	<u>(10,838)</u>	<u>-</u>
Deficit/Use of Reserves or (surplus)	<u><b>100</b></u>	<u><b>173</b></u>	<u><b>(421)</b></u>	<u><b>(594)</b></u>

The original budget was based on making savings and achieving additional income of around £1.6m during the year or around 14% of the net revenue expenditure budget and this has been achieved.

Details of the key variations compared to the revised budget are provided below:-

	<b>Variation £000</b>
<b>Savings:</b>	
Budget savings to be carried forward into 2011/12	436
Salaries and other operational expenditure	116
Housing and Council Tax Benefits	106
Other	75
	<u><b>733</b></u>
<b>Additional Costs:</b>	
Waste collection - Gate Fees	(14)
Grounds Maintenance & Street Cleansing	(10)
	<u><b>(24)</b></u>
Lower net income on a variety of services	(115)
<b>Total net saving compared to budget</b>	<u><u><b>594</b></u></u>

This total net saving includes £556k in relation to budgets carried forward into 2011/12 and an additional transfer to the Capital Projects Earmarked Reserve. The resulting balance has been added to reserves and will be available for use in future years.

#### **The Housing Revenue Account (Council Housing)**

The following table compares the actual position on General Fund income and expenditure with the original and revised budget for the year:

	<b>Original Budget £000</b>	<b>Revised Budget £000</b>	<b>Actual £000</b>
Income	(14,004)	(14,067)	(14,109)
Expenditure (net of appropriations)	<u>13,987</u>	<u>13,969</u>	<u>13,900</u>
Decrease/(Increase) in Housing Revenue Account Balance	<u><b>(17)</b></u>	<u><b>(98)</b></u>	<u><b>(209)</b></u>
Variance from Revised Budget			<b>113</b>

An analysis of this variation is shown below:

	<b>£000</b>
<b>Higher Income:</b>	
Rent income & charges	(17)
Government Grant	54
	<u>37</u>
<b>Additional Costs:</b>	
Repairs & maintenance	120
	-
	<u>120</u>
<b>Savings:</b>	
Energy costs	(20)
Planned maintenance	(45)
Tenancy changes	(98)
Non-Programmed work	(39)
Management and staffing and others	(68)
	<u>(270)</u>
<b>Total net saving compared to budget</b>	<u><u>(113)</u></u>

Of this, £69k is to be carried forward and spent in 2011/12, leaving HRA reserves £44k higher overall than expected in the budget.

## **6. Capital Investment**

Capital Expenditure for the year and how it has been financed is summarised below, comparing it with the original and revised approved capital programme:



	<b>Original Budget £000</b>	<b>Revised Budget £000</b>	<b>Actual £000</b>	<b>Variance £000</b>
<b>Expenditure</b>				
ICT/Information Management	324	238	202	(36)
Asset Management	1,317	727	545	(182)
Community Services	549	656	626	(30)
Private Sector Housing	536	586	459	(127)
The Environment	225	246	11	(235)
Capitalised Redundancy Costs	-	186	179	(7)
Open Spaces and Play Areas (funded from S106 contributions)	-	-	133	133
<b>Total General Fund</b>	<u>2,951</u>	<u>2,639</u>	<u>2,155</u>	<u>(484)</u>
Council Housing	3,604	3,533	3,330	(203)
<b>Total</b>	<u><b>6,555</b></u>	<u><b>6,172</b></u>	<u><b>5,485</b></u>	<u><b>(687)</b></u>
<b>Financed from:</b>				
Supported borrowing	550	550	550	-
Non-supported borrowing	768	57	400	343
Capital Receipts	1,125	295	179	(116)
Grants/external contributions including LABGI	1,083	1,710	1,529	(181)
Major Repairs Allowances *	2,413	2,342	2,121	(221)
Revenue *	616	1,218	706	(512)
<b>Total</b>	<u><b>6,555</b></u>	<u><b>6,172</b></u>	<u><b>5,485</b></u>	<u><b>(687)</b></u>

\* All Council Housing apart from £90k use of revenue from earmarked revenue reserves in the revised budget

An analysis of the variance compared to the revised budget is shown below:

	<b>Variance £000</b>
Green Waste Scheme	135
Haven Gateway Projects (externally funded)	64
Car Parks	73
Council Housing	203
Affordable Housing	150
Other	62
	<u><b>687</b></u>

The majority of this expenditure will be carried forward and take place in 2011/12 or future years.

In terms of borrowing, the current strategy is to use internal surplus funds where appropriate to temporarily to finance the capital expenditure indicated above. Long-term external borrowing of £2m has been undertaken during the year to take advantage of the prevailing low interest rates that were available during the year. The Council's net borrowing requirement shown below indicates the extent to which the Council has temporarily borrowed internal resources to finance capital expenditure rather than

borrow externally. Advice is sought regarding the timing of replacing any internal borrowing with external borrowing:

	<b>£000</b>
Underlying need to borrow at 31 March 2011 (Capital Financing Requirement)	7,905
Long Term Borrowing at 31 March 2011(Public Works Loan Board	<u>(2,800)</u>
Net Borrowing Facility at 31 March 2011	<u><u>5,105</u></u>

## **Treasury Management**

The CIPFA prudential code sets out the governance arrangements for borrowing and lending. It states that the authorised limit and operational boundary is for its total external debt, excluding investments, separately identifying borrowing from other long-term liabilities.

Current long term borrowing is from the government's Public Works Loan Board (PWLB). One new fixed rate loan was undertaken during the year, taking advantage of low interest rates, of a £2m, 10 year EIP loan repayable in equal half yearly instalments over the term of the loan. At the year end external long-term debt was £3m. Short term borrowing during the year was kept to a minimum to aid cash flow and cover daily cash flow requirements.

The underlying need to borrow and actual borrowing are prudent in relation to the Council's overall capital investment plans and the total long term asset value of around £180m as at the 31 March 2011.

Surplus funds were invested with counterparties with high credit ratings as determined in the Treasury Management Strategy documents. At the 31 March 2011, surplus funds invested were £3.5m. The approved limits established for borrowing and the operation boundary were set at £9.6m and £5.5m.

Further details on treasury management activity are shown in note 33 to the Core Statements.

## **7. Pensions**

There is a substantial deficit on the Council's Pension Fund, administered by Suffolk County Council. The most recent triennial valuation and actuarial review on the 31 March 2011 puts this deficit at £12.6m. This is £5.9m more than reported at the last tri-ennial valuation in 2007 but considerably less than the £31.5m reported as at the 31 March 2010 (under Financial Reporting Standard 17). The reasons for the changes between 2010 and 2011, as assessed by the Fund's actuary, are given in the Notes to the Financial Statements. Annual lump sum payments are being made towards the deficit.

The lump sum payments, annual contribution rates towards current/future pensions and costs shown in the accounts for 2010/11 and previous years are, however, based on the previous valuation that was done in March 2008. Based on this, the Council's contribution rate to the Pension Fund, over and above the lump sum deficit payments, for the last 3 years has been 16.0%.

## 8. Sources of Funds/Reserves

A summary of the Council's funds available to meet its future expenditure plans and other financial commitments is shown below:

	<b>31 March 2011 £000</b>	31 March 2010 £000
<b>General Fund</b>		
General Reserves	2,045	1,624
Earmarked Reserves	989	1,467
Collection Fund	-	(13)
	<b>3,034</b>	<b>3,078</b>
<b>Housing Revenue Account</b>		
General Reserves	1,423	1,214
Major Repairs Reserve	286	186
	<b>1,709</b>	<b>1,400</b>
	<b>4,743</b>	<b>4,478</b>

There are plans to use some of these reserves in future years. Specifically, some of the money will be needed to meet the expenditure in relation to budgets carried over from 2010/11, which are estimated at £495k (General Fund and HRA combined).

The Council's Strategy Committee will be considering some changes to the level and use of earmarked reserves on the 7 July, including setting money aside to meet the initial costs of service integration with Mid Suffolk District Council. These changes will not materially affect the overall reserves position stated above but will provide increased flexibility in the use of reserves to generate future savings.

## 9. Future Plans and Challenges

### Annual Savings

The Council needs to achieve significant savings and efficiencies in future budgets and to meet the Government's planned reduction in the public sector deficit. It is currently forecast that further very significant savings or additional income of around £5m over the next 4 years. This will depend upon a range of factors including the scale of Government grant cuts over this period that affect the Council.

The Council will continue to aim to minimise the impact on services of making the above savings, by working with others, including local communities, to find new ways of delivering services.

### Shared Services and Partnerships

The Council has established a Shared Revenues Partnership with Mid Suffolk District Council and Ipswich Borough Council and service provision will commence on 1<sup>st</sup> April 2011.

The Council is progressing its work with Mid Suffolk District Council to integrate staff and services and explore opportunities to transform how services are provided in the future. Following the 'No vote' in the advisory residents poll on constitutional merger and the creation of a single Council, each Council will continue to account separately for its own expenditure and income and for assets, liabilities, income, expenditure and cash flows.

The above plans are expected to make a significant contribution towards the future savings that will be required

## **10. Further Information**

The Council publishes a number of important documents to inform the public about the work of the Council. These (including the annual Statement of Accounts and Summary Financial Information) can be viewed and downloaded via the Council and Democracy page of the Council's website: [www.babergh.gov.uk](http://www.babergh.gov.uk).

Further information about the accounts is available from the Council's Director of Finance.

Mr Barry Hunter CPFA  
Babergh District Council  
Council Offices  
Corks Lane  
Hadleigh  
IPSWICH  
Suffolk  
IP7 6SJ

Tel: 01473 825819; Fax: 01473 823594; Email: [barry.hunter@babbergh.gov.uk](mailto:barry.hunter@babbergh.gov.uk)