

# Highland and Western Isles Valuation Joint Board

Report to Members and the Controller of Audit on the 2009/10  
audit

September 2010



 AUDIT SCOTLAND





# Contents

<b>Key Messages</b>	<b>1</b>	<b>Future outlook - Finance</b>	<b>5</b>
<b>Introduction</b>	<b>2</b>	<b>Corporate governance</b>	<b>8</b>
<b>Financial statements</b>	<b>3</b>	Overview	8
Auditor's report	3	Anti-fraud and corruption arrangements	8
Financial position	4	Systems of internal control	9
Issues arising	4	Future outlook - Governance	9
Legality	4	<b>Final Remarks</b>	<b>10</b>
Statement on the system of internal financial control (SSIFC)	5	<b>Appendix A: Action Plan</b>	<b>11</b>



# Key Messages

In 2009/10 we have audited the financial statements and looked at aspects of governance within Highland and Western Isles Valuation Joint Board. This report sets out our main findings.

Overall, we found the financial stewardship of Highland and Western Isles Valuation Joint Board (the Joint Board) during the year to be satisfactory. The main conclusions and outcomes from the audit are highlighted below:

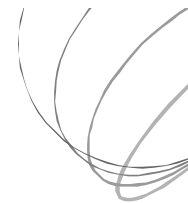
- An unqualified opinion has been issued on the financial statements for 2009/10
- The Statement on the System of Internal Financial Control included in the accounts complies with accounting requirements and is not inconsistent with audit findings.
- Final accounts preparation procedures and working papers were good and this enabled the audit to progress smoothly.
- Many aspects of a sound corporate governance framework are in place.
- A fraud strategy and written procedures for investigating suspected fraud cases are in place.

The Highland Council internal audit services, the Joint Board's Internal Auditor concluded that "reasonable assurance can be placed upon the adequacy and effectiveness of the Assessor's internal control systems for the year to 31<sup>st</sup> March 2010."

The Joint Board operates the corporate financial systems of The Highland Council under a Service Level Agreement. As external auditor of the council, we have also been able to take assurance from our work on these systems.

The UK economy is in its longest recession on record and the public sector is now facing deep and prolonged cuts in funding. It will be very challenging to maintain current levels of public services and meet new demands when resources are tight. This is further compounded by the on-going issue of funding pension liabilities. The Joint Board will not be immune to these financial pressures and will need to identify ways of delivering services with decreasing levels of income.

**Audit Scotland  
September 2010**



# Introduction

1. The members and officers of the Joint Board are responsible for the management and governance of the organisation. As external auditors, we review and report on the arrangements in place and seek to gain assurance that:
  - the financial statements have been prepared in accordance with statutory requirements and that proper accounting practices have been observed;
  - the Joint Board's system of recording and processing transactions provides an adequate basis for the preparation of the financial statements and the effective management of assets and interests;
  - the Joint Board has adequate corporate governance arrangements which reflect the three fundamental principles of openness, integrity and accountability;
  - the systems of internal control provide an appropriate means of preventing or detecting material misstatement, error, fraud or corruption; and
  - the Joint Board has proper arrangements for securing best value in its use of resources.
2. This report summarises the most significant issues arising from our work during 2009/10.



# Financial statements

3. The financial statements of the Joint Board are the means by which it accounts for its stewardship of the resources made available to it and its financial performance in the use of these resources. It is the responsibility of the Joint Board to prepare financial statements that provide a true and fair view of its financial position and the income and expenditure for the year.
4. In this section we summarise key outcomes from our audit of the Joint Board's financial statements for 2009/10, aspects of the Joint Board's reported financial position and performance to 31 March 2010, and provide an outlook on future financial reporting issues.

## Auditor's report

5. We have given an unqualified opinion on the financial statements of Highland and Western Isles Valuation Joint Board for 2009/10, concluding that the financial statements:
  - show a true and fair view, in accordance with relevant legal and regulatory requirements and the 2009 SORP, the financial position of the Joint Board as at 31 March 2010 and its income and expenditure for the year then ended; and
  - have been properly prepared in accordance with the Local Government (Scotland) Act 1973.
6. The Joint Board's balance sheet at 31 March 2010 shows net liabilities of £4.519 million. Auditing standards require auditors to consider an organisation's ability to continue as a going concern when forming an opinion on the financial statements. One of the indicators that may give rise to going concern considerations is an excess of liabilities over assets.
7. The net liability position is due to the requirements of Financial Reporting Standard 17 (retirement benefits) where there is an obligation to recognise the Joint Board's full pension obligations in the year they are earned. This technical accounting requirement has had no impact on the underlying basis for meeting current and ongoing pension liabilities which will be met, as they fall due, by contributions from constituent authorities in the normal way. In common with similar authorities, the Joint Board has considered it appropriate to adopt a going concern basis for the preparation of the financial statements as future actuarial valuations of the pension fund will consider the appropriate employer's contribution rate to meet the fund's commitments. The constituent authorities of the Joint Board are also liable to fund the Joint Board's liabilities as they fall due. We are satisfied that the process the Joint Board has undertaken to consider going concern is reasonable.



## Financial position

8. The Joint Board's net operating expenditure for 2009/10 amounted to £2.553 million (after elimination of FRS 17 pension adjustments) and was met by constituent authorities' contributions of £2.685 million resulting in an underspend for the year of £0.132 million. This will be refunded to the constituent authorities. The Treasurer's Report to the Board contained within the financial statements summarises performance against budget. There was an underspend in staff costs due to vacancies, and savings on property and supplies and services costs.

## Issues arising

9. The Joint Board's financial statements were submitted to the Controller of Audit by the deadline of 30 June. Final accounts preparation procedures and working papers were good and this enabled the audit to progress smoothly.
10. Local authorities in Scotland are required to follow the Code of Practice on Local Authority Accounting in the United Kingdom – A Statement of Recommended Practice (the 'SORP'). No major changes were introduced by the 2009 SORP. Overall, we were satisfied that the Joint Board had prepared the accounts in accordance with the revised SORP.
11. Audited accounts were finalised prior to the target date of 30 September 2010 and are now available for presentation to the Joint Board and for publication. The financial statements are an essential means by which the Joint Board accounts for its stewardship of the resources made available to it and its financial performance in the use of those resources.

## Legality

12. Each year we request written confirmation from the Treasurer that the Joint Board's financial transactions accord with relevant legislation and regulations. Significant legal requirements are also included in audit programmes and checklists. The Treasurer has confirmed that, to the best of his knowledge and belief and having made appropriate enquiries of members and officials of Highland and Western Isles Valuation Joint Board, the financial transactions of the Joint Board were in accordance with the relevant legislation and regulations governing its activities.
13. There are no additional legality issues arising from our audit which require to be brought to members' attention.



## Statement on the system of internal financial control (SSIFC)

14. Scottish authorities are required by the local authority SORP to include a statement on the system of internal financial control with their statement of accounts. The 2009/10 financial statements include a Statement on the System of Internal Financial Control which highlights the Treasurer's view that the Board can place reliance upon the effectiveness of the Board's financial systems.
15. The Joint Board operates the corporate financial systems of The Highland Council under a service level agreement. The statement highlighted that assurance had been taken from the work done by The Highland Council's internal audit service on these corporate financial systems and also work done on the Centralised Assessors Tax System. The statement complies with accounting requirements and is not inconsistent with the findings of our audit.
16. The SORP states that authorities *may choose* to include a wider statement of internal control in place of a statement of internal financial control. The CIPFA framework document *Delivering good governance in local government* recommends that the review of the effectiveness of the system of internal control should be reported in an annual governance statement. LAAP bulletin 71 *The Annual Governance Statement* clarifies that authorities are encouraged (but not required) to include an annual governance statement with their accounts. The Joint Board may wish to consider moving to an Annual Governance Statement in future years.

## Future outlook - Finance

### National economic conditions

17. The UK economy is in its longest recession on record and the public sector is now facing deep and prolonged cuts in funding. At a UK level, real term reductions of 2.3 per cent each year are projected for Departmental Expenditure Limit (DEL) budgets between 2011 and 2014. Current forecasts are that any real term growth in public spending over the next two spending review periods (2011 to 2018) will continue to be constrained and will not return to the levels seen over the last decade.
18. Whilst the Scottish Government has implemented an economic recovery programme to support the economy through this period of decline, demand for public services continues to rise adding to the on-going strain on public sector resources. The Joint Board will not be immune to these financial pressures. It will need robust information about activity, costs and performance to identify ways of more effectively delivering services with decreasing levels of income. The Joint Board may wish to consider developing a "recession impact action plan" to help address the future funding difficulties.

**Key risk area 1**

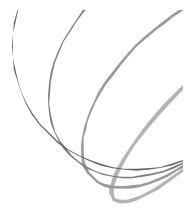




## Pension liabilities

19. Financial planning and accounting for the costs of pensions presents a difficult challenge. The amounts involved are large, the timescale is long, the estimation process is complex and involves many areas of uncertainty that are the subject of assumptions. In accounting for pensions, Financial Reporting Standard 17 (Retirement of Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in a very large future liability being recognised on the face of annual accounts.
20. The Joint Board participates in the Local Government superannuation Scheme (Highland Pension Fund), a defined benefits scheme administered by The Highland Council. Note 6 to the Core Financial Statements highlights that the Joint Board's scheme net liabilities at 31 March 2010 are £13.808 million, an increase of £4.788 million from the previous year. This was due to significant reduction in bond yields which outweighed the large increases in the market values of assets.
21. A full actuarial valuation of the Highland Pension Fund was carried out as at 31 March 2008 which showed an increase in the funding level, calculated as the ratio of fund assets to past service liabilities, increasing from 92% as at March 2005 to 98% as at March 2008. This is mainly due to the fund achieving a better rate of investment return than had been anticipated in the previous valuation and better statistical outcomes than assumed in 2005, for example, more early leavers, lower number of retirements and less death in service. The actuary is required to make a 3-year assessment of the contributions that should be paid by the employing authorities as from April 2009 to maintain the solvency of the fund. The current 3-year assessment set budgeted contributions, expressed as a percentage of employees' contribution rates at 275% for 2009/10 and 290% for the next two years.
22. In 2006/07 changes to the pension regulations allowed individuals to elect to receive a larger lump sum payment in return for a reduced annual pension. An assumption that 50% of retirees would opt to take the larger lump sum in return for a reduced annual pension was made. This is one of a number of assumptions made by the actuary in calculating pension costs. However, we are not aware of the Joint Board, or the administering authority undertaking any confirmation that the assumptions applied are appropriate to local circumstances. We would highlight that actuarial reports are only advisory and the Joint Board should confirm it is satisfied with the assumptions/rates used in these reports.

**Key risk area 2**



## International Financial Reporting Standards Adoption

23. Local government will move from UK Generally Accepted Accounting Principles to International Financial Reporting Standards (IFRS) with effect from 2010/11. A comparative balance sheet as at 1 April 2009 will be required as well as at 31 March 2010 and 2011. We have been advised that preparatory work on the IFRS balances has started and that restated opening balances are now available.



# Corporate governance

24. In this section we comment on key aspects of the Joint Board's governance arrangements during 2009/10 and provide an outlook on future governance issues.

## Overview

25. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviours at the upper levels of the organisation. The Joint Board has a responsibility to put in place arrangements for the conduct of its affairs, ensure the legality of activities and transactions and to monitor the adequacy and effectiveness of these arrangements in practice.
26. In previous years we have concluded that the Joint Board has many aspects of a sound corporate governance framework in place and have reached the same conclusion this year. It was reported in the April 2010 board meeting that some corporate governance arrangements and policies are undergoing review to make them more relevant and up to date and progress will be reported to the next board meeting.
27. It was reported to the Joint Board in November 2009 that there has been modest progress in activities relating to its equality duties. The Board believes that the process of consolidating these equality policies under a single scheme will provide the opportunity for a more realistic and committed approach to ensure the Joint Board's legal and moral obligations in these areas are met.
28. Internal audit plays a key role in the Joint Board's governance arrangements, providing an independent appraisal service to management by reviewing and evaluating the effectiveness of the internal control system. The Highland Council's internal audit service has provided an internal audit service to the Joint Board during 2009/10.

## Anti-fraud and corruption arrangements

29. The Joint Board has appropriate arrangements for the prevention and detection of fraud and corruption. These arrangements include a strategy for the prevention and detection of fraud and corruption, written procedures for the investigation of suspected cases of fraud and corruption and a whistle blowing policy. As mentioned above, these documents are among those currently being reviewed to make them more up to date.



## Systems of internal control

30. The Highland Council internal audit service, the Joint Board's internal auditors, concluded "...that reasonable assurance can be placed upon the adequacy and effectiveness of the Assessor's internal control systems for the year to 31<sup>st</sup> March 2010."
31. During the year we reviewed the Internal Audit structure and function in accordance with International Standard on Auditing 610 and concluded that The Highland Council's internal audit service was well managed and operated to acceptable standards. We reviewed the internal audit work on the Computerised Assessors Tax System and have been able to take assurance that overall the controls can be relied on.
32. The Joint Board operates the corporate financial systems of The Highland Council under a service level agreement. As external auditors of the Council, we have been able to take assurance from our work on these systems. We have also undertaken audit testing focussing on the high level controls in place at the Joint Board within the main accounting, budgetary, accounts payable and NDR/valuation systems and have concluded that we can rely on these systems to give us assurance on the financial statements. However the absence of written detailed procedural guidance covering accounts payable and budgetary systems is a weakness.

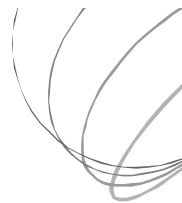
**Key Risk Area 3**

## Future outlook - Governance

### Single Status and Equal Pay

33. The 1970 Equal Pay Act makes it unlawful for employers to discriminate between men and women in terms of their pay and conditions where they are doing the same or similar work. In 1999 a single status agreement was reached between Scottish local authorities and trades unions to harmonise the terms and conditions of manual and administrative, professional, technical and clerical workers (covering pay, working hours, leave and negotiating mechanisms). There was a presumption that single status would be cost neutral with any increased costs being offset by savings arising from changes to other conditions of service or from efficiencies.
34. The Joint Board has yet to conduct a formal exercise to ensure that it is compliant with single status and equal pay legislation. Due to the profile of its workforce, the Joint Board believes that it does not have a material exposure to any potential liability arising from the eventual implementation of the afore-mentioned issues. However, until this exercise is completed the Joint Board is not compliant with the legislation.

**Key Risk Area 4**



# Final Remarks

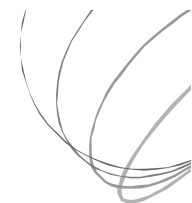
35. Attached to this report is an action plan setting out the key risks identified by the audit which we are highlighting for the attention of members. In response, officers have considered the issues and have agreed to take the specific steps set out in the column headed 'planned management action'. On occasion, officers may choose to accept the risk and take no action. Alternatively, there may be no further action that can be taken to minimise the risk. Where appropriate, the action plan clearly sets out management's response to the identified risks.
36. Appropriate mechanisms should be considered and agreed by members for monitoring the effectiveness of planned action by officers. We will review the operation of the agreed mechanism as part of the 2010/11 audit.
37. The co-operation and assistance given to us by Highlands and Western Isles Valuation Joint Board members and staff is gratefully acknowledged.



# Appendix A: Action Plan

## Key Risk Areas and Planned Management Action

Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
1	18	<p>The Joint Board does not have a “recession impact action plan” to help address future funding difficulties. It will need robust information about activity, costs and performance to identify ways of more effectively delivering services with decreasing levels of income.</p> <p><b>Risk: The Joint Board may not be adequately prepared to deal with the impact of recession and funding constraints.</b></p>	<p>A recession impact action plan will be presented to the November board meeting.</p>	Assessor	Nov 2010
2	22	<p>In accounting for pensions, Financial Reporting Standard 17 (Retirement of Benefits) is based on the principle that an organisation should account for retirement benefits at the point at which it commits to paying them, even if the actual payment will be made years into the future. This requirement results in a very large future liabilities being recognised on the face of annual accounts. An actuarial calculation of the FRS17 impact is provided to the Joint Board each year however no review of the assumptions or rates applied by the actuary is carried out to ensure the Joint Board is satisfied that these are appropriate to local circumstances.</p> <p><b>Risk: FRS 17 pension costs, assets and liabilities are based on inaccurate or inappropriate assumptions.</b></p>	<p>Actuaries request and are provided fund specific information on which to base their FRS 17 estimates.</p> <p>The Pensions team in the Highland Council will in future conduct a high level check of the FRS 17 reports for assurance where possible that the reports are broadly consistent with the fund specific data provided.</p> <p>However it will not be possible to conduct a detailed review all of the actuarial assumptions and consequent outcomes.</p>	Treasurer	31 May 2011



Action Point	Refer Para No	Risk Identified	Planned Management Action	Responsible Officer	Target Date
3	32	<p>The Joint Board does not have detailed procedural guidance covering the day to day operations of its accounts payable and budgetary control systems.</p> <p><b>Risk: Procedures may not be applied consistently and in accordance with instructions resulting in errors and irregularities.</b></p>	Procedures will be drawn up.	Assessor	Nov 2010
4	34	<p>The Joint Board has yet to conduct a formal exercise to ensure that it is compliant with single status and equal pay legislation. Due to the profile of its workforce, the Joint Board believes that it does not have a material exposure to any potential liability arising from the eventual implementation of the aforementioned issues.</p> <p><b>Risk: the Joint Board is not compliant with the legislation and may be exposed to lower staff morale</b></p>	The Board's personnel adviser is looking into this and the review is planned for 2011/12.	Assessor	During 2011/12