

Stevenage Borough Council

Report to Those Charged With Governance (ISA 260)

For the year ended 31 March 2012

Contents

1	Executive summary	2
2	Key audit issues	4
3	Audit adjustments	8
4	Design effectiveness of internal controls	9
5	Other reporting matters	11
6	Value for Money	13
A	Recommendations	15
B	The small print	16

1 Executive summary

1.1 Purpose of this report

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

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

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

1.2 Introduction

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

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

- updating our post balance sheet events review, to the date of signing of the accounts
- receipt of the letter of representation

- receipt of bank and investment confirmations
- receipt of legal letters
- final review of financial statements
- review of Whole of Government Accounts.

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

1.3 Key audit and financial reporting issues

Financial statements opinion

We did not identify any significant audit adjustments that impact on the Council's income and expenditure position (statement of comprehensive income) or balance sheet (statement of financial position). Adjustments processed to the accounts were minor and of a presentational nature only and had no overall net effect on the Council's reported assets and liabilities.

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

- In order to align the valuation of non-HRA properties with HRA properties at 1 April, there was no valuation completed as at 31 March 2012. The valuation as at 31 March 2011 was rolled over to 1 April 2011. We have reviewed the approach used by the Council in terms of the valuations performed for non-HRA properties and assessed whether the valuation of non HRA properties is still applicable and appropriate. We are satisfied that the procedures in place are sound

and that judgements which impact the value of the assets have been applied appropriately.

Further details are set out in sections 2 and 3.

At this stage of the audit, we anticipate issuing an unmodified audit opinion, following approval of the financial statements by the Audit Committee.

Value for money conclusion

We are pleased to report that, based on our review of the Council's arrangements, we propose to issue an unqualified opinion. We have identified a number of findings that should be addressed by the Council in order to ensure continued financial resilience, and sustainable economy, efficiency and effectiveness in its use of resources.

Further details are set out in section 6.

1.4 Controls

Roles and responsibilities

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

Our audit is designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we did identify any material control weaknesses, we report these to the Council.

1.5 Acknowledgement

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

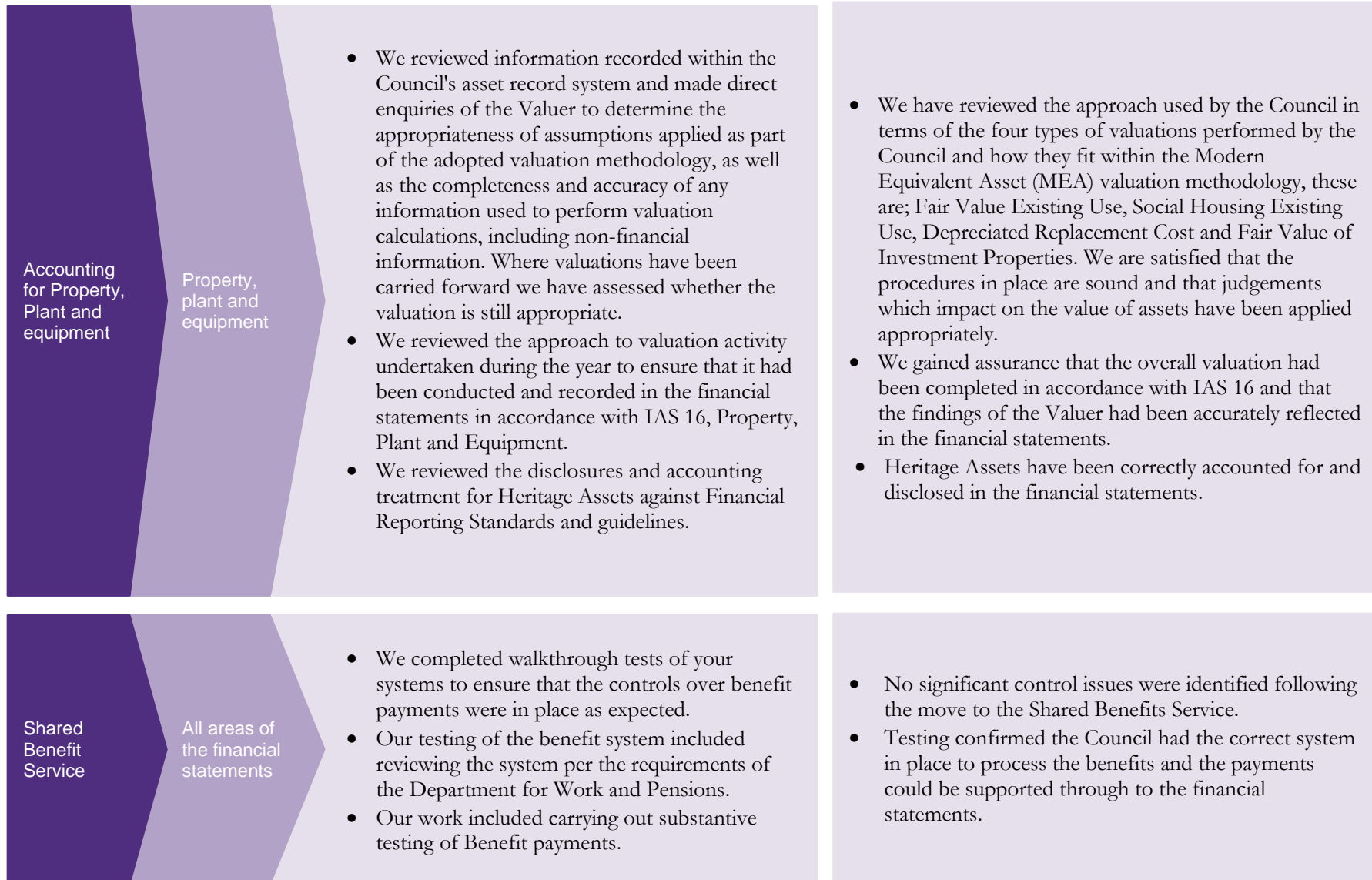
Grant Thornton UK LLP

24 August 2012

2 Key audit issues

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

Issue	Audit areas affected	Work completed	Assurances gained
Financial performance pressures	All areas of the financial statements	<ul style="list-style-type: none"> We have maintained on-going liaison with the Finance Team regarding any emerging issues. We have reviewed the Executive and Audit Committee minutes and papers to identify and understand the key pressures that the Council is facing in meeting the agreed budget. 	<ul style="list-style-type: none"> We have tested both revenue and expenditure, concluding that the reported total comprehensive income and expenditure balance does not appear to be materially misstated. We monitored the financial position of the Council as well as reviewing the use of reserves during the year. This has not identified any significant issues. We carried out a specific review on the Council's financial resilience as part of our Value for Money work. The key findings from this report are included within section 6 of this report.



Stevenage Homes	All areas of the financial statements	<ul style="list-style-type: none">• We confirmed with management the basis for integrating the Stevenage Homes accounting within the Council financial reporting process.	<ul style="list-style-type: none">• Although the integration was effective from the date of transfer (1 December 2011), the full impact of savings as result of the integration will not been seen until the end of 2012/13.• Testing performed on HRA balances did not highlight any significant issues.
IT Control Environment	All areas of the financial statements	<ul style="list-style-type: none">• Our specialist Technology Risk Services (TRS) team have followed up on the 2010/11 review of the IT control environment in place at the Council.	<ul style="list-style-type: none">• From the work undertaken, we were able to conclude that there are no material weaknesses which are likely to adversely impact on the Council's financial statements.• Our findings from the review have been included within Section 4 of this report.
Use of estimates and judgements	All areas of the financial statements	<ul style="list-style-type: none">• We have considered the key risk areas within the financial statements and those areas where estimates and judgements are likely to be used.• We reviewed significant estimates and judgements including ensuring they are in accordance with the requirements of the Code of Practice.	<ul style="list-style-type: none">• The Council continues to apply key estimates and judgements over impairments of receivables, property, plant & equipment and provisions. Testing performed throughout the course of the audit has provided assurance over the judgements made by the Council.• We are satisfied that the council has viewed all significant estimates and judgements in accordance with the Code of Practice.

2.1 Matters identified during the course of the audit

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

HRA I&E Statement, return of SHL surplus:

The Council recorded £764k in relation to the surplus at Stevenage Homes Limited within non-dwelling rental income. This represents the cumulative surplus within SHL to the date of transfer of housing from SHL on 1 December 2011. The Council have previously agreed the return of surpluses in excess of £400k from SHL (when it was a separate entity), which was recorded within management fees. This is considered a non-recurring item this year. Management have confirmed that they consider this to be the most suitable place to record the balance. We agree with this treatment.

Note 21, Cash and cash equivalents:

At the year end the accounting records included a bank balance of overdrawn (£488k), however, in the notes to the financial statements the balance is recorded as overdrawn (£8k). This is as a result of the ledger bank account not reflecting an overnight transaction. A manual adjustment of £480k was therefore made to accurately reflect the actual bank account position at 31 March 2012. We agree with this presentation.

Note 20 & 23, Council Tax re-classification:

The Council had incorrectly disclosed the proportion of debtors and creditors which relate to the precept authorities Hertfordshire County Council and Hertfordshire Police Authority. We have proposed an adjustment of £1,197k so that only SBC debtors are recorded within the collection fund. This has been adjusted in the financial statements.

3 Audit adjustments

3.1 Introduction

A number of adjustments to the draft accounts have been identified during the audit process. We have reported all misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

3.2 Impact of adjusted misstatements

All adjusted misstatements are set out in detail below.

	Detail	Balance sheet £000	Statement of comprehensive income,£000
1	Reclassification: An adjustment was made to correct debtors and creditors in respect of the precept authority's share of the collection fund.	1,197	-
2	Reclassification: An adjustment was made to write off a double counted HRA plant and equipment as a de-recognition rather than as a revaluation adjustment.	1,219	-
3	Disclosure: There were a number of minor presentational changes that arose during the course of the audit that have been made to the financial statements.	-	-
Net Impact		-	-

3.3 Unadjusted misstatements

There were no unadjusted misstatements.

4 Design effectiveness of internal controls

4.1 Accounting system and internal control

Our audit is not designed to identify all significant weaknesses in the Council's internal controls but is designed primarily for the purpose of expressing our opinion on the financial statements of the Council. However, where, as part of our testing, we identify any control weaknesses, we report these to you.

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

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

4.2 Management of the risk of fraud

We have considered the processes in place to identify and respond to the risk of fraud at the Council.

The Council considers that there are adequate processes in place to mitigate against the risk of fraud occurring at the Council and that those charged with governance have sufficient oversight over those processes to give them the assurances they require in this area.

4.3 Review of information technology controls

Our information systems specialist performed a high level review of the general IT control environment, as part of our overall review of the

internal controls system. We also performed a follow up of the issues that have been raised in the previous year.

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

We have, however, reiterated areas for improvement identified during the course of our work in these areas. We do not consider these to pose a significant risk to the accounts, and have provided some detail below. Where appropriate, we have made recommendations for improvement, as set out in the agreed action plan at Appendix A.

IT Security Policy approval and awareness:

Within the IA report dated May 2011, the Council committed to address the following areas:

- general tightening of security controls, policies and processes
- improved laptop security
- stricter controls for 3rd party access to the SBC network
- a solution for managing removable media
- clearer protocols for the use of smart phones
- better informed staff able to work safely and securely
- staff sanctions to be agreed with HR

At the time of our review, we noted that draft policies and procedures over IT security had not yet been approved by the Strategic Management

Board (SMB) and consequently, these had not yet been communicated to Council members of staff except for the policy for Internet and Email use. We were informed that the revised target date for the approval of the policies was by April 2012.

Subsequent discussions with management have identified that Removable Media and Security Incident Management Policies were agreed by the Council's Senior Management Board on 3 July 2012. This followed a period of consultation with staff about the new policies conducted via a survey and a series of drop in sessions and was followed by communication of the new policies to all staff.

The solution for encrypting data held on USB sticks has been implemented on all devices bar laptops. The project to implement this solution on laptops and to encrypt laptops generally is 75% complete and has been hindered by the absence on long term sickness of a key member of staff.

The smart phone security project has also now concluded and as a result smart phones using android, blackberry, Symbian and apple operating systems will be supported by the ICT Team and are considered to meet the requirements of the Council's security policies.

In addition, at the time of the review, no defined plans and target dates had been agreed with the Human Resources (HR) department to ensure that existing staff will go through security awareness training. Discussion with management has confirmed that the new security policies will be incorporated into the existing training provided on ICT security to all new starters. Discussions are also to take place with HR to establish how ICT security refresher training should be incorporated into the new corporate training programme.

Remote access:

The Internal Audit (IA) review in May 2011 stated that remote access to the network is allowed, with a list of staff who have such authorised access on a list held by CSBI. All staff are issued with relevant instructions. This access is not restricted to SBC managed equipment, as

with approximately 200 current users having logged into the system on at least one occasion, the cost of providing managed equipment for so many is considered to be prohibitive.

We noted that not all remote access users are authenticated using two-factor mechanism. However, there is a risk based approach related to the impact level of data that can be accessed by the user and where a job role requires access to sensitive data, two-factor mechanism is used. This process is detailed in the IT Security Policy. ICT network administrators have been using two-factor authentication for over 12 months.

Review of user access rights:

We noted that there is also no periodic review of users' AD group membership. If group memberships are not reviewed by Service Delivery Unit management on a regular basis, there is a risk that there will be an accumulation of access rights. To aid in this process, IT are attempting to create job based groups across the Council. This will attach rights and privileges to a role and individuals will be moved between these relevant roles as necessary.

Audit policy settings:

Audit policy settings in AD were not defined at the time of the review, but have subsequently been switched on. In place of AD, the Council had been using 'Event Tracker' to perform the function. This was considered to be an adequate mechanism to capture relevant events which may be useful in identifying potential security breaches or for use in investigations when a security incident takes place.

5 Other reporting matters

5.1 Other assurance reviews

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

VAT

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

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

From the information available, there did not appear to be any material VAT issues. Two recommendations have been raised in Appendix A around the following points:

- a) No partial exemption calculations have been carried out in the last three years. This could result in claims for potentially irrecoverable VAT. Having considered the overall activities and the relatively steady nature of those activities, there is no compelling reason to assume that the Council exceeds the 5% threshold. However, the calculations should be carried out at the earliest opportunity.
- b) The arrangements for the Leisure Facility lease could result in VAT recovery. It would, therefore, be prudent for the Council to

review the arrangements to determine the basis for VAT recovery relating to the basis on which leisure facilities have been provide to Stevenage Leisure Ltd.

Fraud

A high level review of the overall adequacy of arrangements was undertaken to ensure that the risk of fraud and corruption is being effectively addressed by the Council's current arrangements. No issues were noted from the review completed.

5.2 Annual governance statement

We have examined the Council's arrangements and processes for compiling the AGS. In addition, we have read the AGS and considered whether the statement is in accordance with the requirements of the Code and consistent with our knowledge of the Council.

We have considered that the Council has good arrangements in place to compile the AGS and provide an appropriate audit trail for the Chief Executive and Leader to sign the statement.

5.3 Public Challenge Matters

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

5.4 Next steps

The Audit Committee is required to recommend to Council the financial statements for the year ended 31 March 2012. In forming its conclusions the Committees attention is drawn to the financial statements and the required Letter of Representation.

6 Value for Money

6.1 Value for money conclusion

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

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

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

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

The Council has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

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

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

6.2 Key findings

Securing financial resilience

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

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

The key findings from this review are:

- The Council has a good track record in managing expenditure against budget. This reflects good performance in challenging financial times.
- The lack of brought forward capital receipts for the General Fund means that borrowing is required. Currently, the Council are utilising investment balances in preference to taking out additional borrowing. The Council have recognised that borrowing is not a long term solution and that this can only really support the capital programme in the short term.
- With the introduction of the Localism Bill, there are to be some fundamental changes to Council financing going forward. From 2013/14, there will be the localisation of both Council Tax Benefit and Business Rates and also the centralisation of other benefits with the

introduction of the Universal Credit from 1 October 2013. These all represent significant changes for the Council to respond to, and they must ensure that planning is able to react to the uncertainties that these changes will bring.

- The Council are currently progressing their Asset Management Strategy. It is recognised that that *"in order to have a sustainable, affordable General Fund Capital Strategy, it is imperative that the Asset Management Plan is implemented to release resources to reduce the burden on the General Fund and ensure that the capital programme delivers the right investment outcomes for the Council's assets."*

Our detailed findings will be reported separately to the September Audit Committee.

Challenging economy, efficiency and effectiveness

To support our conclusion against this criteria we have reviewed whether the Council has prioritised its resources to take account of the tighter constraints it is required to operate within by achieving cost reductions and improved productivity and efficiencies.

We have completed a review against key risk indicators which has not highlighted any significant issues that would impact on our conclusion in respect of this criteria.

As part of our 2011/12 audit plan, we agreed with management the benefits of reviewing the Council's plans for developing a detailed business case for ICT shared services across North Hertfordshire District Council, East Hertfordshire District Council and Stevenage Borough Council. This was to enable us to gain an understanding of the Council's key internal control, risk management and governance activities in

assessing the potential business benefit of establishing such a shared service.

We have reviewed and challenged the risk assessment that the Councils' are performing. Although we have not performed any financial assessment of the business case itself, we have provided guidance around what the Councils should consider if they make a decision to pursue a shared service. The Councils have engaged the services of an independent third party, SOCITM, to review the technical arrangements for the proposed hosting data centre, for any shared service that is pursued.

We have met with key staff at both the operational and senior management level, to gain an understanding of the governance structures in place to oversee the business case development process. In addition, we have reviewed key documents that support the process in place for risk management and governance activities and controls, to assess how well current and future needs and investment decisions are made, and whether they are at the appropriate level. This review has not highlighted any significant issues with the governance arrangements.

Our detailed findings will be reported to the Audit Committee separately in November 2012.

6.3 Overall conclusion

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

A Recommendations

	Assessment	Recommendation	Management comments	Implementation date and responsibility
<i>IT recommendations:</i>				
1	Medium	Defined plans should be agreed with the HR department on the roll out of training sessions to existing SBC staff.	Discussions are to be undertaken with HR to establish how security refresher training should be incorporated into the new corporate training programme.	A date will be agreed once the internal review of HR priorities has been completed.
2	Medium	We recommend Service Delivery Unit management periodically review AD group membership of users on a rolling basis, i.e. department by department basis. This will help give management assurance that user access is appropriate to their job responsibilities. In addition, IT should ensure that job based groups are set up across the Council to help attach the relevant rights and privileges to individuals.	ICT now use role based groups in active directory and have done so for more than a year. We agree to implement a form of management review for the role based groups within active directory.	ICT Services, Security and Standards Manager by October 2012.
<i>VAT recommendations:</i>				
3	Medium	Partial exemption calculations should be carried out at the earliest opportunity.		
4	Medium	The Council should review the arrangements to determine the basis for VAT recovery relating to the basis on which leisure facilities have been provided to Stevenage Leisure Ltd.		

B The small print

ISAUK 260 requires communication of:

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

Purpose of report

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

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

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

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

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

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

Responsibilities of the directors and auditors

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

Clarification of roles and responsibilities with respect to internal controls

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

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

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

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

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

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

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

Independence

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

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

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

Statutory audit	£140,730
Other assurance services	£40,000*
Total	£185,730

* Certification of claims and returns £40,000 (est)

Audit quality assurance

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

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

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



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