

**EXTRAORDINARY PERFORMANCE SELECT COMMITTEE held at
COUNCIL OFFICES LONDON ROAD SAFFRON WALDEN at 6.00 pm on
11 DECEMBER 2007**

Present:- Councillor H S Rolfe – Chairman.
Councillors S Barker, A J Ketteridge, T P Knight and
P A Wilcock.

Also present:- Councillors K R Artus, C A Cant, R H Chamberlain,
R P Chambers, J F Cheetham, A Dean, C M Dean,
K L Eden, E J Godwin, J E Menell, G Sell and
A C Yarwood.

Officers in attendance:- A Bovaird, D Bradley, A Clarke, R Pridham,
C Roberts, A Webb and P Woolcott.

Also present:- P King, M Matthews and C Rockall – Audit Commission.

PS47 APOLOGIES FOR ABSENCE

Apologies for absence were received from Councillors M L Foley, M A Gayler
and J Salmon.

PS48 STATEMENT OF INTERNAL CONTROL 2006/07

The Committee considered the report of the Acting Chief Financial Officer
containing the Statement of Internal Control 2006/07.

The Acting Chief Financial Officer introduced Mr D Bradley, the Acting Head
of Finance. Mr Webb then explained that a suitable revised form of words had
been achieved with the assistance of the Audit Commission for the
appropriate paragraphs of the revised Statement of Internal Control.

Mr P King of the Audit Commission agreed but asked that in the third
paragraph on page 6 the word 'robust' be deleted and that in the penultimate
on page 7 the words 'currently ... IT etc' be replaced by 'currently the Acting
Chief Financial Officer is carrying out the responsibilities of the Chief Finance
Officer and further support at a senior level is being provided by resources
from Public Sector Consultants Ltd'.

Mr King added that the Audit Commission's report expressed the Audit
Officer's warm appreciation of the support given to their investigations by the
Acting Chief Financial Officer and his staff.

RECOMMENDED that the Statement of Internal Control be approved
and published.

**AUDIT COMMISSION'S REPORTS – ANNUAL GOVERNANCE REPORT
AND USE OF RESOURCES SUMMARY REPORT**

Mr P King of the Audit Commission explained that these reports were a follow up to the report submitted to the previous meeting of the Performance Select Committee in November. He asked that they be read in the context of the report submitted to that meeting.

He referred to the key messages at paras 6-8 of the report and to para 10. A question had arisen as to the correctness of the categorisation of the waste vehicle leasing arrangement. Following receipt of technical advice the Audit Commission was of the view that it was in fact a finance lease rather than an operating lease. They had taken into account the terms of the agreement and its substance as well as the penal nature of the clause providing for payment to opt out, at year five, of the ultimate purchase of the vehicles.

In the light of this it was considered that the arrangement was in substance a finance lease even though it fell technically within the band of arrangements presumed to be operating leases. The consequences of this were that the vehicles should have been disclosed as assets within the Council's balance sheets and the accounts would require to be re-worked to accommodate this.

In answer to questions from the Chairman he confirmed that the five-year break clause was of no cost benefit to the Council and that the arrangement should be treated as a seven year lease; the accounts could be re-worked to recognise the vehicles as fixed assets with liability and the annual lease payment divided between principal and interest for the purpose of allocating costs. If the accounts were not re-worked the situation would attract a qualified audit statement.

Councillor S Barker asked how soon it was necessary for the Council to decide on its action in this regard. She also asked about the status of the vehicles as an asset since a capital asset could not form part of the reserves.

Mr King answered that the debt free status of the Council would no longer apply since the arrangement was a finance lease and treated as borrowing. Mr D Bradley explained that the process of re-working would involve a substantial amount of re-writing of the accounts; the asset value would be a fair value of the lease.

Councillor T Knight asked in the light of the complexity of the matter, why specialised advice had not been sought by the then Director of Resources. She also asked whether the reauditing of the accounts by the Audit Commission would be done at twice the price of one audit or whether there would be a discount. She asked the Audit Commission to proffer advice as to how the Council should extricate itself from this particular problem.

The Chairman of the Committee commented that he thought the arrangement was structured so as to fall within the threshold of arrangements presumed to amount to operating leases. He enquired about the consequences and Mr P King said that if the accounts were reworked the asset would go on the balance sheet and therefore the Council's debt free status would disappear

but he thought that this would happen whether or not the accounts were reworked.

Councillor Rolfe asked what impact the situation would have on the revenue account and Mr King said that the £310,000 per annum lease charge would be charged to the revenue account. He was however unsure of the impact on the revenue account of treating that arrangement as a finance lease; it was not clear whether that would reduce the charge to the new account. In the light of this he was unsure which option was the best for the Council.

Mr Bradley confirmed that the situation had been revealed only that afternoon and it was not yet possible to assess the implications.

The Acting Chief Financial Officer stressed that since the Audit Commission said the arrangement was a finance lease the question was whether to correct it for 06/07 or to accept that the 06/07 accounts would be qualified and then correct the accounts for 07/08. Mr King added that the arrangement was regarded as a finance lease unless the Audit Commission received further evidence from the Council to rebut this assumption. In answer to a question from Councillor Wilcock he confirmed that although it was clear that the intention of the Council had been to enter an operation lease, this did not alter the substance of the actual arrangement.

In answer to questions from the Chairman, Mr King explained that there were no criminal sanctions for not reworking the accounts. Bad publicity was the main disadvantage and it would be possible for the Audit Commission to insert into the Audit opinion of the accounts that there was intent to rectify the matter in the next financial year, provided this was peer reviewed and acceptable within the Commission.

In answer to questions from Councillor T Knight the Acting Chief Financial Officer explained that the waste vehicle arrangement was entered into on the decision of the Director of Resources with a consultant. He added that there was a time delay between the purchase of the vehicles and the lease arrangement which had been entered into due to insufficient funds for the scheme.

Members agreed that they would recommend that the Council accept the qualification on the accounts rather than the alternative of re-working the accounts, in the light of the information about the altered category of the waste vehicle leasing arrangement.

Mr King then explained the remainder of his reports referring to the written representations from management to be contained in the letter within the report. It was noted that paragraph (o) of that letter became redundant in view of the decision about the leasing arrangement.

Mr King also drew attention in particular to the adjustments to the financial statements and expressed appreciation to Adrian Webb and David Bradley for their work with the Audit Commission on this aspect. It was stressed that the adjustments referred to were material and were recorded in Appendix one of the report.

In answer to questions from the Chairman of the Committee whether any of the reserves were affected by the adjustments, Mr King explained that the deficit on income expenditure, the fixed asset statements and the cash flow statement were affected by the adjustments but that there were no changes to the cash reserves.

Members were concerned to be assured that procedures had now been tightened so as to prevent recurrence of similar need for adjustments. Councillor S Barker said that it seemed that audits were topic based rather than process based.

The Chief Executive said that he intended, with the Chief Financial Officer and internal and external audit representatives, review the current and future audit plans to ensure that all involved had a better appreciation of each others roles and that a report would be brought to the next meeting of the Performance Select Committee on this.

Councillor T Knight suggested that external audit should act more closely with internal audit to anticipate and prevent this sort of problem. In particular they should have quarterly contact with internal audit to this end. The Chairman of the Committee agreed that this aspect would be addressed at the next meeting of the Performance Select Committee.

Mr King agreed that the Audit Commission needed to work more closely with internal audit and said he accepted the comments made and would take note of them.

Members were agreed that the Chairman on behalf of the Performance Select Committee would discuss with the Audit Commission the points being raised by individual Members and the Chief Executive said that he expected to bring a revised Audit Plan to the Committee for approval.

Mr King referred to the list of audit issues still to be resolved, set out in appendix 3, explaining current progress. It was noted that in the appendix 5 conclusion, the date 31 March 2006 should read 31 March 2007.

In answer to a question from Councillor A Dean, Mr King informed him, in the context of the value for money conclusion, that the current list of criteria not met was greater than the previous year's list.

RESOLVED that

- 1 the Committee recommends the Council to accept a qualified audit statement on the accounts rather than undertaking reworking of the accounts for 2006/07.
- 2 subject to the removal of para (o) from the Management Representation Letter as a consequence of 1 above, the letter be approved for signature and despatch.
- 3 the Chairman of the Committee on behalf of the Performance Select Committee discusses with the Audit Commission points regarding liaison of internal and external audit raised by Councillor T Knight

STATEMENT OF ACCOUNTS 2006/07

The Acting Chief Financial Officer circulated a replacement cash flow statement document to update the one in the Statement of Accounts.

The Chairman of the Committee referred to the summary report from the Audit Commission. He commented in particular on the mis-statements about budget interest and also about pensions which had been repeated in the 2007/08 accounts. He also drew attention to the Council having drawn £1.5m from the reserves in 2006/07.

Mr D Bradley explained that the process of budgeting for the 2007/08 accounts had been started before the 2006/07 accounts were completed, hence the repetition of the earlier figures. Currently however budgeting monitoring reports were being taken direct from the ledger itself. Heads of Division were receiving monitoring on revenue and capital and there was to be a detailed review of budgeting before April 2008.

Mr P Woolcott asked if the original processes had been correct, what had changed in 2006/07 to permit the errors to be made.

The Chairman of the Committee answered that there had been a trend. A deficit of £335,000 had occurred in 2005/06 and in 2006/07 £1.5m had been drawn from reserves. The Council had been living beyond its means two years previously.

Members discussed the detail of the Statement of Accounts and Councillor K Eden asked about the valuation of Section 106 Agreements. Mr Bradley explained that they were not valued but were cash received which had to be spent as stipulated by the agreements, and was not the Council's money.

In answer to a question from Councillor S Barker, Mr Bradley explained how the subsidy elements of the negative housing subsidy had changed.

In answer to a question from Councillor K Artus, Mr P King explained that the Council was regarded as the highest audit risk in Essex because of the significant number of misstatements which had been discovered in the 2006/07 accounts.

RESOLVED that a report be brought to the next meeting of the Committee on the financial operation of the Section 106 agreements.

RECOMMENDED having considered all issues and the observations of the Audit Commission that the Performance Select Committee is content to refer the revised statement of accounts for 2006/07 to the Council recommending:

- 1 that the Council does not rework the 2006/07 accounts and accepts the consequences of a qualified audit statement on the account and the loss of debt free status
- 2 that it be noted that:-

the Council has entered a finance rather than an operating vehicle lease for its waste vehicles;

the Council has received a classification of category one ("inadequate") from the Audit Commission as regards its use of resources;

the Council did not set a balanced budget for 2006/07, which led to an overspend of £770K and unplanned use of reserves.

The meeting ended at 7.23 pm.