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Loch Lomond & The Trossachs National Park Authority

Internal audit report 2014-15

Fixed Asset Register

23 February 2015

Contents

This report is for:

Action

Jaki Carnegie – Director of Corporate Services (Loch Lomond & The Trossachs National Park)

Information

Audit Committee

Notice: About this report

This Report has been prepared on the basis set out in our Engagement Letter addressed to Loch Lomond & The Trossachs National Park Authority and Cairngorms National Park Authority ("the Clients") dated 15 June 2011 and extended as of the letter dated 28 August 2014 (the "Services Contracts") and should be read in conjunction with the Services Contract. Nothing in this report constitutes a valuation or legal advice. We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the Services Contract. This Report is for the benefit of the Clients only. This Report has not been designed to be of benefit to anyone except the Clients. In preparing this Report we have not taken into account the interests, needs or circumstances of anyone apart from the Clients, even though we may have been aware that others might read this Report. We have prepared this report for the benefit of the Clients alone. This Report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Clients) for any purpose or in any context. Any party other than the Clients that obtains access to this Report or a copy (under the Freedom of Information (Scotland) Act 2002, through the Clients' Publication Scheme or otherwise) and chooses to rely on this Report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this Report to any party other than the Clients. In particular, and without limiting the general statement above, since we have prepared this Report for the benefit of the Clients alone, this Report has not been prepared for the benefit of any other central government body nor for any other person or organisation who might have an interest in the matters discussed in this Report, including for example those who work in the central government sector or those who provide goods or services to those who operate in the sector.

Introduction and background

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Introduction and scope

In accordance with the 2014-15 annual internal audit plan for Loch Lomond & The Trossachs National Park Authority ("LLTNPA") and Cairngorms National Park Authority ("CNPA"), as approved by the audit committees, we have performed an internal audit of fixed asset register at LLNPA ("the Authority").

The objective of the audit was to consider the processes to ensure that valuations are complete and accurately processed in the fixed asset register. The audit also considered if controls mitigate the risk of inaccurate or unauthorised capital additions. The specific objective, scope and approach, as agreed with management, is detailed in appendix one.

Background

Expenditure on fixed assets is the second largest cost to the public sector after payroll costs and robust capital accounting and monitoring is of increasing importance. The Authority has a responsibility to ensure that the accounting for property, plant and equipment is in accordance with IAS 16 *Property, plant and equipment* and IAS 36 *Impairment of assets* (as interpreted by the HM Treasury Financial Reporting Manual (FReM).

The Authority holds a number of categories of tangible assets, with a current net book value of £9.1 million. All categories of assets, with the exception of land and buildings, are carried at depreciated historical cost; with depreciation charged over the useful economic life of the asset. Land and buildings are subject to periodic valuation in accordance with IAS 16 every five years, the last valuation exercise was carried out as at 31 March 2014 and the relevant valuations have been updated in the fixed asset register.

The Authority is required to maintain an accurate and up-to-date register of fixed assets which is updated on an annual basis to reflect changes to assets including revaluation, additions, disposals, depreciation charged and the current net book value, this information is used to inform the accounts preparation process at the year end.

Executive summary

We identified no 'critical' or 'high' graded recommendations in the course of our work.

We identified three 'low' graded recommendations.

We also identified areas of good practice.

The findings identified during the course of this internal audit are summarised below. A full list of the findings and recommendations are included in this report. Management has accepted the findings and agreed reasonable actions to address the recommendations.

	Critical	High	Moderate	Low
Number of internal audit findings	-	-	-	3
Number of recommendations accepted by management	-	-	-	3

The review of the fixed asset register identified that the controls are designed effectively, although we identified minor weaknesses in their operating effectiveness as set out in the action plan. Areas of good practice are summarised as:

- Through review of the fixed asset register we identified that management has put considerable effort into allocating the revaluation reserve balance to specific assets, rather than adopting an easier holistic approach;
- Management plans to conduct impairment reviews for assets when they are brought onto balance sheet and conduct an annual desktop review for all in-use assets rather than waiting until the next planned revaluation before impairments are considered.

Action plan: areas for added value

The focus of this review included efficiency, enhancement and changes in the fixed asset register processes including the greater achievement of good practice from the fixed asset register processes. The findings noted below identify areas where greater efficiencies could potentially be achieved:

- The fixed asset policy could be revised, to ensure it is fully in line with current practices at the authority.
- The use of the fixed asset software could be reintroduced to record the fixed assets, to improve the quality and robustness of the information and provide a clearer audit trail.
- There could be more frequent management reporting of capital expenditure with qualitative information.

Summary of internal audit findings

We outline the main findings from our review.

Fixed asset policies

We reviewed the authority's fixed asset policies, to assess robustness and efficiency. We considered against the Scottish Public Finance Manual, the FReM and our experience of best practice across the public sector. From this review we have provided a template to aide with the update of the fixed asset policy at Appendix three.

Accounting for fixed assets and the update of the fixed asset register is performed by the finance and procurement manager, supported by the finance and performance manager. We reviewed the processes and controls to verify that the fixed asset register is updated on an annual basis and did not identify exceptions.

We did not identify exceptions with the design and implementation and operating effectiveness of the controls for updating the fixed asset register. However we identified that the current fixed asset policy is out of date and refers to a number of processes that are no longer in place. Management should update the fixed asset policy to ensure it reflects current practices and facilitates efficient and effective asset management.

There is a risk that asset management is inefficient and ineffective due to lack of up-to-date guidance.

Recommendation one

Revenue expenditure

The Authority identifies and records capital additions at the year end, therefore we were unable to test capital additions for 2014-15, however as part of the 2013-14 external audit the auditor tested capital additions and no audit adjustments were reported. To verify the operation of the related controls, including review of revenue expenditure and whether items have been correctly allocated as capital or revenue expenditure, we selected a sample of 25 expenditure lines from both operational expenditure and project expenditure and asked management to identify how they would account for the expenditure at the year end. Through our testing we did not identify any issues and all the items tested were allocated correctly.

Summary of internal audit findings

Scottish Government Capital Grant

In 2014-15 the forecast capital grant in aid (‘GIA’) is £1.17 million, of which £1.15 million has been allocated to capital elements of projects and the remainder, £25,000 (2%), allocated to operational capital expenditure. The capital GIA is either expended on assets for the authority’s own use, which are capitalised and recognised in the statement of financial position, or capital grants awarded to third parties and third party assets which are recognised through the statement of comprehensive net expenditure. We reviewed the process for identifying the application of the Scottish Government Capital Grant, we did not identify exceptions and all items had been correctly accounted for.

In line with the FReM and good practice, the Authority plans to carry out an initial impairment assessment on all new specialist assets once they are transferred from assets under construction to land and buildings. HM Treasury guidance requires the Authority to request non-cash AME budget cover for expected asset impairments. Through discussion with management we confirmed that an application for £0.85 million non-cash AME funding had been made in respect of these asset impairments.

Management information

At the beginning of the financial year the operational and business plan budgets are set and the forecast capital expenditure identified. Management accounts and variance analysis against budget are reported to management on a quarterly basis. We reviewed the November management accounts and found that for projects there was no split of capital and revenue expenditure. Variance analysis was provided but it was unclear if the variance was due to the capital or revenue element of the projects.

A review of spend against capital GIA is reported as part of the quarter two review, with a further review carried out in January looking at how much expenditure against projects is forecast to be capital; however this did not provide qualitative information on variance to budget. There is a risk that management is not made aware of overspends or slippage in capital project expenditure until the quarter two review, which may impact application of GIA in the year. Management reporting could be enhanced by including capital project expenditure against budget as part of the management accounts, allowing more frequent reporting of capital expenditure and further qualitative analysis.

Recommendation two

Summary of internal audit findings

Fixed Asset register

The Authority maintains a fixed asset register in an excel spreadsheet which is updated on an annual basis to reflect changes such as depreciation, revaluation, impairment, additions and disposals at year end. We reviewed the fixed asset register and found it reflected the assets in use by the Authority as at 31 March 2014, depreciation had been applied in line with the accounting policy to all class of assets, the 2013-14 revaluation and impairments had been processed correctly, the transactions correctly input to the asset register and the revaluation reserve was correctly allocated to each asset.

The fixed asset register does not reflect the addition of the assets transferred at nil net book value and their subsequent immediate revaluation. There is a risk that the fixed asset register does not reflect the substance of the transactions and makes reconciliation to the financial statements difficult without knowledge of the history of the acquisition of the fixed assets.

Management should ensure that the asset register is updated to reflect the recognition and initial measurement at nil net book value to enable the reconciliation of the revaluation reserve to revaluations and impairments, and ensure that previous revaluations have been appropriately reported within the fixed asset register. The Authority has fixed asset software which integrates to the ledger however they stopped using this when they accounted for indexation and introduced the current excel spreadsheet. The use of the fixed asset software could be reintroduced to record the fixed asset register to improve the quality and robustness of the information and provide a better audit trail.

Recommendation three

Revaluations and Impairments

In 2014 the quinquennial valuation was carried out by Ryden LLP, in accordance with the Royal Institute of chartered Surveyors ('RICS') appraisal and valuation manual, insofar as the terms were consistent with the requirements of the FReM. Ryden were appointed as the valuer through a full tender process and instructions for the valuation were provided to Ryden LLP with additional information provided by the finance and procurement manager. There was continued discussion with the valuers throughout the process and any inconsistences in the final report were reviewed by management. We reviewed the governance arrangements in respect of the revaluations and did not identify exceptions.

Losses in value reflected in valuations were appropriately accounted for in accordance with IAS 36 *impairment of assets*. The consumption of economic benefit was taken to the revaluation reserve to the extent of any previous valuation gain and any further loss charged to the statement of comprehensive net expenditure.

Action plan

The action plan summaries specific recommendations, together with related risks and management's responses.

Findings and risk	Recommendations	Agreed management actions
1 Fixed asset policy		**Low**
The fixed asset policy was last updated in December 2011. We did not identify exceptions with the design and implementation or operating effectiveness of the controls for updating the fixed asset register. We identified that the current fixed asset policy is out-of-date and refers to a number of processes that are no longer in place at the Authority. There is a risk that asset management is inefficient and ineffective due to lack of up-to-date guidance.	Management should update the current fixed asset policy to ensure it reflects current practices at the authority ensuring that the policy is robust and allows for efficient asset management, appropriate update of the fixed asset register and accurate reflection of the Net Book Value of all assets in use by the Authority for accounting purposes.	Management accept that the policy needs updated. **Responsible officer:** Finance and Performance Manager **Implementation date:** 30 November 2015

Action plan

Findings and risk	Recommendations	Agreed management actions
2 Capital reporting		**Low**
Although forecast variances against budget, is identified as part of the management accounting process, it was unclear if the variance was due to the capital or revenue element of the projects. A review of spend against capital GIA is reported as part of the quarter two review, with a further review carried out in January looking at how much expenditure against projects is forecast to be capital; however this did not provide qualitative information on variance to budget. There is a risk that management are not made aware of overspends or slippage in capital project expenditure until month seven which may impact application of GIA in the year.	Management reporting could be enhanced by including capital project expenditure against budget as part of the management accounts, facilitating more frequent reporting of capital expenditure and further qualitative analysis	The budget for 2015/16 analyses expenditure between capital and revenue expenditure. The Finance & Performance Manager will develop appropriate management reporting so that capital expenditure can monitored on a monthly basis. **Responsible officer:** Finance and Performance Manger **Implementation date:** 31 July 2015

Action plan

Findings and risk	Recommendations	Ageed management actions
3 Fixed Asset register		**Low**
The fixed asset register does not reflect the addition of the assets transferred at nil net book value and their subsequent immediate revaluation. There is a risk that the fixed asset register does not reflect the substance of the transactions and makes reconciliation to the financial statements difficult without knowledge of the history of the acquisition of the fixed assets.	Management should ensure that the asset register is updated to reflect the recognition and initial measurement at nil net book value to allow the reconciliation of the revaluation reserve to revaluations and impairment and ensure that previous revaluations have been appropriately reported within the fixed asset register. The use of the fixed asset software could be reintroduced to record the fixed asset register to improve the quality and robustness of the information and provide a better audit trail.	Fixed Asset opening balances will be adjusted to reflect transfer at nil value plus subsequent upward revaluation. We will assess whether the use of the fixed asset software would be more beneficial than the Excel spreadsheet. **Responsible officer:** Finance and Performance Manager **Implementation date:** 31 January 2016

Appendices

Objective, scope and approach

Objective

In accordance with the 2014-15 internal audit plan for Loch Lomond & The Trossachs National Park Authority we will undertake an internal audit review of the fixed asset register.

The Authority holds fixed assets which are subject to periodic valuation and this audit will consider the processes to ensure that valuations are complete and accurately processed in the fixed asset register. The audit will also consider if adequate controls exist to mitigate the risk of inaccurate or unauthorised capital additions.

Scope

We will perform a review of the policies and processes in respect of fixed assets. We will:

- consider the design of fixed asset policies, to assess the robustness and efficiency, comparing with Scottish Public Finance Manual, Financial Reporting Manual, application of procurement processes and similar organisations' policies;
- test a sample of capital additions, to verify the operation of controls including review of appropriateness of capital charges;
- test a sample of revenue expenditure items, to verify the operation of controls including review of whether items have been correctly allocated;
- review the process for identifying the application of the Scottish Government Capital Grant;
- review the procedures designed to ensure that the fixed asset register is up-to-date and accurately reflects the assets in use including review of the use of management information to identify capital expenditure on an ongoing basis;
- review the policy for the treatment of any revaluations or impairments, and consider appropriateness of the treatment and the overall governance arrangements in respect of the revaluations.

Approach

We will adopt the following approach in this review:

- project planning and scoping;
- conduct interviews with staff to gain an understanding of the procedures and processes;
- identify and agree key risks and processes with management;
- review the adequacy and effectiveness of key processes through sample testing and discussion;
- compare the processes and policies to other organisations; and
- agree findings and recommendations with management.

Classification of internal audit findings

The following framework for internal audit ratings has been developed and agreed with management for prioritising internal audit findings according to their relative significance depending on their impact to the process.

Rating	Definition	Examples of business impact	Action required
Critical	Issue represents a control weakness, which could cause or is causing severe disruption of the process or severe adverse effect on the ability to achieve process objectives.	■ Potential financial impact of more than 1% of total expenditure. ■ Detrimental impact on operations or functions. ■ Sustained, serious loss in brand value. ■ Going concern of the organisation becomes an issue. ■ Decrease in the public's confidence in the Authority. ■ Serious decline in service/product delivery, value and/or quality recognised by stakeholders and customers. ■ Contractual non-compliance or breach of legislation or regulation with litigation or prosecution and/or penalty. ■ Life threatening.	■ Requires immediate notification to the Authority's audit committee. ■ Requires executive management attention. ■ Requires interim action within 7-10 days, followed by a detailed plan of action to be put in place within 30 days with an expected resolution date and a substantial improvement within 90 days. ■ Separately reported to chairman of the Authority's audit committee and executive summary of report.
High	Issue represents a control weakness, which could have or is having major adverse effect on the ability to achieve process objectives.	■ Potential financial impact of 0.5% to 1% of total expenditure. ■ Major impact on operations or functions. ■ Serious diminution in brand value. ■ Probable decrease in the public's confidence in the Authority. ■ Major decline in service/product delivery, value and/or quality recognised by stakeholders and customers. ■ Contractual non-compliance or breach of legislation or regulation with probable litigation or prosecution and/or penalty. ■ Extensive injuries.	■ Requires prompt management action. ■ Requires executive management attention. ■ Requires a detailed plan of action to be put in place within 60 days with an expected resolution date and a substantial improvement within 3-6 months. ■ Reported in executive summary of report.

Classification of internal audit findings (continued)

Rating	Definition	Examples of business impact	Action required
Moderate	Issue represents a control weakness, which could have or is having significant adverse effect on the ability to achieve process objectives.	■ Potential financial impact of 0.1% to 0.5% of total expenditure. ■ Moderate impact on operations or functions. ■ Brand value will be affected in the short-term. ■ Possible decrease in the public's confidence in the Authority. ■ Moderate decline in service/product delivery, value and/or quality recognised by stakeholders and customers. ■ Contractual non-compliance or breach of legislation or regulation with threat of litigation or prosecution and/or penalty. ■ Medical treatment required.	■ Requires short-term management action. ■ Requires general management attention. ■ Requires a detailed plan of action to be put in place within 90 days with an expected resolution date and a substantial improvement within 6-9 months. ■ Reported in executive summary of report.
Low	Issue represents a minor control weakness, with minimal but reportable impact on the ability to achieve process objectives.	■ Potential financial impact of less than 0.1%*of total expenditure. ■ Minor impact on internal business only. ■ Minor potential impact on brand value. ■ Should not decrease the public's confidence in the Authority. ■ Minimal decline in service/product delivery, value and/or quality recognised by stakeholders and customers. ■ Contractual non-compliance or breach of legislation or regulation with unlikely litigation or prosecution and/or penalty. ■ First aid treatment.	■ Requires management action within a reasonable time period. ■ Requires process manager attention. ■ Timeframe for action is subject to competing priorities and cost/benefit analysis, eg. 9-12 months. ■ Reported in detailed findings in report.

Fixed asset policy template

Fixed asset policy template based on good practice noted from our client base.

Heading	Description
1. Introduction	■ Outline the purpose and scope of the policy.
2. Categories of fixed assets	■ List describing the categories of non-current assets most commonly used by the authority.
3. Criteria for capitalisation of assets	■ Expenditure eligible for capitalisation (consider de minimis level and whether the current value of £600 is still appropriate). ■ Detail costs of the asset that meet the capitalisation criteria defined in IAS 16 and the FReM. ■ Treatment of low value assets charged to I&E.
4. Delegated authority	■ Authorisation required for approving the purchase and disposal of fixed assets.
5. Accounting treatment	■ Assets recognised at costs. ■ Recognition of expenditure eligible for capitalisation.
6. Revaluation of assets	■ Policy for revaluation of freehold and long leasehold land and buildings. ■ Accounting for gains and losses on revaluation.
7. Impairment	■ Policy for impairment of assets brought ton balance sheet and annual desktop review.
8. Depreciation	■ Depreciation is charged against the fixed asset over the expected useful life of the asset to reflect the usage of the asset over time. ■ Method of deprecation. ■ Table detailing the period over which the asset category is depreciated. ■ Policy of depreciation on the year of acquisition or disposal.
9. Disposal	■ Process for disposal of asset. ■ Recognition of profit/loss on disposal of asset.
10. Assets under construction	■ Accounting treatment and recognition.
11. Fixed asset register	■ Process for recording of assets. ■ Authority to update the fixed asset register.

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