The Gateshead Housing Company
Resources and Audit Committee

Tuesday 10 July 2012 at 2pm
Board Room 1, The Gateshead Housing Company, Keelman House, Fifth Avenue Business Park, Fifth Avenue, Team Valley Trading Estate, Gateshead NE11 0XA

Agenda

Item	Business
1.	**Apologies for Absence**
2.	**Declarations of Interest**
	ITEMS FOR DECISION
3.	**Report on the Statement of Internal Control – 2011/12 (Pages 2-7)** Report of Head of Finance
4.	**Draft Directors' Report and Financial Statements – 2011/12 (Pages 8-38)** Report of Acting Chief Executive
5.	**KPMG Management Report – Year Ended 31 March 2012 (Pages 39-60)** Report of Head of Finance

Contact: Stuart Gibson Tel: (0191) 433 5308 Date: 4 July 2012

Report to the Resources and Audit Committee

10 July 2012

Title: Report on the Statement of Internal Control – 2011/12

Report of: Head of Finance

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Purpose of Report

1. To consider the report on the statement of internal control for the year ended 31 March 2012 and recommend approval to the Board.

Background

2. It is a requirement under the UK Corporate Governance Code that companies undertake at least annually a review of the effectiveness of their systems of internal control. A company's board should undertake this review for the purposes of making its public Statement of Internal Control which is published as part of the financial statements.

Statement of Internal Control

3. The statement of internal control as published as part of the financial statements is included in the Appendix.

4. This report is designed to provide assurance that the information as stated within the statement of internal control is accurate and reliable and can be published as part of the financial statements.

5. This review of the effectiveness of internal control has been carried out by the Director of Corporate Services in his key responsibilities as detailed in the Governance Handbook.

Governance and Risk Management

6. Although we have never formally adopted a Code of Governance, we carry out an annual review of governance which has resulted in significant improvements in the way we are governed.

7. Previous governance reviews have been specifically linked to Codes of Governance that were considered to be best practice at that time, namely: -

- The Independent Commission for Good Governance in the Public Sector; and

- The Langlands Report.

8. Action Plans were formulated following these reviews to ensure identified development needs were addressed.

9. Other changes to the way we are governed following governance reviews included a new Board and committee structure, payment to directors and an updated Code of Conduct for Directors.

10. We have adopted the principles of risk management to protect the health, safety and welfare of its employees and the people it serves, to protect its property, assets and other resources and to maintain its reputation and good standing in the wider community.

11. The company has reviewed its risk management arrangements and introduced an updated policy. A risk manager and risk owners regularly review the company's operational risks and these are scrutinised in detail by Resources and Audit Committee. Operational risks are escalated to the Strategic Risk Register as appropriate and these are scrutinised in detail by the Board.

12. The company's appetite for taking risk is low, however there many be occasions when its appetite may increase for example for specific projects or new ventures. Any such increase would be subject to Board approval.

Performance Management

13. We have a performance management framework in place which is underpinned by the appraisal and development process and 1-2-1 progress meetings for all employees.

14. The appraisal process sets out the individual objectives for the year, including development and training needs. This is reviewed after six months to measure progress and re-evaluate targets and development needs.

15. The 1-2-1 progress meetings are held at least every three months, or more regularly if required to measure progress on key tasks and provide support where needed to enable employees to achieve their individual objectives.

16. A range of performance indicators and service standards enable us to assess performance, identify trends, compare ourselves with others and highlight areas where corrective action is needed.

17. The Gateshead Housing Company and Gateshead Council agree top-line Key Performance Indicators (KPIs) that Gateshead Council uses to assess the company's performance. They include a number of agreed local indicators, giving an overview of customer satisfaction and areas of operational service delivery.

18. Performance is monitored and reported as follows:

    - To Gateshead Council – monthly. Company officers meet with the Council to review performance and to agree any action to improve services.

- To the Liaison Meeting – quarterly - strategic employees of the company and Council meet to review progress against performance indicators on a quarterly basis.
- To the Board – quarterly.
- To tenants - through the tenants newspaper and the company website.
- To the corporate management teams - monthly.

19. Performance against milestones in agreed action plans is monitored regularly through the performance management framework and by lead officers. Overall progress reports are provided on a monthly basis to managers.

20. We are members of Housemark and participate in the National ALMO Benchmarking Club which helps us to compare our performance with other ALMOs locally and nationally.

Financial Management

21. The Company sets its budgets using a zero based budget approach and all efficiency savings generated are re-invested in front-line services.

22. Monthly management accounts are prepared by the finance department and provided to budget holders to enable them to review spend against budgets. Quarterly management accounts are reported to Resources and Audit Committee for scrutiny, as well as provided to the Gateshead Council. Annually the financial statements are scrutinised by Resources and Audit Committee prior to being approved for Board sign-off.

23. Budget holders are responsible for providing assurance that their budgets have been used to provide services in line with the company's memorandum of association.

24. The finance department and Head of Finance are responsible for ensuring that the company's standing orders and financial regulations are followed and bring to the attention of the Resources and Audit Committee any issue they may be aware of. There is a fraud and whistle blowing policy in place. No issues are raised or noted in relation to the financial controls in place.

Internal Audit

25. The Internal Audit Service has undertaken audit work throughout the year based on the risk based audit plan agreed by the Resources and Audit Committee on 28 April 2011. Progress against this plan has been reported through the Committee on a quarterly basis. The Chief Internal Auditor has also undertaken a self-assessment against the CIPFA Code of Practice for Internal Audit to ensure the work of the Internal Audit Service meets the standards as set out in the Code. This review found Internal Audit to be operating effectively and in compliance with the Code of Practice for Internal Audit.

26. No reports issued in 2011/12 identified any significant weaknesses in the control environment within the Company and therefore based on the work undertaken it is considered effective internal controls and systems are in place. A report will be submitted to the Resources & Audit Committee on 31 July 2012 providing more information in this area.

External Audit

27. External assurance is provided through the audit of the financial statements which includes the statement of internal control. The main purpose of the audit, which is carried out in accordance with International Standards on Auditing (‘ISAs’) issued by the Auditing Practices Board, is to issue an opinion on whether the financial statements:

- give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of The Gateshead Housing Company Limited’s affairs as at the financial year end and of the results for the year then ended; and
- have been properly prepared in accordance with the Companies Act 2006.

28. The external auditors KPMG are wholly independent of the housing company and ensure that the objectivity of the partner and audit staff are not impaired. KPMG produce a management report following the audit highlighting any issues raised with management and any issues found during the audit process. No significant weaknesses were found or highlighted.

Link to values

29. This report is in line with the following values of the company :-

- Being honest, accountable and transparent
- Being motivated trained, and committed across the company.

Impact on tenants

30. Appropriate financial monitoring and control will ensure efficiencies are maximised and redirected to services that directly impact on tenants.

Risk Management Implications

31. Risk management implications are contained within the report and Appendix.

Financial Implications

32. There are no financial implications arising from this report.

Equality and Diversity Implications

33. There are no equality or diversity implications arising from this report.

Health Implications

34. There are no direct health implications arising from this report.

Value for Money implications

35. There are no direct value for money implications arising from this report.

Environmental Implications

36. There are no direct environmental implications arising from this report.

Consultation carried out

37. None directly for this report.

Recommendation

38. The committee is requested to recommend approval of the Statement of Internal Control contained within the Financial Statements for the year ended 31 March 2012 to the Board.

Statement of Board on Internal Controls

The Board acknowledge their ultimate responsibility for ensuring that the Company has in place a system of controls that is appropriate to the various business environments in which it operates. These controls are designed to give reasonable assurance with respect to:

- the reliability of financial information used within the Company or for publication;
- the maintenance of proper accounting records; and
- the safeguarding of assets against unauthorised use or disposal.

It is the Board's responsibility to establish and maintain systems of internal control. Such systems can only provide reasonable and not absolute assurance against material financial misstatement or loss. Key elements include ensuring that:

- formal policies and procedures are in place, including the documentation of key systems and rules relating to the delegation of authority, which allow the monitoring of controls and restrict the unauthorised use of the Company's assets;

- experienced and suitably qualified staff take responsibility for important business functions. Annual appraisal procedures have been established to maintain standards of performance;

- forecasts and budgets are prepared which allow the Board and managers to monitor the key business risks and financial objectives and progress towards financial plans set for the year and the medium term; regular management accounts are prepared promptly, providing relevant, reliable and up-to-date financial and other information and significant variances from budgets are investigated as appropriate;

- all significant new initiatives, major commitments and investment projects are subject to formal authorisation procedures by the Board following scrutiny by the relevant Board committees;

- the Board reviews reports for management, from internal auditors, from the external auditors and from its own Resources and Audit Committee to provide reasonable assurance that control procedures are in place and are being followed. This includes a general review of the major risks facing the Company; and

- formal procedures have been established for instituting appropriate action to correct weaknesses identified from the above reports.

ITEM 4

Report to the Resources and Audit Committee

10 July 2012

Title:	Draft Directors' Report and Financial Statements – 2011/12
Report of:	Acting Chief Executive

Purpose of Report

1. To consider the report and financial statements for the year ended 31 March 2012 and recommend approval to the Board.

Background

2. The report and financial statements for 2011/12 will be presented to the company's Annual General Meeting, which will be held before the meeting of the Board on 20 September 2012.

3. The fourth quarter management report presenting the provisional outturn of expenditure against budget was considered by the committee at its meeting on 10 May 2012.

4. These accounts and the associated management report will be reported to the Board for approval on 19 July 2012.

Statement of Accounts

5. A report including the financial statements as agreed with the auditors, KPMG is attached at the Appendix to this report.

6. The financial result for the period was a deficit of £99,000 *(2011: £3,718,000 surplus).* The fourth quarter management accounts indicated that the financial result was an expected deficit of £34,000. Below is a table that explains how the management accounts are reconciled to the statutory accounts.

7. The deficit was made up as follows:

	2011/12 £	**2010/11 £**	
Operating surplus/(deficit)	(21,000)	(4,000)	*This is the deficit on the management accounts (before interest)- note this changed from an expected £34,000 deficit to a £21,000 deficit*
Pension Scheme Adjustment	(240,000)	3,740,000	*This is the net operating cost adjustment for pension costs. In 2010/11 this included a change in the measure of inflation.*
Pre Tax and Interest Surplus/(deficit)	**(261,000)**	**3,736,000**	
Interest Receivable	2,000	2,000	*This is the interest received on the cash balance during the year*
Pension Scheme Finance (Income / Costs)	160,000	(20,000)	*This is an accounting adjustment in relation to the pension scheme*
Financial Statements Surplus/(deficit)	**(99,000)**	**3,718,000**	

8. The company achieved a pre-tax and interest deficit in the year of £261,000 prior to interest receivable of £2,000 and pension scheme finance income costs of £160,000 *(2011: interest receivable of £2,000; finance costs of £20,000)*.

9. The balance sheet has been reduced due to the deficit and the actuarial losses in the pension scheme, resulting in closing revenue reserves excluding net pension provisions of £588,000 (*2011: £607,000*). The directors and management continue to implement efficiency savings ahead of targets and as a result believe the company is in a strong financial position to deliver its strategic and operational goals.

10. In line with last year's accounts, it has been necessary under FRS 17 (a financial reporting standard) to adjust the accounts for the pension fund liability attributable to the company's employees. The net pension liability was £13.85m as at 31 March 2012 (£8.27m as at 31 March 2011) as calculated by the Pension Fund's actuary.

11. KPMG produced a management report following the audit they have carried out. The management report is included as a separate report.

Link to values

12. This report is in line with the following values of the company :-

- Being honest, accountable and transparent
- Being motivated trained, and committed across the company.

Impact on tenants

13. Appropriate financial monitoring and control will ensure efficiencies are maximised and redirected to services that directly impact on tenants.

Risk Management Implications

14. The external audit carried out by KPMG is one element of the controls in place to ensure that the strategic risk within the business plan (Insufficient available financial resources) is effectively controlled.

Financial Implications

15. The financial implications are contained within the report and Appendix.

Equality and Diversity Implications

16. There are no equality or diversity implications arising from this report.

Health Implications

17. There are no direct health implications arising from this report.

Value for Money implications

18. The implementation of efficiency savings ahead of targets will continue to drive value for money throughout the organisation.

Environmental Implications

19. Environmental consideration is given during the day to day management of financial resources through the drive to ensure that purchasing methods are sustainable and through the reduction of energy costs through energy efficient measures being introduced in working practices.

Consultation carried out

20. None directly for this report.

Recommendation

21. The committee is requested to recommend approval of the Directors Report and Financial Statements for the year ended 31 March 2012 to the Board.

Contact: Jon Mallen-Beadle, Acting Chief Executive Tel No: (0191) 433 5306

The Gateshead Housing Company Limited

Directors' report and financial statements

Registered number 04944719

31 March 2012

Contents

Directors and advisors

Council Directors
Pauline Dillon
Kathryn Ferdinand
Paul Foy
John Walter Hamilton
Peter Mole

Tenant Directors
Robert Buckley
Stanley Dawson
Dr Joachim Moussounda Mouanda (reappointed 22 September 2011)
Gordon Spring
William Patterson (resigned 10 November 2011)

Independent Directors
Richard Armitage (reappointed 22 September 2011)
Joanne Carr
George Clark
Barbara Elaine Dennis (Chair)
Sara Woolley

Secretary and Registered Office
Jon Mallen-Beadle (Company secretary)
Keelman House
Fifth Avenue Business Park
Fifth Avenue, Team Valley Trading Estate
Gateshead, NE11 0XA

Auditor
KPMG LLP
Quayside House
110 Quayside
Newcastle upon Tyne, NE1 3DX

Internal Auditors
Gateshead Council
Civic Centre
Regent Centre
Gateshead, NE8 1HH

Bankers
Co-operative Bank plc
53-57 Blandford Square
Newcastle upon Tyne NE99 1AN

Report of the Board for the year ended 31 March 2012

The Board present their Board report and financial statements for the year ended 31 March 2012.

Principal activities

The principal activity of the Company is the day to day management, maintenance and improvement of the housing stock of Gateshead Council and Keelman Homes. The Company provides housing management services for a number of properties which are owned by other registered providers.

The Company also manages the building of new properties to be owned and managed by the Company and manages new build programmes for both Gateshead Council and Keelman Homes when required.

Result for the year

The financial result for the period was a deficit of £99,000 *(2011: £3,718,000 surplus due to the change in the measure of inflation used to increase pension benefits from RPI to CPI. Excluding this adjustment of £3,850,000, other FRS 17 pension cost adjustments of £130,000 and interest receivable of £2,000, the underlying deficit in 2010/11 was £4,000).*

The Company achieved a pre-tax and interest deficit in the year of £261,000 prior to interest receivable of £2,000 and pension scheme finance income of £160,000 *(2011: interest receivable of £2,000; finance costs of £20,000)*. The deficit in 2011/12 is due to FRS17 pension operating cost adjustments that are required in the profit and loss account, excluding this, the underlying deficit is £19,000.

The balance sheet has been reduced due to the underlying deficit and the actuarial losses in the pension scheme, resulting in closing revenue reserves excluding net pension provisions of £588,000 (*2011: £607,000*). The directors and management continue to implement efficiency savings ahead of targets and as a result believe the Company is in a strong financial position to deliver its strategic and operational goals.

Review of business

We continued to provide the day to day management for the housing stock owned by Gateshead Council as well as those properties owned directly by the Company and the housing stock owned by Keelman Homes, our charitable subsidiary. The Company have management agreements with both Gateshead Council and Keelman Homes covering the day to day management, maintenance and improvement of these properties..

Our services were delivered in line with customer priorities identified as part of the 2011 annual survey and the work of the Service Improvement Groups continued to drive services forward.

We implemented a Customer Complaints Panel consisting of tenants and leaseholders who assist in driving forward service improvements and learning from our complaints.

We also worked closely with the Council to consult with customers around the introduction of a scrutiny panel to scrutinise housing services provided by both the Company and the Council. Appointments were made to the scrutiny panel during the year, training was delivered and they embarked on their first scrutiny exercise. The scrutiny panel importantly chose a name and an identity for themselves to show their independence from the Company and the Council.

- The Tenant and Leaseholder Independent Scrutiny Management (TALISMAN)

There were also, a number of significant projects which were embarked on or completed during the year. The most significant was a review of the delivery of housing services. The Company worked with the Council to develop the consultation and work around the review of who should deliver housing services in the future. A test of opinion was carried out with all tenants and leaseholders and the results of the review will be published in 2012/13.

Also during 2011/12 the Company embarked on a procurement exercise with the Council to retender the repairs and maintenance contract. A new contractor was appointed and Mears began their new contract on 1 April 2012.

Achievements during the year can be linked to each of our strategic objectives:

Report of the Board for the year ended 31 March 2012 *(continued)*

- **Continue to deliver excellent housing services**

The majority of our contacts with customers are via our repairs service, with around 62,000 repairs orders being raised annually. Satisfaction with the repairs service has increased from 95% in 2008/09 to 97.2% in 2011/12.

Performance by our repairs partner continued to improve during 2011/12 with 98.8% of all emergency, urgent and routine repairs completed within the timescales we set. This was an excellent result when considering the fact that the repairs contractor changed in April 2012 and a demobilisation period of 3 months took place within the year.

The estate tours that we carried out during 2011/12 were attended by customers 73.5% of the time. In total we carried out 792 Estate Tours.

Service Standards are outlined in "The Guide to Services you can expect from The Gateshead Housing Company" and during 2011/12 this guide was revised and updated to ensure it was measuring the most appropriate service standards. Customers were involved in reviewing the appropriateness of the service standards and agreeing the relevant performance measures to be monitored. This revised version was launched in May 2012.

The Company and the Council produced the second Annual Report for Tenants and Leaseholders which provided our customers with a report of how we were meeting the Tenants Services Authority ("TSA") standards as well as reviewing our performance for the previous year. Customers were involved in interviewing our employees as part of this report.

We carried out 402 involvement events and activities ranging from Service Improvement Groups, forums, roadshows, mystery shopping and sheltered scheme meetings. Customers were involved on more than 8,500 occasions.

Our Moving Forward Training programme saw 227 customers attending training courses, with 25 courses taking place in total. This included help with employment courses, gardening and basic DIY courses, advice on managing money and scam awareness and understanding health improvement. In addition, some tenants were supported to attend national conferences held by the Northern Housing Consortium and the Chartered Institute of Housing.

We retained the government's national standard for customer service excellence in recognition of the high quality services delivered to our customers every day.

We piloted the Customer Assessment Tool (CAT) and this will now be implemented across all neighbourhoods in 2012/13. This will enhance our approach to supporting vulnerable victims of anti-social behaviour.

- **Effectively manage housing assets to achieve sustainable homes and neighbourhoods**

We successfully completed the Decent Homes programme during 2011/12. By the end of the year over 21,000 properties had met the decent homes standard, and over £330 million has been invested in the stock during the lifetime of the programme.

Work continues on the Kibblesworth New Build programme being delivered through Keelman Homes. This will create up to 154 new homes in the village of which 94 will be owned by Keelman Homes and managed by the Company. The scheme is scheduled for completion in December 2012.

Report of the Board for the year ended 31 March 2012 *(continued)*

The company also delivered the Council's Homes and Communities Agency ("HCA") funded new build programme with the following schemes:

- At Harlow Green 45 two bedroom extra care flats and 6 two bedroom bungalows were completed and let.
- 4 three bedroom bungalows were completed and let at Norfolk Avenue, Barley Mow.
- 12 new bungalows at Cranesville, Cresthaven and 5 family homes at Portobello were also completed and let during the year.

In 2011/12 we delivered 43 Neighbourhood Pride projects investing £50,000 of TGHC funding. This attracted a total of £131,041 other funding enabling us to develop a joint approach to delivering safer, cleaner, greener and stronger communities.

For the second year in a row we achieved 100% in the servicing of all gas and solid fuel heating appliances.

- **Secure adequate resources both human and financial to effectively support our business**

Throughout 2011/12 we worked in partnership with Gateshead Council in their housing stock options review, involving customers in an appraisal over future management arrangements of the housing stock. We carried out a number of consultation events with the Council and the Independent Tenants Advisor ("Woodholmes"), jointly producing a number of documents informing tenants and leaseholders of the review which cumulated in a test of opinion document that was sent to all customers in early 2012. The test of opinion will be one part of a number of factors considered when determining future management arrangements of council housing.

Following two rounds of voluntary redundancies, we completed a restructure of the company, strengthening in key areas to ensure we can maintain the customer focused services that we provide to our customers and stakeholders.

We worked closely with the Council to review the self-financing proposals which replace the Housing Subsidy System in April 2012. We have worked together to create a 30-year business plan using the known debt settlement figures, as well as agreeing and including regeneration schemes within the Borough. This plan provides a basis to ensure we can continue to maintain decency within the self-financing regime.

Our focus on work life balance for employees has resulted in sickness levels reducing with a year end result of 8.47 days per employee, nearly half when compared to the 15.1 days in 2008/09.

We continue to be committed to environmental standards and retained the ISO 14001 international standard for environmental management. A successfully passed audit confirmed we are conforming to the standard and demonstrated that we have a robust system for monitoring, managing and reducing our impact on the local environment.

Customer Priorities

Our customer priorities are the most important challenge in ensuring that we spend our money in the most appropriate way. Our 2011 annual survey asked customers what their top priorities were, these were as follows:-

1. High quality, timely repairs
2. Well maintained environment outside the home
3. Tackling anti-social behaviour

Our key actions in 2011/12 were undertaken to address these customer priorities to ensure that we provided services which meet our customers' needs.

Report of the Board for the year ended 31 March 2012 *(continued)*

Policy and practice and payment of creditors

As a controlled Company of a local authority, the Company adheres to BVPI8 which requires the payment of undisputed creditor invoices within 30 days of receipt of the invoice. Where disputes arise we attempt to resolve them promptly and amicably to ensure delays in payment are kept to a minimum.

We are currently participating in the local authorities scheme to assist the local economy by paying local suppliers within 10 days of receipt of the invoice.

Future Developments

Work continues on the redevelopment of the area of Kibblesworth by our charitable subsidiary, Keelman Homes. As part of this redevelopment scheme, the Company are managing the new build project on behalf of Keelman Homes and will also provide the day-to-day management of the properties as part of their management agreement.

Self-financing for the Housing Revenue Account was introduced by the Department of Communities and Local Government. We assisted the Council in the production of their 30-year business model to inform the future financing requirements for the management, maintenance and investment in the housing stock. This assisted with the production of the capital programme for the next 5 years.

The Decent Homes Programme has now been completed and the Company are now embarking on a programme of maintaining decency in all the properties they manage to ensure that they meet the statutory requirements as set out by the Homes and Communities Agency.

The Homes and Communities Agency Framework around regulation for Social Housing, was issued in April 2012. This focuses heavily on transparency, the need for true engagement with customers and tenant scrutiny at all levels within an organisation and perhaps most significantly value for money to be at the forefront of all we do.

The Welfare Reform Bill attained Royal Assent during 2012 meaning we are on the cusp of the most significant and radical changes to the benefits system for over 50 years. The impact for many customers will be significant and whilst some of the detail has yet to be confirmed, it is inevitable that the changes will have a detrimental impact on the rental income that Gateshead receives.

More fundamental changes are planned from 2013 with the introduction of Universal Credit. This single benefit will be paid to claimants directly, in arrears and will replace a number of means tested benefits, including Housing Benefit. A key focus this year therefore is to educate customers and staff about the changes and we anticipate that resources will need to be redirected to ensure the impact is minimised.

The Board and Executive Officers

Under guidance for the setting up of Arms Length Management Organisations, issued by the Office of the Deputy Prime Minister ("ODPM"), the Company's Board of non-executive directors has equal representation of Tenant, Council and Independent members. Council Directors are appointed and removed directly by the Council, whilst Tenant Directors are appointed through interview by tenants and leaseholders living in Gateshead. Independent Directors are selected by the Board. Tenant and Independent Directors are subject to rotational retirement rules contained in the Company's Articles of Association.

The operational day to day running of the Company is delegated to paid Strategic Employees by the Board, through the Company's Scheme of Delegation and in the first instance, to the Company's Chief Executive. None of the Corporate Management Team are Board members.

Report of the Board for the year ended 31 March 2012 *(continued)*

Corporate Governance

The Company signs up to the principles of the Combined Code in so far as they are applicable to an organisation of its size and structure. As well as having robust codes of conduct for Board members, the Company has a clear Risk Strategy in place which underlies its key decisions.

In addition to the main Board, the Company has a number of formal Board Committees as follows:

- Customers and Communities
- Asset Management
- Resources and Audit
- Executive Overview

The committees have been aligned to the objectives within the Company's Business Plan. Each committee has clear terms of reference detailing their functions, together with decisions that should be referred to the Board for approval and those that have been delegated. All the Company's corporate governance arrangements are set out in a Governance Handbook issued to all Board members. The Company continues to review its governance arrangements annually to ensure that the needs of the organisation are being met effectively.

Statement of Board on Internal Controls

The Board acknowledge their ultimate responsibility for ensuring that the Company has in place a system of controls that is appropriate to the various business environments in which it operates. These controls are designed to give reasonable assurance with respect to:

- the reliability of financial information used within the Company or for publication;
- the maintenance of proper accounting records; and
- the safeguarding of assets against unauthorised use or disposal.

It is the Board's responsibility to establish and maintain systems of internal control. Such systems can only provide reasonable and not absolute assurance against material financial misstatement or loss. Key elements include ensuring that:

- formal policies and procedures are in place, including the documentation of key systems and rules relating to the delegation of authority, which allow the monitoring of controls and restrict the unauthorised use of the Company's assets;

- experienced and suitably qualified staff take responsibility for important business functions. Annual appraisal procedures have been established to maintain standards of performance;

- forecasts and budgets are prepared which allow the Board and managers to monitor the key business risks and financial objectives and progress towards financial plans set for the year and the medium term; regular management accounts are prepared promptly, providing relevant, reliable and up-to-date financial and other information and significant variances from budgets are investigated as appropriate;

- all significant new initiatives, major commitments and investment projects are subject to formal authorisation procedures by the Board following scrutiny by the relevant Board committees;

- the Board reviews reports for management, from the internal auditor, from the external auditor and from its own Resources and Audit Committee to provide reasonable assurance that control procedures are in place and are being followed. This includes a general review of the major risks facing the Company; and formal procedures have been established for instituting appropriate action to correct weaknesses identified from the above reports.

Report of the Board for the year ended 31 March 2012 *(continued)*

Fair employment policies for disabled persons

The Company, as part of its Equal Opportunities Policy;

- welcomes job applications from people with disabilities
- does not discriminate unlawfully when it decides who to employ
- advertises widely to ensure it receives as many applications as possible, especially from disadvantaged groups
- reviews and monitors its recruitment and selection procedures to ensure it does not discriminate against people with disabilities
- encourages all employees to reach their full potential
- wherever possible, provides a workplace that is accessible to people with disabilities
- where possible, retains in suitable employment those employees who become disabled
- when required, ensures additional provision in the form of access, or transport costs, is available for people with disabilities to enable them to fully participate in interviews and training.

Employee involvement

The Company:

- shares ideas and information with its employees
- maintains a genuine exchange of views between managers and employees or their representatives
- negotiates with employees or their representatives on any proposed changes to terms and conditions of employment
- has an Employee forum, with representation from representatives of the workforce, to ensure that employees are informed about the company's economic situation and are informed and consulted about decisions likely to lead to substantial changes in work organisation
- The Employee Forum also
  - deals with consultation issues such as terms and conditions, employment policies and other employment issues specific to employees
  - develops the Company's employment policies.

An appraisal process is used for all employees, linked to individual employees' needs and performance against agreed objectives and targets, comprising two meetings each year for individuals and their line manager to appraise and review performance, to help employees to;

- get feedback on how they are doing and recognition for their achievements
- understand what is expected of them
- understand how what they do fits in with what the company is trying to achieve
- talk about the issues facing them over the next 12 months
- agree what training and development they need to perform their job effectively.

Disclosure of information to auditor

The directors who held office at the date of approval of this directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

Report of the Board for the year ended 31 March 2012 *(continued)*

Auditor

Pursuant to section 487 of the Companies Act 2006, the auditor is deemed to be reappointed and KPMG LLP will therefore continue in office.

The directors' report was approved on 19 July 2012 and signed on its behalf by:

B Dennis
Chair

J Mallen-Beadle
Company Secretary

Statement of directors' responsibilities in respect of the directors' report and the financial statements

The directors are responsible for preparing the Directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the surplus or deficit of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

KPMG LLP
Quayside House
110 Quayside
Newcastle upon Tyne
NE1 3DX
United Kingdom

Independent auditor's report to the members of The Gateshead Housing Company Limited

We have audited the financial statements of The Gateshead Housing Company Limited for the year ended 31 March 2012 set out on pages 11 to 25. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members, as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 8, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the APB's website at www.frc.org.uk/apb/scope/private.cfm.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 March 2012 and of its deficit for the year then ended;
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Independent auditor’s report to the members of The Gateshead Housing Company Limited *(continued)*

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

MR Thompson (Senior Statutory Auditor) 19 July 2012
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
Quayside House
110 Quayside
Newcastle upon Tyne
NE1 3DX

Income and Expenditure Account
for the year ended 31 March 2012

	Note	**2012**	2011
		£000	£000
Turnover	*2*	**35,608**	35,592
Operating costs (including exceptional past service credit of £nil *(2011: £3,850,000)* in respect of pension change from RPI to CPI)	*2*	**(35,869)**	(31,856)
Operating (deficit)/surplus	*2-5*	**(261)**	3,736
Interest receivable and similar income	*6*	**2**	2
Other finance income/(costs)	*7*	**160**	(20)
(Deficit)/surplus on ordinary activities before taxation		**(99)**	3,718
Taxation on (deficit)/surplus from ordinary activities	*8*	**-**	-
(Deficit)/surplus for the financial year	*15*	**(99)**	3,718

All amounts relate to continuing activities.

Statement of Total Recognised Surpluses and Deficits
for the year ended 31 March 2012

	2012	2011
	£000	£000
(Deficit)/surplus for the financial year	**(99)**	3,718
Actuarial loss recognised in the pension scheme	**(5,500)**	(760)
Total recognised (deficit)/surplus relating to the period	**(5,599)**	2,958

Balance Sheet
as at 31 March 2012

	Note	2012		2011	
		£000	**£000**	£000	£000
Fixed assets					
Tangible assets	*9*		**1,004**		1,091
Current assets					
Debtors	*11*	**1,179**		2,919	
Cash at bank and in hand		**6,501**		3,751	
		7,680		6,670	
Creditors: amounts falling due within one year	*12*	**(7,878)**		(6,872)	
Net current liabilities			**(198)**		(202)
Provisions for liabilities	*13*		**(218)**		(282)
Total assets less current liabilities			**588**		607
Creditors: amounts falling due after more than one year					
Net pension liability	*17*		**13,850**		8,270
Capital and reserves					
Revenue reserves excluding net pension costs		**588**		607	
Net pension liability		**(13,850)**		(8,270)	
Revenue reserve including pension liability	*15*		**(13,262)**		(7,663)
Total long term liabilities, capital and reserves			**588**		607

These financial statements were approved by the Board of directors on 19 July 2012 and were signed on its behalf by:

B Dennis
Chair

Company registered number: 04944719

Cash Flow Statement

for the year ended 31 March 2012

	Note	2012	2011
		£000	£000
Net cash inflow/(outflow) from operating activities	*18a*	**2,892**	(3,726)
Returns on investments and servicing of finance			
Interest received		**2**	2
		2,894	(3,724)
Capital expenditure			
Purchase of tangible fixed assets		**(144)**	(401)
Increase/(decrease) in cash	*18b*	**2,750**	(4,125)

Notes
(forming part of the financial statements)

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the financial statements.

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards, and under historical cost accounting rules.

The company is exempt by virtue of s400 of the Companies Act 2006 from the requirement to prepare group financial statements. These financial statements present information about the company as an individual undertaking and not about its group.

The company's business activities, together with the factors likely to affect its future development, performance and position are set out in the directors' report on pages 2 to 8.

The company has cash at bank and in hand of £6,501,000 at the end of the year, with no external debt. The company's primary customer is Gateshead Council with whom there is a management agreement in place for the company to provide services until 31 December 2013. As a consequence the Directors believe that the company is well placed to manage its business risks successfully despite the current uncertain economic outlook.

As the company is a wholly owned subsidiary of Gateshead Council, the company has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with entities which form part of the group (or investees of the group qualifying as related parties). The consolidated financial statements of Gateshead Council, within which this company is included, can be obtained from the address given in note 19.

After making enquiries, the directors have a reasonable expectation that the company have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing these financial statements.

Fixed assets and depreciation

Depreciation is provided to write off the cost less the estimated residual value of tangible fixed assets by equal instalments over their useful economic lives as follows:

Buildings	-	50 years
Leasehold improvements	-	life of lease
Fixtures and fittings	-	2-4 years
IT	-	4 years

Freehold land is not depreciated.

Operating leases

Operating lease rentals are charged to the income and expenditure account on a straight line basis over the period of the lease.

Government grants

Capital based government grants are included within accruals and deferred income in the balance sheet and credited to the income and expenditure account over the estimated useful economic lives of the assets to which they relate.

Notes *(continued)*

1 Accounting policies *(continued)*

Retirement benefits

The Company participates in the Tyne and Wear Pension Fund. The scheme is a final salary Local Government Pension Scheme and retirement benefits to employees of the Company are funded by contributions from all participating employers and employees in the scheme. The assets of the scheme are held separately from those of the Company.

Pension scheme assets are measured using market values. For quoted securities the current bid price is taken as market value. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on a high quality corporate bond of equivalent term and currency to the liability.

The pension scheme surplus (to the extent that it is recoverable) or deficit is recognised in full. The movement in the scheme surplus/deficit is split between operating charges, finance items and, in the statement of total recognised gains and losses, actuarial gains and losses.

Taxation

The charge for taxation is based on the result for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Turnover

Turnover represents primarily management fees received from Gateshead Council for the management and maintenance of Gateshead Council’s housing stock and is stated net of value added tax.

Income is recognised on an accruals basis.

The Company acts as agent on behalf of Gateshead Council in respect of capital work and as such only includes the commission receivable within turnover.

Cash at bank and in hand

Cash at bank represents the Company’s share of bank balances managed on its behalf by Gateshead Council.

Notes *(continued)*

2 Analysis of turnover, operating costs and operating (deficit)/surplus

	2012 £000	2011 £000
Turnover		
Management fee	**30,433**	31,391
External funding	**34**	89
Capital fees	**2,100**	2,500
Other	**3,041**	1,612
	35,608	35,592
Operating costs		
Management of housing stock	**14,711**	11,640
Repairs and maintenance of housing stock	**19,058**	17,716
Revenue expenditure supporting capital programme	**2,100**	2,500
	35,869	31,856
Operating (deficit)/surplus	**(261)**	3,736

3 Notes to the income and expenditure account

	2012 £000	2011 £000
(Deficit)/surplus on ordinary activities before taxation is stated after charging:		
Depreciation on tangible fixed assets – owned	**231**	297
Hire of plant and equipment – operating leases	**25**	25
Hire of other assets – operating leases	**330**	327
Auditor's remuneration:		
Audit of these financial statements	**16**	17

4 Remuneration of directors

The aggregate amount of emoluments and expenses paid to Board Members was £25,597 (*2011: £18,016*).

Notes *(continued)*

5 Staff numbers and costs

The average number of persons employed by the Company during the year, excluding directors, expressed as equivalent full time employees was:

	Number of employees	
	2012	2011
Housing management	**210**	229
Administrative and clerical	**124**	140
	334	369

The aggregate payroll costs of these persons were as follows:

	2012	2011
	£000	£000
Wages and salaries	**8,925**	9,688
Social security costs	**576**	646
Other pension costs (note 17)	**1,361**	1,866
Exceptional past service credit (note 17)	**-**	(3,850)
	10,862	8,350

On 22 June 2010, the government announced that it intended for future increases in public sector pension schemes to be linked to changes in the Consumer Prices Index (CPI) rather than as previously, the Retail Price Index (RPI). The directors considered the LGPS Tyne and Wear Pension Scheme rules and associated members' literature and concluded that this was a change in benefits and recognised the resulting credit in the income and expenditure account, in accordance with UITF 48.

6 Interest receivable and similar income

	2012	2011
	£000	£000
Bank interest	**2**	2

Notes *(continued)*

7 Other finance income/(costs)

	2012	2011
	£000	£000
Expected return on pension scheme assets	**2,160**	1,820
Interest on pension scheme liabilities	**(2,000)**	(1,840)
	160	(20)

8 Taxation

In January 2007 HMRC agreed that the Company is able to take advantage of the beneficial tax treatment described in HMRC's guidance due to there being insufficient commerciality between the ALMO and its parent Council.

Analysis of charge in period

	2012	2011
	£000	£000
UK corporation tax		
Current tax on income for the period	**-**	-
Total current tax	**-**	-
Deferred tax	**-**	-
Tax on (deficit)/surplus on ordinary activities	**-**	-

Factors affecting the tax charge for the current period

The current tax charge for the period is lower than the small company's rate of corporation tax in the UK of 20 % *(2011: 21%)*. The differences are explained below:

	2012	2011
	£000	£000
Current tax reconciliation		
(Deficit)/surplus on ordinary activities before tax	**(99)**	3,718
Current tax at 20 % *(2011: 21%)*	**(20)**	781
Effects of:		
Expenses not deductible for tax purposes	**45**	62
Non taxable income	**(25)**	(843)
Total current tax charge (see above)	**-**	-

Notes *(continued)*

9 Tangible fixed assets

`

	Land and buildings	Leasehold improvements £000	Fixtures and fittings £000	IT equipment £000	Total £000
Cost					
At beginning of year	343	583	70	1,139	2,135
Additions	144	-	-	-	144
At end of year	487	583	70	1,139	2,279
Depreciation					
At beginning of year	-	155	70	819	1,044
Charge for year	10	39	-	182	231
At end of year	10	194	70	1,001	1,275
Net book value					
At 31 March 2012	**477**	**389**	**-**	**138**	**1,004**
At 31 March 2011	343	428	-	320	1,091

10 Fixed asset investments

	Interest in group undertaking 2012 £000
Cost and net book value	
At beginning and end of year	-

The company is the sole member of Keelman Homes Limited, a charitable company which is limited by guarantee, which is incorporated in England. The company's liability in respect of Keelman Homes Limited is restricted to £10. The principal activity of Keelman Homes Limited is the construction and management of social housing in Kibblesworth.

Notes *(continued)*

11 Debtors

	2012	2011
	£000	£000
Amounts owed by parent undertaking	**541**	948
Amounts owed by other group undertakings	**177**	170
Trade debtors	**28**	1,417
Prepayments and accrued income	**433**	384
	1,179	2,919

All debtor balances are due within one year.

Deferred tax assets of £2,770,000 *(2011: £1,737,000)*, arising on the pension scheme deficit have not been recognised due to uncertainty surrounding their future recoverability against taxable profits.

12 Creditors: amounts falling due within one year

	2012	2011
	£000	£000
Amounts owed to parent undertaking	**4,000**	2,327
Amounts owed to other group undertakings	**75**	12
Trade creditors	**802**	977
Other taxation and social security	**1,717**	1,174
Accruals and deferred income	**1,284**	2,382
	7,878	6,872

Notes *(continued)*

13 Provisions for liabilities

	Insurance provision £000
At beginning of year	282
Utilised during year	(57)
Released during the year	(7)
At end of year	**218**

Provisions relate to amounts held to cover insurance claims, which fall below the current excess limit on the company's insurance policy.

14 Share capital

The Company does not have any share capital as it is limited by guarantee of £1 per member. Membership at 31 March 2012 was 1 *(2011: 1)*.

15 Revenue reserves

	Revenue reserves £000
Balance at 1 April 2011	(7,663)
Deficit from income and expenditure	(99)
Actuarial loss recognised in the pension scheme	(5,500)
Balance at 31 March 2012	**(13,262)**

16 Commitments

Annual commitments under non-cancellable operating leases are as follows:

	2012		2011	
	Land and buildings £000	**Other £000**	Land and buildings £000	Other £000
Operating leases which expire:				
Within one year	**-**	**12**	-	-
In the second to fifth years inclusive	**305**	**4**	305	22
Over five years	**-**	**-**	-	-

Notes *(continued)*

17 Pensions

The Company participates in the Tyne and Wear Pension Fund, a Local Government Pension Scheme ('LGPS'), which is a funded defined benefit scheme based on members final pensionable pay. The latest full actuarial valuation was carried out by Aon Hewitt Limited at 31 March 2010 and was updated for FRS 17 purposes to 31 March 2011 and 31 March 2012 by Aon Hewitt Limited a qualified independent actuary.

The information disclosed below is in respect of the whole of the plans for which the Company is either the sponsoring employer or has been allocated a share of cost under an agreed group policy throughout the periods shown.

	2012	2011
	£000	£000
Present value of funded defined benefit obligations	**(42,850)**	(36,970)
Fair value of plan assets	**29,000**	28,700
Deficit	**(13,850)**	(8,270)
Related deferred tax asset	**-**	-
Net liability	**(13,850)**	(8,270)

Movements in present value of defined benefit obligation

	2012	2011
	£000	£000
At 1 April	**36,970**	35,740
Current service cost	**1,260**	1,540
Past service cost/(credit)	**420**	(3,850)
Interest cost	**2,000**	1,840
Actuarial losses	**3,810**	1,740
Contributions by members	**440**	510
Benefits paid	**(2,050)**	(550)
At 31 March	**42,850**	36,970

Movements in fair value of plan assets

	2012	2011
	£000	£000
At 1 April	**28,700**	24,510
Expected return on plan assets	**2,160**	1,820
Actuarial (losses)/gains	**(1,690)**	980
Contributions by employer	**1,440**	1,430
Contributions by members	**440**	510
Benefits paid	**(2,050)**	(550)
At 31 March	**29,000**	28,700

Notes *(continued)*

17 Pension schemes *(continued)*

Expense/(income) recognised in the income and expenditure account

	2012 £000	2011 £000
Current service cost	**1,260**	1,540
Past service cost/(credit)	**420**	(3,850)
Interest on defined benefit pension plan obligation	**2,000**	1,840
Expected return on defined benefit pension plan assets	**(2,160)**	(1,820)
Total	**1,520**	(2,290)

The expense/(income) is recognised in the following line items in the income and expenditure account:

	2012 £000	2011 £000
Operating costs	**1,680**	(2,310)
Other finance (income)/costs	**(160)**	20
	1,520	(2,290)

The total amount recognised in the statement of total recognised gains and losses in respect of actuarial gains and losses is £5,500,000 loss *(2011: £760,000 loss).*

Cumulative actuarial losses reported in the statement of total recognised gains and losses for accounting periods ending from 31 March 2006 are £14,662,000 *(2011: £9,162,000).*

The fair value of the plan assets and the return on those assets were as follows:

	2012 Fair value £000	2011 Fair value £000
Equities	**19,866**	19,516
Government bonds	**2,059**	2,009
Corporate bonds	**3,364**	3,358
Property	**2,668**	2,325
Cash	**551**	344
Other	**492**	1,148
	29,000	28,700
Expected return on assets	**2,160**	1,820
Actuarial (loss)/gain on assets	**(1,690)**	980
Actual return on plan assets	**470**	2,800

Gateshead Housing Company employs a block building approach in determining the rate of return on fund assets. Historical markets are standard and assets with higher volatility assumed to generate higher returns consistent with widely accepted capital market principles. The assumed rate of return on each class of asset is set out within this note. The overall expected rate of return on assets is then derived by aggregating the expected return for each asset class over the actual asset allocation for the fund at 31 March 2012.

Notes *(continued)*

17 Pension schemes *(continued)*

Principal actuarial assumptions (expressed as weighted averages) at the year end were as follows:

	2012	2011
	%	%
Discount rate	**4.8**	5.4
Rate of increase in pensions in payment	**2.6**	2.8
Rate of increase to deferred pensions	**2.6**	2.8
Future salary increases	**5.1**	5.2
Inflation increase		
- RPI	**3.6**	3.7
- CPI	**2.6**	2.8

The assumptions relating to longevity underlying the pension liabilities at the balance sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity. The assumptions are equivalent to expecting a 65-year old to live for a number of years as follows:

- Current pensioner aged 65: 21.6 years (male), 23.8 years (female).
- Future retiree upon reaching 65: 23.4 years (male), 25.7 years (female).

History of plans

The history of the plans for the current and prior periods is as follows:

Balance sheet

	2012	2011	2010	2009	2008
	£000	£000	£000	£000	£000
Present value of scheme liabilities	**(42,850)**	(36,970)	(35,740)	(24,400)	(20,270)
Fair value of scheme assets	**29,000**	28,700	24,510	16,680	18,960
Deficit	**(13,850)**	(8,270)	(11,230)	(7,720)	(1,310)

Experience adjustments

	2012	2011	2010	2009	2008
	£000	£000	£000	£000	£000
Experience adjustments on scheme liabilities	**(1,690)**	(2,490)	5,360	(20)	(1,860)
Experience adjustments on scheme assets	**(110)**	980	60	(5,010)	180
	(1,800)	(1,510)	5,420	(5,030)	(1,680)

The Company expects to contribute approximately £1,070,000 to its defined benefit plans in the next financial year.

Notes *(continued)*

18 Notes to the cash flow statement

a) Reconciliation of operating (deficit)/surplus to net cash inflow/(outflow) from operating activities

	2012	2011
	£000	£000
Operating (deficit)/surplus	**(261)**	3,736
Depreciation	**231**	297
Decrease in debtors	**1,740**	1,859
Increase/(decrease) in creditors	**1,006**	(5,781)
Decrease in provisions	**(64)**	(97)
Charge/(credit) in relation to FRS 17 pension adjustment	**240**	(3,740)
Net cash inflow/(outflow) from operating activities	**2,892**	(3,726)

b) Reconciliation of net cash inflow to movement in net funds

	£000	£000
Increase/(decrease) in cash in the year	**2,750**	(4,125)
Net funds at start of year	**3,751**	7,876
Net funds at end of year	**6,501**	3,751

c) Analysis of changes in net funds

	At start of year £000	Cash flows £000	**At end of year £000**
Cash at bank and in hand	3,751	2,750	**6,501**

19 Ultimate parent undertaking

The Company is a subsidiary undertaking of Gateshead Council which is considered to be the ultimate parent undertaking. The consolidated accounts of the group are available to the public and may be obtained from Gateshead Council, Civic Centre, Regent Street, Gateshead, NE8 1HH.

ITEM 5

Report to the Resources and Audit Committee

10 July 2012

Title: KPMG Management Report – Year Ended 31 March 2012

Report of: Head of Finance

Purpose of Report

1. To seek approval of the external auditor's management report on the financial statements for the year ended 31 March 2012.

Background

2. The company's external auditors KPMG carried out an audit of the report and financial statements for 2011/12 during June 2012.

3. A report presenting their findings is attached at Appendix 1 to this report.

4. A report with the financial statements as agreed with the auditors, KPMG, is included as a separate item on the agenda for this meeting.

Management Report

5. KPMG produced a management report following the audit they have carried out.

6. There were no significant issues raised in the report and all of the recommendations have been responded to by the company.

Management Representation Letter

7. As part of the audit, KPMG require the letter to be signed by the Chair and the Company Secretary on behalf of the Board. The letter is Appendix 4 of the management report that is attached at the Appendix to this report.

Link to values

8. This report is in line with the following values of the company :-

- Being honest, accountable and transparent
- Being motivated trained, and committed across the

Impact on tenants

9. Appropriate financial monitoring and control will ensure efficiencies are maximised and redirected to services that directly impact on tenants.

Risk Management Implications

10. The external audit carried out by KPMG is one element of the controls in place to ensure that the strategic risk within the business plan (Insufficient available financial resources) is effectively controlled.

Financial Implications

11. The financial implications are contained within the report and appendices.

Equality and Diversity Implications

12. There are no equality or diversity implications arising from this report.

Value for Money implications

13. There are no value for money implications arising from this report.

Health Implications

14. There are no direct health implications arising from this report.

Environmental Implications

15. There are no direct environmental implications arising from this report.

Consultation carried out

16. None directly for this report.

Recommendation

17. It is recommended that the committee: -

(i) approve the management report for the year ended 31 March 2012;
(ii) recommend to the Board that they authorise the Chair and the Company Secretary to sign the management representation letter on behalf of the Board

---

Contact: Sarah Thompson, Head of Finance   Tel No: (0191) 433 5350

KPMG
cutting through complexity™

The Gateshead Housing Company Limited

Audit Highlights Memorandum – Year ended 31 March 2012

10 July 2012

Contents

The contacts at KPMG in connection with this report are:

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The report is intended solely for use for internal purposes by the management and the Resources and Audit Committee of The Gateshead Housing Company Limited (the 'Company') and should not be used by or distributed to others without our prior written consent. 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 Beneficiaries.

Executive summary – audit progress and key audit issues

Our audit has addressed the issues and risks identified at the planning stage. The key judgements and significant impacts are summarised below. Aside from the outstanding items identified, all matters have been satisfactorily addressed.

Issue	Summary
Audit progress and status	Our audit is now substantially complete and we anticipate issuing an unqualified audit opinion for the year on the Company's financial statements, following the approval of the financial statements by the Resources and Audit Committee and Board. The following matters are currently outstanding: ■ Receipt of the management representation letters ■ Post balance sheet events review ■ Final review of financial statements

Acknowledgements

We would like to take this opportunity to thank Jon Mallen-Beadle, Director of Corporate Services, Sarah Thompson, Head of Finance, Mark Banks, Finance Manager and all other staff who have assisted us during our audit.

This section of our report highlights the main features of the Company's financial performance during year, providing a 'profit bridge' from the reported deficit to the underlying operating performance.

Underlying financial performance

A reconciliation from the reported surplus to the underlying result is shown below:

Underlying financial performance		
£000	**31 March 2012**	**31 March 2011**
(Deficit)/surplus for the year	**(99)**	**3,718**
Which includes:		
Past service credit arising from the change of measure of inflation used to increase pension benefits from RPI to CPI	-	(3,850)
FRS 17 Operating costs	240	110
FRS 17 Finance (income)/cost	(160)	20
Deficit including one off costs	**(19)**	**(2)**
Redundancy costs	598	1,086
Underlying surplus	**579**	**1,084**

Source: Draft financial statements.

During both 2010/11 and 2011/12 there are a number of significant items to highlight that affect the reported surplus for the year.

Management agreement

The current management agreement with Gateshead Council extends to December 2013 which supports the going concern basis of preparation.

Audit differences

Under the requirements of ISA 260 ‘Communication of audit matters with those charged with governance’, we are required to report any unadjusted audit differences other than those that are ‘clearly trivial’ (if there are any) to the Audit Committee. These can be seen at Appendix 3.

We are also required to report any adjusted audit differences arising from our work. One adjusted audit difference was identified, and details can be seen at Appendix 3.

Audit recommendations

Audit recommendations for 2012 and a follow up on prior year matters are set out in Appendices 1-2.

Internal audit

In accordance with ISA 610 ‘Considering the work of Internal Audit’ we have reviewed work carried out by the internal auditors during the year, including a review of:

- the overall scope of their work as set out in their strategic and annual plan;
- the detailed work they have carried out in the areas identified within the annual plan.

We have reviewed internal audit reports during the audit process and have relied on their work only to the extent that it gives us comfort over the Company’s high level control environment.

Taxation

We have considered tax risks during the course of our audit work and have no matters to raise.

Independence

KPMG conforms to the highest governance standards at all times and ensures that any additional services are approved to ensure transparency in our relationship.

ISA 260 ‘Communication of audit matters with those charged with governance’ requires us to communicate at least once a year regarding all relationships between KPMG and the Company that may be reasonably thought to have bearing on our independence.

We have provided the following non-audit services in the year to 31 March 2012:

- Corporate tax compliance – £4,150
- Feed in tariff tax advice – £2,240
- VAT review - ongoing, £TBC

We have made enquiries and there are no other matters in relation to independence that have occurred during the financial year on which we are to report.

Other matters

ISA 260 requires us to communicate ‘audit matters of governance interest that arise from the audit of the financial statements’ to you which includes:

- material weaknesses in internal control identified during the audit;
- matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. issues relating to fraud, compliance with laws and regulations, subsequent events etc.);
- other audit matters of governance interest.

There are no others matters which we wish to draw to your attention.

The Bribery Act 2010 was designed to provide a more effective legal framework to combat bribery in the public and private sectors and to replace the fragmented and complex offences in common law and in the Prevention of Corruption Acts 1889-1916. The Act came into force on 1 July 2011.

The Act defines four new criminal offences:

- two new general offences of offering or paying a bribe; and of
- requesting or receiving a bribe
- a discrete offence of bribing a foreign public official (a specific offence required to comply with the OECD Convention on Combating Bribery of Foreign Public Officials)
- a new corporate offence of failing to prevent bribery being undertaken on its behalf (it will be a defence if the organisation has adequate procedures in place to prevent bribery)

Penalties under the Act include imprisonment for up to 10 years, and unlimited fines for the Company. This latter penalty arises where it is proven that the offence was committed 'with the consent or connivance of a) a senior officer of the body corporate, or (b) a person purporting to act in such a capacity' in which case the senior officer or person (as well as the body corporate or partnership) is guilty of the offence and liable to be proceeded against and punished accordingly.

The Act provides that if the organisation can show that it has adequate bribery prevention procedures in place, such 'adequate procedures' are a defence to a prosecution. In September 2010 the Ministry of Justice released its 'Consultation on guidance about commercial organisations preventing bribery (section 9 of the Bribery Act 2010)'. The stated purpose of this document is to provide guidance, as required under section 9 of the Act, to 'support businesses in determining the sorts of bribery prevention measures they can put in place.'

The resulting 'Adequate procedures' guidance, published in March 2011, lists 'Six Principles for Bribery Prevention' which the Ministry of Justice believes are good international practices for such adequate procedures and are designed to assist businesses in determining what bribery prevention procedures they can put in place.

These are:

- Proportionate Procedures
- Top level commitment
- Risk Assessment
- Due Diligence
- Communication (including training)
- Monitoring and review

While a number of the 'higher risk' factors such as working in the defence or aerospace industries, or having operations in difficult geographic locations are far less relevant to the housing sector, activities such as corporate hospitality or working with joint ventures could increase the risk to the Company. Crucially, because the Act covers the actions not only of employees but also those of third part associates, it is imperative that Boards have considered how the Act affects not only the organisation itself but also those it works with.

We note that the Company has recently implemented a new policy in light of the Act. Following the introduction of the Act, companies need to consider whether their existing financial controls and procedures, including guidance on gifts and hospitality and the reporting of those are sufficient . Companies also need to consider whether their procedures cover the actions of third party associates. Boards need to document clearly how they have satisfied themselves that 'adequate procedures' are in place.

As your auditors, we are not required to express an opinion on your compliance with the act, but we will need to satisfy ourselves that there are sufficient controls in place to reduce the risk of corruption at least to the extent that the company is not at risk of prosecution for a material issue. There is therefore scope for us to perform an additional review to assess the controls in place, should this be something you require.

Reporting developments – International Financial Reporting Standards (IFRS) and Regulatory changes

There have been some recent updates to the UK Accounting Standards Board's convergence programme for UK GAAP, with the wider use of the simplified version of IFRS.

Implementation has been delayed for another year and this is currently expected in 2015/16, but will require closing balance sheets for 2013/14 and 2014/15, plus an I&E for 2014/15.

Welfare reform and housing benefit changes will be implemented from early 2013.

Following a consultation on the original proposals for 'the future of financial reporting' the Accounting Standards Board announced a number of tentative changes in late 2011 followed by revised Financial Reporting Exposure Drafts: 46, 47 and 48 in January 2012. These were under consultation until 30 April 2012.

The revisions respond to concerns that the proposals would be unduly burdensome in terms of time and cost and that they would lead to a two tier reporting system for those applying the full and simplified versions of IFRS. The revised proposals result in IFRS being applied no more widely than currently required under Company Law, instead favouring wider use of the simplified version of IFRS.

A summary of the main changes under the proposals is as follows:

- the simplified version of IFRS will now be referred to as FRS102 (previously the Financial Reporting Standard for Medium Size Entities, FRSME);
- accounting options that currently exist under current FRS and IFRS will now also be permitted under FRS 102. This means that fixed assets may be stated at cost or valuation (previous only cost) and interest capitalisation will be permitted;
- the formats adopted will follow those currently applied under Company Law;
- The adoption date has been delayed another year to January 2015 (2015/16 year end);
- The public benefit entity requirements now form part of FRS102 rather than being set out in a separate standard.

While these changes will reduce the burden of transition to IFRS there are nevertheless certain areas that will require attention well in advance of the mandatory adoption date, financial instruments, in particular. FRS102 will require certain financial instruments, such as standalone interest rate swaps, caps and collars to be booked at market value in the balance sheet and with gains / losses passing through the income statement. The gains and losses could be particularly significant with the potential to result in covenant breaches. Hedge accounting provides a means to mitigate the impact on the income statement where certain tests of effectiveness are met and where appropriate documentation is put in place. IFRS 9, which is still being drafted, will provide a simpler framework for what has up until now been a complex approach for hedge accounting.

Wider considerations when adopting IFRS will include:

- considering the timing of undertaking the conversion work given that 2015 comparatives and 2014 opening balances will need to be restated;
- examining whether current IT systems will be sufficient for reporting under IFRS;
- reviewing whether your organisation has the appropriate level of expertise to carry out the conversion;
- ensuring that sufficient time and resource is allocated to the conversion process; and
- With the revised Exposure Drafts in place, work will now commence on the revised housing SORP with consultation expected to take place in late 2012.

As the timetable and form of convergence becomes clearer we will continue to highlight the most significant areas of impact.

Regulatory changes - Welfare reform

The potential changes to housing benefit and welfare systems have been much discussed in the housing and broader media, and in some cases are continuing to evolve as government policy. However, in recent months, we are seeing our clients begin to consider the implications and actions needed in more detail. Key issues are:

- Increase in non dependant deductions from Housing Benefit (already effective from April 2011)
- Universal credit and direct payment to tenants (March 2013)
- Reduction in benefit for under occupation (April 2013)

These changes will have a significant effect on many of the Company's tenants, as well as creating risks to income recovery. Significant work is likely to be required to mitigate these risks, and is likely to require targeted and proactive contact with affected tenants.

As proposed changes become firmer and more imminent, the Company needs to ensure it has clear action plans in place to respond to these changes. These plans should address the changes needed from a people, systems and process perspective – all of which may need to be reviewed in light of future requirements.

The Company should seek to assure itself that this action plan is comprehensive and that arrangements are in place to monitor progress.

The global financial pressures of the last few years have resulted in a more cautious approach to financing by the banks. This is resulting in a number of housing associations exploring alternative methods of financing or investigating way to get as much value as possible from their current financing arrangements. Whilst this section is more relevant to housing associations, we thought you would be interested in current hot topics in the sector.

Against a backdrop of the government's reduction in the affordable housing budget by 60% over the next 4 years, Organisations have been looking at sources of funding to compensate for this reduction.

However, with these government changes coinciding with a difficult funding environment in the UK, a funding gap is starting to emerge. In the past, 89% of agreed facilities for Organisations related to bank funding, with 10% being capital market funding

This is driving associations to look at alternative methods of funding, and we have seen a number of these initiatives across the sector:

Bond financing

Listed bond markets (both institutional and retail) are becoming increasingly attractive to associations because they provide access to large long term debt. They offer greater flexibility and simple covenant structures, and investors see housing as a good long term investment.

Associations thinking about bond issues for the first time need to consider the time and effort taken to prepare for a bond issue as well as the fact that it is crucial to maintain a good credit rating and engage with investors.

New Registered Providers (RPs)

For some associations, the difficulty with obtaining additional bank funding is around the covenant limits on existing facilities. For instance, associations are finding that taking on more debt pushes them over their existing gearing covenants. One option that a number of associations are considering is to set up a second RP, registered with the Tenants Service Authority (TSA); this new RP can raise its own finance and fund new developments. A transfer of properties from the original RP to the new one is often used as security for the initial tranche of finance.

However, a number of potential issues need to be considered beforehand. These include

- requirement for TSA approval;
- approval from the existing lenders may be required;
- there may be restrictions in the existing loans regarding the number of properties that can be transferred to the new association; and
- any covenants which calculate ratios based on all entities in the group combined need to be considered.

Joint Ventures

The creation of strategic partnerships with private sector developers has been on the increase for a number of years. This kind of relationship can create benefits for both parties, with associations often having access to cheaper sources of funds and a ready tenant list, with developers having attractive land banks and a variety of specialist skills.

The key to a successful JV is the choice of partner; different priorities and methods of working are inevitable, but a shared sense of purpose is crucial to success.

One other important consideration is how to structure and finance a JV. There are many different options and careful consideration needs to be given to this in advance.

Mergers

Mergers continue to be an agenda item for those charged with governance, particularly with the increasing focus on Value for Money and the need to achieve efficiencies.

Mergers could be one method to achieve the above but there are several factors to consider before proceeding with a merger including:

- time and cost of a merger;
- generating cost savings and efficiencies post merger;
- assessing the common goals and aims between the merging parties;
- enhancement of the current skills set;
- tenant involvement;
- financial viability of the RP post merger; and
- banks re-pricing borrowings in the event of a merger.

Given the current changes in the sector we expect to continue to have conversations and to offer advice to RP's in relation to the above.

Other options

For associations where these type of options are not feasible, the focus will be on maximising existing funding and creating as much covenant headroom as possible. For instance:

- maintaining good relationships with lenders;
- robust financial planning and modelling;
- discussions with lenders around the impact of component accounting and IFRS on covenants;
- funding and payment plans with developers and subcontractors designed to maximise cash flow advantages; and
- changing the mix of properties developed to maximise cross-subsidies from properties built for outright sale.

There have been a number of recent changes to taxation rates and compliance rules.

Please feel free to talk to your audit team about any tax concerns you may have, and where appropriate they can put you in touch with one of our housing tax specialists.

Employment Tax

Like all other employers, Registered Providers will need to consider the impact of the introduction of Real Time Information ("RTI").

Under the proposed RTI system, employers will need to provide HMRC with details regarding the amount of income tax, NIC, and other amounts relating to each employee's pay when, or before, they make the salary or wage payment to the employee. Currently this happens at the end of every tax year by submitting forms P35 and P14 to HMRC. RTI will be equivalent to carrying out this same end of year reporting – but on a monthly "real time" basis.

RTI will be launched on 1 October 2013. Over the next year all employers will need to review their current payroll reporting systems to see not only whether they hold the required information necessary to deal with RTI but also to consider how best the information can be submitted to HMRC.

Stamp Duty Land Tax (SDLT) - Relief for the purchase of multiple dwellings

A new measure was introduced in 2011 and as a result a relief will apply where there is a bulk purchase of residential properties.

Previously, SDLT would have been calculated with reference to the aggregate amount or value of the consideration given for all of the properties. If the aggregate was over £500,000 then the 4 per cent rate applied. The change will mean that the SDLT on the consideration will now be calculated with reference to the average price of all of the properties purchased, ie the aggregate consideration divided by the number of dwellings. If therefore 10 housing units are purchased each with a price of £150,000, then the 1 per cent rate would apply resulting in a charge of £15,000 compared to the charge of £60,000 charge which would have applied on the same transaction previously.

This is not expected to impact on Registered Providers purchasing development land, as in the majority of cases they should be able to claim relief on the purchase of land for affordable dwellings, either under the Registered Provider relief or charity relief. It will however impact of development subsidiaries buying a number of existing residential properties from a developer or investor, or those Registered Providers who are not able to benefit from relief on multiple purchases from the same vendor.

The new relief applies to residential property only and took effect from 19 July 2011.

VAT - Increased VAT rate

The increase of VAT to 20% which came in last year has increased costs for Housing Associations and Charities. This, in turn, is increasingly leading such organisations to consider ways to mitigate VAT costs, including:

•Repair and maintenance costs

A number of Housing Associations are looking at innovative arrangements with third party contractors aimed at increasing security of provision (after the demise of leading contractors) and mitigating the VAT cost. These arrangements typically involve 'partnering' with the private sector and may involve the establishment of a separate legal entity (for example, a Limited Liability Partnership (LLP)).

•Use of 'design and build' contracts

Following representations against a proposed change of policy, HMRC accepted that 'design and build' contracts remain an effective way to reduce VAT costs on new build residential developments.

•Cost Sharing Exemption

The cost sharing exemption is scheduled to be introduced in the summer of 2012. This measure should remove the VAT cost that currently arises when organisations share costs (for example, back-office finance or IT functions).

VAT registration and deregistration limits

With effect from 1 April 2012, the taxable turnover limit which determines whether a business has to be registered for VAT was increased from £73,000 to £77,000. The taxable turnover limit which determines whether a business may apply for deregistration was increased from £71,000 to £75,000.

Corporation tax

The standard rate of corporation tax from 1 April 2012 is 24 per cent and will decrease by 1 per cent to 23 per cent from 1 April 2013. The small profits rate remains at 20 per cent.

All Taxes – Public Sector Bodies Group

Registered Providers of Social Housing fall within the remit of the HMRC Public Sector Bodies Group (PSBG). The purpose of the PSBG is to pool sector knowledge and apply many of the principles adopted by HMRC's large and complex business unit to the public sector.

We are seeing a number of Registered Providers being allocated HMRC 'Client Relationship Managers' (CRMs). The role of the CRM is to assess the Registered Provider's tax risk management procedures in order to allocate them an appropriate risk profile.

The CRMs and the risk profiles cover all taxes and will determine the level of HMRC interventions and visits.

This section summarises some current pension issues affecting the sector around benefit changes and auto-enrolment. Both of these issues are areas which the company should be considering.

Pensions – Benefit changes

Employees of social housing organisations typically receive pension benefits from one or more of The Local Government Pension Scheme (LGPS), the Social Housing Pension Scheme (SHPS), or a bespoke pension scheme set up directly by the organisation.

You may be aware from recent press coverage that LGPS benefits will change significantly within the next couple of years with the principles of the changes having now been agreed. Equally the benefits provided by the SHPS are also currently under review. Finally, in turn, these reforms are also triggering benefit reviews by many organisations operating their own pension schemes (where often the benefits are designed to be comparable to other public sector schemes).

Whilst some organisations are monitoring the changes from a distance, many are unaware of the potential effect of the changes or the timescales in which they are to be implemented.

These benefit reforms are already underway and the new LGPS structure is expected to be in operation by April 2014. The short consultation with employers on deficit repayment is expected to take place until the end of June 2012. The valuation takes place against a backdrop of difficult market conditions, such as falls in the stock market and low interest rates. These will both have adversely affected the Scheme's funding position.

The changes represent a significant issue for housing organisations and their employees. However in our experience the detail of what is happening is often not understood.

Employers need to understand the changes and put in place a strategy to:

- Understand the impact of the changes on their costs;
- Agree a pension scheme design that provides sustainable, competitive benefits (where flexibility in design possible); and
- Communicate effectively with employees and support them through the changes.

Pensions – Auto-enrolment

Legislation has been introduced requiring employers to automatically enrol ("auto-enrol") employees into a qualifying pension scheme in the future.

There are no exemptions for the public sector despite the fact that the duty was designed to boost pension scheme membership in the private sector.

The requirements for the public sector are identical to the private sector although the impact could be less pronounced since many public sector employees are already members of qualifying schemes.

The auto-enrolment requirements will begin to apply for many organisations within the next twelve months. With this deadline fast approaching, employers need to make sure that they have a plan in place to ensure compliance.

This is a significant issue because:

- Employer pension costs are likely to increase; and
- Significant administrative requirements apply to monitor the eligibility of workers and manage the enrolment process.

Other key considerations will be:

- The staging date;
- Ensuring payroll systems are appropriate and can be in place on time;
- Identifying an appropriate pension scheme to offer to employees who are not currently pension scheme members and new employees; and
- Understanding the current pension schemes and taking the opportunity to refresh these, taking into account the cost.

KPMG has responded innovatively to a growing demand for assurance/reassurance from both non-executives and senior management by developing the concept of Maximum Assurance. This allows us to extend the work we do as part of the statutory audit into other areas. Whilst this section is more relevant to housing associations, we thought you would be interested in current hot topics in the sector.

What is Maximum Assurance?

Within the social housing sector a combination of:

• economic pressures;

• lack of capacity of internal auditors to meet all of the assurance needs of the social housing providers;

• regulatory change; and

• governance failures

have created a desire to get high quality assurance over all that matters to the organisation, not just the statutory accounts.

Since we are already working with you, understand your business and have access to your staff, extending our role can therefore be an efficient and effective way to obtain any wider assurances you need.

We have provided some examples below of recent additional assurance projects we have undertaken in the sector. This is by no means an exhaustive list; equally, not every service will be appropriate for you, and of course we are careful to avoid a potential conflict of interest with the external audit.

If you feel there is an area where you would like additional assurance, please speak to your audit team about how, as part of our external audit, we could provide other services to help maintain confidence, trust and comfort in your operations.

Financing

Where organisations are increasingly looking at alternative sources of funding, this brings with it a number of challenges. KPMG are able to help provide assurance around risk points, and assess areas where the organisation may wish to strengthen existing procedures, or incorporate best practice ideas.

Our work can be extended to include the following:

- Review of existing covenant monitoring and forecasting procedures;
- Assessment of new strategic plans again terms of existing loan agreements (eg limits on numbers of disposals);
- Readiness review in advance of a bond issue;
- Benchmarking of quality and timeliness of information provided to finance or treasury committees;
- Review of Joint Venture arrangements and procedures; and
- Involvement of KPMG's financing advisory team who specialise in advising clients on financing options. This team can be introduced to you if you wish.

Development scheme appraisal assumptions

The reduced level of grant funding on development schemes means that there is a heightened risk around viability of projects. With this increased level of risk, the accuracy of appraisal assumptions is more important than ever.

We have conducted a review of appraisal assumptions at a number of clients, either on a one off basis to focus on particularly big / high risk schemes or focusing on all schemes that exceed a certain value. A report of 15-25 pages is produced summarising our findings to the relevant Committee and management, thereby providing a robust check on what is a key control for many organisationss.

Review of controls around appointment of contractors

Under more challenging financial conditions there is an increased risk of businesses failing and this has been illustrated with a number of high profile examples. The need for strong controls around the appointment of contractors is therefore more important than ever both in relation to professional advisors such as employers agents but also in relation to the appointment of building contractors on development schemes. We have carried out a review of controls around appointment of contractors at clients including:

- Review of the financial checks carried out around viability of suppliers added to the approved supplier list;
- The extent to which annual checks are updated to review ongoing viability of contractors;
- Consideration of the financial checks carried out where a contractors not on the approved list is used;
- Where financial checks are carried out using a third party provider considering the robustness of those checks; and
- Following the review a brief report of the findings and suggested control improvements is presented to management and the Audit Committee.

Appendices

Appendix 1
Audit recommendations

Our objective is to use our knowledge of The Gateshead Housing Company gained during our routine audit work to make useful comments and suggestions for you to consider. However, you will appreciate that our routine audit work is designed to enable us to form an audit opinion on the financial statements of the Company and it should not be relied upon to disclose all irregularities that may exist nor to disclose errors that are not material in relation to those financial statements.

- This report is provided on the basis that it is for your information only and that it will not be quoted or referred to, in whole or in part, without our prior written consent.
- Our report is designed to include useful recommendations that may help improve performance and avoid weaknesses that could lead to material loss or misstatement. However, it is your obligation to take the actions needed to remedy those weaknesses and should you fail to do so we shall not be held responsible if loss or misstatement occurs as a result.

We have identified below each of the observations arising from our work where further action is required. Each of our recommendations has been graded:

- **High** – recommendations which are fundamental to the system of internal control or have a potential material effect on the financial statements and should be addressed immediately by management;
- **Medium** – recommendations which will significantly enhance internal controls and should be addressed promptly by management;
- **Low** – recommendations which will improve performance but are not vital for internal control performance.

We have no new audit recommendations arising from the work we have performed in the current year audit.

Update on prior year audit recommendations

We set out below the issues we raised in 2010/11 and comment on progress toward the recommendation in 2011/12.

Observation and risk	Recommendation and 2010/11 management response	KPMG update and updated management response
Supplier statement reconciliations		
Medium – Supplier statement reconciliations are only performed on Morrison's supplier statements. This can lead to the omission of liabilities due to suppliers.	Supplier statements should be requested from other major suppliers, primarily Gateshead Council. These should be reconciled to the accounting records each month in order to ensure that no discrepancies arise between the Company's records and those of its suppliers. **Management response:** We share an accounting system and receive a trial balance annually from Gateshead Council therefore, we do not feel that undertaking a supplier statement reconciliation with them is necessary. Ad hoc supplier statements received are reconciled on a monthly basis and filed. No further work is considered necessary by the Company on this as the main supplier statement reconciliation is carried out.	Morrison's statements continued to be reconciled up to the end of their contract in March 2012, however no statement is received from the Council. We understand that a new maintenance contract has been entered into with Mears, and statements from Mears will be reconciled when received in the 2012/13 year. **Updated response** We share an accounting system and receive a trial balance annually from Gateshead Council, as well as agree the year end cash balance, therefore, we do not feel that undertaking a supplier statement reconciliation with them is necessary. Ad hoc supplier statements received are reconciled on a monthly basis and filed. No further work is considered necessary by the Company on this as the main supplier statement reconciliation is carried out.
Bank account		
Low –The Company does not have access to its own banking facilities and uses a shared facility operated by Gateshead Council. This can lead to a lack of clarity as to which transactions relate to the Company and reduces the level of control of the Company over its assets.	The company should consider opening a fully functional bank account such that it can process its own cash transactions, which would enable the Company to control its assets and to maintain clear records of its cash transactions. **Management response:** The Company and Council continue to discuss this recommendation, however, resource constraints have prevented this from being actively pursued.	The company still uses a shared facility for the majority of its transactions. Discussions have been held with the Council in respect of the matter. **Updated response** The Council and Company do not consider this to be a current priority. Cash balances are agreed with the Council at the year end.
Old debtors		
Low - It was noted during the audit that some debtors are still outstanding from the prior year end. Although these amounts are due from Gateshead Council and Morrison, hence the credit risk is considered to be low, recovery of debts may become more challenging as balances become older.	Monitoring and follow up of outstanding debtors would improve the company's working capital position and would further reduce credit risk. **Management response:** We have received confirmation from Morrison and Gateshead Council that the monies owed will be paid.	**Resolved –** No issues were identified with debtors during the 2011/12 audit.

Audit differences

This appendix sets out the audit differences identified for the year ended 31 March 2012.

The Gateshead Housing Company Limited				
	Income and expenditure account		Balance sheet	
Uncorrected audit differences (£000)	**Debit**	**Credit**	**Debit**	**Credit**
Pension creditor				
Dr Other taxation and social security			110	
Cr Accruals and deferred income				(110)
Being the misclassification of the pension creditor				
Total	£nil	£nil	110	(110)
Overall net I&E effect	*£nil*	*£nil*		

The Gateshead Housing Company Limited				
	Income and expenditure account		Balance sheet	
Corrected audit differences (£000)	**Debit**	**Credit**	**Debit**	**Credit**
VAT debtor				
Dr Other taxation and social security			114	
Cr Trade debtors				(114)
Being the receipt of the VAT element of an invoice prior to year end, not posted to the VAT account.				
Total	£nil	£nil	114	(114)
Overall net I&E effect	*£nil*	*£nil*		

Letter of management representations

KPMG LLP
Quayside House,
110 Quayside,
Newcastle upon Tyne,
NE1 3DX

19 July 2012

Dear Sirs

This representation letter is provided in connection with your audit of The Gateshead Housing Company Limited ("the Company"), for the year ended 31 March 2012, for the purpose of expressing an opinion:

I. as to whether these financial statements give a true and fair view of the state of the Company's affairs as at 31 March 2012 and of the Company's profit or loss for the financial year then ended;
II. whether the financial statements have been properly prepared in accordance with UK Generally Accepted Accounting Practice; and
III. whether the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

These financial statements comprise the Balance Sheet, the Income and Expenditure Account, the Cash Flow Statement, the Statement of Total Recognised Surpluses and Deficits, and notes, comprising a summary of significant accounting policies and other explanatory notes.

The Board confirms that the representations it makes in this letter are in accordance with the definitions set out in the Appendix to this letter.

The Board confirms that, to the best of its knowledge and belief, having made such inquiries as it considered necessary for the purpose of appropriately informing itself:

Financial statements

1. The Board has fulfilled its responsibilities, as set out in the terms of the audit engagement dated 4 November 2009, for the preparation of financial statements that:
   - give a true and fair view of the state of the Company's affairs as at the end of its financial year and of the surplus or deficit for that financial year;
   - have been properly prepared in accordance with UK Generally Accepted Accounting Practice ("UK GAAP");
   - have been prepared in accordance with the requirements of the Companies Act 2006.

The financial statements have been prepared on a going concern basis.

2. Measurement methods and significant assumptions used by the Board in making accounting estimates, including those measured at fair value, are reasonable.
3. All events subsequent to the date of the financial statements and for which FRS 21 *Events after the balance sheet date* requires adjustment or disclosure have been adjusted or disclosed.
4. The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the financial statements as a whole. A list of the uncorrected misstatements is attached to this representation letter.

Information provided

5. The Board has provided you with:
   - access to all information of which it is aware, that is relevant to the preparation of the financial statements, such as records, documentation and other matters;
   - additional information that you have requested from the Board for the purpose of the audit;
   - unrestricted access to persons within the Company from whom you determined it necessary to obtain audit evidence.
6. All transactions have been recorded in the accounting records and are reflected in the financial statements.
7. The Board acknowledges its responsibility for such internal control as it determines necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error. In particular, the Board acknowledges its responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.

The Board has disclosed to you the results of its assessment of the risk that the financial statements may be materially misstated as a result of fraud.

8. The Board has disclosed to you all information in relation to:
   a) Fraud or suspected fraud that it is aware of and that affects the Company and involves:
      - management;
      - employees who have significant roles in internal control; or
      - others where the fraud could have a material effect on the financial statements;
   b) allegations of fraud, or suspected fraud, affecting the Company's financial statements communicated by employees, former employees, analysts, regulators or others.
9. The Board has disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
10. The Board has disclosed to you and has appropriately accounted for and/or disclosed in the financial statements in accordance with FRS 12 *Provisions, Contingent Liabilities and Contingent Assets*, all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.
11. The Board has disclosed to you the identity of the Company's related parties and all the related party relationships and transactions of which it is aware and all related party relationships and transactions have been appropriately accounted for and disclosed in accordance with FRS 8 Related party disclosures.
12. The Board confirms that:
    a) The financial statements disclose all of the key risk factors, assumptions made and uncertainties surrounding the Company's ability to continue as a going concern as required to provide a true and fair view.
    b) Any uncertainties disclosed are not considered to be material and therefore do not cast significant doubt on the ability of the Company to continue as a going concern.

Appendix 4
Letter of management representations (cont.)

13. On the basis of the process established by the Board and having made appropriate enquiries, the Board is satisfied that the actuarial assumptions underlying the valuation of pension scheme liabilities are consistent with its knowledge of the business.

The Board further confirms that:

a) all significant retirement benefits, including any arrangements that are:
   - statutory, contractual or implicit in the employer's actions;
   - arise in the UK and the Republic of Ireland or overseas;
   - funded or unfunded;
   - approved or unapproved,

   have been identified and properly accounted for; and

b) all settlements and curtailments have been identified and properly accounted for.

This letter was tabled and agreed at the meeting of the Board of Management on 19 July 2012.

Yours faithfully,

Director

Appendix to the Board Representation Letter of The Gateshead Housing Company Limited: Definitions

Financial Statements

A complete set of financial statements comprises:

- A Balance Sheet as at the end of the period;
- An Income and Expenditure Account for the period;
- A Statement of Total Recognised Surpluses and Deficits for the period;
- A Cash Flow Statement for the period;
- notes, comprising a summary of significant accounting policies and other explanatory information.

Material Matters

Certain representations in this letter are described as being limited to matters that are material.

The ASB's Statement of Principles for Financial Reporting states that:

"An item of information is material to the financial statements if its misstatement or omission might reasonably be expected to influence the economic decisions of users of those financial statements, including their assessments of management's stewardship."

Fraud

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users.

Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorisation.

Error

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

- was available when financial statements for those periods were authorised for issue; and
- could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

Management

For the purposes of this letter, references to 'management' should be read as 'management and, where appropriate, those charged with governance'.

Related party

A related party is a person or entity that is related to the entity that is preparing its financial statements (referred to in FRS 8 Related Party Disclosures as the "reporting entity").

a) A person or a close member of that person's family is related to a reporting entity if that person:
   i. has control or joint control over the reporting entity;
   ii. has significant influence over the reporting entity; or
   iii. is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.
b) An entity is related to a reporting entity if any of the following conditions applies:
   i. The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
   ii. One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
   iii. Both entities are joint ventures of the same third party.
   iv. One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
   v. The entity is a retirement benefit scheme for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a scheme, the sponsoring employers are also related to the reporting entity.
   vi. The entity is controlled or jointly controlled by a person identified in (a).
   vii. A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

Related Party Transaction

The transfer of assets or liabilities or the performance of services by, to or for a related party irrespective of whether a price is charged.

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