

Audit Committee update

Swale Borough Council

Audit 2011/12

The Audit Commission is a public corporation set up in 1983 to protect the public purse.

The Commission appoints auditors to councils, NHS bodies (excluding NHS Foundation trusts), police authorities and other local public services in England, and oversees their work. The auditors we appoint are either Audit Commission employees (our in-house Audit Practice) or one of the private audit firms. Our Audit Practice also audits NHS foundation trusts under separate arrangements.

We also help public bodies manage the financial challenges they face by providing authoritative, unbiased, evidence-based analysis and advice.

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Introduction

1 The purpose of this paper is to provide the Audit Committee with a report on progress in delivering our responsibilities as your external auditors. It includes an update on the externalisation of the Audit Practice.

2 This paper also seeks to highlight key emerging national issues and developments which may be of interest to members of the Audit Committee. The paper concludes by asking a number of questions which the Committee may wish to consider in order to assess whether it has received sufficient assurance on emerging issues.

3 If you require any additional information regarding the issues included within this briefing, please feel free to contact me or your Audit Manager using the contact details at the end of this update.

Executive summary

4 We continue to meet with finance staff to discuss progress and our visit to begin our phase one interim work took place in February 2012. There are no significant matters arising from our audit which we need to bring to your attention at the current time.

5 Appendix 1 of this report sets out matters we are required to discuss with those charged with governance, we would appreciate a formal response either by letter or email by 30 April 2012.

Andy Mack

District Auditor

8 March 2012

Progress report

Financial statements

1 We are required to audit the financial statements and to give our opinion on:

- whether they give a true and fair view of the financial position of the Council and of its income and expenditure for the year in question; and
- whether they are prepared properly in accordance with relevant legislation and applicable accounting standards.

2 We are also required to:

- review whether the Annual Governance Statement is presented in accordance with relevant requirements; and
- Audit the whole of government accounts consolidation pack based on the information provided in the financial statements.

3 Appendix 2 sets out the progress made in completing our work.

4 We continue to hold regular meetings with the Finance team to discuss issues arising in relation to the 2011/12 financial statements audit. We have also held discussions with Internal Audit to discuss the progress of their internal audit plans and any emerging issues highlighted from their reviews.

VFM conclusion

5 Our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness is based on two criteria, specified by the Commission, related to your arrangements for:

- securing financial resilience – focusing on whether the Council is managing its financial risks to secure a stable financial position for the foreseeable future; and
- challenging how the Council secures economy, efficiency and effectiveness – focusing on whether the Council is prioritising its resources within tighter budgets and improving productivity and efficiency.

6 Following completion of our risk assessment the work will focus on:

- The progress made in updating the medium term financial strategy and business planning; and
- We will assess the overall financial standing and progress in delivering its medium term financial strategy.

7 We will minimise the burden for you from this work, by making use as far as possible of existing Council information. We will aim to provide helpful and constructive feedback during and at the end of the audit.

Certification of claims and returns

8 In 2011/12 we anticipate being required to certify the following grant claims and returns:

- Housing and Council Tax Benefits Subsidy Claim;
- National Non-Domestic Rates Return; and
- Disabled Facilities Grant Return (dependent on value of the return).

9 Each return has a separate deadline for certification and we will liaise with staff to ensure work is completed to meet the specified deadline.

Government response to consultation on the future of local public audit

10 In August 2010, the government announced its intention to bring forward legislation to abolish the Audit Commission and put in place a new framework for local public audit. In March 2011, the government published a consultation paper and, in January 2012, announced its response to the consultation to which it received 453 responses, the majority from audited bodies.

11 The Audit Commission is currently in the process of the award of contracts for the work currently undertaken by the Audit Practice for the period 2012/13 to either 2014/15 or 2016/17 (see 'update on the externalisation of the Audit Practice' below). The government envisages the retention of the Audit Commission as a small residuary body until the end of those contracts, to oversee them and to make any necessary changes to individual audit appointments.

12 Thereafter, the government proposes that a new local public audit regime will apply. The key features of that regime are as follows.

- The National Audit Office will be responsible for developing and maintaining audit codes of practice and providing support to auditors.
- Mirroring the Companies Act provisions, auditors will be subject to the overall regulation of the Financial Reporting Council (the FRC). The FRC will authorise one or more Recognised Supervisory Bodies (in practice, the professional institutes) to register and supervise audit firms and engagement leads.
- Directly-elected local government bodies will appoint their own auditor on the advice of an independent audit appointment panel with a majority of independent members. Such panels may be shared between audited bodies.
- Audited bodies must run a procurement exercise for their external audit appointment at least every five years, although there would be no bar on the reappointment of the incumbent audit firm (for a maximum of one further five-year term);
- Audited bodies will be able to remove their auditor, but only after due process, involving the independent audit appointment panel and culminating in a public statement of the reasons for the decision.
- The audit will continue to cover arrangements for securing economy, efficiency and effectiveness, but without imposing further burdens on audited bodies. There will be further consultation on the approach to value for money.
- The power to issue a public interest report will be retained.

- Audit firms will be able to provide non-audit services to audited bodies, subject to complying with ethical standards and gaining approval from the independent auditor appointment panel.
- The right to object would be retained, but the auditor will be given the power to reject vexatious, repeated or frivolous objections.
- Grant certification will be subject to separate arrangements between grant paying bodies, audited bodies and reporting accountants (who could be the external auditors).
- The National Fraud Initiative will continue. Discussions on how this will be achieved are ongoing.

13 The government is holding further discussions with audited bodies and audit firms to develop its proposals. The Regional Improvement and Efficiency Partnerships has organised events in January and February 2012 to which audited bodies were invited. The government intends to publish draft legislation for pre-legislative scrutiny in Spring 2012.

Update on the externalisation of the Audit Practice

14 The Audit Commission's Chief Executive, Eugene Sullivan, wrote to clients on 21 September 2011 summarising the Department for Communities and Local Government's plans for externalising the Audit Commission's work that is currently undertaken by the Audit Practice. An update on progress was provided in Eugene's subsequent letter of 10 November 2011.

15 The key points are as follows.

- Contracts will be let from 2012/13 on a three- or five-year basis. The earliest you will be able to appoint your own auditors is therefore for the 2015/16 audit.
- The work is split into four regions, comprising ten 'lots'. Each lot will be awarded separately, but any individual bidder can only win a maximum of one lot in each region (ie four lots in total).
- The Commission is managing a fair and equitable procurement process to allow suitable private sector providers the opportunity to compete for the contracts.
- Thirteen potential providers were invited to tender following the initial pre-qualification stage. The deadline for return of the tenders was 16 December 2011. Tenders received are currently being evaluated. The Commission plans to announce the successful tenderers in March 2012.
- The Commission is planning to set out, early in 2012, the consultation process to be followed for individual audit appointments. For bodies currently audited by the Audit Practice, there will be an opportunity to attend an introductory event in each contract area with the Commission and the firm awarded the contract. The events will take place in May 2012.
- Appointments will start on 1 September 2012. As such, the Commission is extending the current audit appointment to allow any audit issues arising between 1 April 2012 and 31 August 2012 to be dealt with. The Commission's Director of Audit Policy and Regulation wrote to clients on 19 December 2011 setting out more details on this 'interim' appointment.
- Audit Practice staff in each lot area will in the main transfer to the successful bidders on 31 October 2012.

16 Further details are available on the Commission's website. We will continue to keep you updated on developments and will provide a verbal update at the Audit Committee meeting.

17 Against this background, the Audit Practice's focus remains.

- Fulfilling our remaining responsibilities –delivering your 2011/12 audit - to the high standards you expect and deserve.
- Managing a smooth transition from the Audit Practice to your new audit provider.

Other matters of interest

2010/11 Accounts

18 In December 2011 the Audit Commission published a report - Auditing the Accounts 2010/11 - which summarises its findings of the accounts audits in 2010/11.

19 The report covers the quality and timeliness of financial reporting by councils, police authorities, fire and rescue authorities and other local public bodies. In addition to auditors' work on the 2010/11 financial statements, the report also covers:

- the results of the first year of International Financial Reporting Standards (IFRS) implementation;
- auditors' work on the Whole of Government Accounts returns;
- auditors' local value for money work;
- public interest reports and statutory recommendations issued by auditors since December 2010; and
- the key challenges facing bodies for 2011/12.

20 Auditors were able to give opinions on the accounts by the target date of 30 September 2011 at most organisations and this performance compares well with the previous year.

21 However, the challenges presented by the transition to IFRS are demonstrated by an increase in the number of bodies, from seven last year to eighteen this year, where the auditor's opinion was still outstanding after 31 October. There was also a significant increase in the number of bodies needing to make material adjustments to their accounts following the audit.

22 On 18 January 2012, the Audit Commission published 'Let's be clear: Making local authority IFRS accounts more accessible and understandable'.

23 This briefing supplements the report on the 2010/11 accounts referred to above and focuses on a long-running debate of how to make local government accounts easier to understand.

24 While the statutory accounts give comprehensive information on each local authority's financial position and performance, reflecting the range of activities which they cover, they are a poor way of communicating the key information to lay readers.

25 The briefing notes that:

- elected members and local people would benefit from having access to well-presented extracts from the accounts, which would provide the key information on each authority's financial position and performance;

- the accounting profession and the Audit Commission could do more to encourage auditors and preparers of accounts to reduce clutter in statutory accounts; and
- each authority could do more to ensure their accounts are shorter and more accessible. Those preparing accounts need to look critically at the previous year's accounts. They should identify how these accounts could be sharper and more focused before starting work on the next set.

26 The briefing concludes by identifying possible steps to make local authority accounts more accessible and easier to understand, and the implications of doing so.

27 The Audit Commission is seeking views on the issues raised within the briefing and has invited comments by 16 March 2012 - further information on this is available on the Audit Commission's website.

Managing Workforce Costs

28 The Audit Commission and Local Government Association have jointly launched 'Work in progress: Meeting local needs with lower workforce costs'.

29 The joint report - which can be found on the Audit Commission's website - is aimed at councils as employers and shows how local authorities across England are reducing their workforce costs, with some finding creative solutions.

30 As government funding for councils shrinks by over a quarter between 2011/12 and 2014/15, councils need to reduce their workforce costs substantially while still providing much needed services. Not all councils face the same financial challenges, but the message is that all must reassess what they do, how they do it, and what their priorities are. Those opting for major restructuring will take more time to realise savings.

31 Councils are finding ways to cut their pay bills without losing jobs, but the report says that redundancies are inevitable. Local government was already reducing posts before the cuts in government funding. In the past year an estimated 145,000 jobs have gone and this figure will increase in the future. So far many redundancies have been voluntary, but the report warns that compulsory ones are set to rise.

32 The report is supported by a number of resources including:

- an agency workers expenditure tool which shows councils how much they spend on agency workers, compared with groups of similar councils;
- a workforce expenditure tool which shows councils how much they spend on staff as a proportion of their net current expenditure, and how this has changed over time;
- five case studies which provide examples of the different approaches councils are taking to reduce the costs of employing people while protecting valuable services. The case studies show what the councils did and why - and the benefits achieved; and

- a practical guide on how to undertake effective pay benchmarking, providing a series of steps to follow when starting a pay benchmarking process and highlighting the main issues that should be considered.
- 33** The report is supplemented with a briefing for elected members that includes a number of questions designed to help members assess how well their council decides the size, shape and cost of its workforce and how these decisions will affect services and communities.
- 34** The questions are in two parts:
- the information that should be available to members about the workforce; and
 - the savings strategies councils could follow in the light of that information.

CIPFA's Prudential Code for Capital Finance

35 CIPFA has recently updated its Prudential Code for Capital Finance in Local Authorities. This new version reflects the introduction of IFRS which required:

- PFI schemes to be included on organisations' balance sheets; and
- The accounting treatment of leases to be reviewed – with many more likely to be considered as finance leases and thus also included on the relevant balance sheets.

36 The code also includes guidance on the treasury management implications of the housing self-financing reforms.

37 Although local authorities determine their own capital programmes, they are required to have regard to CIPFA's Prudential Code (the Code) in order to ensure that these capital investment plans are affordable, prudent and sustainable.

38 To demonstrate that these objectives have been met, the Code sets out the indicators that must be used and the factors that must be taken into account.

39 The Code does not include suggested indicative limits or ratios and these are for the local authority to set itself, subject to some overriding controls.

40 The prudential indicators required by the Code should be considered alongside its Treasury Management performance indicators. These indicators are both are designed to support and record local decision making and are not designed to be comparative performance indicators.

2011/12 Accounts: CIPFA Guidance Notes for Practitioners

41 CIPFA has recently published a set of guidance notes to provide support in preparing the 2011/12 year-end accounts. These offer constructive advice on all aspects of the requirements for 2011/12 and provide detailed guidance on the key changes, including accounting for:

- heritage assets;
- business rate supplements;
- community infrastructure levies;
- related party disclosures;
- exit packages;
- trust funds;
- financial instruments; and
- interests in joint ventures.

42 The key changes to your financial statements in 2011/12 will also be covered by our final accounts workshops.

For information: Board Governance Essentials

43 The Public Chairs' Forum and CIPFA have recently published a joint 'how to' guide for Chairs and Boards of public bodies.

44 'Board Governance Essentials: A Guide for Chairs and Boards of Public Bodies' offers advice across four key areas.

- Good corporate governance.
- Roles, responsibilities and relationships.
- Standards of behaviour in public life.
- Effective financial management and transparency.

45 This guide may provide interesting reading for all members.

Local Government Finance Bill

46 In December 2011 the government introduced proposals to devolve greater financial powers and freedoms to councils. The Local Government Finance Bill sets out the legislative foundations to implement the changes from April 2013. The most significant proposals relate to non-domestic rates, which are currently pooled and redistributed nationally.

47 The Bill provides for councils to:

- retain a portion of their business rate growth;
- borrow against future income from business rates to pay for roads and transport projects alongside other local priorities;
- ensure a stable starting point for all authorities. No authority will be worse off as a result of their business rates base at the start of the scheme;
- establish a national baseline alongside a system of top ups and tariffs. Councils with business rates in excess of a set baseline would pay a tariff to government whilst those below would get an individually assessed top up from government; and
- create a levy to take back a share of growth from those councils that gain disproportionately from the changes. This money would be used to fund a safety net providing financial help to those authorities which experience significant drops in business rates, for example caused by the closure or relocation of a major business.

48 The Bill provides for much of the detail of the arrangements, including the sharing of business rate growth between billing and precepting authorities, to be left to secondary legislation.

Guide to HRA Self Financing

49 The introduction of self-financing to the housing revenue account (HRA) in April 2012 will fundamentally change the way that local authority housing is funded.

50 CIPFA has therefore recently produced a publication which brings together the latest guidance to assist those working in the sector to understand the changes and help with their implementation.

Key considerations

51 The Audit Committee may wish to consider the following questions in respect of the issues highlighted in this briefing paper.

- Has the Council reviewed the Audit Commission's report on the 2010/11 accounts and, in particular, considered the key challenges facing bodies for 2011/12?
- Has the Council reviewed its 2010/11 accounts and identified ways in which these could be streamlined or clarified?
- Has the Council reviewed the Audit Commission / Local Government Association joint report on managing workforce costs and is the Audit Committee satisfied that appropriate use has been made of the supporting materials?
- Has the Council circulated the briefing for elected members on the Audit Commission's workforce report to Members? Is the Audit Committee satisfied that the questions within the briefing have been properly considered by the Council*?
- Has the Council reviewed its prudential indicators in the light of CIPFA's revised prudential code?
- Has the Council reviewed CIPFA's guidance notes for the 2011/12 financial statements and made satisfactory arrangements for their implementation?

Appendix 1 – Assurances for 2011/12 audit opinion work

Understanding how the Audit Committee gains assurance from management

I have a good understanding of how the Audit Committee as those charged with governance gains assurance over management processes and arrangements. This enables me to deliver an efficient audit, reducing the time your staff need to spend responding to auditor queries.

However, auditing standards require me to formally update my understanding annually. Therefore, I am writing to ask that you please provide a response to the following questions. Where your response to questions 2 to 5 is 'yes', please provide details.

1) How do you exercise oversight of management's processes in relation to:

- undertaking an assessment of the risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments);
- identifying and responding to risks of fraud in the Authority, including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist;
- communicating to employees its view on business practice and ethical behavior (for example by updating, communicating and monitoring against the Authority code of conduct); and
- communicating to you the processes for identifying and responding to fraud or error.

2) How do you oversee management processes for identifying and responding to the risk of fraud and possible breaches of internal control? Are you aware of any breaches of internal control during 2011-12?

3) How do you gain assurance that all relevant laws and regulations have been complied with? Are you aware of any instances of non-compliance during 2011-12?

4) Are you aware of any actual or potential litigation or claims that would affect the financial statements?

5) Have you carried out a preliminary assessment of the going concern assumption and if so have you identified any events which may cast significant doubt on the Authority's ability to continue as a going concern?

In addition to the above questions about how you gain assurance from management, I have included at Appendix 1, 8 questions about your views on fraud. Your responses will inform my assessment of the risk of fraud and

error within the financial statements, which in turn determines the extent of audit work I undertake.

Please provide a response by 30 April 2012 and please contact me if you wish to discuss anything in relation to this request.

Yours sincerely

Andy Mack
District Auditor

Appendix 1

No.	Questions for those charged with governance.	Those charged with governance response
1	Are you aware of any instances of actual, suspected or alleged fraud during the period 1 April 2011 – 31 March 2012?	
2	<p>Do you suspect fraud may be occurring within the Authority?</p> <ul style="list-style-type: none"> ➤ Have you identified any specific fraud risks within the Authority? ➤ Do you have any concerns that there are areas within your Authority that are at risk of fraud? ➤ Are there particular locations within the Authority where fraud is more likely to occur? 	
3	<p>Are you satisfied that internal controls, including segregation of duties, exist and work effectively?</p> <ul style="list-style-type: none"> ➤ If not where are the risk areas? ➤ What other controls are in place to help prevent, deter or detect fraud? 	
4	<p>How do you encourage staff to report their concerns about fraud?</p> <ul style="list-style-type: none"> ➤ What concerns about fraud are staff expected to report? 	
5	<p>From a fraud and corruption perspective, what are considered to be high risk posts within your Authority?</p> <ul style="list-style-type: none"> ➤ How are the risks relating to these posts identified, assessed and managed? 	
6	<p>Are you aware of any related party relationships or transactions that could give rise to instances of fraud?</p> <ul style="list-style-type: none"> ➤ How do you mitigate the risks associated with fraud related to related party relationships and transactions? 	
7	<p>Are you aware of any entries made in the accounting records of the Authority that you believe or suspect are false or intentionally misleading?</p> <ul style="list-style-type: none"> ➤ Are there particular balances where fraud is more likely to occur? ➤ Are you aware of any assets, liabilities or transactions that you believe were improperly included or omitted from the accounts of the Authority? ➤ Could a false accounting entry escape detection? If so, how? ➤ Are there any external fraud risk factors, such as benefits payments or collection of tax revenues which are high risk of fraud? 	

8	<p>Are you aware of any organisational, or management pressure to meet financial or operating targets?</p> <ul style="list-style-type: none">➤ Are you aware of any inappropriate organisational or management pressure being applied, or incentives offered, to you or colleagues to meet financial or operating targets?	
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Appendix 2 – Audit progress as at February 2012

Area of work	Timetable	Progress to date	Final report due/issued	Summary of findings/other comments
Audit fee	to April 2011	Original fee letter 15 April 2011 agreed by the Audit Committee 25 May 2011.	April 2011	Work plan agreed, as summarised below.
Financial Statements				
Interim audit: Compliance with International Standards on Auditing- assessing the effectiveness of the controls operating over the material financial systems	February 2012 to March 2012	We will complete updating our documentation and walkthroughs of material systems in March 2012. Where appropriate we will test key controls identified to assess their operating effectiveness in March 2012. As part of this we will draw on the findings of internal audit as appropriate. We will also complete any early substantive testing where	Interim audit memorandum to be issued March 2012 if required.	We plan to place reliance on key controls where identified.

Comment [A1]: This seems a little late. Won't we be doing this by March 2009?

Area of work	Timetable	Progress to date	Final report due/issued	Summary of findings/other comments
		possible.		
Financial Statements audit	July to September 2012	Onsite visit due to commence in July 2012. However, we have begun to consider items that could require specific testing during the final accounts audit.	Annual Governance Report due September 2012. A Final Accounts Memorandum will be issued if there are any other key issues to report.	The Annual Governance Report will summarise our conclusions under the Code of Audit Practice for those charged with governance prior to giving our opinion on the financial statements and our value for money conclusion.
Whole of Government Accounts	September 2012	We are required to audit the whole of government accounts consolidation pack. Our work is performed following completion of the audit of the Council's financial statements.	Audit report provided September 2012	
VFM conclusion	January to March 2012	In 2011/12 auditors will again give their statutory Value for Money (VFM) conclusion on the arrangements to secure economy, efficiency and effectiveness based on two criteria	VFM conclusion September 2012. Findings to be reported in the Annual	Ongoing updates to be provided

Area of work	Timetable	Progress to date	Final report due/issued	Summary of findings/other comments
		<p>specified by the Commission, relating to a Council's arrangements for:</p> <ul style="list-style-type: none"> ■ securing financial resilience - focusing on whether the Council is managing its financial risks to secure a stable financial position; and ■ challenging how it secures economy, efficiency and effectiveness – focusing on whether the Council is prioritising its resources within tighter budgets and improving productivity and efficiency. <p>Our work will commence in February 2012.</p>	Audit Letter 2012	
Certification of grant claims and returns	July onwards	<p>In 2011/12 we anticipate being required to certify the following grant claims and returns:</p> <ul style="list-style-type: none"> ■ Housing and Council Tax Benefits Subsidy Claim; ■ National Non-Domestic Rates 	Various deadlines	We will liaise with staff to ensure work is completed to meet the specified deadlines.

Area of work	Timetable	Progress to date	Final report due/issued	Summary of findings/other comments
		Return; and <ul style="list-style-type: none"> ■ Disabled Facilities Grant Return (dependent on value of the return). 		

Appendix 3 - Contact details

52 If you would like further information on any items in this briefing, please feel free to contact either myself or Steve Golding, Audit Manager.

53 Alternatively, all Audit Commission reports - and a wealth of other material - can be found on our website: www.audit-commission.gov.uk.

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- any third party.



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