

Annual Audit Letter

South Cambridgeshire District Council

Audit 2010/11

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Traffic light explanation



Red ■ Amber ◆ Green ●

Key messages

This report summarises the findings from my 2010/11 audit. My audit comprises two elements:

- **the audit of your financial statements; and**
- **my assessment of your arrangements to achieve value for money in your use of resources.**

I have no recommendations to make in this report.

| Key audit risk | Our findings |
|---|---|
| Unqualified audit opinion |  |
| Proper arrangements to secure value for money |  |

Audit opinion and financial statements

- The changes arising from the introduction of International Financial Reporting Standards (IFRS) affected both the Council's preparation and my audit of the financial statements. The Council's IFRS implementation plan was on course until the increased workload arising from the implications of the Comprehensive Spending Review resulted in key plan and closedown quality deadlines not being met. In line with the national position this led to an increase in the number of errors within the financial statements presented for audit to 3 material and 16 non-trivial errors. These errors were mainly disclosure and presentational issues and did not impact on the usable reserves of the Council.
- I was also able to certify the Whole of Government Accounts (WGA) return by 30 September as required by the Code of Practice.

- The constructive response to the issues raised at audit meant that I was still able to issue an unqualified opinion and certificate on the financial statements on 30 September 2011. This compares well with the 38 bodies that did not receive an opinion and certificate by the due date.
- The documentation and working papers supporting the accounts were of a good standard.
- I did not identify any significant weaknesses in your internal control arrangements.

Value for money

- The Council's arrangements in both of the criteria are such that I issued an unqualified value for money conclusion stating that the Council had proper arrangements to secure economy, efficiency and effectiveness in your use of resources on 30 September 2011.

Grant certification

- I have completed my work on the certification of the Council's 2010/11 claims and two of the six claims were subject to minor amendment.

Current and future challenges

This is a period of challenge for the public sector. The following outline some of the key challenges that will be faced over the next few years.

Welfare reform

The Welfare Reform Bill was introduced in Parliament in February 2011. The Bill means significant changes to the welfare system. It provides for the introduction of a 'Universal Credit' to replace a range of existing means-tested benefits and tax credits for people of working age, starting from 2013. These include Housing Benefit and Council Tax Benefit, which are administered by councils. The Bill follows the November 2010 White Paper, 'Universal Credit: welfare that works', which set out the Coalition Government's proposals for reforming welfare to improve work incentives, simplify the benefits system and tackle administrative complexity.

Besides introducing Universal Credit and related measures, the Bill makes other significant changes to the benefits system. The changes that specifically affect councils include:

- restriction of Housing Benefit entitlement for social housing tenants whose accommodation is larger than they need;
- up-rating of Local Housing Allowance rates by the Consumer Price Index; and
- capping of the total amount of benefit that can be paid.

The Coalition Government has yet to confirm the detailed timescale over which the full move from the existing Housing Benefit and Council Tax Benefit systems to the Universal Credit would take place. However, it is clear that this will have significant operational and resource implications for the Council. This is identified as a key issue and is being actively monitored within the risk management system.

More recently the Coalition Government released a consultation paper on local support for council tax. This stated that council tax support would not form part of Universal Credit and would remain a local authority responsibility. The paper also set out the need for a 10 per cent cut in the existing level of support.

Housing Revenue Account (HRA) self financing

Under the existing housing subsidy system councils with housing stock are required to prepare a notional HRA. This uses a set of predetermined factors for items such as, maintenance costs and rental income to reflect the mix and age of the housing stock. In simple terms, if this notional account is in credit then the surplus is payable to central government and if in a deficit situation an equivalent payment is made to the council to support the housing landlord function. The Council's notional HRA is in credit and it was therefore required to make a contribution of some £11.7 million to Central Government in respect of their HRA in 2010/11.

The current year, 2011/12, is to be the last year of the existing system. Under a new financing system, councils will be responsible for financing of the HRA, and the existing system of grants and payments will end. To fund this Central Government will be making payments to certain local authorities and in the case of the Council and other local authorities that currently contribute to the scheme, transferring a debt liability. The debt liability transfer, in the region of £205 million prior to rebasing, is to take place on 28 March 2012. Therefore, instead of making a contribution to Central Government the Council will be funding the interest and principal charges on the debt transfer.

The Council has been working with Cambridge City Council, another net contributor to the system, regarding the logistics and financial implications of the change. The authorities have recently jointly procured the services of an external financial adviser to assist in this complex area. A key issue is how the £205 million plus debt transfer will be financed. Recent Coalition Government announcements have indicated that authorities with debt transfers will now be able to borrow at preferential rates from the Public Works Loans Board (PWLB) rather than via the Money Market by way of loans or bonds. It is expected that the availability of these lower rates will lead to the majority of councils funding their debt transfer via the PWLB.

Localism Act

This Act received Royal Assent on 15 November 2011. As well as allowing the Housing Revenue Account self financing proposals discussed earlier to proceed the Act has other far reaching implications for local authorities including:

- granting of a 'general power of competence', to provide councils with the legal power to do what is not specifically prohibited;
- new rights and powers for communities. These include:
 - 'community right of challenge' – would allow voluntary and community groups to express an interest in taking over and running local authority services;
 - 'community right to buy' – local authorities to hold a list of community value assets and if wish to dispose of community groups must be allowed time to put together bids and finance;
- planning system reforms including changes to the community infrastructure levy with a proportion going to neighbourhoods affected by the developments.

The full implementation of the provisions of the Act will have significant service provisions and hence budgetary implications for the Council.

Development of the area

In order to deliver its housing needs the Council is involved in a number of development initiatives to increase the provision of both private and social housing. Progress on a number of these developments slowed dramatically as a consequence of the economic downturn. However, more recently there has been good progress on the Cambridge fringe sites as well as Cambourne. The lack of certainty over the improvements to the A14 has proved detrimental to development within the area. Despite this, work is beginning to produce an updated planning application for Northstowe, although Cambridge East shows no sign of moving forward in the short term.

The Council is actively working with private and public sector partners to ensure that development continues in a structured manner, to an agreed strategy and in a sustainable way.

Economic downturn and pressure on the public sector

The economic downturn is placing increasing pressure on the public sector as a whole. This is reflected in the:

- challenging Comprehensive Spending Review settlement;
- increasing demand for key services; and
- reduced ability of members of the public to pay for services.

In addition to the general changes arising from the economic downturn, the financial implications arising from HRA self-financing and slow development progress there are other financial pressures on the Council. These include the:

- reduction in the supporting people grant funding; and
- increased level of pension costs arising from the triennial revaluation and changing assumptions regarding pensionable employees.

All of these issues are considered and fully reflected within the Medium Term Financial Strategy (MTFS). The Council has a good record of delivering within budget by a systematic budgetary control approach which the more consistent use of option appraisal has improved. Continuation of this soundly based financial approach is essential in the changing economic circumstances.

Financial statements and annual governance statement

The Council's financial statements and annual governance statement are an important means by which the Council accounts for its stewardship of public funds.

Overall conclusion from the audit

I issued an unqualified opinion and certificate on 30 September 2011.

The move to IFRS set all councils the difficult task of reviewing their past accounting policies and accounts and restating them in the format required by IFRS, as well as preparing the 2010/11 accounts in that format. The Council had an implementation plan which was on course until earlier this year. The increased workload arising from the implications of the Comprehensive Spending Review was a major contributor to the timetable not being met. In particular, the restatement of prior year accounts was not available for audit in advance of the 2010/11 closedown as originally agreed. This has meant that revised accounting approaches and detailed disclosure note formats could not be agreed in advance of the production of the financial statements and has increased the number of errors that are noted in this report. Nationally, there has been an increase in the number of errors identified in the financial statements presented for audit. As a result some 38 bodies did not receive an opinion and certificate by the due date.

The accounts submitted for audit contained 3 material errors, with 16 non-trivial errors. However, the majority of these errors related to disclosure and reporting and have not reduced the usable reserves of the Council.

The 3 material errors, which I set out in detail in my Annual Governance Report covered to the:

- application of the social housing factor and council dwelling depreciation calculation;;
- disclosure of the size of the social housing factor change;
- disclosure of future leasing commitments.

In assessing the quality of your financial statements I considered aspects of your accounting practices, accounting policies, accounting estimates and financial statements disclosures. The documentation and working papers supporting the accounts were of a good standard.

Due to the slippage in the closedown programme arising from the adverse impact of the Comprehensive Spending Review the normal quality review programme was not carried out. This led to an increase in the number of typographical, casting and consistency errors, both within the financial statements and between the financial statements and the explanatory foreword.

My Annual Governance Report made a number of recommendations to further improve the closedown procedures. These have been accepted by the Council and were incorporated within the Annual Governance Statement for 2010/11.

Whole of Government Accounts

I am also required to certify the council's WGA return by 30 September. This work was completed with certification and submission taking place on 30 September following adoption of the Council's accounts.

Significant weaknesses in internal control

I did not identify any significant weaknesses in your internal control arrangements.

Value for money

I considered whether the Council is managing and using its money, time and people to deliver value for money. I assessed your performance against the criteria specified by the Audit Commission and have reported the outcome as the value for money (VFM) conclusion.

I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against two criteria specified by the Audit Commission. My overall conclusion is that the Council has adequate arrangements to secure, economy, efficiency and effectiveness in its use of resources.

My conclusion on each of the two areas is set out below.

Value for money criteria and key messages

| Criterion | Key messages |
|--|---|
| <p>1. Financial resilience</p> <p>The organisation has proper arrangements in place to secure financial resilience.</p> <p>Focus for 2010/11:</p> <p>The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.</p> | <p>The leadership team understands the significant and rapidly changing financial management challenges and risks facing the organisation and is taking appropriate action to secure a stable financial position. Key to this assessment are the:</p> <ul style="list-style-type: none">■ regular financial briefings by the Executive Director Corporate Services, who is a member of the senior management team (SMT), to Cabinet;■ MTFS, which was updated prior to the full settlement announcement, includes an analysis of the impact of the recession and covers a 5 year business plan;■ use of option appraisal approach to spending/operational change decisions which link into budget revisions and MTFS;■ linkages in the MTFS and budget to strategic objectives; and■ detailed scrutiny of financial proposals, budget and accounts via Portfolio Holders' meetings, Corporate Governance Committee, Scrutiny and Overview Committee and full Council. |

Criterion

Key messages

To support effective financial management the Council has a:

- varied financial training programme in place for both members and staff;
- Audit committee function, as carried out by the Corporate Governance Committee, which continues to be adequately discharged;
- Treasury Management Strategy which sets out a balance between security, liquidity and yield. This is regularly monitored and the Council are performing well against pre set benchmarks;
- improved analysis of the impact of financial changes on operational performance;
- approach to financial modelling that has taken account of such issues as:
 - Future levels of grant;
 - Changes in concessionary fares funding and responsibility;
 - HRA self financing; and
 - Opportunities for joint working.
- identification of a target level for reserves with a track record of achievement; and
- active monitoring of income sources and recovery of debts.

The Council has a track record of delivering within budget despite the changing financial pressures of recent years.

2. Securing economy efficiency and effectiveness

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

Focus for 2010/11:

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

The revised option appraisal approach to decision making ensures that both financial and performance issues are now considered together. It has also supported the consideration of a wider range of approaches to service provision.

The Council has adopted a number of approaches to public consultation. More recently this has covered the implications of the spending cut requirements. The Council did get to consultation stage with tenants regarding the possibility of a transfer of the housing stock to a registered social landlord, although tenants chose not to make that move.

Clear recognition of the benefits that partnership working can make. Significant initiatives with registered social landlords in respect of housing including shared waiting list.

More recently the options for shared services and joint working are now being considered, although looking to ensure that the maximum benefit accrues to the Council. Decided not to pursue joint Housing Benefits option with another Council as considered that the majority of savings could be achieved in-house, as has occurred. Currently, working with Cambridge City in respect of the implications of and approach to HRA self financing.

The Council is also one of the 11 Total Assets Pathfinder areas as part of the Department for Communities and Local Government's (CLG) Total Place Initiative. Making Assets Count (MAC) is undertaking an asset mapping exercise of all the public sector assets within Cambridgeshire covering local government, health, police, fire and central government. South Cambridgeshire Hall is the only non housing asset that the Council has. For the Council MAC is an opportunity to ensure full use of this asset and access to other public sector facilities within the district area.

The service planning process requires SMT to quantify and rank in priority order future spending pressures. The integration of the option appraisal approach means that as part of the consideration of the spending pressures the potential risks to service provision are recognised. The budget process identifies bids for funding to realise efficiencies or meet changing legislation.

Following my qualification of the VFM conclusion in respect of the use of natural resources last year, the Council has made a number of changes to their approach which has improved the use and the monitoring of the use of natural resources. These changes address the issues that led to the qualification.

Grant Certification

As the Council's auditor, I am required to certify the Council's claims and returns.

I carry out this work on the following basis:

- Claims below £125,000 are not subject to certification.
- Claims between £125,000 and £500,000 are subjected to a reduced, light-touch certification.
- Claims over £500,000 are subjected to a certification approach relevant to the auditor's assessment of the control environment and management preparation of claims. A robust control environment leads to a reduced certification approach for these claims.

I am required to certify a total of six claims in relation to 2010/11. A summary of the claims, their value and the respective certification fee is set out in Appendix 2. All claims have been certified and submitted.

Minor amendments were made to two claims. This continues the previously reported improvement in grant preparation and despite the additional requirements of the Housing finance base data return resulted in a 7% reduction in the claims fee reported in Appendix 2.

Closing remarks

I have discussed and agreed this letter with the Chief Executive and the Executive Director, Corporate Services. Copies of the letter will be made available to Members by the 30 November deadline. I will present this letter at the Corporate Governance Committee meeting on 16 December 2011.

Further detailed findings, conclusions and recommendations in the areas covered by my audit are included in the Annual Governance Report issued to the Council in September 2011.

The Council has taken a positive and constructive approach to all aspects of my audit. I wish to thank the Council staff for their support and co-operation during the audit.

Paul King
District Auditor

November 2011

Appendix 1 - Fees

The table below sets out the audit fee. The original audit fee proposed in my audit fee letter dated 19 March 2010 was £132,000. This was reduced when I submitted my Audit Opinion Plan to reflect the improvement in final accounts closedown in 2009/10 and the introduction of the protocol with Internal Audit. In addition, the Audit Commission as regulator, made two rebates during the year totalling £9,116 (7.6% of audit fee).

| | Actual fee (£) | Audit Opinion Plan fee (£) | Variance (£) |
|--------------|----------------|----------------------------|--------------|
| Audit fee | 120,000 | 120,000 | nil |
| Total | 120,000 | 120,000 | nil |

Appendix 2 - Summary of 2010/11 claims

| Claim or return | Value of claim/return (£) | 2009/10 fee (£)** | 2010/11 fee (£) |
|--|---------------------------|-------------------|-----------------|
| BEN01: Housing and council tax benefits | 30,212,123 | 22,800 | 20,563 |
| CFB06 Pooling of housing capital receipts | 851,337 | 1,463 | 1,890 |
| HOU01 Housing subsidies and grants | -11,675,134 | 1,999 | 2,009 |
| HOU02 Housing finance base data return# | N/A | 3,780 | 4,982 |
| HOU21 Disabled facilities grant | 244,000 | 1,165 | 471 |
| LA01 National non-domestic rates | 56,893,122 | 5,747 | 4,459 |
| Total | n/a | 36,954 | 34,374 |

Significant changes to claim in 2010/11 to provide DCLG with additional information to support transition to HRA self financing.

** Pro rata allocation of grant supervision

Appendix 3 - Glossary

Annual governance statement

Governance is about how a Council ensures that it is doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner. It comprises the systems and processes, cultures and values, by which the Council is directed and controlled and through which it accounts to, engages with and where appropriate, leads its community.

The annual governance statement is a public report by the Council on the extent to which it complies with its own governance code, including how it has monitored the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.

Audit closure certificate

A certificate that I have completed the audit following statutory requirements. This marks the point when I have completed my responsibilities for the audit of the period covered by the financial statements.

Audit opinion

On completion of the audit of the financial statements, I must give my opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Opinion

If I agree that the financial statements give a true and fair view, I issue an unqualified opinion. I issue a qualified opinion if:

- I find the statements do not give a true and fair view; or
- I cannot confirm that the statements give a true and fair view.

Materiality and significance

The Auditing Practices Board (APB) defines this concept as ‘an expression of the relative significance or importance of a particular matter for the financial statements as a whole. A matter is material if its omission would reasonably influence users of the financial statements, such as the addressees of the auditor’s report; also a misstatement is material if it would have a similar influence. Materiality may also be considered for any individual primary statement within the financial statements or of individual items included in them. We cannot define materiality mathematically, as it has both numerical and non-numerical aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

‘Significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

Weaknesses in internal control

A weakness in internal control exists when:

- a control is designed, set up or used in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements quickly; or
- a control necessary to prevent, or detect and correct, misstatements in the financial statements quickly is missing.

An important weakness in internal control is a weakness, or a combination of weaknesses that, in my professional judgement, are important enough that I should report them to you.

Value for money conclusion

The auditor’s conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources based on criteria specified by the Audit Commission.

The Code of Audit Practice defines proper arrangements as corporate performance management and financial management arrangements that form a key part of the system of internal control. These comprise the arrangements for:

- planning finances effectively to deliver strategic priorities and secure sound financial health;
- having a sound understanding of costs and performance and achieving efficiencies in activities;
- reliable and timely financial reporting that meets the needs of internal users, stakeholders and local people;
- commissioning and buying quality services and supplies that are tailored to local needs and deliver sustainable outcomes and value for money;
- producing relevant and reliable data and information to support decision making and manage performance;

- promoting and displaying the principles and values of good governance;
- managing risks and maintaining a sound system of internal control;
- making effective use of natural resources;
- managing assets effectively to help deliver strategic priorities and service needs; and
- planning, organising and developing the workforce effectively to support the achievement of strategic priorities.

If I find that the audited body had adequate arrangements, I issue an unqualified conclusion. If I find that it did not, I issue a qualified opinion.

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