

# **Governance**

# **Committee**

# **update**

**Dover District 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.**

# Contents

<b>Introduction .....</b>	<b>2</b>
<b>Progress report .....</b>	<b>3</b>
Financial statements.....	3
VFM conclusion .....	3
Other areas of work – grant certification .....	4
<b>Government response to consultation on the future of local public audit...5</b>	<b>5</b>
<b>Update on the externalisation of the Audit Practice.....</b>	<b>7</b>
<b>Other matters of interest .....</b>	<b>8</b>
2010/11 Accounts .....	8
Managing Workforce Costs .....	9
CIPFA's Prudential Code for Capital Finance.....	10
2011/12 Accounts: CIPFA Guidance Notes for Practitioners.....	10
Guide to HRA Self Financing.....	11
For information: Board Governance Essentials .....	11
Local Government Finance Bill.....	11
Key considerations .....	12
<b>Contact details .....</b>	<b>13</b>

# Introduction

**1** The purpose of this paper is to provide the Governance 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 Governance Committee. The paper concludes by asking several questions which the Committee may wish to consider to assess whether it has received enough assurance on emerging issues.

**3** If you require any extra information on 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.

**4** Finally, please also remember to visit our website ([www.audit-commission.gov.uk](http://www.audit-commission.gov.uk)) which now enables you to sign-up to be notified of any new content that is relevant to your type of organisation.

Darren Wells

District Auditor

10 February 2012

# Progress report

## Financial statements

**5** We will complete our work on your 2011/12 financial statements in three key stages:

- February 2012 – detailed accounts planning and review of key financial systems;
- March 2012 - cyclical controls testing and early substantive testing; and
- August –September 2012 - year-end audit work.

**6** In addition we will review your Whole of Government Accounts return in September 2012.

**7** We are currently completing our detailed accounts planning and the first stage of our final accounts audit, during which we update our financial systems documentation and complete our walk through testing. This testing will confirm whether we are able to place reliance on key controls at the Council for opinion purposes.

## VFM conclusion

**8** We assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against two criteria specified by the Audit Commission:

- Financial resilience: The organisation has proper arrangements in place to secure financial resilience.
- Securing economy efficiency and effectiveness: The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

**9** We will complete our work on the VFM conclusion in three key stages:

- February 2012 – VFM opinion planning;
- March – August 2012 – initial assessment and follow-up of any specific risks identified; and
- September 2012 - completion and reporting of VFM conclusion.

**10** The specific risks we have identified for the financial statements audit and VFM conclusion are reported in my opinion plan, which is a separate paper on today's agenda. I will report the results of my audits to the Audit Committee in my annual governance report in September 2012.

## Other areas of work – grant certification

**11** During 2011/12 we will complete grant certification work, as specified by the Audit Commission. I expect the number of grants requiring audit to be broadly the same as in 2010/11.

**12** We will report the results of our grant certification work in our annual grant certification report. Our 2010/11 report is included as a separate item on today's agenda.

# Government response to consultation on the future of local public audit

**13** 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.

**14** 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.

**15** 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.

**16** The government is holding further discussions with audited bodies and audit firms to develop its proposals. The government intends to publish draft legislation for pre-legislative scrutiny in Spring 2012.



# Update on the externalisation of the Audit Practice

**17** 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.

**18** 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.
- 13 potential providers were invited to tender following the initial pre-qualification stage. The deadline for return of the tenders was 16 December 2011. The Commission plans to announce the successful tenderers in March 2012.
- The Commission is planning to set out, early in 2012, the consultation process 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.

**19** Further details are available on the Commission's website. We will continue to keep you updated on developments.

**20** 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; and
- Managing a smooth transition from the Audit Practice to your new audit provider.

# Other matters of interest

## 2010/11 Accounts

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

**22** 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 audited bodies for 2011/12.

**23** 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.

**24** 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.

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

**26** 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.

**27** 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.

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

## Managing Workforce Costs

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

**30** 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.

**31** 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.

**32** 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.

**33** 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.

**34** The report is supplemented with a briefing for elected members, which 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 affect services and communities.

**35** 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**

**36** 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.

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

**38** 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.

**39** 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.

**40** 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.

**41** The prudential indicators required by the Code should be considered alongside its Treasury Management performance indicators. These indicators 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**

**42** 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.

**43** The key changes to your financial statements in 2011/12 are also covered by our final accounts workshops, which your officers are attending in February 2012.

## Guide to HRA Self Financing

**44** 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. 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.

## For information: Board Governance Essentials

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

This guide may provide interesting reading for 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.

## Key considerations

49 The Governance 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?
- Is the Governance Committee satisfied that the questions within the Audit Commission / Local Government Association joint report on managing workforce costs briefing have been properly considered by the Council and that appropriate use has been made of the supporting materials?
- 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?
- Has the Council reviewed CIPFA's guidance on HRA self-financing and made satisfactory progress for its implementation?

## Contact details

**50** If you would like further information on any items in this briefing, please feel free to contact either your District Auditor or Audit Manager.

**51** Alternatively, all Audit Commission reports - and a wealth of other material - can be found on our website: [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk).

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