

# Annual governance report

Nottingham City Council

Audit 2011/12



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# Key messages

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**This report summarises the findings from the 2011/12 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.**

## Financial statements

As at 7 September 2012 I expect to issue an unqualified audit opinion.

My audit found one material error and five non-material errors which management have amended for in the Council's revised financial statements. There are no non-trivial errors or uncertainties that management have declined to amend for. A small number of minor errors have been reported directly to management during the course of the audit.

The Council produced its unaudited 2011/12 financial statements to a high standard and supported these with good working papers. Responses to queries and requests for information during the course of the audit were prompt and timely. Following production of financial statements under IFRS requirements for the first time in 2010/11, the Council

## Value for money (VFM)

I expect to issue an unqualified VFM conclusion.

My audit found that the Council has well established arrangements for securing financial resilience. However, the authority faces a substantial future resource gap (£24m) from 2013/14 which will require continuing action to address.

The Council also has arrangements in place to secure economy, efficiency and effectiveness in the use of resources. My follow-up work this year of my 2010/11 Future Jobs Fund report confirmed that the Council had taken action in response to my report recommendations.

## Certificate

As I have not yet issued my Whole of Government Accounts (WGA) review report, I am not able to certify completion of the 2011/12 audit.

I expect to complete the remaining WGA work and report my findings to management by 5 October 2012. I plan to issue my certificate by 5 October 2012.

# Before I give my opinion and conclusion

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**My report includes only matters of governance interest that have come to my attention in performing my audit. I have not designed my audit to identify all matters that might be relevant to you.**

## **Independence**

I confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) - Integrity, Objectivity and Independence.

I am not aware of any relationships that may affect the independence and objectivity of the Audit Commission, the audit team or me, that I am required by auditing and ethical standards to report to you.

The Audit Commission's Audit Practice has not undertaken any non-audit work for the Authority during 2010/12.

## **I ask the Audit Committee to:**

- take note of the adjustments to the financial statements included in this report (appendix 2); and
- approve the letter of representation (appendix 3), on behalf of the Authority before I issue my opinion and conclusion.

# Financial statements

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**The Authority's financial statements and annual governance statement are important means by which the Authority accounts for its stewardship of public funds. As elected Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.**

## **Opinion on the financial statements**

Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the financial statements. Appendix 1 contains a copy of my draft audit report.

## **Uncorrected errors**

My audit has not identified any errors other than those which management have agreed to amend for in a revised set of financial statements.

## **Corrected errors**

My audit identified one material misstatement related to the cessation of the existing tram PFI scheme (NET 1) that management has amended for. I also found other non-material misstatements linked to my work on PFI and LIFT schemes, heritage assets and Icelandic investments.

Appendix 2 contains details of these corrected errors and uncertainties.

I have also identified some disclosure issues within the notes to the accounts that management have amended for. Where these are significant I have made reference to them in the detail below.

### **PFI scheme cessation - Nottingham Express Transit (NET) phase 1**

On 15th December 2011, the Council purchased shares in the special purpose consortium company Arrow Light Rail Limited (ALRL) which then became a wholly owned subsidiary of the Council. The purpose of the acquisition was to terminate the PFI contract in place with Nottingham Tram Consortium to operate the existing tram network. Another consortium (Tramlink Nottingham) was awarded a new PFI contract in December 2011 to design, build and operate an extended tram network in Nottingham.

The accounting transactions for the cessation of this PFI scheme are complex. Reasons for this include:

- contract termination being effected by share purchase of the company operating the scheme rather than a termination payment; and
- cessation of the scheme being linked to the award of a new concession and associated PFI contract.

I have worked closely with the Council during 2011/12 as it developed its accounting proposals ahead of the contract termination in December 2011. I also carried out a detailed review of the accounting transactions in the Council's 2011/12 financial statements linked to the cessation of this scheme. I still have a few outstanding queries and will update members on progress at the audit committee.

#### *Financial impairment of investment in ALRL*

My review found that the Council valued its short term investment in ALRL in its 31 March 2012 balance sheet at cost (£32.3m). IAS 36 (impairment of assets) requires investments in subsidiary companies to be valued at fair value rather than cost. I estimated the fair value of the Council's investment in ALRL at £1.4m and concluded that the value of the Council's investment had been impaired. As no impairment of the ALRL investment was recognised in the Council's 2011/12 financial statements, I concluded that the valuation was materially overstated by £30.9m.

I found two other non-material, non-trivial errors affecting the valuation of trams and the calculation of the PFI scheme lease liability.

#### *Valuation of trams*

The Council purchased 15 trams owned by ALRL for £18m prior to acquiring its 100% shareholding in the company on 15 December 2011. My audit found these vehicles were valued at £26.1m using the IAS 17 (leases) valuation basis used in previous years. On purchasing the trams, the Council de-recognised the purchase cost of the vehicles rather than their IAS 17 value thus overstating their value by £8.1m. The Code of Practice requires initial recognition of the purchased vehicles to be at cost.

#### *PFI scheme lease liability*

My detailed testing found that the Council's PFI liability and subsequent write-off on cessation of the scheme was overstated by £5.5m. This is due to incorrect assumptions being used when estimating the PFI interest payments for 2011/12.

#### *Disclosure requirements for ALRL*

My review found that the disclosures in the notes to the group accounts for ALRL did not meet the requirements of IFRS 3 (Business Combinations including acquisitions of subsidiaries). Additional disclosures including the fair value of the cost of acquisition and termination of the PFI contract are needed to satisfy the requirements.

## **Heritage assets**

I found one non-material, non-trivial error affecting the valuation of heritage assets at 31 March 2010 and subsequent year ends too. The valuation at 31 March 2010 was calculated using a previous one which was uplifted for inflation. An inappropriate RPI rate was used for this calculation.

## **Bulwell Riverside Joint Service Centre (LIFT)**

I performed procedures to satisfy myself that your financial statements are materially stated in respect of your disclosure for the Bulwell Joint Service Centre LIFT scheme.

In preparing its 2010/11 financial statements, the Council assessed the arrangements for this LIFT scheme concluding that the accounting requirements of IFRIC 12 (service concession arrangements) applies. As the centre was not yet operational, the accounting disclosures made in 2010/11 were limited.

For 2011/12, the requirements of IFRIC 12 apply in full as the centre became operational from January 2012. My audit included a detailed review of both the initial asset (property) and liability (the present value of future lease payments) values determined at the financial close of the scheme. I found that the Council had overstated the initial value of both its asset and liability by £1.4m.

I still have a few outstanding queries in relation to the LIFT scheme and will update members at the audit committee.

## **LIFT and PFI disclosure**

My review of remaining PFI contract payments at 31 March 2012 (table 6.5.11(a)) found that the actual basis of disclosure (including inflation) was inconsistent with the basis stated in the note (excluding inflation). In response, the Council has reworked its contract payment estimates to exclude inflation leading to a £45m reduction in the value of total contract payments disclosed. This reduction is material.

## **Financial instrument disclosures**

My testing found one material and three non-material non-trivial disclosure errors:

- Table 6.2.16 (b) Financial liabilities: materially overstated by £38.5m as creditors include receipts in advance. These do not meet the definition of a financial liability per IAS 32 (financial instruments: disclosure) and should be excluded.
- Table 6.2.16 (a) Financial assets: overstated by £2.7m as short term debtors value includes prepayments. These do not meet the definition of a financial asset per IAS 32 and should be excluded;
- Table 6.2.16 (d) Financial instruments – fair value: fair value of PWLB at 31 March 2012 understated by £8.1m due to omission of accrued interest;
- Table 6.2.16 (b) Financial liabilities: current other long term liabilities – PFI and finance lease liabilities at 31 March 2012 overstated by £2.3m. Liability double counted as also included within the value for creditors – financial liabilities at amortised cost at 31 March 2012;

None of these errors affect the core financial statements.



## **Operating lease disclosures**

My review of operating leases granted by the Council (table 6.5.10(h)) found that the total value of future minimum lease payments was materially overstated. The Council had included in error £53m of finance lease payments in addition to the operating lease payments.

## **Icelandic investments**

I performed procedures to satisfy myself that your financial statements are materially stated in respect of recognising and measuring the recoverable amount from your investment in Icelandic banks.

My review found that the Council followed CIPFA guidance (LAAP bulletin 82) to estimate the impairment in value for its deposits held with Icelandic banks. Although the Council's impairment calculation followed the latest update to the bulletin (number 6) issued in May 2012, it did not take into account a late revision to the update issued in June 2012. This specific revision provided further guidance on estimating the impairment for deposits held with Landsbanki bank.

In response, the Council has recalculated its estimate taking into account this further guidance. The outcome of this is that its impairment estimate is overstated by £428k. In addition, the guidance revises assumptions made about the timing of repayments from Landsbanki bank such that £1.4m of deposits classified as long-term investments become short-term investments.

## **Significant risks and other specific risks - my findings**

I reported to you in my March 2012 Audit Plan the significant risks that I identified relevant to my audit of your financial statements. In Table 1 I report to you my findings against each of these risks.

Table 1: Risks and findings

Risk	Finding
<p><b>Significant risks</b></p> <p><b>Nottingham Express Transit (NET) phase 2</b></p> <p>In December 2011 the Council entered into a major new PFI scheme when it awarded a concession to Tramlink Nottingham for the NET phase 2 extension. As this also included operation of the current tram network, the existing PFI concession with Arrow Light Rail Limited ceased at the same time.</p> <p>Early cessation of an existing PFI scheme linked to the inception of a new one involved a number of complex financial transactions and disclosures in the Council's financial statements. The Council sought external advice on these matters.</p> <p>Risk of material error in the financial statements due to large, complex accounting transactions and disclosures for both the existing and new NET PFI schemes.</p>	<p>I carried out specific reviews of the Council's proposed accounting treatment and associated accounting advice sought by the authority covering the:</p> <ul style="list-style-type: none"> <li>■ termination of the existing scheme (NET phase 1);</li> <li>■ exit of Nottinghamshire County Council from the existing scheme; and</li> <li>■ new phase 2 concession and PFI scheme (2011/12 transactions only).</li> </ul> <p>My testing identified one material and two non-material, non-trivial errors and a need for additional disclosures which have been referred to previously within the 'Corrected errors' section of my report.</p>
<p><b>Heritage Assets</b></p> <p>The 2011/12 Code adopts the requirements of FRS 30 Heritage Assets.</p> <p>The Council carried out an exercise during the year to identify and review heritage assets using criteria set out in FRS 30. It also determined its proposed accounting treatment and disclosures for these assets.</p> <p>However, there remained a risk that the Council may not comply fully with the accounting and disclosure requirements of FRS 30 leading to a material accounting or disclosure error in the financial statements.</p>	<p>I carried out an on-going review of the Council's exercise to identify heritage assets and its associated proposed accounting treatment and disclosures. I am pleased to note that your assessment was comprehensive and I concluded that your proposals were sound.</p> <p>I performed detailed tests to satisfy myself that you have recognised, valued and disclosed material heritage assets in your financial statements.</p> <p>My testing has not identified any significant issues to bring to your attention other than the non-material error referred to previously within the 'Corrected errors' section of my report.</p>

## Risk

### HRA reform

The government reformed local authority housing finance by adopting a self-financing model from 1 April 2012. This included a one-off settlement payment from central government in March 2012 to adjust the HRA debt of the authority.

Risk of material misstatement due to the complexity, magnitude and timing of the HRA reform.

### Other specific risks

#### Accounts payable

I stated in my 2010/11 annual governance report that controls in this area remained weak following the introduction of new accounts payable arrangements in August 2009.

Extra audit testing was required to provide me with sufficient assurance over expenditure to inform my 2010/11 opinion.

Steps were taken by the Council to address these weaknesses.

Risk that action taken during 2011/12 being insufficient and lead to a material error arising in the financial statements.

#### Payroll

I stated in my 2010/11 annual governance report that the Council did not maintain an up to date establishment list.

Lack of any establishment related checks increases the risk of material error in payroll costs within the financial statements.

Last year, this weakness made it more difficult to obtain

## Finding

I have evaluated management's oversight of HRA reforms and the transactions required by the Authority. I have agreed the detail on the settlement payment or receipt to the DCLG notification.

My testing has not identified any significant issues to bring to your attention.

I evaluated the design and implementation of controls over the Council's accounts payable system. I found that controls in this area had improved significantly during 2011/12. Actions taken to address weaknesses included reducing a significant backlog for processing payments and the introduction of a new invoice imaging system.

My review of controls provided some assurance over expenditure. However, this was not sufficient for the purposes of my opinion. As last year, I performed extensive substantive testing of expenditure transactions during the year to provide sufficient assurance that expenditure within the financial statements is accurate and correctly treated.

Looking ahead, the move to a new accounting system (Oracle) in 2012/13 provided by East Midlands Shared Services (EMSS) is expected to address in full all accounts payable related control weaknesses.

My testing has not identified any significant issues to bring to your attention.

I evaluated the design of controls over the Council's payroll system which provided me with continuing assurance in this area. As in 2010/11, my review found that the Council had no up to date establishment list this year.

However, work was carried out by the Council in 2011/12 to validate its payroll before transfer to EMSS in 2012/13. This exercise included a comprehensive check on the existence of all Council staff on the payroll by service area.

Risk	Finding
<p>assurance that payroll costs were complete and accurate.</p>	<p>My review of this exercise provided sufficient assurance to confirm the existence of staff listed on the Council's payroll. Looking ahead, the move to new payroll and HR systems in 2012/13 provided by EMSS is expected to address this weakness.</p> <p>My testing has not identified any significant issues to bring to your attention.</p>
<p><b>De-recognition of Property, Plant and Equipment</b></p> <p>I concluded in my 2010/11 annual governance report that the Council had insufficient information to allow de-recognised amounts to be calculated accurately.</p> <p>During 2011/12, the Council has developed a method to calculate de-recognised amounts that collects the extra information required.</p> <p>Action taken during 2011/12 may be insufficient leading to risk of material estimation uncertainty and error linked to de-recognition of components.</p>	<p>I carried out an on-going review of the Council's method for calculating de-recognised amounts between October 2011 and January 2012.</p> <p>My review found that the Council had developed a comprehensive method to collect the required information and produce a robust de-recognition estimate for 2011/12.</p> <p>I performed detailed tests to satisfy myself that you have correctly valued and accounted for de-recognised components in your 2011/12 financial statements.</p> <p>My work involved checking a number of replaced or restored components (assets) on a sample basis.</p> <p>My testing has not identified any significant issues to bring to your attention.</p>
<p><b>HRA – valuation</b></p> <p>The value of the Council's housing stock may be materially misstated if the Council does not comply fully with the CIPFA Code of Practice and the Housing Revenue Account (Accounting Practices) Direction 2011 when preparing HRA asset valuations.</p>	<p>I have evaluated management's oversight of the valuation of housing stock, including arrangements for instructing a valuer and management controls over information provided to valuer. I have performed detailed tests of valuations to satisfy myself that financial statements are materially stated in respect of the valuation of the Authority's housing stock.</p> <p>My testing has not identified any significant issues to bring to your attention.</p>

## Significant weaknesses in internal control

It is the responsibility of the Authority to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. My responsibility as your auditor is to consider whether the Authority has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

I have tested the controls of the Authority only to the extent necessary for me to complete my audit. I am not expressing an opinion on the overall effectiveness of internal control. I have reviewed the Annual Governance Statement and can confirm that:

- it complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
- it is consistent with other information that I am aware of from my audit of the financial statements.

I identified no weaknesses in internal control during the audit that are relevant to preparing the financial statements other than those already referred to in table 1 above.

## Other matters

I am required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Authority's financial reporting process including the following.

- Qualitative aspects of your accounting practices
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions.
- Other audit matters of governance interest

Other matters that I wish to report are set out in the following table.

Table 2: **Other matters**

Issue	Finding
<b>Related party transactions – note 6.5.8</b>	<p>I have previously reported to you my concerns about members' responses to requests for confirmation of related party transactions. In my view this represented an important weakness in control since the effectiveness of the Council's process was limited due to the lack of a 100% response rate. My 2010/11 annual governance report noted that 26% of questionnaires remained outstanding following officer action to encourage responses.</p> <p>I am pleased to report this year that a near 100% response rate has been achieved for both members and officers. This reflects the substantial effort made by officers to facilitate responses including the use of e-mail returns.</p> <p>The Council was unable to obtain responses from four officers whose employment ceased during the year. From 2012/13, the Council plans to update its process such</p>

Issue	Finding
	<p>that responses are obtained prior to officers leaving Council employment.</p> <p>Looking ahead, the Council should maintain this level such that 100% response rates are achieved in future years.</p>
<p><b>Exit packages – note 6.5.5</b></p>	<p>The Code of Practice introduced a requirement for the first time in 2011/12 to report summary information about exit packages. Table 6.5.5 (c) includes aggregated cost figures for exit packages analysed in payment bands.</p> <p>My review of this note found that the cost figures had been compiled based on payments made during 2011/12. This is inconsistent with the Code of Practice which requires disclosure of the value of exit packages agreed during the year. The Council is aware of this requirement but was unable to meet it due to insufficient information. From 2012/13, the Council plans to collect additional information so that it can meet this requirement.</p>
<p><b>Property, plant and equipment – note 6.2.1</b></p>	<p>My audit work included checks to confirm the existence of property, plant and equipment.</p> <p>I found that records for a specific group of infrastructure assets were incomplete. These were transferred to the authority from Nottinghamshire County Council in 2001 and related to highways work. The limited information available restricted the extent of my verification work.</p> <p>The Council has agreed to review these ‘transferred from County Council’ assets during 2012/13 to confirm whether the assets are separately identifiable and still exist. The total net book value of these assets at 31 March 2012 is £6m.</p>

## Whole of Government Accounts

Alongside my work on the financial statements, I also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. As at 7 September 2012 I have not completed the procedures specified by the NAO. I expect to complete my report by the deadline set by the NAO for this work (5 October 2012).

# Value for money

**I am required to conclude whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is the value for money conclusion.**

I assess your arrangements against the two criteria specified by the Commission. In my March 2012 Audit Plan I reported to you the significant risks that were relevant to my conclusion. I have set out below my conclusion on the two criteria, including the findings of my work addressing the significant risk that I identified.

I intend to issue an unqualified conclusion stating that the Authority has proper arrangements to secure economy, efficiency and effectiveness in the use of its resources. I include my draft conclusion in Appendix 1.

Table 3: **Value for money conclusion criteria and my findings**

Criteria	Findings
<p><b>1. Financial resilience</b></p> <p>The organisation has proper arrangements in place to secure financial resilience.</p> <p>Focus for 2011/12:</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 Council has well established arrangements for securing financial resilience and has a good track record of managing financial pressures.</p> <p>My assessment has been informed through an assurance based review of financial resilience and on-going monitoring of the Council's financial position and plans.</p> <p><b>Financial performance</b></p> <p>The Council met its general fund revenue budget in 2011/12 reporting a £215k under spend for its corporate year-end outturn (pre-audit).</p> <p>Management took timely and effective action in response to significant forecast overspends early in 2011/12. This reversed a potential £6.2m forecast overspend at the end of period 3 with much of the reversal occurring between July 2011 and January 2012.</p> <p>Pressures and overspends on demand led budgets (Adult Support and Health) were managed in 2011/12. In my view these remain risk areas for 2012/13 and future years.</p>

Criteria	Findings
	<p><b>Financial position</b></p> <p>Looking ahead, the Council has an up to date medium-term financial plan for the next three financial years (2012/15). This includes a balanced revenue budget for 2012/13. Beyond then, the Council faces a substantial £24m gap in resources to fund its revenue spending over the 2012/15 period. Continuing action will be required by the authority to mitigate this future risk.</p> <p><b>Conclusion – criterion met.</b></p>
<p><b>2. Securing economy efficiency and effectiveness</b></p> <p>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p> <p>Focus for 2011/12:</p> <p>The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.</p>	<p>The Council has arrangements in place for securing economy, efficiency and effectiveness.</p> <p>My assessment has been informed through both an assurance based review and consideration of the VFM profiles for 2010/11 published by the Audit Commission. I used the profiles to consider the performance of the Council relative to its ‘nearest statistical neighbours’ across a number of different indicators.</p> <p>I also considered one significant risk related to financial governance and used my findings to inform this assessment (see below).</p> <p><b>Conclusion – criterion met.</b></p>

In my March 2012 Audit Plan I reported to you the significant risks that were relevant to my conclusion. I have set out below the findings of my work addressing each of the risks I identified.

Table 4: **Significant risks**

Risk	Finding	Impact on VFM conclusion
<p><b>Financial governance</b></p> <p>Non-compliance with standing orders on procurement linked to grants.</p>	<p>I reviewed the follow-up action taken by the Council in response to the findings and recommendations in my 2010/11 Future Jobs Fund report.</p> <p>My review has not identified any significant issues to bring to your attention.</p>	<p>Supports ‘criterion met’ assessment for the ‘securing economy, efficiency and effectiveness’ criterion.</p>



# Fees

## I reported my planned audit fee in the March 2012 Audit Plan.

I will complete the audit within the planned fee.

Table 5: Fees

	Planned fee 2011/12 (£)	Expected fee 2011/12 (£)
Audit	£380,700	£380,700
Claims and returns	£64,200	£64,200
Non-audit work	£nil	£nil
<b>Total</b>	<b>£444,900</b>	<b>£444,900</b>

# Appendix 1 – Draft independent auditor’s report

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## **Opinion on the financial statements**

I have audited the financial statements of Nottingham City Council for the year ended 31 March 2012 under the Audit Commission Act 1998. The financial statements comprise the Authority and Group Movement in Reserves Statement, the Authority and Group Comprehensive Income and Expenditure Statement, the Authority and Group Balance Sheet, the Authority and Group Cash Flow Statement, the Housing Revenue Account Income and Expenditure Account, the Movement on the Housing Revenue Account Statement and Collection Fund Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Nottingham City Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

## **Respective responsibilities of the Chief Financial Officer and auditor**

As explained more fully in the Statement of the Chief Financial Officer’s Responsibilities, the Chief Financial Officer is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. My 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 me to comply with the Auditing Practices Board’s Ethical Standards for Auditors.

## **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Financial Officer; and the overall presentation of the financial statements. In

addition, I read all the financial and non-financial information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

### **Opinion on financial statements**

In my opinion the financial statements:

- give a true and fair view of the financial position of Nottingham City Council as at 31 March 2012 and of its expenditure and income for the year then ended;
- give a true and fair view of the financial position of the Group as at 31 March 2012 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

### **Opinion on other matters**

In my opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which I report by exception**

I report to you if:

- in my opinion the annual governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007;
- I issue a report in the public interest under section 8 of the Audit Commission Act 1998;
- I designate under section 11 of the Audit Commission Act 1998 any recommendation as one that requires the Authority to consider it at a public meeting and to decide what action to take in response; or
- I exercise any other special powers of the auditor under the Audit Commission Act 1998.

I have nothing to report in these respects.

## **Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources**

### **Respective responsibilities of the Authority and the auditor**

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

### **Basis of conclusion**

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2011, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

### **Conclusion**

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2011, I am satisfied that, in all significant respects, Nottingham City Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

### **Delay in certification of completion of the audit**

I cannot formally conclude the audit and issue an audit certificate until I have completed the work necessary to issue my assurance statement in respect of the authority's Whole of Government Accounts consolidation pack. I am satisfied that this work does not have a material effect on the financial statements or on my value for money conclusion.

Sue Sunderland  
Officer of the Audit Commission

Westthorpe Business Innovation Centre  
Westthorpe Fields Road  
Killamarsh  
Sheffield  
S21 1TZ

25 September 2012

# Appendix 2 – Corrected errors

I identified the following errors during the audit which management have addressed in the revised financial statements.

Item of account	Nature of error	Comprehensive income and expenditure statement		Balance sheet	
		Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
<b>Short term investments (NET phase 1)</b> - Taxation and non-specific grant income - Short term investments	Impairment of investment in Arrow Light Rail Limited (special purpose subsidiary company).	30,901			30,901
<b>Property, plant and equipment (NET phase 1)</b> - Property, Plant and Equipment - Unusable reserves	Overstated valuation for NET trams at 31 March 2012 based in error on IAS 17 value (£26.1m) rather than cost (£18m).			8,050	8,050
<b>PFI liability (NET phase 1)</b> - Short term investments - Cost of services - Surplus or deficit on revaluation of PPE assets - Financing and investment income and expenditure	Overstated PFI liability and write-off due to error in estimation of PFI interest payments for 2011/12.	4,370	1,105 8,790	5,525	
<b>Heritage assets</b> - Heritage assets - Unusable reserves	Incorrect RPI rate used to calculate value of heritage assets at 31 March 2010.			216	216

		Comprehensive income and expenditure statement		Balance sheet	
Item of account	Nature of error	Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
<b>Heritage assets (2010/11)</b>	As above.				
- Heritage assets				209	
- Unusable reserves					209
<b>Heritage assets (2009/10)</b>	As above.				
- Heritage assets				262	
- Unusable reserves					262
<b>Bulwell LIFT scheme</b>	Overstatement of initial IFRIC 12 asset and liability values for new Bulwell LIFT scheme.				
- Property, Plant and Equipment					1,390
- Other long term liabilities				1,293	
- Short term creditors				54	
- Financing and investment income and expenditure		43			
- Property, Plant and Equipment	Understated revaluation adjustment linked to overstatement above.			1,390	
- Unusable reserves (capital adjustment account)					1,390
<b>Note 6.5.15 Icelandic bank deposits</b>	Overstatement of financial impairment relating to Landsbanki cash deposits.				
- Long term investments					1,402
- Short term investments				1,830	
- Financing and investment income and expenditure	Council unaware of late guidance issued by CIPFA (June 2012).		428		

		Comprehensive income and expenditure statement		Balance sheet	
Item of account	Nature of error	Dr £'000s	Cr £'000s	Dr £'000s	Cr £'000s
<b>Note 6.2.8 Short term debtors</b>	Classification error.				
- Other local authorities	Non-material, non-trivial adjustment.			513	
- Other entities and individuals					513
<b>Note 6.2.10 Short term creditors</b>	Classification error.				
- Other entities and individuals	Non-material, non-trivial adjustment.			7,312	
- Central government bodies					7,312
<b>Note 6.1.5 Grant income</b>	Classification error.				
- Department of Transport: PFI Grants	Non-material, non-trivial adjustment.	5,203			
- Department of Education: PFI Grant			3,419		
- Other revenue grants			1,784		



# Appendix 3 – Draft letter of management representation

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## **Nottingham City Council - Audit for the year ended 31 March 2012**

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Nottingham City Council, the following representations given to you in connection with your audit of the Authority's financial statements for the year ended 31 March 2012.

### **Compliance with the statutory authorities**

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Authority, for the completeness of the information provided to you, and for making accurate representations to you.

### **Uncorrected misstatements**

The effects of uncorrected financial statements misstatements are not material to the financial statements, either individually or in aggregate.

### **Supporting records**

I have made available all relevant information and access to persons within the Authority for the purpose of your audit. I have properly reflected and recorded in the financial statements all the transactions undertaken by the Authority.

### **Internal control**

I have communicated to you all deficiencies in internal control of which I am aware.

### **Irregularities**

I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk the financial statements may be materially misstated as a result of fraud.

### **Law, regulations, contractual arrangements and codes of practice**

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Authority has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

### **Accounting estimates including fair values**

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

For the measurement and valuation of investments and borrowings disclosed under financial instruments, I confirm:

- the appropriateness of the measurement method; and
- that subsequent events do not require adjustment to the fair value measurement.

### **Group entities**

I acknowledge that the Council supports and will continue to support the financial position of its wholly owned subsidiary companies including Enviroenergy Limited and Nottingham City Homes Limited.

### **Related party transactions**

I confirm that I have disclosed the identity of the Authority's related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the Code.

### **Subsequent events**

I have adjusted for or disclosed in the financial statements all relevant events subsequent to the date of the financial statements.

### **Comparative financial statements**

A restatement of £1.3m was made to correct a non-material misstatement in the prior period group financial statements. This affects the comparative information contained within the Group Movement in Reserves Statement. Written representations previously made in respect of the prior period remain appropriate.

Signed on behalf of Nottingham City Council

I confirm that this letter has been discussed and agreed by the Audit Committee on 21 September 2012.

Signed

Name            Tony Kirkham

Position        Director of Strategic Finance

Date             21 September 2012

# Appendix 4 – Glossary

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## **Annual Audit Letter**

Letter issued by the auditor to the Authority after the completion of the audit that summarises the audit work carried out in the period and significant issues arising from auditors' work.

## **Annual Governance Report**

The auditor's report on matters arising from the audit of the financial statements presented to those charged with governance before the auditor issues their opinion [and conclusion].

## **Annual Governance Statement**

The annual report on the Authority's systems of internal control that supports the achievement of the Authority's policies aims and objectives.

## **Audit of the accounts**

The audit of the accounts of an audited body comprises all work carried out by an auditor under the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

## **Audited body**

A body to which the Audit Commission is responsible for appointing the external auditor.

## **Auditing Practices Board (APB)**

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

## **Auditing standards**

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

**Auditor(s)**

Auditors appointed by the Audit Commission.

**Code (the)**

The Code of Audit Practice for local government bodies issued by the Audit Commission and approved by Parliament.

**Commission (the)**

The Audit Commission for Local Authorities and the National Health Service in England.

**Ethical Standards**

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

**Financial statements**

The annual statement of accounts that the Authority is required to prepare, which report the financial performance and financial position of the Authority in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

**Group accounts**

Consolidated financial statements of an Authority and its subsidiaries, associates and jointly controlled entities.

**Internal control**

The whole system of controls, financial and otherwise, that the Authority establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

**Materiality**

The APB defines this concept as 'an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement

within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative 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**

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

### **Those charged with governance**

Those entrusted with the supervision, control and direction of the Authority. This term includes the members of the Authority and its Audit Committee.

### **Whole of Government Accounts**

A project leading to a set of consolidated accounts for the entire UK public sector on commercial accounting principles. The Authority must submit a consolidation pack to the department for Communities and Local Government which is based on, but separate from, its financial statements.

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- any director/member or officer in their individual capacity; or
- any third party.

