

Annual Audit Letter

Nottingham City 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 included only significant recommendations in this report. The Council has accepted these recommendations.

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

Audit opinion and financial statements

Your officers coped well with the introduction of the complex International Reporting Standards (IFRS) and I gave an unqualified opinion on the financial statements on the 30 September 2011.

Significant matters arising from the audit include:

- Internal control – operation of Council’s process for identifying related parties improved this year but remains weak.
- Accounts payable – controls in this area remained weak following introduction of new arrangements in August 2009. Steps are being taken by the Council in 2011/12 to address these weaknesses.

- Payroll – continuing weakness as the Council has no formal establishment list. The Council plans to address this weakness through new HR and finance systems from April 2012.

Value for money

I gave an unqualified VFM conclusion on the 30 September 2011.

Significant matters that are relevant to proper arrangements to secure VFM

- Jobs plan review – in August 2010 I received a number of allegations concerning two significant elements of the Council’s Jobs Plan. Given the nature of the allegations I determined that it was appropriate to carry out further work as part of the statutory audit and withheld my certificate on the 2009/10 audit. I have now completed my review and issued a report to the Council detailing my findings, conclusions and recommendations.

Certificate

I issued separate certificates of audit completion for both 2009/10 and 2010/11 on 11 November 2011 following completion of my

consideration of matters brought to my attention by local authority electors in relation to elements of the Council's Jobs Plan.

Current and future challenges

Economic downturn and pressure on the public sector

All local authorities face increased financial pressure due to the economic downturn and reduction in central government funding over the coming years. Financial resilience will be essential for local authorities so that they can continue to deliver cost-effective services.

The Council recognises the importance of this by making 'securing financial standing and sustainability' a key financial objective.

Financial pressures

The Council has a good track record of effectively managing financial pressures. During the year management closely monitored income and expenditure and addressed a forecast overspend at the year-end. This led to the Council successfully containing expenditure within its 2010/11 revenue budget.

Pressures on demand led budgets for adult and children's services were managed in 2010/11 but in my view remain an on-going risk for 2011/12 and future financial years.

Looking ahead, the authority has an up to date medium term financial strategy (MTFS) that takes into account the economic downturn and future reductions in government funding.

Cost reduction

Cost reduction forms an important part of the Council's MTFS.

Not all cost reductions were achieved as planned this year (£3.2m below £18.1m target) although unplanned reductions (£1.6m) were achieved from other sources.

This extra financial pressure did not affect the Council's final revenue position for 2010/11 but in my view cost reduction will continue to be a risk in future years. The Council has set a challenging £25.5m target for 2011/12.

Longer term cost reduction is more effective when savings continue in future years rather than just for a single financial year. The Council's overall budget process and 'Strategic Choices' programme encourages sustainable, recurrent changes to the Council's base budget.

It is important however that recurrent savings continue in future and that the use of non-recurrent savings is minimised and closely managed by the Council.

Service competitiveness

In my 2009/10 annual audit letter I reported that service competitiveness continued to be an area for development by the Council.

Service provision

The Council is currently working in partnership with Leicestershire County Council to establish a shared service organisation (East Midlands Shared Services). The aim of EMSS is to provide joint HR, payroll and finance transaction processing services for both authorities. Full implementation is planned for May 2012.

Development of this partnership will be a challenge for both the Council and its partner authority. The Council needs to assure itself that sound governance, financial management and performance management arrangements are put in place for the EMSS programme.

Looking ahead, the Council will need to ensure that the projected service benefits and cost savings are made when services become operational.

Benchmarking

The Council continues to routinely use cost data to inform decision making. However, the use of comparative data and benchmarking information remains limited.

Nottingham Express Transit (NET) phase 2

In March 2011 the Council announced that Tramlink Nottingham was its preferred bidder for the NET phase 2 tram extension. Since that time, the Council has continued with its preparatory work looking at the governance and affordability aspects of the project ahead of awarding the contract.

Having a capital value of over £435m, this is a major project for the authority. It faces a number of challenges including:

- Cessation of the existing NET concession agreement with Arrow Light Rail;
- Financial settlement with Nottinghamshire County Council following its withdrawal from NET and NET phase 2;
- Negotiation and implementation of a new concession agreement with Tramlink Nottingham; and
- Implementation of the workplace parking levy to provide the funding required that is not met through the Private Finance Initiative (PFI).

Given the scale of this project, close monitoring by the Council of the concession agreement over the construction phase will be vital. The Council recognises that it needs to ensure that the project is delivered on time, to budget whilst meeting agreed design and service specifications.

Treasury management

The Council holds £34m of deposits with three Icelandic banks where repayment is overdue. It has impaired the value of these deposits by £7m reducing their value in its 2010/11 financial statements to £27m.

My audit work included review of the Council's impairment and I concluded that this had been estimated properly using relevant accounting guidance. This assumes that the Council will receive between 85% and 100% of its total deposit which will vary for each bank.

Recovery in full of these deposits continues to be a priority for the authority to minimise the effect on its future financial position. It has estimated a net loss of just over £3m which it has accounted for in its future financial planning.

International Financial Reporting Standards (IFRS)

The Council responded well to the challenge of producing financial statements meeting IFRS requirements for the first time this year. This is a significant achievement given that the Council's financial statements are complex and as many authorities struggled to implement IFRS in a timely manner.

Preparation of financial statements under IFRS will remain an important aspect of the Council's financial reporting process in the future. Although the Council has good procedures in place for preparing its financial statements under IFRS, it is keen to develop and embed these.

Recommendations

Recommendation

- R1** Continue to closely monitor financial performance for the 2011/12 financial year. Continue to pay specific attention to demand led budgets for adult and children's services to promptly identify and manage any overspending in these areas and ensure ongoing trends are adequately reflected in the medium term financial plan.
- R2** Deliver in full cost reduction targets for 2011/12 and future years, ensuring that delivery against financial targets is embedded within the performance management system.
- R3** Ensure the refreshed Council Plan and medium term financial plan fully reflect the changed financial landscape and fully address future funding gaps particularly ensuring sufficient sustainable and ongoing savings.
- R4** The Council should satisfy itself that the financial, accounting and governance risks of NET phase 2 are fully understood and covered by the concession agreement with Tramlink Nottingham. Ensure arrangements for monitoring the agreement during the construction phase of this scheme are robust.

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

The financial statements were submitted for audit ahead of the statutory date.

I am pleased to report that the Council responded well to the challenge of producing financial statements under International Financial Reporting Standards (IFRS) requirements for the first time this year.

Opinion

I issued my audit report on the 30 September 2011 and gave an unqualified opinion on the Council's 2010/11 financial statements. My annual governance report for 2010/11 contains detailed audit findings. This was reported to members of the Council's Audit Committee at their September 2011 Audit Committee meeting.

As my ongoing investigation of issues raised by a local government elector was not completed at that time, I issued a separate certificate of audit completion on 11 November 2011. As the matters related to my previous year audit, I also issued a certificate of audit completion for my 2009/10 audit on the same date.

Accounts payable

I reported last year that the Council experienced significant problems with its new accounts payable arrangements (introduced in August 2009). At that time, extra year-end procedures were put in place by the Council to mitigate the effect of these problems. These procedures together with extra audit work testing payments gave me sufficient assurance in this area.

My audit found continuing weaknesses in the operation of the accounts payable system as action taken by the Council to address these in 2010/11 was insufficient. As last year, extra work by the Council and myself was required at the year-end. I am aware that the Council is implementing a plan to address these weaknesses and improve performance in this area during 2011/12.

Payroll

In my 2009/10 annual audit letter, I reported that the Council lacked a definitive establishment list (schedule of approved posts). This weakness made it more difficult for me to obtain sufficient assurance that the Council's payroll costs were accurate. Further work was required last year to gain this assurance.

My audit found that this was a continuing issue in 2010/11. In the absence of an establishment check, I performed alternative work to gain assurance about the Council's payroll costs. Again, significant extra work was required by both Council staff and my audit team to gain this assurance.

During 2012/13, the Council will transfer its HR and Financial Services to a new shared service organisation (East Midlands Shared Services). New processes will be introduced that are expected to address this weakness. However, this weakness will still be an issue in 2011/12.

Significant weaknesses in internal control

I did not identify any significant weaknesses in your internal control arrangements. My audit found one area of continuing weakness concerning members' responses to requests for confirmation of related party transactions. Although the Council has a process to identify related parties, its effectiveness is limited.

I reported this matter in my 2009/10 annual audit letter and recommended that the Council improved the operation of its process this year. My audit found that efforts by officers this year led to substantially improved response rates for both senior officers and members. However, the overall rate remained significantly below 100% increasing the risk of undisclosed related parties in the Council's financial statements. I consider this to be a governance weakness that members of the Council need to address.

Recommendation

Recommendation

R5 Improve operation of the Council's process for identifying related parties by:

- Encouraging all members and senior officers to respond promptly to requests for information; and
- Appointing a senior officer to lead and oversee the process.

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 / does not have 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 Council has well established arrangements for securing financial resilience.</p> <p>My assessment has been informed through an assurance based review of financial resilience and ongoing monitoring of the Council's financial position and plans.</p> <p>Criteria met.</p>

Criterion	Key messages
<p>2. Securing economy efficiency and effectiveness</p> <p>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p> <p>Focus for 2010/11:</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 2009/10 published by the Audit Commission.</p> <p>By using the profiles, I was able to compare the performance of the Council with other similar authorities using a number of key indicators and measures covering:</p> <ul style="list-style-type: none"> • Income (including trading income); • service expenditure; and • efficiency savings. <p>Criteria met.</p>

Report by exception

The Audit Commission requires me to report by exception where significant matters come to my attention, which I consider to be relevant to proper arrangements to secure economy, efficiency and effectiveness in your use of resources.

Jobs plan review

In 2009 Nottingham City Council developed a Jobs Plan to help get 2000 city residents into employment or onto training courses by March 2011. Two key elements of the Jobs Plan were the Future Jobs Fund (£6.5m funding awarded) and the Community Programme (funded by the Working Neighbourhoods Fund). The Council was the 'accountable body' for both sources of funding and as a consequence governance arrangements are determined by the external funding bodies, and by the Council's own constitution, standing orders and financial regulations.

There is much to commend the Council for in bringing forward so quickly these two large citywide programmes to support the creation of 1600 jobs in total. It should be stressed that my investigation has not reviewed the impact of either programme in delivering the objectives of the Jobs Plan to get residents into employment or onto training courses and I am not seeking to question the benefit that individuals have derived as a consequence of their participation in the programmes.

However, in August and September 2010 I received a number of allegations concerning both the Future Jobs Fund and Community Programme. Given the nature of the allegations I determined that it was appropriate to carry out further work as part of the statutory audit. I have now completed my review and issued a report to the Council detailing my findings, conclusions and recommendations.

The main conclusions are summarised below:

- The Council (acting as accountable body) has failed to comply with the requirements of its own constitution, standing orders and financial regulations in awarding Future Jobs Fund and Community Programme contracts. In particular, specific individuals failed to demonstrate appropriate accountability for the decisions taken. These failures were compounded by poor record keeping within the Council.
- My investigation has led me to conclude that the relevant Portfolio Holder's conduct may have been in breach of paragraph 3(2)(d) of the Code of Conduct (conduct which has compromised or is likely to compromise the impartiality of officers). My concerns arise from the need for transparency and good corporate governance rather than that there was any actual inappropriate allocation of contracts (in relation to which I did not find any evidence).
- The role of partners as set out in the original bids did not fully materialise in practice: As a consequence, some partners felt let down and had concerns around consistency and transparency. In my view the Council could have done more to allay these concerns by being more open and transparent about the need for changes and to ensure everyone was given an equal opportunity to respond to these changes.

I have made a number of recommendations to the Council to address the issues identified. The Council's initial response to these findings highlighted the intense national and local pressure to deliver on these programmes and that it has been successful in doing this. However, it also accepts that this review demonstrates that there should have been greater consistency around compliance and record keeping.

Closing remarks

I have discussed and agreed this letter with the Deputy Chief Executive and Corporate Director for Resources. I will present this letter at the Audit Committee on 6 January 2012 and will provide copies to all board members.

Further detailed findings, conclusions and recommendations in the areas covered by our audit are included in the reports issued to the Council during the year.

Report	Date issued
Annual governance report	September 2011
Jobs plan review	November 2011

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

Sue Sunderland

District Auditor

November 2011

Appendix 1 - Fees

	Actual	Proposed	Variance
Scale fee	£423,000	£423,000	£nil
Non-audit work	£nil	£nil	£nil
Total	£423,000	£423,000	£nil

The scale fee quote above is gross of rebates from the Audit Commission of around just under £45,000

NB: The above fees are those relating to the 2010/11 audit. It is worth noting that additional audit fees have been incurred in relation to the completion of my investigation into the matters raised by local government electors in 2009/10. In total these have amounted to £47,000.

Appendix 2 - Glossary

Annual governance statement

Governance is about how local government bodies ensure that they are 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 local government bodies are directed and controlled and through which they account to, engage with and where appropriate, lead their communities.

The annual governance statement is a public report by the Council on the extent to which it complies with its own local 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 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.

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.

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 conclusion.

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