

Annual Audit Letter

Halton Borough Council

Audit 2008/09

November 2009



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Status of our reports

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/ members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

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

This report summarises the findings from our 2008/09 audit. It includes messages arising from the 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.

Audit Opinion

- 1 I issued an unqualified audit opinion on the Council's 2008/09 financial statements on 30 September 2009. My draft audit report was included as Appendix 2 of my Annual Governance Report, as reported to the Business Efficiency Board on 30 September 2009.
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Financial Statements

- 2 The audit of the Council's 2008/09 financial statements was less straightforward than in previous years. In our 2007/08 Annual Governance Report we raised the issue of the accounting treatment of the development costs on the Mersey Gateway scheme. In essence our view is that the majority of the costs incurred to date should have been treated as revenue costs rather than capitalised. The Council sought a capitalisation direction from the Department for Communities and Local Government (DCLG) regarding the costs incurred to date. The late receipt of this direction meant that the Council's draft abstract of accounts whilst available for audit on 30 June 2009 could not be approved by the Business Efficiency Board until 12 August 2009.
 - 3 The DCLG decision was received in late July and allowed the Council to capitalise up to £3.7m of 2008/09 expenditure. In addition the Department for Transport (DfT) amended the terms of £3m of capital grant to enable this to be used for revenue purposes during 2008/09. The outcome of the decisions from DCLG and DfT did not allow the Council to capitalise any of the expenditure incurred in previous years. As a result a material amount of expenditure from earlier years remained, in my view, incorrectly accounted for as capital expenditure. The majority of this expenditure had been incurred in 2006/07 and 2007/08.
 - 4 Following significant input from finance officers and agreement of the amendments with my audit team the draft abstract was revised to reflect a prior period adjustment of £8.43m. This related to the development costs on the Mersey Gateway scheme incurred during 2006/07 and 2007/08. Costs capitalised before 2006/07 remain in the balance sheet but are in total below our materiality gauge and go back to 2001 and for some elements of these there could be a justifiable case to argue that they could be accounted for as capital expenditure. The amount of this expenditure is £4.675m. I have agreed with the Operational Director – Financial Services not to amend the accounting treatment of this earlier expenditure.
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- 5 My audit also identified a further material adjustment on fixed assets of £11.4m. Several voluntary aided and voluntary controlled schools, not owned by the Council, had been incorrectly included on the Council's balance sheet since the transfer of these assets from Cheshire County Council in 1998. The schools had been shown as assets in the accounts of the former County Council on transfer and therefore included in the Council's asset register. The 2008/09 abstract was amended to remove the schools from the Council's balance sheet.

Use of resources

- 6 Use of Resources is a scored judgement which determines how well councils manage and use their financial resources. I concluded that the theme and KLOE (key lines of enquiry) scores reflect a council that is performing consistently above the minimum standards specified by the Audit Commission, level 3 performance.

Mersey Gateway

- 7 The Council has continued to make good progress in managing the Mersey Gateway project. It has received reconfirmation of 'Programme Entry' status from the DfT, secured additional grant funding towards preparation costs and is awaiting the results of the Public Inquiry carried out earlier this year. Its preparations for the next key stage of the DfT approval process are well underway.

Value for Money Conclusion

- 8 I issued an unqualified conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources.

Comprehensive Area Assessment and Organisational Assessment

- 9 The Audit Commission introduced a new assessment regime during 2009, Comprehensive Area Assessment (CAA). This aims to review the performance of local partners in delivering better outcomes for local people. The assessment is designed to focus attention on areas that need attention in order to deliver additional and sustained improvement. Our work in this area is being led by the local Comprehensive Area Assessment Lead (CAAL). The CAAL has shared draft findings with officers and he is due to formally report on 10th December 2009. Alongside the CAA report we will issue our organisational assessment which combines our judgements on your use of resources and managing performance. Any issues arising will be discussed with you and planned into future years audit and assessment activity.

Key messages

Audit Fees

- 10 My fee proposals were communicated to the Business Efficiency Board in my Audit Plan for 2008/09. In my updated Opinion Plan, presented in June 2009, I reported that I was satisfied that the audit fee was appropriate and no adjustment was required. I expect to contain the 2008/09 audit fee within the £222,554 total agreed with you.
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Actions

- 11 Recommendations are shown within the body of this report and have been agreed with the Business Efficiency Board.
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Independence

- 12 I can confirm that the audit has been carried out in accordance with the Audit Commission's policies on integrity, objectivity and independence.

Financial statements and annual governance statement

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

Significant issues arising from the audit

- 13** The accounting treatment adopted by the Council for the development costs on the Mersey Gateway scheme was the most significant issue during the 2008/09 audit. I had ongoing discussions during the year with the Operational Director – Financial Services on the accounting treatment. The DCLG and DfT decisions in July 2009, and the financial statements approved by members on 12 August, dealt with the 2008/09 in year costs of £6.7m. It did not however resolve the costs which had been incurred in previous years, in particular the costs incurred in 2007/08 and 2006/07 which totalled £8.430m. My view was that these costs should be accounted for as revenue expenditure rather than capital expenditure. I agreed with the Operational Director – Financial Services that the financial statements would be amended to reflect the correct accounting treatment.
- 14** The amendment of previous years' expenditure on Mersey Gateway required a prior period adjustment (PPA). This PPA corrected the £8.430m of expenditure previously charged to capital in 2006/07 and 2007/08 and included in the Fixed Assets balance as infrastructure costs, which should have been charged to the Income and Expenditure Account as revenue expenditure. To enable this adjustment to be made officers have utilised £4.930m from the capital reserve and £3.5m from NWDA grant funding. Various other accounting entries have been affected by this PPA, the detail of the amended entries is provided at note 38 to the abstract. It is essential that officers continue to review the costs incurred on the scheme to ensure that proper accounting practice is followed in future years.
- 15** My audit also identified another material error in the Council's 2008/09 financial statements. This related to fixed assets on the balance sheet. Audit testing of the Council's operational assets (land and buildings) highlighted two voluntary controlled schools valued at £4.8m which were not owned by the Council but were included on the Council's balance sheet. Following further testing carried out by Council staff, a further two voluntary controlled schools and two voluntary aided schools were found to have been incorrectly included on the Council's balance sheet. The six schools totalled some £11.4m in value. The 2008/09 accounts have been amended to correct this error, again via a PPA. These schools have been accounted for in this manner since their transfer from Cheshire County Council when Halton Borough Council was established as a unitary council.

Material weaknesses in internal control

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

Accounting Practice and financial reporting

17 I considered the qualitative aspects of your financial reporting.

18 My audit identified several issues including:

- Scope to further enhance compliance with the disclosure requirements of CIPFA's Statement of Recommended Practice (the SORP).
- The need for more accurate categorisation of expenditure between capital and revenue on all capital schemes.
- Using prior period restatements to correct only material adjustments arising from either changes in accounting policies or to correct fundamental errors in the previous years' accounts.

I have included several recommendations for improvement within the Annual Governance Report presented to the Business Efficiency Board on 30 September, these are included below. Officers are currently finalising the agreed action plan.

Recommendation
R1 Further develop year end closedown arrangements to ensure that the 2009/10 abstract of accounts meets all relevant disclosure requirements.
R2 Ensure staff follow year end procedures relating to the coding of expenditure.
R3 Review and strengthen processes to ensure the correct categorisation of expenditure between revenue and capital.
R4 Restate prior year figures only where there is a material change in accounting policy or to correct a fundamental error.

International Financial Reporting Standards (IFRS)

19 In March 2008 the Treasury announced that the annual financial statements of government departments and other public sector bodies would be prepared using International Financial Reporting Standards (IFRS) from 2009/10 onwards. For local government bodies the first full year of application is the 2010/11 financial statements but the starting period for this (the transition date) is 1 April 2009. Local government bodies will be required to produce their 2009/10 Whole of Government Accounts return on an IFRS basis. The expected deadline for the WGA return is 1 October 2010.

- 20 As part of my 2008/09 audit I have completed an Audit Commission survey on the Council's progress in preparing for the implementation of the IFRS. Whilst the Council has started its preparation it is at a very early stage and behind where it expected to be at this time. A significant amount of work will be needed during 2009/10 to meet the new IFRS information requirements and the timeframes for restatement. Capacity is a particular risk given the other changes, such as the internal restructure, that are taking place within the Council.

Recommendation

- R5** Review arrangements in place for implementing IFRS to ensure appropriate processes, people and skills are in place to meet the new accounting requirements and the associated deadlines.

Value for money and use of resources

I considered how well the Council is managing and using its resources to deliver value for money and better and sustainable outcomes for local people, and gave a scored use of resources judgement.

I also assessed whether the Council put in place adequate corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money (VFM) conclusion.

Use of resources judgements

- 21 In forming my scored use of resources judgements, I have used the methodology set out in the [use of resources framework](#). Judgements have been made for each key line of enquiry (KLOE) using the Audit Commission's current four point scale from 1 to 4, with 4 being the highest. Level 1 represents a failure to meet the minimum requirements.
- 22 I have also taken into account, where appropriate, findings from previous use of resources assessments (updating these for any changes or improvements) and any other relevant audit work.
- 23 The Council's use of resources theme scores are shown in Table 1 below. The key findings and conclusions for the three themes, and the underlying KLOE, are summarised in Appendix 5.

Table 1 Use of resources theme scores

Use of resources theme	Scored judgement
Managing finances	3
Governing the business	3
Managing resources	2

- 24 Overall the Council has performed well scoring level 3, exceeds minimum requirements - performs well, in two of the three use of resources themes.

Managing finances

- 25 The Council continues to manage its finances well to deliver value for money and it continues to deliver services that achieve high satisfaction ratings from local people.
- 26 The Council has a proven track record of robust financial management and good financial standing. Its previous prudent approach to managing its finances has meant that it has sufficient balances and reserves to deal with the Mersey Gateway amendment discussed earlier in this report. It is now in the process of revisiting its medium term financial strategy (MTFS) and reserves and balances strategy to reflect the impact of the Mersey Gateway accounting treatment.
- 27 I found established treasury management processes in place at the Council with no exposure to foreign bank investments in 2008/09. Following the Icelandic bank issue, the quarter 3 treasury management report included a review of the approved counter party list. This was not due until January 2010 but because of the rapidly changing circumstances and volatility in credit ratings officers felt it was prudent to rework the list on an interim basis. Internal Audit's review of the Council's treasury management arrangements highlighted a couple of areas to further strengthen including the need to review treasury management arrangements against recently produced CIPFA guidelines. I understand that officers are in the process of doing this.
- 28 The Council has a good understanding of its costs and comparative performance and it has achieved both cost and service efficiencies in 2008/09. It is currently going through a major efficiency programme which should help deliver significant efficiency savings to the local community by 2011/12. It is essential that the Council is able to demonstrate achievement of the first stage of the efficiency programme in 2009/10.
- 29 At the time of my review in early 2009 the Council did not have a systematic approach to reviewing services to ensure they deliver value for money. It is developing this as part of the wider efficiency programme.

Governing the business

- 30 The Council has well established governance arrangements in place which are well understood by both officers and members. There is a strong ethical framework and culture within the organisation and a real commitment to deliver good quality services which meet the needs of the local community. Satisfaction levels with Council services are good. The Council has continued to develop its commissioning and procurement functions and we have seen good evidence of joint procurement initiatives with partners and neighbouring organisations. There is generally good use of data to inform decision making and service delivery with some good examples of improved outcomes being delivered.
- 31 Data quality arrangements continue to develop but further progress is needed to evidence good data quality arrangements across all service areas. In addition officers should progress the plans in place to further strengthen commissioning and procurement, including the third sector.

Managing resources

- 32** I concluded that the Council's management of its natural resources is adequate and continues to develop. It has put in place some good energy saving and green initiatives but it now needs to ensure its baseline information on its environmental impact is complete and comprehensive. This needs to be supported by appropriate targets, and more systematic monitoring and reporting arrangements.
- 33** Over the past year the Council has strengthened its strategic approach to asset management. It has continued to manage and use its assets well at an operational level with some good examples of Council assets being used to benefit the local community and enhance service delivery. Progress is ongoing in updating the asset management information database.

Recommendation	
R6	Revisit the MTFS and reserves and balances strategy to reflect the impact of the Mersey Gateway accounting treatment.
R7	Ensure that a service review framework and programme is agreed in 2009/10.
R8	Progress the plans in place to further strengthen commissioning and procurement arrangements and evidence improved outcomes.
R9	Develop plans to ensure a corporate approach to supporting the third sector in commissioning and procurement.
R10	Develop a complete and comprehensive baseline of the Council's environmental impacts.
R11	Establish a more strategic and systematic approach to managing natural resources, including the setting of targets and monitoring and reporting of performance against these periodically through the year.
R12	Ensure the asset management information database is complete and up to date.

Mersey Gateway

- 34** I have continued to review the Council's arrangements for managing the Mersey Gateway project to build a new toll bridge over the River Mersey.
- 35** In March 2006, DfT granted the Mersey Gateway Project 'Programme Entry' status and awarded provisional financial support in the form of £123m PFI Credits and £86m grant for land acquisition and some decontamination works, subject to a number of conditions. Final confirmation of funding support will be given by DfT immediately prior to contract award to the successful bidder, currently planned for 2012.
- 36** The Council has continued to make good progress during the year, in particular it has:
- obtained reconfirmation of 'Programme Entry' status following a further review of value for money by DfT;
 - secured additional grant from DfT of £6.4m towards preparation costs;

- completed preparations for the Public Inquiry of the statutory orders and planning applications required for the scheme, and this was held in May and June 2009;
 - made preparations for the next key stage of the DfT approval process, being submission of the Outline Business Case required to secure 'Conditional Funding Approval' from the DfT and the HM Treasury Project Review Group; and
 - made plans for the formal procurement process to ensure it can commence as soon as practical after the Secretary of State decision on the planning process, expected early in 2010.
- 37** I will continue to review the Council's arrangements as it proceeds with this large and complex procurement.
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VFM Conclusion

- 38** I assessed your arrangements to secure economy, efficiency and effectiveness in your use of resources against criteria specified by the Audit Commission. From 2008/09, the Audit Commission will specify each year, which of the use of resources KLOE are the relevant criteria for the VFM conclusion at each type of audited body. My conclusions on each of the areas are set out in Appendix 1.
- 39** I issued an unqualified conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources.

Closing remarks

- 40 The economic downturn, public sector funding and the banking crisis is having a very significant impact on public finances and the bodies that manage them. It is envisaged that there will be wide ranging and more fundamental impacts on the ability of public sector bodies to fund service delivery and capital programmes in the short to medium term, including pressures on income streams. There are further challenges for policy priorities where patterns of demand for services are also changing. In addition the Council is going through its own wide ranging efficiency review including a fundamental internal restructuring exercise. These changes and the Council's response will be a key focus of my attention for future audits.
- 41 I have discussed and agreed this letter with the Chief Executive and the Strategic Director Corporate and Policy. I will present this letter at the Executive Board on 3 December 2009 and will provide copies to all board members/committee members.
- 42 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.
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- 43 As in previous years the Council has taken a positive and constructive approach to our audit. I wish to thank the Council's staff for their support and co-operation during the audit.

Michael Thomas
District Auditor
November 2009

The Audit Commission

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

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