Annual Audit Letter

Thurrock Council

Audit 2010/11

Contents

Traffic light explanation

Red ■ Amber ◆ Green ●

Key messages

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

1 I was unable to issue my audit opinion by the due date of 30 September, because the Council's arrangements for producing the financial statements and supporting working papers were inadequate. The Council struggled to produce restated accounts under International Financial Reporting Standards (IFRS). The quality of working papers supporting the initial accounts provided for audit was also poor. As a result my audit has taken significantly longer than planned and resulted in a sizeable additional audit fee. The Council has taken some six months to produce amended accounts, providing a revised version for audit in mid March 2012. The standard of the revised accounts and working papers was much improved and I was able to issue an unqualified opinion on 20 April 2012. This is however over six months after the statutory deadline of 30 September. I have not yet been able to complete my audit of the whole of government accounts return as this was not updated to reflect the changes in the accounts until May 2012. As a result, I am not yet able to issue my audit completion certificate.

2 As a result of the problems with the accounts, I made two recommendations to the Council under section 11 of the Audit Commission Act 1998. The recommendations, which the Council was required to formally consider at a public meeting, were included in my interim annual governance report presented to Members in November. The recommendations for improving the arrangements for producing the 2011/12 accounts, include:

- ensuring enough resources are available to produce the accounts;
- developing a robust project plan including production of good quality supporting working papers and undertaking quality assurance of the accounts and working papers;

- providing relevant training to staff; and
- reporting progress to the Audit Committee during the year.

3 The Council has responded positively to these recommendations and is taking steps to improve the processes for the production of the 2011/12 accounts.

Value for money

4 I qualified my value for money conclusion for 2009/10 because I assessed the Council's arrangement for planning for financial health, governance and strategic asset management as inadequate.

5 One of the key issues resulting in my qualification for 2009/10 was the Council's low level of balances. It is pleasing to report that at 31 March 2011 the Council had increased these to the minimum level of £5 million considered necessary by the Director of Finance and Corporate Governance, and the draft outturn for 2011/12 shows a provisional level of £8 million compared to the desirable level of £7 million. The Council's spending for 2010/11 was also in line with budget. This is a significant improvement from the previous year, when the Council overspent the budget by £3.9 million, and is a commendable achievement given the in-year budget cuts of £4 million required as a result of reductions in funding by the new government. As a result, I have not qualified my 2010/11 value for money conclusion for financial resilience, the first element of my assessment.

6 I have however qualified my value for money conclusion in relation to the second element of my assessment, the Council's arrangements to challenge economy, efficiency and effectiveness. This is because:

- the Council only approved its strategic asset management plan in February 2011and for most of the year there was no plan in place; and
- the Cabinet report in July 2010, which sought approval for the review of the Council's external debt structure to reduce financing costs in the medium term, did not include information on the future costs and risks associated with this key decision. In particular, it did not clearly highlight the Council's greater exposure to the risk of fluctuations in future borrowing rates when it has to replace its short term loans.

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

7 Overall, the arrangements for producing the Council's accounts and supporting working papers were inadequate. The main issues identified resulted from errors in the restatement of the 2009/10 accounts and opening balance sheet to meet international financial reporting standards (IFRS). However, there were also many instances where figures within the accounts did not agree to supporting working papers and also where working papers included errors.

8 2010/11 was the first year councils had to produce their accounts in line with IFRS. As a result, the 2010/11 accounts are in a different format and contain restated balance sheets at 1 April 2009 and 31 March 2010, as well as at 31 March 2011. All 2009/10 comparators have also had to be restated. Thurrock prepared poorly for the change to IFRS. Most councils produced restated figures for audit in early 2011. Although the Council agreed to provide IFRS figures for audit in line with these timeframes, no figures were produced until late March and, at this stage, only comprised an incomplete restated balance sheet at 1 April 2009 and draft accounting policies. The full IFRS restatements were not produced until the draft accounts were presented for audit on 30 June. It was therefore not possible to undertake any early audit work on these figures.

9 I identified a number of weaknesses in the Council's financial statements, including:

- accounting policies were incomplete in some places and in others did not reflect the Council's practices;
- the Council made many technical errors in the IFRS restatement, particularly in the areas previously identified as likely to be problematic;
- as in previous years, the Council did not produce a full set of working papers at the start of the audit. Working papers had to be requested throughout the audit. Although some were immediately available, in many cases officers had to prepare the working papers as they were not produced as part of the closedown process. This delayed the audit, is an unproductive use of officer time, and indicates that appropriate quality checking of the statements and supporting working papers had not been undertaken; and
- quality checking of the accounts was ineffective, as evidenced by the fact that the accounts provided contained many inconsistencies and obvious errors.

10 As a result of these issues, I was unable to issue my opinion by the deadline of 30 September. I reported the detailed findings from my audit in my Interim Annual Governance Reports which were presented to the Audit Committee on 22 September, 10 November and 7 December. The Council brought in additional resource and has completely re-done the IFRS restatement of the 1 April 2009 balance sheet, the 2009/10 figures and also the IFRS amendments required for 2010/11, as well as correcting non-IFRS related errors in the 2010/11 accounts. My final Annual Governance Report, detailing the findings from my audit, was reported to the Audit Committee on 28 March 2012 with a further update on 20 April detailing the final amendments made to the accounts. I issued my final opinion, which was unqualified, on 20 April 2012.

Recommendations made under s11(3) Audit Commission Act 1998

11 To ensure the Council takes appropriate action to address the significant issues identified during this year's audit, I made recommendations to the Council under Section 11 of the Audit Commission Act 1998. These recommendations were contained in my interim Annual Governance Report considered by the Audit Committee on 10 November. The Council must consider the recommendations at a formal meeting which has been appropriately advertised within one month of the date of my recommendations. At the meeting, the Council must decide if the recommendations are to be accepted and what action should be taken. After the meeting the Council must publish a summary of its decisions in a local newspaper. The Council considered my recommendations at the full Council meeting on 1 December. My Section 11 recommendations are repeated below.

Recommendations made under s11(3) Audit Commission Act 1998

R1 The Council should put in place robust arrangements for the production of the 2011/12 financial statements, which meet statutory requirements and international financial reporting standards. In order to achieve this the Council should:

- ensure sufficient resources are available to support the accounts production;
- develop a comprehensive project plan which ensures:
  - the entries in the accounts are supported by good quality working papers which are available at the start of the audit; and
  - the financial statements and working papers have been subject to robust quality assurance prior to approval by the Director of Finance and Corporate Governance;
- provide additional training, where necessary, to ensure all staff involved in the accounts production process have the necessary skills and information; and
- monitor the production of the financial statements through regular reporting to Directors Board and the Audit Committee.

R2 The Council should develop a robust framework through which members of the Audit Committee can obtain assurance that controls within financial systems are operating effectively. This should include ensuring reconciliations are completed on a timely basis.

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.

12 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 the Council does not have adequate arrangements to secure, economy, efficiency and effectiveness in its use of resources. My conclusion on each of the two specified criteria is set out overleaf. In summary, I have conclude that the Council:

- has proper arrangements in place to secure financial resilience; but
- does not have proper arrangements for challenging how it secures economy, efficiency and effectiveness.

13 I have assessed the Council's arrangements to challenge how it secures economy, efficiency and effectiveness as inadequate because:

- the Council only approved its strategic asset management plan in February 2011 and for most of the year there was no plan in place. The plan that was approved was also incomplete, although more work has been completed on this during 2011/12; and
- the Cabinet report in July 2010, which sought approval for the review of the Council's external debt structure to reduce financing costs in the medium term, did not include information on the future costs and risks associated with this key decision. In particular, it did not clearly highlight the Council's greater exposure to the risk of fluctuations in borrowing rates when it replaces its short term loans with longer term borrowing at higher rates.

14 Last year, I qualified the Council's value for money conclusion in respect of arrangements for financial management, governance and strategic asset management. I am pleased to report that, although I am still qualifying my 2010/11 value for money conclusion as outlined above, the Council's financial management arrangements have improved significantly in a number of areas. Some of the main areas of improvement include:

- the Council has successfully increased the general fund balance from £2.1 million at 31 March 2010 to £6.6 million at 31 March 2011, which is in line with the Director of Finance and Corporate Governance's assessment of the minimum level of balances the Council should hold; and
- the Council's spending was in line with the 2010/11 budget, which is a notable achievement given the £4.5 million in-year cuts required by the emergency budget in July 2010 and the £3.9 million overspend against budget identified at the end of 2009/10.

Value for money criteria and key messages

Criterion	Key messages
1. Financial resilience **The organisation has proper arrangements in place to secure financial resilience.** Focus for 2010/11: 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.	The Council has successfully increased the general fund balance from £2.1 million at 31 March 2010 to £6.6 million at 31 March 2011 (£5.1 million after deducting sums which the Council has agreed to carry forward to 2011/12). This balance is now in line with the Director of Finance and Corporate Governance's assessment of the minimum level of balances the Council should hold, although it is still below the desirable level of £7 million. Budget setting, monitoring and control have also improved. The Council's spending was in line with the 2010/11 budget. This is a notable achievement given the £4 million in-year cuts required by the emergency budget in July 2010 and the £3.9 million overspend against budget identified at the end of 2009/10. However, the Council still needs to improve its financial resilience arrangements in the following areas: ■ the MTFS, although improved, remains a basic document and needs more scenario planning; ■ schools balances are high compared to other education authorities and the Council should review and take action on unspent balances; ■ ensuring all financial management objectives are SMART (specific, measurable, achievable, realistic and time-bound); and ■ improving the coding structure to make producing the financial statements easier. The level of balances held at 31 March 2011 is still low compared to other unitary authorities. The £7 million target level set by the Director of Finance and Corporate Governance will increase them to the average.
2. Securing economy efficiency and effectiveness **The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.** Focus for 2010/11:	I qualified my value for money conclusion in 2009/10 as the Council did not have a strategic asset management plan in place. The Council only approved a plan in February 2011, and it was still incomplete. To improve it's asset management arrangements the Council needs to: ■ identify assets that are surplus; ■ consider asset sharing with partners; ■ improve asset data such as stock conditions, financial data and maintenance information;

Criterion	Key messages
The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.	■ produce performance indicators for assets and use in benchmarking; and ■ consider alternatives for property occupancy and produce detailed plans to underpin the Strategic Asset Management Plan. The debt rescheduling exercise undertaken by the Council in August 2010 achieved the Council's short-term objective of rebuilding balances to the minimum level recommended by the Director of Finance and Corporate Governance. However, the Cabinet report in July 2010, which sought approval for the review of the Council's external debt structure to reduce financing costs in the medium term, did not include information on the future costs and risks associated with this key decision. The Council paid £17.5 million to redeem its long term loans as part of this exercise and, in the medium to longer term, the total discounted cash flow cost to the Council from the rescheduling has been calculated as just over £5.6 million. The advice provided to officers when the decision was taken suggested savings would finish in 2014/15 and costs would rise after this date. Interest rates have not risen as predicted before the debt was rescheduled, which has increased the savings period to 20 years. As the Council's short term loans mature and the currently low costs of short term borrowing increase, the Council will need to take out longer term borrowing at higher rates to replace its current loans. The Council therefore has a greater exposure to the risk of fluctuations in borrowing rates. For example, the costs of public works loan board borrowing was increased by the Government in October 2010. The Council has not recalculated its projections the figures to assess the impact of this. The Council needs to ensure that Members are kept fully informed of the current and long term financial impact of any future changes in interest rates and any changes to the Council's loans portfolio.

Certification of claims and returns

15 Funding from government grant-paying departments is an important income stream for the Council. The Council needs to manage claiming this income carefully and demonstrate that it has met the conditions which attach to these grants. I produced a report earlier this year summarising the findings from my certification of the Council's 2009/10 grant claims.

16 My audit of claims in previous years found the Council's arrangements for managing and quality assuring grant claims were variable and required further improvement. Although my work on 2010/11 claims is still in progress, overall the level of fees for grant claims has fallen and the workload involved has reduced. This is because:

- better quality working papers have been produced to support the claims;
- fewer queries have arisen as a result; and
- fewer claims have been qualified this year.

17 Table 1 compares the findings from my audit of 2009/10 claims to 2010/11 and shows the Council has improved the arrangements for producing grant claims and supporting working papers this year.

Table 1: **Comparison of grant claims performance for 2010/11 to 2009/10**

Work so far on 2010/11 claims shows an improved performance

Claim	2009/10	2010/11 to date
Housing benefits	This is a complex and high value claim. A qualification letter was issued, but it was shorter and with less reported errors than for 2008/09. The claim was amended, as in previous years.	The improvement seen in 2009/10 has been maintained, although a qualification letter and amendments were required as in 2009/10.

Claim	2009/10	2010/11 to date
Capital receipts pooling	The claim was amended and qualified due to the incorrect calculation of administrative costs.	The same issue has arisen as in 2009/10.
Sure Start	The audit of the claim was problematic. It was submitted late and required both amendments and qualification.	There has been considerable improvement. The claim was submitted to the Department on time with neither amendments nor qualification.
National non-domestic rates	Amendment of £4.1 million was made in 2009/10 due to an error in the treatment of backdated arrears.	A £500k amendment was made, but overall the claim was well-supported.
Single programme	The claim was problematic, being submitted late and qualified.	Considerable improvement has been made. The claim was submitted to the Department on time and with no qualification.
HRA subsidy base data return	The claim was of reasonable quality, but was amended.	No change to 2009/10.
HRA subsidy	The claim was reasonable quality and did not require any amendments or qualification.	The claim was of reasonable quality. Although I issued a qualification letter, this was because I was unable to issue my accounts opinion before the claim deadline.
Teachers pension	The claim was of reasonable quality, but was amended.	The claim was again of reasonable quality and no amendments or qualification were required.

Current and future challenges

Economic downturn and pressure on the public sector

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

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

19 So far, the Council has responded well to these challenges. I have provided added commentary on my assessment of the Council's financial resilience in the value for money section above.

Joint arrangements and shared services

20 Central Government has identified joint arrangement and shared services as a key element in councils reducing their overall costs. The Council has a long-term contract with Vertex for the delivery of many of its services, which constrains its ability to look into shared service arrangements.

Thurrock Thames Gateway Development Corporation (TTGDC)

21 The TTGDC has closed and all the assets, liabilities and functions transferred to the Council on 30 March 2012. This involves the transfer of key roles including full responsibility for planning and also for regeneration and economic development back to the Council, along with the staff working for the TTGDC. The assets and liabilities transferring to the Council are valued at approximately £60 million. This will have a significant impact on the Council's accounts for 2011/12 as well as on its operational and strategic plans. The accounts will have to be produced in line with merger accounting rules, and will therefore need to including restated 2010/11 comparators and be prepared on the basis that the TTGDC had always been part of the Council.

Housing Revenue Account (HRA) self-financing

22 Under the existing housing subsidy system, councils with housing stock have to prepare a notional HRA. This uses a set of predetermined factors for such items as maintenance costs and rental income to reflect the mix and age of the housing stock. In simple terms, if this notional account is in credit then the surplus is payable to central government and if in deficit an equivalent payment is made to the council to support the housing landlord role.

23 The current year, 2011/12, is to be the last year of the existing system. Under a new financing system, councils will be responsible for financing of the HRA, and the existing system of grants and payments will end. To fund this Central Government will make payments to certain local authorities and for local authorities that currently contribute to the scheme, transfer a debt liability. The debt liability transfer for Thurrock is around £161 million, and took place on 28 March 2012.

Localism Bill

24 This Bill received Royal Assent in early 2012 to allow the HRA self-financing proposals discussed earlier to continue. However, the Bill has far-reaching implications for local authorities including:

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

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

Welfare reform

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

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

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

28 The Government has yet to confirm the detailed timescale over which the full move from the existing Housing Benefit and Council Tax Benefit systems to the Universal Credit will take place. However, clearly this will have significant operational and resource implications for the Council.

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

Treasury management

30 I qualified my value for money conclusion because of the increase in the Council's exposure to fluctuations in interest rates following the decision to reschedule all the debt held with PWLB to short term borrowing in August 2010. The transfer of more debt following the closure of the Development Corporation and the changes to the HRA system will also affect the Council's treasury management strategy. It is therefore important that reports to Members set out clearly all potential treasury management costs and risks.

Closing remarks

31 I have discussed and agreed this letter with the Chief Executive and the Director of Finance and Corporate Governance. I will present this letter at the Audit Committee on xx and will provide copies to all Council Members.

32 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
Audit and inspection fee letter	April 2010
Interim audit report	July 2011
Interim annual governance reports	September 2011, November 2011, and December 2011
Annual audit letter	May 2012
Final annual governance report	March 2012 and April 2012
Auditor’s report giving an opinion on the financial statements and value for money conclusion	April 2012

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.

Debbie Hanson
District Auditor

May 2012

Appendix 1 - Fees

	Proposed	Actual	Variance
Audit fee	£328,200	£383,200 (estimated)	£55,000 (estimated)
Total	**£328,200**	**£383,200**	**£55,000**

The proposed audit fee for 2010/11 was £328,200, as set out in my detailed audit plan issued in early 2011.

I raised a number of issues in my Annual Governance report, which have been summarised in this letter, on the extent of issues around the transition to IFRS, the quality of the draft financial statements presented for audit and the weaknesses in supporting working papers. These issues resulted in significant extra audit work being undertaken to gain sufficient audit assurance for opinion purposes. The fee for the audit will therefore be higher than proposed within my audit fee letter. This was discussed and agreed with the Director of Finance and Corporate Governance during September to November 2011. As my audit is not yet complete (Whole of Government Accounts work is outstanding) I cannot yet confirm the exact level of the additional fee, although it is likely to be around £55,000. This additional amount has already been billed to the Council.

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.

If you require a copy of this document in an alternative format or in a language other than English, please call:
0844 798 7070

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