Report of the:	Director of Policy and Resources	Agenda Item No:6	
		Meeting:	12 April 2016

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

EXTERNAL AUDIT REPORTS

1. OBJECT AND KEY POINTS IN THIS REPORT

1.1 To consider external audit's reports:
- External Audit Plan 2015/16
- Certification of Grants and Returns Report 2014/15
- Technical Update and Progress Report; and
- Local Government Budget Survey

2. BACKGROUND INFORMATION

2.1 The Audit Plan 2015/16 (appendix A) provides details of external audit's work required to give an opinion on whether the accounts give a true and fair view and a statutory conclusion on the council's arrangements to secure economy, efficiency and effectiveness. The proposed fee for the audit is £104,138, a 25% reduction on 2014/15. However the fee only provides for basic audit work and does not include items such as challenge from ratepayers or following up detailed audit issues. Some extra costs above the basic fee could be incurred.

2.2 The Certification of Grant Claims and Returns 2014/15 report is attached at appendix B. One recommendation to reduce overpayment errors is included this will be addressed by additional training as required.

2.3 The Technical Update and Progress Report provides the Audit Committee with a summary on progress in delivering external audit's statutory responsibilities. It also highlights key emerging national issues and developments which may be of interest to Members. A copy of the report is attached in appendix C.

2.4 The Budget Survey is designed to support KPMG clients when thinking about the budget information required to help address financial challenges.

3. OPTIONS FOR CONSIDERATION

3.1 The Audit Committee should consider the external auditor's reports and the assurance that has been given or can be implied from their conclusions. The Committee should seek clarification from the external auditors or council officers as necessary.

4. ANALYSIS OF OPTIONS

4.1 The Audit Plan is the result of a risk assessment and complies with statutory requirements governing external audit and inspection work.

5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

5.1 Audit Plan fees of £104,138 are met within existing budgets.

6. OUTCOMES OF INTEGRATED IMPACT ASSESSMENT (IF APPLICABLE)

6.1 An Integrated Impact Assessment is not required.

7. OUTCOMES OF CONSULTATION AND CONFLICTS OF INTERESTS DECLARED

7.1 All reports have been discussed and agreed with the Director of Policy and Resources.

7.2 There are no conflicts of interests to declare.

8. RECOMMENDATIONS

8.1 That the Audit Committee notes the following reports:

- External Audit Plan 2015/16
- Certification of Grants and Returns Report 2014/15
- Technical Update and Progress Report; and
- Local Government Budget Survey

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DIRECTOR OF POLICY AND RESOURCES

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Ashby Road
SCUNTHORPE
North Lincolnshire
DN16 1AB

Author: Carol Andrews
Date: 18 March 2016

Background Papers used in the preparation of this report:
KPMG reports:

- External Audit Plan 2015/16
- Certification of Grants and Returns Report 2014/15
- Technical Update and Progress Report; and
- Local Government Budget Survey

External Audit Plan 2015/2016

North Lincolnshire Council

February 2016

Headlines

Financial Statements Audit

There are no significant changes to the Code of Practice on Local Authority Accounting in 2015/16, which provides stability in terms of the accounting standards the Council needs to comply with.

Materiality

Materiality for planning purposes has been based on last year's expenditure and set at £7.0 million.

We are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance and this has been set at £0.35 million.

Significant risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error have been identified as:

- Implementation of the Financial Services shared service;
- Introduction of a new payroll system at the service provider;
- Management override of Controls; and
- Revenue Recognition.

Other areas of audit focus

We have not identified any risks with less likelihood of giving rise to a material error but which are nevertheless worthy of audit understanding.

See pages 3 to 5 for more details.

Value for Money Arrangements work

The National Audit Office has issued new guidance for the VFM audit which applies from the 2015/16 audit year. The approach is broadly similar in concept to the previous VFM audit regime, but there are some notable changes:

- There is a new overall criterion on which the auditor's VFM conclusion is based; and
- This overall criterion is supported by three new sub-criteria.

Our VFM risk assessment is ongoing. Should any risks arise from our risk assessment, we will report them to officers and the Audit Committee.

See pages 6 to 8 for more details.

Logistics

Our team is as follows:

- John Prentice – Director
- Linda Wild – Manager
- Matthew Moore – Assistant Manager
- Louise Stables – Assistant Manager

More details are on **page 11.**

Our work will be completed in four phases from January to September and our key deliverables are this Audit Plan and a Report to those charged with Governance as outlined on **page 10.**

Our fee for the audit is £104,138 (£138,850 in 2014/2015) - see **page 9.**

Introduction

Background and Statutory responsibilities

This document supplements our Audit Fee Letter 2015/16 presented to you in April 2015, which also sets out details of our appointment by Public Sector Audit Appointments Ltd (PSAA).

Our statutory responsibilities and powers are set out in the Local Audit and Accountability Act 2014 and the National Audit Office's Code of Audit Practice.

Our audit has two key objectives, requiring us to audit/review and report on your:

- *Financial statements (including the Annual Governance Statement):* Providing an opinion on your accounts; and
- *Use of resources:* Concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the value for money conclusion).

The audit planning process and risk assessment is an on-going process and the assessment and fees in this plan will be kept under review and updated if necessary.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

Financial Statements Audit

Our financial statements audit work follows a four stage audit process which is identified below. Appendix 1 provides more detail on the activities that this includes. This report concentrates on the Financial Statements Audit Planning stage of the Financial Statements Audit.

Value for Money Arrangements Work

Our Value for Money (VFM) Arrangements Work follows a five stage process which is identified below. Page 6 provides more detail on the activities that this includes. This report concentrates on explaining the VFM approach for the 2015/16 audit.

Financial Statements Audit Planning

Our planning work takes place during January to February 2016. This involves the following key aspects:

- Risk assessment;
- Determining our materiality level; and
- Issuing this audit plan to communicate our audit strategy.

Risk assessment

Professional standards require us to consider two standard risks for all organisations. We are not elaborating on these standard risks in this plan but consider them as a matter of course in our audit and will include any findings arising from our work in our ISA 260 Report.

- Management override of controls – Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.
- Fraudulent revenue recognition – We do not consider this to be a significant risk for local authorities as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk and do not incorporate specific work into our audit plan in this area over and above our standard fraud procedures.

The diagram opposite identifies, significant risks and other areas of audit focus, which we expand on overleaf. The diagram also identifies a range of other areas considered by our audit approach.

Keys: ● Significant risk ● Other area of audit focus ● Example of other areas considered by our approach

Financial statements audit planning (cont.)

Significant Audit Risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error.

Significant Risk 1 – Implementation of Financial Services Shared Service with North East Lincolnshire Council

- Risk – the Council has agreed that its financial services team is to be part of a shared service from 1st April 2016, alongside neighbouring council North East Lincolnshire. This will mean a new structure and additional pressures for the service to closedown two sets of financial statements. Whilst it is accepted there will be longer term benefits to the Council in the form increased resilience over time and streamlining of accounts and audit processes, at this stage there is a risk that the changes in structure will lead to disruption to, or a reduction in the quality of, the closedown process and production of the accounts and audit working papers.
- Approach – we will discuss the and review the Council's proposed closedown plans with the new shared service team leaders when they have been appointed, this is likely to be part of our interim audit visit. We will agree with the new shared service team a joint approach to the audit across both Authorities to ensure that any accounting or audit issues are identified at the earliest opportunity.

Significant Audit Risks

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error.

Significant Risk 2 – Implementation of new payroll system at the Council's service provider

- Risk – the Council uses East Riding of York Council (ERYC) as its service provider for payroll processing. During 2015/16 ERYC implemented a new payroll system. North Lincolnshire Council operates the controls over inputs to the system and changes to standing data. However there is a risk that data may not have been transferred correctly and completely into the new system at ERYC.
- Approach – we will document the process relating to the system change and we will assess how the Council satisfied itself that the implementation of the new system at ERYC did not cause or create any discrepancies to the Council's output or standing data on the system.

Materiality

We are required to plan our audit to determine with reasonable confidence whether or not the financial statements are free from material misstatement. An omission or misstatement is regarded as material if it would reasonably influence the user of financial statements. This therefore involves an assessment of the qualitative and quantitative nature of omissions and misstatements.

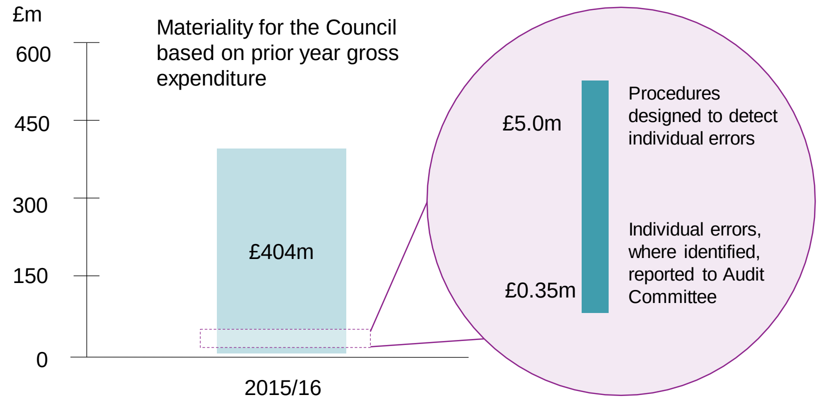
Generally, we would not consider differences in opinion in respect of areas of judgement to represent 'misstatements' unless the application of that judgement results in a financial amount falling outside of a range which we consider to be acceptable.

Materiality for planning purposes has been set at £7.0 million which equates to 1.7 percent of gross expenditure.

We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work.



Under ISA 260(UK&I) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK&I) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

In the context of the Council, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.35 million.

If management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.

Value for money arrangements work

Background to approach to VFM work

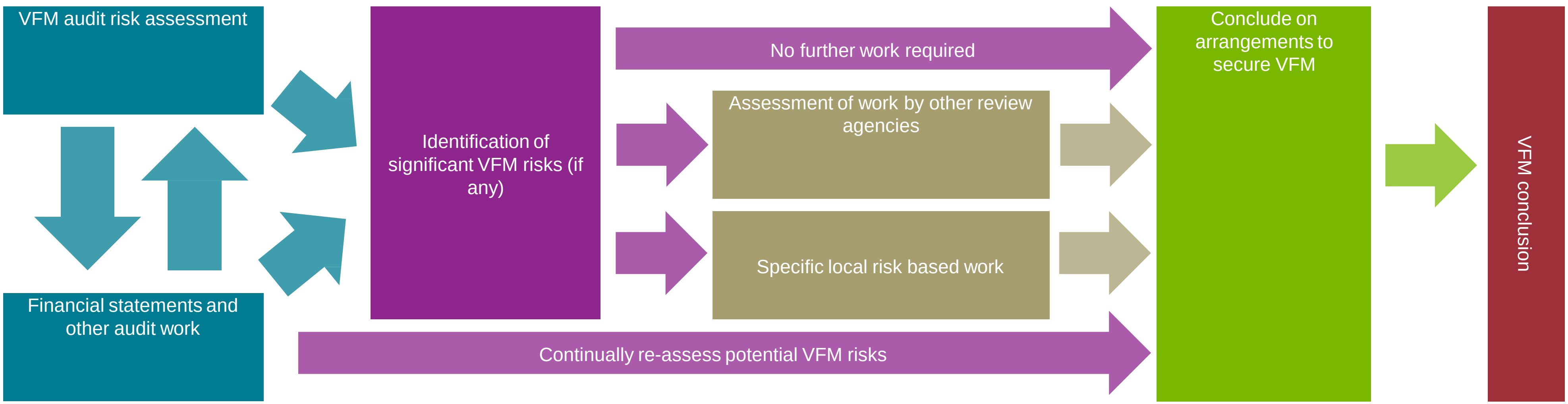
The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the Council 'has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources'.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to 'take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor's judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body's arrangements.'

The VFM approach is fundamentally unchanged from that adopted in 2014/15 and the process is shown in the diagram below. However, the previous two specified reporting criteria (financial resilience and economy, efficiency and effectiveness) have been replaced with a single criterion supported by three sub-criteria. These sub-criteria provide a focus to our VFM work at the Council. The diagram to the right shows the details of these criteria.

Overall criterion

In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.



Value for money arrangements work (cont.)

VFM audit stage	Audit approach
VFM audit risk assessment	We consider the relevance and significance of the potential business risks faced by all local authorities, and other risks that apply specifically to the Council. These are the significant operational and financial risks in achieving statutory functions and objectives, which are relevant to auditors' responsibilities under the *Code of Audit Practice.* In doing so we consider: ■ The Council's own assessment of the risks it faces, and its arrangements to manage and address its risks; ■ Information from the Public Sector Auditor Appointments Limited VFM profile tool; ■ Evidence gained from previous audit work, including the response to that work; and ■ The work of other inspectorates and review agencies.
Linkages with financial statements and other audit work	There is a degree of overlap between the work we do as part of the VFM audit and our financial statements audit. For example, our financial statements audit includes an assessment and testing of the Council's organisational control environment, including the Council's financial management and governance arrangements, many aspects of which are relevant to our VFM audit responsibilities. We have always sought to avoid duplication of audit effort by integrating our financial statements and VFM work, and this will continue. We will therefore draw upon relevant aspects of our financial statements audit work to inform the VFM audit.
Identification of significant risks	The Code identifies a matter as significant *'if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public. Significance has both qualitative and quantitative aspects.'* If we identify significant VFM risks, then we will highlight the risk to the Council and consider the most appropriate audit response in each case, including: ■ Considering the results of work by the Council, inspectorates and other review agencies; and ■ Carrying out local risk-based work to form a view on the adequacy of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources.

Value for money arrangements work (cont.)

VFM audit stage	Audit approach
Assessment of work by other review agencies and **Delivery of local risk based work**	Depending on the nature of the significant VFM risk identified, we may be able to draw on the work of other inspectorates, review agencies and other relevant bodies to provide us with the necessary evidence to reach our conclusion on the risk. If such evidence is not available, we will instead need to consider what additional work we will be required to undertake to satisfy ourselves that we have reasonable evidence to support the conclusion that we will draw. Such work may include: ■ Meeting with senior managers across the Council; ■ Review of minutes and internal reports; ■ Examination of financial models for reasonableness, using our own experience and benchmarking data from within and without the sector.
Concluding on VFM arrangements	At the conclusion of the VFM audit we will consider the results of the work undertaken and assess the assurance obtained against each of the VFM themes regarding the adequacy of the Council's arrangements for securing economy, efficiency and effectiveness in the use of resources. If any issues are identified that may be significant to this assessment, and in particular if there are issues that indicate we may need to consider qualifying our VFM conclusion, we will discuss these with management as soon as possible. Such issues will also be considered more widely as part of KPMG's quality control processes, to help ensure the consistency of auditors' decisions.
Reporting	We will report on the results of the VFM audit through our ISA 260 Report. This will summarise any specific matters arising, and the basis for our overall conclusion. The key output from the work will be the VFM conclusion (i.e. our opinion on the Council's arrangements for securing VFM), which forms part of our audit report.

Our VFM risk assessment is ongoing. Should any risks arise from our risk assessment, we will report them to officers and the Audit Committee.

Other matters

Whole of government accounts (WGA)

We are required to review your WGA consolidation and undertake the work specified under the approach that is agreed with HM Treasury and the National Audit Office. Deadlines for production of the pack and the specified approach for 2015/16 have not yet been confirmed.

Elector challenge

The Local Audit and Accountability Act 2014 gives electors certain rights. These are:

- The right to inspect the accounts;
- The right to ask the auditor questions about the accounts; and
- The right to object to the accounts.

As a result of these rights, in particular the right to object to the accounts, we may need to undertake additional work to form our decision on the elector's objection. The additional work could range from a small piece of work where we interview an officer and review evidence to form our decision, to a more detailed piece of work, where we have to interview a range of officers, review significant amounts of evidence and seek legal representations on the issues raised.

The costs incurred in responding to specific questions or objections raised by electors is not part of the fee. This work will be charged in accordance with the PSAA's fee scales.

Our audit team

Our audit team will be led by John Prentice and managed by Linda Wild. This provides the Council with continuity on the audit. Appendix 2 provides more details on specific roles and contact details of the team.

Reporting and communication

Reporting is a key part of the audit process, not only in communicating the audit findings for the year, but also in ensuring the audit team are accountable to you in addressing the issues identified as part of the audit strategy. Throughout the year we will communicate with you through meetings with the finance team and the Audit Committee. Our communication outputs are included in Appendix 1.

Independence and Objectivity

Auditors are also required to be independent and objective. Appendix 3 provides more details of our confirmation of independence and objectivity.

Audit fee

Our Audit Fee Letter 2015/2016 presented to you in April 2015 first set out our fees for the 2015/16 audit. This letter also sets out our assumptions. We have not considered it necessary to make any changes to the agreed fees at this stage.

The planned audit fee 2015/16 is £104,138 This is a reduction in audit fee, compared to 2014/15, of £138,850 (25%).

Our audit fee includes our work on the VFM conclusion and our audit of the Council's financial statements.

Appendix 1: Key elements of our financial statements audit approach

Communication

Continuous communication involving regular meetings between Audit Committee, Senior Management and audit team

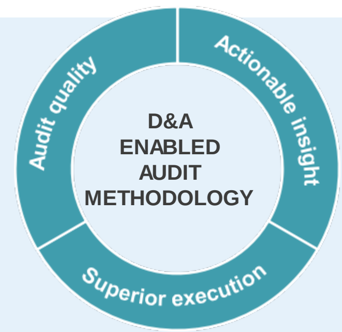
- Audit strategy and plan
- Interim report (if required)
- ISA 260 (UK&I) Report
- Annual Audit Letter

Jan Feb Mar Apr May Jun Jul Aug Sep Oct Nov Dec

Audit workflow

- Initial planning meetings and risk assessment
- Interim audit
- Year end audit of financial statements and annual report
- Sign audit opinion

Planning	Control evaluation	Substantive testing	Completion
■ Perform risk assessment procedures and identify risks ■ Determine audit strategy ■ Determine planned audit approach	■ Understand accounting and reporting activities ■ Evaluate design and implementation of selected controls ■ Test operating effectiveness of selected controls ■ Assess control risk and risk of the accounts being misstated	■ Plan substantive procedures ■ Perform substantive procedures ■ Consider if audit evidence is sufficient and appropriate	■ Perform completion procedures ■ Perform overall evaluation ■ Form an audit opinion ■ Audit Committee reporting



Driving more value from the audit through data and analytics

Technology is embedded throughout our audit approach to deliver a high quality audit opinion. Use of Data and Analytics (D&A) to analyse large populations of transactions in order to identify key areas for our audit focus is just one element. We strive to deliver new quality insight into your operations that enhances our and your preparedness and improves your collective 'business intelligence.' Data and Analytics allows us to:

- Obtain greater understanding of your processes, to automatically extract control configurations and to obtain higher levels assurance.
- Focus manual procedures on key areas of risk and on transactional exceptions.
- Identify data patterns and the root cause of issues to increase forward-looking insight.

We anticipate using data and analytics in our work around key areas such as accounts payable and journals. We also expect to provide insights from our analysis of these tranches of data in our reporting to add further value from our audit.

Appendix 2: Audit team

Your audit team has been drawn from our specialist public sector assurance department. You have a new Assistant Manager who will co-ordinate the audit alongside the shared financial services with North East Lincolnshire Council; the remainder of the team is the same team as last year, to provide continuity.

Name	John Prentice
Position	Director ‘My role is to lead our team and ensure the delivery of a high quality, valued added external audit opinion. I will be the main point of contact for the Audit Committee and Chief Executive.

John Prentice
Director
0113 2313935 / 07827 939020
john.prentice@kpmg.co.uk

Name	Linda Wild
Position	Manager ‘I provide quality assurance for the audit work and specifically any technical accounting and risk areas. I will work closely with John, the Director, to ensure we add value. I will liaise with the Director of Policy and Resources and other Executive Directors.’

Linda Wild
Manager
0113 2313512 / 07717 483538
linda.wild@kpmg.co.uk

Name	Matthew Moore
Position	Assistant Manager ‘Working closely with Louise, I will be responsible for the on-site delivery of our work and will supervise the work of our audit assistants.’

Matthew Moore
Assistant Manager
0113 2313663 / 07468 369807
matthew.moore@kpmg.co.uk

Name	Louise Stables
Position	Assistant Manager ‘Working closely with Matthew, I will be responsible for the on-site delivery of our work and will supervise the work of our audit assistants.’

Louise Stables
Assistant Manager
0113 2314747 / 07880 052693
louise.stables@kpmg.co.uk

Appendix 3: Independence and objectivity requirements

Independence and objectivity

Professional standards require auditors to communicate to those charged with governance, at least annually, all relationships that may bear on the firm's independence and the objectivity of the audit engagement partner and audit staff. The standards also place requirements on auditors in relation to integrity, objectivity and independence.

The standards define 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case this is the Audit Committee.

KPMG LLP is committed to being and being seen to be independent. APB Ethical Standard 1 Integrity, Objectivity and Independence requires us to communicate to you in writing all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place which, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and the audit team.

Further to this auditors are required by the National Audit Office's Code of Audit Practice to:

- Carry out their work with integrity, independence and objectivity;
- Be transparent and report publicly as required;
- Be professional and proportional in conducting work;
- Be mindful of the activities of inspectorates to prevent duplication;
- Take a constructive and positive approach to their work;
- Comply with data statutory and other relevant requirements relating to the security, transfer, holding, disclosure and disposal of information.

PSAA's Terms of Appointment includes several references to arrangements designed to support and reinforce the requirements relating to independence, which auditors must comply with. These are as follows:

- Auditors and senior members of their staff who are directly involved in the management, supervision or delivery of PSAA audit work should not take part in political activity.
- No member or employee of the firm should accept or hold an appointment as a member of an audited body whose auditor is, or is proposed to be, from the same firm. In addition, no member or employee of the firm should accept or hold such appointments at related bodies, such as those linked to the audited body through a strategic partnership.
- Auditors and their staff should not be employed in any capacity (whether paid or unpaid) by an audited body or other organisation providing services to an audited body whilst being employed by the firm.
- Auditors appointed by the PSAA should not accept engagements which involve commenting on the performance of other PSAA auditors on PSAA work without first consulting PSAA.
- Auditors are expected to comply with the Terms of Appointment policy for the Engagement Lead to be changed on a periodic basis.
- Audit suppliers are required to obtain the PSAA's written approval prior to changing any Engagement Lead in respect of each audited body.
- Certain other staff changes or appointments require positive action to be taken by Firms as set out in the Terms of Appointment.

Confirmation statement

We confirm that as of January 2016, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Engagement Lead and audit team is not impaired.

This report is addressed to the Council and has been prepared for the sole use of the Council. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. We draw your attention to the Statement of Responsibilities of auditors and audited bodies, which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact John Prentice, the engagement lead to the Council, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers, by email to Andrew.Sayers@kpmg.co.uk After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

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KPMG

cutting through complexity

KPMG Annual Report on grants and returns work 2014/15

North Lincolnshire Council

February 2016

Contents

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Matthew Moore
Assistant Manager

Tel: 0113 231 3663
matthew.moore@kpmg.co.uk

This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. We draw your attention to the Statement of Responsibilities of auditors and audited bodies, which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact John Prentice, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers, by email to andrew.sayers@kpmg.co.uk. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

Headlines

Introduction and background	**This report summarises the results of work we have carried out on the Council's 2014/15 grant claims and returns.** **This includes the work we have completed under the Public Sector Audit Appointment certification arrangements, as well as the work we have completed on other grants/returns under separate engagement terms. The work completed in 2014/15 is:** ■ Under the Public Sector Audit Appointment arrangements we certified one claim – the Council's 2014/15 Housing Benefit Subsidy claim. This had a value of £46,080,546 (subsidy claimed). ■ Under separate assurance engagements we certified two claims/returns as listed below: – Teachers Pensions Return which had a value of contributions paid of £6,225,132; and – National College of Training and Leadership Annual Grant where the grant certified was £45,000.	
Certification results	**Our work on the Council's Housing Benefit Subsidy Claim was subject to a qualification letter.** ■ Testing of Rent Allowances identified one error where the classification of an overpayment was incorrect; further testing identified an additional seven errors. The extrapolated overpayment error was overstated by £40,865 in cell 114, and understated by £40,865 in cell 113. ■ The issue above was not amended in the claim but reported in the qualification letter. **Our work on the other grant assurance engagements resulted in the following reports:** ■ Both engagements resulted in a clear report with no amendments or qualifications	**Pages 3 – 4**
Audit adjustments	**An adjustment was necessary to one of the Council's grants and returns as a result of our certification work this year.** ■ During the audit the Housing Benefit subsidy claim was amended which led to the Authority receiving £1,324 more subsidy for Non-HRA Rent Rebates and £22,335 less subsidy for Rent Allowances; and ■ These are similar adjustments to those that have been made to previous years claims.	**Pages 3 – 4**
Fees	**The indicative fee for our work on the Council's 2014/15 Housing Benefit Subsidy Claim was set by Public Sector Audit Appointments at £20,820 (exc VAT). The actual fee for this work was £20,820 (exc VAT).** **Our fees for the other 'assurance' engagements were subject to agreement directly with the Council and were:** ■ Teachers Pensions Return – fee agreed £3,500 (exc VAT); and ■ National College of Training and Leadership Annual Grant – fee agreed £3,500 (exc VAT).	**Page 5**

Summary of reporting outcomes

Overall, we carried out work on three grants and returns:

- **Two were unqualified with no amendment; and**
- **one required a qualification to our audit certificate due to minor errors.**

Detailed comments are provided overleaf.

Detailed below is a summary of the reporting outcomes from our work on the Council's 2014/15 grants and returns, showing where either audit amendments were made as a result of our work or where we had to qualify our audit certificate or assurance report.

A qualification means that issues were identified concerning the Council's compliance with a scheme's requirements that could not be resolved through adjustment. In these circumstances, it is likely that the relevant grant paying body will require further information from the Council to satisfy itself that the full amounts of grant claimed are appropriate.

	Comments overleaf	Qualified	Significant adjustment	Minor adjustment	Unqualified
Public Sector Audit Appointments arrangements					
■ Housing Benefit Subsidy	1	●		●	
Other assurance engagements					
■ Teachers Pensions Return					●
■ National College of Training and Leadership Annual Grant					●
		1	0	1	2

Summary of certification work outcomes

This table summarises the key issues behind each of the adjustments or qualifications that were identified on the previous page.

Ref	Summary observations	Amendment
1	**Housing Benefits Subsidy** ■ Testing of Rent Allowances identified one error where the evidence showed the reason for the overpayment as LA/Admin error and not an eligible overpayment, further testing identified an additional seven errors. The extrapolated error affected cell 114, which was overstated by £40,685 and cell 113, which was understated by £40,685. These errors were not adjusted in the claim but reported in the Qualification Letter. ■ During the audit of the Housing Benefit Subsidy, the claim was amended which led to the Authority receiving £1,324 more subsidy for Non-HRA Rent Rebates and £22,335 less subsidy for Rent Allowances; and ■ These adjustments were made due to the system generated reports which identifies potential claims where the subsidy claimed may be incorrect. The Council reviews these claims following the initial submission.	**- £21,011**

Fees

Our fees for the Housing Benefit Subsidy Claim are set by Public Sector Audit Appointments (and previously the Audit Commission).

Our fees for other assurance engagements on grants/ returns are agreed directly with the Council.

The overall fees we charged for carrying out all our grants/returns work in 2014/15 was £27,820 (exc VAT)

Breakdown of fees for grants and returns work

Breakdown of fee by grant/return	2014/15 (£)	2013/14 (£)
Housing Benefit Subsidy claim	20,820	17,880
Teachers Pensions Return	3,500	4,000
National College of Training and Leadership Annual Grant	3,500	3,500
Total fee	**27,820**	**25,380**

All fees are exclusive of VAT.

Public Sector Audit Appointments certification arrangements

Public Sector Audit Appointments (and previously the Audit Commission) set an indicative scale fee for our work on the Council's Housing Benefit Subsidy Claim in 2014/15 of £20,820 (exc VAT). Our actual fee was the same as the indicative scale fee, and this compares to the 2013/14 scale fee for this claim of £17,880.

Grants subject to other assurance engagements

The fees for our assurance work on other grants/returns are agreed directly with the Council. Our fees for 2014/15 were in line with those in 2013/14. However, there was a small reduction of £500 (exc VAT) in the agreed fee for the Teachers Pensions Return to reflect additional planning costs incurred in 2013/14.

Recommendations

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority rating for recommendations		
❶ Issues that are fundamental and material to your overall arrangements for managing grants and returns or compliance with scheme requirements. We believe that these issues might mean that you do not meet a grant scheme requirement or reduce (mitigate) a risk.	❷ Issues that have an important effect on your arrangements for managing grants and returns or complying with scheme requirements, but do not need immediate action. You may still meet scheme requirements in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸ Issues that would, if corrected, improve your arrangements for managing grants and returns or compliance with scheme requirements in general, but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

Issue	Implication		Recommendation	Priority	Comment	Responsible officer and target date
Housing Benefit subsidy						
Overpayment Classification A number of errors of overpayment classification were identified in the testing which led to the Qualification Letter issue.	Currently the incorrect classification of some overpayments means that the Authority is missing out on additional subsidy. In addition, there is a risk that these errors could exceed the LA/Admin threshold leading to a potential loss of subsidy (£118,747 in 2014/15).	1	The Authority should review the errors identified and provide any additional training to the assessors to try and minimise the risk of error. The Authority should carry out sample testing of the cell 114 overpayment cases to ensure that these are correctly classified as eligible overpayments.	❶	Overpayment classification already formed part of our general quality checking routine. As a result of this qualification we now complete additional targeted checks specifically on overpayments created on a daily basis. As a result of the individual feedback we have given from this, we have seen a marked improvement in performance. Additional guidance and support has also been issued to all team members as well as raising the profile of this issue through 1-2-1 and team discussions.	**Responsible Officer** Cindy Laherty, Lead Officer Benefits **Target Date** 31 March 2016

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External audit progress report and technical update

North Lincolnshire Council

April 2016

External audit progress report and technical update – April 2016

This report provides the audit committee with an overview on progress in delivering our responsibilities as your external auditors.

The report also highlights the main technical issues which are currently having an impact in local government.

If you require any additional information regarding the issues included within this report, please contact a member of the audit team.

We have flagged the articles that we believe will have an impact at the Authority and given our perspective on the issue:

- 🔴 **High impact**
- 🟡 **Medium impact**
- 🟢 **Low impact**
- ⚪ **For info**

Progress report

External audit progress report – April 2016

This document provides the audit committee with a high level overview on progress in delivering our responsibilities as your external auditors.

At the end of each stage of the audit we issue certain deliverables, including reports and opinions. A summary of progress against these deliverable is provided in Appendix 1 of this report.

Area of responsibility	Commentary
Planning	*Our planning for 2015/16 is complete. We agreed the Audit Plan with officers in February 2016 and this is being presented to the Audit Committee on today's agenda.*
Financial statements	*We will update this section when we complete the 2015/16 Interim Audit, which is taking place in March 2016.*
Value for Money	*We will update this section when we complete the 2015/16 Interim Audit, which is taking place in March 2016.*
Certification of claims and returns	*We have completed our work on the Council's 2014/15 Housing Benefit and Subsidy Claim. This is the only grant claim to remain under the PSAA regime.* *We have also completed the audit of the following grant claims and returns which fall outside of the PSAA regime:* • *Teacher's Pensions Agency (TPA) Return; and* • *National College for Teaching and Leadership (NCTL) Annual Grant Report and Initial Teacher Training Statements of Income and Expenditure.* *A separate grants report on the above was agreed with officers February 2016 and is presented to the Audit Committee on today's agenda.* *Our work on the Council's 2015/16 Housing Benefit and Subsidy Claim will commence in the Summer of 2015 and will be completed before the deadline of 30th November 2016.*
Other work	*During 2015/16 we have engaged with the Council to carry out the following pieces of additional work:* • *TPA and NCTL grant claims and returns, fees £3,500 each (exc VAT) (see above);* • *Provision of two workshops in relation to the Shared Services, fees £2,000 each (exc VAT); and* • *Review of residential care costs, fees £41,400 (exc VAT).*

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KPMG resources

KPMG resources

Area	Comments
KPMG Local Government Budget Survey	KPMG has recently published the results of its Local Government Budget Survey. The survey collated data from 97 KPMG local authority clients on topics including: ■ The content of budget monitoring reports; ■ Savings plans; ■ Invest-to-save projects; ■ The type of savings being made; ■ Assumptions underlying the medium term financial plan; and ■ Reserve movements. The Survey also poses questions for management and members to consider when reviewing their budget setting and budget monitoring processes. A copy of the report showing the results of the Survey will be presented to the Audit Committee on today's agenda.

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Technical update

Area	Level of Impact	Comments	KPMG perspective
The LGA's 2015 Spending Review submission	**Medium**	In June 2015, the Local Government Association (LGA) set out proposals for the Government to consider as part of the Spending Review, aimed at streamlining public services, growth generating investment and social care and health – all while saving the public purse almost £2 billion a year by the end of the Parliament. The submission focusses on five core issues originally highlighted in *A Shared Commitment* (www.local.gov.uk/documents/10180/6869714/L15-252+Spending+Review_WEB_new.pdf/3101e509-1e22-4c26-91ac-8fd8a953aba5), published in early 2015. The LGA hopes that local government can work with central government to balance the nation's books while improving public services and the local economic environment by delivering new, transformed and high-quality local services while at the same time reducing costs to the public sector. The LGA believes the Spending Review should: ▪ enable wider integration of social care and health services to deliver savings and improve outcomes This requires the annual £700 million funding gap in social care services to be closed and a transformation fund worth £2 billion in each year of the Spending Review period be created to allow new ways of working to become commonplace. The Spending Review should also implement a single place-based budget for delivering all local services through a Local Public Services Fund as part of at least five devolution deals; ▪ promote growth and productivity by accepting the case for further devolution of powers and funding that stretches beyond 25 November. The LGA is calling for devolution of, or local influence over, more than £60 billion of growth, skills and infrastructure funding over the Spending Review period, including: – the components for an ambitious and effective Local Growth Fund with agreed settlements in devolution deals that last until 2020/21 – a central-local partnership to deliver effective and targeted skills and employment initiatives – unlocking the ability of councils to contribute to the Government's target of 275,000 affordable homes built over the lifetime of the Parliament. ▪ help councils adequately resource and deliver high quality public services by transforming the business rate mechanism and providing a four year local government finance settlement; and ▪ help councils focus on driving efficiency and value for money through an assessment of the impact of unfunded cost burdens that core council budgets are going to face over the Spending Review period.	***The Committee may wish to seek assurances that the impact for their Authority is understood.***

Area	Level of impact	Comments	KPMG perspective
DCLG consultation on pension fund investment reform	Low	The Department for Communities and Local Government (DCLG) has recently closed a consultation on revised regulations for the investment of local government pension scheme assets. The proposed regulations include the proposal to allow pension schemes to pool assets for investment purposes. The revised regulations can be found here at www.gov.uk/government/publications/local-government-pension-scheme-investment-reform-criteria-and-guidance The outcome of the consultation will be published here: https://www.gov.uk/government/consultations/revoking-and-replacing-the-local-government-pension-scheme	***The Committee may wish to enquire of officers whether their Authority responded to the consultation and the views expressed.***
CIPFA briefings on accounting for highways infrastructure assets	Low	CIPFA has published the first of a series of briefings on highways infrastructure assets. The first briefing focuses on the decisions made by CIPFA/LASAAC Local Authority Accounting Board following its consultation on the *Code of Practice on Local Authority Accounting in the United Kingdom 2016/17*. The briefing also covers the applicability of the measurement requirements for district councils and the resources available to support the implementation process. In particular the briefing notes: ■ the change to recognising the assets using the depreciated replacement cost approach will be prospective, so will not require the 2015/16 accounts to be restated; and ■ district councils are unlikely to meet the definition of having a single highways network asset, although they will need to reach their own view on this. The first briefing can be found at www.cipfa.org/~/media/files/policy%20and%20guidance/local%20authority%20transport%20infrastructure/final%20briefing%20hna%20no%201.pdf?la=en	***The Committee may wish to seek assurances how their Authority is progressing with the new requirements.***

Area	Level of Impact	Comments	KPMG perspective
2015/16 Code of Practice on Local Authority Accounting in the United Kingdom (the Code) – update	Low	CIPFA/LASAAC has issued an update to the *2015/16 Code of Practice on Local Authority Accounting in the United Kingdom* (the Code) following its consultation process. The 2015/16 Code update should be read alongside the 2015/16 Code published in April 2015. Authorities should note that the update confirms the transitional reporting requirements for the measurement of the Highways Network Asset. The Code does not require a change to the preceding year information for the move to measuring the Highways Network Asset at current value (and under that provision would not require a change to the balance sheet information at 1 April 2015). It also does not require a restatement of the opening 1 April 2016 information but there will need to be an adjustment to those balances. The Code update also includes amendments as a result of legislative changes and particularly the *Accounts and Audit Regulations 2015* for English authorities. It specifies the principles for narrative reporting which CIPFA/LASAAC considers should be used to meet the new requirements of those regulations.	***The Committee may wish to seek assurances that their Authority is aware of the update to the 2015/16 Code.***

Area	Level of Impact	Comments	KPMG perspective
Capital receipts flexibility	Low	The 2015 Spending Review included an announcement that local authorities would be able to use capital receipts on the revenue costs of service reform projects. The Department for Communities and Local Government (DCLG) has now issued guidance on the capital receipts flexibility, including a draft direction setting out the types of project that would qualify and expected governance and transparency framework. In summary: ▪ the flexibility is available from 1 April 2016 to 31 March 2019; ▪ only capital receipts generated during that period can be used for the flexibility; ▪ the Secretary of State's direction will have the effect of allowing authorities to treat revenue expenditure on service reform as capital during the three year period; ▪ authorities will not be allowed to borrow to fund revenue expenditure on service reform; and ▪ authorities are required to have regard to a statutory code which contains certain transparency requirements when taking advantage of the flexibility. We understand that DCLG's aim was that the final signed direction would be issued with the final settlement in February 2016. A copy of the draft guidance can be found at www.gov.uk/government/uploads/system/uploads/attachment_data/file/486999/Capital_receipts_flexibility_-_draft_statutory_guidance_and_direction.pdf	***The Committee may wish to seek assurances how their Authority is planning to use the new flexibility.***
Better Care Fund policy framework 2016/17	Low	The Department of Health, in conjunction with the Department for Communities and Local Government, has recently published *2016-17 Better Care Fund planning guidance*. The guidance introduces a number of changes, requiring local clinical commissioning groups (CCGs), councils and providers to establish risk sharing arrangements to fund unplanned emergency admissions. Local areas will also have to agree to 'stretching' local targets for cutting delayed transfers of care supported by an action plan. The guidance can be found here: www.gov.uk/government/publications/better-care-fund-how-it-will-work-in-2016-to-2017	***The Committee may wish to seek assurances how their Authority is developing these arrangements.***

Area	Level of Impact	Comments
Greater Manchester Combined Authority	For Information	Greater Manchester Combined Authority (GMCA) has pioneered the concept of local devolution within England. 'Devo Manc" encompasses a broad range of proposals to address the challenges and opportunities GM is facing: **Health and Social Care** Greater Manchester is facing an estimated financial deficit of c. £2 billion by 2020/21. A Memorandum of Understanding was signed in February 2015 between all partners in GM, committing the region to produce a comprehensive Strategic and sustainable Plan for health and social care. As part of the Plan, GM is seeking to use its share of the £8 billion promised to the NHS in the CSR to support new recurrent costs and protect social care budgets, closing over a quarter of the funding gap. A further investment by the partners of £500 million, phased over three years, will release future recurrent savings with a likely payback of £3 for every £1 invested. **GM proposals** In addition, GM has made a number of proposals to reform the way public services work together and deliver services within the region: ■ Investment in transport infrastructure ■ New funding mechanisms to support site remediation and infrastructure provision ■ Making better use of Social Housing Assets to support growth ■ Locally led low carbon emissions ■ A scaled-up GM Reform Investment Fund ■ Devolution of decision making for apprenticeships and training, and reform to careers advice and guidance ■ Fundamental review of the way services to children are delivered ■ Research and innovation funding ■ Investment in integrated business support to drive growth and productivity ■ Reform of the New Homes Bonus ■ Further employment and skills reform ■ GM approach to data sharing across public agencies ■ Fiscal devolution, including reform to Business Rates, Council Tax, Stamp Duty Land Tax and a Hotel Bed Tax All of these proposals involve joint working, not just with other GM agencies, but also central government departments. This allows the existing financial resources provided to the region to be redeployed more efficiently to maximise the benefits to GM.

Area	Level of Impact	Comments
Joint report by CIPFA and HFMA: *The Better Care Fund – six months on*	**For Information**	Authorities may wish to be aware of a recent joint report by CIPFA and the Healthcare Financial Management Association (HFMA) examining the progress that has been made six months into the implementation of Better Care Fund arrangements. The report is based on the results of an HFMA and CIPFA joint finance staff survey of NHS bodies and local authorities representing almost a third of BCF sites. The report can be found on the CIPFA website at www.cipfa.org/about-cipfa/press-office/latest-press-releases/better-care-fund-struggling-with-red-tape
Cities and Local Government Devolution Act 2016	**For Information**	Authorities will wish to note that the Cities and Local Government Devolution Act 2016 received Royal Assent on 28 January 2016. The Act provides the enabling legislation to: ■ allow for the election of mayors for a combined authority area; ■ allow for the devolution of functions, including transport, health, skills, planning and job support; and ■ provide a power to establish sub-national transport bodies which will advise the Government on strategic schemes and investment priorities in their own area. Most of the changes under the Act, including the implementation of 'devolution' deals, will be implemented by Orders to be made under the Act.
PSAA update – VFM profiles March 2016 release	**For Information**	Public Sector Audit Appointments Ltd (PSAA) updated its Value for Money Profiles Tool (VFM profiles) on 3 February 2016. The VFM profiles have been updated with the 2014-15 data sourced from the Department for Communities and Local Government – General Fund Revenue Outturn Budget (RO). The values are adjusted with gross domestic product (GDP) deflators from HM Treasury's publication in November 2015. The profiles can be accessed through the PSAA website at www.psaa.co.uk/

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Appendix

Appendix 1 – 2015/16 Audit deliverables

Deliverable	Purpose	Timing	Status
Planning			
Fee letter	Communicate indicative fee for the audit year	April 2015	Complete
External audit plan	Outline our audit strategy and planned approach Identify areas of audit focus and planned procedures	February 2016	Complete
Interim			
Interim report (if required)	Details and resolution of control and process issues. Identify improvements required prior to the issue of the draft financial statements and the year-end audit. Initial VFM assessment on the Council's arrangements for securing value for money in the use of its resources.	March/April 2016	TBC
Substantive procedures			
Report to those charged with governance (ISA+260 report)	Details the resolution of key audit issues. Communication of adjusted and unadjusted audit differences. Performance improvement recommendations identified during our audit. Commentary on the Council's value for money arrangements.	September 2016	TBC
Completion			
Auditor's report	Providing an opinion on your accounts (including the Annual Governance Statement). Concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the VFM conclusion).	September 2016	TBC
WGA	Concluding on the Whole of Government Accounts consolidation pack in accordance with guidance issued by the National Audit Office.	September 2016	TBC
Annual audit letter	Summarise the outcomes and the key issues arising from our audit work for the year.	November 2016	TBC
Certification of claims and returns			
Certification of claims and returns report	Summarise the outcomes of certification work on your claims and returns for Government departments.	December 2016	TBC

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Local Government Budget Survey

February 2016

www.kpmg.com/uk

Contents

Introduction

Introduction

The local government sector faces well-documented, significant financial challenges for the foreseeable future. There are also opportunities linked to economic growth, notably with the new homes bonus and the prospect of local business rates retention, and the potential devolution of power to local areas. There is also an increased exposure to financial risk and volatility if growth is not as high or as sustained as hoped, or if demands for services outstrip expectations and lead to additional pressures. There is also the challenge of responding to the impact of central policies such as the 1% reduction in social housing rents from 2016-17, and the increased emphasis on home ownership rather than social renting. In this changing environment, high quality budget setting and monitoring are more important than ever for local government.

KPMG's 2011 publication 'The Brilliant Local Authority of the future' summarised the challenge facing local authorities.

"As the public sector recession bites and the localism agenda gathers pace, local government will have to address both the threats and opportunities that these forces are creating."

The paper explained that;

"In an age of austerity an iron-like grip on the organisation's financial position will be imperative….. This will entail a focus on management accounting and understanding the financial and operational performance of all parts of the business".

https://portal.ema.kworld.kpmg.com/audit/countries/europe/AuditPeople/DeptSites/IGHAudit/Technical%20guidance%20Library/RRD254220%20Brilliant%20Local%20Authority_v11.pdf

KPMG is proud to be the external auditor of a significant number of local government clients, and our audit teams consider key aspects of budget setting and budget monitoring alongside their external audit work. This paper sets out the results of a survey they completed in 2015, and analyses the assumptions and techniques used by our clients to generate budgets and to monitor them.

Our audit teams were very aware that when our clients were setting the 2015-16 budgets they were waiting for clarity about their funding for future years. Some clients had chosen not to publish a medium term financial plan until there was more certainty. Where this was the case, we took into account the work that officers were doing in preparation of the Comprehensive Spending Assessment.

Purpose of this paper

Our aim is that our clients find this paper useful when thinking about the budget information required to help address the financial challenges that they face. We hope that it will help our clients to take a fresh look at their approach to budget setting and monitoring. As financial risks and rewards continue to be localised, budgets will need to become more and more flexible and responsive to changes within financial years. We recognise that there is no single solution or blueprint for successful budgetary control, and that it is up to each client to find their own balance of summarised information and detailed data.

We plan to carry out a similar review next year. We would welcome feedback on this first version, and if there are any areas that you think that it would be useful to cover please let us know. Please let your local audit team know if you have any feedback or if there is anything you want us to take into account.

Introduction (cont.)

Our clients

We have analysed the 97 survey responses from our audit teams.

Client Type	Responses
Districts	41
London Boroughs	11
Unitary Authorities	11
Metropolitan Boroughs	10
Police & Crime Commissioners	8
Fire & Civil Defence Authorities	7
Counties	6
Transport Executives	2
Combined Authority	1
Total	**97**

Report Format

The paper provides the results of the responses, along with a brief analysis of the highlights (including extra information that audit teams provided where appropriate). We have also provided some possible questions that Members may wish to consider in the context of their own organisations. These questions are collated at the end of the report for ease of reference.

Key messages

We know that our local government clients have already taken significant steps to deal with the changes in their funding structure over the last few years. This paper highlights that as the financial challenges increase over the next few years there are measures that our clients can consider using in order to strengthen elements of their budget preparation, analysis, monitoring and reporting.

The move to more localised risks and rewards mean that techniques such as sensitivity analyses (to identify pressure points) and financial ratios will be key as the potential for financial volatility in the sector increases. This volatility in income and expenditure could happen at any time as well as on the annual budget-setting process, and so it is also increasingly important that our clients are alert and responsive to changes within the year, and to indications that their budgetary assumptions are no longer valid.

Tracking the achievement of savings is not straightforward. Sometimes plans need to be shelved for positive reasons – for example when there is unexpected demand for a service that generates income. It is important to identify the reasons for successful plans as well as those that fail in order to learn for the future.

The likely link between local growth and our clients' financial well-being means that selecting the right 'invest-to-save' schemes is vital, and the survey suggests that more use could be made of key processes for assessing the potential projects.

As financial pressures increase, savings measures may need to be re-considered or revisited, alongside ways to generate income.

As savings become harder to achieve, the distinction between recurrent and non-recurrent savings becomes ever more important, and also an important element of reporting to members. The General Fund Reserve is a critical safety net, and setting the minimum level is a key task that should take into account the level and nature of usable reserves, and in particular if there is a lack of flexibility within those other reserves.

The results of our survey highlight differences in the way that our clients are budgeting for key financial factors such as inflation, borrowing and lending rates and employee related cost pressures. Similarly, there is variation in the factors used to generate the budget, with some such as demographics and population change less used than others. Whilst there is no single correct approach, all of our clients need to be alert to the impact of variations on expectations.

The amount of Local Government reserves is being increasingly challenged, and there needs to be a clear understanding of the reason for the current and planned levels, and what flexibility there is within them if there becomes a need for them to reduce.

Our survey also suggests that there is some scope for further analysis of our clients' assets to identify options for change. Asset management plans that are aligned to service and staffing changes are important for ensuring that those options are co-ordinated and realistic.

We know that many of our clients are still working hard to address gaps in their savings targets for future years, and all of them will need to re-assess their assumptions when the results of the financial settlement are made clear, along with the detail behind recent announcements are made available. It is vital that their budgetary frameworks are fit-for-purpose to respond to the challenges.

The remainder of this report sets out the results of our survey and the questions we have suggested for Members to consider. We look forward to your feedback.

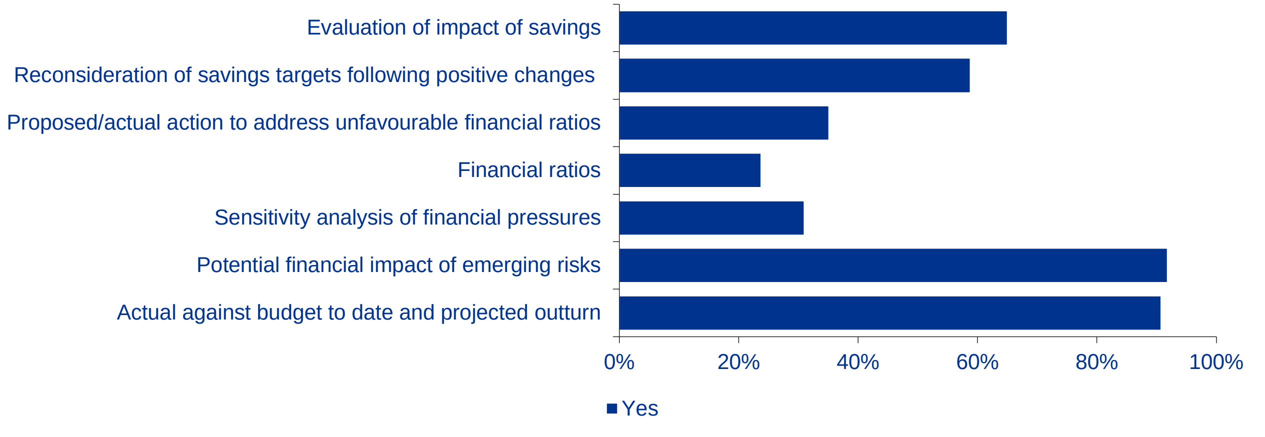
Comparatives

1

What's in your Budget Monitoring Reports?

We looked at our clients' main budget monitoring reports to see if they contained a series of potentially important elements.

Do budget monitoring reports include the following:



As expected, most budget monitoring reports identify the actual position against budget to date and a projected outturn, and the financial impact of emerging risks. The use of sensitivity analysis and financial ratios is less developed. It may be that Members will view these as more important as local financial volatility increases with the move away from block central funding.

Our audit teams highlighted some local practices that influence what goes in to the budget monitoring reports. These included that portfolio holders receive monthly summarised reports for their budget areas that supplement the quarterly reporting, or that particular committees receive detailed reports in addition to the high level reports for all members. Financial ratios are sometimes limited to particular areas, such as in the context of the Treasury Management Strategy.

There is no universal 'right level' of detail in budget monitoring reports – the key is that the reports provide decision-makers with sufficient information in the context of the other information that they receive to allow them to understand the financial position and projections.

Questions to Consider

- Do your budget monitoring reports provide an appropriate level of detail?
- Given the likelihood of increased financial pressures and volatility, do your budget monitoring reports need to evolve?
- Do members have the necessary training, skills & experience to interpret the budgetary reports and information provided?

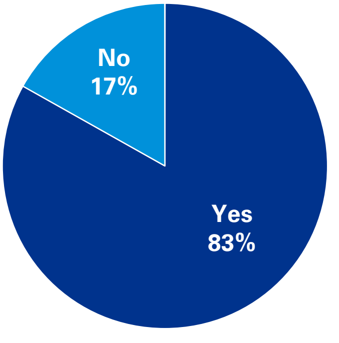
Comparatives (cont.)

2

Did you achieve last year's savings plans?

We looked at the achievement of the overall savings targets alongside the monitoring of the individual savings plans.

Did 2014-15 actual savings meet the budgeted target?



With the uncertainty about the future level and nature of funding, we know that many clients were looking to build up their levels of resilience in 2014-15, and many had savings plans that were designed to help increase useable reserves. The majority of clients met their 2014-15 budgeted savings target.

Some of our audit teams commented that better than expected income had had a significant impact on the net financial outcome – for example from the levels of new homes bonus and planning fees. We recognise that sometimes planned savings such as staff reductions are put on hold in order to meet unexpected demand for services. Tracking the achievement of savings in these circumstances can become complicated, and there is also a risk that unexpected income could result in a reduced focus on making savings elsewhere in the budget.

Our audit teams also noted examples of clients ensuring that the use of reserves is allowed only to provide new or enhanced services, and not to deal with deficits or overspends (which could mask failure to meet the savings targets). They also referred to cases where savings are built into budgets, and so are not separately identified – this links into the question on the following page.

Questions to Consider

- Do you know if your savings to-date in 2015-16 are on target to meet the budgeted amount?
- If you have received unexpected income in 2015-16, are you clear how it has impacted on your savings targets?
- If any of your 2015-16 individual savings schemes or the overall savings targets are not being achieved, do you know why?

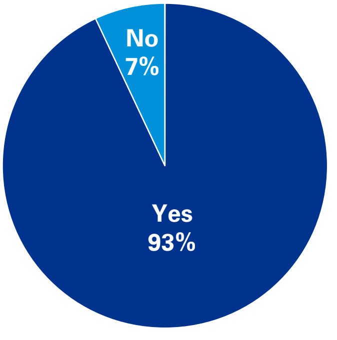
Comparatives (cont.)

3

Are individual savings plans monitored centrally?

We asked whether the individual schemes that make-up the overall savings plans are monitored centrally on an on-going basis.

Were individual savings projects/plans monitored during the year to check that expected savings remained deliverable in 2014-15?



As may be expected, the majority of our clients monitor individual schemes centrally. Audit teams that answered ‘no’ reported that the client approach is to expect budget holders to deliver their overall net financial target which incorporates the savings plans, and so the central monitoring is based on this net position rather than separating out savings plans.

As the pressure on budgets continues, savings will be increasingly hard to find. Whatever system is used to monitor the achievement of savings plans, it is vital that schemes that are failing to achieve the expected results are highlighted early, and that alternative measures are in place to address the financial shortfall. It is also important to learn the lessons as to why schemes fail in order to help avoid problems recurring. Similarly, successful ones can be analysed to understand the success factors, and to see if they can be replicated.

Questions to Consider

– Are you confident that you identify savings schemes that are failing at an early stage?
– Do you have alternative measures to substitute for failing savings schemes?
– Are successful schemes evaluated to identify why they worked, and to see if they can be applied in other parts of your organisation?

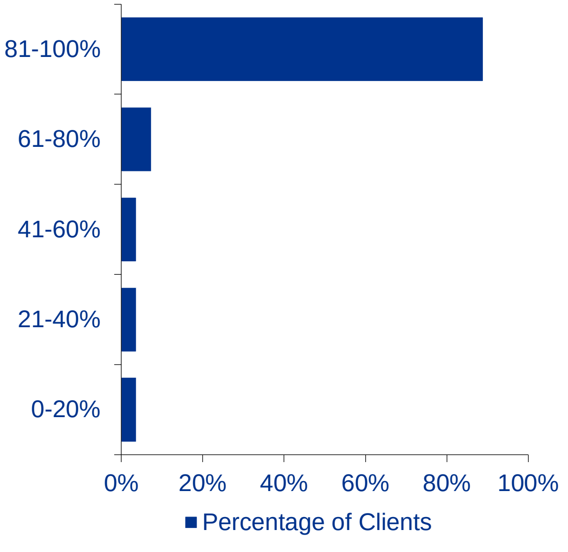
Comparatives (cont.)

4

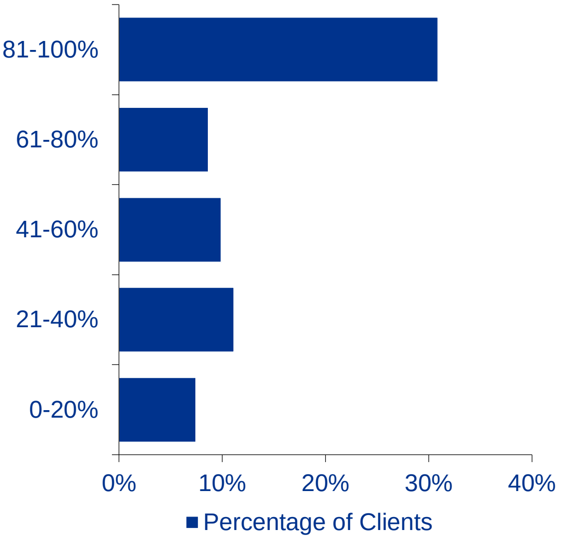
Do you have detailed plans for your savings?

We looked at what proportion of the savings targets for 2015-16 and 2016-17 had detailed plans at the start of the 2015-16 financial year to achieve them. We know that as the level of funding was uncertain beyond 2015-16, officers were estimating what level of savings will be needed.

What percentage of 2015-16 budget savings were backed by detailed plans as at 31 March 2015?



What percentage of 2016-17 budget savings were backed by detailed plans as at 31 March 2015?



At the start of the 2015-16 year, over 80% of clients had detailed plans that covered the level of savings needed. This dropped to below 40% for the 2016-17 year. As the financial position is clarified for 2016-17 and beyond, there will be a need to revisit the expected level of savings to ensure that the assumptions made remain valid and that the plans to achieve them are complete and robust on an ongoing basis.

Questions to Consider

- Are all of your savings targets backed with detailed plans?
- Are you confident that the detailed savings plans are robust and realistic?
- Are detailed savings plans updated to ensure that they reflect changes in circumstances?

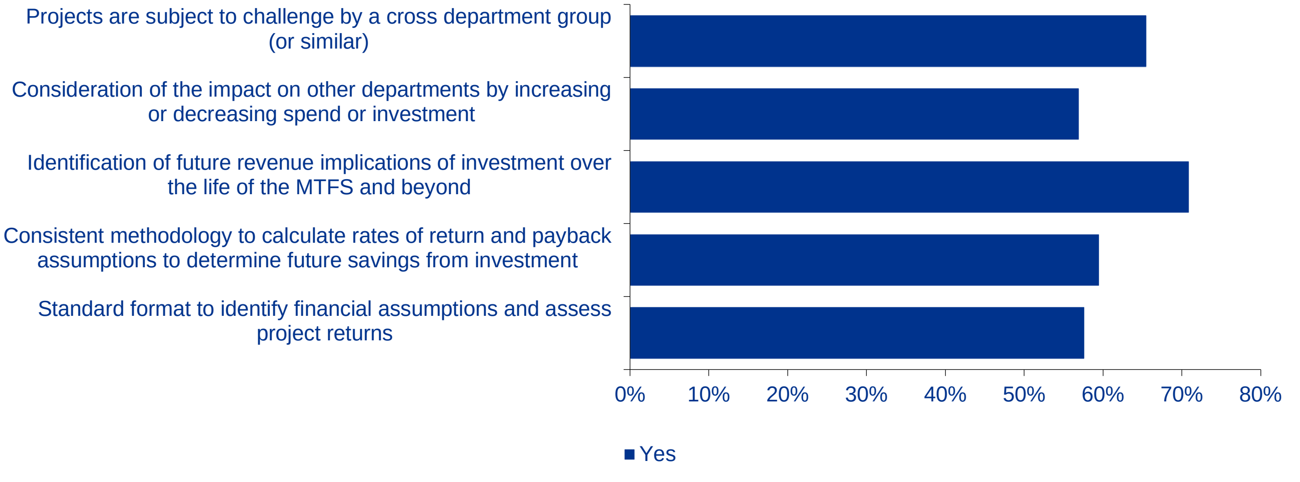
Comparatives (cont.)

5

When you consider possible invest-to-save projects, what factors do you take into account?

Even in financially pressured times we know that our clients will have opportunities to invest in new projects, and that those projects will not necessarily have an immediate or short-term impact, and may go beyond the life of the Medium Term Financial Strategy (MTFS). As available resources become more scarce, and the link increases between local economy growth and councils' financial well-being because of the localisation of economic risk and reward, it is more important than ever to have a strong framework in place to select the most appropriate invest-to-save projects. We looked at all clients for each of the elements below on a yes/no basis.

Are individual invest-to-save projects appraised using the following factors in a consistent way?



Our audit teams identified that not all of the possible tools and techniques available to our clients are being used routinely. We recognise that this may be because for some there is limited opportunity to invest-to-save, and we also recognise that the framework used to select the projects is dependent on local factors, such as the risk appetite, the range of opportunities, potential partners and other factors. However, with the confirmation of the intention to move to local business rate retention and the removal of Revenue Support Grant by 2020, selecting the right invest-to-save projects and monitoring their outcomes against their objectives will become increasingly important. It is also important to check how approved projects perform against the projected outcomes, and to assess why any significant variations have come about.

Questions to Consider

- Is your process for assessing invest-to-save projects robust and consistent?
- Are there tools and techniques you could use to help strengthen your current invest-to-save process?
- How robustly do you review the outcomes of invest-to-save projects?

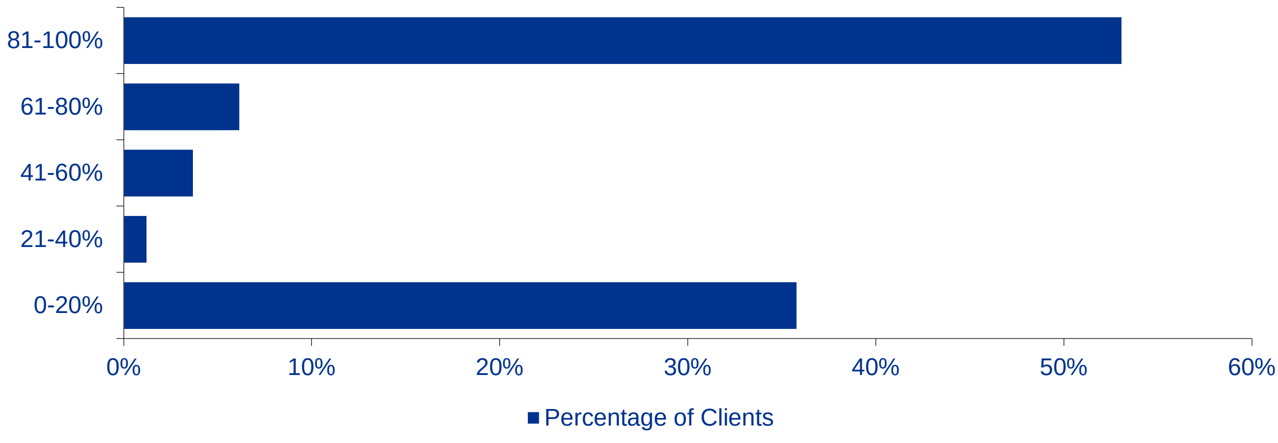
Comparatives (cont.)

6

Are your savings recurrent?

We considered the level of recurrent savings within the overall delivery of the plans. Recurrent savings are those that impact on more than one year. For example, removing a post is a permanent reduction in the budget – a vacancy freeze that delays recruitment to a post is a temporary, non-recurrent measure.

What percentage of 2014-15 actual budget savings were recurrent savings?



The majority or all of many clients' savings were recurrent, which linked to permanent reductions in staffing levels and service reductions. Recurrent savings are particularly important in times where savings are required year-on-year, as any non-recurrent savings from previous years have to be re-achieved alongside the current year's targets.

Unexpected income is welcome, but there can be a risk that it can help to mask either the underachievement of savings. This is a particular problem if the income is non-recurrent, as those savings will need to be made to avoid the financial impact simply transferring to the next year.

In some cases, the proportion of recurrent/non-recurrent savings was not available, and these are included in the 0-20% group above.

Questions to Consider

- Do you know the recurrent and non-recurrent levels in your savings plans for 2015-16 and beyond?
- Has the impact of any non-recurrent savings from previous years been factored into current and future savings plans?
- Do you assess unexpected income to check that it is recurrent/non-recurrent and that it has been factored in appropriately to financial monitoring and plans?

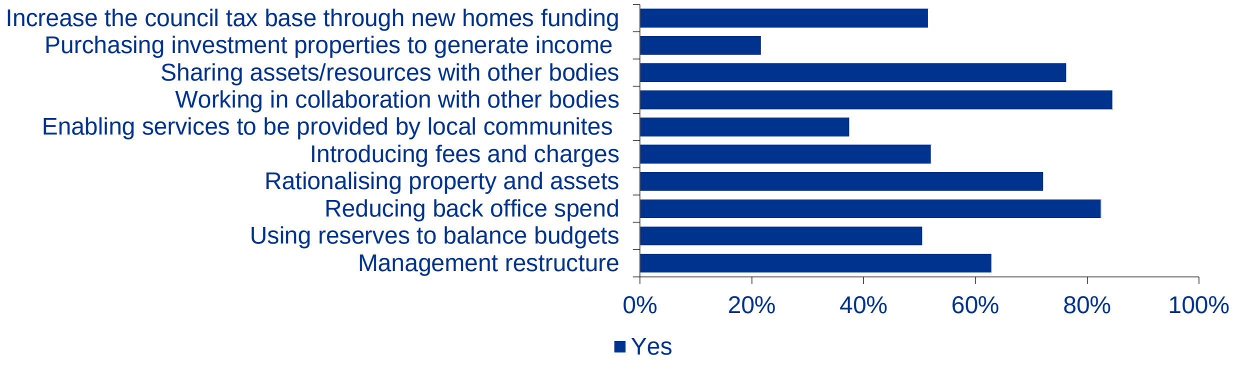
Comparatives (cont.)

7

What savings measures are you relying on for 2015-16 and beyond?

We looked at the savings measures that our clients are using in their budgets to make their medium term financial plans balance.

Which of the following measures are being used to deliver the 2015-16 budget and/or in the following years?



It is inevitable that not all clients will use all the measures, as the levels of financial pressure vary, as does the capacity to implement a variety of measures. We also recognise that some of the ‘no’ answers in the survey are because our clients have already used particular measures in previous years, such as management restructuring, where a period of stability may be appropriate to enable the changes to take effect.

It may be though that previous decisions – for example not to introduce/increase further fees and charges, or to continue to provide the current range of non-statutory services – will need to be revisited as financial pressures increase, and it is inevitable that some clients will need to make very difficult decisions in order to deliver their statutory financial responsibilities.

We asked our audit teams to highlight any other savings measures that were being used by our clients. They highlighted the following examples;

- Vacancy Management;
- Business Rates income growth;
- Withdrawal of services not deemed a priority or affordable;
- Early repayment of debt;
- Establishing a Housing Growth Company;
- Increased joint working and joint venturing;
- Procurement and contracting renegotiations; and
- Assets review and restructuring.

Questions to Consider

- Are you confident that your plans will enable you to continue to meet your statutory financial responsibilities?
- Have you considered all possible savings measures available to you?
- Are there any aspects of your budget that need to be revisited?

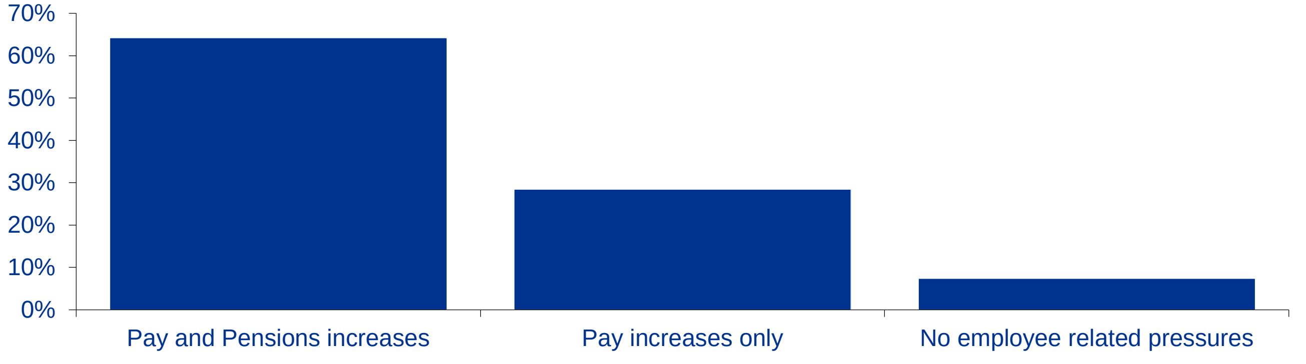
Comparatives (cont.)

8

Do you allow for pay and pension increases in your budget?

We asked all clients about their approach to factoring in employee related cost pressures, namely do you allow for pay and pension increases, just pay, or do you not allocate specific amounts for either?

What employee-related cost pressures does the 2015-16 budget include?



Nearly two-thirds of our clients factored in the impact of pay and pensions increases into the amount given to budget holders to manage. More than a quarter of our clients allowed for pay increases only in 2015-16, and in a year when there is no routine change in the actuary's recommended level of pension contribution (which results from the triennial review), the variation in pension costs is unlikely to be significant overall. However, at an individual budget holder level, pension costs could vary up or down because of factors such as changes in the profile of staff in relation to their age, and decisions by employees to join or leave the scheme. Finally, our survey identified that a small number of clients expect their budget holders to absorb any additional employee-related costs into the overall budget that they are given to manage.

We are aware that our clients will also need to take account of the introduction of the national living wage from April 2016. There may be some internal (including subsidiary company) staff costs, but for many clients the bigger impact will be the additional costs incurred by their suppliers and the need to establish the way forward with them for service provision and continuity.

Questions to Consider

- If you don't allow for pay and/or pension cost increases, can you identify any areas of the budget that are vulnerable to significant cost variations?
- Do you have mechanisms to identify and deal with changes to staff costs within year?
- Have you evaluated the cost of the national living wage across your cost base, including your supply chain?

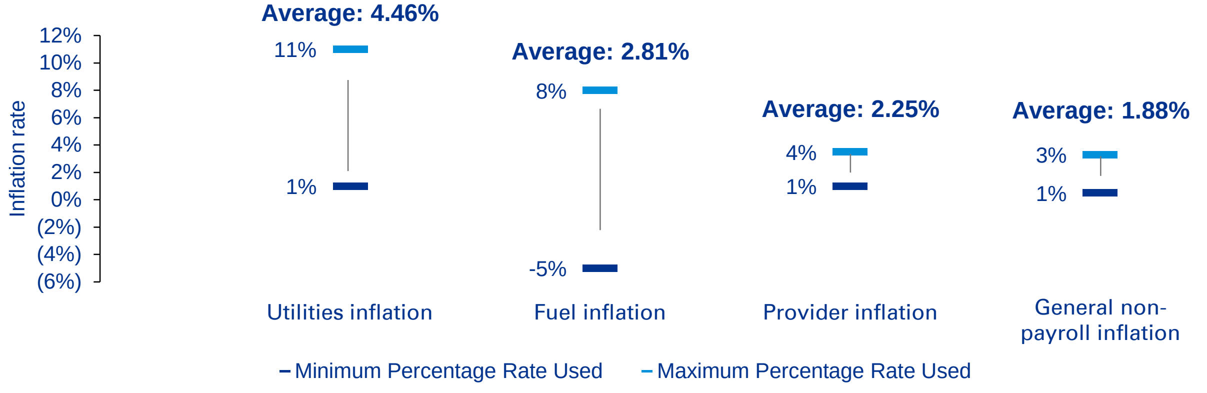
Comparatives (cont.)

9

What inflation rates do you use for particular cost pressures?

We looked at all of our clients' use of non-standard rates of inflation when preparing the budgets, focusing on four common variants. Whilst we were aware that some used a single inflation rate, we knew that others have decided to use differing rates for areas that could have a significant impact on their financial position.

If the 2015-16 budget includes separate inflation rates for the following, which rate is used?



We found that there were some large differences in the inflation assumptions made for fuel and utilities in particular (and we accept that all may be valid due to local circumstances, such as fixed increase, variable or new contract rates). Assumptions by nature are subjective, but they can be updated if it becomes clear that they are not correct. Although overall inflation is at a relatively low level, the current financial pressure means that the impact of variations in aspects of it could make a difference to achieving targets.

Our audit teams also identified that clients used inflation variations for the areas below:

- Hardware and Software price increases;
- Insurance and postage cost increases;
- Indexation increases in partnership arrangements;
- Landfill tax and building repairs; and
- Fee income rates raised to match the overall inflation assumption.

Questions to Consider

- Do you understand how your budget takes inflation into account (e.g. which supplies & services are on fixed/variable rates)?
- Do you know which inflation rate changes would have the biggest impact on your budget?
- How do you deal with inflation variations that happen within the year?

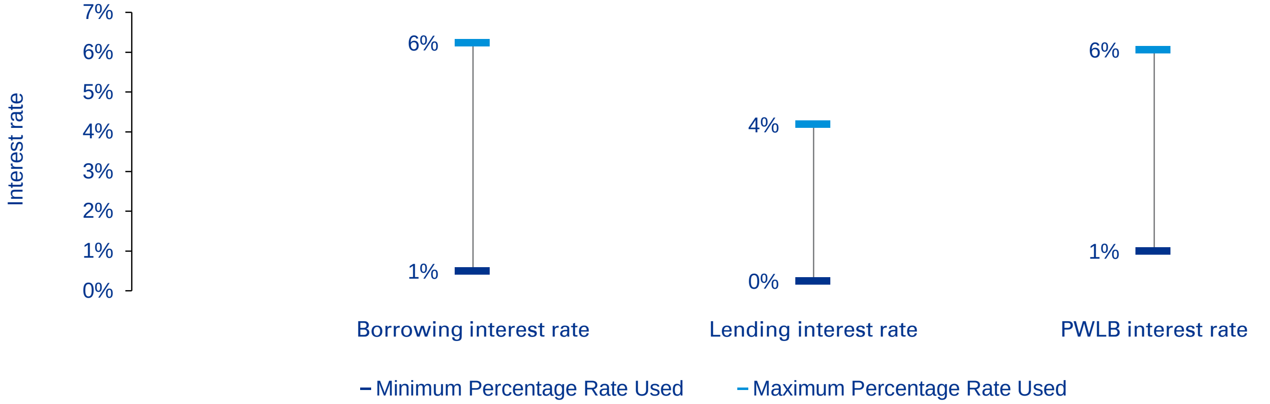
Comparatives (cont.)

10

What rates have you used in your budget for borrowing and lending, and what other specific rates do you factor in to your budget?

We looked at the assumptions about borrowing and lending rates that our clients have used for generating 2015-16 budgets and beyond. We also considered if our clients had identified any further areas of non-pay expenditure for particular rates.

What rates are being used to budget for borrowing and lending?



The chart shows that there were variations in the assumptions used. Lending and borrowing rates are comparatively low historically, but the variations suggest that local circumstances still make a difference to the budget assumptions. This is likely to be related to existing arrangements that date back to when rates were higher.

Audit teams also identified specific assumptions for the following non-pay areas, including the following examples:

- Rent increases;
- Change in the Council Tax base;
- Pension Lump sum increases; and
- Reduction in direct central government support.

Questions to Consider

- Do you know what borrowing and lending assumptions are used when generating the budget?
- Have you identified the areas of your budget where rate assumptions need to be specified?
- Are you alert to changes in rates within year?

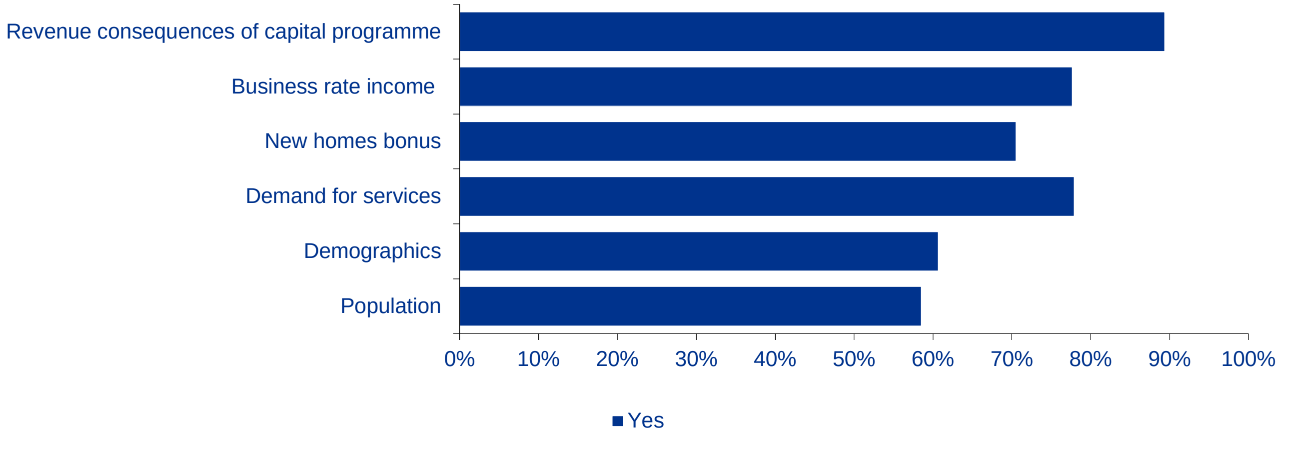
Comparatives (cont.)

11

What factors do you use when developing your budget?

We looked at a particular range of factors that are commonly used when generating budgets, and considered whether our clients used them.

Does the 2015-16 budget include evaluation of the potential financial impact of changes in the following factors?



Although all of these factors were used by the majority of our clients, the proportion using demographics (e.g. deprivation levels, average age) and population (e.g. size and location) factors was smaller than the others. It is generally accepted that the overall population is growing, and that the number of older people with complex needs is likely to increase. However, the impact will vary in different areas.

Income sources such as new homes bonus and business rates, and the demand for services from the public, are subject to variables such as economic conditions and changes in government policy. Scenario planning for the impact of changes is vital to help prepare for different outcomes. It is also important to ensure that the impact of the capital programme is affordable and to update that assessment as budgets are revised.

Questions to Consider

- Do you make use of all available data to help generate your budget?
- Do you understand how your budget is impacted by changes in the factors that drive it?
- Do you revisit the capital programme to ensure its revenue impact remains affordable?

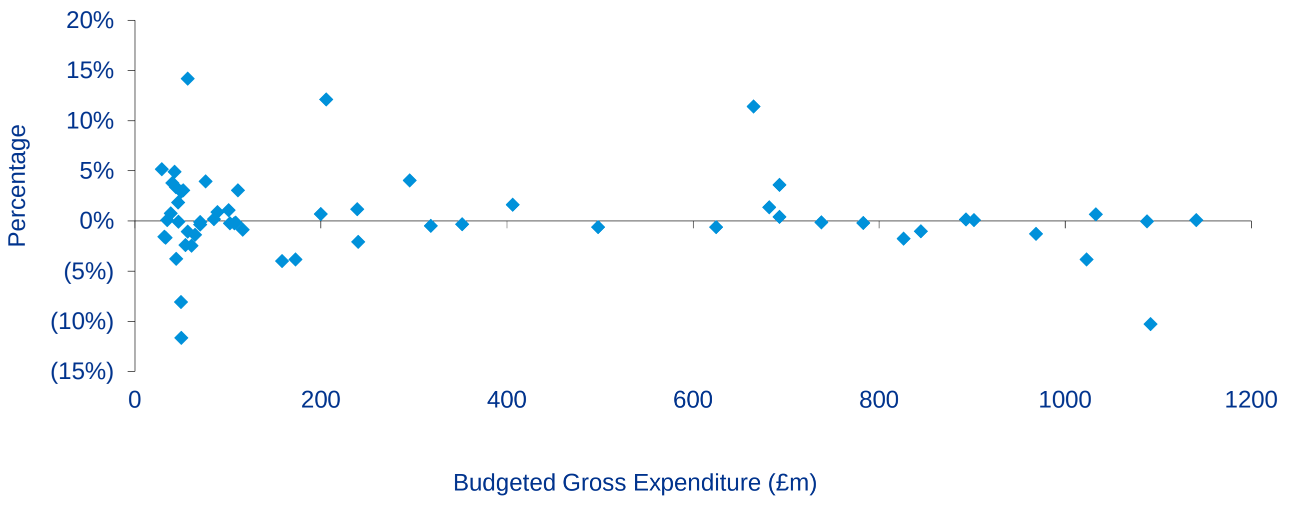
Comparatives (cont.)

12

What is the planned change in usable reserves in 2015-16?

The level of local government reserves is a much-debated topic. We looked at the planned change in the overall level of usable reserves in 2015-16 from the opening to the closing position, and compared it to the level of gross expenditure across all clients. Usable reserves includes amounts earmarked for particular reasons. Earmarked funds can be flexible – changes in policies, intended projects and plans can mean that they can become either insufficient or not needed.

What is the budget change of useable reserves as a percentage of budgeted gross expenditure compared to budgeted gross expenditure?



Many clients are planning to keep usable reserves relatively stable at the end of the year, with most variations within plus or minus 5% of the starting point. A small number have larger variations. The increases reflect that some are aiming to boost financial resilience reserves in preparation for the expected challenges to come. The reductions could be due to the appropriate application of earmarked reserves for planned expenditure. However if reserves are being used to help achieve a balanced budget for 2015-16, this may be a concern given that the financial pressure is expected to increase in the following years.

Questions to Consider

- Do you think the level of your usable reserves is about right?
- Do you understand the reason for any planned changes in the level of usable reserves?
- Do you know how much flexibility you have in your usable reserves?

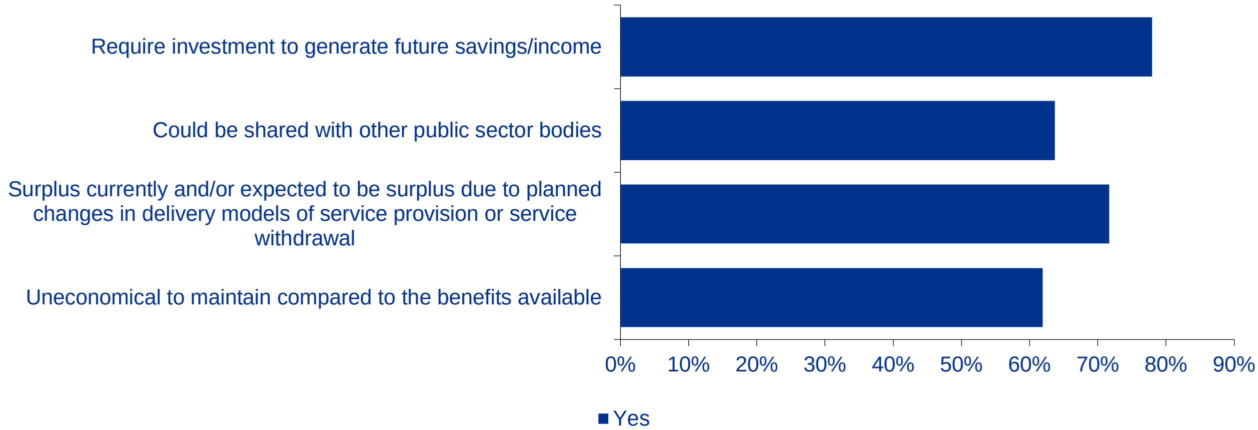
Comparatives (cont.)

13

Have you analysed your asset base?

We are aware that many of our clients are reviewing their assets to see if they can make more use of them. We considered whether our clients had analysed assets that met four categories.

Does the body have an up to date analysis of its assets to identify those that meet the following descriptions:



The results suggest that the analysis of the costs and benefits of assets, and the analysis of current and likely surplus assets is up-to-date at a significant number of clients, but not so at a minority. Similarly, the majority of our clients have an up-to-date analysis of assets that could be made available for shared use, and that more have worked out which assets require investment. However, it is likely that some could do more to fully understand what their options are.

The importance of these assessments will vary depending on the nature of the asset base. We also recognise that some clients are taking steps such as changing ways of working that will release assets in the future, and so their analysis will be on-going. Nevertheless, asset review and management are likely to be important budgetary measures given the financial challenges. An asset utilisation plan can be used to summarise the intended use of assets, and it is vital that it is co-ordinated with any intended changes in the way that services are delivered, or changes to internal operations in order to ensure it is up-to-date.

Questions to Consider

– Do you have a comprehensive and current asset utilisation plan?
– Do your asset plans align with any intended changes to service delivery or internal ways of working?
– Are all options for asset use being considered?

Summary of Questions to Consider

Questions to Consider

1

What's in your Budget Monitoring Reports?

Questions to Consider

- Do your budget monitoring reports provide an appropriate level of detail?
- Given the likelihood of increased financial pressures and volatility, do your budget monitoring reports need to evolve?
- Do members have the necessary training, skills & experience to interpret the budgetary reports and information provided?

2

Did you achieve last year's savings plans?

Questions to Consider

- Do you know if your savings to-date in 2015-16 are on target to meet the budgeted amount?
- If you have received unexpected income in 2015-16, are you clear how it has impacted on your savings targets?
- If any of your 2015-16 individual savings schemes or the overall savings targets are not being achieved, do you know why?

3

Are individual savings plans monitored centrally?

Questions to Consider

- Are you confident that you identify savings schemes that are failing at an early stage?
- Do you have alternative measures to substitute for failing savings schemes?
- Are successful schemes evaluated to identify why they worked, and to see if they can be applied in other parts of your organisation?

4

Do you have detailed plans for your savings?

Questions to Consider

- Are all of your savings targets backed with detailed plans?
- Are you confident that the detailed savings plans are robust and realistic?
- Are detailed savings plans updated to ensure that they reflect changes in circumstances?

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When you consider possible invest-to-save projects, what factors do you take into account?

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What savings measures are you relying on for 2015-16 and beyond?

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- Are you confident that your plans will enable you to continue to meet your statutory financial responsibilities?
- Have you considered all possible savings measures available to you?
- Are there any aspects of your budget that need to be revisited?

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Do you allow for pay and pension increases in your budget?

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– Do you revisit the capital programme to ensure its revenue impact remains affordable?

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Questions to Consider

– Do you think the level of your usable reserves is about right?
– Do you understand the reason for any planned changes in the level of usable reserves?
– Do you know how much flexibility you have in your usable reserves?

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