Accountants &
business advisers

Southend-on-Sea Borough Council

Annual Governance Report 2011/12

September 2012

DRAFT

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Appendices

Code of Audit Practice and Statement of Responsibilities of Auditors and Audited Bodies

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission contains an explanation of the respective responsibilities of auditors and of the audited body. Reports and letters prepared by appointed auditors are addressed to members or officers. They are prepared for the sole use of the audited body and no responsibility is taken by auditors to any member or officer in their individual capacity or to any third party.

We accept no responsibility for any reliance that might be placed on reports and letters for any purpose by third parties, to whom it should not be shown without our prior written consent.

Code of Audit Practice

Statement of Responsibilities

1 Executive summary

1.1 The purpose of this report is to communicate to you the significant findings from the audit of Southend-on-Sea Borough Council's financial statements and arrangements to secure economy, efficiency and effectiveness in the use of resources.

1.2 A summary of our findings and conclusions is set out below:

Area of audit	Findings and conclusion
Financial statements	
Financial statements	Three material errors were identified in relation to property, plant and equipment (PPE). These were corrected by the Council in the financial statements and have no overall impact on the financial outturn for the year. Some uncorrected non-trivial but not material errors have been identified and these are detailed in Appendix B. The detailed findings from our work are set out in section 3. Some areas of work are still outstanding at the time of drafting this report. Should these result in any significant issues, we will give a verbal update to the Audit Committee on 26 September 2012. Subject to satisfactory completion of the outstanding work, we anticipate issuing an **unqualified** true and fair opinion on the financial statements for the year ending 31 March 2012.
Internal controls	A number of significant control weaknesses have been identified relating to both the pre- and post-Agresso implementation periods. These issues, together with additional work necessary as a result of recognised shortcomings in implementation arrangements, have caused additional audit work to be necessary to obtain sufficient assurance to support the provision of our audit opinion. The detailed findings from our work are set out in section 3.
Annual Governance Statement	We are satisfied that the finalised Annual Governance Statement is not inconsistent or misleading with other information we are aware of from our audit of the financial statements.
Whole of government accounts	Our work to review the consistency of the whole of government accounts return with the audited financial statements is in progress and a verbal update will be given at the Audit Committee on 26 September 2012.
Use of resources	
Value for money conclusion	We are satisfied that, in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012. This is based upon the following two Audit Commission criteria: • the organisation has proper arrangements in place for securing financial resilience • the organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness. The detailed findings from our work are set out in section 4. We propose issuing an **unqualified** value for money conclusion.

Acknowledgement

1.3 We would like to thank staff for their co-operation and assistance during the audit and throughout the period.

2 Introduction

2.1 International Standards on Auditing (ISAs) (UK and Ireland) and the Code of Audit Practice require that we report to those responsible for financial governance and financial reporting (those charged with governance) the key findings of our audit prior to issuing our opinion on the financial statements and our value for money conclusion. This report summarises the results of our audit work completed to date in respect of the financial statements and arrangements to secure economy, efficiency and effectiveness in the use of resources for the year ended 31 March 2012.

2.2 Our report is presented to the Audit Committee in accordance with the provisions of ISA (UK & Ireland) 260 Communication with those charged with governance, ISA 265 Communicating Deficiencies in Internal Control to Those Charged with Governance and Management, and the Audit Commission's Code of Audit Practice.

2.3 The contents of this report have been discussed and agreed with the Head of Finance and Resources. We have reported separately to management other non-significant findings from our audit.

Findings

2.4 Recommendations in response to the key findings identified by our audit are provided in the action plan at Appendix A. These recommendations have been discussed with appropriate officers and their responses are included. We would highlight that in this report we do not provide a comprehensive statement of all weaknesses that may exist in the financial and operational systems, but only those matters which have come to our attention as a result of the audit procedures performed. We have only restated weaknesses already reported by Internal Audit where we consider these to be significant.

Fee outturn

2.5 The Audit Commission's Standing Guidance for Auditors requires us to report the outturn fee position for the year against the budgeted fee included within our 2011/12 Audit Plan.

2.6 As a result of additional work to address both systems and accounts audit issues, additional fees have arisen. Our planned fee was determined based on the assumptions that:

- Agresso would be implemented from 1 April 2011, so being a single accounting system in place for the whole of the financial year;
- the implementation would not give rise to control weakness or discontinuities in activities;
- we would be able to rely on Internal Audit's work;
- the additional work would comprise solely of a review of balance transfers between systems (i.e. an insignificant amount of work, for which no additional charge would be levied)
- all prior year accounts audit recommendations would be implemented.

2.7 These assumptions were not supported, and so some additional fees have been incurred, with estimates of fees communicated to Management during the audit, and updated as the audit progressed.

Independence

2.8 We confirm that we are not aware of any relationships that may bear on our independence and objectivity as auditors and that our independence declaration, included in the Audit Plan for 2011/12, has remained valid throughout the period of the audit.

3 Financial statements

3.1 We are required to provide an opinion on whether your financial statements give a true and fair view of your financial position and income and expenditure and whether they have been prepared properly, in accordance with appropriate legislation and relevant accounting guidance. To do this we carry out risk based procedures designed to obtain sufficient appropriate audit evidence to determine with reasonable confidence whether the financial statements are free from material misstatement and evaluate the overall presentation.

3.2 In carrying out our work we determine and apply a level of materiality. Materiality is the expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole, or individual elements of the financial statements as appropriate. Consequently, the audit cannot be relied upon to identify all risks or potential and actual misstatements.

3.3 We consider misstatements of less than £141,000 to be trivial to the financial statements, unless the misstatement is indicative of fraud, and have not reported them. This is unchanged from the triviality level that was reported in our Audit Plan.

Reporting to those charged with governance

3.4 We have set out below those matters relevant to our audit that, under auditing standards, require reporting to those charged with governance or which be believe should be reported to you to assist you with your governance duties.

Significant risks of material misstatement

3.5 We reported our risk assessment, which brought to your attention areas that require additional or special audit consideration and are considered a significant audit risk, in the 2011/12 Audit Plan issued in December 2011. We have since undertaken a more detailed assessment of risk following the completion of our interim review of financial controls and review of the Council's draft financial statements, and we reported our updated risk assessment to officers on 27 July, and to Members in our letter dated 4 September 2012.

3.6 Our audit approach was designed to address these significant risks and any relevant issues arising have been set out in the remainder of this report.

Accounting practices

Financial statements preparation

3.7 The requirement for Members to approve the draft financial statements by 30 June was removed by the Accounts and Audit Regulations 2011, however these regulations introduced the requirement for the Responsible Financial Officer to sign and present the financial statements for audit by 30 June. The financial statements were signed and presented for audit on 29 June 2012.

3.8 The Council provided us with some electronic working papers on 9 July 2012. However, not all working papers were received in line with the agreed timetable.

3.9 On commencement of the audit on 9 July, the following key pieces of audit evidence were not available:

- Fixed asset register
- Bank reconciliation
- Payroll reconciliation
- Draft Annual Governance Statement (which was agreed to be accepted mid-August)

3.10 All items noted above were received by the end of August, to enable final audit testing to commence.

Accounting policies

3.11 The following changes have been introduced by the 2011 Code of Practice on Local Authority Accounting in the United Kingdom (the 'Code'), resulting in changes in accounting practice:

- the adoption of FRS30 *Heritage Assets,* requiring that heritage assets are carried at valuation, with comprehensive disclosure note requirements
- amendments to the related party disclosures required in respect of central government departments, government agencies, NHS bodies and other local authorities to clarify the nature of those related party relationships and simplify the information disclosed
- new disclosure requirements for exit packages to disclose the number and cost of exit packages agreed in the year
- the introduction of disclosure requirements in relation to the nature and amount of trust funds (a previous Statement of Recommended Practice requirement that the Code has reinstated).

3.12 Some corrections were required to the Heritage Assets recorded in the balance sheet, which are detailed below.

3.13 The exit packages note required amendment to show the split between compulsory redundancies and other exit packages. Additionally, the Council also chose to show the split between staff at the Council and staff at the Schools.

3.14 The Council has dealt with the implementation of the other changes in an appropriate manner and assisted the audit in the review of the changes required

Accounting estimates

3.15 Our testing found that the bad debt provision was understated, despite the increase in the provision made necessary because of the increased debt resulting from the suspension of debt recovery procedures for part of the year following the implementation of Agresso. The accounts did not accurately reflect the bad debt provision calculations that had been undertaken by the Council. More details on this are set out below.

3.16 Our testing identified that there were errors in the calculation of depreciation as a result of forty assets, of the forty thousand included in the fixed asset register, that should have been depreciated not being so. With the help of finance staff we have calculated the depreciation that should have been calculated on these assets and have concluded that this would be trivial in total.

3.17 In addition, the difficulties reconciling the fixed asset register to the accounts identified that there were some differences between the classification between asset classes for some immaterial elements of the accumulated depreciation. This has been resolved through the changes that the Council have made to make the accounts consistent with the fixed asset register.

3.18 We have no other matters to report.

Disclosures

3.19 We identified a number of departures from the expected presentation of the financial statements or where notes and other disclosures had not been presented in accordance with the Code. These have been amended by the Council.

Omitted primary statement comparative

3.20 The movement in reserves statement did not include a comparative note in the draft financial statements. This has now been included to ensure that the statement is compliant with accounting standards. The disclosure note, Note7, which details the adjustments made between the accounting basis and the funding basis, also did not include a comparative note, but this has now also been added in.

Omitted separate disclosure of "REFCUS"

3.21 The note disclosing all grant income recognised in the comprehensive income and expenditure statement (CIES) did not separately disclose revenue expenditure funded from capital under statute (REFCUS) and grant income that was being charged directly to services. Therefore the disclosure note required amendment to separate out the total value of REFCUS grant income of £19.96m, from the grant income being charged directly to services.

Missing Councillors' disclosure declarations

3.22 Five Councillors did not complete and return their related party declaration forms at the time of our audit, despite an initial request letter and two reminder letters. There is a risk that a related party transaction may not be disclosed in the related party note included in the financial statements.

3.23 To mitigate this risk, we have completed a company search on these members to identify any potential relationships with companies that may need to be disclosed in the financial statements. No relationships were identified.

3.24 The Council should endeavour to ensure that declaration forms are received from all councillors in the future and a recommendation has been made to this effect at Appendix A

Omission of material value of debtors from financial instruments disclosure note

3.25 Financial instruments note contains errors because all Central Government and Local Authority debtors have been excluded from the note, regardless of whether they are statutory or contractual debtors. The correct treatment is for only statutory debtors to be excluded from the note. We have carried out additional work to identify the extent of contractual debtors that have been excluded from this note and concluded that there is an extrapolated error of £2.4m of Central Government and Local Authority debtors that should be included in the disclosure.

Rolling programme of revaluation of fixed assets disclosure note

3.26 The disclosure note reporting information on the rolling programme of revaluations has been prepared using the best information available to the Council. The values reported for the volume of assets re-valued in each of the years should be adjusted for the additions that have been made to those assets subsequent to the revaluations. However the Council does not have this information readily available for prior years and therefore has reported the total current value of the assets re-valued in each period. Therefore the information reported is not completely technically accurate, however we do not believe that the difference will have an impact on the reader of the accounts.

Uncorrected misstatements

3.27 We are required to report to you uncorrected misstatements that relate to the current financial year (including those arising in previous periods that have an effect on the current year financial statements) and the effect that they have individually, or in aggregate, on the auditor's report, except for those that are clearly trivial. These are set out below and their potential impact is summarised at Appendix B.

3.28 We have requested that these misstatements be corrected and seek written representation from those charged with governance that they acknowledge these misstatements and that they are satisfied with management's reasoning for not correcting the financial statements. The draft letter of representation is set out in Appendix C.

Debtor balance with DCLG for Business Rates Payment to the National Pool

3.29 The debtor balance with DCLG is overstated by £1,129k, of which £482k is the brought forward error from the prior year audit. The error is as a result of a roll forward figure from the Northgate System that is growing year on year, but where the Council is unable to identify specifically what it relates to so that it can be corrected on the system.

3.30 The Council is working to resolve this issue with Northgate. However, due to the nature of the error, the Council is unaware of the full accounting entries that need to be made to correct the financial statements, to enable them show the correct debtor position at the year end, as well as the corresponding adjustment.

Bad debt provision

3.31 The bad debt provision is understated by £675k due to the Council incorrectly recording on the ledger the value of the required provision that had been calculated. The majority of the understatement of the provision relates to debts with Council Tax payers.

Capitalisation of lease payments

3.32 Our testing identified that a lease payment for the waste disposal facility was incorrectly capitalised within property, plant and equipment, when it should have been treated as REFCUS. As a result, assets are overstated by £164k. The correcting entry would be to charge the amount to expenditure and reverse the expense out of the general fund balance to the capital adjustment account, through the Movement in Reserves Statement..

Intangible assets

3.33 Our testing on a sample of intangible assets identified a group of assets classified as software that could not be verified. The Council were unable to identify these assets and therefore they may not be in existence. As the Council is unable to identify these assets they are also not able to perform an impairment review to determine that they are appropriately valued. The potential misstatement is that assets are overstated by.£1.1m, however, this does not affect the financial outturn for the year.

Grants

3.34 Our testing identified that REFCUS grant income of £1.2m has been misclassified within the CIES and was credited against the service areas in 2011/12, due to the timing difference between receipt of the cash in 2010/11and the utilisation of that funding in 2011/12.

3.35 This is not the correct accounting treatment, as the income had already been recognised in capital grants in 2010/11, when it should have been recognised as service income. The guidance on this was unclear in 2010/11 and therefore we understand why the Council treated it this way in 2010/11, but the guidance has been clarified in 2011/12 and now makes it clear that this was not the way that the Code now expects this to be treated.

3.36 The Council has chosen not to amend for this as the value is not material to the financial statements. As the amount is a misclassification error and has no impact on the general fund balance, this misstatement is not included in Appendix B of this report.

Misstatements corrected by management

Cash Flow Statement

3.37 Amendments were required to the cash flow statement, which the Council remain in the process of resolving. Every entry on the cash-flow statement has been amended, except for the opening balance. The most significant adjustment being £2.5m moving from adjustments for items included in the net provision of services that are investing activities to adjustment to net surplus on the provision of services for non-cash movements.

3.38 There remains a £2.7m unexplained figure within the adjustment for non-cash movements balance. The Council is working to identify the source of this element of the cash flow statement.

Property, plant and equipment (PPE)

3.39 A number of issues were identified from our testing of PPE, which resulted in material misstatements to the accounts, which were all corrected by management. The following issues were identified, however, this does not affect the financial outturn for the year:

Fixed Asset Register

3.40 On commencement of the audit on 9 July an up to date fixed asset register was not available to audit because the additions relating to the housing stock had not been included on the fixed asset register. The financial statements had been prepared from the fixed asset spreadsheets maintained by finance, rather than the fixed asset register.

3.41 A recommendation was made in the 2010/11 Annual Governance Report about the maintenance of the fixed asset register and how this should be kept up to date throughout the year. This had not been done due to the departure of the capital accountant and the resource limitations in the finance department.

3.42 During the course of our audit, the finance team worked to update the fixed asset register, so that this is now the primary record of the fixed assets owned by the Council. However, they were unable to reconcile the register back to the financial statements and were unable to identify the reason why the financial statements did not agree to the register.

3.43 As a result, an adjustment has been made to the assets recorded on the balance sheet to decrease the net book value by £3.7m to make the financial statements consistent with the fixed asset register. This adjustment has been treated as an impairment loss recognised through the CIES.

3.44 The delay in receiving an up to date fixed asset register has had an impact on the audit, which resulted in the audit taking notably longer than anticipated.

3.45 A recommendation has been raised in Appendix A of this report to ensure that the fixed asset register is kept up to date going forward. We have also recommended that the progress on implementing External Audit recommendations that do not relate to the process of annual accounts closedown is monitored and reported to Audit Committee regularly during the year.

Disposals

3.46 On commencement of the audit the Council confirmed that the disposal of Shoebury High School had not been accounted for in the draft financial statements. This disposal had taken place on 1 December 2011, when the land and buildings had been leased to the school for 125 years. The value of the asset disposed of amounted to £27m.

3.47 The disposal had not been accounted for because of uncertainty over the split of one of the assets contained in the fixed asset register between Shoebury High School and Shoebury Youth Centre. The transaction was not processed by the Council until this uncertainty could be resolved. The Council demonstrated that the Shoebury Youth Centre was recorded as a separate asset and therefore all of the asset disposed related to the School and the full £27m needed to be disposed of.

3.48 Audit testing of the fixed asset register identified that the Council also needed to record the disposal of the Shoebury Technical College asset as this asset was part of the asset that had been leased to the school. This disposal amounted to £5m. The total disposal of £32m has now been accounted for within the finalised financial statements.

3.49 In summary, the original accounts included assets that were over-stated by £32m - £27m that officers were aware of, and £5m that was identified by audit testing.

Heritage Assets

3.50 As noted above, the Code requires that the Council adopt FRS 30 (Heritage Assets) for the first time in 2011/12. Our testing on the implementation of this new accounting policy identified £2.6m of additions relating to the pier sprinkler system and the cultural centre included within Heritage Assets which should have been classified as other land and buildings (£1.1m) and vehicles, plant and equipment (£1.5m).

3.51 In addition audit testing highlighted that two of the specific assets recorded on the fixed asset register relating to Porters Lodge had not been adjusted for, despite a revaluation of Porters Lodge overall taking place. As a result the two assets remained on the fixed asset register at their previous carrying values meaning they were double counted by being accounted for in their own right and also as part of the new revaluation for Porters Lodge.

3.52 The Council has removed the two assets from the fixed asset register and the finalised financial statements, resulting in an amendment of £3.6m.

3.53 The Council has amended for these issues within the finalised financial statements, however, this does not affect the financial outturn for the year.

Hinguar Primary School

3.54 The Council is in the process of building a new school on a new site for Hinguar Primary School. The works undertaken on building the new school during 2011/12 have been recorded in the fixed asset register and the financial statements. However the Council was provided with the new land under a section 106 agreement and therefore did not provide any specific consideration for the land. The Council owns this land and should have had the valued in order that it could be recognised in the fixed asset register and financial statements. We have compared the potential value of the site to similar school sites in the vicinity and concluded that the value of the land is not material to the financial statements.

3.55 This will be addressed during 2012/13 when all of the schools are due to be revalued.

Infrastructure

3.56 In our 2010/11 Annual Governance Report we reported that the Council was unable to identify specifically what was included within part of the infrastructure assets balance, because a number of assets had been grouped together in the fixed asset register. The Council agreed that going forward additions to infrastructure would be separately identified and would not be added to the group of infrastructure assets already included on the fixed asset register.

3.57 In 2011/12 our testing identified that additions amounting to £3.6m were again added to the grouped infrastructure assets in the fixed asset register. The finance team had highlighted at our final audit planning stage that the prior year recommendation had not yet been implemented, and then acknowledged during our field visit they had a proposal about the best way to record infrastructure assets in the fixed asset register.

3.58 We understand that the Council is planning to reach an agreement of the treatment of these in time for the end of the 2012/13 financial year. A recommendation has been raised in Appendix A to this report. We have undertaken additional work to perform a reasonableness check on the infrastructure valuation included in the accounts by considering the length of roads owned by the Council and the benchmark values for such roads. This work did not suggest that the value of infrastructure assets reported in the financial statements was overstated.

Physical verification

3.59 As part of our testing we select a sample of assets recorded on the fixed asset register and trace these to the asset to physically verify that it actually exists. Our sample testing identified one asset that the Council could not physically show us. This was because the Council had capitalised consultancy work that took place in 2009, when it should have been charged to revenue.

3.60 As a result we are undertaking additional physical verification checks to ensure that this issue is not more prevalent within the fixed asset register.

Bank reconciliation

3.61 On commencement of our audit on 9 July, a completed bank reconciliation as at 31 March 2012 was not available for audit. The Council worked on producing the reconciliation and resolving the differences highlighted during the course of the audit.

3.62 An error was identified whereby the payroll costs for South Essex Homes had been incorrectly posted to the cash code, resulting in cash being overstated by £372k. An amendment has been made to the financial statements to remove this item from the cash balance and the payroll control codes that feed into the creditors balance on the balance sheet.

3.63 We were provided with a bank reconciliation to use for our audit in early August. However, audit testing demonstrated that not all of the un-presented cheques were included within the un-presented cheque listing, and therefore the bank reconciliation could not be relied upon.

3.64 The Council undertook additional work to resolve the bank reconciliation and we requested that this was completed by the end of August in order that there would be sufficient time to complete our review in advance of issuing our audit opinion.

3.65 At the end of August, the Council finally concluded that it was unable to fully reconcile the bank reconciliation, leaving a difference of £5,891 between the cash book and the bank account. A recommendation has been raised in Appendix A of this report to ensure that the bank reconciliation is completed on a regular basis and is fully reconciled.

3.66 Although this residual difference is not material to the financial statements, it warrants inclusion in this report due to the delays incurred in auditing this area of the accounts and the fundamental importance of the bank reconciliation to both the control of the Council's finances and the audit of the financial statements.

3.67 We consider the absence of bank reconciliations generated by Agresso from November 2011 to August 2012 to represent a significant weakness in the control environment in both 2011/12 and also 2012/13. At the time of drafting this report we understand that the reconciliation for April 2012 has still not completed.

Group Accounts

3.68 On auditing the Group Accounts we identified that the intra company balances had not been eliminated in full. The signed intra company agreement between the Council and South Essex Homes (SEH) showed a total debtor balance owed to the Council of £2.4m. However on consolidation the Council only eliminated the cash in transit element of this balance of £1.1m and as a result an adjustment was required to the Group Balance sheet.

3.69 Some other minor amendments were required to the figures included in the notes to the Group Accounts, as the original values were based on the unaudited SEH accounts, but have now been amended to reflect the audited SEH accounts.

Other matters

3.70 We are required to communicate other 'audit matters of governance interest that arise from the audit of the financial statements' to you which includes:

- significant deficiencies in internal control identified during the audit
- matters specifically required by other auditing standards to be communicated to those charged with governance (for example issues relating to fraud, compliance with laws and regulations, subsequent events etc.)
- other audit matters of governance interest.

Weaknesses in Internal Control

3.71 The Council implemented a new accounting system, Agresso, during the 2011/12 financial year. The Agresso modules incorporating accounts receivable, accounts payable and the general ledger were implemented from the beginning of November 2011. The payroll module was implemented from the beginning of February 2012.

3.72 The implementation of the Agresso system has been undertaken on a risk assessed phased basis, with ongoing developments continuing to the system following the commencement of use of the system. What this means is that controls surrounding the system for various elements (e.g. debt recovery) had not been designed or implemented at the point at which the core computer system was switched on. The "risk assessed" aspect reflects management's decision to cease certain activities entirely until appropriate controls had been designed and implemented.

3.73 In our experience this is an unusual approach to the development of a new system, which would usually involve development, testing and parallel running before full implementation.

3.74 In addition to the design issues, as referred to earlier, both Internal Audit and external audit encountered uncertainties with staff (finance and other) relating to how the systems operated. As a result it was necessary to liaise directly with the Agresso support team to progress our controls assessment and testing work. This suggests weaknesses in the core project development processes.

3.75 The Council has recognised that there are lessons to be learnt from the introduction of the Agresso system in the Annual Governance Statement, and we support that assertion and encourage the Council to take that learning into the ongoing development of the Agresso system and other future system development projects.

3.76 We have previously reported the findings of some of our systems work to the Audit Committee, and we have raised recommendations to address some of the issues, where relevant, in the action plan at Appendix A.

Reliance on Internal Audit's work

3.77 We were able to rely on work completed by Internal Audit where this had been undertaken. However, there have been a number of issues that have contributed towards a reduction in the planned extent of reliance on Internal Audit's work and increased external audit work and fees:

- Timing of work: in a number of cases when Internal Audit had scheduled field work the extent of clarity about the control environment and specific controls, both within and outside of Agresso (although more outside) was insufficient to enable an efficient audit to progress;
- Focus of work and consequences of control failures: External audit work focuses on specific key controls that assist delivery of an efficient audit, where reliance on particular controls allows a reduced level of auditing compared to an approach excluding controls reliance. In some cases, the extent of resource required if controls are not present or fail is critical, even to the extent of preventing the issue of an unqualified opinion. Given the potential consequences of certain control absences or failures, we have had no real alternative but to pursue solutions, including seeking alternative sources of information, understanding and evidence. In some cases this has required direct interaction with Agresso support where finance staff were unable to demonstrate understanding of control framework design and operation, and in others extended sample sizes and/or alternative testing strategies where the original planned approach ran into barriers. This flexibility is not necessarily available to Internal Audit, given their wider remit and balance of resource;
- Internal Audit resources: resource pressures have not permitted persistence with audits where accessible responses and evidence was not made readily available to them. This is linked to the timing and focus issues set out above.

Understanding of system operation and controls

3.78 As a result of the issues raised above our audit information needs required us tomeet with the Agresso Consultant to gain an understanding of the system and controls in place for the Accounts Payable and Accounts Receivable functions. This included understanding the reconciliations being completed and the checks undertaken between modules on Agresso, controls around segregation of duties and general controls around the authorisation processes in place for each of these systems.

3.79 An example of uncertainties causing difficulty was in the recognition of cash payments through the cash receipting system. Under CEDAR, because the cash receipting system was not integrated into the general ledger, it was necessary to post the value of cash receipts taken on a daily basis to the general ledger and the debtors system, in order that the cash receipts would be recognised in the accounts and any debtors that had been raised could be recognised as paid. Under Agresso, because the cash receipting system is integrated into the general ledger and debtors system, this process became automated with the cash receipts automatically recognised in the general ledger and the debtors system.

3.80 However, this was not properly understood by relevant staff and therefore postings of the cash receipts to the general ledger and debtors system were continued. As the Agresso system was already automatically making those postings, this resulted in double counting of the cash receipts on the general ledger and debtors system, which amounted to £9.7m before this was identified by finance staff and reversed. The financial statements were prepared with an awareness of this issue and therefore this had already been adjusted for in the draft accounts that were presented for audit.

System change management

3.81 Internal Audit have undertaken work to review the Council's controls over change management and this has identified that the arrangements have changed since the implementation of Agresso on 1 November 2011. For the period covered by the financial statements, up until 1 April 2012, there was a well structured approach with change request forms that should have been used to document and evidence the need for changes to the system. However, Internal Audit has concluded that this process was not followed on a few occasions and therefore there was a risk of inappropriate changes having been made to the operation of the system.

3.82 In the period since 1 April 2012, after the year of audit, the use of the change request forms ceased with a more informal process adopted, including the disablement of the audit trail log recording activities performed on the system. This means that the audit trail of changes being made to the system is not adequate and there is a risk that unauthorised and inappropriate changes are made to the system and cannot be subsequently identified. At the time of drafting this report we have been unable to determine why the audit trail was disabled or who authorised this action.

3.83 We recommend that the audit trail log recording activities performed on the system be re-instated immediately and that more formal control procedures over the approval and authorisation of changes to the system are re-instated.

Authorisation of journals

3.84 In prior audits we have recommended that the Council strengthens its controls around the authorisation of journals. For the 7 months period where the old system was in place, this remained an issue with no evidence of authorisation of journals being in place and a lack of segregation of duties between raising, authorising and posting a journal.

3.85 The implementation of Agresso has strengthened the control environment as only the three Group Accountants, two Finance Group Managers and the Head of Finance and Resources are now able to authorise journals. However, there remain no controls in place to prevent one of these officers from raising and authorising their own journals, resulting in a lack of segregation of duties. This lack of segregation of duties means there remains a risk of management override of the results reported in the financial statements.

3.86 We understand that, subsequent to the provision of this report, controls have now been changed to introduce appropriate segregation of duties.

Accounts receivable

3.87 A number of control weaknesses were identified within the accounts receivable function of Agresso.

3.88 Testing identified that all staff that have access to the E-Form used to request that an invoice is raised through the intranet. The E-Form is processed to raise the invoice on Agresso by Accounts Receivable officers, who check to confirm the appropriateness of that invoice, but may not have the wider knowledge of the workings of the Council to properly make that check, because their processing role does not encompass this. This creates a risk that invoices are inaccurately raised or that income is incomplete.

3.89 The same issue also applies to credit notes that can be requested by any member of staff with access to Agresso, and are also processed by accounts receivable, with only reasonableness checks being completed. Stronger controls were present when the Council used Cedar as the facility to raise invoice request forms and credit note request forms were restricted to authorised officers only.

3.90 We are aware, and it has been confirmed through our testing, that the Council did not perform any debt recovery action from the period November 2011 to January 2012. During the period February to March 2012, limited recovery action was undertaken. This has resulted in a larger number and value of debtors outstanding at the year end. The Council now has full debt recovery action in place.

3.91 Under the Agresso system the accounts receivable Manager is able to authorise all refunds, irrespective of their value. Previously, stronger controls were in place with the s.151 Officer having to authorise refunds over a certain value. This provides an additional control over the most significant refunds that are being made. In 2011/12, the total value of refunds processed was not material. However, this is a weakness in the control design which should be addressed.

3.92 Our testing also identified that there are 19 officers who can raise invoices on the Agresso system and can receipt income via the paye.net system. This results in a lack of segregation of duties in the income receipting function. As this is a telephone payment system, receiving electronic payments only, the risk of misappropriation is reduced. However, this is a weakness in design which should be addressed.

Accounts payable

3.93 The controls around the accounts payable function were found to be operating effectively for the period of the year for which Agresso was functioning. However, it was noted that Officers continue to process a large number circumventing the electronic Agresso E-Procurement system. This results in an additional workload for the Accounts Payable team as all orders then have to be input manually onto the Agresso system.

3.94 Further, whilst we recognise that the Agresso system has strong and effective controls over payments (in that no payment can be made without necessary authorisation), the weaknesses in ordering mean that by the time this control takes effect, the Council may have taken delivery of goods, or received services, that were not necessary or not at prices that offered value for money, by which time it is too late to change.

3.95 This “culture” issue is not new to the Council, and was visible during the CEDAR periods in terms of the extent to which the Marketplace ordering system was worked around. We understand the efforts being made by the Council to address this cultural issue, and that there will not be an overnight solution. The Council should work towards ensuring that all staff use the E-Procurement system, so that it can deliver its full potential and a recommendation has been raised in Appendix A.

Reconciliations

3.96 On implementation of the Agresso system, reconciliations were not routinely completed or were not completed in accordance with requirements of the control environment.

3.97 As many of the systems are now integrated, there is reduced requirement to complete a manual reconciliation, as the checks between modules should be an automated process. However, officers continued to *complete* manual reconciliations during the period under review.

3.98 Whilst the need to perform manual reconciliations is reduced due to the integrated nature of the accounting modules on Agresso, officers should still be *reviewing* the automated reconciliations to ensure that the transactions have been appropriately recognised by the system, and that the separate modules remain reconciled.

3.99 Issues with and delays in the bank reconciliation have been referred to earlier and are therefore not repeated here.

Annual Governance Statement

3.100 We reviewed the draft Annual Governance Statement and discussed this with senior officers,and, with the appropriate changes now made, we are satisfied that the finalised Annual Governance Statement is not inconsistent or misleading with other information we are aware of from our audit of the financial statements.

Whole of government accounts

3.101 Our work to review the consistency of the whole of government accounts return with the audited financial statements is in progress and a verbal update will be given at the Audit Committee on 26 September.

Foreword to the Statement of Accounts

3.102 We read the Foreword to the Statement of Accounts although this is not part of our true and fair opinion on the financial statements. The Foreword includes the required content specified by the Code.

Written representations

3.103 We are required by ISAs to obtain written confirmation from you of certain representations that have been made during the course of our audit. The draft letter of representation has been attached as Appendix C.

3.104 We do not anticipate any changes being required before providing our opinion on the financial statements.

Audit report

3.105 Subject to satisfactory resolution of the following outstanding issues and final clearance of the audit through our internal quality controls, we anticipate issuing an unqualified audit opinion on the financial statements:

- Resolution of some queries relating to the Cash Flow statement.
- Receipt of some HR contracts for officers working at the Schools to confirm payroll expenditure.
- Completion of additional physical verification testing of fixed assets
- Clearance of manager and partner review points.

3.106 We will provide a verbal update as necessary on these outstanding issues at the Audit Committee.

4 Use of resources

4.1 We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources (value for money).

4.2 In accordance with our Audit Plan, our principal work in arriving at our value for money conclusion was comparing the Council's performance against characteristics specified by the Audit Commission in its guidance to auditors. The focus of our work in 2011/12 involved reviewing the financial resilience of the organisation and its arrangements for securing economy, efficiency and effectiveness in the use of resources.

Financial resilience

4.3 Our financial resilience work has considered the Council's arrangements for financial governance, financial planning and financial control, including improvements in arrangements over the prior year.

4.4 During 2011/12 the Council updated the four year Medium Term Financial Strategy (MTFS), as part of setting the budget for 2012/13, that identifies the budget gap that needs to be addressed through the Council's financial planning arrangements following the financial settlement announced during the year.

4.5 The budget gap of £32.5 million is forecast to arise as follows:

- 2013/14: £13.0 million (increased from £5.5 million in the previous MTFS)
- 2014/15: £ 8.5 million (decreased from £9.0 million in the previous MTFS)
- 2015/16: £11.0 million

4.6 The Council's political and managerial leadership understand the financial position and challenges being faced by the Council over the Medium Term Financial Strategy period, and the need to reduce budgets to match the available resource.

4.7 The Council's financial planning arrangements are being utilised to manage the process. However, there remains work to do to determine specific detailed plans as to how the reductions will be achieved and then implement the actions required by those plans to continue to deliver a balanced financial position into the medium term.

4.8 The Council has maintained its good track record of member and officer involvement in reviewing financial matters and consulting on expenditure priorities. Clear leadership is shown in ensuring that the Council's overall financial position is understood within the organisation and among partners.

Medium Term Financial Strategy

4.9 We reviewed the MTFS, undertaking a comparison exercise with other authorities within our portfolio, and concluded that the assumptions made were reasonable and that the Council had considered all eventualities and the impact of future changes within the local government arena.

Overall, the Council faces challenges in order to be able to manage the delivery of the required savings over the next few years to address the budget gap. However Members and officers are aware of and recognise this situation and are working to find ways to support ongoing financial resilience.

Financial outturn 2011/12

4.10 In 2011/12 the Council overspent against the budget overall for the year by £65k, after making an additional contribution to general earmarked reserves of £4.5m (making a total actual contribution to earmarked reserves of £7.2m (including an increase of schools balances of £0.9m)). This reflects the work that was on-going during 2011/12 to address the financial situation being faced by the Council. The Council will need to continue to demonstrate this level of financial control, and secure further improvements, in order to continue to deliver against the budgets of future years.

4.11 In 2011/12 the HRA overspent against the budget overall for the year by £0.24m, and therefore had to utilise more HRA reserves that had been planned.

4.12 Along with all other Councils, Southend was notified of a reduction in central government funding which lead to the need to identify revenue savings of £15.5m for 2011/12. Saving and efficiency initiatives were identified to fund the gap in 2011/12 as part of the budget setting process, including through a reduction in staff costs and through an expectation of service reviews leading to a transformation in the way services are delivered to reduce resource utilisation and the Accommodation Strategy.

4.13 Given the financial challenge the Council has been facing a new programme of corporate work streams was developed for the 2011/12 financial year to continue with the efficiency drive and to support the identification of savings for future years. This provides the Council with a means drive transformational change in the organisation and should enable a focus to be placed on delivery of the significant savings that will be required over this period.

4.14 The corporate work streams that were established to identify and deliver future corporate savings are:

- Contract rationalisation
- Shared localised delivery
- Shared services and alternative delivery models
- Review & streamlining of systems
- Trading & Trading companies

4.15 The Council's general fund balance at 31 March 2012 is £11.5 million, which is between the Council's approved target optimum level of £10.0 million and maximum level of £12.0m of the net revenue budget. The value of unallocated financial reserves (the general fund balance) as a proportion of total net expenditure is in the highest third quartile compared to other unitary councils, and therefore is not out of line with expectations.

Budget 2012/13 and beyond

4.16 To assist with addressing the budget gap in 2012/13. as part of setting the budget for the year the Council identified planned savings of £11.8m across the Council directorates as follows:

- Adult and Community Services £2.9m (£6.4m in 2011/12)
- Children and Learning £2.0m (£3.4m in 2011/12)
- Enterprise, Tourism and the Environment £1.6m (£3.3m in 2011/12)
- Support Service £0.9m (£1.9m in 2011/12)
- Corporate £0.4m (£0.5m in 2011/12)
- Workstreams £4.0m

4.17 From our review of the latest forecast position, the Council is slightly ahead of where it planned to be to deliver its 2012/13 financial objectives and targets. Management are now working to maintain this position for 2012/13 and are beginning to develop the budget for 2013/14 and beyond. Arrangements for reporting progress to Members have been enhanced to include commentary on both year to date and forecast outturn variances, as well as a Red / Amber / Green ratings for the progress in delivering the budget savings targets.

4.18 Variances against both the service budgets and the budget savings will need to be addressed so that the Council can achieve its planned financial position for 2012/13 as a further stepping stone to addressing the medium term budget gap. If the 2012/13 plans are not achieved this will exacerbate the reductions to be delivered in future periods, making it even more difficult to achieve a balanced budget position in future periods.

4.19 Review of the Audit Commission's VFM profile tools indicates that net expenditure per head of population is high compared to other unitary councils, although the actual level of expenditure is low when compared to other unitary councils.

4.20 Most services are operating at an average level of expenditure per head, although adult social care costs per adult are in the top third for unitary councils and this may be an area for further consideration as part of future budget setting rounds.

4.21 Overall the Council is working to manage the delivery of the required savings over the MTFS period and currently has sufficient flexibility in its reserves to remain financially resilient.

Challenging economy, efficiency and effectiveness

4.22 Our review of economy, efficiency and effectiveness has considered the Council's arrangements for prioritising resources and improving efficiency and productivity.

4.23 The budget set for 2011/12 ensured that resources were allocated in accordance with the Council's priorities. As the Council continues to challenge the resource allocation in the next round of budget and medium term financial planning, the Council must ensure that it continues to focus resources to address priorities, and re-visit these priorities to ensure that they remain appropriate to the needs of the Borough.

4.24 The gap for 2012/13 has been identified as another £12.0m reduction in resource, in addition to the £15.5m reduction required in 2011/12. If the 2012/13 savings are not realised, then this will increase the savings required in 2013/14 and beyond. Staff are currently being actively engaged in a reinvigoration of the process to identify ways of transforming services, by being encouraged to put forward suggestions for other saving and efficiency ideas and are being challenged to produce these ideas through the use of People and Organisational Development staff and methodologies. To achieve the significant savings required in the medium term it will be necessary to identify and implement more transformational changes to the way services are delivered, in order that different ways of working, that are more efficient and require reduced resource input, whilst continuing to deliver those services, are identified and implemented.

4.25 Members have a clear understanding of the Council's financial challenges and are being supportive of officers in the budgetary process and on-going financial management of delivering against the budget, and the change in the balance of political power that occurred in May must not be allowed to distract attention from the focus on delivering the radical changes that will be required to continue to balance the finances in the medium term.

4.26 Key focus areas in the medium term include:

- ensure that the anticipated financial benefits are realised from the work being done on transforming services
- ensure that the anticipated financial benefits are realised from the work being done on rationalising and renegotiating external contracts
- ensure that the anticipated financial benefits are realised from the work being done on the Civic Centre and the rationalisation of accommodation requirements through the new ways of working
- review and update the strategic priorities, ensuring key stakeholder engagement in the process and sufficient capacity and resources are invested, to align the revised financial resources to strategic priorities and
- review the latest Audit Commission value for money profiles tools to identify areas to target for potential cost reduction.

Links between budget proposals and service performance

4.27 There is a clear trail of considerations made by the Council in terms of the potential impact that budget decisions may have on services, through initial service considerations against their budget, efficiency savings proposals from services and challenge by the Performance Improvement Task Group, Cabinet, Scrutiny and Council.

4.28 Explicit links between performance targets set for services and the decisions made as part of the budget process were less clear, although we understand the Council's objective of maintaining front line service performance and the need to set stretching targets where financial resources available are reducing.

4.29 The availability of more accurate assessments of the impact on performance of budget/resource levels at the point of budget setting (i.e. some form of sensitivity analysis, articulated in terms of relevant performance indicators) should improve managers' ability to identify viable efficiency gains and provide improved information to base strategic and policy-driven resource decisions.

Performance against 2011/12 priorities

4.30 The Council has been recognised for the progress that it continues to make, despite the challenges that it faces, by being awarded the Council of the Year award by the Local Government Chronicle.

4.31 The Council refined its formal performance management reporting during 2011/12, to reflect the reduced resource that is available to the Policy and Performance Team As a result the number of corporate performance indicators has been reduced to 30, alongside 11 "outward facing" indicators that the Council expects to be of interest to the public.

4.32 Of the 30 corporate performance indicators 26 (86.6%) met their year end targets. This compares to 84% of corporate performance indicators achieving their targets in 2010/11. Of the 24 indicators for which data is available for the previous year, 18 have maintained or improved performance in 2011/12.

4.33 All of the 11 "outward facing" indicators met their target for 2011/12.

4.34 Performance and other achievement highlights for the year include:

- Being judged as Council of the Year by the Local Government Chronicle
- Being judged as having the Children's Services team of the year by the Local Government Chronicle
- Delivery of significant projects including the new City Beach, the revitalised Warrior Square Gardens and the improved Victoria Gateway
- Being awarded the Purple Flag accreditation, by the Association of Town Centre Management, recognising excellence in the management of town and city centres at night
- A reduced number of average working days lost to sickness from 7.45 days in 2010/11 to 7.27 days in 2011/12, marginally behind the target of 7.26 days, but better than the sector average
- Reduction in the number of schools in Ofsted special measures category from three to zero
- Levels of recycling have improved year on year from 28% five years ago to 46.6% in 2011/12 compared to a target of 45%, and at the same time residual household waste has reduced and came in under the target of 520kg, at 497kg per household

Housing Revenue Account self-financing

4.35 The Government have changed the financial support arrangements in place for the housing revenue account, withdrawing the current subsidy arrangements, whilst giving Councils more freedom to manage the housing stock in a way that is self-sustaining.

4.36 This has involved the Council incurring an additional £34.7m of debt, as the Government process has concluded that the stock value is greater than the existing housing debt supported by the HRA subsidy. These new arrangements pose a risk to the financial resilience of the HRA and therefore it is important that the financial position is effectively managed.

4.37 As a result the Council has produced a 30 year HRA financial business plan indicating rental and other income streams, as well as repairs and other stock management expenditure over the 30 year time horizon. This is based on expectations and assumptions set now about how things will change and develop in the future.

4.38 This plan indicates the financial results that need to be achieved each year to manage and maintain the HRA's financial position, and based on the current position indicates that the HRA debt is expected to be fully paid down by 2030/31, after which the financial position would become much stronger.

4.39 Clearly trying to make assumptions and set expectations many years into the future is fraught with difficulty and uncertainty. Therefore the Council needs to monitor progress against the HRA business plan and update and revise assumptions as circumstances change and the situation begins to crystallise. This will enable to the Council to manage the financial position of the HRA and ensure that this remains resilient into the future.

4.40 The Council is also considering the options available to structure the relationship between the Council and the housing management service (currently ALMO), in order that this can be structured on the optimum basis given the new environment in which the housing management service is operating. A proposal will be made through the pre-Cabinet scrutiny process through October 2012, ready for the Cabinet meeting in November 2012 to make a decision about the best structure to take the housing management service forward. At this point in time the pitfalls and benefits of all options are being considered and balanced in order that a recommendation can be made to the Cabinet meeting in November.

4.41 Overall the Council has a long term business plan that sets out the expected financial performance and position of the HRA over the next 30 years. However, this needs to be developed further into a more detailed strategic plan for the HRA that sets out how this is going to be delivered and what actions are going to be taken to make this happen.

Health and Wellbeing Board

4.42 Following the passing of the Health & Social Care Act, as part of the Government's changes to the management of the NHS, top tier and unitary councils have been required to create a Health and Wellbeing Board to act as a forum where key leaders from the health and care system work together to improve the health and wellbeing of their local population and reduce health inequalities.

4.43 Each top tier and unitary council will have its own health and wellbeing board. Board members will collaborate to understand their local community's needs, agree priorities and encourage commissioners to work in a more joined up way. As a result, patients and the public should experience more joined-up services from the NHS and local councils in the future.

4.44 Health and wellbeing boards are a key part of the Government's broader plans to modernise the NHS to:

- ensure stronger democratic legitimacy and involvement
- strengthen working relationships between health and social care, and
- encourage the development of more integrated commissioning of services.

4.45 The boards will help give communities a greater say in understanding and addressing their local health and social care needs.

4.46 Boards will take on their statutory functions from April 2013 and are operating in shadow form, preparing to take on their responsibilities until then.

4.47 The Southend Shadow Health & Wellbeing Board has a terms of reference that sets out it's time limited nature in preparing the way for the introduction of the statutory board by April 2013. The terms of reference clearly set out the aims and objectives of the Shadow Board.

4.48 The Shadow Board members provide a range of representation that is compliant with the minimum requirements specified in the legislation, except that there is currently no representative from Healthwatch, which the terms of reference recognise and have made provision to include from April 2013 when the Board achieves statutory status. The Shadow Board should consider the potential benefits of expanding the membership of the Board to include a wide range of perspectives and expertise, such as representatives from the charity or voluntary sectors, in order to gain the benefit of their insight and understanding of the needs of the local population.

4.49 The key work being undertaken by the Shadow Board at the moment is the:

- refresh of the Joint Strategic Needs Assessment
- development of the Health and Wellbeing Strategy
- informing of the Clinical Commissioning Groups plans

4.50 The first two of these are in the final phases of development before going out to public consultation, so that the responses from the public can be assessed and used to inform the JSNA and H&WB strategy in advance of their formal adoption by the Health and Wellbeing Board.

4.51 The Council needs to ensure this work is prepared and completed before the Board achieves statutory status from April 2013, and has a timetable in place to deliver the work in advance of the commencement of the statutory board.

4.52 Overall the Council has been making good progress with the development of the machinery for the Health and Wellbeing Board in preparation for the Board to take on its statutory functions from 1 April 2013. However, the Board needs to fully embed these arrangements and develop action plans for the work that needs to be undertaken particularly in respect of the development of targets and performance management arrangements. This will be aided by the forward planning work that the Shadow Board has approved to be undertaken.

Audit report (value for money conclusion)

4.53 Our value for money conclusion is based on considering our overall risk assessment, focusing on the two criteria set by the Audit Commission, and the results of risk based audit work, as well as consideration of the processes underpinning your review of the effectiveness of your controls as described in your Annual Governance Statement.

4.54 We are satisfied that, in all significant respects, the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2012. We propose issuing an unqualified value for money conclusion.

Appendix A: Action Plan

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
Financial statements				
1. Fixed asset register As reported in the prior year, the Real Asset Management system (RAM) had not been fully operated and kept up to date through the 2011/12 financial year, because of resourcing issues faced by the finance team at the Council. As a result the information contained within the system had become out of date and needed additional work at the year end, resulting in a delay in providing the information for audit.	The RAM system should be used throughout the year to record the transactions undertaken relevant to the Council's fixed assets. This will ensure that the year end production of the financial statements is less time consuming and can more easily demonstrate that all assets and transactions have been included within the financial statements.	Agreed - as each asset event (e.g. revaluations, depreciation, additions etc.) is undertaken throughout the year, the RAM system and the general ledger will be updated at that time. The RAM system and the general ledger will be reconciled after each of these events to ensure they remain in balance.	Caroline Fozzard (Group Manager - Financial Planning & Control)	September 2012
2. Fixed assets classification Our testing identified some assets that were categorised within other land and buildings, when they were fixtures and fittings and therefore should have been classified as vehicles, plant and equipment. The Council should ensure that all assets are correctly classified on the fixed asset register to ensure correct inclusion in the financial statements.	Ensure that all assets recorded on RAM are correctly classified to ensure correct inclusion in the PPE notes within the financial statements.	Agreed - a review of the fixed asset register will be undertaken during 2012/13 and a sample of assets will be checked each financial year.	Caroline Fozzard (Group Manager - Financial Planning & Control)	March 2013

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
3. Fixed asset register Our testing identified that additions amounting to £3.6m were again added to the grouped infrastructure assets in the fixed asset register. Grouping of assets is no longer appropriate and makes it impossible to identify the specific assets that are recorded in the fixed asset register, and therefore the financial statements. It is also not possible to identify whether the register is correctly recording all of the assets that are owned by the Council and whether the assets recorded on the register continue to exist.	We recommend that as far as possible the Council populate the RAM system with accurate records on each individual asset held by the Council to ensure the FAR is fully complete and that the assets recorded continue to exist.	It would not be practical or possible to do this for assets already recorded on the RAM system – for example we do not have the information to disaggregate the infrastructure asset that relates to the road network transferred to the Council when it became a Unitary Authority. We accept the recommendation but wish to avoid a situation where the RAM system records every individual road link and piece of street furniture separately, as this would become unwieldy to administer. A pragmatic approach has been agreed whereby broad asset types within infrastructure assets will be identified and used from the 2012/13 financial year. For example, 'road network', 'street furniture' etc.	Caroline Fozzard (Group Manager - Financial Planning & Control)	March 2013
4. Related Party Transactions Our testing identified some that five members had not returned the documents requesting disclosure of relationships that may impact on their work as Members.	Ensure that all Members return their disclosure forms declaring potential relationships that should be disclosed as related party transactions, to ensure the completeness of the notes within the financial statements.	Agreed – guidance to Members will be updated to further stress the need to provide this information	Ian Ambrose (Group Manager – Financial Management)	March 2013

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
5. Debtor with DCLG for Business Rates As in the prior year, there is a difference between the debtor recorded in the financial statements for business rates compared to that expected to be recorded as a debtor under the NNDR agency arrangements. In the prior year, this amounted to £482k, however this difference has now increased to £1,129k (including the prior year difference). The difference has arisen within the Northgate system, however the Council is unable to identify exactly what this relates to. The Council is working with Northgate to resolve this difference.	Liaise with Northgate to resolve the recurring difference within the Northgate system to ensure that this is rectified before the compilation of the 2012/13 financial statements.	Agreed.	Caroline Fozzard (Group Manager - Financial Planning & Control) Ian Ambrose (Group Manager – Financial Management)	June 2013
6. Car Park Income Our testing identified that the Council do not complete a reconciliation between the amount of income received from the company which runs the credit card services for the Council's parking machines, and the amount of credit card payments made per the audit ticket from the individual parking machines. This means that the Council could be losing income if the correct amount is not being paid over by the credit card company.	Complete a reconciliation on a regular basis between the actual income received and the income per the receipts (minus any fee taken by the company) to ensure that income received through this means is at the level expected.	Agreed – ETE will carry out a monthly reconciliation of electronic car parking payments.	Derek Kenyon (Car Parking Manager)	October 2012

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
7. Analysis of Debtors and Creditors Our testing identified instances where debtors and creditors were misclassified in the analysis notes within the financial statements. In particular, the accounts receivable and payable codes were all posted as 'general' debtors and creditors without being appropriately analysed into the sub-headings within their associated notes. Some receipts in advance with central government were included as central government creditors and some were classified as receipts in advance. The differences arise due to Group Accountants treating items differently when they post items to the ledger codes. Although the Council did amend for all misclassifications above triviality, the Council should endeavour to ensure that the classifications within these notes are accurate.	Ensure that Group Accountants use a consistent approach when posting debtor and creditor balances on the ledger to ensure that they are correctly classified within the debtor and creditor analysis notes. Complete a check on the amounts included within the accounts payable and receivable codes to ensure that they are re-analysed in the debtor and creditor notes as appropriate.	Agreed - year end guidance to the finance teams will be updated to stress the necessity of consistent analysis of debtor and creditor balances to ensure correct treatment in the analysis notes of the Financial Statements.	Ian Ambrose (Group Manager – Financial Management)	June 2013
Internal controls				
1. Change management The use of the change request forms has ceased with a more informal process adopted. This increases the risk that unauthorised and untested changes to the system lead to unnecessary disruption or affect data integrity.	Document and enforce formal change control procedures when amending the Agresso software. Ensure all changes to systems are specified, approved, tested and authorised for implementation.	Agreed - this has already been implemented	N/A	N/A

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
2. Audit trail The disablement of the audit trail of activities performed on the system means that the audit trail of changes being made to the system is not adequate and there is a risk that unauthorised and inappropriate changes are made to the system and cannot be subsequently identified.	The system audit trail should be enabled and monitoring processes established to detect unauthorised changes to the system.	Agreed – appropriate audit trails will be established and implemented through the Change Control procedure, and suitable monitoring arrangements put in place via the Change Advisory Board (CAB).	Andy Mardon Caroline Fozzard (Group Manager - Financial Planning & Control)	
3. Reconciliations Our audit work identified that the bank and payroll reconciliations were not being completed on a monthly basis. This resulted in a delay in receiving the year end reconciliations for these areas and adjustments being required to be made to the financial statements as a result. We also identified that, since the implementation of Agresso, Officers have not been utilising the reconciliation / checks between the feeder modules as the system intends. Instead manual reconciliations were being used.	Ensure that all reconciliations are completed on a monthly basis and that the year end reconciliations are completed in time for the closure of the 2012/13 financial statements. Ensure that reconciliations within the Agresso system are completed as the system intended, making use of the automated reconciliation controls within the system.	Agreed. We are working towards that position, however there needs to be changes to systems outside of Agresso so that the cashbook information can be disaggregated in a way that enables automated reconciliation. Until automation can be successfully enabled, reconciliations will continue to be manually compiled.	Caroline Fozzard (Group Manager - Financial Planning & Control)	May 2013

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
4. Authorisation of Journals Six officers are able to raise and process their own journals. These are: the three Group Accountants, two finance Group Managers and the Head of Finance of Resources. There is a risk of management override as any of these officers is able to raise and post their own journal without a secondary check. A mitigating control should be put in place to prevent unauthorised journals being processed.	Amend the parameters within the Agresso system to ensure that these six officers are unable to raise and authorise their own journals.	Agreed and actioned - parameters within Agresso have been updated such that senior finance staff can no longer load journal files into Agresso.	N/A	N/A

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
5. Accounts Receivable - **Invoice / credit notes** Testing identified that all staff that have access to the Agresso system are able to request that an invoice is raised using the E-Form provided by Agresso. The E-Form is processed by Accounts Receivable officers, who check to confirm the appropriateness of that invoice, but may not have the detailed knowledge of the workings of the Council to properly make that check. This creates a risk that invoices are inaccurately raised or that income is incomplete. This also applies to credit notes, which can be requested by any member of staff that has access to Agresso and is processed by accounts receivable, with only reasonableness checks being completed. Stronger controls were present when the Council used Cedar as the invoice request forms and credit note requests were restricted to authorised officers only.	Review user access to the invoice request module on Agresso and ensure that access is limited to appropriate officers or introduce checks within individual departments on the invoice request forms before they are processed by the accounts receivable department.	Agreed – a review will be undertaken to establish an appropriate control arrangement.	Christine Lynch (Revenues Manager)	December 2012
- **Refunds** The accounts receivable Manager is able to authorise all refunds irrespective of their value. Previously stronger controls were in place and the S151 Officer had to authorise refunds over a certain value. In 2011/12 the value of refunds processed was not material, however this is a weakness in the control design which should be addressed.	Enforce authorisation limits on the processing of refunds to ensure that they are appropriately authorised by Senior Officers at the Council.	Agreed – a review will be undertaken to establish an appropriate control arrangement.	Christine Lynch (Revenues Manager)	December 2012

Conclusions from work	Recommendations	Management responses	Responsibility	Timing
- **Segregation of duties** Our testing identified that there are 19 officers who can raise invoices on the Agresso system and can also receipt income via the paye.net system. This results in a lack of segregation of duties in the income receipting function. As this is a telephone payment system the risk of misappropriation is minimal, however this is a weakness in design which should be addressed.	Ensure that there is adequate segregation of duties in place between the requesting and receipting function within accounts receivable.	Agreed – a review will be undertaken to establish an appropriate control arrangement.	Christine Lynch (Revenues Manager)	December 2012
6. Accounts Payable Officers continue to process a large number of orders outside of the electronic Agresso E-Procurement system. This results in an additional workload for the Accounts Payable team as all orders then have to be input on the Agresso system. The Council should work towards using the E-Procurement system to its full potential.	Remind staff the importance of using the Agresso E-Procurement system for raising orders and work towards restricting staff from raising orders outside of this system.	Agreed – continued action around the cultural shift, training and guidance throughout the organisation for compliance with E-Procurement system.	Joe Chesterton (Head of Finance and Resources)	March 2013
7. Progress with recommendations Progress with the implementation of external audit recommendations is not routinely reported to the Audit Committee. As a result the Audit Committee is not provided with ongoing assurance that agreed external audit recommendations are being implemented appropriately.	Progress with the implementation of external audit recommendations should be reported to the Audit Committee on a regular basis.	Agreed – progress with implementing external audit recommendations will form part of the regular progress report to those charged with governance from PKF.	Joe Chesterton (Head of Finance and Resources)	January 2013

Appendix B: Uncorrected misstatements

The table below details the potential differences recorded during the audit which are not adjusted for currently within the financial statements:

Unadjusted misstatements	Income Over/ (Under) £'000	Expenses (Over)/ Under £'000	Assets (Over)/ Under £'000	Liabilities Over/ (Under) £'000	Reserves (Over)/ Under £'000	Management comments
Factual misstatements						
Overstatement of the debtor balance with DCLG for the Business Rates payment to the pool. The debtor figure included in the financial statements is greater than the amount expected from review of the figures and the adjustment required to account for NNDR on an agency basis. The error is as a result of a roll forward balance within the Northgate system, which the Council is unable to identify what this relates to in order for a correction to be made. The overstatement of £1,129k includes the prior year error of £482k, which has rolled forward within this balance.			(1,129)		1,129	These are immaterial misstatements in the context of the financial statements and will therefore not be amended.
Lease payments Testing identified the incorrect capitalisation of lease payments for the waste disposal facility. This should be treated as REFCUS.		164	(164)			

Unadjusted misstatements	Income Over/ (Under) £'000	Expenses (Over)/ Under £'000	Assets (Over)/ Under £'000	Liabilities Over/ (Under) £'000	Reserves (Over)/ Under £'000	Management comments
Judgemental misstatements						
Intangible assets Within intangible assets there is a group of software items that the Council is unable to identify. We were unable to confirm the existence of these assets through our testing.		1,144	(1,144)			These are immaterial misstatements in the context of the financial statements and will therefore not be amended.
Bad debt provision Testing identified that the bad debt provision included within the financial statements is understated. This is due to the incorrect value being posted on the ledger compared to the workings prepared by the Council for the provision required.			(675)		675	
Hinguar school land The Council owns the land provided for the new school site, but has not undertaken a valuation in order that it could be recognised in the fixed asset register and financial statements. Compared to the value of similar school sites in the vicinity it is likely that the assets are understated by approximately £1.75m.			1,750		(1,750)	
Projected misstatements (extrapolation of errors) None.						
Total net misstatements		1,308	(1,362)		54	
Total net misstatements						
- Net overstatement of costs		1,308				
- Net understatement of net assets			(1,308)			

Appendix C: Draft letter of representation

The following draft letter of representation covers the Council's Statement of Accounts which includes the pension fund financial statements. Representations for the preparation of the Statement of Accounts will be sought from the Director of Corporate Resources (as the Chief Finance Officer) and from Members on behalf of the Council in relation to its responsibility to approve the Statement of Accounts and the Annual Governance Statement.

PKF (UK) LLP
16 The Havens
Ransomes Europark
Ipswich
Suffolk
IP3 9SJ

28 September 2012

Dear Sirs

Financial statements of Southend-on-Sea Borough Council for the year ended 31 March 2012

This representation letter is provided in connection with your audit of the financial statements of Southend-on-Sea Borough Council for the year ended 31 March 2012 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view, have been properly prepared in accordance with the relevant financial reporting framework and have been prepared in accordance with the requirements of applicable law.

I confirm to the best of my knowledge and belief, and having made appropriate enquiries of directors and management of the Council, the following representations given to you in connection with your audit of the Council's financial statements:

FINANCIAL STATEMENTS

Responsibility for the financial statements

I acknowledge as Head of Finance and Resources and s151 Officer my responsibilities for the Statement of Accounts, which include the financial statements, and for ensuring that these are prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom.

Accounting policies

I confirm that the selection and application of the accounting policies used in the preparation of the financial statements are appropriate.

Significant assumptions

The following significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable and appropriate:

(a) Pension fund assumptions

I confirm that the actuarial assumptions underlying the valuation of the Local Government Pension Scheme (LGPS) scheme liabilities, as applied by the scheme actuary, are reasonable and consistent with my knowledge of the business. These assumptions include:

- Rate of inflation (RPI) 3.3%
- Rate of inflation (CPI) 2.5%
- Rate of increase in salaries 4.3%
- Rate of increase in pensions 2.5%
- Rate for discounting scheme liabilities 4.6%
- Expected return on assets 5.8%

I also confirm that the actuary has applied up-to-date mortality tables for life expectancy of scheme members in calculating scheme liabilities.

(b) Carrying value of land and buildings

Non-current assets revalued at fair value by the Council's expert valuers were assumed to be in a reasonable standard of repair, free from planning proposals likely to affect their value, and included in their valuation any relevant plant or machinery considered to form part of the asset;

(c) Valuation of Housing Stock

The useful economic lives of the housing stock and its constituent components, used in the valuation of the housing stock and the calculation of the depreciation charge for the year are consistent with those advised to us by the expert valuer appointed by the Council to provide this information.

(d) Bad debt provision

Amounts owed to the Council have had impairment allowances made for potential doubtful or bad debts, based on factors such as the age of the debt.

Plans or intentions

I confirm that the Council has no plans or intentions that may materially alter the carrying value and, where relevant, the fair value measurements or classification of assets and liabilities reflected in the financial statements.

Litigation and claims

I have disclosed to you all known actual or possible litigation and claims, the effects of which should be considered when preparing the financial statements and these have been accounted for and disclosed in accordance with the applicable financial reporting framework.

Related parties

I confirm that related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of the applicable financial reporting framework.

Subsequent events

All events occurring subsequent to the date of the financial statements for which the applicable financial reporting framework requires adjustment or disclosure have been adjusted or disclosed.

Uncorrected misstatements

I believe that the uncorrected misstatements identified during the audit are immaterial both individually and in aggregate to the view given by the financial statements as a whole. A list of these items is attached as an appendix to this letter.

Going concern

I confirm that I am satisfied that it is appropriate for the financial statements to have been drawn up on the going concern basis. In reaching this conclusion I have taken into account all relevant matters of which I am aware and have considered a future period of at least one year from the date on which the financial statements will be approved.

Comparative information

I confirm that, in respect of the restatements to implement the accounting policy changes for heritage assets, the adjustments relate to changes in accounting policies as I believe that the new accounting policies are more appropriate, and accordingly to ensure the consistency of accounting treatment between periods it is necessary to restate the current and corresponding periods on the basis of the new policies.

INFORMATION PROVIDED

Completeness of information

All the accounting records have been made available to you for the purpose of your audit. I have provided you with all other information requested and given unrestricted access to persons within the Council from whom you determined it necessary to obtain audit evidence. All other records and related information, including minutes of all management and Committee meetings held during the year and up to the date of this letter have been made available to you.

All transactions undertaken by the Council have been recorded in the accounting records and are reflected in the financial statements.

There is no relevant audit information needed by you in connection with preparing your audit report of which you are unaware.

Internal control

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

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

Fraud

I have disclosed to you the results of my assessment of the risk that the financial statements could be materially misstated as a result of fraud.

I have disclosed to you my knowledge of fraud or suspected fraud affecting the Council involving management, employees who have significant roles in internal control or others where the fraud could have a material effect on the financial statements

I have disclosed to you my knowledge of any allegations of fraud, or suspected fraud affecting the financial statements communicated to me by employees, former employees, analysts, regulators or others.

Compliance with law and regulations

I am not aware of any actual or possible instances of non-compliance with laws and regulations whose effects should be considered when preparing the financial statements of the Council.

Related parties

I confirm that I have disclosed to you the identity of the Council's related parties and all the related party relationships and transactions of which I am aware.

Liabilities, contingent liabilities or guarantees

There are no liabilities, contingent liabilities or guarantees to third parties other than those disclosed in the financial statements.

Title to assets

The Council has satisfactory title to all assets and there are no liens or encumbrances on the assets except for those disclosed in the financial statements.

Yours faithfully

Joe Chesterton

Head of Finance and Resources

Representations of the Council

We confirm to the best of our knowledge and belief, and having made appropriate enquiries of other officers and members of the Council, the following representations given to you in connection with your audit of the Council's financial statements.

Responsibility for the financial statements

We acknowledge our responsibilities to make arrangements for the proper administration of the Council's financial affairs and to approve the Statement of Accounts, which include the financial statements. The Head of Finance and Resources is responsible for the preparation of the Statement of Accounts, which include the financial statements, in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom.

Uncorrected misstatements

We have considered the uncorrected misstatements in the financial statements as listed in Appendix 1 to this letter together with the explanations provided by the Head of Finance and Resources for not correcting these misstatements, and we consider them to be immaterial to the view given by the financial statements.

Annual Governance Statement

We confirm that the Council has conducted a review during the year of the effectiveness of its system of internal control. We are satisfied that the Annual Governance Statement appropriately reflects the circumstances of the Council and includes an outline of the actions taken, or proposed, to deal with significant internal control issues.

Yours faithfully

Councillor Collins

Chair of the Audit Committee

Signed on behalf of the Council

Note: Appendix 1 referred to in this letter relates to Appendix B in this report