



PUBLIC SECTOR

## **Annual Audit Letter 2008/09**

Gloucester City Council  
19 November 2009

AUDIT

# Content

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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document.

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

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Ian Pennington, who is the engagement partner to the Authority, telephone 029 2046 8205, email [ian.penninton@kpmg.co.uk](mailto:ian.penninton@kpmg.co.uk) who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 236 4000, email [trevor.rees@kpmg.co.uk](mailto:trevor.rees@kpmg.co.uk), who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Investigation Officer, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by e mail to: [complaints@audit-commission.gov.uk](mailto:complaints@audit-commission.gov.uk). Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421

**Purpose**

This Annual Audit Letter (the Letter) summarises the key issues arising from our 2008/09 audit at Gloucester City Council (the Council). Although this Letter is addressed to the Members of the Council, it is also intended to communicate these issues to key external stakeholders, including members of the public. The Letter will also be published on the Audit Commission website at [www.audit-commission.gov.uk](http://www.audit-commission.gov.uk). It is the responsibility of the Council to publish the letter on its website at [www.gloucester.gov.uk](http://www.gloucester.gov.uk). Throughout our audit we have highlighted areas of good performance and also provided recommendations to help you improve performance. A summary of our key recommendations is set out in Appendix 1. We have reported all the conclusions in this letter to you throughout the year and a list of all reports we have issued is provided in Appendix 2.

**Scope of our audit**

The statutory responsibilities and powers of appointed auditors are set out in the Audit Commission Act 1998. Our main responsibility is to carry out an audit that meets the requirements of the Audit Commission's *Code of Audit Practice* (the *Code*) which requires us to review and report on your:

- *use of resources* - whether you have made proper arrangements for securing economy, efficiency and effectiveness (value for money) in your use of resources (UoR). Our work is summarised in section 2; and
- *accounts* – the Financial Statements and the Annual Governance Statement, summarised in section 3.

**Key Messages**

- Our **use of resources** assessment, the first under the Audit Commission's new UoR regime, demonstrated that the Council had sound processes in place for most elements of the assessment. However, we identified some weaknesses during our audit affecting aspects of each of the themes. These weaknesses had a specific impact on our assessment of the Council's arrangements for financial reporting, commissioning and procurement, and workforce planning. Despite the identification of such weaknesses we concluded that the Council had for the most part made proper arrangements to secure economy, efficiency and effectiveness in its use of resources. Our value for money conclusion was however qualified on the basis of these weaknesses.
- This year's **accounts** audit was difficult. The draft financial statements presented to the Council's Audit Committee in June 2009, and subsequently made available for public inspection, were of poor quality. Our audit work identified a number material errors and omissions along with a series of presentational and disclosure issues. Because of the difficulties in auditing the accounts we were not able to issue our audit opinion by the 30 September deadline. We worked closely with Finance staff to ensure the errors in the draft financial statements were addressed and, following this, we issued an unqualified opinion on the revised financial statements on 18 November 2009. We recognise that the Council's Finance department was under strain this year and this greatly affected the effectiveness of its arrangements for closing down its annual accounts. It is important that the Council takes steps to ensure that a complete and materially accurate set of financial statements can be produced by the statutory deadline next year. The Council has now recruited additional Finance staff which should help address these issues next year.

**Future Issues**

- From 2010/11, local government bodies are required to prepare their financial statements under International Financial Reporting Standards (IFRS), which contain a number of significant differences from the current financial reporting regime. The Council has started preparing for this transition, although as with all local authorities there remains much to be done to identify the full impact of IFRS on its accounting arrangements and to make the necessary changes.
- Those local authorities in the Carbon Reduction Commitment scheme will need to start reporting their usage from 1 April 2010 and recording these transactions within their financial statements with effect from 1 April 2011. There will be implications for cash flow, energy bills, and investment decisions and these could be significant. There are opportunities in addressing sustainability with clear cost reduction benefits from saving energy which will become more significant over time. There are also opportunities to use the sustainability agenda to support the achievement of business challenges. It puts carbon reduction firmly amongst the priority areas for local authorities, with the opportunities outlined above applying even for those authorities who are not captured by the scheme.

**Future Issues (continued)**

- Sustainability performance - The Treasury is developing guidance for 2010/2011 which will require all public sector bodies to report publicly on sustainability performance in annual reports. CIPFA is in discussion with the Treasury about when and in what form this requirement will be formalised for local authorities. The reported information will be subject to audit and scrutiny. Sustainability reporting will be difficult to implement and many organisations will need to act quickly to implement new information gathering processes. Next year's UoR assessment will also consider sustainability issues within the Natural Resources element of the Managing Resources theme.
- Public expenditure forecasts indicate that there will be significant pressure on local authorities' funding in the medium term. Future financial settlements will be tight, increasing the need for local authorities to have comprehensive efficiency programmes supported by sound financial management arrangements. It is likely that bold measures will be required to generate sufficient savings to mitigate the impact on priority services. More than ever before, officers and Members will need to focus on identifying these significant savings measures and ensuring that robust arrangements are in place to monitor their delivery to ensure they are realised. The Council has a good track record in delivering such efficiency and savings targets. It will, however, be necessary to revisit and update the Council's plans to ensure that you can deliver the levels of savings required for the future.

**Acknowledgement**

This has been KPMG's second year as the Council's external auditor following our appointment by the Audit Commission in 2007. We would like to thank the Council's management and staff for the help, support and co-operation they have provided throughout our audit. We recently agreed our audit plan for our 2009/10 audit and look forward to working closely with the Council in the coming year to deliver this programme of work.

The main elements of our use of resources work are:

- *Use of Resources* - from 2008/09, the Audit Commission introduced a new UoR assessment framework which forms part of the Comprehensive Area Assessment (CAA). This replaced the former UoR assessment which was predominantly focused on processes. The scope of the new regime is wider as it also considers whether public bodies have achieved significant and sustainable outcomes. UoR assessment comprises three themes which consider:
  - Managing finances – focusing on sound and strategic financial management;
  - Governing the business – focusing on strategic commissioning and good governance; and
  - Managing resources – focusing on the management of natural resources, assets and people.
- *Value for money conclusion* – we issue a conclusion on whether we are satisfied that you have put in place proper arrangements for securing economy, efficiency and effectiveness in your use of resources. This is based on the UoR assessment.
- *Specific risk based work* – we carry out specific reviews of issues facing you, based on a risk assessment and from risks raised with us from various sources. This year we undertook a review of the Council's arrangements for working with the voluntary sector.

The findings from this work are summarised below.

Element of work	Key findings								
<b>Use of Resources</b>	<p>Our assessment of Gloucester City Council against the three themes resulted in the following scores on a scale of one (inadequate) to four (performing strongly):</p> <table border="1" style="margin-left: auto; margin-right: auto;"> <thead> <tr> <th style="background-color: #003366; color: white;">Area</th> <th style="background-color: #003366; color: white;">Score</th> </tr> </thead> <tbody> <tr> <td style="background-color: #e6f2ff;">Managing money</td> <td style="background-color: #e6f2ff;">2</td> </tr> <tr> <td style="background-color: #e6f2ff;">Governing the business</td> <td style="background-color: #e6f2ff;">2</td> </tr> <tr> <td style="background-color: #e6f2ff;">Managing resources</td> <td style="background-color: #e6f2ff;">1</td> </tr> </tbody> </table> <p>These scores build on last year's UoR assessment when the Council scored level 2 (performing adequately) against the financial reporting, financial standing, financial management, internal control and value for money themes. It should be noted, however, that direct comparisons cannot be made between the previous UoR scores and those awarded this year due to the differences in each assessment framework. For example, for district councils the Managing Resources assessment focused this year only on workforce planning arrangements, an area not formerly considered by the previous UoR framework. The issues leading to the level 1 score had therefore not been covered by previous audit work.</p> <p>In achieving level 2 for the other themes, the Council has been able to prove that overall it has adequate arrangements in place. However, there are elements of both themes where we identified specific weaknesses which were scored at level 1 at a more detailed assessment level. For Managing Money, this related to the issues encountered during the audit of the Council's financial statements. For Governing the Business, the issues related to aspects of the Council's commissioning and procurement processes. In all these cases, the Council is taking steps to strengthen its arrangements.</p> <p>The scores reflect the position during 2008/09 and we acknowledge the work that the Council has been carrying out to improve its arrangements. Officers have outlined to us a number of changes that have been made that they believe may have a positive impact on the UoR scores for 2009/10. This will of course have to be assessed in detail during next year's audit.</p>	Area	Score	Managing money	2	Governing the business	2	Managing resources	1
Area	Score								
Managing money	2								
Governing the business	2								
Managing resources	1								

**Use of resources (continued)**

Element of work	Key findings
<b>Value for money conclusion</b>	<p>Based on our use of resources assessment we conclude that the Council had appropriate arrangements in place to ensure the effective use of its resources, except for specific weaknesses that were identified during our audit which impact on our assessment of the Council's arrangements for:</p> <ul style="list-style-type: none"> <li>● financial reporting;</li> <li>● commissioning and procurement; and</li> <li>● workforce planning.</li> </ul> <p>Our VFM conclusion was therefore qualified on this basis.</p>
<b>Review of arrangements for working with the third sector</b>	<p>As part of this year's audit we undertook a specific review of the Council's arrangements for working with the voluntary sector, also referred to as the 'third sector'. We found that the Council has a strong commitment to supporting voluntary sector organisations and committed a significant amount of funding to this area, with this level of funding having been established and supported by Members over a long period of time. There are clear and effective structures and arrangements for managing the Council's engagement with voluntary sector organisations and for ensuring its funding of these organisations is co-ordinated.</p> <p>There are however opportunities for the Council to strengthen its arrangements further and a number of challenges that will need to be addressed moving forward. The specific conclusions from our audit report are as follows:</p> <ul style="list-style-type: none"> <li>● increasing financial pressures for the Council will mean there is an increasing need to review and challenge expenditure to the third sector;</li> <li>● the Council needs to clarify and articulate more clearly how its relationships with the third sector links to corporate priorities;</li> <li>● linked to this, the Council should develop more clearly the outcomes it is trying to achieve from its funding of the third sector so that it can measure success, and to support this it will also need to help educate the third sector about how best to collect and present information supporting the achievement of these outcomes;</li> <li>● communication within the Council has resulted in the operations of the Community Strategy and Engagement Team being somewhat isolated from the Council's management, which the Council has recognised and taken steps to address;</li> <li>● there are very strong working relationships with the third sector but there is a risk that this focus is not balanced and that staff working with the third sector are less focused on the internal objectives of the Council and are more focused on helping the third sector to reach its objectives; and</li> <li>● internal processes will need to be re-shaped to help deliver objectives.</li> </ul> <p>The key findings, as summarised, above, have been discussed with officers, who are currently considering our draft report.</p>

**Accounts production and adjustments to the accounts**

The original draft accounts, approved in June 2009 and submitted for audit, contained numerous material and significant errors. There were a number of mistakes and errors of presentational and numerical nature. The accounts did not initially balance and they were incomplete. Due to this, several further versions of draft accounts were produced in between this date and the conclusion of our audit in November 2009.

The material errors and most of the significant errors were adjusted by management in the final version of the financial statements. It should be noted that the final accounts were significantly different to the version approved by the Audit Committee in June 2009. This was reported to the Audit Committee on 29 September 2009.

The quality of working papers, once provided, was mixed. A number of them met the standards specified in our accounts audit protocol but the overall standard needs to be improved next year.

The speed of response to audit queries was, on the whole, quite good. The main contacts within the finance department were helpful and did their utmost to respond to queries in a timely fashion, especially when considering the difficult audit issues arising. Where queries required time to resolve, we were informed of expected dates and these were generally adhered to.

The Council followed guidance issued by CIFPA to calculate a £627,000 impairment charge against its £3m investments with the UK subsidiary of an Icelandic bank. The Council had these funds on deposit in October 2008 when the Icelandic banking system collapsed. This impairment charge represented the best estimate of the cost to the Council of this event (i.e. it is the amount that is likely to prove irrecoverable). The final cost will not be known with certainty for some time and at present the Council, like all authorities affected, is working to the repayment plan set out by the bank's administrators which will see the Council recovering its funds over a number of years. In the meantime, in its 2008/09 accounts the Council exercised the option available under regulations to defer the impact of this impairment for up to two years so this cost has yet to 'hit' the General Fund.

**Audit opinion**

Because of the difficulties in auditing the accounts we were not able to issue our audit opinion by the 30 September deadline. We worked closely with Finance staff to ensure the errors in the draft financial statements were addressed and, following this, we issued an unqualified opinion on the revised financial statements on 18 November 2009.

We recognise that the Council's Finance department was under strain this year and this greatly affected the effectiveness of its arrangements for closing down its annual accounts. It is important that the Council takes steps to ensure that a complete and materially accurate set of financial statements can be produced by the statutory deadline next year. The Council has now recruited additional Finance staff which should help address these issues next year.

## Appendix 1: Key recommendations

This appendix summarises the main high priority recommendations that we identified during 2008/09, along with your response to them. Other lower priority recommendations are contained, as appropriate, in our audit reports (which are listed in Appendix 2).

Issue/ Recommendation	Management Response / Timescale for implementation
<b>Financial statements audit</b>	
<b>Material errors in first draft set of accounts</b>	
<p><u>Issue</u></p> <p>The draft accounts approved by the Audit Committee and submitted for audit did not balance, omitted certain financial statements and contained a number of material and significant errors and disclosure omissions. This could have been prevented, or at least reduced, by a thorough independent review by management of the draft accounts (e.g. use of SORP disclosure checklist, checking arithmetical accuracy throughout, identification and removal of typographical errors, formatting issues etc).</p> <p><u>Recommendation</u></p> <p>Ensure a thorough management review of the draft accounts takes place prior to their approval by the Audit Committee and submission for audit.</p>	<p>The restructure of Financial Services is now complete, with all of the key qualified accountant posts recruited. This will ensure appropriate and qualified resources are available. The second Service Manager takes up post in October 2009. A draft timetable has been prepared which includes production of the first draft of accounts by 31 May 2010 to enable key review stages to take place by the Group Manager Financial Services, based on the SORP checklist as well as a pre-audit committee review by both KPMG and the Director of Resources.</p> <p><u>Officer and due date</u></p> <p>Group Manager (Financial Services), 31 May 2010</p>
<b>Independent Review of council tax refunds by a Senior Officer</b>	
<p><u>Issue</u></p> <p>For a sample of refunds it could not be demonstrated that a Senior Officer had reviewed the details of requested refunds prior to their payment.</p> <p><u>Recommendation</u></p> <p>The senior officer who is reviewing refunds reports annotates each refund entry to demonstrate that they have been reviewed.</p>	<p>Agreed. This has now been introduced.</p> <p><u>Officer and due date</u></p> <p>Group Manager (Revenues, Fees and Charges)</p> <p>Complete</p>
<b>Monitoring</b>	
<p><u>Issue</u></p> <p>There have been no formally documented and retained comprehensive review of users and their access rights for all applications deemed as in scope for testing (i.e. Cedar, IBS and Chris21).</p> <p><u>Recommendation</u></p> <p>A review of users is essential to ensure permitted access rights remain appropriate for job roles in order to minimise the risk of fraud. It will also help identify any staff leavers and transfers that may remain on the system, and measure the effectiveness of the leavers process in place. In order to ensure reviews are carried out regularly, and that they monitor both appropriate access and inactivity, we recommend that evidence of such reviews is retained and signed off by management on a regular basis.</p>	<p>The Application administrators will control joiners and leavers of their application. We will contact the various system administrators to put these recommendations and procedures into force.</p> <p><u>Officer and due date</u></p> <p>Wayne Thomas, 30 November 2009</p>
<b>Change management</b>	
<p><u>Issue</u></p> <p>Without formally documented change control procedures in place it is possible that changes may be placed into the live environments that have not been appropriately tested or given approval by appropriate individuals. This could lead to issues with system availability and security.</p> <p><u>Recommendation</u></p> <p>The procedure for change management should be formally documented for future reference.</p>	<p>Agree, the procedure for application change management to be formally documented for future reference</p> <p><u>Officer and due date</u></p> <p>Wayne Thomas / Jane Pagan, 30 November 2009</p>

## Appendix 1: Key recommendations (continued)

Issue/ Recommendation	Management Response / Timescale for implementation
<b>Use of Resources audit</b>	
<p><b>Regular review of the financial and performance reports</b></p> <p>During the UoR review, it was noted that aside from the annual performance report submitted to the Cabinet and Council members in May 2008, there were no other updates (overall performance) made except for regular verbal updates to Cabinet and Scrutiny.</p> <p>We therefore recommended that, in line with best practice, there is regular financial and performance reporting to Cabinet/Members. The reports should be made available to the reviewers prior to the meeting so to have a more detailed and meaningful scrutiny/challenge. The reports as well as the minutes of the meetings should also be made available on the internet in order to promote transparency.</p>	<p>Financial monitoring reports were made to Cabinet as part of the Three Year Money plan process in 2008/09. Comprehensive performance reports covering all services for the quarter ending December 2008 which included financial monitoring, were presented to both Scrutiny Committees in January 2009.</p> <p>Building on these arrangements, the process for 2009/10 has been further improved with scheduled financial updates for both Cabinet and Overview and Scrutiny Committee, the papers for which will be available on the internet.</p> <p><u>Officer and due date</u></p> <p>Group Manager (Financial Services) and Group Manager (Policy and Partnerships)</p> <p>On-going through 2009/10</p>
<p><b>Implementation and monitoring of staff appraisal process</b></p> <p>The Council could not demonstrate that it had effective performance management arrangements in place as evidenced by the absence of an effective monitoring of the annual appraisal. There was no data available to identify the proportion of staff who received an appraisal for 2008/09 as this was not previously monitored and enforced.</p> <p>However, a new staff appraisal process has been implemented from May 2009. As such, we recommend that the Council should strictly implement this process improvement by monitoring the progress of the staff appraisal process and ensuring that issues identified are properly addressed.</p>	<p>Agreed. This process is already happening. Reports on progress are being made to GLT by the Group Manager, Organisational Development to ensure full compliance.</p> <p><u>Officer and due date</u></p> <p>Monitoring: Group Manager (Organisational Development)</p> <p>Implementation: All group and Service Managers</p>

## Appendix 2: Audit reports issued

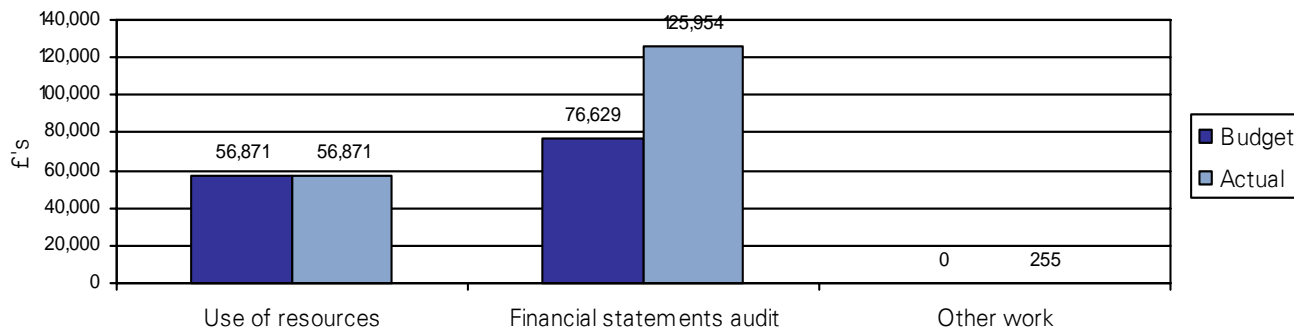
A summary of the reports issued in the year to date is set out below.

Report	Date issued
Audit and Inspection Plan 2008/09	June 2008
Report to those charged with governance 2007/08	September 2008
Managing outsourced service delivery	March 2009
Audit and Inspection Plan 2009/10	March 2009
Report to those charged with governance 2008/09	September 2009
Working with the third sector (draft)	November 2009
Annual Audit Letter	November 2009

## Appendix 3: Audit Fee

To make sure that there is openness between us and your Audit Committee about the extent of our fee relationship with you, we have summarised below the out-turn against the 2008/09 agreed external audit fee:

### External audit fee for 2008/09



The financial statement audit fee increased due to the significant additional work that was required to address the issues identified. This meant that our final fee for the 2008/09 audit was £182,825, against the original proposed fee of £133,500.

The grants fee will be confirmed through our planned summary report on the certification of grants and returns.

The 'Other' fee of £255 is a charge for time spent considering and responding to correspondence received from local electors.