

Government and Public Sector

November 2009

# Leicestershire County Council

## 2008/09 Annual Audit Letter

Members of the Corporate Governance Committee  
Leicestershire County Council  
County Hall  
Glenfield  
Leicester  
LE3 8RA

09 November 2009

Ladies and Gentlemen

We are pleased to present our Annual Audit Letter summarising the results of our 2008/09 audit. We look forward to presenting it to the Audit Committee on 23 November 2009.

Yours faithfully

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

*In April 2008 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and of audited bodies'. It is available from the Chief Executive of each audited body. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas. Our reports and management letters are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to members or officers 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.*

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# Executive Summary

## The purpose of this letter

The purpose of this letter is to provide a high level summary of the results of the 2008/09 audit work we have undertaken at Leicestershire County Council that is accessible for members and other interested stakeholders.

We have already reported the detailed findings from our audit work to those charged with governance in the following reports:

- Audit opinion for 2008/09 financial statements, incorporating the conclusion on Use of Resources
- Report to those charged with Governance (ISA (UK&I) 260)

The matters reported here are those that we consider are most significant for the Authority.

## Scope of work

Our audit work is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The Authority is responsible for preparing and publishing its financial statements, including the Annual Governance Statement. It is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- forming an opinion on the financial statements;
- reviewing the Authority's Annual Governance Statement;
- forming a conclusion on the arrangements that the Authority has in place to secure economy, efficiency and effectiveness in its use of resources; and
- undertaking any other work specified by the Audit Commission.

## Audit Findings

We audited the Authority's accounts in line with approved Auditing Standards and issued an unqualified audit report on 25 September 2009.

We have not identified any material weaknesses in the Council's accounting and internal control systems during the audit.

The Council already faces a number of financial challenges and there is every likelihood that following the general election in 2010 further significant cuts in public sector expenditure will have to be made.

The new use of resources framework forms part of the Comprehensive Area Assessment (CAA). We evaluated the arrangements against the guidance

issued by the Audit Commission and reached a score of 3 (performs well) for each of the three areas under assessment (namely managing finances, governing the business and managing resources). It is important to note that although the one to four scoring definition is the same as that used in previous years, the underlying assessment methodology is fundamentally different. A score under the old use of resources system cannot therefore be compared to a score under the new system. It is a harder test and there is no like for like comparison.

We issued an unqualified conclusion on the Authority's arrangements for its Use of Resources on 25 September 2009.

### **Summary of Recommendations**

We have made a number of minor control recommendations to the Council during the year, however, there are no material control weaknesses that we have identified during the course of our work.

The key areas that the Council should continue to focus on in delivering the current Medium Term Financial Strategy are:

- Sound financial management and keeping to budgets, in spite of service pressures;
- Achieving the significant savings targets identified in the Medium Term Financial Strategy;
- Continuing to improve and modernise services through service reconfiguration, making them more efficient and affordable;
- Continuing to improve relationships with district councils to deliver closer collaborative working and service delivery;
- Ensuring that up to date risk assessments are maintained for the Council's major schemes that may be impacted by the economic downturn;
- Sound management of the Council's capital programme.

We have also noted in this letter a number of areas under Use of Resources which the Council may wish to consider developing further.

# Audit findings

## Accounts

We audited the Authority's accounts in line with approved Auditing Standards and issued an unqualified audit report on 25 September 2009.

The key issues arising from our audit of the 2008/09 accounts were reported to the Audit Committee on 25 September 2009 and are summarised below.

### Unadjusted Differences

We identified one unadjusted difference which related to the pooled budget arrangement with Leicestershire County and Rutland Primary Care Trust (PCT) for learning disabilities, which is hosted by the Council.

The Cabinet agreed a financial arrangement with the PCT which re-phased the revenue contributions to the pooled budget. The PCT paid its contributions for 2008/09 (£4 million) and 2009/10 (£3 million) in advance in 2007/08.

In 2007/08 the Authority decided to recognise this early contribution of £7m as income in the Income and Expenditure Account, rather than as a receipt in advance in the Balance Sheet. The basis for this decision was to be consistent with the accounting treatment applied by the PCT and to avoid any resultant impact on the Whole of Government Accounts process. The impact of the current treatment is to overstate income by £7 million in 2007/08 and understate income by £4 million in 2008/09 and £3 million in 2009/10.

The Authority decided not to adjust for this misstatement on the grounds of materiality and the impact on Whole of Government accounts as noted above.

In relation to the Leicestershire County Council Local Government Pension Scheme, there were no unadjusted misstatements:

### Adjusted Differences

During the course of our work we identified a small number of changes and disclosure matters in the Council's draft accounts. There was only one material adjustment identified which is set out below.

### Overstatement of Private Equity investments (Pension Fund)

As a result of our audit procedures (which include confirmation of valuations with third parties) it was identified that the value of investments reported by the investment managers at 31 March 2009 were 3.3% lower than the estimated values used by the Actuary in their calculations.

Therefore, an adjustment was made to the County Council Accounts to reduce the Pension Fund asset and Pension Fund reserve by £17.2m (ie. 3.3%). This was only a Balance Sheet adjustment, with no impact on the Income and Expenditure Account.

In our experience of pension fund accounts audit such amendments are to be expected, given that asset valuations as at the year end are not always available at the time draft accounts are typically produced.

The detail of all adjustments made on both the Council and Pension Fund draft accounts have been reported to the Corporate Governance Committee previously in our ISA 260 report.

### Systems of internal control

We are required to report to you any material weaknesses in the accounting and internal control systems identified during the audit. We are pleased to report that we have not identified any such material weaknesses during the course of our audit procedures.

### Financial Standing

In the Annual Audit and Inspection letter last year some of the challenges facing the Authority were set out. The key theme which predominates is the pressure upon the Authority's financial health over the medium term and the need for the Council to mitigate the effects of the global downturn on residents and businesses of Leicestershire. This challenge is considered further below.

#### Current Financial Performance

In 2008/09 the Council achieved an outturn position of £8.6m surplus against the budget, after carrying forward to 2009/10 £3.3m of resources to meet high priority issues and commitments.

In order to deliver the 2009/10 budget, the Council needs to achieve its savings target of £10.3 million. Current indications are that the Council is on course to achieve this target.

#### Medium term financial forecasts and associated risk

The September 2009 Cabinet Report set out resource requirements for 2010/11 of £335.6 million as set out in the table below.

	<b>2010/2011 £ million</b>
<b>Net Budget Requirement Before Use of General Fund Reserves (incorporating £8.8 million of efficiency saving proposals)</b>	<b>335.6</b>
<i>Less: Further Savings to be Identified</i>	<i>1.0</i>
	<b>334.6</b>
Formula Grant	100.7
Council Tax (based on a 2.5% increase over 2009/2010 levels)	233.9
<b>Total Resources</b>	<b>334.6</b>

The Council will need to deliver just under £70 million in savings over the coming 4 years, which is a significant challenge. This is split between approximately £42 million efficiency savings and £28 million in service reductions. These figures assume Council Tax increases of 2.5% per annum in 2010/11, 2011/12 and 2012/13, with a 0% increase in 2013/14. A consultation on this proposal is currently being undertaken.

The main areas of risk to the achievement of the above forecasts are:

- Waste from landfill costs, diversion from landfill and recycling costs
- Decreasing income levels in relation to, for example, grants and contributions, other income and treasury management (interest rates)
- Increased costs associated with demand led services such as looked after children and vulnerable adults, for example in home care, placements and learning disabilities.

The Council already faces a number of financial challenges and your plans to address these are based on a number of assumptions. In these circumstances, and given the budget risks the Council has itself already

identified over the coming years, it remains imperative that the Council continues to focus on the following areas:

- Sound financial management and keeping to budgets, in spite of service pressures;
- Achieving the significant savings targets identified in the Medium Term Financial Strategy;
- Continuing to improve and modernise services through service reconfiguration, making them even more efficient, affordable and generating greater efficiency savings;
- Continuing to improve relationships with district councils to deliver closer collaborative working and service delivery;
- Ensuring that up to date risk assessments are maintained for the Council's major schemes that may be impacted by the economic downturn;
- Sound management of the Council's capital programme.

### **Use of Resources**

The new use of resources framework forms part of the Comprehensive Area Assessment (CAA) and comprises the following three areas:

- Managing finances
- Governing the business.
- Managing Resources.

We evaluated the arrangements against the guidance issued by the Audit Commission in underlying Key Lines of Enquiry (KLoE) and reached a score for each based on the following:

- 1 Failure to meet minimum requirements – inadequate performance;
- 2 Meets only minimum requirements – performs adequately
- 3 Exceeds minimum requirements – performs well; or
- 4 Significantly exceeds requirements – performs excellently.

The scores for these KLoEs then determines the overall score for each area, using rules issued by the Commission. The Commission in turn then determines an overall score for the Authority.

It is important to note that although the above one to four scoring definition is the same as that used in previous years, the underlying assessment methodology is fundamentally different. A score under the old use of resources system cannot therefore be compared to a score under the new system. There is no like for like comparison. The Audit and Inspection Letter for 2007/08, issued to the Council in March 2009 summarises this well when it states that the “2009 use of resources assessment framework will be more demanding than previous use of resources assessments. It is broader in scope and embraces wider resource issues such as people and workforce planning, and the use of natural resources. It also places more emphasis on considering outcomes for local people. It is particularly important to recognise that the key lines of enquiry are more strategic and focus much more explicitly than previously on value for money achievements rather than on processes.” Put simply it was easier to score, for example, a 3 under the previous methodology than is the case now.

## Managing Finances

We have scored the KLoEs for managing finances reporting as follows:

Key Line of Enquiry		Score
1.1	The Authority plans its finances effectively to deliver its strategic priorities and to secure sound financial health	3
1.2	The Authority has a sound understanding of its costs and performance and achieves efficiencies in its activities	3
1.3	The Authority's financial reporting is timely, reliable and meets the needs of internal users, stakeholders and local people	3

### Summary Findings

The financial planning process is forward looking and proactive, involving a wide range of stakeholders and community groups. Finance and service planning is strongly integrated as part of setting corporate objectives and includes partnership working. The Medium Term Financial Strategy is comprehensive and provides for effective longer term planning by covering a 4 year period. A range of alternative scenarios and modelling has been undertaken.

The Council has a track record of managing spending within the available resources effectively whilst meeting strategic targets and maintaining or improving performance. For example, £32.4m efficiency gains (£25m cashable) were achieved up to the end of 2007/08 to count towards the three-year target of £22m that was set as part of the 2004 Spending Review. The individual and collective responsibilities for financial management are clearly addressed by officers and members.

The Council has a robust understanding of its costs through regular benchmarking to understand relative performance and effectively influence decision-making and commissioning, securing ongoing value for money. There is a well established Change Management Programme and the Authority continues to be proactive.

There is evidence of innovation in some areas, including partnership working. For example, the County is the lead Authority of the Midlands Highways Alliance, which won the national Government Opportunities (GO) award for "Best Collaborative Procurement" and was highly commended in the 2008 "4 P's" awards. The Authority was also prominent in ensuring that National Indicator 179 is included in its Local Area Agreement and Multi Area Agreement from 2008/09 to ensure greater accountability, one of the few areas nationally to do so.

There is a consistent pattern of low to moderate cost and high performance against CIPFA nearest neighbours. Specific recognised high performance includes being awarded the top 3 star-rating by CSCI for the quality of its Adult and Social Care for 7 years in a row and being named Council of the Year by the Local Government Chronicle.

Budget monitoring and forecasting is accruals based, reliable, relevant and produced on a timely basis with significant variations actively managed. Key demand budgets such as waste, adult social care, children's services and winter maintenance are regularly reviewed and latest trend information is reflected in forecasting information. All significant variations during 2008/09 have been managed within the funds available.

### Potential areas for development

In order to achieve a level 4 the Council will need to demonstrate innovation and best practice across all of the individual areas of a specific KLoE.

The Council has undertaken a participatory budgeting pilot in Loughborough; to further strengthen the involvement of partners in the financial planning process the Council could engage with community forums or the new Public Services Board, for example.

The Council needs to continue to achieve value for money, maintaining the Authority's current status as a low cost high performing Authority and ensuring that the longer term challenges presented by the economic situation are planned for proactively. A widespread budget consultation is now taking place which reflects the Councils proactive approach to the current economic climate. There is potential for unit costing to be implemented across more aspects of the Council's functions.

The Council should seek the views of stakeholders about what information is required in its communication and tailor it accordingly. Diversity issues could also be more widely addressed. The Council should look at innovative ways of engaging with the local community to obtain useful feedback in relation to its communication.

### Governing the business

We have scored the KLoEs for governing the business as:

Key Line of Enquiry		Score
2.1	The Authority commissions and procures quality services and supplies, tailored to local needs, to deliver sustainable outcomes and value for money.	3
2.2	The Authority produces relevant and reliable data and information to support decision making and manage performance	3
2.3	The Authority promotes and demonstrates the principles and values of good governance	3
2.4	The Authority manages its risks and maintains a sound system of internal control	3

### Summary Findings

Through the Joint Strategic Needs Assessment, medium term priorities for improving health and well-being needs were identified and the council has then identified how these will be taken forward through a multi agency approach using the Leicestershire Performance Framework, which is based on the Sustainable Community Strategy (SCS). The SCS is underpinned by detailed needs analyses.

The Council consults with stakeholders on key decisions. Members of the public are consulted on major decisions impacting local areas and the views of suppliers have been built in to the Sustainable Commissioning and Procurement Strategy.

The Council has a clear vision for service transformation. The Organisational Efficiency Programme is delivering a fundamental review of back office services and in March 2009 a new Employee Service Centre was formed. The programme exceeded its savings target in 2008/09 and going forward achievement of the efficiency savings within the Programme will be key to successfully delivering the medium term financial strategy.

The Council produces relevant and reliable data and information to support decision making and manage performance. There is clearly defined responsibility and accountability for Data Quality (DQ) at both officer and member level which is replicated through the Council. Data Quality is embedded into processes and this is supported by a comprehensive, embedded DQ Strategy which includes clear objectives and plans for improvement across the organisation. The Council has driven the governance and leadership arrangements in the LSP and has ensured they cover other partnership arrangements. Our Data Quality Spot Checks in both 2008 and 2009 concluded that there were no significant issues arising.

There are robust systems in place for the collection, recording, analysis and reporting of the data used to monitor performance. A variety of formats are utilised to aid understanding. There is also regular reporting on the accuracy of data supporting key performance information, which has included recent reports on attendance management and satisfaction surveys to give members and officers additional assurance.

The Authority continues to have good arrangements in place for ensuring that information systems are robust and that the continuity of information is secured in line with government requirements. Standards are specified for data supplied by third parties and there are arrangements in place for the sharing of data with key partners.

The Authority monitors performance against its priorities and targets effectively, with information being used to improve and manage services. Performance data is considered by Departmental Management Teams, Corporate Management Team, Cabinet and Lead Members. All performance reports include explanations for significant variances from targeted performance. Explanations in in-year reports include details of remedial action to be taken.

The Council has adopted, promotes and demonstrates the principles of good

governance. In particular, this is reflected through the close relationships between lead members and officers who work effectively together along clearly defined functions, for example through effective cabinet briefings and the members' information service. The capacity of members and officers to be effective is supported by the Members Learning and Development Strategy, which has been effective in supporting members in their roles. These arrangements have contributed towards the success of the Council in delivering its strategic objectives.

There is a strong ethical framework and culture which is fostered through the Codes of Conduct for members and staff, the work of the Standards Committee, Constitution Committee, Corporate Governance Committee and Internal Audit. This is supplemented by embedded whistle-blowing procedures, arrangements to monitor gifts and hospitality, the arrangements for governing interests of senior staff and members and a proactive approach to handling complaints.

The principles and values of good governance are applied to its partnership working. The LSP is underpinned by a Partnership Agreement with a focus on compliance with a code of governance. A partnership self assessment toolkit is used to support the governance of partnership working at all levels of the Authority, whilst there is a separate voluntary sector compact and infrastructure agreement that underpins the relationship with the voluntary sector.

The Council has strong risk management arrangements in place which are embedded throughout the organisation. This is supported by relevant training, members awareness and clear lines of accountability. In addition to day to day activities, this focus extends to major projects and partnership working. There is a structured approach to assessing partnership risk and all key partnerships have been considered.

The council has substantially revised its corporate risk register in 2008/09, following a risk management workshop with managers and members, and it now reflects the additional risks facing the council and is more accessible and user friendly in its format.

The council has appropriate arrangements in place to maintain a sound system of internal control which is demonstrated both operationally through low level controls, and strategically through the Annual Governance

Statement, Scrutiny Commission and Corporate Governance Committee, which plays a key role by challenging management appropriately on matters flagged by auditors and takes action when issues arise.

The Authority has carried out an assessment of the risk management, governance and business continuity arrangements of partnerships and further work is being carried out in 2009/10 to strengthen business continuity arrangements within partnerships.

#### Potential areas for development

Service users and the wider community should be involved at each stage of the commissioning cycle: assessing needs, establishing priorities, designing services, and reviewing performance. The Council should over time continue to demonstrate that it is on track to deliver key intended outcomes such as better quality, more responsive services, sustainability and value for money.

Going forward the council will need to maintain an up to date strategic needs assessment across services, which should be driving forward long term commissioning decisions and partnership objectives, aligning resources and priorities around the areas of greatest need.

The Council will need to maximise the effectiveness of partnership working, looking to establish a shared understanding of the totality of resources that partnerships can bring to bear, with a view to increasing the efficient and effective use of those resources.

There should be full implementation of Oracle as an ERP system to support the development of the organisation.

Work has already commenced looking at the adequacy of business continuity arrangements at partner organisations. This work should be fully completed and form part of the ongoing assessment of the adequacy of partnership arrangements, along with an assessment of risk management and governance.

To achieve a level 4 in this area, the Council will need to demonstrate innovation and best practice across the whole range of the KLOEs.

## Managing resources

We have scored the KLoEs for managing resources as:

Key Line of Enquiry		Score
3.1	The Authority makes effective use of natural resources.	3
3.2	The Authority manages its assets effectively to help deliver its strategic priorities and service needs.	3

### Summary Findings

The Council's Environmental Policy, Strategy and Action Plan date back to 2004 and was fully revised in March 2009. Governance arrangements in relation to the review and oversight of the Council's use of natural resources have been revised and focus on the achievement of 10 priorities.

The Council has demonstrated close working with other bodies to enable the achievement of its own targets.

Examples of successful cross cutting initiatives include the Council's school replacement programme, eco schools, environmental procurement, the work well project and County Hall travel plan. The Council's eco schools have received national recognition.

The Council's performance for recycling and composting is comparatively high. The Council has a good track record of reducing carbon emissions since 2005 and is currently aiming to achieve its target of a 30% reduction over the next few years.

A number of energy savings initiatives have been undertaken during the year, initiatives that have arisen through the Council's Energy Management Unit (established to improve energy efficiency).

The Council has a County Hall waste action plan and progress has been made during the year in the reduction of waste from County Hall. The Council's Work Well project is the Council's mobile and flexible working programme and some success has been achieved to date in encouraging

employees to work more flexibly with consequential environmental benefits.

The Council has appropriately targeted reductions in waste within Highways, as the highest contributor to waste within the Council. The Council has successfully achieved significant waste reductions in this area through a variety of initiatives including footway recycling and more effective treatment of water from roadside gullies.

There is evidence of the Council working effectively with partners to improve air quality by focusing on areas of poorest air quality. The Council is also recognised at a regional and national level for its role in relation to bio diversity.

Significant progress has been made in improving environmental procurement including the development and use of an environmental audit tool to identify contracts with significant risks; the development of a new Environmental Purchasing Policy; a programme of procurement training to reinforce the importance of environmental issues; and the development of performance indicators on the Council's Sustainable Commissioning and Procurement Strategy. Increases in the purchase items denoted as environmental options through the Eastern Shire Purchasing Organisation have also been achieved.

A variety of methods are employed to communicate environmental information to staff and the community.

The Council has a strategic and corporate approach to asset management. An effective process is in place to ensure assets are managed in line with strategic priorities. Governance arrangements in place allow for member involvement in, and scrutiny of decisions around asset management. The Council is a member of COPROP (Association of Corporate Property Officers) Benchmarking Club and participates in CIPFA's National Best Value Benchmarking Scheme. Benchmarking information supports Asset Challenge work and has helped to identify those assets which are being under utilised.

The Council is working well with its partners to better utilise its buildings.

### Potential areas for development

Several initiatives are in the process of development, or in-part underway (for example, the Council's accommodation strategy). It is important that the Council continues to monitor closely the success of these initiatives in order that planned levels of savings to be made are realised.

Whilst the Council has demonstrated an understanding of its resource usage in all areas, further improvement could be made to the way in which the Council's carbon footprint is reviewed and reduced, holistically.

### **Conclusion on Use of Resources**

We were also required to issue a conclusion on the adequacy of the Authority's arrangements for ensuring economy, efficiency and effectiveness in its use of resources.

We issued an unqualified conclusion on the Authority's arrangements for its Use of Resources on 25 September 2009.

### **Annual Governance Statement**

Local Authorities are required to produce an Annual Governance Statement (AGS). The AGS was included in the financial statements.

We reviewed the AGS to consider whether it complied with guidance issued by relevant professional bodies and whether it is misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

### **Treasury Management**

During the year, the collapse of the Icelandic banking system, together with the disclosure that a number of public sector bodies in the UK held significant investments there, raised concerns nationally as to the adequacy of treasury management practices within the public sector. In response to such concerns, and as part of our use of resources assessment we completed a Treasury Management 'workbook' issued to us by the Audit Commission. This work, which was in the form of a questionnaire completed with the assistance of council staff, identified no matters for concern. The Council

does not hold funds in Icelandic banks but has in the light of this issue, reviewed its policies and strategies in this area.

### **Expenses**

In light of the recent furore nationally on politicians expenses, we have raised the matter of expenses with the Council. Our discussions gave no indications that the Council's arrangements in this area were not operating effectively.

### **Matters affecting future accounting periods**

#### Transition to International Financial Reporting Standards (IFRS)

CIPFA has issued the Exposure Draft and Invitation to Comment on the Code of Practice on Local Authority Accounting in the United Kingdom 2010. This will apply to accounting periods starting on or after 1 April 2010. The new Code is the first to be prepared under IFRS. Because of the need to have comparative information for the first set of full IFRS accounts the effective date of the transition is 1 April 2009. The Authority will need to have values for assets and transactions as they should be recognised under IFRS from this date.

The Authority has made good progress in the transition to IFRS by engaging with us early in discussion and having an impact analysis completed which was used to develop a project plan.

It is important that the Authority continues with this progress and ensures that it has a good grasp of the changes to accounting requirements under the new Code, and robust plans to enable collection and processing of the information needed to comply with the new Code.

In our experience the key features of a successful IFRS conversion project have proven to be:

- Completed impact analysis and comprehensive conversion plans;
- The commitment of key stakeholders in the organisation;
- Operational steering and technical groups;

- Cabinet/audit committee oversight;
- Regular progress reporting against the plan;
- The necessary project management resources; and
- Timely training for all members and officers with IFRS involvement.

