

Wolverhampton City Council

OPEN INFORMATION ITEM

Audit Committee

Date **6 July 2012**

Originating Service Group(s)

DELIVERY

Contact Officer(s)/

PAT MAIN

Telephone Number(s)

4410

Title

EXTERNAL AUDIT UPDATE REPORT

RECOMMENDATION

That the report be received.

EXTERNAL AUDIT UPDATE REPORT

1. PURPOSE

- 1.1 The Council's external auditors, PricewaterhouseCoopers (PwC) presented their 2011/12 Audit Plan to the Audit Committee on 30 January 2012. The purpose of the report attached at Appendix 1 is to:
- update Councillors on their progress in delivering their Audit Plan;
 - update Councillors on their view of the progress of the closedown process;
 - inform Councillors of the results of their review of the work of Internal Audit;
 - inform Councillors about some recent publications from PwC's Public Sector Research Centre.

2. BACKGROUND

- 2.1 Representatives from PwC will be in attendance at the meeting to present their report and to respond to Councillors' questions.

3. FINANCIAL IMPLICATIONS

- 3.1 There are no financial implications arising directly from PwC's report. The costs are included within the agreed annual fee for provision of external audit services.

[JH/29062012/Q]

4. LEGAL IMPLICATIONS

- 4.1 There are no direct legal implications arising from this report.

[MW/29062012/M]

5. EQUAL OPPORTUNITIES IMPLICATIONS

- 5.1 There are no equal opportunities implications arising from this report.

6. ENVIRONMENTAL IMPLICATIONS

- 6.1 There are no environmental implications arising from this report

7. SCHEDULE OF BACKGROUND PAPERS

External auditor working papers and reports, PricewaterhouseCoopers

External Audit Plan 2011/2012 (Report to Audit Committee 30 January 2012)

Wolverhampton City Council

External Audit Update 2011/12

Government and Public
Sector

June 2012

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In March 2010 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 and on the Audit Commission’s [website](#). 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 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.

Section 1 - Introduction and Executive Summary

Introduction and Executive Summary

The key messages from our work to date are as follows:

Audit Area	RAG	Comments
Risk based work (per Audit Plan)	Green	We are making good progress against our plan. Our interim audit fieldwork took place as planned between the 11 th and 20 th April. We were provided with all the information we requested during our visit. We evaluated the effectiveness of key controls as planned. We identified no significant or material control weaknesses. Work on some areas is ongoing. We will complete our work during our final accounts audit visit which will begin on 16 July 2012.
Review of the Council's closedown plans	Green	The finance team has worked very hard to improve the management of the closedown process, and we have no significant concerns. The final accounts audit will test these new arrangements in practice.
Review of the work of Internal Audit	Green	As planned we are able to place reliance on the work of Internal Audit. We have also concluded that we can rely on the controls within the Council's key financial systems as planned.

Key

Red - significant improvements required

Amber - some improvements required

Green - no or some minor improvements required.

In the next sections of this report we set out in further detail our progress in delivering our plans.

Section 2 – Audit Plan risk update

Update on risks – Financial Statements

We set out below our progress in responding to the risks we identified in our Audit Plan (presented to the Audit Committee on 30 January 2012):

Risk	Progress and issues noted	Remaining action
<p>Fraud and management override of controls</p> <p>ISA (UK&I) 240 requires that we plan our audit work to consider the risk of fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk that management may override controls in order to manipulate the financial statements. In your organisation, as the pressure to deliver savings increases, so does the risk of management override.</p>	<p>As planned we have:</p> <ul style="list-style-type: none"> • evaluated the work of internal audit; • considered the design and effectiveness of key controls within key financial systems (such as cash, creditor payments and payroll); • reviewed the Council’s draft accounting policies; • reviewed the Council’s processes for raising and approving journals; • undertaken detailed testing of those IT systems which underpin the Council’s accounts; and • tested financial system access controls. <p>Based on our work to date we have concluded that:</p> <ul style="list-style-type: none"> • we have identified no significant or material weaknesses; and • there are no issues that should impact on our planned audit approach. 	<p>As planned we will perform final accounts audit procedures in relation to:</p> <ul style="list-style-type: none"> • testing the appropriateness of journal entries and other adjustments; • reviewing accounting estimates for biases; • evaluating the business rationale underlying significant transactions; • testing exceptional and unusual items highlighted by the Council’s bank account (and other) reconciliations; and • performing unpredictable procedures.

<p>Revenue recognition (of income and expenditure)</p> <p>Under ISA (UK&I) 240 there is a presumption that there are risks of fraud in revenue recognition.</p> <p>There is a risk that the Council could adopt accounting policies or treat income and expenditure transactions in such a way as to lead to a material misstatement in the reported revenue position.</p> <p>Given that the Council is experiencing increased pressured on many of its budgets as economic conditions have worsened, there is the potential for budget holders to feel under more pressure to push costs into future periods, or to miscode income and expenditure.</p>	<p>As planned we have:</p> <ul style="list-style-type: none"> evaluated the work of internal audit relating to the income , debtors, expenditure, creditors and payroll business cycles; considered the design and effectiveness of key controls; and reviewed the Council’s draft accounting policies relating to income and expenditure. <p>We have also started our testing of specific income and expenditure items included in your 11/12 accounts as part of a risk based approach.</p> <p>Based on our work to date we have concluded that:</p> <ul style="list-style-type: none"> systems are generally operating effectively; we have identified no significant or material weaknesses; and there are no issues that should impact on our planned audit approach. 	<p>As part of our final accounts audit we will perform detailed testing of revenue and expenditure transactions, focussing on the areas we consider to be of greatest risk.</p> <p>Our testing will include procedures in relation to:</p> <ul style="list-style-type: none"> the appropriateness of journal entries and other adjustments; income and expenditure cut off; and reviewing the accounting estimates for revenue, expenditure, deferred revenues and provisions.
<p>Valuation of properties</p> <p>Property, plant and equipment (PPE) is the largest balance in your balance sheet. You value your properties at fair value using a range of assumptions and the advice of internal and external experts.</p> <p>We have to consider how expertise is used, how your processes ensure the balance is fairly stated, and your assumptions.</p> <p>Specific areas of risk include:</p> <ul style="list-style-type: none"> asset valuation data may be inaccurate or incomplete; the Council’s valuation assumptions may not be appropriate; assets’ actual market value may fluctuate materially but may not have been re-valued in the accounts; and capital expenditure may not be accurately allocated between enhancing and non-enhancing. 	<p>The Finance Team have shared with us its proposed approach to valuing properties within the 11/12 accounts.</p> <p>We have provided feedback on this proposed approach.</p> <p>We have reviewed the Council’s draft accounting policies with respect to the measurement and valuation of property, plant and equipment assets and identified no concerns.</p>	<p>As part of our final accounts audit we will:</p> <ul style="list-style-type: none"> agree the source data used by your Valuer to supporting records; finalise our assessment of the work of your Valuer through use of our own internal specialists where required; and agree the outputs to your Fixed Asset Register. <p>Where assets are not re-valued in year we will discuss with you the steps you have taken to ensure that your balance sheet is materially accurate at the year end.</p>

<p>Equal Pay and Single Status</p> <p>The Council is yet to reach an affordable Single Status pay agreement. There are also a number of unsettled equal pay claims against the Council.</p> <p>Work is ongoing aimed at resolving these matters. There are a number of risks associated with this including:</p> <ul style="list-style-type: none"> the arrangement may not provide value for money outcomes for the Council; financial decisions may not be appropriately reviewed and approved in line with the Council's policies; the control environment surrounding any payments may not be robust; and payments and / or liabilities recorded in the financial statements may not be accurate and / or complete. 	<p>We have met with key officer to discuss the Council's arrangements for managing these matters. While our work is still ongoing we have noted a number of good practices including:</p> <ul style="list-style-type: none"> Project governance has been clearly articulated and includes a Single Status Steering Group and an Equal Pay Project board; Critical project management disciplines such as project plans, progress reporting and risk logs have been put in place; and An ongoing assurance role has been played by Internal Audit across a number of key areas (including data quality) regarding both single status and equal pay. <p>The Deputy S151 Officer has kept us updated on developments regarding the Council's efforts to settle its outstanding equal pay liabilities.</p>	<p>We will complete our review of the Council's arrangements. This work will consider the steps the Council has taken to:</p> <ul style="list-style-type: none"> gain assurance on key matters; get appropriate legal advice; and achieve value for money; <p>We will test whether the 2011/12 financial statements appropriately record transactions and liabilities in relation to the matters of Equal Pay and Single Status. We will review your disclosures and assess whether they meet relevant financial reporting standards.</p>
<p>Closedown Plans</p> <p>We reported in our 'Report to those charged with governance (ISA (UK&I) 260)' that the Council must learn the lessons from the 2010/11 accounts closedown and audit process (when shortcomings in the quality and timeliness of the Council's accounts and working papers delayed the completion of the audit).</p> <p>Since completing our audit the Council has shared with us its provisional plans for 2011/12 which if implemented will better prepare the Council for next year's audit.</p> <p>There remains a risk however that the accounts closedown and audit timetable is not planned, executed and / or monitored effectively.</p>	<p>See Section 3.</p>	<p>We will begin our final accounts audit, as planned, on 16 July 2012.</p> <p>We will update the Section 151 Officer (and Audit Committee) of any issues with regards to the quality of the Council's financial statements and supporting working papers in practice.</p>

<p>Investment in Birmingham Airport Holdings Ltd</p> <p>Wolverhampton City Council owns 4.7% of the ordinary shares of Birmingham Airport Holdings Ltd. The value of this shareholding is held at £16.8 million on your balance sheet.</p> <p>There is a side agreement which has previously reduced the market value of this asset, however this expires during the 2011/12 financial year. We therefore previously recommended that you reconsider the basis of this valuation.</p>	<p>Management has updated us on its plans to ensure the accuracy of the balance sheet value of this shareholding.</p> <p>We understand that as part of the Council's closedown plans, an updated valuation assessment will be undertaken by the Council's partners in conjunction with external valuation expertise.</p> <p>We have also confirmed that an (updated) side agreement remains in place.</p>	<p>We will review the value of the investment in the financial statements.</p> <p>We will review supporting evidence, including any updated valuation.</p>
<p>Changes to Accounting for Heritage Assets</p> <p>For the first time the 2011/12 Code requires you to present information about the heritage assets you hold. There is a risk that information relation to the value of such assets is incomplete and / or inaccurate.</p> <p>Where it is practicable to obtain a valuation, the Code now requires material amounts of heritage assets to be carried in the Balance Sheet at that valuation.</p>	<p>We have reviewed the Council's procedures for identifying, valuing and disclosing its heritage assets which appear, in principle, to be reasonable and robust.</p>	<p>We will review the accounting entries and related disclosure notes during the year end final audit.</p> <p>We will agree the valuation of a sample of heritage assets to third party insurance documentation.</p>

Update on risks - Other Audit Code responsibilities

Risk	Progress and issues noted	Remaining action
<p>The Medium Term Financial Strategy and savings requirements</p> <p>The Council has recently updated its Medium Term Financial Strategy (MTFS). This shows that (before new savings proposals are taken into account) the projected cumulative budget deficit amounts to £72.7 million over the next five years.</p> <p>This represents a significant financial challenge. The Council has plans in place to deliver £50.2 million of efficiency savings over this period and has a further savings requirement therefore of £20.5 million.</p> <p>There are a number of risks associated with the MTFS including the following:</p> <ul style="list-style-type: none"> • Identified savings options may not be achieved; • Further efficiency savings may not be identified; • Spending may exceed budgets and/or income may fall short of budgets; • Inflationary pressures may increase; • Demand for council services may exceed estimates; and • Future finance settlements may vary from current assumptions. <p>Effectively managing the above risks is critical to Council's future financial resilience and therefore a key part of our assessment on your arrangements for securing economy, efficiency and effectiveness in the use of Council resources.</p>	<p>Our work in this area is nearing completion. We have</p> <ul style="list-style-type: none"> • reviewed your updated MTFS and its key assumptions; • benchmarked your inflation, growth and efficiency projections as well as your reserve balances; • continued to meet regularly with the Section 151 Officer and the Chief Executive to discuss the Council's financial position and plans; • reviewed in-year finance reports on a rolling basis and considered their impact on budgets and plans; and • undertaken a high level assessment of the strength of your existing plans to deliver savings and efficiencies. <p>The next stage of our work is to set out our provisional findings for discussions with the Finance Team.</p>	<p>We will report our detailed MTFS findings to the Section 151 Officer.</p> <p>We will consider the findings of our detailed testing on the Council's estimates, provisions and journals undertaken as part of our final accounts audit work. If any of these findings have a significant impact upon the Council's financial plans we will feedback our findings to the Section 151 Officer and Audit Committee.</p> <p>We will report a summary of all our findings to the Section 151 Officer and Audit Committee within our ISA 260 report.</p>

<p>Procurement</p> <p>The Council has identified that its procurement processes require strengthening and work is ongoing to ‘transform’ the contract life cycle.</p> <p>The Council will need to closely monitor the implementation of its procurement transformation plans to ensure that they are delivered. Ensuring the Council has sufficient capacity to drive these plans will be particularly important.</p> <p>There is a risk that these plans are not implemented or that they are delayed, and that as a result planned value for money improvements and savings are not achieved.</p> <p>There is also a risk that planned developments in the control environment surrounding procurement and contracts are not delivered.</p>	<p>Our work in this area is ongoing.</p>	<p>We will complete our work and report back to the Section 151 Officer and the Audit Committee.</p>
<p>Axon</p> <p>In March 2011, following a detailed scoping exercise, the Council commissioned an independent review into the matters surrounding the proposed partnership with Axon Solutions Ltd.</p> <p>The Council has recently received a report of recommendations on this matter which it has shared with us.</p>	<p>As planned, in February 2012, we met privately with the review team and in doing so confirmed that the original terms of reference had been covered.</p> <p>We requested a Council response to the report of recommendations and the Chief Executive updated us, back in March, of the Council’s plans for gaining assurance that lessons had in practice been learnt. At that time these plans involved a report to the Joint Standards and Audit Committee in June 2012.</p> <p>At that point we concluded that no further immediate action was needed and that we should await the outcome of the June report.</p> <p>Since this plan the Chief Executive has updated us on developments regarding the Council IT replacement project. These developments are relevant here. The Chief Executive has therefore agreed to meet with us on the 9 July to discuss these matters, and the steps the Council has taken to assure itself on this project.</p>	<p>We will consider the outcome of the 9 July meeting and consider what, if any, further action is needed.</p>

Section 3 – Closedown plans

Following difficulties experienced during the 2010/11 accounts closedown process, our 2011/12 Audit Plan identified a specific risk in relation to your closedown plans. We therefore agreed with you that we would:

- review your closedown plans;
- meet regularly with the Finance Team throughout the year to monitor the Council’s progress in executing its plans;
- meet regularly with the Section 151 Officer to discuss the Council’s progress and feedback; and
- consider the Council’s arrangements for monitoring its closedown plans including any progress reports.

Our work has not identified any areas of significant concern with regards to the achievability of the overall closedown plan or indeed the timely production of a sound draft set of financial statements supported by robust working papers.

At our last meeting with the Finance Team (on 12 June 2012) we were made aware of a small number of areas the Council still had to complete.

We anticipate that these matters will be completed however and therefore plan to begin our final accounts audit as planned on 16 July 2012.

Ultimately, it is our final accounts audit which will test how successful the Council’s final accounts closedown process has been. We are however at this stage able to confirm that the Council has made significant developments to the way it manages its accounts closedown process. In particular we have noted the following developments:

Planning	The closedown team have invested time in making sure that its closedown plans included the appropriate actions and key milestones.
Team	Time was taken to revisit the core team and to clarify roles and responsibilities.
Monitoring	The Council has put in place a number of measures to ensure performance against their closedown plans is challenged and reviewed. The finance team have met weekly with the Financial Controller (Deputy s151 Officer) and monthly with the s151 Officer to discuss progress against the closedown plans
Departmental closedown	The core closedown team have invested time in engaging with directorate finance teams as part of its closedown plans. The core finance team has provided support and clear guidance, including the design of proformas listing the actions expected of the service directorates and the relevant deadlines.
Quality assurance	The closedown team has revisited its approach to quality assuring accounting entries and the evidence supporting these entries. This has been started much earlier in 2011/12 and has included peer review over working papers.

Section 4 – Review of the work of Internal Audit

We have reviewed the work of Internal Audit across the following key financial systems:

- Cash / general ledger
- Debtors
- Creditors
- Treasury management (borrowings and investments)
- Budgetary control
- Property, plant and equipment
- Payroll
- Council tax income
- Housing benefits and rent

In completing our work we found that:

- the scope of the work of Internal Audit met our requirements;
- the quality of the work undertaken by Internal Audit was of a good standard;
- the conclusions of Internal Audit were consistent with the work they had completed;
- our re-performance testing (of a sample of work undertaken by Internal Audit) reached the same conclusion in every instance;

Our review of the aforementioned reviews of Internal Audit also found that:

- no material control weaknesses were identified; and
- all systems achieved an assurance rating of at least 'satisfactory';

On the basis of the above we were able to conclude that:

- we are able to place reliance on the work of Internal Audit, as planned;
- we are able to place reliance on the controls within the Council's key financial systems, as planned; and
- there are no findings which would require changes to our planned audit approach.

Our final accounts audit approach will therefore continue as planned.

We have provided feedback to the Internal Audit Team on their good performance and suggested a number of areas where efficiencies could be gained in the delivery of the managed audit in future years.

Section 5 – Recent publications

As part of our regular reporting to you, we plan to keep you up to date with the emerging thought leadership we publish. The PricewaterhouseCoopers Public Sector Research Centre (PRSC) produces a range of research and is a leading centre for insights, opinion and research on best practice in government and the public sector. We have highlighted some recent publications that may be of interest to the Council below:

Valuing social impacts: Should Government pay for results?

Deepening spending cuts and sluggish economic growth is driving Government to do things differently. Engaging and incentivising voluntary and social enterprises to tackle social issues and improve outcomes for vulnerable groups is a key part of the Big Society programme.

Government has embarked on a number of pilot Payment by Results (PbR) programmes. The expectation is that PbR will deliver new and enhanced services to address social needs that, in turn, will lead to better outcomes and consequently reduce public exchequer costs.

In order to understand whether these outcomes are achievable it is important to understand how social impacts can be measured, monetised and traced to actual reductions in public sector activities and/or expenditure.

This Talking Points publication, the first in a series of three, provides an approach to measuring social impacts and looks at practical steps to achieve wider adoption of Payment by Results schemes across government and the public sector.

Fighting fraud in government

Since our 2009 Global Economic Crime Survey, governments around the world have taken action to address their faltering economies and this has directly impacted on those who work for, and with, the public sector.

This public sector analysis of our 2011 Global Economic Crime Survey examines the current fraud landscape, taking a close look at who is committing economic crime, what new types of fraud are emerging and how they can be addressed.

Given the pressures placed on both individuals and organisations, we have, unsurprisingly, seen a rise in the number of frauds committed against the public purse.

Government and public sector organisations worldwide will need to be increasingly vigilant and proactive when fighting fraud, alongside the wider challenges they face.

In the event that, pursuant to a request which Wolverhampton City Council has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PwC promptly and consult with PwC prior to disclosing such report. Wolverhampton City Council agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Wolverhampton City Council shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC, Wolverhampton City Council discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

This report has been prepared for and only for *Wolverhampton City Council* in accordance with the Statement of Responsibilities of Auditors and of Audited Bodies (Local government bodies) published by the Audit Commission in March 2010 and for no other purpose. We do not accept or assume any liability or duty of care for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

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