Agenda Item No: **8a**

Audit Committee

23 September 2013

Report Title	**2012/2013 Report to those charged with Governance**
Classification	Public
Cabinet Member with Lead Responsibility	Councillor Andrew Johnson Resources
Accountable Strategic Director	Keith Ireland, Delivery
Originating service	Delivery
Accountable officer(s)	Mark Taylor — Assistant Director - Finance Tel — 6609 Email — Mark.Taylor@wolverhampton.gov.uk

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Recommendations for noting:

The Committee is asked to note:

1. The 2012/13 report to those charged with governance from the council's external auditors PricewaterhouseCoopers.

1.0 Purpose

1.1 To present to members of the committee the 2012/13 Report to those Charged with Governance

2.0 Background

2.1 ISA 260 is an auditing standard that requires external auditors to communicate relevant matters relating to the audit of the financial statements to those charged with governance of the entity, sufficiently promptly to enable them to take appropriate action.

3.0 Content of the report

3.1 The attached external audit report covers:

(a) Issues arising from the external audit of the financial statements, which were previously submitted to the Audit Committee on 6 July;

(b) The results of work undertaken in forming an opinion on the council's arrangements for securing economy, efficiency and effectiveness in its use of resources.

3.2 In addition, the external auditors will also provide an update on audit work.

4.0 Financial implications

4.1 This report has no direct financial implications. Where the ISA 260 report refers to changes to the council's Statement of Accounts, these are discussed in agenda item 6a.

4.2 The ISA 260 report, and the audit of the accounts, are of fundamental importance to the council's governance and financial control frameworks, and play a key role in ensuring accountability and transparency in the council's finances.

[CF/17092013/J]

5.0 Legal implications

5.1 The Accounts and Audit Regulations require the 2012/13 Statement of Accounts to be produced in accordance with proper practice. This is the Code of Practice on Local Authority Accounting which is published by CIPFA. These regulations also require that the accounts are certified by the Section 151 Officer by 30 June 2013 and published by 30 September 2013.

[MS/17092013/Z]

6.0 Equalities implications

6.1 There are no equalities implications arising from this report.

7.0 Environmental implications

7.1 There are no environmental implications arising from this report.

8.0 Schedule of background papers

Draft Statement of Accounts 2012/13, report to Audit Committee, 8 July 2013

2012/13 Statement of Accounts Progress Update, report to Audit (Final Accounts Monitoring and Review) Sub Committee, 22 April 2013

Appendix 1

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Wolverhampton City Council

Report to those charged with governance (ISA 260)

Government and
Public Sector

September 2013

Report to the Audit Committee of the Council on the audit for the year ended 31 March 2013

Contents

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

In April 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. 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.

An audit of the Statement of Accounts is not designed to identify all matters that may be relevant to those charged with governance. Accordingly, the audit does not ordinarily identify all such matters.

We have issued a number of reports during the audit year, detailing the findings from our work and making recommendations for improvement, where appropriate. A list of these reports is included at Appendix 2.This report contains a summary of the results of our audit and matters which we ask the Audit Committee to consider.

Please note that this report will be sent to the Audit Commission in accordance with the requirements of its standing guidance.

Executive summary

Background

This letter contains the significant matters we wish to report to you arising from all aspects of our work.

We presented our plan to you in March 2013; we have reviewed the plan and concluded that it remains appropriate. We will provide an update on our progress at the Audit Committee meeting on 23 September 2013 and look forward to discussing our report with you then.

Audit Summary

- Your draft accounts (including pension fund) were submitted to us before the 30 June deadline and were of a high quality. Initial supporting working papers were provided on time in the majority of cases and were generally of a good quality.
- Key contacts in the finance team and elsewhere were available during the audit and responded readily to our questions and requests for information. We would like to thank the Finance Team and others for their support and assistance during the audit.
- The most complex issues this year have been:
  - Ensuring that revised valuations of Council land and buildings are based on accurate data;
  - Confirming the adequacy of the Provision for Equal Pay;
  - Determining that schools transferring to Academy status have been accounted for correctly; and
  - Considering the financial standing of the Council over the medium term.

  Further detail is given later in this report on all of these topics. The accounts have now been corrected for all adjustments required in these areas.
- A number of minor disclosure issues were identified, discussed and appropriately amended.
- The Audit Committee need to confirm the proposed treatment of the unadjusted misstatement in Appendix 1.

Audit Status

We have completed the majority of our audit work and expect to be able to issue an unqualified audit opinion on the Statement of Accounts and value for money conclusion by 30 September 2013 following approval by the Section 151 Officer. We do have a small number of outstanding matters, where our work has commenced but is not yet finalised.

Internal controls

We have not identified any material deficiencies in internal control. There is one more minor issue we bring to your attention regarding segregation of duties on posting journals.

Risk of fraud

We have not identified any instances of fraud that would impact on our audit opinion.

We look forward to discussing our report with you on 23 September 2013. Attending the meeting from PwC will be Richard Bacon and Richard Vialard.

We utilise a range of technology to support what we do, including data auditing, bespoke delivery centres and out cutting edge Auditing software 'Aura'.

We have summarised within the following page how we have brought together our people, approach and technology to deliver your audit in 2012/13.

Audit approach

Smart People

We continue to deploy our best people on your audit, supported by a substantial investment in training and in our industry programme.

Your audit team has been drawn from our government and public sector team based in the Midlands, but is further supported by our specialists both in the sector, and across other services.

Our intention is that, wherever possible, staff work on the audit each year, developing effective relationships and an in depth understanding of your business.

Our team (including our Pension Fund and IT specialists) was very stable for 2012/13 with the Engagement Leader, Senior Manager, Manager and Team Leader all having significant experience on your audit.

Smart Approach

Data auditing

We use technology-enabled audit techniques to drive quality, efficiency and insight.

In 2013 the work included:

- Using data analysis in auditing housing income. We automatically match revenue transactions to accounts receivable and cash in a targeted way.
- We have used benchmarking as part of our work on Value for Money. This has included using Audit Commission tools to compare you to other City Councils, and our own analysis when assessing your Medium Term Financial Strategy.

We will also continue to explore ways to extend our use of smart technology and data into other areas where we see an opportunity to add value, as well as for quality and efficiency.

Centre of Excellence

We have a Centre of Excellence in the UK for Local Government which is a dedicated team of specialists which advises, assists and shares best practice with our audit teams in more complex areas of the audit.

Our team has been working side by side with the Centre of Excellence to ensure we are executing the best possible audit approach.

Delivery centres

We use dedicated delivery centres to deliver parts of our audit work that are routine and can be done by teams dedicated to specific tasks; for example these include confirmation procedures, preliminary independence checks and consistency and casting checks of the Statement of Accounts.

Benefits for the audit

The key benefit of our approach for your audit has been the use of our delivery centres which have reviewed in detail your compliance with the 2012/13 Code of Practice.

In 2013 the work undertaken by the delivery centres included consistency and casting checks on the draft financial statements. This enabled our core teams to focus on areas of higher risk and judgement.

Smart Technology

We have designed processes that automate and simplify audit activity wherever possible. Central to this is PwC's Aura software, which has set the standard for audit technology. It is a powerful tool, enabling us to direct and oversee audit activities. Aura's risk-based approach and workflow technology results in a higher quality, more effective audit and the tailored testing libraries allow us to build standard work programmes for key local government audit cycles.

We reported our planned audit approach to you in our 2012/13 Audit Plan. This was supplemented by a report to the Audit Committee in June 2013.

These documents set out the risks to be addressed as part of the audit and the work we planned to do in response to those risks.

We have summarised these risks and our actual responses in the table opposite and on the following pages.

The first two risks, Management Override of Controls and the Recognition of Income and Expenditure, are presumed to be significant risks under International Standards on Auditing.

Risk assessment

We set out below our actual responses to the risks we identified in our Audit Plan.

Risk	Category	Audit approach
Fraud and Management Override of Controls 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.	● - **Significant risk**	As planned we have: • 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; • reviewed the Council's draft accounting policies relating to income and expenditure. • tested in detail a risk based sample of the income and expenditure balances; • tested a sample of journal entries to ensure they are appropriate and are supported; • tested the cut off of income and expenditure at the 31 March 2013; and • reviewed key accounting estimates for revenue, expenditure and provisions. **Based on our audit work have concluded that:** • **systems are generally operating effectively;** • **we have identified no significant or material weaknesses; and** • **there are no issues that impacted on our planned audit approach.**

Risk	Category	Audit approach
Recognition of income and expenditure Under ISA (UK&I) 240 there is a (rebuttable) presumption that there are risks of fraud in revenue recognition. There is a risk that the Council could adopt accounting policies or treat income and expenditure transactions in such way as to lead to material misstatement in the reported revenue and expenditure position.	● - Significant risk	As planned we have: • 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; • tested financial system access controls.; • understood the processes involved with raising journals and selecting a risk based sample for testing; • tested the appropriateness of journal entries and other adjustments; • reviewed accounting estimates for bias (including provisions, asset valuations and debtor/creditor balances); • tested in detail the Council's year end bank account (and other) reconciliations focussing on any unusual items; and • applied unpredictable procedures when performing detailed testing. **Based on the work set out above we have:** • **identified no significant or material weaknesses; and** • **concluded that there are no issues requiring the attention of the Audit Committee in this area.**

Risk	Category	Audit approach
Valuation of properties 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. We have to consider how expertise is used, how your processes ensure the balance is fairly stated, and your assumptions. Specific areas of risk include: • 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.	● - Significant risk	We held discussions with the finance team to understand the approach to revaluing the Council's estate in 2012/13. We engaged our internal valuation specialists to ensure appropriate input into the process. We reviewed the Council's draft accounting policies with respect to the measurement and valuation of property, plant and equipment assets and identified no concerns. We considered controls in place to ensure the completeness and accuracy of asset values within the accounts. This has included following up control issues raised during the 2011/12 audit. We reviewed and validated the key judgements, assumptions and supporting data used. We assessed the reasonableness of estimation techniques applied. We reviewed the expertise of your internal Valuer. We have considered the steps you have taken to ensure that your balance sheet is materially accurate at the year end and that there are no indicators of general impairment. **We have identified a small number of misstatements that have required adjustment and have made associated control recommendations.** *More details on the results of our audit procedures are included in the section 'Significant audit and accounting matters' and 'Internal Controls' below.*

Risk	Category	Audit approach
Provision for Equal Pay As in previous years, the Council is expected to include a provision in the accounts to reflect its liability for Equal Pay and back pay claims. Over the last four years the Council has received notification of employment tribunal claims against the Council alleging breach of Equal Pay legislation. The Council has engaged Solicitors to provide legal advice and conduct proceedings on behalf of the Council in relation to these claims. On the basis of the advice provided and the information available the Council concluded that at 31 March 2012 the most probable liability was £30 million. This figure reflected known claims as well as other potential claims.	● - Elevated risk	We have updated our understanding of the Council's arrangements for managing these matters through discussion with key officers. We reviewed the Council's draft accounting policies with respect to the recognition of related expenditure and the measurement and valuation of related liabilities, and have no concerns to report. We tested whether payments, journal entries and other adjustments in the financial statements relating to Equal Pay were materially accurate and whether they met relevant financial reporting standards. We understood and evaluated the assumptions made regarding each sub-group of claimant, underlying claimant and unknown potential claimants. We received confirmation from the Council's legal advisors that the Council's interpretation of legal advice provided was reasonable and that there are no changes to the legal judgements or level of cases received that we have not been advised of. We reviewed and challenged assumptions made by the Council regarding relevant case law and the associated implications for the Council's provision. We have understood that, consistent with previous years, the Council can only make informed estimates about the level of second generation claims that may be received at a future date. **Although we recognise that there remains some unavoidable risk associated with second generation claims, based on our work we have concluded that the £26.5 million provision is not unreasonable and is materially accurate based on available information.**

Risk	Category	Audit approach
		More details on the results of our audit procedures are included in the section 'Significant audit and accounting matters' below.
Trading Surpluses and internal charging In 2010/11 we reported that your trading areas, particularly Catering and Cleaning services, were consistently reporting large surpluses within the financial statements. During 2011/12 another large surplus position (£2.6m) was recorded. We have discussed with management the risk that inaccurate charging could represent a transfer of resources between services. The Council is currently undertaking its own review of how it records trading income and expenditure, including how it apportions overhead costs.	● - Normal risk	We reviewed the Council's accounting policies with respect to the treatment of trading accounts, and have no concerns to report. We discussed progress made in reviewing internal charging with management and reviewed the outputs of the work undertaken. Essentially, service areas have been rebated so that the surplus on trading activities has been eliminated. **We satisfied ourselves that the method being used to ensure that income and expenditure recorded within the Comprehensive Income and Expenditure Statement by service area was appropriate and mitigated against the risk of cross-subsidies between services from internal trading. Disclosure note 2A – Trading Operations had not been correctly disclosed in the draft accounts but adjustments have subsequently been made.** *More details on the results of our audit procedures are included in the section 'Supplementary Matters' below.*

Risk	Category	Audit approach
Treasury Management Accounting Practices As a response to the new Housing Revenue Account (HRA) Self-Financing regulations and budgetary pressures on the general fund, the Council has taken the opportunity to develop new methods of calculating interest charges and to revisit the current methods of financing capital expenditure to ensure they remain most appropriate for the Council. The Council has developed new methods for splitting interest costs between the HRA and the General Fund. The Council has also revisited how it calculates and records an appropriate Minimum Revenue Provision (MRP). The adoption of different methods can have a significant impact on the in-year financial outturn and the MTFS for both the general fund and the HRA. As with any accounting change or judgement there is a risk that the new treatment may be in contravention of the relevant accounting standards.	● - Normal risk	We understood the Council's revised approach to determining the annual MRP charge as well as calculating and apportioning interest charges between HRA and General Fund. We reviewed the new methods that are proposed against the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom and other sector guidance. We considered whether the additional voluntary set-aside was consistent with the need to 'determine for the current financial year an amount of minimum revenue provision that it considers to be prudent.' We considered the appropriateness of updating the formula for inferred net cash balances of each fund and understood why this was deemed most appropriate and prudent for the Council. **We concluded that the revised methodologies did not contradict the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom and met the requirements for a prudent approach**.

Risk	Category	Audit approach
Additional support on your Accounts Closedown Plan Within our 2012/13 audit plan we noted considerable improvements made to the Council's accounts closedown process during 2011/12. We also recognised the remaining risk that with competing demands for resources in the Corporate Finance team the accounts closedown and audit timetable may not be properly planned, executed and / or monitored effectively.	N/A	We held regular meetings with the finance team during the year to monitor progress and review closedown plans. We met regularly with the Section 151 Officer to discuss progress and feedback our observations. We identified no significant concerns in the run up to the accounts close, during the accounts compilation process or in the run up to the audit. The finance team made strong progress against closedown plans and delivered a good set of draft accounts and working papers.

We plan and perform our audit to provide reasonable assurance that the financial statements are free from material misstatement and give a true and fair view. We use professional judgement to assess what is material. This includes consideration of the amount and nature of transactions.

We identify and assess the risks of material misstatement at two levels: the overall financial statement level; and in relation to financial statement assertions for classes of transactions, account balances and disclosures.

Our audit methodology requires us to identify three quantitative materiality thresholds. These help us to plan the nature, timing and extent of our work and to evaluate the significance of any unadjusted differences from our audit procedures.

Materiality

The following table details the materiality levels which we have worked to as part of the audit. These are consistent with the levels previously reported to you.

Type of materiality	Threshold
Overall materiality	Our overall materiality for the Council was revised on receipt of the 2012/13 draft financial statements to £17.9 million. This is calculated as a percentage of expenditure (in line with auditing standards) and represents the level at which we would consider qualifying our audit opinion.
Performance materiality	This is the level to which we plan our audit work and identify significant accounts, which for 2012/13 was £9 million.
De minimis threshold	ISA (UK&I) 450 (revised) requires that we record all misstatements identified except those which are "clearly trivial". Matters which are clearly trivial those which we expect not to have a material effect on the financial statements even if accumulated. When there is any uncertainty about whether one or more items are clearly trivial, the matter is considered not to be clearly trivial. It is not unusual to find relatively small misstatements which should not be of significant concern to you. We have discussed these smaller misstatements with management, and apply a threshold to the value of individual misstatements that we report to the Audit Committee. We will not report misstatements below the agreed threshold level unless we believe that the nature of the misstatement should be of concern. For clarity, where we find systematic issues which are not material but could impact the Council significantly in other ways or in the future, we will report them to you, regardless of the impact on the accounts. We have applied a reporting threshold of £0.1 million which was approved in March 2013. We apply our professional judgement to determine this threshold. The factors which we consider include: • the number and amount of prior years' misstatements, whether corrected or uncorrected; and • the results of our risk assessment.

This section of the report summarises the significant audit and accounting matters we have identified in our work sufficiently promptly for you to take appropriate action.

You prepared your accounts to a high standard and the working papers were ready for audit on a timely basis.

We anticipate issuing an unqualified audit opinion.

Significant audit and accounting matters

Auditing Standards require us to tell you about relevant matters relating to the audit of the Statement of Accounts sufficiently promptly to enable you to take appropriate action.

Accounts

We have completed the majority of our audit of the Council's accounts in line with auditing standards. At the time of writing, we have work to complete in a small number of areas. This includes:

- Completing our review of audit adjustments and corresponding ledger entries from draft to final accounts;
- Receiving working papers to support our audit of the Council's capitalisation of expenditure relating to the Highfields PFI;
- Receipt of the signed Letter of Representation;
- Completion of our final subsequent events review and quality control procedures;
- Review of the final set of accounts, including a reconciliation of any amendments posted during the audit and disclosure issues recorded;
- Completion of our final review of the accounts; and
- Receiving responses and evidence to address our final queries in the draft Whole of Government Accounts return;

Subject to the satisfactory resolution of these matters, the finalisation of the Statement of Accounts and their approval of them we expect to issue an unqualified audit opinion.

As part of our work on the Statement of Accounts we have also examined the Whole of Government Accounts schedules submitted to the Department for Communities and Local Government and anticipate issuing an opinion stating in our view they are consistent with the Statement of Accounts.

Accounting issues

Valuation of Property, plant and equipment (PPE)

The Council has to present a materially accurate valuation of its 'property, plant and equipment' (PPE) at each balance sheet date. Asset values are reviewed at least every five years.

Identifying, valuing and accurately recording changes in value involves property, valuation and finance staff, and is a largely manual process. Our experience is that errors can occur.

We identified three valuation errors; all of these misstatements will be adjusted in the final version of the accounts.

1) Valuations differentiate open space from hard standing land. We found that the data used for the 2012/13 valuation was out of date and was from a previous valuation. The valuations have now been recomputed. This has resulted in a net increase in the valuation of PPE of £5.4m at 31 March 2013 (£8.9m increase in prior year) with corresponding increases in unusable reserves carried forward for the years ending 31 March.
2) We tested the gross internal floor area (GIFA) and found that the valuer used the wrong area for one school,

because recent building work had not been included. We then reviewed all schools valued with recent building work and found no further errors; we concluded that this must have been an isolated case. This has resulted in a net increase in the valuation of PPE of £1.2m at 31 March 2013 with a corresponding increase in unusable reserves carried forward for 2012/13.

3) One asset due for sale after 31 March was correctly valued at expected sale value of £5.3m. In the new financial year it became clear that only £4.2m would be received. The balance sheet value has now been reduced accordingly. This has resulted in a net decrease in the valuation of PPE of £1.1m with a corresponding decrease in unusable reserves carried forward for 2012/13.

None of these adjustments has any impact on the General Fund.

Equal Pay provision

As in previous years, the Council has included a provision in the accounts to reflect the most probable liability relating to equal pay and back pay claims.

Over the last five years the Council has received notification of a number of employment tribunal claims alleging breach of Equal Pay legislation. The Council has engaged Solicitors to provide legal advice and conduct proceedings.

In 2012/3, £3.5m of Equal Pay claims were settled. A much larger value of other known or potential claims remains unresolved. The Council has considered the legal advice and other information and included a provision of £26.5m.

We have reviewed the documentation and calculations supporting this provision and concluded that although there remains some unavoidable risk associated with potential second generation claims, the £26.5 million provision is not unreasonable and is materially accurate based on available information.

We have received formal confirmation from the Council's legal advisors that the proposed accounting treatment is consistent with the advice they have provided. We are also seeking representation from the Section 151 Officer on this matter and, subject to receiving this, we anticipate being able to conclude that the provision of £26.5 million is reasonable and meets relevant financial reporting standards.

Investment in Birmingham Airport

49% of Birmingham Airport Holdings Ltd (BAHL) is owned by seven local councils - Wolverhampton, Coventry, Dudley, Sandwell, Solihull, Walsall and Birmingham. Birmingham City Council is the largest ordinary shareholder with 18.68%. Wolverhampton City Council owns 4.7% of the ordinary shares.

The valuation of your shareholding was £18.6 million in your 2011/12 accounts, based on a valuation performed last year. A new valuation was commissioned, showing your share should be valued at £18.9 million. You have not updated your accounts to reflect the £0.3 million change in valuation.

In satisfying ourselves that the new valuation is materially accurate we have consulted with our airport valuation experts and:

- Considered the outcome of the updated valuation review undertaken by Solihull MBC in conjunction with BDO, on behalf of the Council;
- Reviewed the valuer's assumptions and concluded that the valuation was prudent, based on a number of factors, including regulation, capacity for expansion, economic and sector conditions and earnings potential; and
- Confirmed that a new side agreement (which restricts the sale of shares by all seven stake-holding councils) is in place until 2022.

Your Pension Fund assets and liabilities are one of the most significant items in your Statement of Accounts. The net pension liability was £551.8 million as at 31 March 2013, an increase of 24% from the previous year.

The letter of representation asks you to confirm that there is no other information that should be taken into account, and that you are satisfied with the valuation. Because the difference in valuation is, technically, an error identified during the audit that has not been adjusted by management, we raise this issue in Appendix 1 and formally request that you consider whether you would wish the accounts to be amended.

Should you consider selling your stake in Birmingham Airport, you should commission a thorough up to date valuation.

Accounting for Academy Schools

The most important factors in transfers are:

1) the *timing* of when to de-recognise assets from the Council's balance sheet when they are transferred to academies; and
2) how to put an appropriate *value* on assets that have historically been valued as operational schools when there are no plans to use the assets as schools in the near future.

Our work identified three instances where the treatment was not consistent with the relevant accounting rules.

Two schools were transferred in previous years so a prior year adjustment has been made.

The third exception relates solely to the timing of when new academy school assets had been derecognised. Accepted accounting practice is that ownership of school assets transfers on conversion to academy status and not on completion of building schemes. As a result, the Council has now removed the assets from the opening balance sheet and amended the prior year accounts for the associated capital expenditure in the previous year.

The overall impact of correcting theses errors was to reduce the brought forward PPE value, and brought forward reserves, by £46.9m and to reduce the 31 March 2013 PPE value by £31.3m with a corresponding reduction in unusable reserves carried forward.

None of these adjustments has any impact on the General Fund.

Pensions liability

The most significant estimate in the Statement of Accounts is in the valuation of net pension liabilities for employees in the West Midlands Pension Fund.

The accounts currently reflect the March 2010 triennial Pension Scheme funding review. Between reviews, the movement in assets is estimated using a "roll forward" approach, adjusting for known trends. Your net pension liability at 31 March 2013 was £551.8m (2012 - £443.4m).

The value of your pension assets has risen by 11% over the year to £0.75 billion and your pension liabilities have increased by 16% to £1.3 billion.

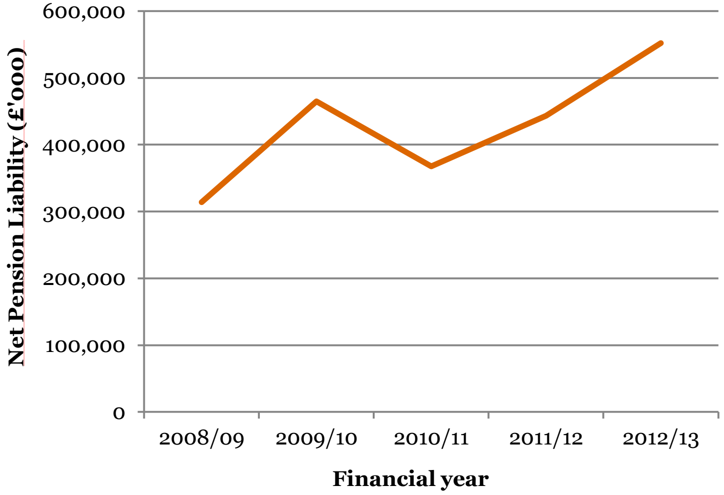
The 2013 triennial valuation is yet to be concluded and will be reflected in the 2013/14 Statement of Accounts. The deficit for the Local Government Pension Scheme as a whole is expected to have increased from £38bn to £80bn since 2010.

Although assets increased in value in this period by 20%, the value of the liabilities has increased by more than 40% as these are linked to gilt prices which are at an all-time high.

The chart below shows the significant movement in your net pension liability over the last few years.

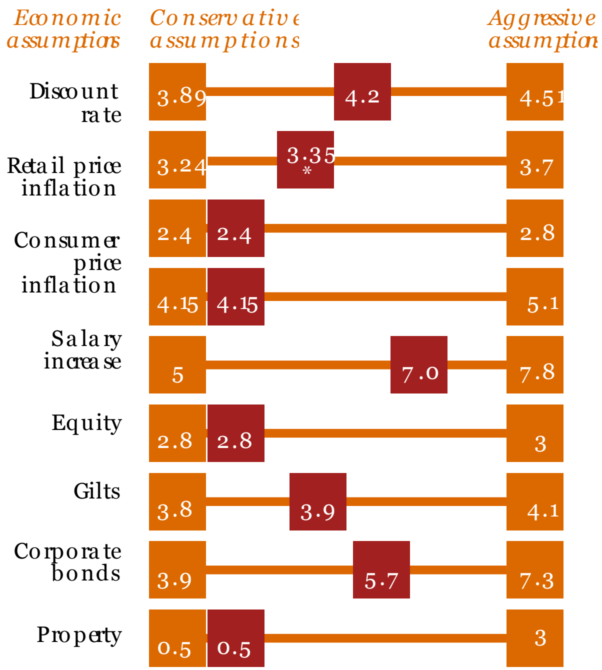
We used the work of our own experts to assess the assumptions made by your actuary. We found the assumptions you have used to be reasonable.

Council Pension Liability between 2007/08 and 2012/13



We reviewed the reasonableness of the liability assumptions, and we are comfortable that the assumptions are within an acceptable range when compared with both our general expectations as at 31 March 2013 and with the assumptions being used by various actuaries associated with other Local Government Pension Funds:

Analysis of the assumptions being used by other actuaries:



* - indirect calculation

The LGPS actuary is provided with details of scheme membership to calculate the figures for the accounts. We validated the data supplied to the actuary on which to base their calculations.

There are some changes to the accounting standard for Employee Benefits (IAS 19) for 2013/14.

Your actuary has estimated that if those changes had been applied in 2012/13, the deficit on provision of services would have increased by £7.9 million.

We are required to tell you about all misstatements we have identified that management have chosen not to amend the accounts for. A summary of these is included in Appendix 1.

Changes to IAS 19: Employee Benefits

From 2013/14 there will be changes to the accounting for defined benefit schemes and termination benefits. For defined benefit schemes the net finance cost will be used. The net scheme liabilities/assets will be unwound using the discount rate for the pension liability and the costs of administering the scheme will be recognised directly in expenses.

The definition of termination benefits has changed and does not now include liabilities where there is a future service element. They do not include any 'voluntary' element.

The 2012/13 accounts need to include disclosure of standards issued but not adopted and estimates of their likely financial effect. As a result, estimates of the impact of IAS 19 (Revised) have been obtained from the actuary. The impact on the Council in 2012/13 would have been to increase the Deficit on the Provision of Services by £7.9 million. It is anticipated that the change in requirement will have no impact on the net pension liability.

Misstatements and significant audit adjustments

We have to tell you about all uncorrected misstatements we found during the audit, other than those which are trivial. Please refer to Appendix 1 for details.

We also bring to your attention misstatements that have been corrected by management but which we consider you should be aware of in fulfilling your governance responsibilities. We have included all such misstatements in the section 'Accounting Issues' above.

The overall impact of these adjustments to the draft accounts presented to the Audit Committee is summarised below:

Accounts heading (Council figures for 2012/13 or 31 March 2013)	June 2013 financial statements (£'000)	Total net adjustment (£'000)	Latest financial statements (£'000)
Net cost of services	319.2	2.1	321.3
Total Comprehensive (Income) / Expenditure	237	-12.1	224.9
Net assets	396.6	-25.8	370.8
General Fund	15.9	0	15.9
Usable reserves	-128.8	0	-128.8
Unusable reserves	-267.8	25.8	-242

Significant accounting principles and policies

Significant accounting principles and policies are disclosed in the notes to the Statement of Accounts. We will ask the Section 151 Officer to represent to us that the selection of, or changes in, significant accounting policies and practices that have, or could have, a material effect on the Statement of Accounts have been considered.

As part of preparing the accounting, management make a number of judgements and accounting estimates.

During our audit we review and challenge management on these judgements. We consider whether they are reasonable in light of the information available.

We found that management has made materially appropriate judgements in preparing the Statement of Accounts.

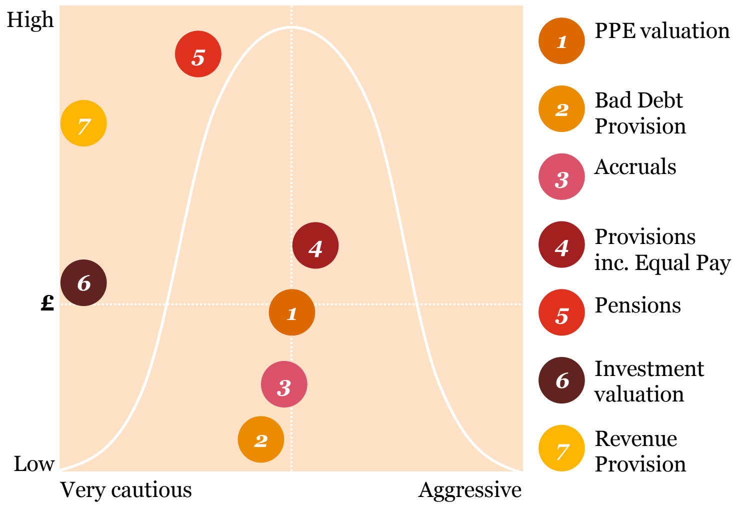
Judgments and accounting estimates

The following significant judgments or accounting estimates were used in the preparation of the Statement of Accounts:

- **Property, Plant and Equipment - Depreciation and Valuation -** You charge depreciation based on an estimate of the Useful Economic Lives of your Property, Plant and Equipment (PPE). This involves a degree of estimation. You also value your PPE in accordance with your accounting policies to ensure that the carrying value is true and fair. This involves some judgement and reliance on your internal valuers. You have estimated the value of your housing stock using beacon principles and guidance issued to you by DCLG.
- **Bad Debt Provision** – Your Bad Debt Provision for sundry debtors is calculated on the basis of age and an assessment of the potential recoverability of invoices. There is an inherent level of judgement involved in calculating these provisions.
- **Accruals -** You raise accruals for expenditure where an invoice has not been raised or received at the year end, but you know there is a liability to be met which relates to the current year. This involves a degree of estimation.
- **Provisions**: Provisions are liabilities of an uncertain timing or amount and therefore there is an inherent level of judgement to be applied. Your equal pay provision is your most significant provision and has been considered above.
- **Pensions:** See above. You rely on the work of an actuary in calculating these balances.
- **Investment valuation -** You have estimated the value of the Council's investment in Birmingham Airport based on information provided by partners and valuation experts. We have also considered this above.
- **Minimum Revenue Provision –** You have determined a prudent method of calculating MRP that allows you to redeem your debt liability over a period which is expected to be equal to, or shorter than the period over which the capital expenditure is estimated to provide benefits. There is a degree of estimation involved and your provision is relatively prudent.

We will ask you to represent to us that you are satisfied with the assumptions made in arriving at these judgements and estimates in the accounts.

We outline below a summary of our view of the key accounting judgments applied by management:



We have previously raised concerns about the level of surpluses recognised in the financial statements relating to trading accounts.

We reviewed the work undertaken by management to ensure that overheads have been adequately treated and disclosed.

We ask management to send us a letter of representation before we sign our audit opinion. A draft of that letter is included in Appendix 3.

Supplementary matters

Trading accounts

For the last two years we have reported that your trading areas, particularly catering and cleaning services, were consistently reporting large surpluses. Although not material to our audit, they are of concern because surpluses essentially transfer resources between services. We asked for this to be reviewed in a previous year.

The draft 2012/13 again disclosed surpluses on trading accounts. We satisfied ourselves that the method used to ensure that income and expenditure recorded by service area was appropriate and mitigated the risk of cross-subsidies between services from internal trading. This method has been in place since 2011/12.

Although the correct amounts were disclosed for each service area in the Comprehensive Income and Expenditure Statement the same approach had not been applied in the draft accounts to Note 2A – Trading Operations. The accounts have now been amended. There is no impact on the underlying accounting records or financial position as this is a disclosure note only.

Management representations

The final draft of the representation letter that we ask management to sign is attached in Appendix 3.

This includes specific representations to confirm that:

- The Equal Pay provision represents the Council's best estimate of the most likely future costs to the Council and that no other additional or contradictory advice has been received and not shared with us.
- The inclusion of the Council's investment in Birmingham Airport Holdings Ltd at £18.6 million is appropriate.
- The Council has considered indicators of impairment and is satisfied that there are no indicators that the Council's asset base has been materially impaired.
- The Council is satisfied that using Major Repairs Allowance as an estimate for depreciation of council dwellings in the Housing Revenue Account is reasonable.
- The general ledger system is complete and that there are no material differences between the assets recorded on the Property Services Database and those recorded on the general ledger system (FMIS), that is used to populate the financial statements.
- The Council's new policy for calculating Minimum Revenue Provision and for splitting interest cost between the HRA and General Fund is appropriate, prudent and compliant with relevant Capital Finance and Accounting Regulations.
- All schools that have transferred to Academy status have been removed from the appropriate balance sheet. All current school assets for which the future use is unknown have been valued at the most appropriate market value. No decisions have been taken about the future use of school assets that have not been reflected in their valuation.

Going Concern

We are required to report to you if we identify any events or conditions that may cast significant doubt that your financial position should enable you to '*continue to operate for at least the foreseeable future*'. The definition of 'foreseeable future' for this purpose is 12 months from the date of the auditor's report on the relevant set of financial statements.

We have not identified any material uncertainties relating to events and conditions that may cast significant doubt on your ability to continue for the foreseeable future. The use of the going concern assumption is appropriate in the preparation and presentation of the financial statements. This view is informed by the Council having:

- a strong net asset position of £396.6 million (pre-audit);
- demonstrated a continued ability to generate strong operating cash flows, with a net inflow of £52.2 million (pre-audit)
- a positive cash balance at year end of £3.5 million (pre-audit) and sufficient funds to meet forecast demand over the year;
- a higher than average level of reserves (general and earmarked) when compared with similar authorities;
- a generally good track record in recording surpluses and achieving financial targets, having identified savings totalling almost £100 million over the last five financial years despite facing difficulties in 2012/13;
- a balance of £6m in the Efficiency Reserve that is not yet committed;
- a strong 30-year HRA Business Plan that is not expected to draw on general fund reserves;
- banked £6.6 million of the 2013/14 savings target of £17.3 million with a further £7.8 million having been estimated with a high level of confidence; and
- a programme in place to take steps over the coming months to address the medium term funding shortfall.

To continue to be able to demonstrate that you have sufficient resources available to meet your commitments in the short term we think it is essential that you:

- Focus on translating the £7.8 million of 2013/14 savings that are estimated with a high level of confidence into realised, measurable savings and continue to identify opportunities to deliver the remaining £2.9 million from the initial savings target.
- Continue to deliver additional one-off savings during 2013/14 to address the currently projected over spend in 2013/14 and reduce the call on the General Fund balance. This cannot be overlooked as efforts are turned toward the 2014/15 budget and the MTFS.
- Ensure that the cost pressures in Children, Young People & Families are very actively monitored and reported accurately.

Our work on financial standing has also identified a number of areas of concern that put the Council's longer term financial standing at risk if not managed effectively. Please refer the section *'Economy, efficiency and effectiveness'* for more details.

We are required to demonstrate our independence by professional standards. Maintaining our independence is important to us in delivering you a robust external audit.

We have considered a range of factors to demonstrate our independence as auditors, including the provision of non-audit work.

We have concluded that we are independent and comply with the relevant UK regulatory and professional requirements.

Audit independence

We are required to tell you at least annually about all relationships between PricewaterhouseCoopers LLP in the UK and other PricewaterhouseCoopers' firms and associated entities ("PwC") and the Authority that, in our professional judgement, may reasonably be thought to bear on our independence and objectivity.

For the purposes of this letter we have made enquiries of all PricewaterhouseCoopers' teams whose work we intend to use when forming our opinion on the truth and fairness of the Statement of Accounts.

Relationships and Investments

We have not identified any potential issues in respect of personal relationships with the Group or investments in the Group held by individuals.

Employment of PricewaterhouseCoopers staff by the Group

We are not aware of any former PwC partners or staff being employed, or holding discussions in respect of employment, by the Group as a director or in a senior management position covering financial, accounting or control related areas.

Business relationships

We have not identified any business relationships between PwC and the Group.

Services provided to the Group

The audit of the consolidated financial statements is undertaken in accordance with the UK Firm's internal policies. The audit is also subject to other internal PwC quality control procedures such as peer reviews by other offices.

In addition to the audit of the consolidated financial statements, PwC has also undertaken other work for the Group. We confirm our independence and overall assessment of threats and safeguards in the 'fees' section below.

Fees

The analysis of our audit and non-audit fees for the year ended 31 March 2012 is included on page 18. In relation to the non-audit services provided, none included contingent fee arrangements.

Services to Directors and Senior Management

PwC does not provide any services e.g. personal tax services, directly to directors, senior management.

Rotation

It is the Audit Commission's policy that auditors at an audited body at which a full Code audit is required to be carried out should act for an initial period of five years.

The Commission's view is that generally the range of regulatory safeguards it applies within its audit regime is sufficient to reduce any threats to independence that may otherwise arise at the end of this period to an acceptable level.

Therefore, to safeguard audit quality, and in accordance with APB Ethical Standard 3, it will subsequently approve auditors for an additional period of up to no more than two years, provided that there are no considerations that compromise, or could be perceived to compromise, the auditor's independence or objectivity.

We have not exceeded the maximum five year initial cap on this engagement.

Gifts and hospitality

We have not identified any significant gifts or hospitality provided to, or received from, a member of the Council or Group's board, senior management or staff.

You are required to produce an Annual Governance Statement (AGS). We reviewed your AGS and found no areas of concern to report.

Conclusion

We hereby confirm that in our professional judgement, as at the date of this document:

- we comply with UK regulatory and professional requirements, including the Ethical Standards issued by the Auditing Practices Board; and
- our objectivity is not compromised.

We would ask the Audit Committee to consider the matters in this document and to confirm that they agree with our conclusion on our independence and objectivity.

Annual Governance Statement

Local Authorities are required to produce an Annual Governance Statement (AGS), which is consistent with guidance issued by CIPFA / SOLACE: "Delivering Good Governance in Local Government". The AGS was included in the Statement of Accounts.

In 2011/12 we identified that future versions of the AGS ought to contain:

- a more detailed action plan for the significant governance matters identified; and
- a clearer statement as to what extent the Council's systems of internal control include Wolverhampton Homes whose significant activity falls within the Council's group boundary.

We reviewed an early draft of the 2012/13 AGS to consider whether it complied with the CIPFA / SOLACE "Delivering Good Governance in Local Government" framework; whether it was misleading or inconsistent with other information known to us from our audit work; and whether it addressed our prior year recommendations.

We made some recommendations to management on how the statement could be further improved when assessed against good practice and these were adopted by management.

We found no areas of concern to report in the final AGS and concluded that The Statement, which has been presented in a new format this year, contains all of the additional pieces of information required.

We also understood the risk identification process that was used to produce the statement and considered whether any governance issues appear to have been omitted. We did not identify any significant omissions and will re-consider this as part of our completion procedures prior to the conclusion of the audit.

As part of our value for money work we reviewed your Medium Term Financial Strategy. Our detailed findings were reported to you at the meeting in June 2013. We have summarised our findings on this page.

Economy, efficiency and effectiveness

Our value for money code responsibility requires us to carry out sufficient and relevant work in order to conclude on whether the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in the use of resources.

The Audit Commission guidance includes two criteria:

- The organisation has proper arrangements in place for securing financial resilience; and
- The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

We also determine a local programme of audit work based on our audit risk assessment, informed by these criteria and our statutory responsibilities. Our audit plan identified the following particular areas of focus:

- Savings plans and the Medium Term Financial Strategy (MTFS);
- Single Status implementation;
- Shared Services Transformation Programme *(replaced by FutureWorks)*;
- Restructuring costs; and
- Procurement follow up.

The main points of our work in these areas are detailed in the table below. Below the table we provide a summary of our conclusions on your financial standing is included here.

Conclusion

We anticipate issuing an unqualified value for money conclusion.

Area of focus from risk assessment	Work undertaken and conclusions
Savings Plans and the Medium Term Financial Strategy 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 £59.18 million over the next five years and this already assumes the successful delivery of savings amounting to £38.630M over five years and £28.517M over the next two years. This represents a significant financial challenge. We also note that the 2013/14 budget is in balance only after the use of £3.716m of general balances and the successful delivery of £17.3m of savings. There are a number of significant risks associated with the 2013/14 budget and the wider MTFS including: • 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. Effectively managing the above risks is critical to the Council's future financial resilience and therefore a key part of our assessment on your	We met regularly with the Section 151 Officer and the Chief Executive to discuss the Council's financial position and plans. We reviewed in-year finance reports to identify any issues and considered their impact on budgets and plans. We reviewed your updated MTFS and its key assumptions. We benchmarked the assumptions you made in the following areas against our national portfolio of audit clients: • Pay Inflation • Non-Pay Inflation • Council Tax increases • Future Government Grant assumptions • Use of general reserves • Level of general reserves • Level of earmarked reserves • Growth pressures • Efficiency targets • Capital spending profiles On the basis of this work we have concluded that the key assumptions supporting your MTFS are broadly consistent with those seen elsewhere in the sector, and whilst there are some notable deviations the assumptions employed appear reasonable and acknowledge the scale of the financial challenge presented. In those areas where assumptions appear less prudent than our benchmark sample you have subsequently revisited the appropriateness of those assumptions in light of updated information, and have adapted your forecasts accordingly. **We have identified no areas where further risk based audit work is required at this time regarding the assumptions in your MTFS and have prepared a more detailed report on this which we are due to**

Area of focus from risk assessment	Work undertaken and conclusions
arrangements for securing economy, efficiency and effectiveness in the use of Council resources.	**present at the September Audit Committee.** **We have highlighted concerns regarding the size of the financial challenge you face in the section '*Financial standing*' above.**
Single Status implementation At the time of drafting our annual audit plan the Council had not yet implemented an affordable Single Status pay agreement The Council is continuing to work toward reaching and implementing an agreement and a number of key activities and decisions are due to take place prior to the date we expect to issue our VfM conclusion. These activities and decisions could impact our VfM conclusion.	We identified that if the Council failed to reach a Single Status agreement in readiness for the 2013/14 financial year we would need to consider the impact on our VfM conclusion. We kept abreast of developments through regular meetings with senior Officers and through review of relevant documentation to monitor progress made throughout the year. We are pleased to note that the Council reached a negotiated agreement with the recognised Trade Unions to implement the National Single Status Agreement; a binding collective agreement and implemented the new structure with effect from 1 April 2013. We have reviewed the documentation supporting the key stages of the decision making process and have not identified any breaches of the Council's own policies and procedures nor any instances of legal advice being overlooked. **We have not identified any significant indicators that value for money has not been achieved by the Council and have concluded that no amendment is required to our VFM conclusion.**

Area of focus from risk assessment	Work undertaken and conclusions
Shared Service Transformation Programme *(replaced by FutureWorks)* The Council has a very old IT system. Various options for replacement are being sought which could have a significant impact on the accounting arrangements and on value for money at the Council. At the time of drafting our Audit Plan the programme team was focussed on the procurement phase of the Transformation Programme. The team was expecting to sign contracts with the future supplier on the 1st April 2013. The team divided the procurement phase into a number of stages in order to appropriately evaluate any potential suppliers. The team has involved a number of stakeholders, including legal advisors. An assurance framework for the procurement phase was drafted. Procurement exercises of this nature pose a number of risks that need to be carefully managed.	We carried out an audit 'health check' of the Shared Services Transformation Programme in March and April of 2013. The scope of this review was to consider the Council's programme management controls as at 30 March 2013. Our work specifically focused on the overall programme structure, the Council's assurance framework and controls over the procurement phase of the programme. We reviewed key project documentation and discussed progress with the Programme Team. **We concluded that as at April 2013 the Council had good programme and risk management arrangements in place for the procurement phase of the Shared Service Transformation Programme but that more needs to be done to clarify and formalise its future assurance needs for the delivery phase.** *We will re-visit the programme this summer for a short, high level review to ensure the robust programme management approach is being maintained post getting the supplier is on-board.*
Restructuring costs The Council has incurred costs relating to restructuring and staff changes during 2012/13. We consider the risk of materially misstating these costs to be very low. However, we are required to consider whether the settlements in aggregate or the governance process surrounding the payments would impact our VfM conclusion.	We understood and evaluated your arrangements for ensuring that individual financial settlements represent value for money and comply with your own regulations regarding decision making. We obtained a complete listing of financial settlements reached in year and sample tested these payments to ensure that policies were adhered to. In particular we ensured that there was • evidence of legal involvement; • a signed official agreement; • appropriate authorisation sought for each of the cases and that authorisation was in line with the constitution limits; • evidence of a sound business case;

Area of focus from risk assessment	Work undertaken and conclusions
	• evidence of following legal advice where received; and • there was appropriate involvement of Human Resources support the business case. **We concluded that adequate procedures were in place that had been followed in each case without exception.** **We considered the level of severance payments in totality and concluded that these should not impact our value for money conclusion.**

Area of focus from risk assessment	Work undertaken and conclusions
Procurement follow up The Council has a significant savings target over the medium term that will be a huge challenge to meet. Success is, in no small part, reliant on procurement savings and although we concluded in prior year that the Council had made some progress we did identify that further work was required to deliver significant savings and that the Council should renew its efforts to improve its procurement related processes and performance. We also recommended that the Council's Internal Auditors undertake a follow up review of its previous findings in this area; not only to ensure that basic controls are adequate during significant change, but also to ensure that these controls are being complied with in practice. We understand that Internal Audit is revisiting this area during the 2012/13 financial year. The Interim Head of Strategic Sourcing has since produced a number of reports that have identified further shortcomings associated with the Contracts Database, the use of e-shop, external consultancy support and the viability of planned procurement savings projections. Delays in implementation of procurement initiatives and reductions in the related assumptions about what can be achieved are reflected in the latest MTFS but further slippage or failure to meet savings requirements is a significant risk to the Council that needs to be well managed.	We have discussed the Council's progress in delivering its plans to achieve the vision of having a more proactive procurement service which acts a key strategic partner to the Council. We are aware that significant steps have been taken to develop the Council's procurement systems and its processes. For instance the team's internal procedures have been overhauled and a new (fully automated and integrated) tendering management tool will go live in November 2013. Steps have also been taken to develop the team with granular performance management information (regarding commitment and utilisation statistics) being available for the first time. There are some signs of improved performance. In terms of improved compliance we understand that members are no longer requested to approve exemptions to the application of tendering rules. We are also aware that efficiency savings have been made. This area however clearly remains a work in progress - and management recognise that there is some way to go still. Delivering improvements in procurement forms part of the Council's broader transformation agenda – implementation of the new Agresso system will deliver a new system and also some procurement staff (and responsibilities) will move to the Transaction Hub next year. Progress on procurement matters should not therefore be considered in isolation from this broader agenda and there is clearly lots of change for the Council to manage over the coming months across this agenda. In terms of key next steps we understand that the new Procurement Code is due to be considered for approval by Cabinet over the coming weeks and that the Procurement Team will be focused on getting these and other developments in place and embedded. **We will maintain a watching brief on this area, but have concluded at this stage that no further detailed work on this area is appropriate.**

Financial Standing

In our audit plan we highlighted the significant financial challenge facing the Council as a specific audit risk and have summarised our findings on the detail of your Medium Term Financial Strategy (MTFS) in this report against that risk as well in a separate report to this Committee. A broader view of your financial challenge makes reaching a positive conclusion on your financial standing increasingly difficult. As you have highlighted in your recent communications to staff, the Council cannot make up the budgeted difference in funding from reserves because 'if you carry on as [you] are by April 2015 those reserves will have been reduced to an unsustainable level.'

Below we highlight areas where further work is needed over the coming 12 months for us to continue to assess the Council as complying with Audit Commission guidance regarding our value for money code responsibilities.

Budgetary control

We were surprised and concerned that the Council overspent against its General Fund budget by £3.6m in 2012/13. This variance exceeded the £2.5m forecast at the third quarter of £2.5m, which we understand was considered to be a prudent estimate. A number of variances were recognised between quarter three forecast and actual outturn position across directorates; most notably within the Delivery and Education and Enterprise. This appears to have been primarily due to the incorrect classification of certain items of expenditure as 'non-controllable' when they should instead have treated as 'controllable'. As a result of this misclassification the budgetary control and monitoring and reporting of spend in this area was lacking and significant variances against these budgets were overlooked by both budget holders and service accountants.

Internal Audit are currently performing two separate reviews in relation to the 2012/13 budget over spend, on recharging for Property Services and Education and Enterprise recharges. We eagerly await the outcome of these reviews and will consider the effectiveness of management's actions to address any issues identified. As a minimum, we think it is essential that weaknesses in budget monitoring are addressed immediately and that more regular monitoring of such expenditure is introduced.

Taking a radical approach to service provision

To continue to be able to demonstrate that you have sufficient resources available to meet your commitments for a longer period we think it will be of paramount importance that the Council:

- continues to consider a broad range of alternative service delivery models where appropriate. We understand that a range of options are currently being explored and this must continue as the 2014/15 budget and MTFS are developed; and
- works together to ensure there is a strong consensus about the need for change. Cuts in Government funding mean that it is no longer possible for the council to carry on with 'business as usual' so tough decisions will need to be made and previously unpalatable options will need to be considered thoroughly including scaling back those activities which don't make a clear contribution to Corporate Plan priorities.

Information for decision making

To be able to make the most appropriate decisions for your local circumstances it is vital that the Council:

- is able to make tough decisions on cost reductions and cuts based on robust information on costs and cost drivers. Officers must ensure that sufficient information is available to make informed and rounded decisions based on thorough cost-benefit analysis and options appraisals. Improvements have been made in this area but there is further work to do to improve productivity based on thorough investigation and interpretation of benchmark data including data on unit costs. This data may serve as a useful consideration during the coming round of resource prioritisation discussions; and

- continues to develop an understanding of its cost base and unit costs. This should help you to make informed decisions on which areas have the greatest opportunities to make savings and may inform decisions on which areas to invest more effort in.

Managing the financial impact of the redundancy programme

The Council is planning a significant programme of redundancies in 2013/14, accompanied by restructures and business reviews. We absolutely recognise the need to consider reducing your pay bill considering non-schools General Fund services have an associated pay bill of £140m per annum of your £256m net budget requirement. We also recognise that the Council has a number of reserves which could be utilised to support the upfront costs of such a scheme. However, we note that the use of general fund reserves during 2013/14 is highly likely. Member approval must be obtained for any reduction in the General Fund below the £15m current required by your own reserves policy. It is imperative that once all upfront costs and longer term savings are taken into consideration you are still able to demonstrate the ability to set a balanced budget with an appropriate level of reserves.

Management are responsible for developing and implementing systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice.

As auditors, we review these arrangements for the purposes of our audit of the Statement of Accounts and our review of the annual governance statement.

Internal controls

Accounting systems and systems of internal control

We have considered the control issues identified during the audit and while we have concluded that no issues were identified that would materially impact on our accounts audit, we have set out in the section below a small number of recommendations in relation to control issues identified during the year.

Reporting requirements

We have to report to you any deficiencies in internal control that we found during the audit which we believe should be brought to your attention. We identified no material control weaknesses, however we wanted to bring your attention to the following:

Summary of significant internal control deficiencies

Deficiency	Recommendation
Valuations Land values are determined in accordance with site acreage and building values are calculated based on gross internal floor areas. Accordingly, it is important that this data is complete and accurate at each balance sheet date. At present this is not achieved which may result in over- or under-statement of the balance sheet. This is particularly relevant to schools, for which works are regularly being carried out, but applies to all asset types.	There is a need for the property and asset management teams to carry out a data validation exercise before every valuation and again at the end of the financial year to ensure that any increases or reductions in and or building size are recorded on a timely basis. This ought to include liaison with the Building School's for the Future team but may require consultation with other relevant departments within the Council who hold up to date information on the Council's assets.
Academies We identified a small number of assets relating to academy schools that: • remained in the balance sheet after they should have been written out; or • were overvalued as a result of not being revalued to reflect the change in the future use of existing assets.	There is a need to strengthen procedures to ensure that the finance, property and valuation teams share a common understanding of what the accounting requirements are for assets associated with academy schools. A policy should be drafted and clear accountability defined to ensure that the valuation team is:

There seems to be a lack of clarity regarding which assets need to be revalued, when and on what accounting basis.	• aware of any changes in use of school assets; • aware of any milestones being reached on any academy conversion or new build progress; and • clear what the accounting rules require.

We ask that the Audit Committee, as those charged with governance, confirm to us that there are no additional matters relating to fraud that should be brought to our attention.

As part of work to address the risk of fraud, we use auditing techniques to select journal entries which we believe have a greater risk of containing fraud or error.

We identified no issues to report to you as part of this work.

Risk of fraud

We discussed with you your understanding of the risk of fraud and corruption and any reported instances when presenting our plan.

During the year the Council has informed us of a small number of matters of actual and/or potential fraud which have been investigated by Internal Audit. We have considered these matters and the course of action taken in response to them by the Council and have identified no issues or concerns to report in this context.

In presenting this report to you we ask for your confirmation that there have been no changes to your view of fraud risk and that no additional matters have arisen that should be brought to our attention. A specific confirmation from management in relation to fraud is included in the letter of representation.

Although it is not our primary responsibility to detect fraud, our audit procedures seek to identify material misstatements resulting from fraud. We included two fraud risks in our audit plan and summarised our audit findings in the section 'Audit Approach'.

Our fee proposals were included in our 2012/13 Audit Plan which we reported to you in January 2013.

At that time our Audit Plan noted that due to the degree and pace of change within the Council and the importance of achieving change in a safe and controlled way, additional audit support would be required to address additional risks.

Fees update

Fees update for 2012/13

We reported our fee proposals in our plan. Our actual fees are expected to be in line with our proposals:

	2012/13 outturn	2012/13 fee proposal	2011/12 outturn
Statement of Accounts (including whole of government accounts) and Value for Money Conclusion	251,100	251,100	418,500
Work on additional risks	65,800	65,800	72,000
TOTAL	**316,900**	**316,900**	**490,500**

Our fee for certification of grants and claims is yet to be finalised for 2012/13 and will be reported to those charged with governance by March 2014 within the Grants Report to Management in relation to 2012/13 grants.

Non audit services

In addition to the statutory services provided as your Appointed Auditor, PwC has, during the year, provided a small number of non-audit services which fell outside of the Code of Audit Practice.

These services, and the associated fees (excluding VAT), were:

- Accelerated Asset Review – Phase 4, Stage 1 office workstream pre-tender planning. The fee for this work during 2012/13 was £36,000.
- Exploring New Financial Models to Invest in Housing. The fee for this work was £9,000.

We confirm to you that we have appropriate safeguards in place to maintain our audit independence.

Appendices

We are required to report to you all uncorrected misstatements we have identified.

If the accounts remain unadjusted for this item, we will need a written representation explaining why.

A proposed letter of representation is included in Appendix 2 to this report.

Appendix 1: Summary of uncorrected misstatements

We found the following error during the audit that has not been adjusted by management. You are requested to consider this formally and determine whether you would wish the accounts to be amended. If the misstatements are not adjusted we will need a written representation from the Council explaining your reasons for not making the adjustment.

No	Description of misstatement	Income statement		Balance sheet		Management comment
		Dr	Cr	Dr	Cr	
1	**Valuation of Birmingham Airport investment** Dr Non Current Investments Cr (Surplus) or Deficit on Revaluation of Non-Current Assets Wolverhampton City Council owns 4.7% of the ordinary shares in Birmingham Airport Holdings Ltd. The measurement basis for this investment is 'Fair Value'. In order to ensure an accurate fair value is used at each balance sheet date the Council receives an annual valuation from a third party provider. The valuation for 31 March 2013 was received after the draft 2012/13 accounts had been produced. The valuation indicated that the most accurate valuation for the Council's shares had risen by £283k from last year to a new valuation of £18,903k. The valuation in the final accounts has not been amended so remains at £18.6m. *NOTE: This amendment, if made, would have been reversed out of the Total Comprehensive Income and Expenditure position as a required 'Adjustment between Accounting Basis & Funding Basis under Regulations' so that there would have been no net impact on the tax payer.*		283	283		The revised estimate is materially similar to the value in the draft accounts. We understand that none of the other Councils are amending for the update so our decision is consistent with all the other Councils.
	TOTAL	**0**	**283**	**283**	**0**	

The total impact of unadjusted audit misstatements on the CIES would have been to reduce the deficit by £283k.

We have issued a number of reports to those Charged with Governance relating to our 2012/13 audit. These are summarised here.

Appendix 2: Audit reports issued in 2012/13

The following table outlines the audit reports that have been issued or are due to be presented in year:

Stage of the audit	Output	Date
Audit planning	**Audit Plan**	March 2013
Audit findings	**External audit update report** • Audit Progress update • Control weakness and audit findings to date • Communications about fraud risk	June 2013
VfM findings	**Medium Term Financial Strategy report** • Analysis of key assumptions in your MTFS • Comparisons to our other External Audit clients • Summary of findings that feed our value for money conclusion	August 2013
Audit reports	**ISA (UK&I) 260 report incorporating specific reporting requirements, including:** • Any expected modifications to the audit report • Uncorrected misstatements, i.e. those misstatements identified as part of the audit that management have chosen not to adjust • Material weaknesses in the accounting and internal control systems identified as part of the audit • Our views about significant qualitative aspects of your accounting practices including accounting policies, accounting estimates and financial statements disclosures. • Any significant difficulties encountered by us during the audit; • Any significant matters discussed, or subject to correspondence with, Management; • Any other significant matters relevant to the financial reporting process; and • Summary of findings from our use of resources audit work to support our value	September 2013

	for money conclusion.	
Audit reports	**Financial Statements opinion including Use of Resources conclusion**	September 2013
Other public reports	**Annual Audit Letter** A brief summary report of our work, produced for Members and to be available to the public.	November 2013

There are a number of matters on which we are required to ask for a written representation.

A draft letter of representation is included in this appendix.

Appendix 3: Letter of representation

PricewaterhouseCoopers LLP
Cornwall Court
19 Cornwall Street
Birmingham
B3 2DT

Dear Sirs

Representation letter – audit of Wolverhampton City Council's (the Council) statement of accounts for the year ended 31 March 2013

The Council is responsible for preparing consolidated statement of accounts in respect of itself and its subsidiary undertakings (together "the group").

Your audit is conducted for the purpose of expressing an opinion as to whether the Statement of Accounts of the Council and the group give a true and fair view of the state of affairs of the Council and group as at 31 March 2013 and of the deficit and cash flows of the group for the year then ended have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 supported by the Service Reporting Code of Practice 2012/13.

Subsequent references in this letter to "the Statement of Accounts" refer to both the statement of accounts of the Council and the consolidated statement of accounts of the group.

I acknowledge my responsibilities as the Assistant Director Finance (Section 151 Officer) for preparing the Statement of Accounts as set out in the Statement of Responsibilities for the Statement of Accounts. I also acknowledge my responsibility for the administration of the financial affairs of the Council and that I am responsible for making accurate representations to you.

I confirm that the following representations are made on the basis of enquiries of other chief officers and members of the Council and the group with relevant knowledge and experience and, where appropriate, of inspection of supporting documentation sufficient to satisfy myself that I can properly make each of the following representations to you.

I confirm, to the best of my knowledge and belief, and having made the appropriate enquiries, the following representations:

Statement of accounts

- I have fulfilled my responsibilities for the preparation of the Statement of Accounts in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 supported by the Service Reporting Code of Practice 2012/13; in particular the Statement of Accounts give a true and fair view in accordance therewith.
- All transactions have been recorded in the accounting records and are reflected in the statement of accounts.
- Significant assumptions used by the Council and group in making accounting estimates, including those surrounding measurement at fair value, are reasonable.
- All events subsequent to the date of the statement of accounts for which the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 requires adjustment or disclosure have been adjusted or disclosed.

- The effects of uncorrected misstatements are immaterial, both individually and in the aggregate, to the statement of accounts as a whole. A list of the uncorrected misstatements is attached to this letter.

Information Provided

I have taken all the steps that I ought to have taken in order to make myself aware of any relevant audit information and to establish that you, the Council's auditors, are aware of that information.

I have provided you with:

- access to all information of which I am aware that is relevant to the preparation of the statement of accounts such as records, documentation and other matters, including minutes of the Council and its committees, and relevant management meetings;
- additional information that you have requested from us for the purpose of the audit; and
- unrestricted access to persons within the group from whom you determined it necessary to obtain audit evidence.

So far as I am aware, there is no relevant audit information of which you are unaware.

Accounting policies

I confirm that I have reviewed the Council's and the group's accounting policies and estimation techniques and, having regard to the possible alternative policies and techniques, the accounting policies and estimation techniques selected for use in the preparation of Statement of Accounts are appropriate to give a true and fair view for the Council's and the group's particular circumstances.

Fraud and non-compliance with laws and regulations

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

I have disclosed to you:

- the results of our assessment of the risk that the statement of accounts may be materially misstated as a result of fraud.
- all information in relation to fraud or suspected fraud that we are aware of and that affects the group and involves:
  - management;
  - employees who have significant roles in internal control; or
  - others where the fraud could have a material effect on the statement of accounts.
- all information in relation to allegations of fraud, or suspected fraud, affecting the Council and group's statement of accounts communicated by employees, former employees, analysts, regulators or others.
- all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing statement of accounts.

I am not aware of any instances of actual or potential breaches of or non-compliance with laws and regulations which provide a legal framework within which the Council and the group conducts its business and which are central to the Council's and the group's ability to conduct its business or that could have a material effect on the statement of accounts.

I am not aware of any irregularities, or allegations of irregularities including fraud, involving members, management or employees who have a significant role in the accounting and internal control systems, or that could have a material effect on the statement of accounts.

The pension fund has not made any reports to the Pensions Regulator nor am I aware of any such reports having been made by any of our advisors. I confirm that I am not aware of any late contributions or breaches of the schedule of contributions that have arisen which I considered were not required to be reported to the Pensions Regulator. I also confirm that I am not aware of any other matters which have arisen that would require a report to the Pensions Regulator.

There have been no other communications with the Pensions Regulator or other regulatory bodies during the year or subsequently concerning matters of non-compliance with any legal duty.

Related party transactions

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

Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the requirements of Section 3.9 of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

We confirm that we have identified to you all senior officers, as defined by the Accounts and Audit Regulations 2011, and included their remuneration in the disclosures of senior officer remuneration.

Employee Benefits

I confirm that we have made you aware of all employee benefit schemes in which employees of the Council and the group participate.

Contractual arrangements/agreements

All contractual arrangements (including side-letters to agreements) entered into by the Council and the group have been properly reflected in the accounting records or, where material (or potentially material) to the statement of accounts, have been disclosed to you.

Litigation and claims

I have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the statement of accounts and such matters have been appropriately accounted for and disclosed in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

Taxation

I have complied with UK taxation requirements and have brought to account all liabilities for taxation due to the relevant tax authorities whether in respect of any direct tax or any indirect taxes. I am not aware of any non-compliance that would give rise to additional liabilities by way of penalty or interest and I have made full disclosure regarding any Revenue Authority queries or investigations that we are aware of or that are ongoing.

Pension fund assets and liabilities

All known assets and liabilities including contingent liabilities, as at the 31 March 2013, have been taken into account or referred to in the statement of accounts.

Details of all financial instruments, including derivatives, entered into during the year have been made available to you. Any such instruments open at the 31 March 2013 have been properly valued and that valuation incorporated into the statement of accounts.

The pension fund has satisfactory title to all assets and there are no liens or encumbrances on the pension fund's assets.

The value at which assets and liabilities are recorded in the net assets statement is, in the opinion of the Council, the market value. We are responsible for the reasonableness of any significant assumptions underlying the valuation, including consideration of whether they appropriately reflect our intent and ability to carry out specific courses of action on behalf of the pension fund. Any significant changes in those values since the date of the statement of accounts have been disclosed to you.

Pension fund registered status

I confirm that the West Midlands Pension Fund is a Registered Pension Scheme. We are not aware of any reason why the tax status of the scheme should change.

Bank accounts

I confirm that we have disclosed all bank accounts to you including those that are maintained in respect of the pension fund.

Accounting Estimates

Regarding accounting estimates that were recognised in the financial statements:

- The Council has used appropriate measurement processes, including related assumptions and models, in determining the accounting estimate in the context of the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13;
- Measurement processes were consistently applied from year to year;
- The assumptions appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Council, where relevant to the accounting estimates and disclosures;
- Disclosures related to accounting estimates are complete and appropriate under the Code; and
- No subsequent event requires adjustment to the accounting estimates and disclosures included in the financial statements.

Financial Instruments

All embedded derivatives have been identified and appropriately accounted for under the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

Provisions

Provisions for depreciation and diminution in value including obsolescence have been made against property, plant and equipment on the bases described in the financial statements and at rates calculated to reduce the net book amount of each asset to its estimated residual value by the end of its probable useful life in the Council's and the group's business. In this respect I am satisfied that the probable useful lives have been realistically estimated and that the residual values are expressed in current terms.

Full provision has been made for all liabilities at the balance sheet date including guarantees, commitments (in particular in relation to redundancy plans) and contingencies where the items are expected to result in significant loss. Other such items, where in my opinion provision is unnecessary, have been appropriately disclosed in the financial statements.

Full provision has been made for all liabilities at the balance sheet date including guarantees, commitments and contingencies where the items are expected to result in significant loss. Other such items, where in my opinion provision is unnecessary, have been appropriately disclosed in the consolidated financial statements. The provision of £26.5 million that we have included in our accounts for the potential liability for equal pay and back pay claims complies with International Accounting Standard (IAS) 37 and is supported, in good faith, by the external legal advice received.

This represents our best estimate of the most likely future costs to the Council and we have not received any other additional or contradictory advice that has not been shared with you.

The Council has determined a proper application of the statutory provisions for the neutralisation of the impact of Single Status provisions on the General Fund balance.

Investments

I confirm that all significant assumptions made in relation to fair value measurement and disclosures are reasonable and appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the Council and the group to the fair value measurements or disclosures.

I confirm that we believe the inclusion of the Council's investment in Birmingham Airport Holdings Ltd at £18.6 million is appropriate because:

- this materially reflects the latest valuation of the Ordinary Shares and preference shares provided as at the balance sheet date as provided by Solihull Council and BDO (£18.9 million versus prior year £18.6m).
- there remains in place a side agreement which restricts the sale of shares by all seven stake-holding councils and therefore, whilst the valuation given provides a best estimate of a price that could be achieved on the open market, the restrictions mean that the open market value (OMV) is always likely to overstate the value that any Council would actually be willing to pay. This is deemed particularly significant in the current economic climate when there is unlikely to be any Council with sufficient spare resources to purchase an additional share in the Airport - especially at an OMV;
- the terms of the work had been agreed by all relevant Appointed Auditors;
- the methods followed are reasonable given the requirements of the Code; and
- the findings are fed by a number of factors and because many of these are judgements, every valuer is bound to make different assumptions but the assumptions taken do not appear unreasonable.

Using the work of experts

I agree with the findings of Solihull Council and BDO, experts in evaluating the Airport Valuation, regarding their valuation of our share of Birmingham Airport Holdings Ltd and have adequately considered the competence and capabilities of the experts in determining the amounts and disclosures used in the preparation of the financial statements and underlying accounting records. The Council did not give or cause any instructions to be given to experts with respect to the values or amounts derived in an attempt to bias their work, and I am not otherwise aware of any matters that have had an impact on the objectivity of the experts.

Valuation of Property, Plant and Equipment

I have considered indicators of impairment for our Property, Plant and Equipment asset based and am satisfied that there are no indicators that the Council's asset base has been materially impaired.

Depreciation of housing stock

The Council has assessed the impact of using the Major Repairs Allowance as an estimate for depreciation of council dwellings in the Housing Revenue Account and is satisfied that this amount is a reasonable estimate of the amount of depreciation charge for these assets.

Completeness of Fixed Asset records on the General Ledger

I am satisfied that the general ledger system is complete and that there are no material differences between the assets recorded on the Property Services Database and those recorded on the general ledger system (FMIS), that is used to populate the financial statements.

Revenue provision

I am satisfied that our revised methods for determining an annual revenue provision, and for splitting interest cost between the HRA and General Fund are appropriate, prudent and compliant with the requirements of The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended by Statutory Instrument 2008 no. 414 s4).

Deficiencies in internal control

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

Subsequent events

Other than those already disclosed, there have been no circumstances or events subsequent to the period end which require adjustment of or disclosure in the statement of accounts or in the notes thereto.

Accounting for Academy Schools

All schools that have transferred to Academy status have been removed from the appropriate balance sheet. All current school assets for which the future use is unknown have been valued at the most appropriate market value. No decisions have been taken about the future use of school assets that have not been reflected in their valuation.

As minuted by the Audit Committee at its meeting on 23 September 2013

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Assistant Director Finance (Section 151 Officer)

For and on behalf of Wolverhampton City Council

Date ....

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