



PUBLIC SECTOR

Annual Audit Letter 2008/09

Kettering Borough Council
19 January 2010

AUDIT

Purpose

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

Scope of our audit

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

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

Key Messages

- Our **use of resources** assessment, the first under the Audit Commission's new UoR regime, demonstrated that the Council had adequate processes in place across all Key Lines of Enquiry (KLOE) and scored an overall level 2. The Council produced a brief self assessment to facilitate the audit and is planning to build on this in the new year by producing case studies to highlight key achievements in 2009/10. As the assessment process will get tougher year on year, the Council will need to demonstrate improvement if it is not only to retain its score but also improve it. The areas the Council will need to focus on include demonstrating that its performance levels are high relative to other Council's in its key service areas, undertaking more work to assess relative value for money in front line and back office services, assessing the effectiveness of key partnerships and setting out its approach and rational for the commissioning of key services. Despite the identification of the above issues we concluded that the Council had for the most part made proper arrangements to secure economy, efficiency and effectiveness in its use of resources. Our value for money conclusion was therefore unqualified on this basis.
- We identified one issue during the course of the financial statements audit that was considered to be material. The Council adjusted the financial statements and we issued an unqualified audit opinion on the Council's revised financial statements on 29th September 2009.

Fees

Our fee for the audit is £111,000 (excluding work on grant claims which is billed separately). This is in line with the fee agreed with you in our audit plan.

The contacts at KPMG in connection with this report are:

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1. Key recommendations
2. Reports issued

This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document. External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Saverio Della Rocca, who is the engagement director to the Authority, telephone 0121 335 2367, email saverio.dellarocca@kpmg.co.uk who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 236 4000, email trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Investigation Officer, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by e mail to: complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421

Future Issues

- From 2010/11, local government bodies are required to prepare their financial statements under International Financial Reporting Standards (IFRS), which contain a number of significant differences from the current financial reporting regime. The Council has started preparing for this transition, although as with all local authorities there remains much to be done to identify the full impact of IFRS on its accounting arrangements and to make the necessary changes.
- Sustainability performance - The Treasury is developing guidance for 2010/2011 which will require all public sector bodies to report publicly on sustainability performance in annual reports. CIPFA is in discussion with the Treasury about when and in what form this requirement will be formalised for local authorities. The reported information will be subject to audit and scrutiny. Sustainability reporting will be difficult to implement and many organisations will need to act quickly to implement new information gathering processes. Next year's UoR assessment will also consider sustainability issues within the Natural Resources element of the Managing Resources theme.
- Public expenditure forecasts indicate that there will be significant pressure on local authorities' funding in the medium term. Future financial settlements will be tight, increasing the need for local authorities to have comprehensive efficiency programmes supported by sound financial management arrangements. It is likely that bold measures will be required to generate sufficient savings to mitigate the impact on priority services. More than ever before, officers and Members will need to focus on identifying these significant savings measures and ensuring that robust arrangements are in place to monitor their delivery to ensure they are realised. The Council has a good track record in delivering such efficiency and savings targets. It will, however, be necessary to revisit and update the Council's plans to ensure that you can deliver the levels of savings required for the future.

Acknowledgement

We would like to thank the Council's management and staff for the help, support and co-operation they have provided throughout our audit. We have agreed our audit plan for the 2009/10 audit and look forward to working closely with the Council in the coming year to deliver this programme of work.

The main elements of our use of resources work are:

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

The findings from this work are summarised below.

Element of work	Key findings								
<p>Use of Resources</p>	<p>Our assessment of Kettering Borough Council against the three themes resulted in the following scores on a scale of one (inadequate) to four (performing strongly):</p> <table border="1" data-bbox="445 913 1179 1100"> <thead> <tr> <th>Area</th> <th>Score</th> </tr> </thead> <tbody> <tr> <td>Managing finances</td> <td>2</td> </tr> <tr> <td>Governing the business</td> <td>2</td> </tr> <tr> <td>Managing resources</td> <td>2</td> </tr> </tbody> </table> <p>These scores build on last year’s UoR assessment when the Council scored level 3 against the financial reporting, financial standing, financial management, internal control and value for money themes. It should be noted, however, that direct comparisons cannot be made between the previous UoR scores and those awarded this year due to the differences in each assessment framework. For example, for district councils the Managing resources assessment focused this year only on workforce planning arrangements, an area not formerly considered by the previous UoR framework.</p> <p>In achieving an overall level 2, the Council has been able to prove that overall it has adequate arrangements in place across all of the KLOE. However, there is some work required across all three themes to achieve a level 3.</p> <p>For Managing finances, the issues related to developing the Council’s Medium Term Financial Strategy ensuring that it adequately considers potential funding scenarios and address any future funding gaps. For Governing the Business, the issues related to aspects of the Council’s commissioning and procurement processes and in particular ensuring that the Council has considered the different ways of providing services from a value for money and performance perspective. For Managing Resources, the issues related to developing a workforce succession plan and benchmarking tools to compare the Council’s staff costs with other organisations.</p> <p>The scores reflect the position during 2008/09 and we acknowledge the work that the Council has been carrying out to improve its arrangements. Officers have outlined to us a number of changes that have been made that they believe may have a positive impact on the UoR scores for 2009/10. This will of course have to be assessed in detail during next year’s audit.</p>	Area	Score	Managing finances	2	Governing the business	2	Managing resources	2
Area	Score								
Managing finances	2								
Governing the business	2								
Managing resources	2								
<p>Value for money conclusion</p>	<p>Based on our use of resources assessment and relevant local risk work set out above, we concluded that the Authority has appropriate arrangements in place to ensure the effective use of its resources.</p> <p>Our VFM conclusion was therefore unqualified on this basis.</p>								

Audit opinion

We issued an unqualified opinion on your accounts on 29th September 2009. This means that we believe the accounts give a true and fair view of the financial affairs of the Council and of the income and expenditure recorded during the year.

Before we give our opinion on the accounts, we are required to report to 'those charged with governance' any significant matters identified. We did this in our report to the Monitoring & Audit Committee on 29th September 2009 and the key issues are summarised below.

Accounts production and adjustments to the accounts

- We received a complete set of draft accounts by the 30th June deadline supported by good quality working papers.
- Our audit identified one audit adjustment which was material in nature to the financial statements in relation to the accounting treatment for the impairment of council dwellings. We identified four non-material audit differences which were corrected by the Council. We also identified a number of presentational adjustments which the Council adjusted in its final set of financial statements.
- Our audit resulted in three recommendations regarding financial controls, of which one had been implemented between our interim and final audits. We also highlighted a further recommendation relating to IT controls from the previous year's audit for which management have set a revised targets date.

There were no other issues raised for the attention of the Monitoring & Audit Committee.

Appendix 1: Key recommendations

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

Issue/ Recommendation	Management Response / Timescale for implementation
Financial statements audit	
Procurement	
<p><u>Issue</u></p> <p>During 2008/09, Internal Audit carried out a review surrounding Procurement as a result of concerns over potential fraudulent activity. Based on the evidence and information made available to them, Internal Audit were unable to confirm whether fraudulent activity had occurred, however they did identify a number of instances where financial regulations were not followed.</p> <p>Internal Audit raised a significant number of recommendations as a result of this review, and consequently gave a "limited assurance" rating.</p> <p><u>Recommendation</u></p> <p>The Council should ensure appropriate action is taken to implement the recommendations raised by Internal Audit.</p> <p>The Council will also need to consider the impact on the overall control environment and include comments in their Annual Governance Statement.</p>	<p>The Council is making good progress with the recommendations. A follow up audit is planned for September 2009, which will assess the level of progress made.</p> <p>The Council through the Corporate Governance Group is revising the Corporate Anti-Fraud and Corruption Strategy and will update all staff in due course.</p> <p><u>Officer and due date</u></p> <p>Head of Housing, 30 September 2009</p> <p>Head of Finance, 31 October 2009</p>
Financial systems issues	
<p><u>Issue</u></p> <p>We have identified, through our testing and review of Internal Audit's work, a number of issues in relation to financial system controls, including:</p> <ul style="list-style-type: none"> • a lack of debt monitoring and debt recovery action; • a lack of independent review of data input into the payroll system; • no independent review of permanent changes made to payroll files. <p>These issues increase the risk of significant misstatement of related accounts balances. There is also an increased risk income owing to the Council in not being collected.</p> <p><u>Recommendation</u></p> <p>The Council should ensure that sufficient resource is allocated to these areas during the closedown process to ensure that the risk of misstatement in the accounts is minimised.</p> <p>A robust review of the accounts should be undertaken by a senior officer, with particular focus on these areas.</p> <p>The Senior Management Team (SMT) should reinforce the importance of the control environment across the Council in relation to the key financial systems and the importance of Internal Audit's findings.</p>	<p>The payroll issues were historical and revised processes were in place when the audit was undertaken. The recommendations relating to debt monitoring and recovery have been implemented.</p> <p>Full reconciliations are undertaken as a matter of course through the final accounts process.</p> <p><u>Officer and due date</u></p> <p>Head of Finance</p> <p>Complete</p>

Issue/ Recommendation	Management Response / Timescale for implementation
<p>Housing Revenue Account Balance</p> <p><i>Issue</i></p> <p>During the last five years, the balance on the Housing Revenue Account (HRA) has been falling (from £780k as at 31 March 2004 to £220k as at 31 March 2007). This downward trend was reversed at the end of the 2007/08 financial year as the balance increased to £299k. However, this balance is projected to fall to £147k at the end of the 2008/09 financial year.</p> <p>As part of their budget monitoring process, the Council identified a significant overspend on repairs and maintenance. The Council carried out a review to understand the reason for the overspend and identified significant weaknesses in how non-urgent repairs works had been delivered. As a result, the Council has identified the need for a new Stores and Appointments system.</p> <p><i>Recommendation</i></p> <p>The Council will need to undertake regular monitoring of both the HRA balance and repairs and maintenance expenditure.</p> <p>The Council will need to ensure that adequate project management arrangements are in place to ensure the new Stores and Appointments system is implemented effectively.</p>	<p>The Council continues to be heavily penalised by the Housing Subsidy system, which is exacerbated by changes in interest rates. The Council has budgeted to return its HRA balance to in excess of £300,000 in 2009/10.</p> <p>It was during regular monitoring that the above issues were identified and subsequently resolved. The Stores system has now been implemented and the Appointments system is expected to be implemented toward the end of 2009.</p> <p><i>Officer and due date</i></p> <p>Head of Housing, 31 December 2009</p>
<p>IT control issues</p> <p><i>Issue</i></p> <p>The IT control environment over the Council's key financial systems underpins the financial system controls in place and provides additional assurance over the robustness of those systems.</p> <p>We noted a number of weaknesses in the IT control environment, currently there is no formalised IT Security Policy, Business Continuity and Disaster Recovery Plan in place and in parts the documents are in-complete, in addition backups are not subject to regular review.</p> <p><i>Recommendation</i></p> <p>The Council should ensure that a formalised IT Security Policy is put in place and the Business Continuity and Disaster Recovery plans are complete and approved and that they are fully embedded across the Council.</p>	<p>The Council is working to draft documents for Security, Business Continuity and IT Disaster Recovery. The Council is working with Zurich Municipal to formalise its approach and this will be completed by October 2009.</p> <p><i>Officer and due date</i></p> <p>Head of Finance, 31 October 2009</p>

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

Report	Date issued
Audit and Inspection Plan 2008/09	30 September 2008
Annual External Audit Report 2007/08	9 March 2009
Annual Audit & Inspection Letter 2007/08	30 April 2009
Interim Audit Report 2008/09	30 April 2009
Annual Audit Fee 2009/10	30 April 2009
Report to those charged with governance 2008/09	29 September 2009