

Annual governance report

Cheshire East Borough Council

Audit 2010/11



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Key messages

This report summarises the findings from the 2010/11 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.

Audit opinion and financial statements

The preparation of the Council's 2010/11 accounts was particularly challenging this year as a result of:

- changes in reporting requirements due to the introduction of International Financial reporting standards (IFRS).
- the upgrade of the main financial ledger; and
- implementation of a new revenues and benefits financial system.

The Council increased the capacity of the finance team during the year. This has helped to ensure that the restatement of the opening balances complied with IFRS requirements and that the principles and methodologies used to calculate the restated balances were in line with CIPFA guidance.

The Council's finance team worked hard again this year to prepare the financial statements in line with the statutory deadline and to respond to queries during my audit visit. I recognise the challenging circumstances in which this has been undertaken. However, the financial statements presented for audit in July 2011 contained 2 material and a significant number of other errors. Many of these were identified as part of my consistency checks.

The Council needs to continue to make further improvements to its arrangements for preparing accurate financial statements and responding to audit queries. A better quality assurance process - before the accounts were approved for audit – would have corrected many of these items.

I have not yet completed my audit work. In particular I need to complete my audit of the collection fund and checking through the changes made in the revised financial statements presented to this Committee.

Subject to the satisfactory completion of my work, I expect to issue an audit report including an unqualified opinion on the financial statements by 30 September 2011. If any matters arise as a result of this work I will report this to you verbally at the Audit and Governance Committee meeting on 29 September.

Value for money

I intend to issue an unqualified conclusion stating that the Council has adequate arrangements to secure value for money.

The Council has effective arrangements for financial governance, planning and control. During 2010/11 the Council continued to develop its detailed systems and processes to manage its financial risks and opportunities. The annual budget was based on corporate priorities set out in the Sustainable Community Strategy and Corporate Plan. These were both revised during the year. For 2010/11 the Council included the key elements of its medium term financial plan in its annual budget report. This included a savings target of £7.7m.

In July 2010, the business planning cycle for 2011/14 was launched. It aimed to produce a single integrated business plan and budget setting out how the Council would achieve its objectives both in budgetary and service delivery terms. An efficiency group, comprising officers and members, was established to lead the process and to provide challenge around the Council's transformation programme.

During the year the Council experienced significant budget pressures particularly in children's and adults services. In year monitoring of the 2010/11 budget enabled the early identification of financial pressures. This led to further plans to deliver additional savings. At the year end, the net service overspend was £9.5m before taking account of under spends in other areas of £7.3. The Council planned to repay £4.3m to general fund reserves during the year. This fell to £2.3m at the year end mainly because of the net service overspend. The reported closing balance on the general fund is £12.3m. This is higher than forecast during the 2011/12 budget setting round but does not fully cover the Council's assessed financial risk of £14.7m.

The first quarter finance report for 2011/12 reported a projected net service overspend of £5.7m. Directorate budgets for the year already include a requirement for significant savings. Further action will be necessary to deliver those savings and manage in year pressures. The latest financial projections show a £29.4m shortfall between funding and expenditure over the next three years.

The Council is prioritising its resources within tighter budgets by achieving cost reductions and improving efficiency and productivity through the budget setting and challenge process. For 2010/11, a number of proposals to improve efficiency and / or reduce costs were included within the Council's budget. In year financial pressures required further action to contain costs and find further savings of £10.5m. This was done through a combination of service redesign and short term measures. The corporate management team monitored the delivery of the savings targets on a weekly basis against remedial action plans drawn up by directorates. These processes were in place throughout the year. However it is difficult to clearly establish what proportion of the total savings delivered relates to efficiency projects as opposed to remedial action to manage the in year pressures. For 2011/12 the Council has implemented a traffic light system to report progress against agreed savings targets.

I found evidence that the Council is active in reviewing its services and comparing performance and costs with other organisations. For example, in preparation for the 2010/11 business planning round, Children's Services carried out a value for money assessment to help its understanding of the comparative efficiency and effectiveness of its services. The results informed its business planning and budget proposals for the year. This approach is formalised in the Council's VFM strategy which outlines sources of data and analyses to be performed at both service and corporate levels. The Council has already identified gaps in available benchmarking information and is looking to develop contact with groups which will enable detailed service specific benchmarking.

Before I complete my audit

I confirm to you my independence and the scope of my audit work

My report includes only matters of governance interest that have come to my attention in performing my audit. My audit is not designed to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including Ethical Standard 1 (revised) - Integrity, Objectivity and Independence. I identified a potential threat to the independence of one member of my audit team as his wife is a school governor at a Council run school. I ensured that the individual was not involved in any audit work relating to the school. I discussed the threat with the Director of Finance and Business Services and Head of Finance. By applying this safeguard I was able to reduce this threat to an acceptably low level.

I ask you to confirm to me that you have approved the accounts and agree the letter of representation

I ask the Audit and Governance Committee to:

- consider the matters raised in this report before approving the financial statements;
- take note of the adjustments to the financial statements and the unadjusted mis-statements which are set out in this report (Appendices 1 and 2);
- approve the letter of representation (appendix 3), provided alongside this report, on behalf of the Council before I issue my opinion and VFM conclusion

Financial statements

The Council's financial statements and annual governance statement are important means by which the Council accounts for its stewardship of public funds. As Council members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.

Opinion

Opinion on the financial statements

As at 23 September I have yet to complete my work in the following areas:

- the collection fund;
- cash flow and supporting notes including restatement of 2009/10 comparatives;
- asset revaluations including the valuation of Sir William Stanier school;
- checks to ensure that agreed changes to the financial statements have been included within the final version of the accounts; and
- my final review procedures.

I have also to complete my work on the Council's whole of government accounts return.

Subject to satisfactory completion of my work, I plan to issue an audit report including an unqualified opinion on the financial statements by 30 September 2011. If any matters arise when I am completing my work I will report this to you verbally at the Audit and Governance Committee meeting on 29 September.

Financial statements presented for audit

The Financial statements were prepared in line with the statutory deadline and presented for audit on 4 July as agreed at the June 2011 Audit & Governance Committee. The draft financial statements contained 2 material errors. I also identified 59 adjusted errors and disclosures and 5 other unadjusted items in the accounts. These are listed in appendices 1 and 2.

The overall impact of the amendments to the Balance sheet and Comprehensive Income and Expenditure Statements and comparatives are set out overleaf.

Balance Sheet

- Net increase in Plant Property and Equipment of £10.1m arising from:
 - a decrease in the impairment of Sir William Stanier school (impairment previously disclosed as £16.1m); and
 - and corrections to valuations of Knutsford and Poynton Leisure centres resulting in a decrease in valuation of £3.5m.
- Net increase in short-term creditors of £6.7m due to:
 - reclassification of £5m short term borrowings (now shown separately on the balance sheet);
 - reclassification of £1.2m NNDR receipts in advance (to show as a reduction in short term debtors); and
 - reclassification of £12.9m of unconditional grants as short-term creditors (previously included within useable reserves).
- Net decrease in usable reserves of £10.1m reflecting the
 - reclassification of unconditional grants as short-term creditors (£12.9m), and
 - an increase in the capital receipts reserve (£2.9m) to correct a number of presentational and numeric errors identified by my audit.
- Decrease in unusable reserves to reflect the
 - reduction in valuations of Poynton and Knutsford leisure centres (£3.5m) and
 - the reclassification of items previously included within the capital adjustment account which should have been shown capital receipts reserve (£2.9m).

None of the changes to the usable and unusable reserves impact on the Council's overall financial position. There will be a further adjustment to unusable reserves to reflect the late change in valuation of Sir William Stanier school.

Comprehensive Income & Expenditure Statement:

- Net increase in the surplus on provision of services of £12.8m comprising
 - £5.5m reduction in income allocated to services (reclassification of area based grant as non specific grant income)
 - £17.6m reduction in gross education service expenditure mainly due to the reversal of the impairment of Sir William Stanier School and reclassification of de-recognition of Foundation schools.

Changes to comparative disclosures as at 31 March 2010 and 1 April 2009

The most significant change relates to the reclassification of £12.9m, unconditional grants, as short-term creditors – previously disclosed in usable reserves.

Other changes to the financial statements

In addition to the above changes there have been a number of material and other changes to the amounts disclosed in the movements in reserves statement and to its corresponding note (note 5). These changes have no impact on the reported increase in the general fund balance of £2.3m.

I identified errors in a large number of the notes included in the draft accounts. Twenty of the fifty notes to the accounts have been changed. Some changes relate to the narrative others affect the figures themselves. The most significant of these are changes to

- Note 1 IFRS restatement;
- Note 5 Adjustments between accounting and funding basis;
- Note 12 movements;
- Note 25 Usable reserves;
- Note 26 Unusable reserves; and
- Note 38 related party transactions.

Narrative amendments were needed to ensure greater compliance with disclosure requirements, as set out in CIPFA's Statement of Recommended Practice, or to clarify the existing disclosures. Numeric changes were required:

- to correct mis-statements; or
- to ensure internal consistency between notes and the primary statements; or
- to ensure internal consistency between the notes themselves

Financial statements

Audit risks

I identified four key risks:

- Transition to International financial reporting standards;
- Implementation of new revenues and benefits system
- Upgrade of the main financial system; and
- Access to the general ledger.

The significant audit risks that I identified during my audit were reported to the Audit and Governance Committee previously. As noted in my update report in June 2011, I identified a further significant risk relating to controls over access to the Council's main financial system (ORACLE).

My risk assessment considers aspects of your accounting practices, accounting policies, accounting estimates and financial statements disclosures.

| Key audit risk | Findings |
|---|--|
| Transition to International financial reporting standards (IFRS) The transition to IFRS is complex requiring reconsideration of previous accounting disclosures and presenting a significant amount of new information in a new format. Failures to implement the requirements could lead to material misstatement in the financial statements. | <p>Despite slippage in the Council's timetable for the restatement of its April 2009 and March 2010 accounts, restated balance sheets were prepared by April 2011. I carried out a review of the principles and methodologies used to support the restatement. I identified one error in the accounting treatment of grants which I reported to officers</p> <p>Detailed testing of the 1 April 2009 and 31 March 2010 balance sheets was undertaken during my final accounts visit. One material mis-statement was identified in the classification of grants. This affected the 31 March 2010 and 31 March 2011 balance sheets and Income and Expenditure Statement for 2009/10. In addition the Council was unable to provide detailed comparatives as at 1 April 2009 for debtor and creditor balances.</p> <p>Apart from these two items I am satisfied that the statements have not been materially misstated due to the implementation of IFRS.</p> |

| Key audit risk | Findings |
|--|---|
| <p>Implementation of new revenues and benefits system</p> <p>Key audit risk The Council undertook a major systems implementation to replace its three revenues and benefits systems inherited from predecessor councils. These systems are used to administer council tax and NNDR billing as well as benefits payments. The implementation risk for the financial statements was that loss or corruption of transactional data migrated from old to new systems could lead to a material misstatement.</p> | <p>I reviewed the project and risk management arrangements put in place to deliver the implementation and provide assurance that standing and transactional data was migrated completely and accurately to new system.</p> <p>Officers put in place a wide range of procedures and controls to mitigate the risks around the upgrade, including:</p> <ul style="list-style-type: none"> • A project board with cross section of staff from revenues, benefits, finance, IT and business support which met regularly • Project plan and risk register • Training for relevant staff by qualified trainers • Testing of interfaces and new system prior to go-live • assurance arrangements • reconciliations of opening balances per Northgate to the legacy systems closing balances. <p>We reviewed these reconciliations. They did not identify any significant errors. As part of our general testing on controls testing, we checked the daily cash reconciliations between Northgate, Oracle general ledger and the Cash receipting system (Paris). No issues arose from this testing.</p> <p>At the year end differences were noted between reports generated by Northgate to support the NNDR3 grant claim and the report used to prepare the collection fund. Northgate have confirmed that these differences arose mainly due to the method of data conversion to the new system. They related to in year transactions recorded as brought forward items.</p> <p>As a result we have had to carry out extensive additional audit checks on the collection fund to ensure that it is not materially mis-stated. We also qualified the NNDR3 claim on the basis that the information used in the claim could not be reconciled to the financial statements.</p> <p>The additional work required was very labour intensive for both my audit team and officers. There are clearly issues in the operation and reporting of the Northgate system that need to be resolved in 2010/11. I return to these below.</p> |

Upgrade of the main financial system

Oracle is the core financial system used by both Cheshire East and Cheshire West and Chester councils. It includes payroll, payments, income, procurement, budgeting and financial management. The councils upgraded to a new version, Oracle R12, in January 2011. I identified some key audit risks:

- loss or corruption of data during upgrade;
- deterioration in the quality and accuracy of ledger reports;
- changes to or cessation of operation of existing financial controls; and
- backlog of data processing during downtime of Oracle Financials (potentially resulting in loss of information or errors in processing backlog).

As part of my IT risk assessment I reviewed the Council's controls over the upgrade. I found that change management was generally well controlled and there were no weaknesses compared to best practice. Officers put in place a wide range of procedures and controls to mitigate the risks around the upgrade, including:

- a Programme Board receiving weekly reports;
- appointing a test co-ordinator to manage end to end testing;
- four stages of user acceptance testing; and
- an Internal Audit review of the testing arrangements and the results of the tests.

I reviewed and tested these controls and found the risks reduced to an appropriately low level.

No issues arose from our testing of general ledger controls and checks on the roll forward of the opening balance sheet

| Key audit risk | Findings |
|---|---|
| <p>Access to the general ledger</p> <p>I found weaknesses with access security controls during my IT risk assessment that could impact on the integrity of the data within Oracle. The main weaknesses relate to non-council staff being able to access the general ledger without having effective controls in place. This creates a risk of unauthorised entries being made in the general ledger and other key financial systems. It could lead to a material misstatement of the Council's accounts.</p> | <p>Internal Audit carried out detailed testing which was designed to gain assurance that transactions undertaken by selected users were appropriately authorised and in accordance with Financial Procedure Rules.</p> <p>Based on my review of this testing, I concluded that the risk of unauthorised access to the general ledger has been reduced to an appropriately low level.</p> <p>I return to this issue later.</p> |

Financial statements

Weaknesses in internal control

I identified control weaknesses in the following areas:

- controls over access to the general ledger;
-

The Director of Finance and Business Services will make specific reference to these matters in her letter of representation. This letter is available as a separate document and will be discussed at the Audit and Governance Committee on 29 September 2011.

These weaknesses are only those I identified during the course of the audit that are relevant to preparing the financial statements. I am not expressing an opinion on the overall effectiveness of internal control.

| Description of weakness: | Potential effect: | Management action: |
|---|---|--|
| General ledger access controls There are weaknesses in the operation of controls over access rights to the main accounting system. | Increases the risk of unauthorised and inappropriate entries being made in the general ledger and other key financial systems. | Internal audit have undertaken a review of procedures and controls and performed detailed testing of selected users. A joint officer working group has been set up by the Council and Cheshire West & Chester Council to identify further actions required. |
| Northgate reporting There are differences between the cash receipts and refunds balances reported by Northgate for NNDR and Council Tax and those reported in Oracle. There are differences between Northgate reports used to support the NNDR3 claim and the collections fund | Closing arrears balances as reported by Northgate may be mis-stated. The information used to support the NNDR3 claim may be incorrect leading to under / over claim from the pool. | Management to review cumulative cash receipts and refunds posted to Northgate in 2010/11 to ensure that they reconcile in total to Oracle GL, Paris (cash receipting) and Oracle Accounts Payable. Management to review NNDR3 report and reconcile to Balance sheet report produced by Northgate. |

I will follow up each of these areas as part of my 2011/12 audit work.

Financial statements

Quality of your financial statements

There were clear improvements in accounts preparation process.

There is scope to improve the quality assurance arrangements and reduce the number of errors in the accounts presented for audit

The preparation of the Council's 2010/11 accounts was particularly challenging. In addition to the upgrade of the main financial ledger during the latter half of 2010/11 and the implementation of a new revenues and benefits financial system, officers also had to cope with the introduction of the new reporting requirements under IFRS.

During 2010/11 the Council increased the capacity of the finance team through the addition of two staff in late 2010. This increased capacity helped the Council to restate its opening balance sheets under IFRS by April 2011. In addition the number of material errors identified by audit has dropped from 5 (in 2009/10) to 2 this year. I also noted improvements in the quality of supporting working papers and in the finance team's response times to audit queries.

Despite this the accounts still contained a large number of significant errors. Many of these were identified through consistency checks carried out by my audit team. This indicates that the quality assurance processes around the preparation of the accounts could be more robust. A stronger quality assurance process should reduce the numbers of these types of error within the accounts presented for audit.

The response time by the finance team to audit queries was generally good but my team experienced delays in getting supporting information and explanations from other sections within the Council,

While much of the information provided in the accounts including the notes is required by guidance, there is scope to improve the format and layout of the accounts themselves to aid readers' understanding.

R1 Council to strengthen its accounts quality assurance processes to ensure that draft financial statements are free from internal inconsistencies and contain the final versions of supporting notes.

R2 Finance team to work with other service areas to improve their understanding of accounts preparation and audit timetables and ensure that they deal with requests for information in a timely manner

Annual Governance Statement

The Authority's Annual Governance Statement meets CIPFA's requirements. The disclosures within it are consistent with the information we are aware of from our audit of the financial statements and other work.

Letter of representation

Before I issue my opinion, auditing standards require me to ask you and management for written representations about your financial statements and governance arrangements. The draft letter of representation is available as a separate document.

Value for money

I am required to conclude whether the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money conclusion.

Value for money

The Council has proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against two criteria specified by the Audit Commission. My findings and conclusion on each of the two areas specified in 2010/11 are below. I intend to issue an unqualified conclusion stating that the Council has proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

| Criteria | Findings |
|---|--|
| 1. Financial resilience The organisation has proper arrangements in place to secure financial resilience. Focus for 2010/11: The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future. | <p>The Council has effective arrangements for financial governance, planning and control. During 2010/11 the Council continued to develop its detailed systems and processes to manage its financial risks and opportunities. The Council's annual budget is based on corporate priorities set out in its Sustainable Community strategy and Corporate Plan which were both revised during the year.</p> <p>For 2010/11 the Council included the key elements of its medium term financial plan in its annual budget report. This included a savings target of £7.7m</p> <p>In July 2010, the business planning cycle for 2011/14 was launched. It aimed to produce a single integrated business plan and budget setting out how the Council would achieve its objectives both in budgetary and service delivery terms. The launch event set out the key financial assumptions and challenges facing the Council as well as a timetable for delivery and an outline of available resources and support mechanisms. An efficiency group, comprising officers and members, was established to lead the process and to provide challenge around the Council's transformation programme. The Council's approach to transformation included a review the existing programme looking for opportunities to redesign services and realise efficiencies.</p> <p>During the year the Council experienced significant budget pressures particularly in children's and adults services. In year monitoring of the 2010/11 budget was led by the corporate management team. This enabled the early identification of in</p> |

year financial pressures and establishment of remedial plans to deliver additional savings. By quarter three, the Council faced net underlying budget pressures of £19.2m mitigated by proposed remedial actions of £10.5m, and requests for supplementary funding of £1.0m, leaving an overall forecast overspend of £7.7m at the year end (3.6% of the net service budget).

At the year end, the net service overspend was £9.5m before taking account of under spends in other areas of £7.3. These included central contingencies, corporate services and use of ear marked reserves. Smaller overspends were reported by the Children's and Places teams. The main area of overspend was in adult services totalling £8.8m despite delivering savings of £3.7m.

The Council planned to repay £4.3m to general fund reserves during the year. This fell to £2.3m at the year end mainly because of the net service overspend. The reported closing balance on the general fund is £12.3m. While this is lower than originally planned and does not fully cover the Council's assessed financial risk of £14.7m, it is £5.8m more than assumed when setting the 2011/12 budget. Latest financial projections have highlighted continuing budget pressures with an estimated funding gap of £8.2m for 2012/13. The first quarter finance report for 2011/12 reported a projected net service overspend of £5.7m. Directorate budgets for the year already include a requirement for significant levels of savings. Further remedial actions will be necessary to deliver those savings and manage in year pressures.

In August 2011 the Council published its new Business Planning process for 2012 – 2015. This will bring together the annual budget and corporate planning rounds. It projects a £29.4m shortfall over the three years. The plan is supported by the new performance management system (introduced in 2010/11) which the Council intends will provide fully integrated financial and performance information for monthly monitoring. The Council has also reviewed and updated its strategies for delivering value for money; income and charging, and reserves. These strategies underpin the business planning cycle.

Work is in progress to further improve the Council's performance management system by developing local performance indicators at service and corporate levels. Opportunities to strengthen Members' roles in financial scrutiny and challenge are being reviewed and training provided.

2. Securing economy efficiency and effectiveness

The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

Focus for 2010/11:

The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

The Council has effective arrangements in place for prioritising resources and improving efficiency and productivity.

The Council is prioritising its resources within tighter budgets by achieving cost reductions and by improving efficiency and productivity through the budget setting and challenge process. In July 2010 the Council published its revised sustainable community strategy setting out its overall vision and priorities. The Budget challenge round for 2010/11 sought to challenge services over cost and delivery and set out the following proposals:

- additional £5.4m for safeguarding in Children and Families;
- transformation programmes in Children and Families and Adult services to realise up to £3.6m and £4m in efficiencies respectively;
- Changing working practices in Health & Well Being to reduce the level of direct involvement in service delivery with planned savings of up to £2.5m over three years;
- Allocating additional £1.2m to Waste Minimisation and Recycling to recognise rising costs in delivering the service.

These changes were supported by an investment or savings proposal. Each proposal set out the impact on service users and the wider community together with the revenue, capital and staffing implications.

In year financial pressures required further action to contain costs and find further savings of £10.5m. This was done through a combination of service redesign and short term measures. The corporate management team monitored the delivery of the savings targets on a weekly basis against remedial action plans drawn up by directorates. These processes were in place throughout the year. However it is difficult to clearly establish what proportion of the total savings delivered relates to efficiency projects as opposed to remedial action to manage the in year pressures. For 2011/12 the Council has implemented a traffic light system to report progress against agreed savings targets.

The Council can cite a number of examples where alternative approaches to service delivery have already been implemented or are planned. The Council makes extensive use of shared service arrangements for back office functions. During 2010/11 the People and Places directorates made a number of changes in how services are delivered. For example, the waste collection service plans to improve recycling rates and rationalise existing collection services (taken to Cabinet in March 2011). The Council estimates this proposal will deliver over £1m in savings (of which £726,000 is included in the 2011/12 budget). Within Adult services, a number of initiatives have been implemented to try and reduce costs.

These include:

- changing working practices;
- rationalisation of assets; and
- redesign of services – for example the introduction of the EMpower card which is intended to reduce the level of back office support required.

In preparation for the 2010/11 business planning round, Children's Services carried out a value for money assessment to help its understanding of the comparative efficiency and effectiveness of its services. Using the CIPFA vfm toolkit supported by benchmarking and information from other councils, the service was able to build up a picture of its relative costs and performance. This identified areas of low and average performance as well as high costs. This approach is formalised in the Council's VFM strategy which outlines sources of data and analyses to be performed at both service and corporate levels. The Council has already identified gaps in available benchmarking information and is looking to develop contact with groups which will enable detailed service specific benchmarking.

In August this year OFSTED reported on its inspection of the Council's Looked after Children and Safeguarding services. Overall, these services were assessed as adequate. The inspection team recognised the additional financial investment made by the Council. Action taken has resulted in improved performance and practice in most safeguarding areas, which are now adequate or better. Inspectors found strong leadership and strategic planning, across the partnership, securing commitment and resources to enable safeguarding services to be reshaped and improved. The Director of Children's services, appointed in 2010, provides strong leadership, setting a clear, risk based approach to prioritising improvements required to children's social care services and to safeguarding services. As a result, significant improvements have been achieved, such as the effective restructuring of children's social care services, with improvements in many areas of performance from what was a very low baseline.

Report by exception

The Audit Commission requires me to report by exception where significant matters come to my attention, which I consider to be relevant to proper arrangements to secure economy, efficiency and effectiveness in your use of resources.

There are no matters that I wish to draw to your attention.

Appendix 1 – Amendments to the draft financial statements

I identified the following misstatements during my audit and management have adjusted the financial statements. I bring them to your attention to aid you in fulfilling your governance responsibilities.

| | | Comprehensive income and expenditure statement | | Balance sheet | |
|--|---|--|----------|---------------|----------|
| Adjusted misstatement | Nature of adjustment | Dr £000s | Cr £000s | Dr £000s | Cr £000s |
| Adjustments between first and second versions of the financial statements | | | | | |
| Comprehensive I&E | | | | | |
| Net cost of services | Increase in net expenditure of £3,720k (8 non-trivial errors) | 3,720 | | | |
| Other operating expenditure | Increase in expenditure of £7,038k | 7,038 | | | |
| Financing and Investment I&E | Reduction in expenditure of £238k | | 238 | | |
| Taxation and non-specific grant income | Increase of £4,786k 2009/10 comparative has reduced by £12,238k due to a change in classification of a grant | | 4,768 | | |
| Surplus on revaluation of non | Increase of £593k | | 593 | | |

| | | Comprehensive income and expenditure statement | | Balance sheet | |
|---|--|--|-----|---------------|-------|
| current assets | 2009/10 comparative reduced by £6,097k | | | | |
| Surplus/deficit on revaluation of available for sale assets | A deficit of £617k has changed to a surplus of £24k | | 642 | | |
| Balance sheet | | | | | |
| Property, plant & equipment | Value reduced by £3,488k due to the revaluation of Knutsford and Poynton Schools and related leisure centres. | | | | 3,488 |
| Short term debtors | Reduced £1,219k – NNDR receipts in advance shown as short term creditors rather than netted off the NNDR debtor. | | | -1219 | |
| Short term borrowing | Adjustment to show borrowing due within one year as short term borrowing rather than short term creditor | | | 5,021 | 5021 |
| Short term creditors | Net increase of £6,759k, made up of the opposite entries to short term debtors and short term borrowing above, and an increase of £12,999k due to the incorrect treatment of a grants | | | | 6759 |
| Usable reserves | A net reduction of £10,105k made up of the £12,999 above, offset by an increase in the Capital Receipts reserve (£2,894k) due to a change in the funding of the former Royal Mail site | | | 10105 | |

| | | Comprehensive income and expenditure statement | | Balance sheet | |
|---|--|--|--|---------------|-------|
| Unusable reserves | A reduction of £6,382k made up of the opposite entry to £3,488k reduction in asset values and a decrease in the Capital Adjustment Account as a result of 8 amendments ranging in value from £16.7m to £1.3m | | | 6,382 | |
| Movement in Reserves | | | | | |
| Movement in Reserves statement – General Fund | Overall impact of 10 non-trivial adjustments on the Authority's Usable Reserve | | | | 2,410 |
| Movement in Reserves Statement – Capital Receipts Reserve | To adjust for the change in funding basis for the purchase of the Royal Mail Site | | | 2,894 | |
| Movement in Reserves Statement – Capital Grants Unapplied | To adjust for a grant incorrectly placed in the unapplied account. | | | | 761 |
| Movement in Reserves – Unusable Reserves | Overall impact of 11 non-trivial adjustments on the Authority's Unusable reserves totals. | | | | 7,013 |
| Unusable Reserves – Capital Adjustment Account | Overall impact of 7 non-trivial and one material amendment to the CAA. Material £16.7m amendment was to the amounts written off to the CAA on disposal of non-current assets. | | | 2,894 | |
| Unusable Reserves – Revaluation Reserve | To adjust the reserve for the downward revaluation of assets figures to ensure consistency with the PPE note 12. | | | 3,488 | |

| | | Comprehensive income and expenditure statement | Balance sheet |
|--|--|---|---------------|
| Usable Reserves – Capital Receipts Reserve | To adjust the change in reported funding basis for the purchase of the Royal Mail Site | | 2,894 |
| Usable Reserves – Capital Grants unapplied Account | To adjust for the grant incorrectly placed in the unapplied account. | | 12,999 |

Appendix 2 – Unadjusted misstatements to the financial statements

I identified the following misstatements during my audit, [including uncorrected misstatements from earlier years,] but management has not adjusted the financial statements. I bring them to your attention to help you in fulfilling your governance responsibilities and ask you to correct these misstatements.

If you decide not to amend, please tell me why in the representation letter. If you believe the effect of the uncorrected errors, individually and collectively, is immaterial, please reflect this in the representation letter. Please attach a schedule of the uncorrected errors to the representation letter.

| | | Comprehensive income and expenditure statement | | Balance sheet | |
|-----------------------------|---|--|----------|--------------------|----------|
| Unadjusted misstatement | Nature of required adjustment | Dr £000s | Cr £000s | Dr £000s | Cr £000s |
| 2009/10 | | | | | |
| Property, plant & equipment | Depreciation charged in error on surplus assets and investment properties | | 110 | 110 | |
| | Community assets revalued in error | | | 172 | 172 |
| 2010/11 | | | | | |
| Property, plant & equipment | The Council should include the value | | | Not yet quantified | |

| | | Comprehensive income and expenditure statement | Balance sheet |
|---|---|---|------------------------|
| | of Voluntary Aided schools playing fields within PPE. There are currently no valuations available of relevant playing fields. This will be reviewed in 2011/12. | | |
| | Middlewich Victoria Buildings and Sandbach shop units have been reclassified as investment properties in error – they should be classified within Other Land & Buildings as they are not held solely for rental/capital appreciation purposes. | | 339 |
| Property, plant & equipment additions – Note 12 | Expenditure in 2010/11 on Brine Leas School has been included within OLB and VPE in Note 12 in error (£2,186k and £371k respectively) and written off as capital not adding value. As the school is not an asset of the Council, any capital expenditure should be treated as REFCUS. | | Disclosure issues only |

Appendix 3 - Draft Letter of Representation

Judith Tench
District Auditor
Audit Commission
2nd Floor, Aspinall House
Aspinall Close
Middlebrook, Horwich
Bolton, BL6 6QQ

Cheshire East Borough Council - Audit for the year ended 31 March 2011

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Cheshire East Borough Council, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2011.

Compliance with the statutory authorities

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Council for the completeness of the information provided to you, and for making accurate representations to you.

Uncorrected misstatements

The effects of uncorrected financial statements misstatements summarised in the attached schedule are not material to the financial statements, either individually or in aggregate.

Supporting records

All relevant information and access to persons within the Council has been made available to you for the purpose of your audit, and all the transactions undertaken by the Council have been properly reflected and recorded in the financial statements.

Irregularities

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

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

Law, regulations, contractual arrangements and codes of practice

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Council has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates including fair values

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

Specific representations:

I confirm that:

- all unfunded liabilities e.g. discretionary added years awarded to staff in the LGPS and discretionary benefits awarded to teachers under the Teachers Pension scheme are included within the IAS 19 liability figures, and
- there have been no changes that would affect the split of pension fund liabilities previously notified to the pension fund actuary.
- there have been no difficulties in collecting 2010/11 NNDR and Council tax arrears during 2011/12 that would indicate that these balances were mis-stated at 31 March 2011.

Related party transactions

I confirm that I have disclosed the identity of Cheshire East Borough Council's related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirement of the framework.

Subsequent events

All events subsequent to the date of the financial statements, which would require additional adjustment or disclosure in the financial statements, have been adjusted or disclosed.

Signed on behalf of Cheshire East Borough Council

I confirm that the this letter has been discussed and agreed by the Audit & Governance Committee on behalf of the Council on 29 September 2011.

Signed

Name: Lisa Quinn

Position

Date

Appendix 4 - Draft Audit Opinion

Independent auditor's report to Members of Cheshire East Borough Council

Opinion on the Authority accounting statements

I have audited the accounting statements of Cheshire East Borough Council for the year ended 31 March 2011 under the Audit Commission Act 1998. The accounting statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, and Collection Fund and the related notes. These accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of Cheshire East Borough Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Director of Resources and auditor

As explained more fully in the Statement of the Director of Resource's Responsibilities, the Director of Resources is responsible for the preparation of the Authority's Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom. My responsibility is to audit the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements sufficient to give reasonable assurance that the accounting statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Authority; and the overall presentation of the accounting statements. I read all the information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on accounting statements

In my opinion the accounting statements:

- give a true and fair view of the state of Cheshire East's affairs as at 31 March 2011 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the accounting statements are prepared is consistent with the accounting statements.

Matters on which I report by exception

I have nothing to report in respect of the governance statement on which I report to you if, in my opinion the governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007.

Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

Auditor's responsibilities

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Basis of conclusion

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2010, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2011.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2010, I am satisfied that, in all significant respects, Cheshire East Borough Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2011.

Certificate

I certify that I have completed the audit of the accounts of Cheshire East Borough Council in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

Judith Tench
Officer of the Audit Commission

September 2011

Audit Commission, 2nd Floor, Aspinall House, Aspinall Close, Middlebrook, Horwich, Bolton, BL6 6QQ

Appendix 5 – Glossary

Annual governance statement

A statement of internal control prepared by an audited body and published with the financial statements.

Audit closure certificate

A certificate that I have completed the audit following statutory requirements. This marks the point when I have completed my responsibilities for the audit of the period covered by the financial statements.

Audit opinion

On completion of the audit of the financial statements, I must give my opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Opinion

If I agree that the financial statements give a true and fair view, I issue an unqualified opinion. I issue a qualified opinion if:

- I find the statements do not give a true and fair view; or
- I cannot confirm that the statements give a true and fair view.

Materiality and significance

The Auditing Practices Board (APB) defines this concept as ‘an expression of the relative significance or importance of a particular matter for the financial statements as a whole. A matter is material if its omission would reasonably influence users of the financial statements, such as the addressees of the auditor’s report; also a misstatement is material if it would have a similar influence. Materiality may also be considered for any individual primary statement within the financial statements or of individual items included in them. We cannot define materiality mathematically, as it has both numerical and non-numerical aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

'Significance' applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

Weaknesses in internal control

A weakness in internal control exists when:

- a control is designed, set up or used in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements quickly; or
- a control necessary to prevent, or detect and correct, misstatements in the financial statements quickly is missing.

An important weakness in internal control is a weakness, or a combination of weaknesses that, in my professional judgement, are important enough that I should report them to you.

Value for money conclusion

The auditor's conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources based on criteria specified by the Audit Commission.

The Code of Audit Practice defines proper arrangements as corporate performance management and financial management arrangements that form a key part of the system of internal control. These comprise the arrangements for:

- planning finances effectively to deliver strategic priorities and secure sound financial health;
- having a sound understanding of costs and performance and achieving efficiencies in activities;
- reliable and timely financial reporting that meets the needs of internal users, stakeholders and local people;
- commissioning and buying quality services and supplies that are tailored to local needs and deliver sustainable outcomes and value for money;
- producing relevant and reliable data and information to support decision making and manage performance;
- promoting and displaying the principles and values of good governance;
- managing risks and maintaining a sound system of internal control;
- making effective use of natural resources;
- managing assets effectively to help deliver strategic priorities and service needs; and
- planning, organising and developing the workforce effectively to support the achievement of strategic priorities.

If I find that the audited body had adequate arrangements, I issue an unqualified conclusion. If I find that it did not, I issue a qualified conclusion.

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0844 798 7070

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- any director/member or officer in their individual capacity; or
- any third party.

