

Annual Audit Letter

May 2006



Annual Audit and Inspection Letter

Stevenage Borough Council

Audit 2004-2005

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Key messages

- 1 The key messages arising from our audit and inspection work are outlined below.

Council performance

- 2 The Council has strengthened its management capacity and performance management framework to deliver the outcomes required in its CPA improvement plan.
- 3 There is stronger leadership from councillors and senior managers on the improvement agenda and the approach to citizen and user focus is improving. Community leadership and partnership remains strength for the Council, evident through providing a wide range of well regarded statutory and discretionary services.
- 4 However, the quality of services is mixed. Performance indicators for 2004/05 illustrate that 51 per cent of indicators were above average compared with 53 per cent for 2003/04; furthermore only 47 per cent of indicators have improved since 2002/03. There is, however, evidence from the Council's own un-audited performance monitoring for 2005/06 of recent improvements.
- 5 We undertook a use of resources assessment for the Council covering a review of arrangements for financial reporting, financial management, financial standing, internal control and value for money. Across the board, the Council are performing adequately with areas of good practice. Our feedback to the Council has identified some improvement opportunities and it is encouraging to note that the senior management team have already developed an action plan to address these areas.
- 6 The Council's best value performance plan (BVPP) complied in all material respects with legislation and statutory guidance and an unqualified opinion was issued. The Council has established and strengthened robust performance monitoring arrangements for key performance indicators which is contributing to identifying and taking corrective action for areas of poor performance.

The accounts

- 7 To date; we have been unable to issue an opinion on the Council's accounts for financial year ended 31 March 2005 as the Council are considering an application for a capitalisation direction from the ODPM in respect of the accounting treatment for a repayment of £2.6 million English Partnership debt in 2000/2001. This arose following our review of the Council's calculation of the capital financing requirement for the financial year ended 31 March 2005. We are considering the actions being taken by the Council; in liaison with consultants employed by Sector, to resolve the accounting treatment of this liability before forming a view on the nature and timing of our audit opinion. We will report any further matters to those charged with governance prior to issuing our opinion.

- 8 We completed our audit of the Council's financial statements by 31 October 2005 and; with the exception of the outstanding issue above, agreed adjustments to the financial statements and reported no other significant matters to those charged with governance.
- 9 2004/05 has been a challenging year for the Council with the implementation of a new suite of financial systems, resource requirements to address fire at Harrow Court in February 2005 and the advanced requirements for publication of financial statements. Whilst we recognise that the Council responded positively to the challenges and prepared draft financial statements within the publication timetable, there remains scope to improve the quality of working papers submitted for audit which were noted during our audit and as part of the Council's use of resources assessment. The Council have developed a project management process to address these issues and meet the advanced publication timetable for 2005/06 financial statements.

Financial standing

- 10 The Council continues to retain an adequate level of general fund balances at £11.3 million as reported in last year's letter. During the past year, the Council have strengthened financial management arrangements through an annual budget review process and medium term financial strategy which are contributing towards ensuring a sustainable financial position, annual balanced budgets and retention of a prudent level of reserves and balances.
- 11 The revisions to the budget setting process involve difficult financial decisions for the Council, particularly in shifting resources out of non-priority areas and in correcting historical under spending. However, there is evidence of a clear commitment at all levels to preserve financial standing and ensure financial planning aligns with strategic aims and objectives of the Council.

Systems of internal financial control

- 12 Aside from our use of resources assessment findings, we have not identified any further significant weaknesses in the overall control framework.

Standards of financial conduct and the prevention and detection of fraud and corruption

- 13 Aside from our use of resources assessment findings, we have not identified any further significant weaknesses in your arrangements for maintaining financial conduct and to prevent and detect fraud and corruption.

Legality of transactions

- 14 Overall, we concluded that the Council's arrangements for ensuring the legality of transactions continue to be appropriate.

Action needed by the Council

- Continue to address the improvement plan objectives for the Council, particularly in demonstrating improved service delivery through performance indicators; strengthening arrangements for allocating resources to priority areas and evidencing that learning is shared systematically.
- Develop the project management approach for closedown of 2005/06 financial statements, ensuring sufficient ownership and accountability throughout the process by members and officers.
- Enhance the effectiveness of internal control by developing an assurance framework for the production of the Statement on Internal Control (SIC) and establishing an Audit Committee which is independent of executive and scrutiny.
- Ensure that the Council's future plans directly align with ongoing financial planning to preserve the actions being taken to preserve financial position and retain balance budgets, including a prudent level of reserves and balances.
- Introduce unit cost comparative data as part of key budget setting and performance management processes to improve the understanding of value for money from Council's services.
- Monitor progress implementing all of the improvement actions arising from the Council's use of resources assessment.

Council performance

The Council has strengthened its management capacity and performance management framework to deliver the outcomes required in its CPA improvement plan.

There is stronger leadership from councillors and senior managers on the improvement agenda and the approach to citizen and user focus is improving. Community leadership and partnership remains strength for the Council, evident through providing a wide range of well regarded statutory and discretionary services.

However, the quality of services is mixed. Performance indicators for 2004/05 illustrate that 51 per cent of indicators were above average compared with 53 per cent for 2003/04; furthermore only 47 per cent of indicators have improved since 2002/03. There is, however, evidence from the Council's own unaudited performance monitoring for 2005/06 of recent improvements.

We undertook a use of resources assessment for the Council covering a review of arrangements for financial reporting, financial management, financial standing, internal control and value for money. Across the board, the Council are performing adequately with areas of good practice. Our feedback to the Council has identified some improvement opportunities and it is encouraging to note that the senior management team have already developed an action plan to address these areas.

The Council's best value performance plan (BVPP) complied in all material respects with legislation and statutory guidance and an unqualified opinion was issued. The Council has established and strengthened robust performance monitoring arrangements for key performance indicators which is contributing to identifying and taking corrective action for areas of poor performance.

Direction of travel report

- 15 The Council was assessed as good in the Comprehensive Performance Assessment carried out in 2004. Since the assessment, the Council has clarified and simplified its ambitions and priorities for 2005/06, following a community conference in July 2004 which are:
- community leadership;
 - the regeneration of Stevenage;
 - good housing for all; and
 - transformed council services.

- 16 Underneath these ambitions sit a number of specific priorities and there is effective progress monitoring through the Council's improvement plan and service plans. Ambitions and priorities also inform budget setting and service planning and are now reviewed annually, taking into account public consultation. Some amendments were made for 2006/07, in particular the developments in medium term financial planning and budget savings review exercise, together with corporate business strategy (CBS) to identify resources which can be shifted out of non-priority areas. The Council do recognise that this process could be strengthened further. One area for example, is to challenge service design and consider alternative means of delivery which the Council is taking forward by developing a competitions strategy.
- 17 There is effective financial management. Officers and members describe the framework as 'fit for purpose and there is confidence in the quality of both financial and performance information. There is good overall control of the budgetary position although there have been significant under spends in both revenue and capital budgets in recent years. The Council has now tightened control to prevent similar outcomes in future. The role of the corporate capital review group has been strengthened and a five year capital strategy developed. However, there is not yet a complete understanding of the value for money that individual services provide. In particular, members do not receive information as to the relative cost of services.
- 18 The Council are developing arrangements for delivering clear ambitions and priorities. For example, in promoting environmental well being the Council have published an environmental management policy statement which is supported by an action plan. In contributing to building a fair and inclusive society, the Council has completed year one of a three year programme of impact assessments to assess how policies and services are supporting this ambition.
- 19 Mechanisms are in place to ensure continuing focus on issues that reflect users' needs and expectations, supported by a two year communications strategy programme. Progress has been made during our reviews of diversity, user focus and race equality at the Council. For example, an equality and diversity strategy has been launched and an equalities and diversity officer has been appointed. There is more effective consultation on priorities, through area committees, consultation exercises, the council's newssheet, and the media.
- 20 The Council has introduced a basket of key success measures to measure progress on the priorities under each ambition and these are tracked using survey results and performance indicators. A set of corporate health indicators was also developed in August 2005. Outcomes of major projects and programmes and the CPA improvement plan are monitored through the Programme Management Board (PMB) as well as there being a clear link to ambitions and priorities in the CBS. The Council's 'Forward Plan' focuses on prioritisation and all bids for revenue or capital funding are explicitly linked to corporate ambitions and given a priority ranking.

- 21 Our CPA assessment noted improvements required in the housing service. Focus on housing services has been restored with the development of a housing improvement programme aiming to achieve a two star service by October 2007 and specific enhancements to management capacity within the housing service. Specific responses to rent collection and tenant satisfaction performance have been addressed, including the agreement of a 'voids lettable standard' and a dedicated voids team being established to improve turnaround times for empty properties.
- 22 One key aspect for achieving the decent homes standard has been that following public consultation the Council will form an Arms Length Management Organisation (ALMO) by October 2006. This is considered by the Council to be the most viable and deliverable option to provide funding for investment in council housing to meet decent homes standard by 2010. The Council is in the process of establishing a shadow ALMO and board during March/April 2006 and are submitting bids to the ODPM.
- 23 The Council shows strong community leadership and a commitment to partnership working. There is a strong Crime and Disorder Reduction Partnership (CDRP) and partnerships with neighbouring councils. The Chief Executive is leading the multi-agency group developing targets for the 'Safer and Stronger' block of Local Area Agreements, to access increased government funding for shared local priorities. There are service level agreements with key voluntary sector providers such as the CVS and the CAB.
- 24 Scrutiny continues to develop and will be enhanced further by a member development strategy providing focussed training. There is a new chairman and a new work plan has been developed which has clearer links to ambitions and priorities. Members of the performance, priorities and improvement group (PPIG) have a role to manage and monitor the Council's performance.
- 25 The Council has an effective organisational structure and good working relations between officers and councillors. During 2005 the Chief Executive reduced the senior management team by one and established strategic directors with corporate rather than operational responsibility. The strategic directors are driving the delivery of the council's ambitions and target areas for improvement such as crime and disorder and performance management.
- 26 There is a commitment to investing in people. An outline of a performance management programme has been agreed and will focus on people and leadership. Projects will include the introduction of a competency framework, 360 degree appraisal, and the acquisition of a performance measures software system. This is supported by performance appraisal systems which are valued by staff and which focus on target setting and training needs. The Council has been re-awarded Investors in People (IIP) accreditation. Sickness levels are improving, according to unaudited data, where the Council has responded by introducing a revised sickness management policy, providing training and support for managers and increasing monitoring by SMB and PPIG. Average day's sickness has fallen from 11.4 to approximately ten days during 2005/06.

- 27 An improved performance management framework has been established to support identified priorities. There are clear links between priorities, the MTFs and service planning. Service plans for 2006/07 have a three year horizon and include value for money considerations. SMB is taking a leading role and has introduced BVPI clinics to address 'hot spots' of poor performance. Targets and milestones have been identified for all projects under each priority and these are monitored through the Programme management Board (PMB) which includes officers of SMB but with separate terms of reference.
- 28 The Council delivers a mixed quality of services. Performance indicators for 2004/05 show that 51 per cent of indicators were above average but 49 per cent were below average. Furthermore only 47 per cent of indicators have improved since 2002/03. The Council's own unaudited performance monitoring for 2005/06 suggests stronger performance with over 60 per cent of indicators above average.
- 29 The Council has not performed consistently well in key priority areas where weaknesses were identified during CPA including planning performance, processing of benefit applications and collection of rent/ tenant satisfaction. However, the performance monitoring arrangements developed by the Council; via BVPI clinics have resulted in improvements, particularly during 2005/06 where Stevenage is no longer identified as a planning standards authority and processing of benefit applications during the last quarter is beginning to improve. The Council's performance in processing benefit applications and collection of council tax need to be set in the context of the implementation of new systems during 2004/05 which contributed directly to the deterioration in performance.
- 30 Customer satisfaction with the Council's service is improving, primarily as a result of introducing the customer Service centre (CSC) as part of a major change in the way service will be delivered. The CSC has served a total of 541,250 customers since it opened in Aug 2003, with over 23,000 customers served in December 2005. The 2005 residents' survey reflects improved levels of customer care with 81 per cent of residents judging staff helpful (compared to 78 per cent in 2001) and 74 per cent of residents found staff efficient (compared to 69 per cent in 2001). The CSC programme has been and will be expanded further covering other service areas such as repairs appointment, environment services and revenues.
- 31 A contributory factor to improved customer satisfaction is the level of internal and external communications. There a number of mechanisms which have proved effective including the council magazine, the web site, specific consultation exercises on play and housing and the use of area committees. For staff there is 'The Link' magazine and cascade briefings.

- 32** The Council continues to have strong arrangements in place for securing future investment in realising its ambitions, for example:
- town centre public realm improvements have been completed and plans for town centre regeneration are in development, including ongoing negotiations with a developers; and
 - obtaining agreement from ODPM for the Stevenage West development as part of the regeneration of Stevenage.
- 33** Learning is still not shared systematically across the organisation but mechanisms are developing. The 'Top Team' awards have been re-launched to focus on 'service beyond compare' but it is too early to judge its impact. The Council has developed arrangements for learning by creating a 'Sharing Best Practice' area has been set up on the intranet where staff can record and share examples of their own good practice. The Council has also established 'Learning Link' from January 2006, a series of lunchtime seminars that anyone can attend. In addition, sharing learning is specifically included in the new Performance Management Programme.
- 34** The Council has some key plans and strategies in place that together should establish improved services and a more effective corporate structure. These include:
- corporate business strategy;
 - CPA improvement plan;
 - improved performance management and service planning frameworks;
 - medium term financial strategy and capital programme;
 - Local Development Framework;
 - a review of the Consultation Strategy;
 - a housing improvement plan with a view to setting up ALMO;
 - Equality and Diversity Strategy; and
 - Play Policy and Strategy.
- 35** Continuing focus on performance improvement, sound financial management, business process re-engineering and the delivery of these plans will be key in delivering improved services for the people of Stevenage.

Other performance work

- 36 Under the Local Government Act 1999, specific local government bodies are required to comply with the general duty of best value, which is defined as making arrangements to secure continuous improvement in the way in which their functions are exercised, having regard to a combination of economy, efficient and effectiveness.
- 37 The Council is required to publish annually a BVPP which summarises its assessment of performance and its plans in relation to best value. The Council is responsible for preparing the BVPP and for the information and assessment that are set out within it and the assumptions and estimates on which they are based. It is also responsible for putting in place appropriate performance management and internal control systems, from which the information and assessments in the BVPP are derived.
- 38 Auditors are not required to form a view on the completeness or accuracy of the information or the realism and achievability of the assessments published by the audited body in its BVPP.
- 39 We concluded that the Council's 2005/06 BVPP contains all the key elements required by legislation and statutory guidance and we issued an unqualified opinion on 13 December 2005.
- 40 Our review of best value performance indicators (BVPI's) focussed predominantly on the arrangements that the Council has put in place to ensure accurate data is collected and published. In addition, we were required to assess whether the eight high risk indicators selected by the Audit Commission, including housing investment programme (HIP) indicators, were valid from the initial point of data entry to the final calculation of the indicator. This is in preparation for these indicators to be included within the District CPA framework.
- 41 As reported in last year's letter, the Council have developed and continue to strengthen performance monitoring arrangements via the role of the PPIG and through the implementation of BVPI clinics. There is a clear focus on challenging areas of poor performance and in assessing the accuracy and reliability of data quality and underlying systems for performance information. Internal Audit are used to support this process and provide assurances on overall quality control arrangements in place. Whilst we agreed with officers some minor amendments to the performance indicators reviewed for 2004/05, there were no significant weaknesses in underlying systems and processes to draw to the attention of members.

Accounts and governance

Audit of 2004/05 accounts

To date; we have been unable to issue an opinion on the Council's accounts for financial year ended 31 March 2005 as the Council are considering an application for a capitalisation direction from the ODPM in respect of the accounting treatment for a repayment of £2.6 million English Partnership debt in 2000/01. This arose following our review of the Council's calculation of the capital financing requirement for the financial year ended 31 March 2005. We are considering the actions being taken by the Council; in liaison with consultants employed by Sector, to resolve the accounting treatment of this liability before forming a view on the nature and timing of our audit opinion. We will report any further matters to those charged with governance prior to issuing our opinion.

We completed our audit of the Council's financial statements by 31 October 2005 and; with the exception of the outstanding issue above, agreed adjustments to the financial statements and reported no other significant matters to those charged with governance.

2004/05 has been a challenging year for the Council with the implementation of a new suite of financial systems, resource requirements to address fire at Harrow Court in February 2005 and the advanced requirements for publication of financial statements. Whilst we recognise that the Council responded positively to the challenges and prepared draft financial statements within the publication timetable, there remains scope to improve the quality of working papers submitted for audit which were noted during our audit and as part of the Council's use of resources assessment. The Council have developed a project management process to address these issues and meet the advanced publication timetable for 2005/06 financial statements.

Review of core processes

- 42 We examined the Council's core processes to assess the basis on which the accounts are prepared, namely:
- the main accounting system;
 - the budgetary control process; and
 - the year end closedown process.

- 43 During 2004/05, the Council implemented a new suite of financial systems. We reviewed the implementation of the systems and associated controls and found that robust arrangements were in place to secure the integrity, security and reliability of financial information from all principal and feeder systems. Our review covered the project management process, data conversion, access controls and system management arrangements. We reported our findings to the Council during 2004/05 and noted some minor improvement opportunities, though nothing of significance to report to members.
- 44 During conversion and implementation of systems, Council officers; as part of the closedown process for 2004/05 financial statements raised to our attention the system weaknesses apparent in the cash management module which were resulting in unbalanced bank reconciliation as at 31 March 2005. We were satisfied during liaison with council officers that robust actions were in place to resolve the differences and would be addressed during 2005/06.
- 45 Throughout the preparation of the 2004/05 financial statements and particularly during the closedown process, Council officers drew to our attention the risks arising from implementation of systems and the fire at Harrow Court in February 2005 on the capacity to address fully audit requirements for preparation of the financial statements and associated working papers. We agreed with officers a working arrangement for the supply of auditable working papers and were satisfied that the closedown timetable was sufficiently flexible and robust to ensure the earlier closedown timetable for draft accounts was achieved.
- 46 We concluded that there was generally a low risk of any of these processes leading to a material misstatement in the financial statements. However, we did note some areas for further improvement, particularly in:
- updating budgetary control and monitoring procedures for budget holders; and
 - introducing a project management approach to the closedown timetable for preparation of accounts in future years.

Audit of financial statements

- 47 The draft financial statements were approved by the Council on 28 July 2005, in advance of the statutory deadline of 31 July 2005. This is a strong achievement for the Council in spite of challenges faced by implementation of new financial systems and capacity therein within the finance department.
- 48 We agreed a working arrangement with the Council on the provision of auditable working papers in light of the circumstances noted at paragraph 44 which would enable our audit of the accounts to progress. One example of these arrangements was that nominated officers responsible for aspects of the accounts were to be available to address audit queries and that working papers would be provided on request.

- 49 Whilst we were able to complete our audit by 31 October 2005 and address the queries arising with key officers, we experienced significant elapsed time covering our audit work in the following core areas:
- agreeing the trial balance to the financial statements in which updated versions of the trial balance were provided to us, vouched to the financial statements after we commenced our audit;
 - undertaking audit procedures on the Consolidated Revenue Account which were the responsibility of a contractor who subsequently left the Council prior to the commencement of our audit;
 - access to audit trails substantiating the component parts of debtors and creditors to enable more detailed audit procedures on existence and completeness; and
 - misplaced versions of the Council's working papers being supplied close to completion of our audit.
- 50 Whilst we acknowledged the Council's circumstances for 2004/05 and agreed satisfactory working arrangements, we felt that the issues arising during our audit were fundamental to the provision and access to auditable accounts and working papers at the start of our audit, particularly in enabling audit procedures to occur on material balances contained with the consolidated revenue account and balance sheet (ie debtors and creditors). We did report these matters on an ongoing basis to the Chief Financial Officer and were satisfied that sufficient ownership and actions were taken to address the issues raised which enabled our audit to complete by the statutory deadline.
- 51 For this reason, we could not assess the Council's arrangements as adequate set against the criteria used for the use of resources assessment on working papers, which reviews the adequacy of working papers to support the financial statements in full, including supporting notes and policies at the start of the audit. The Council did provide written representations responding to the issues raised set in the context of the use of resources assessment which were taken into consideration as part of our overall judgement.
- 52 In discussions with the Council, we are aware that arrangements are being secured to strengthen closedown arrangements for production of 2005/06 financial statements with a focus on improving the availability of working papers provided at the start of the audit. In particular, the Council have seconded an Interim Head of Finance with primary responsibility for the project managing the advanced closedown timetable whilst the current Head of Finance is engaged with the Council's ALMO implementation. We have been engaged on the Council's project management approach and have specified our requirements in the form of a working paper requirements checklist and liaison with officers on key technical/ audit issues being considered. We are satisfied; at this stage, that robust arrangements are in place to secure improvements in working papers and in meeting the advanced closure timetables for 2005/06.

Report to those with responsibility for governance in the Council

- 53** Our work on the financial statements was complete by 31 October 2005. Aside from the issues raised above regarding the availability of working papers, all audit queries were addressed and adjustments were agreed to the financial statements, none of which require reporting to members. We have liaised with officers on matters to take into consideration for preparing 2005/06 financial statements.
- 54** However, we have yet to issue our opinion on the financial statements as the Council are considering applying to the ODPM for a capitalisation direction to determine the appropriate accounting treatment for a £2.6 million repayment of English Partnership liability in 2000/01. This issue arose following the Council devoting resources to substantiating a reconciliation difference of £2.490 million in the Council's capital financing requirement as at 31 March 2005.
- 55** We are required by professional standards to report to those charged with governance, in this case to Councillor Taylor as Chair of the Statement of Accounts committee certain matters before we give an opinion on the financial statements.
- 56** We reported to Councillor Taylor on 27 October 2005 that we were unable to undertake satisfactory audit procedures to confirm that the Council's capital financing requirement is fairly stated or whether resolution of the reconciliation difference would not result in a material adjustment to the financial statements which may impact on the Council's General Fund balance or Housing Revenue Account balance.
- 57** Following discussions between Councillor Taylor, Chief Financial Officer and ourselves, we were provided with assurances on the robustness of the Council's actions to resolve the issues such that we agreed to keep open issuing the audit opinion on the Council's accounts pending satisfactory completion.
- 58** The Council since November 2005 devoted significant resources towards reconciling and substantiating the balances and engaged specialists from Sector to review the capital financing calculations. We received a report from the Council on 27 March 2006 which determined that the reconciliation difference of £2.490 million was substantially attributable to the accounting treatment of repayment of English Partnership debt of £2.6 million in 2000/01.
- 59** We reviewed the explanations provided for the accounting treatment of the liability which; in the view of the Council, supported the repayment of the debt through capital as opposed to revenue resources. We considered; in particular, the legality of this transaction against the requirements of Section 64 of the Local Government and Housing Act and Regulation 160 of the Local Authorities (Capital Finance) Regulations 1997 and Section 59 and 60 of the Local Government Housing Act 1989 and Regulation 23 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003.

- 60 In further discussions and correspondence with the Council, we raised concerns that the repayment of the English Partnership liability through capital resources did not meet the requirements of the legislation outlined above, as this liability referred to transferred debt as opposed to external borrowing. The Council is considering this viewpoint and continuing to take advice. It is our view that the Council should be repaying this liability through revenue resources and that appropriate accounting treatment would be to fund the repayment of £2.6 million liability through an adjustment to the Consolidated Revenue Account (CRA) in the 2004/05 financial statements.
- 61 In view of the significant financial consequences that such a transaction would have on the Council's general fund balance, overall financial standing and level of balances and reserves, the Council are now seeking to apply to the ODPM for a direction to enable this liability to be capitalised. The Council will need to satisfy the ODPM's criteria for capitalisation before a direction is issued. Should the Council receive a direction, adjustments will need to be made to the 2004/05 and 2005/06 financial statements as the determination can only be applied to the 2005/06 accounts.
- 62 In light of the current position and actions being taken by the Council, we are currently considering the nature and timing of our audit opinion on 2004/05 financial statements which remains open. When we are in a position to form our audit opinion, we will report any further matters to those charged with governance.

Financial standing

The Council continues to retain an adequate level of general fund balances at £11.3 million as reported in last year's letter. During the past year, the Council have strengthened financial management arrangements through an annual budget review process and medium term financial strategy which are contributing towards ensuring a sustainable financial position, annual balanced budgets and retention of a prudent level of reserves and balances.

The revisions to the budget setting process involve difficult financial decisions for the Council, particularly in shifting resources out of non-priority areas and in correcting historical under spending. However, there is evidence of a clear commitment at all levels to preserve financial standing and ensure financial planning aligns with strategic aims and objectives of the Council.

- 63 General fund net expenditure for the year was £10.529 million which was £1.605 million (13.23 per cent) below the original budget. The balance on the general fund balance reduced by £85,000 to £11.248 million. As explained in the foreword to the accounts, there were a number of departmental under and over spends that resulted in this position. The Council has retained a strong level of balances and reserves despite concerns noted in the medium term financial planning and strategy of projected utilisation of balances in 2004/05.

- 64 The housing revenue account (HRA) reported a surplus of £0.614 million. This is an improvement over the prior year deficit of £0.763 million and results in a balance carried forward of £2.238 million. The Council will need to be mindful of the implications of a future ALMO on the financial arrangements for the HRA and retention of balances and reserves. This is being considered by the Council in preparing bids for ODPM and in developing the 2006/07 capital forward plan.

Future financial position

- 65 The Council considered, on 15 February 2006, the current position in relation to the 2005/06 budget and proposed general fund budget for 2006/07 together with updates to the medium term financial strategy.
- 66 The Council are proposing a General Fund budget requirement of £13.641 million which involves a £1.729 million use of balances, reducing overall balances to £6.973 million. This excludes a £0.8 million set-aside from the Council to cover unforeseen expenditure/losses. As part of the Council's medium term financial strategy; and as reported in previous letters, the Council are projecting utilising reserves and balances in the medium term whilst also addressing the budget requirement/gap.
- 67 The Chief Financial Officer has reported to members on the robustness of estimates and adequacy of reserves as part of preparing the 2006/07 budget. Assurances have also been provided on the funding for the Council's capital programme up until 2010/11 and the adequacy of HRA balances/forward plan prior to the implementation of ALMO. The Council have strong capital programme arrangements and have addressed the requirements of the prudential code for capital finance.
- 68 The 2006/07 budget has been developed since June 2005 and takes into account the Council's updated and revised financial management arrangements, in particular its medium term financial strategy, appraisal of savings and growth targets as part of the fundamental budget reviews and the revised approach taken by the Council to address historical underspending. The budget has been subject to sufficient and appropriate consultation and scrutiny.
- 69 The Council's financial management arrangements are strengthening directly aligned to corporate plans and processes. The Council continues to take a number of actions, involving difficult decisions to dis-invest in non-priority areas linked to corporate aims and objectives and remain engaged to take forward procurement, e-government and partnership arrangement initiatives as alternative means of challenging service delivery and re-engineering business processes. The Council remain committed to delivering efficiency savings and demonstrating value for money. During 2004/05, the Council achieved £612,232 of efficiency savings of which 91 per cent was cashable.

- 70 There is clear commitment to financial stewardship and strong financial management at all levels within the Council and proactive initiatives have been taken, driven by the Chief Executive and Chief Financial Officer, to raise awareness of the medium to longer term risks to the Council's ongoing financial position and in developing robust and sound action plans to ensure there is ongoing financial capacity to deliver the Council's corporate aims and objectives.
- 71 In overall terms, the financial position of the Council remains soundly based. We reported that the Council were performing well for overall financial management during our use of resources assessment but noted adequate performance on financial standing.
- 72 The Council were assessed at adequate performance for financial standing as we were unable to be satisfied that the criteria was fully met for above average performance, relating specifically to ensuring spending remains within budget and without any significant unexpected overspends or underspends.
- 73 We reported in our 2003/04 letter cumulative under spends of £3.74 million since 2001/02 within the general fund budget and that the Council recognised the need to improve the reliability and robustness of its budget setting processes. This has been evidenced further by the developments made in the Council's medium term financial strategy and in the Council's review of annual budgets where references to new processes for correcting historical underspends have been acknowledged.
- 74 Whilst we note that the Council have secured improvements in arrangements for budget setting and monitoring during the past twelve months, we have yet to identify tangible outcomes for the medium to longer term financial position of the Council. The Council were keen to make representations in support of their use of resources self-assessment on the following factors relating to the cumulative under spends since 2001/02, particularly that:
- cumulative underspends reduce by £1.275 million when taking into account the probable estimates against actuals;
 - prudent provisions were set-a-side for legal costs associated with objections to the West of Stevenage development which have yet to be realised, accounting for £0.380 million of the underspends;
 - £0.240 million up to 2004/05 related to Local Development Framework which has been delayed as a result of agreement being sought by planning authorities; with expenditure incurred in 2005/06; and
 - additional investment income and successful rateable value appeals on Council operational buildings accounted for a further £0.628 million of the underspends.
- 75 These factors were formally reported to the Commission's regional director as a lodged appeal on the use of resources score for financial standing. Taking these representations into account, the Commission did not revise the themed score as there was not an overall impact on the use of resources score, and that our reported findings on the significance of the historical underspends and weaknesses in budget monitoring/setting remained accurate.

- 76 Aside from this criteria and the Council developing financial indicators for councillors (which is at the level for performing strongly), the Council achieved all of the other key lines of enquiry criteria for assessing financial standing. In developing arrangements for strengthening budgetary control/monitoring, the Council's revised processes are likely to correct the underlying reasons for historical underspends in the future which; provided tangible evidence is made available, will be taken into consideration for future use of resources assessments.

Use of resources judgements

- 77 The use of resources assessment focuses on financial management but draws linkages to wider strategic management of the Council. In particular, the assessments provides focus on how financial management is integrated with strategy and corporate management, supporting council priorities and delivering value for money. This assessment will be carried out annually, as part of each council's external audit. We anticipate in future the use of resources judgements will form part of the CPA framework.
- 78 We undertook our use of resources assessment during November and December 2005, reporting initial findings to SMB in December 2005 and officially with the themed scores in March 2006.
- 79 The Council invested considerable time and resources; including commitment at senior levels to prepare for the review, evidenced via a detailed self-assessment and documentary evidence being provided for the value for money and non value for money elements both prior to and during the on-site fieldwork. This process has provided a strong baseline for the Council to use in updating its self-assessment and preparing for future use of resources assessments.
- 80 In broad terms, we identified and fed back to the Council that significant developments have occurred in the past 18 months; particularly since the CPA inspection in April 2004, to strengthen financial and performance management arrangements, for example:
- fundamental budget reviews and revisions to medium term financial planning;
 - enhancements to the corporate capital review group which have challenged capital programme and asset management arrangements;
 - introduction of BVPI clinics to challenge areas of poor performance, notable successes including planning performance and processing of benefit claims;
 - implementation of a new suite of financial systems during 2004/05 which will streamline financial control and strengthen budgetary control/monitoring;
 - developments in risk management arrangements via corporate risk register which is now aligned to Council's corporate business strategy and programme management arrangements;
 - organisational reviews, via structural changes to the management team and review of scrutiny/decision making; and
 - continued exploration of partnership arrangements (ie anti-fraud and corruption) to identify alternative means of service delivery and to enable efficiency gains.

- 81 The overall theme was that strong processes were either implemented or being developed which would result in tangible future benefits to the Council, both in aspiring towards performing well or strongly on use of resources and in demonstrating longer term achievement of value for money. However, these processes were not sufficiently developed to evidence tangible outcomes which justified assessments of performing well or strongly across all levels of use of resources. However, some evidence of good practice was identified, in particular:
- publication and consultation on financial reporting with stakeholders (ie use of MORI surveys);
 - robust financial management arrangements, in particular medium term financial strategy being aligned with corporate processes and the effectiveness of the Council's revised capital programme/asset management arrangements;
 - effective utilisation of partnership working (ie anti-fraud and internal audit);
 - effective ethical governance arrangements, in particular robust codes of conduct for members and officers and arrangements for raising awareness of the prevention and detection of fraud and corruption throughout the Council with key stakeholders; and
 - proactive arrangements to take effective action from the National Fraud Initiative (NFI).
- 82 When reporting our findings to the Council, we provided overall conclusions and summary improvement opportunities. In judging the Council's performance, we have assessed the Council's arrangements in five areas, as shown in Table 1.

Table 1 Stevenage Borough Council use of resources assessment

Element	Assessment
Financial reporting	2 out of 4
Financial management	3 out of 4
Financial standing	2 out of 4
Internal control	2 out of 4
Value for money	2 out of 4
Overall	2 out of 4

(Note: 1=inadequate performance, 2= adequate performance, 3=performing well 4=performing strongly)

- 83 In reaching these judgements we have drawn on the above work and supplemented this with a review against specified key lines of enquiry.

- 84 We reported to SMB improvement opportunities where further development is needed. SMB have agreed an improvement action plan to take forward the issues raised, the key areas to note by members are:
- improving the quality of working papers submitted for audit, substantiating all primary statements, notes and disclosures;
 - assessing the financial implications and value for money from partnership arrangements;
 - introducing performance measurement and benchmarking for the use of the council's asset base;
 - introducing risk management training and awareness for members;
 - developing arrangements to ensure that SMB and members identify and review all sources of assurances to support the statement on internal control (SIC) prior to the approval of the financial statements;
 - establishing an Audit Committee together with a formal terms of reference covering audit and governance matters which is independent of executive and scrutiny;
 - introducing unit cost comparative data as part of budget setting process to increase understanding and challenge of value for money across services;
 - developing the use of whole life costing for key capital projects and procurement processes; and
 - enhancing arrangements for assessing the value for money obtained via discretionary services.
- 85 In receiving initial and final feedback from the use of resources assessment, the Council provided representations on specific areas of concern, particularly on the issues with adequacy of working papers to support preparation of accounts and significance of historical underspends on the Council's financial standing. These were taken into consideration before finalising our assessment and comments are noted further at paragraphs 48 to 51 (working papers) and 71 to 75 (historical underspends).
- 86 We will be revisiting our use of resources judgement again towards the end of 2006. The Commission are currently consulting with Council's on the revised methodology, approach and key lines of enquiry for these assessments. We will work with the Council when final guidance is produced as part of planning our approach.

Systems of internal financial control

Aside from our use of resources assessment findings, we have not identified any further significant weaknesses in the overall control framework.

- 87 The Council is responsible for ensuring that systems of internal control are in place, and that there are robust arrangements to monitor their adequacy and effectiveness. Our responsibility is to consider whether the Council has put in place adequate arrangements to satisfy itself that its systems of internal financial control are both adequate and effective in practice.
- 88 The internal audit function is a fundamental part of the Council's governance arrangements. Our review of internal audit's work confirmed that they were compliant with the CIPFA Code of Practice for Internal Audit and we could place reliance upon their work for our purposes.
- 89 The statement of internal control (SIC) included in the financial statements for the year highlights that the system of internal control has been in place for the year. The arrangements for monitoring effectiveness are clearly documented, together with areas for further action. We reviewed the content of the SIC and were satisfied that the disclosures provided and actions necessary to address weaknesses in internal control were consistent with our knowledge.

Standards of financial conduct and the prevention and detection of fraud and corruption

We have not identified any further significant weaknesses in your arrangements for maintaining financial conduct and to prevent and detect fraud and corruption.

- 90 The Council has an appropriate governance framework in place of standing orders, financial regulations and a scheme of delegation. Good practice is evident in relation to the prevention and detection of fraud and corruption with appropriate policies and procedures being in place.

Legality of transactions

Overall, we concluded that the Council's arrangements for ensuring the legality of transactions continue to be appropriate.

- 91 The Council is responsible for ensuring that it has appropriate arrangements to ensure the lawfulness of transactions with a financial consequence. We have reviewed these overall arrangements and there are no issues arising that we need to report.

Other work

Grant claims

- 92** In accordance with the principle of strategic regulation, the Audit Commission has continued with a more risk-based approach to the certification of grant claims. This means:
- for claims and returns under £50,000, no certification is required;
 - between £50,000 and £100,000 perform only part A tests (ie agree from entries to underlying records); and
 - over £100,000 perform part A or parts A and B tests depending on a risk assessment of the control environment (part B is the undertaking of transactional testing).
- 93** We have applied these principles in determining the level of certification work required on claims for Stevenage. In particular, we have developed and agreed with the Council a claims protocol to clarify the respective roles and responsibilities, responding directly to issues arising during 2003/04 on a couple of significant claims where there were insufficient working papers or availability of officers to address queries arising.
- 94** We are pleased to note that the standard of working papers supporting claim preparation by the Council has improved for 2004/05. However, this has been a transitional year for the Council, where the implementation of new financial systems has resulted in more extensive audit testing and procedures on significant claims such as National Non-Domestic Rates Return (NNDR), Housing Benefits and Council Tax Benefit (HB/CTB) subsidy and Housing Revenue Accounts subsidy claims. We experienced a number of audit queries and adjustments to the NNDR claim and our audit of the HB/CTB subsidy claim is still in progress, with an expected completion on or shortly after 31 March 2006.
- 95** We are submitting a qualification letter outlining a number of matters arising from our certification of the HB/CTB subsidy claim which may have ongoing subsidy implications for the Council. These matters relate substantially to system weaknesses arising from data conversion to the new benefits system and in some cases interpretation of entitlement being incorrectly assessed on the new systems. We have liaised with the Council throughout to resolve as many of the issues as possible prior to certification and identifying common unresolved issues for the Council to take action on as part of updating the benefits software with suppliers and in preparing for future years subsidy claims.
- 96** As part of our approach to strategic regulation with claims, we have agreed with the Council to consider engaging internal audit to undertake specific procedures to review benefit cases during 2005/06 which we can place reliance upon as part of planning our audit of subsidy claim for the financial year ended 31 March 2006.

- 97** We expect the arrangements for claim preparation to continue improving at the Council for 2005/06 and the substantive issues arising from systems implementation to be addressed in many cases. We will continue to assess overall arrangements for preparation of claims and incorporate this into our risk assessment/ approach.

National Fraud Initiative

- 98** In 2004/05, the Council took part in the Audit Commission's National Fraud Initiative (NFI). The NFI, which is undertaken every two years, aims to help identify and reduce fraud by bringing together data from NHS bodies, local authorities and government departments and other agencies, to detect a wide range of frauds against the public sector. These include housing benefit fraud, occupational pension fraud, tenancy fraud and payroll fraud as well as, new for 2004/05, right to buy scheme fraud and providing new contact details for former tenants with arrears in excess of £1,000.
- 99** Investigations of the data relevant to the Council by officers have identified savings of £16,000 which is consistent with the level found previously.

Looking forward

Future audit and inspection work

- 100 We have an agreed plan for 2005/06 and we have reported in this letter those aspects that have already been completed. The remaining elements of that plan, including our audit of the 2005/06 accounts, will be reported in next year's annual letter.
- 101 We have sought to ensure, wherever possible, that our work relates to the improvement priorities of the Council. We will continue with this approach when planning our programme of work for 2006/07. We will seek to reconsider, with you, your improvement priorities and develop an agreed programme by 31 March 2006. We have already shared and agreed in principle our plan for 2006/07.

Revision to the Code of Audit Practice

- 102 The statutory requirements governing our audit work, are contained in:
- the Audit Commission Act 1998; and
 - the Code of Audit Practice (the Code).
- 103 The Code has been revised with effect from 1 April 2005. Further details are included in our Audit Plan which has been agreed with the Overview and Scrutiny Committee - Corporate Services in April 2005. The key changes include:
- the requirement to draw a positive conclusion regarding the Council's arrangements for ensuring value for money in its use of resources; and
 - a clearer focus on overall financial and performance management arrangements.

A new CPA framework

- 104 The Audit Commission is currently considering the results of the consultation on the proposals for revising the CPA framework for district councils. We will liaise with the Council in confirming the timetables and implementation for the revised framework.

Closing remarks

- 105** This letter has been discussed and agreed with officers of SMB and has been discussed and agreed with the Leader of the Council and Councillor Taylor as portfolio holder for resources (those charged with governance) prior to 31 March 2006. We intend to present our letter to the next Council Executive; following 31 March 2006 for consideration.
- 106** The Council has taken a positive and constructive approach to our audit and inspection I would like to take this opportunity to express my appreciation for the Council's assistance and co-operation.

Availability of this letter

- 107** This letter will be published on the Audit Commission's website at www.audit-commission.gov.uk and also on the Council's website.

Rob Murray
District Auditor and Relationship Manager
May 2006

Appendix 1 – Background to this letter

The purpose of this letter

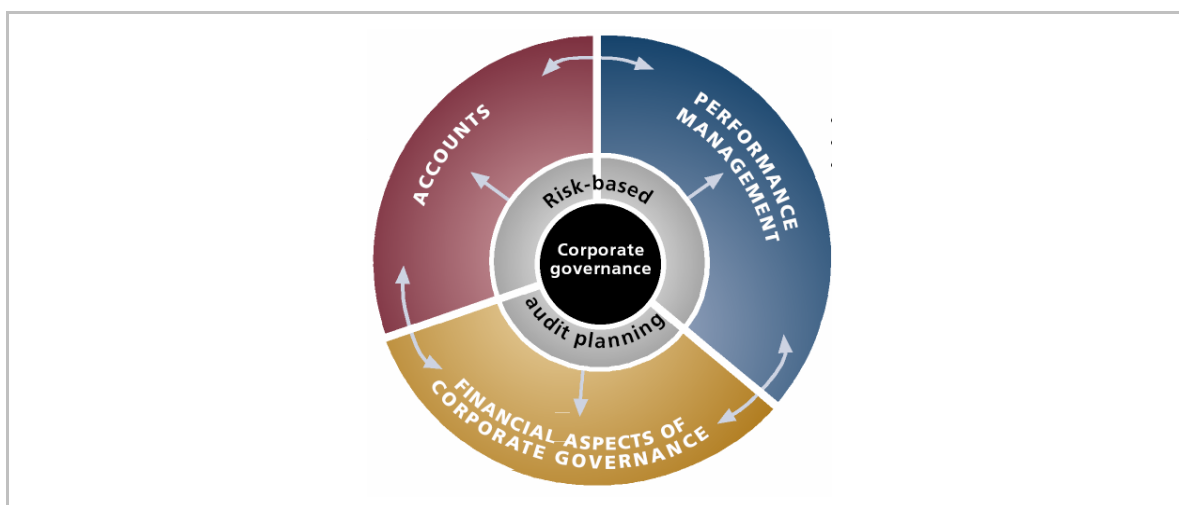
- 1 This is our audit and inspection 'Annual Letter' for members which incorporates the Annual Audit Letter for 2004/05, which is presented by the Council's District Auditor and Relationship Manager. The letter summarises the conclusions and significant issues arising from our recent audit and inspections of the Council.
- 2 We have issued separate reports during the year setting out the findings and conclusions from the specific elements of our programme. These reports are listed at Appendix 2 for information.
- 3 The Audit Commission has circulated to all audited bodies a statement that summarises the key responsibilities of auditors. Our audit has been conducted in accordance with the principles set out in that statement. What we say about the results of our audit should be viewed in the context of that more formal background.
- 4 Appendix 3 provides information about the fee charged for our audit and inspections.

Audit objectives

- 5 Our main objective as your appointed auditor is to plan and carry out an audit that meets the requirements of the Code of Audit Practice. We adopt a risk-based approach to planning our audit, and our audit work has focused on your significant financial and operational risks that are relevant to our audit responsibilities.
- 6 Central to our audit are your corporate governance arrangements. Our audit is then structured around the three elements of our responsibilities as set out in the Code and shown in Figure 2.

Figure 1 Code of Audit Practice

Code of practice responsibilities



Accounts

- Opinion.

Financial aspects of corporate governance

7 Reviewing how effectively the Council ensures:

- financial standing;
- systems of internal financial control;
- standards of financial conduct and the prevention and detection of fraud and corruption; and
- legality of transactions with significant financial consequences.

Performance management

- use of resources;
- performance information; and
- best value performance plan.

Inspection objectives

8 Inspection work is based around section 10 of the Local Government Act 1999, which requires us to carry out inspections and deliver reports that will:

- enable the Council and the public to judge whether best value is being delivered;
- enable the Council to assess how well it is doing;
- enable the Government to assess how well its policies are being implemented; and
- identify failing services where remedial action may be necessary.

Appendix 2 – Audit and inspection reports issued

- 1 Table 3 details the reports that have been issued since the last annual audit and inspection letter was issued in November 2004.

Table 2 Reports issued

Report title	Date issued
Audit plan 2004/05	August 2004
Audit plan 2005/06	April 2005
Presentation - diversity, user focus and race equality	February 2005
Audit opinion	TBC
Statutory opinion on 2005/06 BVPP	December 2005
Matters arising from audit of financial statements (summary issues)	TBC - following completion of our audit. Key messages to the Council.
Direction of Travel statement	March 2006
Use of resources audit score feedback 2005/06	March 2006
Annual audit and inspection letter	March 2006

Appendix 3 – Audit and inspection fee

- 2 The proposed audit and inspection fee was set out in the plan agreed at the start of the audit. Table 4 compares the planned and actual fee for the year.

Table 3 Audit fee update

Audit area	Plan 2004/05 (£)	Actual 2004/05 (£)
Accounts (including planning and control)	85,600	85,600
Financial aspects of corporate governance	19,700	19,700
Performance	51,000	51,000
Total Code of Audit Practice fee	156,300	156,300
Grant claim certification	51,000	70,000 (estimate)
Total	207,300	226,300

- 3 The movement between the planned and actual fee results from:
- Grant claim certification - the variation represents an estimate of additional time taken to undertake audit procedures on the NNDR and the HB/CTB subsidy claims as a result of issues arising from the Council's implementation of systems and data conversion. We will continue to liaise with the Council on the precise fee implications on completion of our certification of the HB/CTB subsidy claim.

Inspection fee update

The full year inspection fee is £26,300. The work reported in this audit and inspection letter has been funded by an element of the fee covering 2004/05 and by an element of the fee covering 2005/06. In both years the actual fee will be in line with that planned.