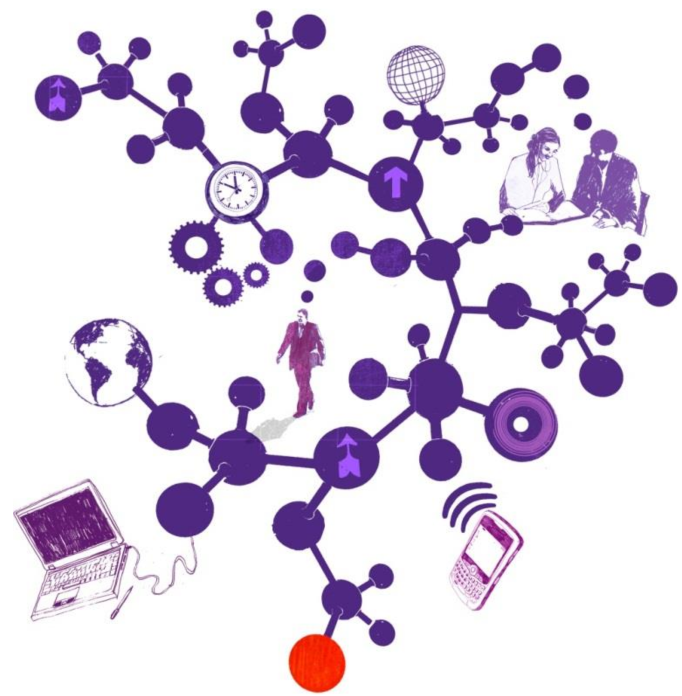
Audit Committee Update for Bath and North East Somerset Council

Year ended 31 March 2015

December 2014



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Introduction

This paper provides the Corporate Audit Committee with a report on progress in delivering our responsibilities as your external auditors. The paper also includes:

- a summary of emerging national issues and developments that may be relevant to you as a unitary council
- includes a number of questions in respect of these emerging issues which the Committee may wish to consider.

Members of the Corporate Audit Committee can find further useful material on our website www.grant-thornton.co.uk, where we have a section dedicated to our work in the public sector. Here you can download copies of our publications – 'Local Government Governance Review 2014 – Working in Tandem', '2016 tipping point – Challenging the current?', 'Pulling Together the Better Care Fund', 'Where Growth Happens' and '2020 Vision?'.

If you would like further information on any items in this briefing, or would like to register with Grant Thornton to receive regular email updates on issues that are of interest to you, please contact either your Engagement Lead or Audit Manager.

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Progress at 24 November 2014

Work	Planned date	Complete?	Comments
2014-15 Accounts Audit Plan We are required to issue a detailed accounts audit plan to the Council setting out our proposed approach in order to give an opinion on the Council's 2014-15 financial statements.	May 2015	Not yet due	
Interim accounts audit Our interim fieldwork visit includes: • updating our review of the Council's control environment • updating our understanding of financial systems • review of Internal Audit reports on core financial systems • early work on emerging accounting issues • early substantive testing • early work for the Value for Money conclusion.	January to February 2015	Not yet due	
2014-15 final accounts audit Including: • audit of the 2014-15 financial statements • proposed opinion on the Council 's accounts • proposed Value for Money conclusion.	July to September 2015	Not yet due	

Progress at 24 November 2014

Work	Planned date	Complete?	Comments
Value for Money (VfM) conclusion The scope of our work to inform the 2014-15 VfM conclusion comprises: • Key indicators of financial performance • Strategic financial planning • Financial governance • Financial control • Prioritising resources • Improving efficiency and productivity • Management of natural resources	February 2015 – July 2015	Not yet due	
Other areas of work If requested, we will certify your Regional Growth Fund returns in accordance with the Government department timetable.	January 2015 & February 2015	Not yet due	
Other activity undertaken • Met with the Divisional Director: Business Support and the finance team to discuss the action taken in response to our audit findings report. • Certification work in progress on housing benefits, transport and teachers' pensions. • Workshop arranged covering the changes in accounting for schools and infrastructure assets. • Shared Grant Thornton national reports with the Divisional Director: Business Support. These included *Pulling Together the Better Care Fund, Where Growth Happens and 2020 Vision*.		Not applicable	• Our report on the certification of claims and returns for 2013-14 will be presented at the February 2015 meeting. • Copies of Grant Thornton national reports have also been made available to members.

Accounting and audit issues

Accounting for schools

The debate about which school land and buildings should be recognised on a local authority balance sheet (which most commentators had thought settled) has been reignited. Grant Thornton is taking a leading role in trying to resolve this unexpected development.

In March, CIPFA/LASAAC Code concluded that under IFRS 10, maintained schools (but not free schools or academies) meet the definition of entities that need to be consolidated in group accounts. However, rather than requiring local authorities to prepare group accounts, the CIPFA/LASAAC Code requires local authorities to account for maintained schools within their single entity accounts. This includes school income and expenditure as well as assets and liabilities. The general expectation in the sector was that:

- the vast majority of voluntary aided, voluntary controlled and foundation schools would be recognised on local authority balance sheets
- a small number of school buildings that are provided at no charge by a religious body and where there was a realistic possibility that they could be taken back by their owners would be treated as assets of the religious body and so not recognised on the local authority balance sheet.

However, at the CIPFA conference in November, CIPFA clarified that it considers that most voluntary aided and voluntary controlled school buildings would **not** be recognised on the balance sheet. This is because the religious bodies have a legal right to take back these assets. Nor does CIPFA consider the position for foundation school building to be clear cut and local judgement would need to be applied. We have not seen evidence that would support the view taken by CIPFA and have concerns about:

- whether the treatment proposed by CIPFA complies with the Code
- the significant practical implications for the sector
- the potential for inconsistent accounting treatments depending on local judgement.

We are taking a leading role in discussions with the Audit Commission, CIPFA and the other audit firms suppliers to try to seek a practical way forward as soon as possible.

Accounting and audit issues

We will continue to share the latest developments with officers. In the mean time we would recommend that you continue your preparations for recognising school land and building including:

- identifying those schools where school buildings are owned by third parties (such as church dioceses) and determining under what circumstances the buildings could be taken back by the third party
- obtaining valuations for school land and buildings for each of the three balance sheet dates (1 April 2013, 31 March 2014, 31 March 2015)
- obtaining sufficient information to enable the authority to restate its revaluation reserve and capital adjustment account.

Issue for consideration

- Has the Divisional Director: Business Support put a plan in place to address the changes in accounting for schools?

Accounting and audit issues

Group accounting standards

The Code has adopted a new suite of standards for accounting for subsidiaries, associates and joint arrangements. These changes affect how local authorities account for services delivered through other entities and joint working with partners.

The key changes for 2014/15 are to:

- the definition of control over other entities. This is set out in IFRS 10 and determines which entities are treated as subsidiaries
- the accounting for joint arrangements. This now follow IFRS 11 and includes changes to the definition of joint ventures and how joint ventures are consolidated in group accounts
- disclosures in relation to subsidiaries, joint arrangements, associates and unconsolidated entities as set out in IFRS 12.

Changes to the definition of control over other entities

Control was previously defined in terms of power to govern the financial and operating policies of an entity. IFRS 10 sets out three elements for an investor to be considered as controlling an investee (all of which must be met):

- the investor has the rights to direct the relevant activities of the investee (relevant activities being the ones that determine the return for the investors – the return could be in the form of a service rather than money)
- the investor has exposure, or rights, to variable returns from its involvement with the investee
- the investor has the ability to use its power over the investee to affect the amount of the investor's returns.

In the commercial sector, this is generally thought to have resulted in more entities being treated as subsidiaries. However, the change is in both directions: some subsidiaries have been redefined as associates. Local authorities with investments in other entities will need to consider whether:

- they control any entities using the new definition. Local authorities will need to pay particular attention to special purpose vehicles and any other entities where there was a close judgement call under the old IAS 27
- there is a need for a prior period adjustment.

Accounting and audit issues

Changes to accounting for joint arrangements

Joint arrangements are contractual arrangements between two or more parties where there is joint control. IFRS 11 makes three key changes from IAS 31:

- there are now only two types of joint arrangements: joint operations and joint ventures
- under IAS 31 joint ventures were legal entities. IFRS 11 bases its definition of joint ventures on the substance of the arrangement rather than legal status. In a joint operation the investing parties have rights and obligations in relation to the arrangement's assets and liabilities, whereas in a joint venture the parties have rights to the arrangement's net assets
- local authorities are still required to consolidate joint ventures in their group accounts but must now do so using the equity (single line) method. The option for proportionate (line-by-line) consolidation has been removed.

The key challenge for most local authorities will be determining whether their joint arrangements are joint ventures or joint operations. The difference should be clear from the contract but in some cases judgement may be required. Local authorities that have previously used the proportionate consolidation method will need to account for the move to equity accounting as a prior period adjustment.

Disclosure of interests in other entities

IFRS 12 makes consistent the requirements for disclosures in relation to subsidiaries, joint arrangements, associates and unconsolidated entities. It includes the need for transparency about the risks to which the reporting entity is exposed as a consequence of its investment in such arrangements.

Issue for consideration

- Has the Divisional Director: Business Support assessed the potential impact of these standards for the authority's financial statements?

Accounting and audit issues

Early close

DCLG is consulting on proposals to bring forward the audit deadline for 2017/18 to the end of July 2018. Although July 2018 is almost 4 years away, both local authorities and their auditors will have to make real changes in how they work to ensure they are 'match-fit' to achieve this deadline. This will require leadership from members and senior management. Local government accountants and their auditors should start working on this now.

Top tips for local authorities:

- make preparation of the draft accounts and your audit a priority, investing appropriate resources to make it happen
- make the year end as close to 'normal' as possible by carrying out key steps each and every month
- discuss potential issues openly with auditors as they arise throughout the year
- agree key milestones, deadlines and response times with your auditor
- agree exactly what working papers are required.

Issue for consideration

- Has the Divisional Director: Business Support put a plan in place to address the earlier close date?

Grant Thornton

2020 Vision

In a time of unprecedented challenge for English local government, how can the sector develop towards 2020 if it is to have a sustainable future? Our latest report provides a thorough analysis of the current political and economic context, explores a range of potential policies and outcomes, and suggests several scenarios to facilitate an open debate on the future for the sector.

Our national report '2020 Vision', produced in collaboration with the University of Birmingham's Institute for Local Government Studies (INLOGOV), suggests that fundamental changes to local government are both operationally necessary and constitutionally inevitable, for the sector to remain relevant by 2020. The report offers a thorough analysis of the current political and economic context and explores a range of potential future policies and outcomes that English local government will need to adopt and strive towards as they seek to adapt and overcome these challenges.

Placed in the context of enhanced devolution, following the Scottish independence referendum, 2020 Vision maintains a wary eye fixed on the 2015/16 Spending Round and looks ahead to the life time of the next government. It highlights that the economic and financial situation remains increasingly untenable, with an expanding North/South divide arising from the pattern of funding reductions and economic growth.

English local authorities continue to face unprecedented challenges, relating to the pressures of austerity and central government funding reductions, and demographic and technological change. Our report highlights the vital role of a successful local government sector and encourages it to think hard about how it will cope in the future.

Informed by the views of a broad range of local authority leaders, chief executives and other sector stakeholders, the report offers a set of six forward-looking scenarios* in which councils could be operating within by 2020. Though not mutually exclusive, we suggest that key stakeholders need to take urgent action to avoid a potential slow and painful demise for some councils by 2020.

Further hard copies of our report are available from your Engagement Lead or Audit Manager.

Grant Thornton

Pulling together the Better Care Fund

Do local authorities and clinical commissioning groups (CCGs) have effective arrangements to develop joint Better Care Plans for agreement by the health and wellbeing boards (HWBs) and how ready are they for the pooled fund in April 2015?

Our report 'Pulling together the Better Care Fund' draws on our review of the introduction of draft Better Care Fund (BCF) plans for both the February and April submissions. It is based on a sample of our findings from 40 HWB localities. It considers the partnership arrangements across a HWB planning area and is supported by discussions with the sector, across the country. The result is a snap shot of progress as at 30 June 2014, prior to the issue of revised planning guidance by NHS England and the Local Government Association on 25 July 2014.

It provides you with:

- an understanding of how your approach to introducing BCF compares to others across the country
- assistance in identifying the key issues to delivering Better Care Fund plans effectively
- insight into current best practice
- practical areas for consideration for improving arrangements in the future.

Further copies of our report are available from your Engagement Lead or Audit Manager.

Grant Thornton

Where Growth Happens

As the UK emerges from recession, increasing attention is being given, both nationally and locally, as to how to accelerate economic sector growth. Our report presents the findings of research undertaken by our Place Analytics team on the dynamics of local growth. It will give FDs and CEOs of local authorities and LEPs:

- an insight into the geographic areas of high growth and dynamic growth (ie the quality of growth)
- an understanding of the characteristics of both growing and dynamic places to help frame policy and sustain future growth
- an understanding of growth corridors and their implications, not only for UK policy makers, but also for those locally sitting within and outside the corridors
- an insight into the views of different leaders charged with making growth happen in their locality.

Our report 'Where Growth Happens' provides a ranking of English cities according to their economic growth over an eight year period (2004 – 2012). Outside of London – which maintains eight of the top 10 best performing districts overall – it places Manchester, Birmingham and Brighton and Hove in the top three, as measured by economic, demographic and place (dwelling stock and commercial floor space) growth.

The analysis also assess the quality of local growth - or 'dynamism' - to identify areas with a vibrant and dynamic economy capable of supporting future expansion, based on five key drivers. London again tops the ranking, with nine out of the top 10 dynamic growth areas. Outside the capital, Cambridge, Reading and Manchester top the list of future sustainable growth.

Based on this analysis of past progress and future prospects, our report reveals a number of 'growth corridors' – functional and large scale local economic areas in England – which are playing a significant role in the country's overall growth levels. Though predominantly stemming from London, the intra-city growth corridors include a number of other large cities at their core, creating a network of key strategic linkages between high growth and dynamic areas.

Further copies of our report are available from your Engagement Lead or Audit Manager.

Grant Thornton

New Routes to Housing Development

We have issued the first in a series of good practice papers on topical issues for local government.

This paper considers good practice in councils' approaches to delivering affordable housing. Until recently, local authorities have acted as an enabler of new affordable housing; increasingly they are now undertaking a direct delivery role. Delivery routes vary and must be structured with the council's objectives and capacity in mind as there is no 'one size fits all' approach. The paper considers the benefits and challenges of council owned housing companies, including:

- Setting and delivering objectives
- Identifying optimal funding routes
- Assessing viability and working with others

The paper stresses the importance of a properly developed business case and business plan to support the setting up of a housing company.

Copies of our good practice paper are available from your Engagement Lead or Audit Manager.

Grant Thornton

Anti-fraud and corruption update

Key current issues include:

Single Fraud Investigation Service (SFIS) - The SFIS will bring together all investigative capacity in relation to benefits and tax credits under the control of the Department of Work and Pensions. However a number of local authorities have expressed concern that such a transfer will cause them to lose the capacity to readily investigate other issues such as employee fraud and corruption allegations.

Corruption risk - In 2013 Transparency International (TI), the world's leading non-governmental anti-corruption organisation, published a report on corruption in UK Local Government. It identified twelve key risk areas covering public procurement, control over outsourced services, personnel transferring between local authorities and companies bidding to provide services, planning issues, collusion in housing fraud and manipulation of electoral registration. TI expressed concern that audit committees were unable to fulfil the function of reducing risks in many authorities.

Non–benefits fraud - There are striking differences between the identification of benefit and non-benefit fraud within local government. The Audit Commission has reported that 79 district councils did not detect a single non-benefit fraud whereas only 9 councils among all London boroughs, metropolitan districts and unitary authorities reported non-benefit frauds. Procurement fraud in particular is consistently estimated as accounting for the largest losses to fraud within local government. In its most recent Protecting the Public Purse publication the Audit Commission estimated annual losses at £876 million, representing 1% of total procurement spend.

Our Forensic Investigation Services provide a range of services to local authorities including fraud prevention and detection. If you are interested in a further discussion on these areas please contact your Audit Manager.

Local government guidance

Managing Council Property Assets

The Audit Commission has issued a briefing paper entitled Managing Council Property Assets: Using Data from the VFM Profiles.

In the paper the Audit Commission:

- advocates that councils should be active and strategic managers of their estates – understanding property markets and asking questions about the properties they own or lease,
- prompts councils to consider whether assets are in the right place, whether they should keep, sell, or transfer them, and how much they should invest in building, buying and maintaining property,
- invites local authorities to balance the value realised through sales of surplus assets, against the cost of maintaining them.

The background to the briefing is the collation of information from the government's capital outturn return which identifies that the local government estate has an net book value of £169.8 billion of which £2.5 billion have been classified as 'surplus' assets. In this context the Audit Commission is calling on councils to ensure they have a strategic approach to managing these assets, in order to get the best value for money they can from this portion of the local government estate. The Audit Commission Chair, Jeremy Newman said:

"*we are neither advocating that local government starts a wholesale sell-off of their land and property nor are we suggesting councils shouldn't spend money on buying assets or on investment to improve their existing property. What we are highlighting is a group of assets that do not provide immediate benefit to local communities, but still require councils to spend money on maintaining them. These assets have potential value for councils. While not all such land or buildings may be sellable, councils should consider how much value they gain from surplus assets and how this could be increased. I urge councils to use the data held in the Commission's 'Value for Money (VFM) Profiles Tool', such as spending on and value of land and property assets and 'surplus' assets, alongside their unique and detailed local knowledge, to regularly review if their estate is fit-for-purpose.*"

Issue for consideration

- Are members satisfied that the Council has adequate management arrangements in place to ensure its property assets are being efficiently and effectively managed?