

Annual Audit Letter

Essex County Council

Audit 2008/09

December 2009



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Status of our reports

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

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

This report summarises the findings from our 2008/09 audit. It includes messages arising from the 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.

Accounts

- 1 The Council was required to prepare and approve their 2008/09 accounts by 30 June 2009. The Council met the deadline but the note on fixed assets was not complete and members had limited time to review the accounts before approving them. Not all working papers to support the accounts were available at the start of the audit.
- 2 We issued an unqualified opinion on the accounts and value for money conclusion on 30 September 2009, which was the deadline.
- 3 Our audit found some material and significant errors in the approved accounts. The Council agreed to correct all material and most significant errors but officers chose not to amend for a small number of others. The uncorrected errors were not so significant as to distort the overall financial position of the Council. I reported these to the Council's Audit Committee (as those charged with the governance of the Council), who agreed with the decision not to amend the accounts for those errors.
- 4 Once the Council had amended the accounts for the material errors, I concluded that the accounts 'presented fairly' the Council's financial position at 31 March 2009 (an unqualified audit opinion) and its income and expenditure for the financial year.
- 5 A new reporting framework, International Financial Reporting Standards (IFRS), is to apply to council accounts in 2010/11. The Council has developed a project plan to implement these standards and is progressing with the implementation of this plan.

Use of Resources

- 6 We assess how the Council makes use of its resources to provide local services. A national framework is applied to our assessment, with a score given between 1 (inadequate and below minimum standards) and 4 (performing strongly) in each of three key areas.
- 7 The Council is performing well overall (Level 3). It achieved the following scores in our assessment.
 - Level 3 in respect of the way it manages its finances.
 - Level 2 (performing adequately) in respect of the way it manages and governs the business as a whole.
 - Level 3 in respect of the way it manages its natural resources and assets.

- 8 As a result of my assessment, I concluded that the Council had proper arrangements in place for the way it manages its use of resources and provides value for money.
- 9 I have issued a separate Use of Resources report which sets out the detailed findings supporting this assessment.

Managing performance

- 10 The Audit Commission also assesses how well the Council manages and improves its services and contributes to wider community outcomes. The assessment considers how successful the Council is in delivering its corporate priorities. The priorities have been drawn from what matters most to local people.
- 11 The Council scores 2 out of 4 for managing its performance (the scoring mechanism is as for Use of Resources).
- 12 The Council is delivering priority services well and has the capability to continue to improve. Most partnership working is effective and delivering good outcomes for local people.
- 13 Services for the well-being and safeguarding of children are inadequate. Staff shortages, high workloads and partners being unclear of their role are recognised as key areas for improvement. There is insufficient capacity in the Council's children's social care which is seriously affecting safeguarding of children. The Council is responding to weaknesses with a range of measures such as appointing an experienced Director of Children's Services, reviewing the Children's Trust and taking a proactive approach to recruitment, although it is not clear if this will give sufficient capacity to significantly improve services.
- 14 The Council is aware of some aspects of the democratic processes that need strengthening.

Overall Organisational Assessment

- 15 The Use of Resources and Managing Performance assessments are combined to give an overall organisational assessment judgement for the Council.
- 16 The Audit Commission has determined that the organisational assessment judgement for the Council is that it performs adequately (level 2). This is because the Council delivers many quality services that meet local need and manages its finances well. However, children's services are not performing adequately notably in ensuring that children are safe and therefore overall the Council's performance is adequate.
- 17 The Council's Managing Performance and Organisational Assessment are being reported in detail separately by the Audit Commission's Comprehensive Area Assessment Lead.

Financial standing

- 18 The last year has seen the country enter a significant economic recession. The consequence locally is an increasing demand for public services and the likelihood of reduced levels of central government funding at the same time as local businesses having to face difficult trading conditions. Together, these provide a significant challenge for local councils as they seek to continue to provide services to local residents and support the local economy, whilst maintaining a sound financial position.
- 19 The Council has been reviewing how it provides its services to identify significant savings. Progress against savings plans is monitored closely and the Council has ambitious plans through its Transformation Programme for making further savings in the future.
- 20 The Council has worked in partnership with an established bank to increase funds available to local businesses and has also worked with post offices threatened with closure to maintain local provision where possible and beneficial to do so.
- 21 The impacts of the recession will continue to present challenges to the Council in the coming financial year. I will continue to monitor the Council's response and actions in this key area.

Treasury management

- 22 The Council invests large sums of money which are held in reserves for future projects or to meet payments as they become due. The recent banking crisis meant that all councils faced increased risks associated with these investments and some councils lost money that had been placed with banks in Iceland.
- 23 The Council has good treasury management arrangements. Risks have been well managed while the focus on obtaining the best possible return has been maintained. The Council had no deposits with Icelandic banks when they were no longer able to meet their liabilities.

Members' allowances

- 24 I am currently concluding my review of members' expenses and will not issue the certificate of completion of the audit until this is completed.

Table 1 Audit fees

	Actual (£)	Proposed (£)	Variance (£)
Financial statements and annual governance statement	246,110	271,110	25,000
Value for money	153,270	153,270	0
Total audit fees	399,380	424,380	25,000
Corporate Assessment	77,060	77,060	0
Other Inspection	16,420	16,420	0
Total	492,860	517,860	25,000

- 25** As reported to the Audit Committee at its meeting on 25 September 2009, the audit fee has increased due to the number of errors made in the accounts and the increased testing required due to a number of material financial systems not having effective controls in place and also because of the number of material and significant errors in the accounts presented for audit.

Actions

- 26** I have made a number of recommendations within this letter, to further develop the arrangements in place at the Council, with the purpose of delivering better outcomes for the residents of the County. The Council should monitor the implementation of these recommendations.

Independence

- 27** As the External Auditor appointed to audit the Council, I have to maintain my independence. I can confirm that the audit has been carried out in accordance with the Audit Commission's policies on integrity, objectivity and independence.

Financial statements and annual governance statement

The Council's financial statements and annual governance statement are an important means by which the Council accounts for its stewardship of public funds.

The Council is also the administering authority for the local government pension scheme in Essex and is responsible for preparing accounts for this scheme.

- 28** I issued an unqualified opinion on the Council's accounts and the Pension Fund accounts on 30 September 2009, which was the deadline set within the accounts and Audit Regulations 2003. In my opinion the accounts for the Council and the Pension Fund present fairly the financial position as at 31 March 2009 and the income and expenditure for the year.
- 29** Before giving my opinion, I reported to those charged with governance, the Audit Committee, on the issues arising from the 2008/09 audit. I presented my report on 25 September 2009. The Council has prepared and is implementing an action plan to address the recommendations in my report, and this was presented to the Audit Committee at its meeting on 1 December 2009.
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Significant issues arising from the audit of the Council's accounts

- 30** Some notes in the accounts approved by members in June 2009 were not complete, including the fixed asset note. A number of working papers were not completed in line with the agreed timetable and those to support the fixed asset balances were not ready when the accounts were approved.
- 31** All the material errors in the accounts related to fixed assets.
- The assets were not impaired (valued downwards) correctly to reflect the reduction in value due to the general decrease in property values in the current economic conditions. This error was estimated to be £248 million.
 - Schools that had become Academy Schools were included on the Council's balance sheet but as the Council does not have the risks and rewards linked with those assets they should have been excluded. This error was £42million.
 - The Council had not accounted for the transfer of two voluntary aided schools to two Dioceses correctly. The error was £27 million.
 - The value of a school was reduced by £6 million accidentally.
 - An asset valued at £5 million had been treated as surplus to requirements but was still being used.
-

- 32** All these errors were corrected. The Council is in the process of implementing a new fixed asset system which may reduce the risk of similar errors being made in the future although there is a risk of errors being made in transferring to a new system.
- 33** The Council year end cash balance includes cash held by schools. There were a number of significant errors on school bank reconciliations but the total estimate of this error was not material. The Council will be issuing improved guidance and training to reduce the risk of cash balances being misstated next year.

Material weaknesses in internal control

- 34** I reported a number of weaknesses in internal control to the Council in September 2009. These included:
- weaknesses on journal controls (the process to move transactions from one account code to another);
 - inadequate arrangements to ensure all transactions are authorised properly;
 - inadequate controls on credit notes;
 - inadequate segregation of duties in some areas so that some officers were able to process transactions without the involvement of anyone else which increases the risk of fraud or error;
 - orders being made with outside suppliers without complying with the Council's official ordering processes;
 - a fixed asset register based on complex spreadsheets that increases the risk of error;
 - incomplete reconciliations between some systems and for some grants received; and
 - incomplete information held on file to support the reduction in the amount received for the sale of a property compared to the original tender.
- 35** The Council is actively working to address these control weaknesses.

Pension Fund Accounts

- 36** The Pension Fund accounts and working papers continued to be of good quality and audit queries were dealt with promptly and appropriately. There were no significant amendments needed to the accounts but I did report that the Pension Fund does not have its own separate bank account. I made a recommendation on this issue and the Council will establish a separate bank account from 1 April 2010.

International Financial Reporting Standards

- 37** The national timetable for the implementation of International Financial Reporting Standards (IFRS) means that these will be first applied in the 2010/11 financial year. However, comparative figures for the 2009/10 financial year will be required.

- 38** Applying IFRS will have significant implications for the way in which local authorities prepare their annual financial statements. The Council has a detailed project plan in place.

Recommendations

- R1** The Council should ensure that sufficient resources are directed towards addressing control weaknesses in material financial systems and producing accounts that are free from material error.
- R2** The Council should continue to monitor progress against the IFRS implementation plan through the Audit Committee and ensure that the implications of IFRS on financial planning are widely understood.

Value for money and use of resources

I considered how well the Council is managing and using its resources to deliver value for money and better and sustainable outcomes for local people, and gave a scored use of resources judgement.

I also assessed whether the Council put in place adequate corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the value for money (VFM) conclusion.

Use of resources judgements

- 39** In forming my scored use of resources judgements, I have used the methodology set out in the [use of resources framework](#). Judgements have been made for each key line of enquiry (KLOE) using the Audit Commission's current four point scale from 1 to 4, with 4 being the highest. Level 1 represents a failure to meet the minimum requirements at level 2.
- 40** I have also taken into account, where appropriate, findings from previous use of resources assessments (updating these for any changes or improvements) and any other relevant audit work.
- 41** The Council's use of resources theme scores are shown in Table 2. A separate Use of Resources report has been issued containing my detailed findings and recommendations. The Council has put in place an action plan to address the recommendations in the report, and this was considered by the Audit Committee at its meeting on 1 December 2009.

Table 2 Use of resources theme scores

Use of resources theme	Scored judgement
Managing finances	3
Governing the business	2
Managing resources	3

Managing finances

- 42** The Council considers finance when planning how to deliver services. The Council takes non-finance strategies into account when setting its annual and medium term budget. When the Council identifies a financial issue it takes action to address it.

Value for money and use of resources

- 43 The Council has made good progress on understanding its costs and using that information to inform planning and decision making. The Council has an ambitious cost saving programme which is closely monitored and has made significant savings to reduce back office costs and re-invest a proportion in front line services.
- 44 The Council monitors its financial position regularly but reports do not always take into account payments the Council is committed to but not yet made. Budget holders and Members understand the financial information they receive. Finance and performance are reported separately but considered together and effective, performance is improving. Internal Audit has identified that financial monitoring of partnerships needs to improve in some areas.
- 45 The Council has started to prepare for the implementation of International Financial Reporting Standards.
- 46 Although financial reporting during the year is sound and effectively supports decision making, the 2008/09 accounts presented for audit were materially misstated and some working papers were not provided within the agreed timescale.
- 47 The Council does not have a strategic approach to charging for services, although charging policies exist in some services such as Adult Social Care. We have not identified any examples where the lack of a policy has had a significant impact on service delivery or access to services.

Governing the business

- 48 The Council has clear priorities based on extensive consultation with service users and the wider public.
- 49 The Council is working with partners to improve the effectiveness of procurement and service to users. Joint funding has led to new posts in response to an identified need. Service design generally supports value for money.
- 50 Users are influencing procurement decisions. The Council is addressing the need to improve its IT arrangements. The Council manages risks of suppliers failing in the current economic conditions. Procurement processes have become more streamlined but improvements are required on the understanding and achievement of savings targets and the establishment of a complete contracts register.
- 51 The framework for data quality in the Council is generally sound. Information is analysed to identify need and areas for improvement. The Council manages performance effectively against priorities, demonstrating improvement. Systems cannot transfer data automatically. Data quality for partnerships needs to improve and the Council is taking steps to address this. Data security has improved significantly but from a low base and Business Continuity arrangements have improved.
- 52 The Council has a governance framework in place but member training and accountability are developing. Member scrutiny and leadership are leading to improved service performance.

- 53 The Council flexes its priorities appropriately which has led to initiatives such as the 'Banking on Essex' project. However the usual governance processes are considered too slow by senior Council officers to support these initiatives so alternative arrangements are made which are not always transparent.
- 54 The Council's legal department is not at the heart of decision making and not always aware of issues it should be advising on or whether or not its advice has been followed. The Council seeks legal advice from outside sources but this is not always committed to formal legal advice in writing until a new initiative is very well developed and expectations of delivery have been raised. Papers for Member meetings are not always available with the agenda or in advance of the meeting. Confidential issues are discussed in Part 2 of Council and Committee meetings. Decisions made in Part 2 meetings are recorded with those made in Part 1 but there is no record held by the Council to record the discussions in Part 2 meetings.
- 55 Risk Management arrangements are in place but member involvement needs to improve. Internal Audit and Counter Fraud arrangements are strong but there are significant system control weaknesses.

Managing resources

- 56 The Council has made significant achievements in its approach to managing natural resources effectively. It is seen as performing well by other Councils and shares its approach with them. The Council can demonstrate a clear understanding of its carbon emissions and how it plans to reduce them; however some plans and targets are still to be developed, especially at a local level such as within individual buildings.
- 57 The Council has gone further than looking just at carbon and has demonstrated work towards a strategy for water conservation which it sees as a key resource and one that needs to be managed more carefully in the future.
- 58 Environmental considerations are taken into account comprehensively in construction projects. Partnership working is effective to address environmental issues including waste management and tree planting. The Council has achieved a low rate of travel to school by car.
- 59 Asset management plans reflect the overall plans of the Council and are effectively performance managed. Assets are managed pro actively to achieve value for money and efficiency savings, in financial and environmental terms.
- 60 The Council is working effectively with partners to use buildings jointly which provides greater value for money and a better service to the public. The Council has joined with other County Councils to jointly procure major capital projects which have improved the project management arrangements in place.

VFM conclusion

- 61** I assessed the Council's arrangements to secure economy, efficiency and effectiveness in your use of resources against criteria specified by the Audit Commission. From 2008/09, the Audit Commission will specify each year, which of the use of resources KLOE are the relevant criteria for the VFM conclusion at each type of audited body.
- 62** Based on the Use of Resources assessment, which was linked to the criteria set out above, I was able to issue an unqualified conclusion, stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources.

Specific risk-based work

- 63** I carried out the following specific pieces of work to provide me with assurance for my Use of Resources assessment in the following areas.
- Follow up of the 2007/08 Health Inequalities review.
 - Follow up of the 2007/08 review of Performance Management which will be reported with Managing Performance.
 - Follow up of the 2007/08 review of the proposed waste PFI scheme.
 - Review of the Council's response to the assessment of Children's Services.
 - Review of progress made by the Council to improve financial and budgetary controls in Highways.

Health Inequalities – Follow-up of 2007/08 Review

- 64** The Council continues to play a lead role in identifying and addressing health inequalities across Essex. This work is being delivered through partnership working which has resulted in significant investment in the areas of greatest concern.
- 65** The outcome of this investment is to improve the lives of many people living in some of the most deprived areas in England, including an increased life expectancy. Some of the improvements will not be evident for many years due to the long term nature of the issues the Council is tackling such as access to improved education, diet and exercise; however the Council needs to monitor the success of initiatives which support reducing health inequalities.
- 66** An action plan was agreed following our review in 2007/08 and we attended key partnership meetings across Essex to monitor action being taken.
- 67** We will continue to monitor progress made against this challenging agenda with further follow up work in 2009/10.

Waste Private Finance Initiative- Follow up of 2007/08 Review

- 68 Waste management is one of the biggest challenges facing Essex, both now and in the future. Through government targets and legislation there is a need to reduce some or all of the waste being sent to landfill. The County Council and the 12 district and borough councils in Essex have formed an Essex Waste Partnership. This now also includes Southend-on-Sea Borough Council, a unitary authority that clearly sees the benefits of working closely with this group. The Partnership is pursuing a long term waste solution through Private Finance Initiative (PFI) funding. The Council is now mid-way through a process of looking at a long term waste solution funded by a PFI.
- 69 Stronger support is now in place to deliver this major project. Good project management of the PFI and a clear governance structure is in place. Key stakeholders are well informed of the progress and reasoning for the new approach to waste disposal. Good financial management is also in place for the project. The needs for future waste disposal are clearly understood and the future waste PFI is likely to improve the service provided.

Review of the Council's Response to the assessment of Children's Services

- 70 In 2007, Children's Services declined in its overall performance rating. One of the reasons for the decline was that performance management arrangements in the Council's Department of Children, Schools and Families (SCF) did not identify underperformance and report it effectively to the corporate centre.
- 71 A review of corporate performance systems identified that the effectiveness of the Council in addressing poor performance was mixed. Issues with the comparative performance of SCF were not identified. In response an improvement board was established and consultants used to develop improved performance processes and provide additional capacity.
- 72 The Joint Area Review (JAR) of children's services completed in November 2008 and published in 2009 judged the contribution of services to improving outcomes for children and young people at risk or requiring safeguarding, as inadequate. The review identified that performance management was adequate with clarity over high-level targets and the approach to monitoring, reporting and managing performance against them. However, target setting was not robust in service planning. The Department is implementing an action plan to address the issues raised in the JAR report including its approach to performance management.
- 73 The Council is effectively prioritising performance management and improvement in SCF although it is not recognised formally as a top risk in the risk register for the Council. SCF has invested in developing a performance culture which is embedded across most of the department. Staff appraisals effectively support performance management although individual targets are not consistently specific and achievable. Robust performance information is monitored and informs performance improvements. A corporate framework for business and service planning is delivering greater consistency in plans but there is insufficient use of measurable outcomes for children and young people.

Value for money and use of resources

- 74 Data quality is improving. The Council is investing in information technology to support performance management. Target setting is improving but remains inconsistent in departmental plans.
- 75 Performance management is now identifying the performance position and leading to performance improvement but sometimes from a lower base than first identified. The integration of performance and financial reporting is at an early stage and impact variable. Performance reporting of equalities and diversity is variable.
- 76 The performance management role of the Children and Young People Strategic Partnership is improving but from a low base. The Partnership delivers insufficient challenge to performance issues and capacity remains an issue for improving performance. Performance management of partnership working is at an early stage and inconsistent.

Highways Performance Management and Budgetary Control

- 77 In 2007/08 the Council overspent its Highways and Transport budget. This led to an analysis of how well budgets were managed within the Highways Department and the need for improvement in budget management.
- 78 Expenditure in the Highways Department is monitored and managed better than in previous years. The overall monitoring of finances now resides formally with a Highways Finance Board. This consists of the Director, key personnel from the Highways departments and dedicated financial support. This group meets monthly to assess both revenue and capital spend against expected outturn. This information enables the Board to monitor key issues and develop actions to resolve problems promptly. The formal process of monitoring detailed information through the Board on monthly is supporting the delivery of a balanced budget at the end of the financial year.
- 79 Financial management processes and procedures are much improved within the Department. A significant change is the implementation of a dedicated highways finance team. This team supports and advises the Director and highways professionals on financial issues. While responsibility for financial outturn remains with the Director, the support given enables a better management of the financial transactions taking place. These new methods of managing the financial aspects of Highways service delivery are reducing the likelihood of high levels of over or under spend through improved management information and monitoring.
- 80 Monitoring and management of capital expenditure has improved within the Department. As with revenue finances, dedicated support is now in place for the Highways Director and his department. While improvements to processes are evident it is difficult to fully see the impact these are having on the overall management of capital expenditure.
- 81 Corporate monitoring of Highways expenditure and performance is improving. Quarterly reports to Cabinet detail both performance and financial management information. A Directorate leadership team also reviews the same performance and financial management information on a monthly basis. As a result budgets are better managed than in previous years.

Closing remarks

- 82** I have discussed and agreed this letter with the Chief Executive and the Executive Director of Finance. I will present this letter at the Audit Committee on 1 February 2010 and will provide copies to all Council Members.
- 83** Further detailed findings, conclusions and recommendations in the areas covered by our audit are included in the reports issued to the Council during the year.

Table 3

Report	Date issued
Audit and inspection plan	May 2008
Supplementary Fee Letter	December 2008
Corporate Assessment	March 2009
Interim Audit Report	July 2009
Annual Governance Report	September 2009
Opinion on financial statements	September 2009
Value for money conclusion	September 2009
Use of resources report	November 2009
Organisation Assessment and Managing Performance	December 2009
Annual Audit Letter	December 2009

- 84** The outcome of our audit on grant claims submitted by the Council will be reported in January 2010.
- 85** The Council has taken a positive and constructive approach to our audit. I wish to thank the Council staff for their support and co-operation during the audit.

Paul King
District Auditor
December 2009

Appendix 1 – Action plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
9	R1 The Council should ensure that sufficient resources are directed towards addressing control weaknesses in material financial systems and producing accounts that are free from material error.					
9	R2 The Council should continue to monitor progress against the IFRS implementation plan through the Audit Committee and ensure that the implications of IFRS on financial planning are widely understood.					

The Audit Commission

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

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