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MEETING: AUDIT AND GOVERNANCE COMMITTEE

DATE: Wednesday 15th December, 2010

TIME: 3.00 pm

VENUE: Town Hall, Bootle

Member	**Substitute**
Councillor	Councillor
Brady (Chair)	Tweed
Friel (Vice-Chair)	McGinnity
Brennan	Mahon
Lord Fearn	Byrne
Maher	Fairclough
McIvor	Sir Ron Watson
Parry (Spokesperson)	Porter
Robertson	Brodie - Browne
Shaw (Spokesperson)	C Mainey
Tonkiss	S Mainey

COMMITTEE OFFICER: Steve Pearce
Head of Committee and Member Services
Telephone: 0151 934 2046
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E-mail: steve.pearce@sefton.gov.uk

If you have any special needs that may require arrangements to facilitate your attendance at this meeting, please contact the Committee Officer named above, who will endeavour to assist.

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A G E N D A

1. Apologies for absence

2. Declarations of Interest

Members and Officers are requested to give notice of any personal or prejudicial interest and the nature of that interest, relating to any item on the agenda in accordance with the relevant Code of Conduct.

3. Minutes of Previous Meeting (Pages 5 - 10)

Minutes of the meeting held on 29 September 2010

4. External Audit - Annual Audit Letter 2009/10 (Pages 11 - 22)

Report of the External Auditors, PricewaterhouseCoopers

5. External Audit - Annual Audit Plan 2010/11 (Pages 23 - 50)

Report of the External Auditors, PricewaterhouseCoopers

6. Treasury Management 2010/11 - Mid Year Review (Pages 51 - 64)

Report of the Interim Head of Corporate Finance and ICT Strategy

7. Exclusion of Press and Public

To consider passing the following resolution:

That, under Section 100A(4) of the Local Government Act, 1972, the press and public be excluded from the meeting for the following items of business on the grounds that they involve the likely disclosure of exempt information as defined in Paragraph 3 of Part 1 of Schedule 12A to the Act. The Public Interest Test has been applied and favours exclusion of the information from the Press and Public.

8. Internal Audit Plan 2010/11 Performance Report - April to November 2010 (Pages 65 - 82)

Report of the Interim Head of Corporate Finance and ICT Strategy

9. Internal Audit Fraud Report (Pages 83 - 88)

Report of the Interim Head of Corporate Finance and ICT Strategy

10. Corporate Risk Register - Update

Report of the Interim Head of Corporate Finance and ICT Strategy

THIS SET OF MINUTES IS NOT SUBJECT TO "CALL-IN"

AUDIT AND GOVERNANCE COMMITTEE

**MEETING HELD AT THE TOWN HALL, BOOTLE
ON 29 SEPTEMBER 2010**

PRESENT: Councillor Brady (in the Chair)

Councillors Brennan, Lord Fearn, Maher, McIvor, Parry, Shaw and Tonkiss

ALSO PRESENT: Mr. D. Newman and Mr. S. Baron from PricewaterhouseCoopers

10. APOLOGIES FOR ABSENCE

Apologies for absence were received from Councillors Friel and Robertson and Brodie-Brown and McGinnity (Substitute Members).

11. DECLARATIONS OF INTEREST

The following declaration of interest was made.

Member	Minute No.	Reason	Action
Councillor Brennan	20 – Corporate Risk Register	Personal – His employer is referred to in the report	Took part in the consideration of the item and voted thereon

12. MINUTES

RESOLVED:

That the Minutes of the meeting of this Committee held on 30 June 2010 be confirmed as a correct record.

13. STATEMENT OF ACCOUNTS 2009/10 - ADJUSTMENTS/EXTERNAL AUDITOR'S COMMENTS

Further to Minute No. 6 of the meeting held on 30 June 2010, the Committee considered a report by the Interim Head of Corporate Finance and ICT Strategy which identified proposed amendments to the 2009/10 Statement of Accounts for consideration and approval following the completion of the audit by the External Auditors, PricewaterhouseCoopers (PwC). The report included the "Letter of Representation" from the Council to the External Auditors for approval and the amended Annual Governance Statement.

The Council, or nominated Committee charged with the responsibility for governance must approve amendments to the Statement of Accounts following the completion of the annual audit. The Audit and Governance Committee had been delegated with this responsibility and consequently must approve the adjustments to the accounts for 2009/10 by 30 September 2010.

The Council was also required to provide a Letter of Representation to the External Auditor at the conclusion of the audit. This letter acknowledged the Council's responsibilities in preparing the Accounts and provided the assurance to the External Auditor that no new information or decisions had been taken that would materially affect the Statement of Accounts for the year. The letter had to be signed by the Chair and Chief Executive once approved.

The report also included the External Auditor's Annual Governance Report which covered the audit of the Statement of Accounts and the Use of Resources Value for Money work. Mr. D. Newman from PwC was present and provided Members with a brief summary of the issues contained in the report and answered their questions as appropriate. He referred in particular to the assurance sought from management with regard to the recovery by the Council of income in respect of the VAT Shelter Agreement with One Vision Housing.

A discussion took place with regard to the monies that remain outstanding from One Vision Housing (OVH) totalling £7.9m. Mr. D. Newman indicated that whilst OVH had confirmed the agreement of the liability with PwC, the receipt of cash or the amount being received within a solicitors holding account is required to provide appropriate evidence of the recoverability of the monies. Either piece of evidence would allow PwC to provide an unqualified opinion on the financial statements and PwC would continue to work with management to resolve the matter. It was noted that the need to await this further evidence means that the Council would miss the deadline of 30 September 2010 for completing the audit of the financial statements.

Mr. D. Newman also indicated that PwC had been made aware of a potential objection to the financial statements from a member of the public. PwC had carried out investigatory work along with management to provide the evidence requested with regards to the potential objection and a deadline for receipt of this objection had been agreed which would delay the completion of the audit. PwC have concluded that the nature of the objection expected would not indicate a material error in the financial statements, so this matter would not delay the issue of the audit opinion.

RESOLVED: That

(1) the amendments to the Statement of Accounts for 2009/2010, be approved;

(2) the amendments to the Annual Governance Statement for 2009/10 be approved;

(3) the comments of PricewaterhouseCoopers LLP, be noted; and

(4) the Letter of Representation be approved and the Chair and Chief Executive be authorised to sign it on the Council's behalf.

14. ANNUAL TREASURY MANAGEMENT REPORT 2009/10

Further to Minute No. 56 of the meeting of the Cabinet held on 8 July 2010, the Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy which provided details of the Treasury Management activities undertaken in 2009/10 covering the following issues:

- borrowing strategy and practice
- the Council's current Debt Portfolio
- compliance with Treasury Limits
- compliance with Prudential Indicators
- investment strategy and practice

RESOLVED:

That the Annual Treasury Management Report for 2009./10 be noted.

15. TREASURY MANAGEMENT 2010/11 - FIRST QUARTER UPDATE

The Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy which provided details of the Treasury Management activities undertaken in the current financial year up until 30 June 2010, in accordance with the Council's Treasury Management Policy and Strategy 2010/11.

RESOLVED:

That the report be noted.

16. INTERNAL AUDIT PLAN 2010/11 - OCTOBER 2010 TO MARCH 2011

The Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy on the Internal Audit Annual Plan for the second six months of 2010/11 which had been drawn up in accordance with the CIPFA Code of Practice for Internal Audit. The auditable areas in the Annual Plan had been identified for Departments/Services and an Audit Risk Assessment had been applied which assists in prioritising audit work relative to risk.

The report also provided details of the School's Internal Audit Plan for 2010/11 to 2012/13 for the Audit and Financial Management Standard in Schools Assessment.

RESOLVED: That

(1) the Internal Audit Plan for the second six months of 2010/11 be approved; and

(2) the Schools Internal Audit Plan for 2010/11 to 2012/13 be approved.

17. EXCLUSION OF PRESS AND PUBLIC

RESOLVED:

That, under Section 100A(4) of the Local Government Act 1972, the press and public be excluded from the meeting for the following item of business on the grounds that it would involve the likely disclosure of exempt information as defined in Paragraphs 3 and 7 of Part 1 of Schedule 12A to the Act. The Public Interest Test has been applied and favoured exclusion of the information from the press and public.

18. INTERNAL AUDIT PLAN 2010/11 PERFORMANCE REPORT - APRIL 2010 TO AUGUST 2010

The Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy which provided a summary of internal audit work undertaken during the period April to August 2010. The Committee was required to be appraised of the Internal Audit and Benefit Fraud Investigation Team work as part of its review of the internal control environment and formulation and overall governance arrangements.

RESOLVED:

That the report be noted.

19. INTERNAL AUDIT FRAUD REPORT

The Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy which provided a summary of the proactive and reactive anti-fraud and investigation work undertaken during the period April to August 2010 by the Internal Audit Team.

RESOLVED:

That the report be noted.

20. CORPORATE RISK REGISTER - UPDATE

The Committee considered the report of the Interim Head of Corporate Finance and ICT Strategy which provided an update on the Corporate Risk Register.

RESOLVED: That

(1) the updated Corporate Risk Register be approved;

(2) the Operational Services Director be requested to review the risk assessment score in respect of the risk of an overspend on the provision of the Specialist Transport Service; and

(3) the Chief Internal Auditor be requested to review the format of future reports on the Corporate Risk Register, including reference to any changes made to risk assessment scores.

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Government and Public Sector

Sefton Metropolitan Borough Council

2009/10 Annual Audit Letter

November 2010

PricewaterhouseCoopers

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The Members
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28 November 2010

Ladies and Gentlemen

We are pleased to present our Annual Audit Letter summarising the results of our 2009/10 audit. We look forward to presenting it to Members on 15 December 2010.

Yours faithfully

PricewaterhouseCoopers LLP

Peter Chambers
Government and Public Sector
PricewaterhouseCoopers LLP

Contents

Section

Code of Audit Practice and Statement of Responsibilities of Auditors and of Audited Bodies

The 'Statement of responsibilities of auditors and of audited bodies' issued by the Audit Commission in April 2008 applies to our 2009/10 audit of Sefton Metropolitan Borough Council under the Code of Audit Practice for Local Government Bodies issued by the Audit Commission in July 2008. A copy of the statement is available from the Chief Executive of Sefton Metropolitan Borough Council. The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is expected of the audited body in certain areas. Our reports and management letters are prepared in the context of this Statement and the Code of Audit Practice. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.

Introduction

The purpose of this letter

The purpose of this letter is to provide a high level summary of the results of the 2009/10 audit work we have undertaken at Sefton Metropolitan Borough Council that is accessible for Members and other interested stakeholders.

We have already reported the detailed findings from our audit work to those charged with governance in the following reports:

- External audit progress report
- Audit opinion for 2009/10 financial statements, incorporating the conclusion on value for money
- Report to those charged with governance (ISA (UK&I) 260)

The matters reported here are those that we consider are most significant for the Authority and a summary of the key recommendations that we have made can be found in Appendix A.

Scope of work

Our audit work is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The Authority is responsible for preparing and publishing its financial statements, including the Annual Governance Statement. It is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- forming an opinion on the financial statements;
- reviewing the Authority's Annual Governance Statement;
- forming a conclusion on the arrangements that the Authority has in place to secure economy, efficiency and effectiveness in its use of resources; and
- undertaking any other work specified by the Audit Commission.

Our 2009/10 audit work has been undertaken in accordance with the Audit Plan that we issued on 1 December 2009.

Audit findings

Accounts

We audited the Authority's accounts in line with International Standards on Auditing (UK & Ireland) and issued an unqualified audit report on 26 October 2010.

We identified the following key issues from our audit of accounts:

Accounting matters:

a) Delayed financial statements signing - One Vision Housing VAT Shelter Income

Upon the transfer of the Council's housing stock to One Vision Housing (OVH) a VAT shelter agreement was signed between the parties. The agreement entitles the Council to a share of the VAT reclaimed by OVH on housing capital expenditure post transfer. Included within the 2009/10 financial statements is accrued income of £5,671,000 (£2,300,000 in 2008/09). The Council has not received any monies, nor provided against this debtor totalling £7,971,000. As at 31 March 2010 £4,157,000 was past the payment date as per the agreed payment schedule.

At 30 September 2010 the Council had not received any of the monies outstanding and were unable to provide the required evidence to support the recoverability of the debtor balance. As a result of this the signing of the financial statements was delayed. The matter has since been resolved, and an unqualified audit report was issued on 26 October 2010.

b) Asset re-classification from Investment Properties to Other Land and Buildings

During the course of the audit it was identified by officers that an asset included within non-operational assets (investment properties) had a valuation incorrectly applied to it. The Council had capitalised expenditure on the asset against the building and revalued the land within its fixed asset register. The resulting adjustment required the land revaluation to be reversed for £5,300,000. Management have adjusted the accounts to transfer the land valued at £350,000 from Investment Properties to Other Land and Buildings.

The property valuation was then applied to the total asset (i.e. the land and the capital expenditure on the building) with a resulting impairment charge of £1,209,000 being charged to the Income and Expenditure Account.

c) Unrecorded impairment in the draft financial statements

Review of the revaluations of assets performed by the Council identified that the draft financial statements incorrectly excluded the impairment of Ainsdale High School. The result of correcting the error was a charge to the Income and Expenditure Account and a reduction in the carrying value of Other Land & Buildings of £5,815,000.

d) Investment to cash re-classification

Audit of the financial statements identified that the Council had included within investments £16,434,000 (£9,095,000 in 2008/09) of amounts held in overnight lodgements. As the balance is in overnight accounts this should be included as cash within the financial statements. The Council amended its financial statements to reflect this.

Systems of internal control

a) Payments to private residential care homes

The Council is liable for the provision of care for persons within residential care homes. The Council incurs expenditure based on its known cases of care within a care home, with the care home being required to confirm post payment that the individuals concerned continue to be residents in the home. Review of these payments identified that the Council does not always receive confirmation back from the care home and instances have arisen where overpayments had been made due to changes to the care provided, or the people within the care homes. We have recommended that the Council reviews its procedures surrounding payments to residential care homes and will reflect this area in our 2010/11 audit plan.

b) The Council has an electronic procurement system (I-Proc) that directly interfaces with the general ledger system. This system has a catalogue of approved suppliers and controls over creating new suppliers, automated controls that ensure order requisitions receive approval from appropriate manager before the order is placed, inbuilt authorisation limits and online recording of goods being received accompanied by automatic matching of invoices to purchase orders. Management estimate that the I-Proc system is currently used for only approximately 5 to10% of purchases, with the majority of remaining procurement relying on paper based procurement and authorisation controls. Control weaknesses were also identified within the current accounts payable process. These are addressed through the implementation of the I-Proc system.

We have recommended the Council should drive forward the use of the I-proc system, with the aim of processing the vast majority of procurement through this system, as this would address the risks identified. Increased use of the system will also assist the Council in achieving savings through the use of preferred suppliers and tendering procedures. Specific targets and timeframes for usage should be put in place, with senior management involvement to ensure that these milestones are met.

Information Technology General Controls

a) The Council has its own IT internal audit function and approximately 150 days of IM&T reviews were planned for 2009/10, based on a risk based plan. However Internal Audit has not completed the planned work during the year, resulting in a risk that recognised risks and control failures may go undiscovered.

b) There is only one data centre location which represents a single point of failure should a major incident occur affecting the Council's significant systems and applications. The loss of access to the data centre and core applications would significantly impact on the Council's ability to provide the necessary services. Disaster recovery arrangements for the data centre should be taken into consideration as part of the Council's business continuity planning arrangements to ensure that services can continue to be provided in the event of any incident affecting access to core applications.

Objection to the Accounts

We have received a formal objection to the accounts under sections 8 and 17 of the Audit Commission Act 1998. The objection relates to entries in the housing market renewal account. We have conducted some preliminary work, and as a result concluded that the sums involved were not material to the financial statements. However we have not yet reached a view about the objection, and until we have done so we will not be able formally to complete our audit for the year.

Conclusion on Use of Resources

We were required to issue a conclusion on the adequacy of the Authority's arrangements for ensuring economy, efficiency and effectiveness in its use of resources.

We issued an unqualified conclusion on the Authority's arrangements for its Use of Resources on 26 October 2010.

Comprehensive Area Assessment

Following the government announcement to abolish comprehensive area assessment (CAA), all work on Use of Resources for Comprehensive Area Assessment ceased at the end of May 2010. We reported detailed findings from the work undertaken to that date within the Report to those charged with Governance (ISA (UK&I) 260) presented to the Audit Committee on 29 September 2010.

Approach to local value for money audit work from 2010/11

Given the scale of the pressures facing public bodies in the current economic climate, the Audit Commission has reviewed its work programme for 2010/11 onwards. As part of this exercise, the Commission has been discussing possible options for a new approach to local value for money (VFM) audit work with key national stakeholders. From 2010/11 we will therefore apply a new, more targeted and better value approach to our local VFM audit work. This will be based on a reduced number of reporting criteria specified by the Commission, concentrating on:

- securing financial resilience; and
- prioritising resources within tighter budgets.

We will determine a local programme of VFM audit work based on our audit risk assessment, informed by these criteria and our statutory responsibilities. We will no longer make annual scored judgements relating to our local VFM audit work. Instead we will report the results of all the local VFM audit work and the key messages for the audited body in our annual report to those charged with governance and in a clear and accessible annual audit letter.

Annual Governance Statement

Local Authorities are required to produce an Annual Governance Statement (AGS) which is consistent with guidance issued by CIPFA / SOLACE. The AGS was included in the financial statements.

We reviewed the AGS to consider whether it complied with the CIPFA / SOLACE guidance and whether it is misleading or inconsistent with other information known to us from our audit work. We found no areas of concern to report in this context.

Audit Plan

We presented our 2009/10 Audit Plan to Members on 1 December 2009. Other than curtailment of CAA Use of Resources work in May 2010, the plan has not been changed in any significant respect. In this report we comment only on those areas where we believe we need to communicate with those charged with governance.

Agenda Item 4

Audit fees update for 2009/10

We reported our audit fee proposals in the fee letter issued on 2 March 2009. Our fees charged were:

	2009/10 Outturn	2009/10 Fee proposal
Financial Statements and Whole of Government Accounts	£179,246	£175,746
Use of Resources / VFM conclusion	£77,491	£77,491
Data Quality	£30,808	£30,808
Total audit fee	**£287,545**	**£284,045**

We reported within our Report to those charged with Governance (ISA (UK&I) 260) that there would be a variation to our fee of £3,500 in relation to the audit of the financial statements due to the amount of additional work we had been required to do on the accounting treatment for the PFI project.

Matters for future accounting periods

Transition to International Financial Reporting Standards (IFRS)

The Code of Practice on Local Authority Accounting in the United Kingdom 2010. will apply to the 2010/11 financial statements. The new Code is the first to be prepared under IFRS.

The Authority needs to ensure that it has a good grasp of the changes to accounting requirements under the new Code. The Authority should now have systems in place to collect and process the information needed to prepare IFRS based accounts and should at this stage be well progressed with preparation of comparative information as at 1 April 2010 for next year's financial statements.

We have discussed with management the Council's progress with IFRS transition is and agreed that we will provide support to the Council throughout the transition. We will seek to carry out an early review of the restated comparatives and draft financial statements. Whilst management are continuing to review changes that arise under adoption of IFRS, the Council are behind against the initial project plan.

In our experience the key features of a successful IFRS conversion project have proven to be:

- completed impact analysis and comprehensive conversion plans;
- the commitment of key stakeholders in the organisation;
- operational steering and technical groups;
- cabinet/audit committee oversight;
- regular progress reporting against the plan;
- the necessary project management resources; and
- appropriate and timely training for all members and officers with IFRS involvement.

Clarity International Standards on Auditing (UK & Ireland)

We will be required to apply Clarity International Standards on Auditing (ISAs) for UK and Ireland to next year's accounts audit for the first time.

The Clarity ISAs overhaul existing auditing standards, both improving clarity of existing standards and introducing new requirements designed to improve audit quality and financial reporting.

A number of standards have been completely revised. There will be approximately one-third more explicit requirements applying to the Authority audit next year as well as other new requirements that apply to the authority group audit.

The actual impact on cost of the audit will depend on a variety of factors, including how effectively we can work with you to obtain additional information needed to enable us to perform the required procedures.

Summary of recommendations

Risk	Recommendation	Management Response	Target Implementation Date
High	We recommend the Council reviews its procedures surrounding payments to residential care homes. We are likely to include this as a specific risk in our 2010/11 Audit Plan.	Senior Officers have already met with Internal Audit to agree on the topics to be covered in a Community Care Audit. This matter had already been identified as a weakness and will be corrected with constructive assistance from Audit Officers following the publication of the Internal Audit findings.	November 2010 Jointly between Colin Speight (Principal Manager, Adult Social Care) and Janice Bamber (Chief Internal Auditor)
High	The Council should take action to drive forward the use of the I-proc system, with the aim of processing the vast majority of procurement through this system. The risks identified are addressed through the use of I-Proc for the Council's purchasing requirements.	Agreed. Plans are in place to expand the roll-out of I-procurement across the Council; this project is being managed by the Central Procurement Unit.	During 2010/11 Tommy Crawford
High	Control weaknesses identified within the current accounts payable process are addressed through the implementation of the I-Proc system noted above.	Agreed. Control weaknesses will be addressed through the roll-out of I-procurement across the Council; this project is being managed by the Central Procurement Unit.	During 2010/11 Tommy Crawford
High	The Council should monitor the delivery of the IM&T internal audit plan to ensure that information risks are being appropriately managed and addressed.	A number of IT reviews were undertaken in 2009/10, these included reviews that were part of the Audit Plan for 2009/10. However, there was not as much planned work undertaken as originally envisaged, the reasons for this are twofold:- i) Arvato government services are responsible for the delivery of IT Services as part of the Contract in place. As part of that contract they are required to provide certain assurances to the Council that they meet requirements within that contract. The Council's Internal Audit Section have included an item in the 2010/11 Audit Plan to review the IS Client Function and the assurance that is provided to them as part of the contract requirements. With regard to the actual review of IT systems operated by arvato, an exercise is currently being undertaken to identify how this task will be performed. The Internal Audit Section has also included in the Audit Plan for 2010/11 a number of reviews of compliance within the Council and also continues to undertake ad hoc work were required to provide advice on control areas and risk in relation to areas related to IT.	March 2011 Janice Bamber (Chief Internal Auditor)

Risk	Recommendation	Management Response	Target Implementation Date
		ii) The IT Audit Manager was acting up into a support / audit advice role for the then Acting Chief Internal Auditor as he had minimal experience in the area of Audit, this impacted on the provision of IT audit as this was not planned for at the beginning of the year.	
High	Disaster recovery arrangements for the data centre should be taken into consideration as part of the Council's business continuity planning arrangements to ensure that services can continue to be provided in the event of any incident affecting access to core applications.	The new data centre has been built to a high standard and has all the appropriate protection and security facilities. Data is backed up to tape which are taken off site. Arvato are looking at an alternative to Bootle Town Hall as the storage centre for the DR tapes. Arvato have submitted costs to SMBC for the construction of a secondary data centre facility to provide hot standby for the 20 critical applications. Sefton's Strategic Leadership Team is due to discuss proposals in the week commencing 20 September 2010.	To be agreed. Linda Price (ICT and Contract Monitoring Client Manager)

The matters reported here are those that we consider are most significant for the authority. We provide an annual summary of recommendations to the Director of Finance and his team. This is also a requirement of the Audit Commission's Standing Guidance for Auditors. Our 2009/10 annual summary of recommendations included 27 recommendations.

Agenda Item 5

Government and Public Sector

Sefton MBC

2010/11 Audit Plan
14 December 2010

PRICEWATERHOUSECOOPERS

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29 November 2010

Ladies and Gentlemen,

We are pleased to present to you our Audit Plan, which includes an analysis of key risks, our audit strategy, reporting and audit timetable and other matters. Discussion of our plan with you ensures that we understand your concerns and that we agree on our mutual needs and expectations to provide you with the highest level of service quality. Our approach is responsive to the many changes affecting Sefton MBC.

We would like to thank Members and officers of the Council for their help in putting together this Plan.

If you would like to discuss any aspect of our Audit Plan please do not hesitate to contact either Peter Chambers or Stuart Baron.

Yours faithfully,

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP

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Contents

In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and of audited bodies'. It is available from the Chief Executive of each audited body and on the Audit Commission's website.

The purpose of the statement is to assist auditors and audited bodies by explaining where the responsibilities of auditors begin and end and what is to be expected of the audited body in certain areas.

Our reports are prepared in the context of this Statement. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the audited body and no responsibility is taken by auditors to any Member or officer in their individual capacity or to any third party.

Introduction

The purpose of this plan

Our Audit Plan has been prepared to inform the officers and Members of Sefton MBC (the Council) about our responsibilities as your external auditors and how we plan to discharge them.

We issued our audit fee letter, setting out our indicative fees for 2010/11, on 15 March 2010 in accordance with Audit Commission requirements. This plan sets out in more detail our proposed audit approach for the year.

Every Council is accountable for the stewardship of public funds. The responsibility for this stewardship is placed upon the Members and officers of the Council. It is our responsibility to carry out an audit in accordance with the Audit Commission's Code of Audit Practice (the Code).

Based upon discussion with management and our understanding of the Council and the local government sector, we have noted in the next section recent developments and other relevant risks. Our plan has been drawn up to consider the impact of these developments and risks.

Period covered by this plan

This plan outlines our audit approach for the period 1 April 2010 to 31 March 2011, including the 2010/11 final accounts audit which we will undertake in July/August 2011.

Code of Audit Practice and Statement of responsibilities of auditors and of audited bodies

We perform our audit in accordance with the Audit Commission's Code of Audit Practice (the Code) which was last updated in March 2010. This is supported by the Statement of Responsibilities of auditors and of audited bodies (the Statement) which was updated in March 2010. Both documents are available from the Chief Executive or the Audit Commission's website.

Risk assessment

Planning of our audit

We have considered the Council's operations and have assessed the extent to which we believe there are potential business and audit risks that need to be addressed by our audit. We have also considered our understanding of how your control procedures mitigate these risks. Based on this assessment we have determined the extent of our financial statements and use of resources audit work.

It is your responsibility to identify and address your operational and financial risks, and to develop and implement proper arrangements to manage them, including adequate and effective systems of internal control. In planning our audit work, we assess the significant operational and financial risks that are relevant to our responsibilities under the Code and the Audit Commission's Standing Guidance. This exercise is only performed to the extent required to prepare our Plan so that it properly tailors the nature and conduct of audit work to your circumstances. It is not designed to identify all risks affecting your operations nor all internal control weaknesses.

In this plan we detail those areas which we consider to be significant risks relevant to our audit responsibilities and our response to those risks. Significant risks are those risks requiring special audit attention in accordance with auditing standards.

In addition, we also identify other risks affecting the Council and our response to these risks.

Our response includes details of where we are intending to rely upon internal controls, other auditors, inspectors and other review agencies and the work of internal audit, if applicable.

Risk assessment results

The following table summarise the results of our risk assessment and our planned responses.

Risks	Audit approach
Significant Risks	
Revenue Recognition There is a risk that the Council could adopt accounting policies or treat income and expenditure transactions in such as way as to lead to material misstatement in the reported revenue position.	We will understand and evaluate controls relating to this risk We will consider the accounting policies adopted by the Council and subject income and expenditure to the appropriate level of testing to identify any material misstatement.
Management Override of Controls In any organisation, management may be in a position to override the financial controls that you have in place. A control breach of this nature may result in a material misstatement. For all of our audits, we are required to consider this significant risk and adapt our audit procedures accordingly.	We will understand and evaluate internal control processes and procedures as part of our planning work We will review the appropriateness of journals processed during the year. We will also look carefully at any management estimations and consider if they are subject to bias. We will design and perform procedures in relation to the business rationale for significant transactions. Our audit procedures are also planned to include an unpredictable element that varies year on year.
2010/11 – the first year of reporting under IFRS The 2010/11 financial statements will be prepared in accordance with IFRS. The 2009/10 financial statements will need to be restated under IFRS as comparatives in the 2010/11 financial statements. As the implementation of IFRS requires the financial statements to be prepared in accordance with a new set of financial standards, there is an increased risk that the accounts could be misstated. Our early work has identified that the Council is behind in its plans to implement IFRS with particular audit risks identified in the following areas: • First time adoption and accounting policies • Leases • Fixed asset accounting • Group accounts • Employee benefits	We are working closely with the Council to ensure that you are aware of the main differences between IFRS and UK GAAP and to resolve any accounting issues on a timely basis. We will perform a review of draft restated statements to identify disclosure issues at the planning stage of the audit. We will communicate the results of this review to management so they may take action to address issues in advance of the final audit. At the final audit stage we will perform an independent 'hot review' of the financial statements and disclosures.

Risks	Audit approach
Elevated Risks	
Increasing Pressure on Financial Position The economic climate has caused falls in the value of many land and building assets, and the risk of such assets being overvalued on the balance sheet remains high. We will expect the Council to have carried out impairment reviews to ensure that assets are not overvalued at the year end, and to process downward revaluations where appropriate. Increased pressures on budgets The Council is likely to be experiencing increased pressures on many of its budgets as economic conditions have worsened. Budget holders may feel under pressure to try to push costs into future periods, or to miscode expenditure to make use of resources intended for different purposes. Local government bodies are expected to make significant efficiency savings over the next three years. There is a risk that savings plans may not be robust or based on long term solutions which could result in short term, year end actions to ensure that the targets are met. There are also risks in relation to financial reporting, that the requirement to report particular financial results overrides best financial reporting practice. Increased demand for services The Council is likely to be experiencing increased demand for its services at a time when funding service provision may be under strain. This may lead to increased risks related to the processing and documentation of financial data.	We will review the procedures the Council have in place for reviewing its estate value and ensure that the Council are performing revaluations in line with IFRS5, whilst considering the Council's procedures for identifying and assessing potential downward revaluations. We will review the accounting treatment of any downward revaluations as part of our audit of the financial statements. We will review the Council's budget monitoring processes to identify any areas of concern. We will also bear these risks in mind when carrying out cut-off testing. As part of our use of resources work as well as our work on financial standing, we will consider the entity's savings plans and consider their robustness. We will also consider the accounting implications of any savings plans and would welcome early discussion of any new and unusual proposals. In particular, we will consider the impact of the efficiency challenge on the recognition of both income and expenditure. As auditors we will discuss with management the costs pressures that are identified during the financial year and discuss with management the actions they plan to manage such demands.
Valuation of Assets and Revaluation Reserve The economic climate has caused falls in the value of many land and building assets, and the risk of such assets being overvalued on the balance sheet remains high. We will expect the Council to have	We will review the procedures the Council have in place for reviewing its estate value and ensure that the Council are performing revaluations in line

Risks	Audit approach
carried out impairment reviews to ensure that assets are not overvalued at the year end, and to process downward revaluations where appropriate. The introduction of the revaluation reserve in 2007/08 will have ongoing implications for the treatment of assets revalued during the year. Particular care will need to be taken over the treatment of any downwards revaluations which exceed revaluation gains recognised since the start of 2007/08. These will need to be charged to the Income and Expenditure Account.	with IFRS5, whilst considering the Council's procedures for identifying and assessing potential downward revaluations. We will review the accounting treatment of any downward revaluations as part of our audit of the financial statements.
Pericles to Northgate Data Migration The Council are transferring its revenue and benefits system from Pericles to Northgate during the year. Risks exist in ensuring that the data from the existing system is completely and accurately transferred to the new Northgate system.	We are working with the Arvarto, the project team and internal audit to ensure that we and the Council obtain the required assurance over the accuracy and completeness of the data transferred.
Normal Risks	
Treasury Management The collapse of the Icelandic banks in 2008/09, and the potential losses suffered by numbers of local authorities on apparently safe deposits, has highlighted the importance of robust treasury management procedures and active and informed management of risk. Weaknesses in this area could lead to losses of assets invested, or held as cash deposits. Risks may not be adequately disclosed in the notes relating to financial instruments.	We will update our understanding of the Council's treasury management procedures, and perform any work necessary to assess their adequacy. We will review the financial instruments disclosures to assess whether the Council has taken appropriate steps to understand the instruments and the related risks, and adequately reflected these in the notes to the accounts.
Prudential Framework The Council has adopted an incremental approach to taking up the freedoms and flexibilities offered by the Prudential Framework for the delivery of services and capital investment. It is our understanding that the Council will continue to develop arrangements to manage the new risks and take advantage of the new opportunities offered by the Framework in 2010/11. For example, many authorities have yet to enter into substantial amounts of prudential borrowing that is supported by future projections of income generation/efficiency savings rather than Government funding. In continuing to develop arrangements, the Council will need to consider the effectiveness of its controls over expenditure and its plans for developing / extending prudential borrowing. Where prudential borrowing is planned, the Council needs to be assured that this is based on robust projections of affordability.	We will review the Council's borrowing levels against the prudential borrowings limits set by management. We will discuss with management the Council's intentions to extent its current borrowings level.
PFI The Council has entered into a PFI scheme in respect of a Crosby leisure centre. With all PFI	We will discuss with management the performance of the PFI arrangement to identify any potential risks arising. We will

Risks	Audit approach
schemes there are risks that: • Value for money will not be achieved; • In partnership arrangements, management does not have sufficient influence or has failed to secure sufficient risk transfer; and • Financial standing will be compromised as governance arrangements are not in place.	review the financial standing of the Council as part of our audit procedures.
Redundancies, severance and ex-gratia payments Terminating the contracts of senior staff could be high profile and costly. Common issues that may arise include: • Contract of employment; • Reasons for termination; • Entitlement on severance, ex-gratia agreements and discretionary benefits; • Value for money; and Compromise agreements, gardening leave, pay in lieu of notice and confidentiality and clawback clauses.	We will review any redundancy, severance and ex-gratia payments as part of our work on the accounts, including consideration of the legality and value for money of any such payments.
Bad debt The economic downturn is likely to have increased the risk of the Council suffering losses due to bad debt. The Council will need to have assessed the collectability of debts, and reviewed its bad debt provision, to avoid overstating its debtors.	We will assess the robustness of the Council's assessment of its exposure to bad debts, and review evidence as to the collectability of year end debtors.

Our approach to the audit

Code of Audit Practice

Under the Audit Commission's Code there are two aspects to our work:

- Accounts including a review of the Annual Governance Statement; and
- Use of Resources.

We are required to issue a two-part audit report covering both of these elements.

Accounts

Our audit of your accounts is carried out in accordance with the Audit Commission's Code objective, which requires us to comply with International Standards on Auditing (ISAs) (UK & Ireland) issued by the Auditing Practices Board (APB). These standards have recently been fully updated and revised to improve their clarity and in some cases this is accompanied by additional audit requirements. We are required to comply with them for the audit of your 2010/11 accounts.

We plan and perform our audit to be able to provide reasonable assurance that the financial statements are free from material misstatement and give a true and fair view. We use professional judgement to assess what is material. This includes consideration of the amount and nature of transactions.

Our overall materiality for the Group is set at £7,025,000, calculated as a percentage of gross operating expenditure; this represents the level at which we would consider qualifying our audit opinion. However, our audit work is planned to a lower materiality level of around £4,918,000.

However, ISA (UK&I) 450 (revised) requires that we record all misstatements identified except those which are "clearly trivial". Matters which are clearly trivial are matters which we expect not to have a material effect on the financial statements even if accumulated. When there is any uncertainty about whether one or more items are clearly trivial, the matter is considered not to be clearly trivial. We propose to treat misstatements less than £50,000 as being clearly trivial. We will include a summary of any uncertainty misstatements identified during our audit in our year-end ISA (UK&I) 260 report.

Our audit approach is based on a thorough understanding of your business and is risk-driven. It first identifies and then concentrates resources on areas of higher risk and issues of concern to you. This involves breaking down the accounts into components. We assess the risk characteristics of each component to determine the audit work required.

We plan our work to have a reasonable expectation of detecting fraud where the potential effects would be material to the financial statements of the Group. Based on the level of management's control procedures, we consider whether there are any significant risks of fraud that may have a material impact on the financial statements and adapt our audit procedures accordingly. We also consider the risk of fraud due to management override of controls and design our audit procedures to respond to this risk.

Our audit approach is based on understanding and evaluating your internal control environment and where appropriate validating these controls, if we wish to place reliance on them. This work is supplemented with substantive audit procedures, which include detailed testing of transactions and balances and suitable analytical procedures.

We also aim to rely on the work done by internal audit wherever this is appropriate. We will ensure that a continuous dialogue is maintained with internal audit throughout the year. We receive copies of all relevant internal audit reports, allowing us to understand the impact of their findings on our planned audit approach.

Our Risk Assurance specialists will undertake a review of the general IT controls. The scope of this review will be:

- IT control activities;
- IT programme changes;
- IT computer operations;
- IT access to programmes and data; and
- IT programme development.

Work on the Whole of Government Accounts consolidation pack is included in the scope of the accounts audit.

Use of Resources

Our Use of Resources Code responsibility requires us to carry out sufficient and relevant work in order to conclude on whether you have put in place proper arrangements to secure economy, efficiency and effectiveness in the use of resources.

In accordance with recent guidance issued by the Audit Commission, in 2010/11 our conclusion will be based on two criteria:

- the organisation has proper arrangements in place for securing financial resilience; and

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

Unlike in previous years, we will not be required to reach a scored judgement in relation to these criteria and the Audit Commission will not be developing ‘key lines of enquiry’ for each criteria. Instead, we will be carrying out sufficient work to allow us to reach a conclusion on your arrangements.

The Audit Commission will be issuing further information on the scope of the criteria and guidance to auditors. We will review that guidance to determine the exact scope of our work and we will communicate that to you.

We will determine our approach to VFM and discuss this with management.

Our team and independence

Audit Team	Responsibilities
Engagement Partner Peter Chambers 0161 247 4311 peter.p.chambers@uk.pwc.com	Engagement Leader responsible for independently delivering the audit in line with the Code of Audit Practice, including agreeing the Audit Plan, ISA (UK&I) 260 report and Annual Audit Letter, the quality of outputs and signing of opinions and conclusions. Also responsible for liaison with the Chief Executive and Members.
Engagement Principal David Newman 0161 247 4130 david.a.newman@uk.pwc.com	Senior Manager on the assignment responsible for overall control of the audit engagement, ensuring delivery to timetable, delivery and management of targeted work and overall review of audit outputs. Completion of the Audit Plan, ISA (UK&I) 260 report and Annual Audit Letter.
Manager Stuart Baron 07809 755 749 stuart.d.baron@uk.pwc.com	Manager on the assignment responsible for managing our accounts work, including the audit of the statement of accounts, and governance aspects of the use of resources.
Team Leader Matthew Chandler 07595 610 299 matthew.s.chandler@uk.pwc.com	Manager on the audit responsible for coordinating the use of resources audit programme including preparing and presenting reports.

Our team members

It is our intention that wherever possible staff work on the Sefton MBC audit each year, developing effective relationships and an in depth understanding of your business. We are committed to properly controlling succession within the core team, providing and preserving continuity of team members.

We will hold periodic client service meetings with you, separately or as part of other meetings, to gather feedback, ensure satisfaction with our service and identify areas for improvement and development year on year. These reviews form a valuable overview of our service and its contribution to the business. We use the results to brief new team members and enhance the team's awareness and understanding of your requirements.

Independence and objectivity

We have made enquiries of all PricewaterhouseCoopers' teams providing services to you and of those responsible in the UK Firm for compliance matters. There are no matters which we perceive may impact our independence and objectivity of the audit team.

Relationships and Investments

Senior officers should not seek or receive personal financial or tax advice from PwC. Members who receive such advice from us (perhaps in connection with employment by a client of the firm) or who also act as director for another audit or advisory client of the firm should notify us, so that we can put appropriate conflict management arrangements in place.

Independence conclusion

At the date of this plan we confirm that in our professional judgement, we are independent accountants with respect to the Council, within the meaning of UK regulatory and professional requirements and that the objectivity of the audit team is not impaired.

Communicating with you

Communications Plan and timetable

ISA (UK&I) 260 (revised) 'Communication of audit matters with those charged with governance' requires auditors to plan with those charged with governance the form and timing of communications with them. We have assumed that 'those charged with governance' are the Audit Committee. Our team works on the engagement throughout the year to provide you with a timely and responsive service. Below are the dates when we expect to provide the Audit Committee with the outputs of our audit.

Stage of the audit	Output	Date
Audit planning	**Audit Fee letter**	March 2010
	Audit Plan	December 2010
Audit findings	Internal control issues and recommendations for improvement (if applicable - may form part of the Audit Memorandum)	June 2011
	ISA (UK&I) 260 report incorporating specific reporting requirements, including: • Any expected modifications to the audit report • Uncorrected misstatements, i.e. those misstatements identified as part of the audit that management have chosen not to adjust • Material weaknesses in the accounting and internal control systems identified as part of the audit • Our views about significant qualitative aspects of your accounting practices including accounting policies, accounting estimates and financial statements disclosures. • Any significant difficulties encountered by us during the audit; • Any significant matters discussed, or subject to correspondence with, Management; • Any other significant matters relevant to the financial reporting process; and • Summary of findings from our use of resources audit work to support our value for money conclusion.	September 2011
Audit reports	**Financial Statements including Use of Resources**	September 2011
Other public reports	**Annual Audit Letter** A brief summary report of our work, produced for Members and to be available to the public.	December 2011

Audit budget and fees

The Audit Commission has provided indicative audit fee levels for Councils for the 2010/11 financial year, which depend upon the level of expenditure and potential risk. Based on your expenditure, the indicative fee scale for audit for the Council is £320,704.

Our audit fee letter dated 15 March 2010 we therefore agreed an audit fee of £310,604, which is broken down as follows:

	2010/11	2009/10
Accounts	£198,758	£181,443
Use of Resources/VFM Conclusion work	£80,029	£78,460
Data Quality	£31,817	£31,193
Sub-total	***£310,604***	***£291,096***
Data migration support	£9,500	-
Response to the accounts objection	-	TBC
Total	**£320,104**	**TBC**

We have based the fee level on the following assumptions:

- Officers meeting the timetable of deliverables, which we will agree in writing;
- We are able to place reliance, as planned, upon the work of internal audit;
- We are able to draw comfort from your management controls;
- No significant changes being made by the Audit Commission to the use of resources criteria on which our conclusion will be based; and
- Our use of resources conclusion and accounts opinion being unqualified.

If these prove to be unfounded, we will seek a variation order to the agreed fee, to be discussed in advance with you.

Certification of grant claims

Our fee for the certification of grant claims is based on the amount of time required to complete individual grant claims at standard hourly rates. We will discuss and agree this with the Director of Finance and his team.

Fees update for 2009/10

We reported our fee proposals as part of our Audit Plan for 2009/10, which we presented to Audit and Governance Committee on 16 December 2009. These fee proposals covered the year ending 31 March 2010.

We varied our fee as a result of additional work on the accounting treatment of PFI and addressing the objection received to the financial statements.

Our fees charged were therefore:

	2009/10 Outturn	2009/10 Fee proposal
Accounts	£181,443	£177,943
Use of Resources	£78,460	£78,460
Data Quality	£31,193	£31,193
Sub-total	***£291,096***	***£287,596***
Response to the accounts objection	TBC	-
Total	**TBC**	**£287,596**

Appendices

Agenda Item 5

Appendix A: Clarity ISAs: What do they mean for Sefton MBC?

What do "Clarity ISAs" mean?

Since 2005, the International Auditing and Assurance Standards Board (IAASB) have been clarifying the **International Standards on Auditing (ISAs)**. The primary aim was to improve the clarity of the ISAs leading to more consistency in their application and to facilitate their adoption throughout the world. As a result, a new set of ISAs were developed and will apply to our 2010/11 audit of the Trust.

Regulators around the world have monitored the project and support the changes, and as a result **their** expectations have been raised. The UK Auditing Practices Board has adopted Clarity ISAs, and issued its own ISAs for use in the UK and Ireland.

Key changes in terminology

Existing PwC Term	To be replaced with	Relevant ISA
Control weakness	Deficiency in internal control	ISA 265.6
Material control weakness	Significant deficiency in internal control	ISA 265.6
Audit difference	Identified misstatement	ISA 450.4
Unadjusted difference	Uncorrected misstatement	ISA 450.4

Key changes which will impact upon your audit

A number of the changes made as a result of the clarity ISA project are minor adjustments or clarifications. Others more expressly require levels of quality which have already been embedded in our audit methodology. These changes will, therefore, have a minimal impact upon the delivery of the Trust's audit.

However there are changes which will have a more noticeable impact on the level of work we are required to perform in certain areas, and may require additional input from members of the finance team. A number of these changes are as a result of an increased focus on assessing risk. The diagram on the following page shows a heat map of the level of change from the previous ISA requirements and the impact on our audit approach. The following points summarise some of the most significant changes.

ISA (UK&I) 450 – Evaluation of misstatements

This standard now requires more explicit consideration of the qualitative aspects of misstatements, for example whether a misstatement impacts upon statutory duties, such as break even. We are also required to undertake greater consideration of potential management bias in financial reporting.

ISA (UK&I 540 – Auditing Estimates

The updated standard requires consideration of the actual outcome against previous estimates when considering the appropriateness of current estimates. Deeper consideration of alternative assumptions is required to be documented along with the decision process used by management to select the estimation technique. We are also required to discuss with management where they consider key estimates and judgements to be and how the level of uncertainty has been assessed.

ISA (UK&I 550) – Related Parties

The wording of the standard places greater onus on management to identify and disclose related parties. If, through the course of our other audit work, we identify a related party which was not reported to us, this necessitates the completion of additional work to address the risk of completeness of related party disclosures. Demonstration of the authorisation and approval process followed where related party transactions have occurred is vital in addressing the requirements of the revised standard. In addition, where transactions with related parties are disclosed as having occurred at "arms length", audit procedures are required to confirm that this disclosure is appropriate.

Work is currently underway to identify how these new requirements will be implemented in public sector audits, where there are particular related party disclosures and policies which must be adhered to.

Using the work of specialists and experts
(ISA (UK&I) 500 – Relevance and reliability of audit evidence
ISA (UK&I) 620 – Using the work of an expert
ISA (UK&I) 220 – Quality control for an audit of financial statements)

A number of changes have been made which clarify the work required when we use the work of experts hired by management or where we have engaged internal specialists to support us in our audit work. The majority of the requirements are already encapsulated in the PwC audit methodology; however there will be some instances where we will need to probe arrangements with management's experts in more detail than previously.

How you will benefit from these changes

We will gain a greater understanding of the risks faced by the Council and your controls to manage these risks, which will make our audit findings more relevant and interesting for you, and will also support the Audit Committee in their work.

Clarity ISAs (UK&I) set a level playing field for auditors in the UK and globally, eliminating ambiguity and helping consistency. They are a robust response to the financial crisis, and in this period of significant turmoil for the NHS, consistent focus on key risk areas such as related party transactions and management areas will ensure that the audit process continues to add value in these difficult times.

Impact on your audit fee

As can be seen by the summary of changes above, the new Clarity ISAs will have a significant impact upon the level of work we will need to perform in certain areas.

Based upon initial considerations of the impact of the additional requirements and the clarifications which have been made, it is anticipated that the additional work required to address the Clarity ISAs will equate to between 2% and 10% of the cost to complete an audit under the previous standards.

We are currently assessing where in this range the impact on our public sector audits is likely to fall. This will then be considered alongside other developments such as the changes in Value for Money work to ascertain the overall impact on our fee. The result of this deliberation will be communicated to the Council.

Appendix B: Other engagement information

The Audit Commission appoint us as auditors to Sefton Metropolitan Borough Council and the terms of our appointment are governed by:

- The Code of Audit Practice; and
- The Standing Guidance for Auditors.

There are four further matters which are not currently included within the guidance, but which our firm's practice requires that we raise with you.

Electronic communication

During the engagement we may from time to time communicate electronically with each other. However, the electronic transmission of information cannot be guaranteed to be secure, virus or error free and such information could be intercepted, corrupted, lost, destroyed, arrive late or incomplete or otherwise be adversely affected or unsafe to use.

PwC partners and staff may also need to access PwC electronic information and resources during the engagement. You agree that there are benefits to each of us in their being able to access the PwC network via your internet connection and that they may do this by connecting their PwC laptop computers to your network. We each understand that there are risks to each of us associated with such access, including in relation to security and the transmission of viruses.

We each recognise that systems and procedures cannot be a guarantee that transmissions, our respective networks and the devices connected to these networks will be unaffected by risks such as those identified in the previous two paragraphs. We each agree to accept the risks of and authorise (a) electronic communications between us and (b) the use of your network and internet connection as set out above. We each agree to use commercially reasonable procedures (i) to check for the then most commonly known viruses before either of us sends information electronically or we connect to your network and (ii) to prevent unauthorised access to each other's systems.

We shall each be responsible for protecting our own systems and interests and you and PwC (in each case including our respective directors, members, partners, employees, agents or servants) shall have no liability to each other on any basis, whether in contract, tort (including negligence) or otherwise, in respect of any error, damage, loss or omission arising from or in connection with the electronic communication of information between us and our reliance on such information or our use of your network and internet connection.

The exclusion of liability in the previous paragraph shall not apply to the extent that such liability cannot by law be excluded.

Access to audit working papers

We may be required to give access to our audit working papers to the Audit Commission or the National Audit Office for quality assurance purposes.

Quality arrangements

We want to provide you at all times with a high quality service to meet your needs. If at any time you would like to discuss with us how our service could be improved or if you are dissatisfied with any aspect of our services, please raise the matter immediately with the partner responsible for that aspect of our services to you. If, for any reason, you would prefer to discuss these matters with someone other than that partner, please contact Paul Woolston, our Audit Commission Lead Partner at our office at 89 Sandyford Road, Newcastle Upon Tyne, NE1 8HW, or Richard Sexton, UK Head of Assurance, at our office at 1 Embankment Place, London, WC2N 6RH. In this way we can ensure that your concerns are dealt with carefully and promptly. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. This will not affect your right to complain to the Institute of Chartered Accountants in England and Wales or to the Audit Commission.

Events arising between signature of accounts and their publication

ISA (UK&I) 560 (revised) places a number of requirements on us in the event of material events arising between the signing of the accounts and their publication. You need to inform us of any such matters that arise so we can fulfil our responsibilities.

If you have any queries on the above, please let us know before approving the Audit Plan or, if arising subsequently, at any point during the year.

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In the event that, pursuant to a request which Sefton Metropolitan Borough Council has received under the Freedom of Information Act 2000, it is required to disclose any information contained in this report, it will notify PwC promptly and consult with PwC prior to disclosing such report. Sefton Metropolitan Borough Council agrees to pay due regard to any representations which PwC may make in connection with such disclosure and Sefton Metropolitan Borough Council shall apply any relevant exemptions which may exist under the Act to such report. If, following consultation with PwC, Sefton Metropolitan Borough Council discloses this report or any part thereof, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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Agenda Item 6

REPORT TO:	Audit & Governance Committee
DATE:	15 December 2010
SUBJECT:	Treasury Management 2010/11 – Mid Year Review
WARDS AFFECTED:	All
REPORT OF:	John Farrell Interim Head of Corporate Finance and ICT Strategy
CONTACT OFFICER:	Jeff Kenah Corporate Finance Manager 0151 934 4104
EXEMPT/CONFIDENTIAL:	No

PURPOSE/SUMMARY:

To review Treasury Management Activities undertaken in the first half of 2010/11 against the Treasury Management Policy and Strategy document 2010/11.

REASON WHY DECISION REQUIRED:

To comply with the requirements of the Council's Treasury Management Policy Statement.

RECOMMENDATION(S):

Audit & Governance Committee is requested to note the Treasury Management Mid-year Review for 2010/11.

KEY DECISION:	No
FORWARD PLAN:	Not appropriate
IMPLEMENTATION DATE:	Immediate

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ALTERNATIVE OPTIONS:
This report is put before Audit & Governance in order to comply with the Treasury Management Policy and Strategy document 2010/11 that was approved by Cabinet in March 2010.

IMPLICATIONS:

Budget/Policy Framework: Compliance with the Policy and Strategy Documents, incorporating appropriate reporting, will enable the Council to secure the most favourable terms for raising funds, maximise returns on investments whilst at all time minimising the level of risk to which it is exposed.

Financial: There are no additional financial implications as a result of the report.

CAPITAL EXPENDITURE	**2010/ 2011 £**	**2011/ 2012 £**	**2012/ 2013 £**	**2013/ 2014 £**
Gross Increase in Capital Expenditure	---	---	---	---
Funded by:	---	---	---	---
Sefton Capital Resources	---	---	---	---
Specific Capital Resources	---	---	---	---
REVENUE IMPLICATIONS				
Gross Increase in Revenue Expenditure	---	---	---	---
Funded by:				
Sefton funded Resources	---	---	---	---
Funded from External Resources	---	---	---	---
Does the External Funding have an expiry date? Y/N		When?		
How will the service be funded post expiry?				

Legal: None.

Risk Assessment: Compliance with the Policy and Strategy Documents minimise the level of risk to which the Council is exposed.

Asset Management: None.

CONSULTATION UNDERTAKEN/VIEWS

Discussion with the Council's Treasury Management Advisor – Sector Treasury Services.

CORPORATE OBJECTIVE MONITORING:

Corporate Objective		Positive Impact	Neutral Impact	Negative Impact
1	Creating a Learning Community		√	
2	Creating Safe Communities		√	
3	Jobs and Prosperity		√	
4	Improving Health and Well-Being		√	
5	Environmental Sustainability		√	
6	Creating Inclusive Communities		√	
7	Improving the Quality of Council Services and Strengthening local Democracy	√		
8	Children and Young People		√	

LIST OF BACKGROUND PAPERS RELIED UPON IN THE PREPARATION OF THIS REPORT

None.

1. BACKGROUND

1.1 The Treasury Management Policy and Strategy document for 2010/11 (approved by Council on 4 March 2010) included a requirement for a mid-year review of treasury management activities in 2010/11. This report is the first of such documents and presents relevant treasury management information for the period ending 30 September 2010. The strategy document also requires a quarterly update on treasury management activity. The quarterly report will be included as part of this mid-year review and no separate quarterly report will be issued for the second quarter to September 2010.

1.2 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2009) was adopted by this Council on 4 March 2010.

The primary requirements of the Code are as follows:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the full council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy for the year ahead, a Mid-year Review Report and an Annual Report covering activities during the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is Audit & Governance Committee.

This mid-year report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic update for the first six months of 2010/11
- A review of the Treasury Management Strategy Statement and Annual Investment Strategy
- A review of the Council's investment portfolio for 2010/11
- A review of interest earned
- A review of the Council's borrowing strategy for 2010/11
- A review of any debt rescheduling undertaken during 2010/11
- A review of compliance with Treasury and Prudential Limits for 2010/11

2 ECONOMIC UPDATE

2.1 Global economy

The sovereign debt crisis peaked in May 2010 prompted, in the first place, by major concerns over the size of the Greek government's total debt and annual deficit. However, any default or write down of Greek debt would have substantial impact on other countries, in particular, Portugal, Spain and Ireland. This crisis culminated in the EU and IMF putting together a €750bn support package in mid - May.

Growth in the US, UK and the Euro zone in quarter 2 of 2010 was particularly driven by strong growth in the construction sector catching up from inclement weather earlier in the year and is unlikely to be repeated; general expectations are for much more subdued figures for the remainder of 2010. Market expectations for all three sectors of the economy is that these have all peaked and are pointing downwards, though not necessarily in to negative territory.

2.2 UK economy

Following the general election in May 2010, the coalition government has put in place a plan to carry out a reduction of the public sector deficit over the next five years. The inevitable result of fiscal contraction will be major job losses during this period as has been highlighted in the press. This will have a knock on effect on consumer and business confidence. House prices have started a negative trend during the summer and mortgage approvals are at very weak levels and also declining.

Economic Growth – GDP growth is likely to have peaked at 1.2% in quarter 2 of 2010.

Unemployment – the trend of falling unemployment (on the benefit claimant count) has now been replaced since July with small increases which are likely to be the start of a new trend of rising unemployment.

Inflation and Bank Rate – the Consumer Price Index (CPI) has remained high so far during 2010. It peaked at 3.7% in April and has fallen back to 3.1% in September. The Retail Price Index (RPI) remains high, at 4.6% in September. Although inflation has remained stubbornly above the MPC's 2% target, the MPC is confident that inflation will fall back under the target over the next two years. The last quarterly Inflation Report in August showed a significant undershoot after the end of 2011.

The Bank of England finished its programme of quantitative easing with a total of £200bn in November 2009 (although there is currently some increase in expectations that there might be a second round of quantitative easing).

The view of our treasury consultants, Sector, is that there is unlikely to be any increase in Bank Rate until the middle of 2011.

AAA rating – prior to the general election, credit rating agencies had been issuing repeated warnings that unless there was a major fiscal contraction, then the AAA sovereign rating was at significant risk of being downgraded. Sterling was also under major pressure during the first half of the year. However, after the Chancellor's budget on 22 June, Sterling has strengthened against the US dollar and confidence has returned that the UK will retain its AAA rating. In addition, international investors now view UK government gilts as being a safe haven from EU government debt. The consequent increase in demand for gilts has helped to add downward pressure on gilt yields and PWLB rates.

2.3 Our Treasury Consultants, Sector, project bank base interest rates and PWLB borrowing rates to be as follows:

	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13
Bank rate	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	2.00%	2.50%	3.00%	3.25%
5yr PWLB rate	2.20%	2.20%	2.20%	2.40%	2.60%	2.80%	3.00%	3.30%	3.60%	3.80%	4.10%	4.40%
10yr PWLB rate	3.30%	3.30%	3.30%	3.40%	3.70%	3.90%	4.00%	4.30%	4.40%	4.60%	4.60%	4.90%
25yr PWLB rate	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.70%	4.70%	4.80%	5.00%	5.00%	5.00%
50yr PWLB rate	4.20%	4.20%	4.30%	4.30%	4.40%	4.50%	4.70%	4.70%	4.80%	5.00%	5.00%	5.00%

3 TREASURY MANAGEMENT STRATEGY STATEMENT AND ANNUAL INVESTMENT STRATEGY UPDATE

The Treasury Management Strategy Statement (TMSS) for 2010/11 was approved by this Council on 4 March 2010. The Council's Annual Investment Strategy, which is incorporated in the TMSS, outlines the Council's investment priorities as follows:

- Security of capital
- Liquidity

The Council will also aim to achieve the optimum return (yield) on investments commensurate with the proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term (maximum investment period of 12 months), and only invest with highly credit rated financial institutions, using Sector's suggested creditworthiness approach, including sovereign credit rating and credit default swap (CDS) overlay information.

A breakdown of the Council's investment portfolio is shown in Section 4 of this report.

Borrowing rates have been at historically low rates during the first six months of the 2010/11 financial year. Any new external borrowing undertaken has been identified in Section 6 of this report.

Investments and borrowing during the first six months of the year have been in line with the strategy.

As outlined in Section 2 above, there is still considerable uncertainty and volatility in the financial and banking market, both globally and in the UK. Against this background it is considered that the strategy approved on 4 March 2010 is still applicable in the current economic climate.

4 INVESTMENTS HELD

4.1 Investments held at the end of September 2010 comprise the following:

Immediate access deposits

Institution	Deposit £m	Rate %	Maturity date	On current counterparty list?
Santander Group	5.000	0.80	N/A	Yes
Natwest	5.000	0.80	N/A	Yes
Blackrock MMF	6.890	0.56	N/A	Yes
Total	16.890			

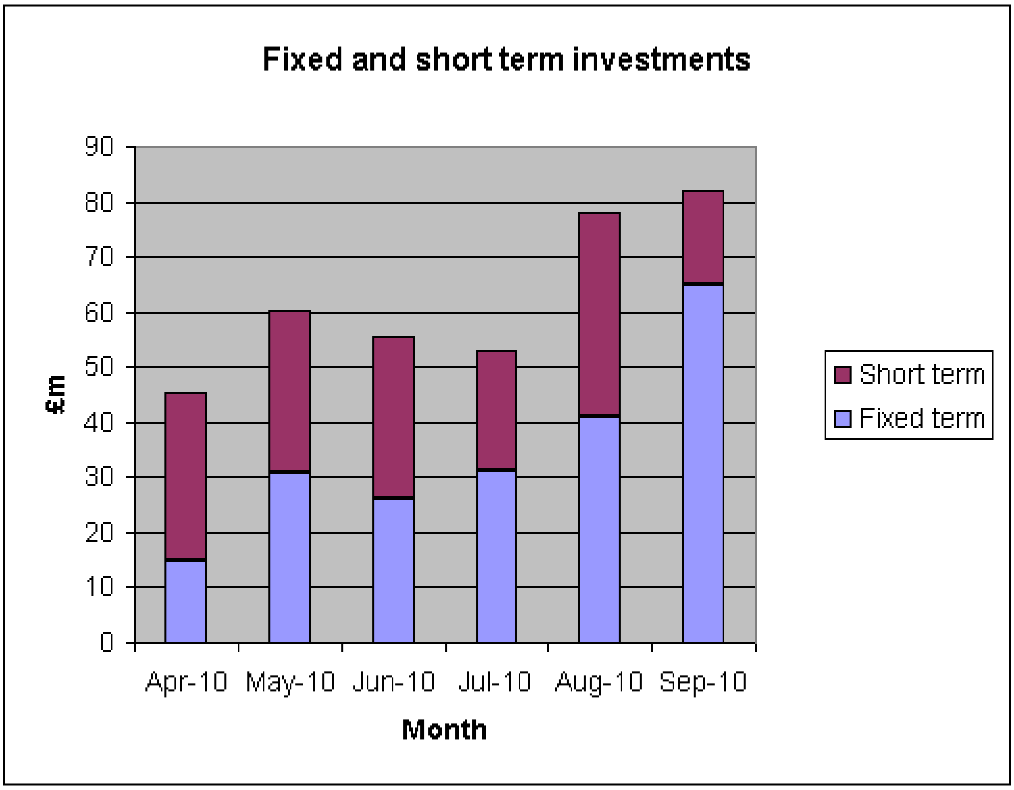
Fixed term deposits

Clydesdale	15.000	0.75	14/10/2010	Yes
Barclays	6.000	0.92	18/11/2010	Yes
Barclays	5.000	0.90	17/11/2010	Yes
Barclays	4.000	0.90	01/03/2011	Yes
Lloyds	5.000	1.82	30/11/2010	Yes
Natwest	10.000	1.32	30/11/2010	Yes
Santander	10.000	1.32	14/04/2011	Yes
Llloyds	10.000	1.70	22/09/2011	Yes
Total	65.000			
TOTAL	81.890			

4.2 All of the organisations are on the current counterparty list. The maximum level of investment permitted in any one institution, or banking group, is currently £25m. Whilst the maximum should be retained, in case conditions change, a day to day operational maximum of £15m is currently being imposed. This will spread the risk of investments for the Council, but will have a small detrimental impact on the returns the Council will receive in the future.

4.3 It should be noted that the deposit with Clydesdale is a 15 day notice account, which until recently had been an immediate access account. An immediate access account is available with Clydesdale but at a much lower rate of interest. This move away from immediate access accounts paying above the Bank of England base rate will continue as banks are required to hold larger capital balances, and hence wish to move away from immediate access accounts which pay above the base rate. This move may cause us to use our money market fund accounts more regularly as they still pay a rate of interest above the base rate.

4.4 The ratio of overnight deposits (i.e. short term) to fixed term investments is illustrated below:



The standard lending list is contained within Appendix A.

5 INTEREST EARNED

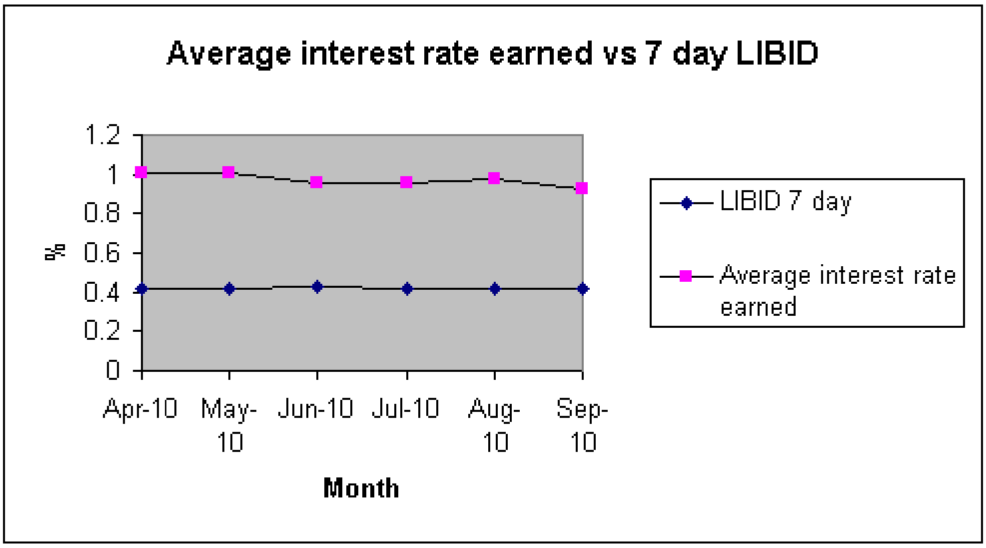
5.1 The actual performance of investments against the profiled budget for the period to 30 September is shown below:

	Budget £'000s	Actual £'000s	Variance £'000s
To 30 September	**96**	**264**	**168**

5.2 The original budget of investment income for 2010/11 was £0.228m (which equated to an average interest rate of 0.515%), was based on investments in place at 1st April 2010.

5.3 The investment income achieved during the first half year is £0.264m, which equates to an average interest rate of 0.97%.

We have outperformed the 7 day LIBID average (standard measure of performance for local authorities) as follows:



6 NEW BORROWING

The Council's capital financing requirement (CFR) for 2010/11 is £200m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (external borrowing) or from internal balances on a temporary basis (internal borrowing). The balance of external and internal borrowing is generally driven by market conditions. Due to the high cost of borrowing as against the low level of interest rates earned on investments, the Council had taken the decision to internally borrow.

Due to a fall in PWLB interest rates on short term loans in recent months, new external borrowing of £20m was undertaken from the PWLB on 31/08/2010 and this has had the impact of reducing our level of internal borrowing. Two loans were taken out, one for £10m over five years at a rate of 1.86%, and one at £10m over six years at a rate of 2.17%. The Council's current level of PWLB borrowing at September 2010 is £131.65m.

As outlined below, the general trend has been a reduction in interest rates during the six months, across all bands, with the low points occurring in the middle to end of August. The high points were in early to mid April. However, following the Comprehensive Spending Review, an additional 1% has been added to the cost of borrowing rates for new borrowings from PWLB with effect from 20 October 2010. By taking the £20m additional borrowing in August the Council has fortuitously the 1% levy. However, future borrowings will be affected; this will impact on our revenue position compared to budget.

It is not anticipated that further borrowing will be undertaken during this financial year.

7 DEBT RESCHEDULING

Debt rescheduling opportunities have been limited in the current economic climate and consequent structure of interest rates. During the first six months of the year, no debt rescheduling was undertaken.

8 PRUDENTIAL INDICATOR MONITORING

8.1 Prudential indicators are an integral component of measuring how prudently a Council is acting with regard to its finances. They were introduced into all local authorities (by CIPFA) following the Local Government Act 2003. A number of measures/limits/parameters including capital financing, external debt, impact on council tax, and treasury management are set prior to the start of the year and are monitored on a monthly basis.

8.2 It should be noted that two of the prudential indicators have been breached.

(i) The Capital Financing Requirement (CFR) limit has been breached by £0.85m. This is because when the indicator was calculated an assumed asset value of £6m was used in respect of the Crosby Leisure Centre PFI scheme, the valuation being supplied by Sector, our Treasury Management Consultants. The actual value of the asset at 31 March 2010 as valued by Capita Symonds was £7.525m, which has caused the breach. This issue was reported in the Prudential Indicators Outturn report 2009/10 as presented to Cabinet on 8 July 2010. This indicator will be monitored over the coming months and a revision of the indicator may be put forward; and

(ii) The Interest Rate Exposure Indicators has been exceeded:

- The limits for fixed rate interest rate exposure expressed as a percentage of net outstanding debt were set to remain between 200% and 120%.
- The limits for variable rate interest rate exposure expressed as a percentage of net outstanding debt were set to remain between -20% and -100%.

8.3 The above indicators are there to prevent either too much investment in fixed or variable interest rate arrangements. This is to ensure a reasonable balance between fixed rate investments where cash is locked away, and variable rate investments that earn a lower rate of interest but give more immediate access to funds.

8.4 The variance in both of these indicators is due to the higher level of overnight deposits being held than originally envisaged. As noted in paragraph 2.3, the problem of identifying institutions with which to invest has meant higher levels of investments in liquid funds, including Money Market Funds. Although these deposits do not earn as much income as fixed term deposits, they are felt to be safer in current economic conditions due the immediate access to funds that they allow. Hence, this breaching of these indicators may continue over coming months, and no corrective action is considered necessary. If monitoring does suggest that these indicators will continue to be breached, a revision of the indicators may be put forward.

8.5 The breaching of these indicators has been caused by specific reasons which are not considered to be an indication of any inherent problems.

9 RECOMMENDATION

Audit & Governance Committee is asked to note the Treasury Management Mid-year Review Report 2010/11.

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APPENDIX A

SEFTON COUNCIL
STANDARD LENDING LIST

UK and International Banks (including Nationwide Building Society	RATING	Negative rating watch?	Individual rating	Support rating	CDS	Deposit £000s
United Kingdom AAA						
Santander UK)	F1+ / AA-	Yes	B	1	Monitoring	
Barclays	F1+ / AA-	Yes	B	1	In range	
Clydesdale Bank	F1+ / AA-	Yes	C	1	N/A	
HSBC	F1+ / AA	Yes	B	1	In range	
Lloyds TSB/HBOS - nationalised	F1+ / AA-		C	1	N/A	
RBS Group – nationalised	F1+ / AA-	Yes	C/D	1	N/A	
Nationwide	F1+ / AA-	Yes	B	1	Monitoring	
Canada AAA						
Bank of Montreal	F1+ / AA-		B	1	N/A	
Bank of Nova Scotia	F1+ / AA-		B	1	N/A	
Canadian Imperial Bank of Commerce	F1+ / AA-	Yes	B	1	N/A	
Royal Bank of Canada	F1+ / AA	Yes	A/B	1	N/A	
Toronto Dominion Bank	F1+ / AA-	Yes	B	1	N/A	
Finland AAA						
Nordea Bank	F1+ / AA-		B	1	N/A	
France AAA						
BNP Paribas	F1+ / AA	Yes	B	1	In range	
CNCE Calyon Corporate & Investment	F1+ / AA-	Yes	C	1	Monitoring	
Credit Industriel et Commercial	F1+ / AA-		B/C	1	N/A	
Germany AAA						
Deutsche Bank	F1+ / AA-	Yes	B/C	1	In range	
Landwirtschaftliche retenbamk	F1+/AAA		W/D	1	N/A	
Netherlands AAA						
Bank Nederlandse Gemeenten	F1+ / AAA		A	1	N/A	

UK and International Banks (including Nationwide Building Society	**RATING**	**Negative rating watch?**	**Individual rating**	**Support rating**	**CDS**	**Deposit £000s**
Coop Centrale Raiffeisen – Boerenleenbank BA	F1+ / AA+	Yes	A/B	1	In range	
Singapore AAA						
DBS	F1+ / AA-		B	1	In range	
Overseas Chinese Banking Corporation	F1+ / AA-		B	1	In range	
United Overseas Bank	F1+ / AA-		B	1	In range	
Sweden AAA						
Nordea Bank	F1+ / AA-	Yes	B	1	N/A	
Svenska Handelsbanken	F1+ / AA-	Yes	B	1	In range	
Switzerland AAA						
Credit Suisse	F1+ / AA-	Yes	B/C	1	In range	
USA AAA						
Bank of New York Mellon	F1+ / AA-		A/B	2	N/A	
Deutsche Bank Trust Company Americas	F1+ / AA-	Yes	N/R	1	N/A	
HSBC Bank USA	F1+ / AA	Yes	B/C	1	N/A	
JP Morgan Chase Bank	F1+ / AA-	Yes	B	1	In range	
Wells Fargo	F1+ / AA-	Yes	B	1	In range	

The recent economic situation has provided challenges for the Council with regard to its investment strategy. The report presented to Cabinet on 11 June 2009 explained the difficulties in identifying banking institutions to invest in (which provided reasonable investment returns), whilst remaining within the deposit limit of £15m. Consequently, Cabinet agreed to increase the deposit limit from £15m to £25m. As noted in 4.2 above, the Council has remained within an operational boundary of £15m. At present, it is not expected that there will be any need to review this limit.

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