

# Sefton Metropolitan Borough Council

Annual Audit Letter for the year ended 31 March 2016

21 NOVEMBER 2016

Ernst & Young LLP

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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ‘Statement of responsibilities of auditors and audited bodies 2015-16’. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psaa.co.uk](http://www.psaa.co.uk))

The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The ‘Terms of Appointment from 1 April 2015’ issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

A hand with white nail polish is writing on a document with a blue pen. In the background, there is a calculator, a laptop, and a white mug. A yellow rectangular box is overlaid on the left side of the image.

## Executive Summary

## Executive Summary

We are required to issue an annual audit letter to Sefton Metropolitan Borough Council (the Council) following completion of our audit procedures for the year ended 31 March 2016.

Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's ▶ Financial statements	We issued an unqualified opinion – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2016 and of its expenditure and income for the year then ended
▶ Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts.
Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We issued a qualified 'except for' VFM conclusion, in regards to weaknesses in arrangements for procuring goods and services across the Council. We reported that with the exception of these matters that we were satisfied that, in all significant respects, the Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

Area of Work	Conclusion
Reports by exception: ▶ Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council.
▶ Public interest report	We had no matters to report in the public interest.
▶ Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	We had no matters to report

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 21 September 2016
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 08 November 2016

In January 2017 we will also issue a report to those charged with governance of the Council summarising the certification work we have undertaken.

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Hassan Rohimun

Executive Director  
For and on behalf of Ernst & Young LLP

Purpose



## Purpose

### The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2015/16 Audit Results Report to the 21 September 2016 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.





Responsibilities



## Responsibilities

### Responsibilities of the Appointed Auditor

Our 2015/16 audit work has been undertaken in accordance with the Audit Plan that we issued on 23 March 2016 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
  - ▶ On the 2015/16 financial statements; and
  - ▶ On the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
  - ▶ If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - ▶ Any significant matters that are in the public interest;
  - ▶ Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - ▶ If we have discharged our duties and responsibilities as established by thy Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on you Whole of Government Accounts return.

## Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement. In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

# Financial Statement Audit



## Financial Statement Audit

### Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 30 September 2016.

Our detailed findings were reported to the 21 September 2016 Audit Committee.

The following financial statement risks were identified as part of our planning process, and responded to as follows:

Significant Risks	Work performed	Conclusion
<p>Risk of management override As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.</p> <p>As a presumed risk specified by international auditing standards we identify and respond to this fraud risk on every audit engagement.</p>	<ul style="list-style-type: none"> <li>▶ We made inquiries of management about risks of fraud and the controls put in place to address those risks.</li> <li>▶ Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.</li> <li>▶ Reviewed accounting estimates for evidence of management bias.</li> <li>▶ Developed a testing approach to journal entries.</li> <li>▶ Assessed accounting estimates, particularly provisions, for evidence of management bias.</li> <li>▶ Remained sceptical for the existence of any significant unusual transactions.</li> <li>▶ Reviewed capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.</li> </ul>	<p>Our audit work did not identify any evidence of management over-ride of controls.</p> <p>In particular, our testing of journal entries did not identify any significant issues.</p>



Significant Risks	Work performed	Conclusion
<p>Revenue and expenditure recognition</p> <p>Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue.</p> <p>In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.</p> <p>As a presumed risk specified by international auditing standards we identify and respond to this fraud risk on every audit engagement.</p>	<ul style="list-style-type: none"> <li>▶ Developed a testing strategy to test material revenue and expenditure streams;</li> <li>▶ Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;</li> <li>▶ Reviewing accounting estimates for evidence of management bias;</li> <li>▶ Evaluating the business rationale for significant unusual transactions; and</li> <li>▶ Reviewed and tested revenue cut-off at the period end date.</li> </ul>	<p>Our audit work did not identify any significant issues in respect of revenue and expenditure recognition.</p>

We also identified the following audit risks during the planning phase of our audit, and reported the outcome of our work to you in our Audit Findings Report.

Other Risks	Work performed	Conclusion
<p><b>Minimum Revenue Provision</b></p> <p>The scheme of Minimum Revenue Provision (MRP) was set out in former regulations 27, 28 and 29 of the 'Local Authorities (Capital Finance and Accounting) (England) Regulations 2003'. This system has now been revised by the amended Statutory Instrument 2008 no. 414 s4 which lays down that: "A local authority shall determine for the current financial year an amount of minimum revenue provision that it considers to be prudent."</p> <p>The operative date of the change was 31 March 2008, and applies to the financial year 2007/8 and subsequent years. Guidance was issued suggesting a number of ways Authorities could approach the calculation of this provision.</p> <p>Officers are in the process of reviewing their approach to the MRP calculation in particular in respect of supported borrowing pre 2008 to decide which alternative approach should be adopted.</p>	<p>We involved our technical experts to:</p> <ul style="list-style-type: none"> <li>▶ Review the revised MRP Policy</li> <li>▶ Review the MRP calculation for the current year of audit incorporating any change in approach</li> <li>▶ Evaluate the justification that approach meets the definition of "prudent"</li> <li>▶ Test the detailed supporting documentation to MRP calculations.</li> </ul>	<p>Initial review of the revised calculation and discussion with management identified issues relating to:</p> <ul style="list-style-type: none"> <li>▶ Duplication of charges regarding transferred debt and payments to MRB;</li> <li>▶ Lease and PFI calculations being based on asset values rather than the outstanding liability;</li> <li>▶ Treatment of long term loans;</li> <li>▶ Consideration that MRP constituted a provision under International Accounting Standard 37 ; and</li> <li>▶ Differing capital financing requirement calculations in elements of the annuity calculation.</li> </ul> <p>Management adjusted their calculations following the above findings.</p> <p>Our review of the revised MRP policy did not identify any areas of non-compliance, and we have concluded that the policy meets the definition of 'prudent'.</p>

A close-up, shallow depth-of-field photograph of a stack of coins. The coins are stacked vertically, with the edges of several coins visible. The lighting is warm, highlighting the metallic texture and the ridges on the edges. A bright yellow rectangular box is overlaid on the left side of the image, containing the text "Value for Money".

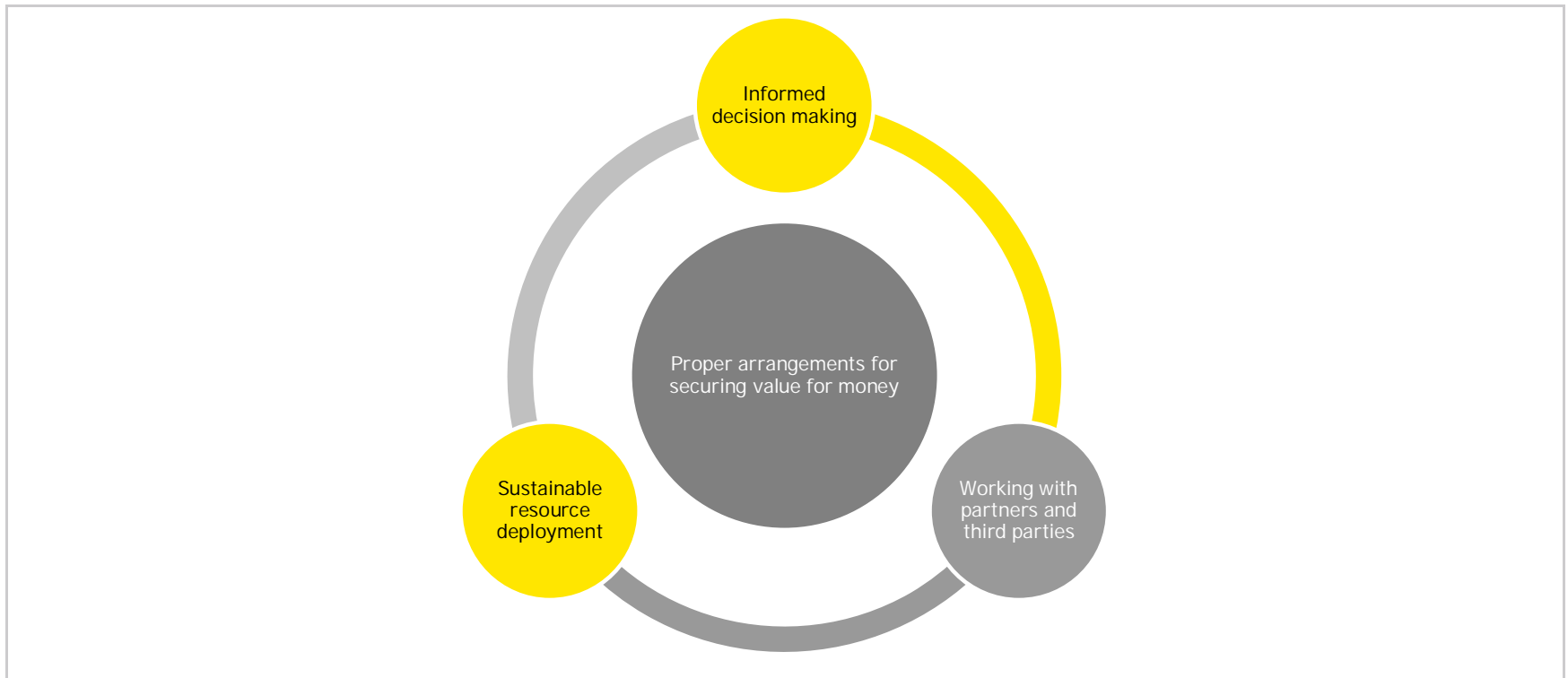
Value for Money

## Value for Money

We are required to consider whether the Council has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.





We issued a qualified 'except for' value for money conclusion on 08 November 2016. We identified that except for weaknesses in the Council's arrangements for procuring goods and services, we were satisfied that, in all significant respects, Sefton Metropolitan Borough Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

Reason for qualified 'except for' VFM Conclusion:

Procurement

In June 2016, the Council engaged an independent review to investigate a specific element of a procurement process. The review identified "*an environment that lacks clearly defined responsibilities and accountability*". The report highlighted general weaknesses including:

- ▶ The roles of the Procurement team and the responsibilities of the Service are not clearly documented.
- ▶ There is no formal approval process for agreeing the final versions of the PQO or ITT or any subsequent changes to documentation.
- ▶ Issues identified with the procurement guidance include:
  - The procedure was last updated in April 2014 prior to the Public Sector Contract Regulations 2015;
  - The contract procedure rules do not refer specifically to the use of Chest or include procedural guidance about how to use the 'electronic tendering method';
  - The rules do not clearly allocate the responsibility for managing the procurement including the split between procurement and the service line ;
  - The rules do not clarify the conditions for communication with suppliers during a tender process;
  - The rules do not clarify the process for approving an ITT; and
  - The rules do not clarify the process for managing ITT variations.

The Council responded quickly to the findings of the review and established an action plan for improvement. However, given the nature of the issues identified for the purposes of our VFM conclusion further work was required in order to assess if the issues identified were isolated or highlighted wider weaknesses in the Council's arrangements for procuring services. Having reviewed further procurement exercises carried out in the year issues were identified which demonstrated that the issues identified in the initial procurement review were not isolated to one exercise or department, but represent weaknesses across the Council in regards to the effectiveness and compliance of controls. This represents significant weaknesses in arrangements for procuring goods and services across the Council.

At the planning stage of our audit we identified significant risks and other areas of focus, our key findings in these areas are summarised below:

### Significant VFM risks - Key Findings

#### Medium term financial planning

The Council has a track record of delivering identified savings and this performance has continued in 2015/16 with savings of £34.8 million, enabling a balanced budget at year end.

Looking forward to 2016/17, the challenges remain just as acute with savings of £37 million in 2016/17 needed to achieve a balanced budget. As at the end of June 2016 the Council were reporting that £28.1million (75%) of the total required savings had been delivered or were on plan; with £1million at some risk of not being fully achieved; and a further £8.2 million of savings was identified as a “Red” risk of not being delivered. The Council are in the process of challenging services to review all areas of expenditure in order to contribute to a year end balanced position, to ensure the outturn position remains within the savings required. It is notable that the budget and forecast outturn includes £6 million of revenue expected from partners in regards to the Better Care Fund, which the Council has identified as being at risk of delivery. The Council are identifying mitigating savings in replacement of the ‘at risk’ revenue.

The forecast financial position for 2017/18 – 2019/20 indicates a budget gap of £64 million. When put into context with the significant savings achieved to date, continued savings of this size require a fundamental change to the services provided by the Council and how they are delivered. The Council is currently developing a transformational change programme in order to create a sustainable future and it has started to develop a three year programme and financial plan to address the medium term challenges.

Despite the scale of the challenges ahead, the Council continues to be ambitious for Sefton and are in the process of developing a ‘2030 vision’ for the Borough. They have engaged with local residents, inviting them to share their aspirations for the Borough and what they want and need now and into the future.

Delivering these plans will be a significant challenge for the Council. Given the scale of the transformational programme the Council needs to ensure that programmes are properly scrutinised, managed and delivered. In doing so Members will need to ensure there are robust plans and performance management processes in place to track the progress and delivery of actions, including the formulation of mitigating plans in the event of non-delivery.

## Significant VFM risks - Key Findings

### Pooled Budget Agreement

We identified in our audit plan that the section75 agreement in place for the Better Care Fund did not fully reflect the expected income, which was exposing the Council to potential shortfalls in expected income due to disagreements on financial obligations with its partners.

The Council contends that they were due an additional £3 million in 2015/16 followed by £6 million in 2016/17. These sums were included in the revenue budget for each respective year, but the liability was disputed by Sefton CCG. Following an arbitration panel meeting, it was determined that the Council would not receive the sums expected in mitigation the Council sought remedial measures and assumed the worst case scenario for financial planning purposes once they were aware of the CCG's position. However, this loss of income does have an impact on the Council's Medium Term Financial Plan (MTFP) and action is being taken to mitigate the loss.

Following the arbitration meeting a Better Care Fund plan for 2016/17 was agreed and submitted to NHS England. The Council recognises that delivery of its objectives will not be fully achieved without the co-ordinated input of all partners within the health and social care system.

Moving in to the second year of the Better Care Fund we are noting, nationally, that many partners have developed their plans for collaborative working, by:

- ▶ Reviewing care pathways to deliver improved patient outcomes and genuine system wide efficiencies;
- ▶ Revisiting governance arrangements after a year's experience;
- ▶ Working towards fully integrating commissioning;
- ▶ Further honing arrangements for reporting financial and non-financial information; and
- ▶ Delivering fair risk share arrangements between partners.

Across the country health and local government bodies will need to work together to a far greater extent than ever before to ensure that sustainability and financial plans are viable, and successfully delivered. Failure to do this could have wider adverse financial and service delivery consequences across the whole local area. In the context of Sefton Council it is important that following the disagreement on funding, partners now work together to deliver on the Better Care Fund objectives. We would also recommend there is formal agreement of all aspects before the start of the financial year.

Other areas of VFM focus were:

#### Other VFM risks - Key Findings

##### OFSTED: Children in need to help inspection

In June 2016 OFSTED, published a report on the Services for Children in Need of Help. The service was rated as 'Requiring improvement to be good' across all areas inspected.

The report highlights that:

- *Children's services in Sefton require improvement to be good. Services for children in need of help and protection have not made progress since they were last inspected in 2011 and services for children looked after have deteriorated. Some areas of improvement identified then, such as ensuring that effective management oversight is clearly recorded in case notes, have not been sufficiently addressed.*
- *No children have been found in situations of unassessed or unacceptable risk through this inspection.*

The report further highlights that heads of service, which are relatively new to the post, have made good progress in introducing measures to support effective practice. However, more improvements need to be done as elements of the service remain inconsistent.

The Council has responded positively by identifying specific area for improvement against each of the recommendations raised. Whilst the report identifies areas of improvement, we are satisfied that, as reported by Ofsted, the Council had started to take action to make these improvements.

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Other Reporting  
Issues

## Other Reporting Issues

### Whole of Government Accounts

We performed the procedures required by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes. We had no issues to report.

### Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and identified a small number of areas where further disclosure was required to reflect the position at the Council. The Council amended the annual governance statement to include these areas.

### Report in the Public Interest

We have duty to consider if there are any matters coming to our notice that should be brought to the public's attention through a public interest report

We had no matters to report in the public interest.

### Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

### Objections Received

We did not receive any objections to the 2015/16 financial statements from members of the public.

### Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

## Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 21 September 2016. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

## Control Themes and Observations

We adopted a fully substantive approach throughout our audit and therefore did not test the operation of controls. However, during the course of our work we identified a number of controls matters which we highlighted in our Audit Results Report. These are summarised below.

The matters reported are limited to those deficiencies that we identified during the audit and that we concluded are of sufficient importance to merit being reported.

Findings	Recommendation
<p><b>Procurement</b></p> <p>An investigation by the Council has identified significant weaknesses in the internal control processes associated with the central procurement function. This issue is being reviewed by the Council and an action plan being implemented.</p>	<p>The Audit Committee should ensure that planned actions for improvement are implemented and ensure a review of overall procurement processes is undertaken.</p>
<p><b>Closedown process</b></p> <p>The draft statements dated 13 June 2016 were superseded by a revised set of statements on 20 June 2016. However, the Council did not have comprehensive working papers in place to support the statements at the outset; this resulted in significant delays and inefficiencies in the audit process.</p>	<p>The Council needs to ensure that its controls and closedown procedures are robust enabling an effective and efficient closedown and production of the accounts within the agreed timescale, supported by a comprehensive set of working papers.</p>
<p><b>Pooled Budgets</b></p> <p>We identified in our audit plan that the section 75 agreement in place for the Better Care Fund did not fully reflect the expected income, which was exposing them to potential shortfalls in expected income due to disagreements on financial obligations with its financial partners. There was an expectation that savings of £3m in 2015/16 which would be achieved between the CCGs and Sefton to contribute to the pressures being experienced by Adult Social Care. This was not achieved leaving a shortfall.</p>	<p>Formal agreements should be implemented before the start of the financial year which reflect the agreed savings targets.</p>

Findings

Asset verification

Over and above the rolling programme of valuations the Council does not have in place formal arrangements to periodically verify the existence of significant moveable assets. Based on the verification testing we have undertaken and the application of our materiality level, we gained assurance regarding the existence of assets. The lack of periodic verification does represent a weakness in central controls and highlights safeguarding issues. The Council should design an appropriate procedure to confirm the existence of assets.

Recommendation

The Council should design an appropriate procedure to confirm the existence of assets.



Appendix A

## Audit Fees



## Appendix A Audit Fees

Description	Planned Fee 2015/16 £	Additional Fee 2015/16 £	Final Fee 2015/16 £
Total Audit Fee – Code work	126,897	21,500*	148,397
Audit Fee – Certification of Housing Benefits grant claim.	10,390		10,390
Audit Fee – Certification of other grant claims.	7,500		7,500
<b>TOTAL FEES</b>			<b>166,287</b>

As detailed above, we have carried out additional work in regards to the certification of grant claims outside of PSAA requirements. We have considered our independence as part of the acceptance of the additional work, and conclude that there were no threats to independence.

\*The additional fee is in regards to:

- £7,500 additional work for Minimum Revenue Provision
- Provisional £14,000 for additional audit resource required as a result of additional procedures to for the value for money conclusion, delays in provision of adequate working papers, and additional time spent following up from the issues and outstanding queries following the initial planned site work.

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ED None

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