

# Public Document Pack

Lancashire County Council

Audit Committee

**Monday, 24th January, 2011 at 2.00 pm in Cabinet Room 'B' - County Hall, Preston**

## Agenda

### Part 1 (Open to Press and Public)

#### No. Item

##### 1. Disclosure of Personal and Prejudicial Interests

Members are asked to consider any Personal/Prejudicial Interests they may have to disclose to the meeting in relation to matters under consideration on the Agenda.

##### 2. Minutes of the Last Meeting

(Pages 1 - 6)

The Committee are asked to agree that the Minutes of the last meeting be confirmed and signed by the Chair.

##### 3. Accounts of Lancashire County Developments Limited 2009/10

(Pages 7 - 34)

##### 4. Risk Management Report

(Pages 35 - 52)

##### 5. Update on treasury management activity

(Pages 53 - 64)

##### 6. Overview of the implementation of International Financial Reporting Standards for the accounts of the County Council

(Pages 65 - 72)

##### 7. CIPFA's statement on 'The role of the head of internal audit'

(Pages 73 - 102)

##### 8. Internal Audit Progress Report

(Pages 103 - 120)

##### 9. Sure Start, Early Years and Childcare Services

(Pages 121 - 122)

##### 10. Annual audit letter 2009/10 - Audit Commission Report

(Pages 123 - 142)

##### 11. Audit Commission - Lancashire County Council and Pension Fund 2010/11 Audit Plans

(Pages 143 - 192)

**12. Urgent Business**

An item of urgent business may only be considered under this heading where, by reason of special circumstances to be recorded in the Minutes, the Chairman of the meeting is of the opinion that the item should be considered at the meeting as a matter of urgency. Wherever possible, the Chief Executive should be given advance warning of any Member's intention to raise a matter under this heading.

**13. Date of Next Meeting**

The next meeting of the Audit Committee will be held on Monday 21 March 2011 at 2.00 p.m. in Cabinet Room B, County Hall, Preston.

I M Fisher  
County Secretary and Solicitor

County Hall  
Preston

# Agenda Item 2

## Lancashire County Council Audit Committee

Monday 27 September 2010

### Minutes

#### Present:

#### County Councillors

S Chapman (Chair)

K Brown  
H Henshaw  
J Lawrenson

M Parkinson  
M Welsh  
M Younis

### Apologies

Apologies were received from County Councillors C Grunshaw and D Westley.

### Officers in attendance

Habib Patel, head of strategic partnerships and performance (Item 3)  
Mike Jensen – head of treasury management and the pension fund (Item 4)  
George Graham – assistant director of finance (Items 5, 7 & 8)  
Roy Jones - assistant county secretary  
Ruth Lowry – head of internal audit (Item 6)  
Ian Rushworth – principal auditor (Item 6)  
Fiona Blatcher – senior audit manager, Audit Commission (Items 7 & 8)  
Clive Portman - district auditor, Audit Commission (Items 7& 8)

### Also in attendance:

Richard Tomlinson – senior accountant  
Joan Grant – senior accountant  
Ian Winston – senior accountancy assistant  
Jenny Salisbury – trainee accountant

### Disclosure of Personal and Prejudicial Interests

County Councillors S Chapman and M Parkinson declared a personal interest in item 8 as they are members of the Lancashire County Pension Fund.

### Minutes of the Meeting held on 28 June 2010

With regard to resolution 9 concerning the recommendations of the Audit Committee to the Scrutiny Committee, it was reported that these had been

raised at the meeting of the Scrutiny Committee on 9 July 2010 and that the Scrutiny Committee intended to add the issues raised to the items under consideration for future reports.

It was also reported that the Health Scrutiny Committee intended to pursue the issue of the administration of medication in care homes, and had approached officers from Audit to supply information on the work they had undertaken.

It was noted that the Scrutiny Committee had given its clear support for the two functions of scrutiny and audit to continue to work together and welcomed the recommendations from the Audit Committee.

**19. Resolved:** That the response of the Overview and Scrutiny Committee be noted with regard to Resolution 9, and that the minutes of the meeting held on 28 June 2010 be confirmed and signed by the chair.

### **Risk Management Update Report (Item 3)**

A presentation was made to the committee by Habib Patel, Head of Strategic Partnerships and Performance, who explained that an important part of the remit of the Audit Committee was to advise the council on the adequacy of the Authority's strategic processes for risk management and to consider reports in respect of the authority's risk register and the action taken in response.

Members were informed that the process for preparing the risk register had been further refined so that the Executive Directors and their senior management teams had direct input into its development. Reference was made to the risks identified in areas of business continuity, emergency planning and health and safety.

In considering whether the content of the draft risk register reflected the key risks facing the council, the committee maintained that the risk associated with the establishment of Local Enterprise Partnerships was a key risk and as such should be included in the risk register. Members also commented that the risks identified under some headings were excessively brief and should contain more detailed information. Officers undertook to provide this.

**14. Resolved:** That:

- i) The content of the corporate risk register be noted.
- ii) The risks associated with Local Enterprise Partnerships be included in the risk register.
- iii) The actions being taken in response to identified risks and the current process for identifying risk be noted.

### **Update on Treasury Management Activity (Item 4)**

A presentation was made to the committee by Mike Jensen, Head of Treasury Management and the Pension Fund who informed members of the general economic environment surrounding treasury management activities and set out the position on the borrowing and lending activities of the county council.

The committee was informed that the overall position was one where the county council had begun to be able to take advantage of its new strategy to de-risk its investments while also being able to access attractive rates for new borrowing where appropriate. Details of the Treasury Management activities were presented at Appendix A.

**21. Resolved:** That the update on treasury management activities as shown at appendix A to the report now presented be noted.

### **Overview of the implementation of International Financial Reporting Standards for the accounts of the county council (Item 5)**

A presentation was made to the committee by George Graham, assistant director of finance (accountancy and financial services) on the progress made in implementing the new International Financial Reporting Standards (IFRS).

It was noted that progress continued to be made, and the IFRS was expected to be implemented in accordance with statutory deadlines.

**22. Resolved:** That the report be noted.

### **Internal Audit Progress Report (Item 6)**

Ruth Lowry, head of internal audit, presented an internal audit progress report for the five months to 31 August 2010.

The report included a summary of the work performed and a comparison with work planned and the progress made in relation to cross cutting and corporate risks; corporate or common controls; and service specific controls.

In response to queries raised by the committee it was reported that:

- Guidance would be provided by the Human Resources team to enable the authority to comply with and monitor compliance with the European Working Time Directive.
- Additional support and advice had been offered to the four out of the six schools audited recently to bring their systems of internal control up to the standard required. It was also reported that the audit service intended to carry out audits on a number of other schools and that a

further report would be presented to the next meeting of the committee in January 2011.

The report also included the results of the annual client satisfaction survey which concluded that the Audit Service had achieved a 'good' overall score.

**23. Resolved:** That the internal audit progress report for the five months to 31 August 2010 as now presented, be noted.

### **Audit Commission**

### **Lancashire County Council Annual Governance Report 2009/10**

The committee considered a report on the Audit Commission's Annual Governance Report for the year ending 31 March 2010. The report included the letter of representation which gave the Audit Commission specific management assurances regarding the accounts of the Lancashire County Council.

In commenting on the report, Clive Portman, district auditor, informed the committee that the financial statements were generally prepared to a good standard. Council officers had identified some amendments that were needed to the accounts following their submission to the June 210 Audit Committee. These largely related to the significant changes in accounting requirements for 2009/10, particularly for PFI schemes. In addition, a small number of amendments had been made in response to issues raised by the Audit Commission. The committee noted that none of the amendments had impacted on the financial position of the authority and that the Audit Commission expected to issue an unqualified opinion on the financial statements by 30 September 2010.

The report also included the Audit Commission's value for money conclusion which assessed whether the council had put in place satisfactory corporate arrangements for securing economy, efficiency and effectiveness in its use of resources. The committee noted that overall the county council had continued its good performance and had improved its arrangements in a number of areas. This included developing further its approach to financial planning, commissioning and procurements which would be important to help the Council address the financial challenges ahead. The council had also recognised the need to develop further in specific areas and had plans in place to do so.

The committee was also informed that the executive director of resources had signed the letter of representation to the district auditor and members were asked to agree to the Chair of the committee signing the letter.

**24. Resolved:** That:

- i) The Audit Commission Lancashire County Council Annual Governance Report covering the audit of the County Council for year ended 31 March 2010 be noted.
- ii) The adjustments to the financial statements as set out in the report now presented be noted.
- iii) The Chair of the committee be authorised to sign the letter of representation tabled at the meeting.
- iv) The findings in relation to the value for money conclusion as set out in the report now presented be noted.

### **Audit Commission Lancashire Pension Fund Annual Governance Report 2009/10**

The committee considered a report on the Audit Commission's Lancashire Pension Fund Annual Governance Report for the year ending 31 March 2010. The report included the letter of representation which gave the Audit Commission specific management assurances regarding the accounts of the Lancashire Pension Fund.

In commenting on the report, Clive Portman, District Auditor, informed the committee that the financial statements had been completed to a good standard and were supported by comprehensive working papers.

The committee noted the action plan issued by the Audit Commission which required the council to provide greater assurance over private equity investment valuations and also continued effort to achieve effective implementation of a separate bank account for the pension fund by 1 April 2011

The committee was informed that the Audit Commission expected to issue an unqualified opinion on the financial statements by 30 September 2009.

The committee was also informed that the executive director of resources had signed the letter of representation to the District Auditor and Members were asked to agree to the chair of the committee signing the letter.

#### **25. Resolved:** That:

- i) The Audit Commission Lancashire Pension Fund Annual Governance Report covering the audit of the County Council for year ended 31 March 2010 be noted.
- ii) The chair of the committee be authorised to sign the letter of representation tabled at the meeting.

- iii) That the proposed action plan set out at Appendix 4 to the report be endorsed.

### **Accounts of the Lancashire County Council's and the Lancashire County Pension Fund 2009/10 (Item 9)**

Following consideration of items 7 and 8, the committee was informed that the executive director of resources had signed the amended 2009/10 Statement of Accounts in respect of the County Council and the Lancashire County Pension Fund and were asked to agree to the chair of the committee signing them.

**26. Resolved:** That the chair of the committee be authorised to sign the amended 2009/10 Statement of Accounts presented at the meeting.

### **Date of Next Meeting**

**27. Resolved:** It was noted that the next meeting of the committee would be held on Monday 24 January 2011 at 2.00 p.m. at the County Hall, Preston.

County Hall  
Preston

I M Fisher  
County secretary and solicitor

# Agenda Item 3

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected: All
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### Accounts of Lancashire County Developments Limited 2009/10

(Appendix 'A' refers)

Contact for further information:

Beryl Rhodes, 01772 533603, Lancashire County Developments Limited  
[beryl.rhodes@lancashire.gov.uk](mailto:beryl.rhodes@lancashire.gov.uk)

#### Executive Summary

This report sets out the Financial Statements of Lancashire County Developments Limited for 2009/10.

#### Recommendation

The Committee is requested to note the 2009/10 Statement of Accounts for Lancashire County Developments Limited.

#### Background

Lancashire County Developments Limited (LCDL) is the council's economic development company and is focussed on delivery in line with the County Council's Economic Development Framework.

On the 17th July 2003, the Full Council, on the recommendation of the Cabinet, resolved that the Lancashire County Developments Limited audited Statement of Accounts be reported to the Audit Committee for information.

An overview of 2009/10 for the company by its Chair can be seen on pages 3 and 4 of the Financial Statements for LCDL, which are attached at Appendix 'A'. Beryl Rhodes, LCDL Head of Finance and HR, will attend the meeting to respond to any questions.

#### Consultations

N/A

#### Advice

N/A

#### Implications:

This item has the following Risk Management implications:

N/A

**Implications:** Other

This item has the following implications:

N/A

**Local Government (Access to Information) Act 1985**

**List of Background Papers**

Paper	Date	Contact/Directorate/Ext
Financial Statements working papers	2009/10	Beryl Rhodes, LCDL Tel : 01772 533603

Reason for inclusion in Part II, if appropriate

N/A



# Financial Statements Lancashire County Developments Limited

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**For the year ended 31 March 2010**

## Company information

**Company registration number :** 1624144

**Registered office :**  
P O Box 78  
County Hall  
Preston  
Lancashire  
PR1 8XJ

**Directors :**  
G Davies (resigned 9 June 2009)  
E Forshaw (resigned 9 June 2009)  
Mrs H Harding (resigned 9 June 2009)  
A C P Martin (resigned 9 June 2009)  
Ms D Pollitt (resigned 9 June 2009)  
V K Riley (resigned 9 June 2009)  
D Ruddick (resigned 9 June 2009)  
J S Sutcliffe (resigned 9 June 2009)  
K A Young (resigned 23 July 2009)  
Mrs E A Smith (resigned 23 July 2009)  
Ms N D Penney  
M Welsh (appointed 17 July 2009)  
H Henshaw (appointed 21 July 2009)  
R J C Lawrenson (appointed 20 July 2009)  
G Driver (appointed 17 July 2009)  
M P France (appointed 22 July 2009)  
G Fitzgerald  
T M Ashton

**Secretary :** I M Fisher

**Bankers :**  
The Royal Bank of Scotland Plc  
97 Fishergate  
Preston  
PR1 2DP

**Auditors :**  
Grant Thornton UK LLP  
Registered Auditors  
Chartered Accountants  
4 Hardman Square  
Spinningfields  
Manchester  
M3 3EB

## Index to financial statements

<b>Chair's statement</b>	3 - 4
<b>Report of the directors</b>	5 - 6
<b>Report of the independent auditors</b>	7 - 8
<b>Principal accounting policies</b>	9 - 10
<b>Consolidated profit and loss account</b>	11
<b>Statement of total recognised gains and losses</b>	11
<b>Reconciliation of movements in members' funds/(deficit)</b>	12
<b>Consolidated balance sheet</b>	13
<b>Company balance sheet</b>	14
<b>Consolidated cash flow statement</b>	15
<b>Notes to the financial statements</b>	16 - 24

## Chair's statement

### **Company performance**

The year under review has been characterised by intense pressures following the near collapse of the financial system in 2009; in parallel the Company has undertaken a profound review of its objectives following the change in political control of Lancashire County Council. The result has been to strengthen the commitment to support economic growth across Lancashire by supporting the development of new, innovative business in a number of key sectors. The County Council's Economic Development Strategy puts particular emphasis on the need to work closely with private sector partners and institutions such as the Universities in achieving the core objective – improving Lancashire's performance against comparable sub regions in terms of gross value added. Raising our collective game is essential if the County is to rise to the challenges posed by the new Age of Austerity.

Whilst income from properties fell by £0.4 million and other investment and grant income was reduced by £0.5 million this was offset by a one off contractual payment relating to a prior year property sale. This financial bonus was a timely reward associated with overage clauses negotiated in a property sale and this has enabled the Company to deliver a profit whilst increasing business expenditure in 2009/10.

The County Council has extended the £5.52 million loan to 30th September 2030 to further support the Company in providing economic development services across Lancashire. This has strengthened the balance sheet increasing the net worth to £47.8 million and emphasises the importance of the Company and further equipping it to lead on the economic development agenda.

Investment property balance sheet values have increased to over £40 million thanks to the Company's investment in high quality offices at Rising Bridge in Rossendale. This investment will eventually span over three financial years with the Company investing £5.7 million in this prestigious development by the end of the next financial year.

It is planned to increase the Company's financial capacity through new borrowing, enabling us to increase our investments in loans, equity shares and commercial property over the next three years, taking advantage of the expected demise of the NWDA and other central government agencies that have been the principal sources of state sponsored investment in the Region. We expect that the reduction of bureaucratic controls and the freeing up of the system will open up new and exciting opportunities which the company is well placed to exploit.

### **Future plans**

The Company's strategic mission is to facilitate growth in the Lancashire economy by removing obstacles and stimulating growth among private sector operators who are the essential drivers of economic prosperity.

Future Activity will be focussed on generating growth in the Lancashire economy, working with the private sector to facilitate their delivery of improved Lancashire prosperity.

This will include the development and expansion of Rosebud investment and loan products to finance businesses with higher growth potential. There will be a particular focus on innovative businesses in the creative and digital and environmental technical services sectors. This will naturally necessitate the Company developing joint projects with the Lancashire Universities notably on graduate employment and spin out businesses and incubation.

Working with private, public and voluntary sector partners, the Company expects to achieve specific outcomes in the following key areas.

- **Economic Growth, Knowledge and Innovation with a focus on Business Development and Creative Industries:**- Unlocking Lancashire's growth potential as a location for nuclear and other energy sectors, enhancing competitive advantage in advanced manufacturing and ensure that the County's deficit in knowledge based and creative sectors is bridged.
- **Spatial:** - Identify and support those areas of the County that have the strongest growth potential in recognition that this is the best way to develop Lancashire as a regional centre of excellence for innovation, financial and professional services and personal development.
- **Skills and Employment:** - Focus on graduate employment and working with the three private sector led Employment and Skills Boards, ensuring that Lancashire has the right supply of NVQ4 plus skills to meet current and future demands and employers maximise their use of apprentices.
- **Infrastructure:** - Support partners in seeking to develop Lancashire's digital infrastructure and ensure Lancashire's new and emerging Local Transport Plan framework supports agreed economic priorities.
- **Partnership Development:** - Support the work to ensure that Lancashire's sub-regional economic partnership is fit for purpose. Work with partners seeking to ensure the Lancashire brand helps to attract and retain strategic investors and highly skilled professionals and establish and strengthen economic trade in India, China, Brazil and USA.

In addition to the re-focus of our activities as highlighted above, to further equip the business to meet the ongoing financial pressures, the Company will deliver specific business improvements that reduce costs and improve income.

I would like to thank the Managing Director and all members of staff for their hard work and dedication over the last twelve months. I look forward to working with them as they deliver against these new priorities and support the private sector led growth of the Lancashire economy.

To find out more, please log onto Lancashire County Council's website:  
[www.lancashire.gov.uk/home/index.asp](http://www.lancashire.gov.uk/home/index.asp) and select L for LCDL or telephone the Group on 01772 536600.

County Councillor Michael Welsh  
Chairman  
Lancashire County Developments Limited

## Report of the directors

The directors present their report together with the audited financial statements of the company and the group for the year ended 31 March 2010.

### **Principal activities**

The principal activities of the group are to invest in Lancashire with a view to acting as a catalyst in promoting the economic development of industry in the County, to provide industrial premises and associated facilities for businesses and to promote job creation and training particularly associated with new technologies.

Lancashire County Developments Limited is a company under the control of Lancashire County Council within the meaning of Part V of the Local Government and Housing Act 1989.

### **Business review**

A detailed review of operations of the group during the year and a commentary on the state of affairs, financial position and plans for the future is contained in the Chair's statement.

The group profit before taxation amounted to £201,260 (2009: £39,588). The group profit after taxation amounted to £79,318 (2009: loss - £261,261), which has been transferred to reserves.

### **Capital funding**

Lancashire County Developments Limited is a company limited by guarantee, therefore, does not have a share capital.

### **Directors and employees**

The Board of Directors during the year ended 31 March 2010 is shown below. All served on the Board throughout the year and thereafter, unless otherwise indicated.

G Davies	(resigned 9 June 2009)
E Forshaw	(resigned 9 June 2009)
Mrs H Harding	(resigned 9 June 2009)
A C P Martin	(resigned 9 June 2009)
Ms D Pollitt	(resigned 9 June 2009)
V K Riley	(resigned 9 June 2009)
D Ruddick	(resigned 9 June 2009)
J S Sutcliffe	(resigned 9 June 2009)
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M J Welsh	(appointed 17 July 2009)
H Henshaw	(appointed 21 July 2009)
J R C Lawrenson	(appointed 20 July 2009)
G Driver	(appointed 17 July 2009)
M P France	(appointed 22 July 2009)
G B Fitzgerald	
T M Ashton	

At 31 March 2010, the group had no paid employees (2009: Nil), because with effect from 1 January 2004 all employees of the group were transferred to become employees of Lancashire County Council. Management services were also provided by the staff of Lancashire County Council and by professional advice.

**Statement of directors' responsibilities**

The directors are responsible for preparing the Report of the directors and the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the group and the company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for maintaining adequate accounting records that disclose with reasonable accuracy at any time the financial position of the group and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the company and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

In so far as the directors are aware :

- there is no relevant audit information of which the company's auditors are unaware; and
- the directors have taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditors are aware of that information

**Auditors**

Grant Thornton UK LLP, having expressed their willingness to continue in office, will be deemed to be reappointed for the next financial year in accordance with Section 487(2) of the Companies Act 2006 unless the company receives notice under 488(1) of the Companies Act 2006.

BY ORDER OF THE BOARD

I M Fisher  
Secretary



# Report of the independent auditor to the members of Lancashire County Developments Limited

We have audited the financial statements of Lancashire Country Developments Limited for the year ended 31 March 2010 which comprise the principal accounting policies, the consolidated profit and loss account, the statement of total recognised gains and losses, the group and parent company reconciliation of movement in members' funds, the consolidated and parent company balance sheets, the consolidated cash flow statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

## **Respective responsibilities of directors and auditors**

As explained more fully in the Statement of directors' responsibilities, set out on page 6, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

## **Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the APB's website at [www.frc.org.uk/apb/scope/UKNP](http://www.frc.org.uk/apb/scope/UKNP).

## **Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the group's and the parent company's affairs as at 31 March 2010 and of the group's profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

## **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Report of the directors for the financial year for which the financial statements are prepared is consistent with the financial statements.



## Report of the independent auditor to the members of Lancashire County Developments Limited

### **Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

STUART MUSKETT (Senior Statutory Auditor)  
For and on behalf of  
GRANT THORNTON UK LLP  
STATUTORY AUDITOR  
CHARTERED ACCOUNTANTS  
MANCHESTER

## Principal accounting policies

The financial statements have been prepared in accordance with applicable United Kingdom accounting standards and under the historical cost convention modified by the revaluation of certain fixed assets.

The principal accounting policies of the group are set out below.

### **Basis of consolidation**

The group financial statements combine the financial statements of Lancashire County Developments Limited and all of its subsidiary undertakings.

In the year of acquisition, the consolidated profit and loss account incorporates the group's share of the results of subsidiary undertakings from the date of acquisition.

The group also holds corporate investments in certain companies where its shareholding is in excess of 20% of the total voting capital of these companies. In order to reflect the investment nature of all holdings, the group accounts for profits and losses on all of its corporate investments upon realisation. As the investments are held primarily for the purpose of promoting economic development, disclosure of share capital, reserves and results for the year of each investment, as required by the Companies Act 2006, is not considered appropriate.

### **Goodwill**

Goodwill arising on consolidation which represents the excess of the fair value of the consideration given over the fair value of the identifiable net assets acquired, is capitalised and amortised over its estimated useful economic life, typically 20 years. Negative goodwill is written back to the profit and loss account to match the recovery of the non-monetary assets acquired, which is 5 years.

### **Income from investments**

Investment income is the amount of income receivable in the accounting period from investments and loans.

### **Income from property**

Property income comprises rents arising from investment properties in the accounting period, but excludes service charges which are credited against the relevant expenditure.

### **Assets under the course of construction**

Assets under the course of construction are capitalised at cost based upon external valuations provided by industry specialists.

### **Investment properties**

In accordance with Statement of Standard Accounting Practice No 19, certain of the group's properties are held for long-term investment and are included in the balance sheet at their open market values. The surplus(es) or deficit(s) on revaluation of such properties are transferred to the investment property revaluation reserve. Depreciation is not provided in respect of freehold investment properties. Leasehold investment properties are not amortised where the unexpired term is over twenty years.

This policy represents a departure from statutory accounting principles, which require depreciation to be provided on all fixed assets. The directors consider that this policy is necessary in order that the financial statements may give a true and fair view, because current values and changes in current values are of prime importance rather than the calculation of systematic annual depreciation. Depreciation is only one of many factors reflected in the valuation and the amount which might otherwise have been shown cannot be separately identified or quantified.

### **Corporate investments**

Investments are stated at cost less provision for impairment. Provision is made against investments if, in the opinion of the directors, the diminution in value is considered permanent and likely to crystallise in the foreseeable future. All costs incurred in connection with the making of corporate investments are written off in the period in which they are incurred.

### **Government and EEC grants**

Government and EEC grants received and receivable in respect of capital expenditure on investment properties are deducted from the cost of the relevant tangible fixed assets. This does not comply with paragraphs 17 and 27 of Schedule 1 to SI 2008/410, which have the effect of prohibiting the deduction of grants from the purchase price of the related asset. This would therefore require the grant to be treated as deferred income.

As stated above no depreciation is provided on investment properties and therefore, there would be no corresponding release of any deferred income to profit and loss account. The directors do not consider that the creation of a permanent deferred credit will show a true and fair view of the state of the affairs of the group at the balance sheet date.

### **Deferred taxation**

Deferred tax is recognised on all timing differences where the transactions or events that give the group an obligation to pay more tax in the future, or a right to pay less tax in the future, have occurred by the balance sheet date. Deferred tax assets are recognised when it is more likely than not that they will be recovered. Deferred tax is measured using rates of tax that have been enacted or substantively enacted by the balance sheet date.

### **Leased assets**

Payments made under operating leases are charged to the profit and loss account on a straight line basis over the lease term.

## Consolidated profit and loss account

<b>Continuing activities</b>	<b>Note</b>	<b>2010</b>	<b>2009</b>
		£	£
Operating income	2	<b>6,981,132</b>	7,835,005
Expenditure		<b>(7,348,712)</b>	<b>(7,053,213)</b>
<b>Operating (loss)/profit</b>		<b>(367,580)</b>	781,792
Profit on sale of tangible fixed assets		<b>860,076</b>	—
Unrealised loss on revaluation of investment properties		—	(705,000)
Provisions against investments		<b>(441,551)</b>	<b>(454,578)</b>
<b>Profit/(loss) on ordinary activities before interest and taxation</b>		<b>50,945</b>	(377,786)
Interest receivable	3	<b>189,632</b>	515,753
Interest payable and similar charges	3	<b>(39,317)</b>	<b>(98,379)</b>
<b>Profit on ordinary activities before taxation</b>	2	<b>201,260</b>	39,588
Taxation on profit on ordinary activities	5	<b>(121,942)</b>	(300,849)
<b>Profit/(loss) retained and transferred to reserves</b>	13	<b>79,318</b>	<b>(261,261)</b>

## Statement of total recognised gains and losses

	<b>2010</b>	<b>2009</b>
	£	£
Profit/(loss) for the financial year	<b>79,318</b>	(261,261)
Unrealised loss on revaluation of investment properties	—	(2,474,973)
Total recognised gains and losses relating to the year	<b>79,318</b>	<b>(2,736,234)</b>

## Reconciliation of movement in members' funds/(deficit)

<b>Group</b>	<b>2010</b>	<b>2009</b>
	<b>£</b>	<b>£</b>
Profit/(loss) for the year	<b>79,318</b>	(261,261)
Revaluation in the year	<b>–</b>	(2,474,973)
Net addition to/(reduction in) members' funds	<b>79,318</b>	(2,736,234)
Members' funds at beginning of the year	<b>41,727,294</b>	44,463,528
Members' funds at end of the year	<b>41,806,612</b>	<b>41,727,294</b>

## Company

Loss for the year	<b>(1,207,859)</b>	(465,641)
Members' deficit at beginning of the year	<b>(9,394,805)</b>	(8,929,164)
Members' deficit at end of the year	<b>(10,602,664)</b>	<b>(9,394,805)</b>

## Consolidated balance sheet

		<b>2010</b>	2009
	<b>Note</b>	<b>£</b>	<b>£</b>
<b>Fixed assets</b>			
Investment properties	7	<b>40,319,345</b>	37,543,468
Corporate investments	8	<b>2,647,223</b>	2,718,594
		<b>42,966,568</b>	40,262,062
<b>Current assets</b>			
Debtors	9	<b>2,493,996</b>	2,483,447
Cash at bank and in hand		<b>9,012,409</b>	11,852,561
		<b>11,506,405</b>	14,336,008
<b>Creditors :amounts falling due within one year</b>	10	<b>(6,660,335)</b>	(12,026,496)
<b>Net current assets</b>		<b>4,846,070</b>	2,309,512
<b>Total assets less current liabilities</b>		<b>47,812,638</b>	<b>42,571,574</b>
<b>Financed by:</b>			
Capital funding reserve	13	<b>8,730,878</b>	8,730,878
Investment property revaluation reserve	13	<b>19,331,317</b>	19,331,317
Investment revaluation reserve	13	<b>712,276</b>	712,276
Profit and loss account	13	<b>13,032,141</b>	12,952,823
<b>Members' funds</b>		<b>41,806,612</b>	41,727,294
<b>Creditors :amounts falling due after more than one year</b>	11	<b>5,942,026</b>	782,280
<b>Provisions for liabilities</b>	12	<b>64,000</b>	62,000
		<b>47,812,638</b>	<b>42,571,574</b>

These financial statements were approved by the Board on  
and signed on their behalf by:

Chair

Company no: 1624144

The accompanying notes form part of these financial statements.

## Company balance sheet

		<b>2010</b>	2009
	Note	£	£
<b>Fixed assets</b>			
Investment properties	7	—	48,996
Corporate investments	8	<b>9,268,725</b>	9,219,729
		<b>9,268,725</b>	<b>9,268,725</b>
<b>Current assets</b>			
Debtors	9	<b>3,920,758</b>	2,345,570
Cash at bank and in hand		—	1,817,635
		<b>3,920,758</b>	<b>4,163,205</b>
<b>Creditors :amounts falling due within one year</b>	<b>10</b>	<b>(17,850,121)</b>	<b>(22,044,455)</b>
<b>Net current liabilities</b>		<b>(13,929,363)</b>	(17,881,250)
<b>Total assets less current liabilities</b>		<b>(4,660,638)</b>	<b>(8,612,525)</b>
 <b>Financed by:</b>			
Capital funding reserve	13	<b>7,660,241</b>	7,660,241
Profit and loss account	13	<b>(18,262,905)</b>	(17,055,046)
<b>Members' deficit</b>		<b>(10,602,664)</b>	(9,394,805)
<b>Creditors :amounts falling due after more than one year</b>	<b>11</b>	<b>5,942,026</b>	782,280
		<b>(4,660,638)</b>	<b>(8,612,525)</b>

These financial statements were approved by the Board on  
and signed on their behalf by:

Chair

Company no: 1624144

The accompanying notes form part of these financial statements.

## Consolidated cash flow statement

		<b>2010</b>	2009
	Note	£	£
<b>Net cash (outflow)/inflow from operating activities</b>	14	(20,400)	312,818
<b>Returns on investments and servicing of finance</b>			
Interest received		189,632	515,753
Interest paid		<u>(39,317)</u>	<u>(98,379)</u>
<b>Net cash inflow from returns on investments and servicing of finance</b>		<b>150,315</b>	417,374
<b>Taxation paid</b>		<b>(326,274)</b>	(309,906)
<b>Capital expenditure and financial investment</b>			
Purchase of investment properties		(2,824,873)	–
Disposal of investment properties		860,076	–
Purchase of corporate investments		<b>(1,014,429)</b>	(878,230)
Disposal and repayment of corporate investments		<b>695,687</b>	617,926
<b>Net cash outflow from capital expenditure and financial investment activities</b>		<b>(2,283,539)</b>	(260,304)
<b>Net cash (outflow)/inflow before financing</b>		<b>(2,479,898)</b>	159,982
<b>Financing</b>			
New loan from parent undertaking		–	110,000
Repayment of bank loans		<b>(360,254)</b>	<b>(310,012)</b>
<b>Net cash outflow from financing</b>	15	<b>(360,254)</b>	(200,012)
<b>Decrease in cash in the year</b>	16	<b>(2,840,152)</b>	<b>(40,030)</b>

The accompanying notes form part of these financial statements.

## Notes to the financial statements

### **1 Constitution**

Lancashire County Developments Limited is a company limited by guarantee. At 31 March 2010 there were 3 members (2009: 3), each of whom on a winding-up had undertaken to contribute an amount not exceeding £1.

### **2 Operating income and profit on ordinary activities before taxation**

Operating income and profit on ordinary activities before taxation are attributable to the group's principal activities, which were carried out entirely within the United Kingdom. The profit on ordinary activities before taxation is stated after charging:

	<b>2010</b>	2009
	£	£
Auditors' remuneration		
– audit services	32,012	25,470
– non-audit services	6,285	33,475
Management fee paid to Lancashire County Council	345,048	349,195
Operating lease rentals		
– land and buildings	<u>97,011</u>	<u>97,011</u>

Non-audit services relate primarily to tax compliance and advisory fees.

### **3 Net interest**

	<b>2010</b>	2009
	£	£
<b>Interest payable and similar charges</b>		
Bank loans	<u>39,317</u>	<u>98,379</u>
<b>Interest receivable</b>		
Bank interest receivable	<u>189,632</u>	<u>515,753</u>

### **4 Directors and employees**

The chairman received £Nil (2009: £Nil) during the year. The total received from the group by the other directors was £Nil (2009: £Nil).

The employees of the group were officially transferred to Lancashire County Council with effect from 1 January 2004. The average number of employees in the year ended 31 March 2010 was Nil (2009 : Nil). Employee costs of £2,474,686 for the year (2009 : £2,017,354) were recharged from Lancashire County Council to Lancashire County Developments Limited and are included within administrative expenses.

**5 Taxation**

	<b>2010</b>	2009
	<b>£</b>	<b>£</b>
Corporation tax on profit on ordinary activities at 28% (2009 : 28.5%)		
– current year	90,000	159,681
– adjustment in respect of prior years	29,942	143,168
	<b>119,942</b>	<b>302,849</b>
Deferred taxation		
– current year (other)	(11,000)	2,000
– adjustment in respect of prior years	13,000	(4,000)
	<b>2,000</b>	<b>(2,000)</b>
Tax on profit on ordinary activities	<b>121,942</b>	<b>300,849</b>

**Factors affecting the tax charge for the year**

The tax assessed for the year differs from the standard rate of corporation tax in the United Kingdom of 28% (2009 : 28.5%). The differences are explained as follows :

	<b>2010</b>	2009
	<b>£</b>	<b>£</b>
Profit on ordinary activities before taxation	<b>201,260</b>	<b>39,588</b>
Profit on ordinary activities before taxation multiplied by standard rate of corporation tax in the United Kingdom of 28% (2009 : 28.5%)	56,353	11,283
Effect of:		
Expenses not deductible for tax purposes	25,574	149,259
Differences between capital allowances and depreciation	7,934	(861)
Group relief	139	–
Adjustment in respect of prior years	<b>29,942</b>	<b>143,168</b>
	<b>119,942</b>	<b>302,849</b>

## **6 Profit and loss account**

Under the provisions of s480 of the Companies Act 2006, Lancashire County Developments Limited has not published its own profit and loss account. The loss dealt with in the financial statements of the parent undertaking is £1,207,859 (2009 : £465,641).

## **7 Investment properties**

Group	Freehold £	Assets under the course of construction £	Total £
<b>Cost or valuation and net book value</b>			
At 1 April 2009	37,294,171	249,297	37,543,468
Additions	–	2,824,873	2,824,873
Reclassifications	(48,996)	–	(48,996)
At 31 March 2010	<u>37,245,175</u>	<u>3,074,170</u>	<u>40,319,345</u>
<b>Cumulative grants</b>			
At 31 March 2010			<u>3,143,187</u>
At 31 March 2009			<u>2,343,633</u>

The properties were externally revalued on an open market basis as at 31 March 2007 by King Sturge LLP. The properties were internally revalued by the group's parent undertaking (Lancashire County Council) on an open market basis at 31 March 2009 and this valuation has subsequently been updated by the directors to 31 March 2010. The historical cost of the premises are as follows :

	£
At 31 March 2009	23,408,089
Additions	2,824,873
At 31 March 2010	<u>26,232,962</u>

### **Company**

At the year end the cost and net book value of the assets was £nil (2009: £48,996).

### **Capital commitments**

At 31 March 2010, the group and the company had capital commitments of £1,798,570 (2009: £nil).

**8 Corporate investments**

	<b>2010</b> <b>£</b>	<b>Group</b> <b>2009</b> <b>£</b>	<b>2010</b> <b>£</b>	<b>Company</b> <b>2009</b> <b>£</b>
Shares in subsidiary undertakings	—	—	200	200
Shares in associated undertaking	<b>163,136</b>	163,136	—	—
Loans to subsidiary undertakings	—	—	<b>9,219,529</b>	9,219,529
Other investments in shares	<b>1,466,594</b>	1,417,598	<b>48,996</b>	—
Other participating interests	<b>16,709</b>	17,208	—	—
Other loans	<b>1,000,784</b>	1,120,652	—	—
	<b>2,647,223</b>	<b>2,718,594</b>	<b>9,268,725</b>	<b>9,219,729</b>

<b>Subsidiary undertakings</b>	<b>Principal activity</b>	<b>% of ordinary shares</b>	<b>% of preference shares</b>
Lancashire County Developments (Investments) Limited	Investment company	100	—
Lancashire County Developments (Property) Limited	Property investment	100	—
Lancashire Enterprises (Investments) Limited	Investment company	100	100
Lancashire County Enterprises (Leasing) Limited	Dormant	100	—
The Lancashire Rosebud (Small Firms) Fund Company Limited	Dormant	—	—

**Associated undertaking**

North West Regional Fund Limited	Investment company	25	—
----------------------------------	--------------------	----	---

**Other participating interests**

Other participating interests at 31 March 2010 represent investments in The HSBC (UK) Enterprise Fund for the North West and the Enterprise Venture Fund. The interests are 11.9% and 15.7% respectively (2009 : 11.9% and 15.7% respectively).

**Corporate investments (continued)**

**Group**

	Shares in associated undertakings	Other participating interests	Other investment in shares	Loans	Total
	£	£	£	£	£
<b>Cost</b>					
At 1 April 2009	163,136	17,208	2,058,445	2,298,399	4,537,188
Additions	—	—	—	1,014,429	1,014,429
Reclassifications	—	—	48,996	—	48,996
Amounts written off	—	—	—	(100,492)	(100,492)
Repayments	—	—	—	(666,174)	(666,174)
Net share of profits of other participating interests	—	(499)	—	—	(499)
At 31 March 2010	<u>163,136</u>	<u>16,709</u>	<u>2,107,441</u>	<u>2,546,162</u>	<u>4,833,448</u>
<b>Provisions</b>					
At 1 April 2009	—	—	640,847	1,177,747	1,818,594
Charge for the year	—	—	—	438,610	438,610
Amounts written off	—	—	—	(70,979)	(70,979)
At 31 March 2010	<u>—</u>	<u>—</u>	<u>640,847</u>	<u>1,545,378</u>	<u>2,186,225</u>
<b>Net book value</b>					
At 31 March 2010	<u><b>163,136</b></u>	<u><b>16,709</b></u>	<u><b>1,466,594</b></u>	<u><b>1,000,784</b></u>	<u><b>2,647,223</b></u>
At 31 March 2009	<u>163,136</u>	<u>17,208</u>	<u>1,417,598</u>	<u>1,120,652</u>	<u>2,718,594</u>

	Principal activity	% of ordinary shares held at 31 March 2010	% of preference shares held at 31 March 2010
<b>Other investments</b>			
C Probe Technologies Limited	Remedial cathodic protection for structural concrete	19	54
Manhattan Showers Limited	Manufacture of shower screens	20	—
M B Aseptic Technology Limited	Development of aseptic food filling machinery	35	100
North West Regional Fund Limited	Investment company	25	—
Plant Impact Plc	Development of crop nutrients and natural pesticides	3.72	—
Porpoise Viscometers Limited	Manufacture of measuring equipment	36	85
Select Hearing Systems Limited	Manufacture of electronic hearing aid accessories	12	33
SOL Publications Limited	Publishing and Media company	15	—
Noetic Associates Ltd trading as Malagasy	Producer/distributor of fine food, drink and health products	3.5	—
Outerlin Limited (formerly EXML Systems)	Development of Expense World Expenses System	2	—
Notren Limited	Development and sale of dietary and health recording products	2	—

The group holds other investments in which more than 20% of share capital is held. The group does not include these as associated undertakings as no significant influence is exerted over these companies.

**9 Debtors: amounts falling due within one year**

	<b>2010</b> <b>£</b>	<b>Group</b> <b>2009</b> <b>£</b>	<b>2010</b> <b>£</b>	<b>Company</b> <b>2009</b> <b>£</b>
Trade debtors	<b>1,826,428</b>	1,537,456	<b>649,318</b>	282,196
Accrued income and prepayments	<b>471,584</b>	289,431	<b>36,560</b>	22,346
Amounts owed by parent undertaking	<b>31,364</b>	82,083	<b>24,490</b>	—
Amounts owed by other group undertakings	—	—	<b>2,990,755</b>	1,477,705
Amounts owed by related undertakings	<b>58,813</b>	353,947	<b>58,813</b>	353,947
Social security and other taxes	<b>105,807</b>	220,530	<b>105,822</b>	155,376
Deferred taxation (note 12)	—	—	<b>55,000</b>	54,000
	<b><u>2,493,996</u></b>	<b><u>2,483,447</u></b>	<b><u>3,920,758</u></b>	<b><u>2,345,570</u></b>

**10 Creditors: amounts falling due within one year**

	<b>2010</b> <b>£</b>	<b>Group</b> <b>2009</b> <b>£</b>	<b>2010</b> <b>£</b>	<b>Company</b> <b>2009</b> <b>£</b>
Bank overdraft	—	—	<b>939,707</b>	—
Bank loans (note 11)	<b>300,000</b>	300,000	<b>300,000</b>	300,000
Amounts owed to parent undertaking - Lancashire County Council (note 11)	<b>1,710,000</b>	7,230,000	<b>1,710,000</b>	7,230,000
Trade creditors	<b>409,104</b>	309,390	<b>409,104</b>	257,540
Amounts owed to parent undertaking	<b>425,423</b>	74,161	<b>425,423</b>	74,161
Amounts owed to other group undertakings	—	—	<b>12,959,702</b>	13,101,167
Amounts owed to related undertakings	—	8,626	—	8,626
Corporation tax	<b>90,000</b>	294,332	—	—
Social security and other taxes	—	291,771	—	—
Accruals and deferred income	<b>3,725,808</b>	3,518,216	<b>1,106,185</b>	1,072,961
	<b><u>6,660,335</u></b>	<b><u>12,026,496</u></b>	<b><u>17,850,121</u></b>	<b><u>22,044,455</u></b>

**11 Creditors: amounts falling due after more than one year**

	<b>Group and Company</b>	
	<b>2010</b>	<b>2009</b>
	£	£
Amount owed to parent undertaking -		
Lancashire County Council	5,520,000	-
Bank loans	422,026	782,280
	<b>5,942,026</b>	<b>782,280</b>

The loan from Lancashire County Council included in creditors: amounts falling due after more than one year of £5,520,000 is interest free and is repayable in full on 30 September 2030.

The Royal Bank of Scotland plc bank loans are repayable as follows :

	<b>Group and company</b>	
	<b>2010</b>	<b>2009</b>
	£	£
Within one year	300,000	300,000
After one and within two years	300,000	300,000
After two and within five years	122,026	482,280
	<b>722,026</b>	<b>1,082,280</b>

The bank loan is secured by fixed and floating charges over all assets of the group and is repayable by equal quarterly instalments. Interest is based upon bank LIBOR rate.

**12 Provisions for liabilities**

**Deferred taxation**

	<b>Group</b>	<b>Company</b>
	£	£
Provision/(asset) at 1 April 2009	62,000	(54,000)
Charge/(credit) for the year	2,000	(1,000)
Provision/(asset) at 31 March 2010	<b>64,000</b>	<b>(55,000)</b>

Deferred taxation provided for in the financial statements is set out below.

	<b>Group</b>		<b>Company</b>	
	<b>Amount provided</b>		<b>Amount provided</b>	
	<b>2010</b>	<b>2009</b>	<b>2010</b>	<b>2009</b>
	£	£	£	£
Accelerated capital allowances	111,000	109,000	(22,000)	(21,000)
Other timing differences	(47,000)	(47,000)	(33,000)	(33,000)
	<b>64,000</b>	<b>62,000</b>	<b>(55,000)</b>	<b>(54,000)</b>

**13 Reserves**

Group	Capital funding reserve £	Investment property revaluation reserve £	Investment revaluation reserve £	Profit and loss account £
At 1 April 2009	8,730,878	19,331,317	712,276	12,952,823
Profit for the year	-	-	-	79,318
At 31 March 2010	<u><b>8,730,878</b></u>	<u><b>19,331,317</b></u>	<u><b>712,276</b></u>	<u><b>13,032,141</b></u>
Company		Capital funding reserve £		Profit and loss account £
At 1 April 2009		7,660,241		(17,055,046)
Loss for the year		-		(1,207,859)
At 31 March 2010		<u><b>7,660,241</b></u>		<u><b>(18,262,905)</b></u>

**14 Net cash (outflow)inflow from operating activities**

	2010 £	2009 £
Operating (loss) / profit	(367,580)	781,792
Increase in debtors	(10,549)	(321,143)
Increase/ (decrease) in creditors	<b>357,230</b>	(82,496)
Share of loss/ (profit) in participating interests (note 8)	<b>499</b>	(65,335)
Net cash (outflow)/inflow from operating activities	<u><b>(20,400)</b></u>	<u><b>312,818</b></u>

**15 Reconciliation of net cashflow to movement in net funds**

	2010 £	2009 £
Decrease in cash in the year	(2,840,152)	(40,030)
Cash outflow from movement of debt	<b>360,254</b>	200,012
Movement in net funds	<b>(2,479,898)</b>	159,982
Opening net funds	<b>3,540,281</b>	3,380,299
Closing net funds	<u><b>1,060,383</b></u>	<u><b>3,540,281</b></u>

**16 Analysis of changes in net funds**

	At 31 March 2009	Cashflows	At 31 March 2010
	£	£	£
Cash at bank and in hand	11,852,561	(2,840,152)	<b>9,012,409</b>
Cash at bank	11,852,561	(2,840,152)	<b>9,012,409</b>
Bank loans:			
The Royal Bank of Scotland plc	(1,082,280)	360,254	<b>(722,026)</b>
Other loans:			
Lancashire County Council	(7,230,000)	-	<b>(7,230,000)</b>
	<u>3,540,281</u>	<u>(2,479,898)</u>	<u><b>1,060,383</b></u>

**17 Operating lease commitments**

Operating lease payments due within one year are as follows :

	2010 Land and Buildings £	2009 Land and Buildings £
Expiring after five years	<u>92,860</u>	<u>92,860</u>

**18 Related parties**

The company has made purchases on behalf of Lancashire and Blackpool Tourist Board Limited of £76,041 (2009 : £137,706). The amount owed by this related party at 31 March 2010 is £8,813 (2009 : £277,032).

Sales from Lancashire Technology Centre during the year amount to £Nil (2009: £29,779). The amount owed by this related party was £50,000 (2009 : £76,915). The amount owed to this related party at 31 March 2010 was £Nil (2009: £8,626).

Sales from Lancashire County Council during the year amount to £2,340,990 (2009: £2,257,466). Purchases with Lancashire County Council amount to £3,760,862 (2009: £3,348,302). The amount owed by this related party at 31 March 2010 is £28,490 (2009: £82,083). The amount owed to this related party at 31 March 2010 is £425,423 (2009: £74,161).



# Agenda Item 4

**Audit Committee**  
24 January 2011

Electoral Division affected:  
All

## **Risk Management Report** (Appendices 'A' & 'B' refer)

Contact for further information:  
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### **Executive Summary**

An important part of the remit of the Audit Committee is to advise the council on the adequacy of the Authority's strategic processes for risk management and to consider reports in respect of the Authority's risk register and the action taken in response.

This report introduces the latest version of the register.

### **Recommendation**

In accordance with the Audit Committee's terms of reference, members may wish to consider whether:

- the content of the corporate risk register reflects the key risks facing the council and whether there are any perceived gaps;
- the actions being taken in response to identified risks appear to be appropriate and, in the light of these considerations; and
- the current process for identifying risk is effective.

### **Background**

Risk management has been an integral feature of corporate and directorate business and financial planning over many years. The corporate risk register is a high level summary of the significant risks which the council faces. It may be regarded as a checklist to identify and track the status of key risks and how these are being managed.

The process for preparing the register has been further refined so that Executive Directors and their senior management teams have direct input into its development. Reference has also been made to risks identified in the areas of business continuity,

emergency planning and health and safety, to ensure that no important risks have been overlooked and all significant risks are reported in one place.

### **The corporate risk register**

A copy of the corporate risk register is attached at Appendix A. It identifies the significant directorate and cross-cutting risks which the council faces together with current and planned actions to mitigate the risks. A scoring system has been introduced with 1 being low and 5 being high, (Appendix B).

The process for maintaining and updating the register will be as follows:

- Directorate senior management teams and contributors from other 'risk' areas identify risks and mitigating actions for inclusion in corporate risk register. Each risk is allocated a lead officer to ensure that proposed actions are completed and a review date is set.
- The Executive Leadership Team has the opportunity to review the updated register prior to it being reported to the Audit Committee.
- The register is presented to the Audit Committee for scrutiny.
- A summary report is prepared for the Executive Leadership Team which comprises cross-cutting and 'high' risks; risks which have been specifically identified for their attention, and any risks which the Audit Committee may refer for further information or action.
- The register is updated with any new actions and changes to risks.

### **Future risk reporting**

The corporate risk register will be updated and presented quarterly, so that members of the Audit Committee are kept up to date with significant changes to the content of the risk register and will be able to scrutinise the actions being taken in response.

### **Background and Advice**

N/A

### **Consultations**

N/A

### **Implications: Risk management**

Risk management is the subject matter of the report.

### **Local Government (Access to Information) Act 1985 List of Background Papers**

<b>Paper</b>	<b>Date</b>	<b>Contact/Directorate/Ext</b>
Risk Management update report to Audit Committee	27 September 2010	Habib Patel, OCE Policy Unit Tel. 36099
Risk Management report to Audit Committee	25 January 2010	"
Risk Management Update report Audit Committee	28 September 2009	"
Risk Management Update report Audit Committee	30 March 2009	"
Risk management update to Cabinet Committee for Performance Improvement	11 February 2009	"
Risk Management Update report Audit Committee	29 September 2008	"
Quarterly Update to Risk Register report to Cabinet Committee for Performance Improvement	18 September 2008	"

Reason for inclusion in Part II, if appropriate

N/A



# Corporate Risk Register – Audit Committee January 2011

# Appendix A

Dir	Potential risk areas	Score without controls		Summary of existing controls and mitigations	Score with controls		What else do we need to do? By whom and by when?	Lead officer on actions	Review date
		Impact	Likelihood		Impact	Likelihood			
ELT	<b>Government Spending Cuts and impact on LCC resources</b>	4	3	Financial scenario taken into account as part of financial planning process  All budget options risk and service impact assessed on an ongoing basis  Regular reports to ELT and cabinet on budget options, ensuring frontline services are protected	3	2	On-going 'horizon scanning' of likely financial scenarios  Continued robust financial and performance monitoring at ELT and Cabinet	ELT	Quarterly
ELT / RES	<b>Strategic Partnership with British Telecommunications plc</b>  - Unprecedented partnership working with a private sector organisation.	3	3	Joint governance arrangements in place prior to commencement  Staff at a senior level from both LCC and BT have been involved to date and will continue to be involved to establish, develop and provide continuity around relationships  LCC Cabinet Committee on the Strategic Partnership established	2	1	Joint Venture Company Board meetings to be held quarterly  Annual Review process to be followed, as contractually agreed	Eddie Sutton, Director of Special Projects	Quarterly
ELT	<b>Effective delivery of the corporate strategy</b>  - failure to measure stated outcomes  - no ownership of the corporate strategy  - no plans in place to highlight and address poor performance	3	3	A council-wide executive performance group chaired by a member of ELT has been established to oversee the delivery of the corporate strategy  A basket of indicators has been established to measure the delivery of the corporate strategy (and Corporate Scorecard)  A performance management framework which identifies under performance and leads to recovery plans being developed and discussed by ELT and the Cabinet Committee for Performance Improvement (CCPI)	2	2		ELT	Quarterly

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OCE	<b>Lancashire Local Enterprise Partnership (LEP)</b> - Need to establish a single economic voice for Lancashire  - Need to engage key business leaders in shaping and delivering agreed economic priorities	3	3	Economic Development Framework agreed  Shadow business leadership group in place  Majority of local authorities in support of Lancashire LEP  Draft LEP governance arrangements in development	2	2	Continue to engage positively with private sector business leaders  Continue to make the case to Government for formal LEP approval	Martin Kelly, Director of Economic Development	Ongoing
ELT / CCG	<b>The Authority to effectively manage the consequences of an emergency, thereby impacting on the delivery of services.</b>	5	3	The Authority has established a governance mechanism through the Corporate Contingencies Group (CCG) to oversee the strategic issues relating to Business Continuity Planning (BCP).  There is a planned roll-out of BCP throughout the Authority in order to build resilience within services.  A reporting system has been established through the Directorate structures to enable the Authority to capture the impacts from Emergencies on Service delivery and to take the appropriate actions to mitigate the effects on service users (i.e. public).  Directorate Emergency Liaison Team established within ACS and currently being developed for CYP & ENV.	3	3	Complete the roll-out of Business Continuity Planning to all services within the Authority and complete the establishment of Directorate Emergency Liaison Team to increase the ability of Directorates to respond to, and manage, emergencies which affect service delivery.	CCG / ELT	April 2011
OCE / PU	<b>Review of Locality Working</b>  Uncoordinated integrated working initiatives with District Councils  Not capitalising on	3	3	Strategy Group established by Executive Director of Policy including Senior Directorate and District Council representatives  On-going liaison with Leadership and facilitation of Leader – Leader discussions	2	2	Need to successfully conclude current round of joint member meetings to agree joint working priorities in each district – by February 2011  Arrange initial meetings of the pilot "Three Tier Forums" in Burnley,	Deborah Ashton Executive Director of Policy	Quarterly

Dir	Potential risk areas	Score without controls		Summary of existing controls and mitigations	Score with controls		What else do we need to do? By whom and by when?	Lead officer on actions	Review date
		Impact	Likelihood		Impact	Likelihood			
Page 41	opportunities to work across tiers of local government in Lancashire to achieve efficiencies and/or improved service outcomes			On-going negotiations with District Councils, including joint discussions at Leader/Executive Member level			South Ribble and Wyre by February 2011		
	Financial, legal or reputational implications not fully considered or addressed			Legal and Financial advice to the Strategy Group			Roll out of Three Tier Forums by April 2011		
	Frontline county councillors feel disengaged when carrying out their role			Package of measures developed to enhance the role of County Councillors, in liaison with the Member development Working Group					
	Lack of clarity around direction of travel with locality working			Report approved at Cabinet 4/11/10 on key elements of way forward, including governance and engagement of all tiers of local government					
				Package of internal and external communications measures implemented November 2010					
OCE / PU	<b>Voluntary Community Faith Sector (VCFS)</b> Sustainability of Third Sector Lancashire (VCFS consortium): no structure through which to facilitate strategic engagement of the sector  Breach of compact principles leading to a challenge for breach resulting in bad reputation and time and resources responding to challenge	3	2	A named LCC officer directly supports and advises the Chair of the Third Sector Lancashire (TSL)  By ensuring that all directorates are fully aware of compact and understand the implications of a breach of the agreement	2	1	Principal Policy Officer CPT continues close relationship with Chair TSL.  Information sharing event to be held in October 2010. Event held November 2010. Now awaiting publication of revised national compact prior to further internal review and communication.	Adrienne Banks	Ongoing
				By setting up internal network of commissioning/procurement teams to ensure understanding and application of third sector principles etc			Information sharing event to be held in October 2010. Core network of relevant officers identified via attendance at information sharing event November 2010. Directors of		
				By ensuring that the financial database is able to deliver reports on full extent					

Dir	Potential risk areas	Score without controls		Summary of existing controls and mitigations	Score with controls		What else do we need to do? By whom and by when?	Lead officer on actions	Review date
		Impact	Likelihood		Impact	Likelihood			
Page 42	Increased involvement of the sector in public service delivery: the risk is not yet clear and is dependent on the extent to which coalition expect to see evidence of more third sector commissioning			financial investment to any VCFS organisation and developing new processes for joint commissioning across directorates			commissioning across authority now agreeing a general approach to commissioning prior to developing a VCFS commissioning framework		
	Uncoordinated approach to funding leading to the possibility of double funding and missed opportunity for joint commissioning and efficiency savings			By reviewing our investment in capacity building to include capability building as well.			Process for tagging VCFS organisations is in progress, but there is still work to do in the accounts payable area. This work is continuing and will be considered as part of the review of commissioning as described above		
	Increased involvement of the VCFS in public service delivery – risk = lack of capacity/capability within the sector to respond			By ensuring that core grants are not awarded to organisations who are already delivering services on our behalf or are likely to submit a competitive tender			Undertake a full review of investment in capacity building and develop proposals for how capability can be developed. This review is continuing and has led to changes to the central gateway programme in relation to funding infrastructure groups. Capacity building will be an integral element of the VCFS commissioning framework.		
	Competition aid i.e. giving core grants to organisations who are tendering for services – risk = possible legal challenge from other VCFS or private sector organisation on the grounds of unfair advantage in competitive market						Undertake a critical analysis of current core funding grants and then consult across the authority on the implications of withdrawing this kind of support. This analysis has been carried out and the outcome is reflected in a new approach to core funding VCFS organisations via the Central Gateway grants programme.		
ACS	<b>Failure of the working partnership between Adult Community Services and health:</b> strategic and operational	4	4	Working more closely with partner organisations in light of changes in government policy, introducing stronger Partnership agreements and looking at joint Project Governance	2	3	Commissioning to prioritise areas where health funding is crucial to delivery of our priorities, secure senior management support within health for the priority areas and	Tony Pounder	Sept 11

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		Impact	Likelihood		Impact	Likelihood			
	failures and negative publicity			<p>arrangements.</p> <p>Collaborating on service delivery with, for example, joint funded posts and integrated delivery teams and the introduction of Public Health within the authority</p> <p>Collaborating on projects with shared project plans and objectives.</p> <p>Prioritising strategic work with new working arrangements in health to maintain ongoing relationships</p>			<p>develop contingency plans in the event of failure.</p> <p>Consider the publication of new government white papers and the implications for ACS and Health and establish change programmes to ensure delivery</p>		
ACS Page 43	<b>Market failure of Adult and Older People provider services – market withdrawals and take-overs leading to reduced capacity for choice.</b>	4	3	<p>Developing robust commissioning and procurement planning systems and strategies which ensure the current and future market is understood and themes are identified for development.</p> <p>Working with providers in identifying their service offer and costs, changes in requirements and areas which might lead to business failure. Development of a preferred supplier list and provider engagement strategy</p> <p>Framework agreements set up with providers providing a broad market across small, medium and large providers which mitigates some of the risks if a provider ceases business</p>	4	2	<p>Using and evaluating an information framework to improve intelligence on market changes, budgetary issues and use of monitoring information.</p> <p>The development and monitoring of more flexible contracting arrangements which assist the use of individual budgets and cut out unnecessary costs from the system</p>	Ann Mylie	May 11
ACS	<b>Recession combined with increased call on budgets on Older People and changing demographic profile (ageing population) leading to increased requirements for services.</b>	4	5	<p>Medium Term Financial planning in place.</p> <p>Robust forecasting tools. Robust and regular Budget monitoring.</p> <p>Well developed financial reporting systems.</p> <p>Careful monitoring of work programmes. Redirection of resources where necessary.</p>	3	5	<p>This risk is now an issue as we await the understanding of what the Government's cuts in budgets means for the Directorate</p> <p>Regular reporting and monitoring by ACS Combined Finance Team and up to Senior Management Team (SMT).</p>	Roger Hulme	March 11

Dir	Potential risk areas	Score without controls		Summary of existing controls and mitigations	Score with controls		What else do we need to do? By whom and by when?	Lead officer on actions	Review date
		Impact	Likelihood		Impact	Likelihood			
							Contingency planning with Heads of Service and agreement with SMT.  Discussions with ELT and Cabinet member on proposals.  Consultations with the public commencing on service cut proposals.		
ACS	<b>Unexpected death or serious injury of service user with Adult Community Services</b>	<b>5</b>	<b>3</b>	Safeguarding Board and Governance in place, Safeguarding Project established, with an Action Plan. Safeguarding Procedures have been refreshed.  Procedures in place should something happen, including Communications unit available to deal with any public information / communication issues.  In House-Providers: comprehensive set of Risk Assessments and Health and Safety Procedures in place.  Staff training programme in place to raise practice standards in safeguarding and familiarise with procedures Deprivation of liberty (DoL) work, like restraint etc training courses, procedures well established Arrangements to review serious cases, including domestic homicide reviews safeguarding on a multi agency basis, so that we can all learn when things go well	<b>5</b>	<b>2</b>	Continue roll out of Safeguarding and Awareness Training.  Complete the Safeguarding Project Action to further improve Safeguarding arrangements and responses.  Approval of Item: Principles of the Mental Capacity Act (MCA) and Dols need to be embedded for people living in their own homes or Supported tenancies. Sufficient capacity and financial funding from the MCA Grant needs to be made available to operations.	Olive Carroll (Mike Banks)	March 11
ACS	<b>Death or serious injury of staff member working within Adult Community Services</b>	<b>5</b>	<b>3</b>	For work with service users: Lone Worker Policy, Risk Assessments and Health and Safety Procedures in place. Robust on call arrangements, use of mobile phones and safety	<b>5</b>	<b>2</b>	Review of framework for all SU related risk assessments to be undertaken as part of Personal Social Care (PSC) work programme: an interim review has	Olive Carroll (Barbara Lewis)	March 11

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		Impact	Likelihood		Impact	Likelihood			
				<p>alarms. Use of virtual whiteboard to track staff whereabouts and monitor returns. Handover arrangements to brief staff of potential problems.</p> <p>PSC Quality Framework project has embedded changes and improvements into PSC working practices. This project completes Jan 2011.</p> <p>Risk Assessment flag in Integrated Social Services Information System</p> <p>For worker self harm: Use of Occupational Health Unit (OHU) assessment where medical conditions exist, return to work procedures for staff who have medical problems.</p>			<p>been done, but once Self Directed Services (SDS) and the PSC restructure is complete, they will be reviewed and updated again.</p> <p>All PSC team lone-worker policies to be reviewed in the context of Agile Working.</p> <p>PSC Quality Framework recommendations need to be fully embedded. This project completes Jan 2011.</p>		
LCCG page 45	<b>Public sector spending cuts leading to threats to workload within the county commercial group services</b>	3	5	Being flexible to reduce fixed costs. Good capacity mgt. Review of Options.	3	4	Awareness, cost reduction and efficiency measures. Development of Options.	Nigel Finnamore	Ongoing
LCCG	<b>Sustainability post Equal Pay Review within Commercial Services</b> - increased costs - disaffected employees - impact on costs and competitiveness	3	4	As above Working with Equal Pay Review team so implications of proposals clear Sustainability and affordability for directorates will be considered	3	3	Identify measures to be taken to mitigate costs.	Nigel Finnamore / Bernard Noblett	Ongoing
LCCG	<b>Serious Health and Safety Service Failure</b> (including food hygiene) potentially involving:  - employee - someone in our care - member of public  <b>Costs associated with accidents</b> (fines,	5	4	<p>Existing Integrated Management System with areas of the organisation 3rd part registered to OHSAS 18001.</p> <p>Other part of the organisation operating management systems in accordance with OHSAS 18001.</p> <p>Audits by IMS team</p> <p>Competency based training in</p>	5	3	<p>Review of Integrated Management Systems to simplify, integrate and to reduce bureaucracy and increase accessibility via the intranet*. Action By MDS (Dec 2012)</p> <p>Revision of Catering procedures to determine suitability. Action By Janette Mason / IMS (Jan 2011)</p>	Nigel Finnamore	Quarterly

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Page 46	litigation, insurance costs), business disruption, LCCG's reputation. Resulting in reduced profitability e.g. impact of Corporate Manslaughter and Corporate Homicide Act – Larger fines, publicity orders and impact on future business.			Operations.  Health and Safety Performance reported at all Senior Management Teams.  Greater emphasis on incident reviews and lesson learned. IMS team's audit schedule with increased audits and non conformance close outs monitored and trends analysed. Hazard Analysis and Critical Control Point for School and Care Catering			Improved Health and Safety Performance data management through development of Incident reporting software. Action By MDS / BIS (Apr 2011)	Nigel Finnamore	Quarterly
							IMS Business Plan to address main health and safety issues Action By MDS (Apr 2011)	Nigel Finnamore	Monthly
Adverse impacts of weaknesses in quality or security of information, information systems or information handling within the organisation, in electronic and paper forms.	4	4	Corporate Information Governance Group  Directorate information Champions  Guidance, policies and procedures on Intranet and in e-Learning Course.  Management processes in place and in business planning process.  Security controls and encryption protection  Statements of conformity, spot checks and security breach procedures.	3	3	Annual Information Risk Review underway.  External review of all governance documentation  Technical infrastructure review underway plus penetration testing.  Data Quality Strategy Statement of Conformity returns being collected.  Large intranet site full of guidance: <a href="http://lccintranet2/corporate/web/view.aspx?siteid=4305">http://lccintranet2/corporate/web/view.aspx?siteid=4305</a>	SIRO + CIGG	June 11	
Failure to comply with Information Governance requirements e.g. Freedom of Information Act, Data Protection Act  Legal penalties in the event of breaches of	4	4	Management controls, including effective logging and tracking, complaints and appeals procedures Effective use of technology The Publication Scheme has been reviewed and updated, and the model publication scheme approved by the Information Commissioner adopted.	3	3	Some staff training and awareness sessions have taken place with many more still to take place. The work load of the Access to Information Team continues to increase due to the growing number of Freedom of Information requests and Data Protection enquiries/subject access requests.	SIRO + CIGG	June 11	

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	<b>Data Protection Act e.g. Civil Monetary Penalty, potentially up to £0.5million</b>						Additional resources for the team are being considered Directorate IG champions to be vigilant looking for examples of data misuse in particular that data is: 1. Fairly and lawfully processed 2. Processed for limited purposes 3. Adequate, relevant and not excessive 4. Accurate 5. Not kept longer than necessary 6. Processed in accordance with the data subject's rights 7. Secure 8. Not transferred to countries without adequate protection. CIGG to review security breach records from security breach procedure and look for trends and issue action plans and guidance accordingly		
Page 47 CYP	<b>Death or serious injury of a child known to us, or who have been known to us as a result of systemic failure</b>	5	3	Multi-agency safeguarding children Board Arrangements in place and safeguarding children procedures updated. Mechanisms in place Closely monitor referrals and assessments and children subject to Child Protection Plans Provide training and support to staff including multi-agency training Child death and Serious Case Review Panels in place to learn lessons and disseminate learning to practitioners and managers Monitor Educational Visits and policy and guidelines in place	3	3	Continued implementation of service and post inspection action plans Multi-agency conferences disseminating lessons from Serious Case Reviews both within Lancashire, regionally and nationally. Complete roll out of Contact and Referral Team to improve responses to referrals and improve assessments. Continue to improve information sharing between agencies via training and agreed procedures and protocols. Continue to explore integrated and co-located multi-agency teams to improve assessments and information sharing between agencies.	Tony Morrissey Head OF Safeguarding Inspection & Audit	Ongoing

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CYP	<b>Failure in performance in schools and other educational settings</b>	<b>4</b>	<b>5</b>	Quality Audit Tool used by Early Years (EY) consultants with EY settings. Early warning system identifying schools/settings at risk of failure on wide range of factors. Settings where there are concerns are monitored and supported by the Early Years Special Support Group. Schools where there are concerns relating to Finance, Personnel, Governance, Standards, Quality of Education are reported to, monitored and supported by the Directorate Special Support Group. Contracts of support are provided for schools in difficulty including school to school support. Review the Early Warning systems in the light of the new Ofsted Framework for Inspection (Head of QCI March 2010).	<b>2</b>	<b>4</b>	Develop the Early Years Workforce so that all settings have an accredited Early Years Professional in post by 2015 (Head of QCI). Develop the support/challenge / monitoring arrangements for Children's Centres as they become established and subject to Ofsted inspection (Head of QCI July 2010). Further develop school to school support programmes through collaborations / federations, particularly where appointment of head teachers is problematic (Head of QCI/D&I July 2010).	Ann Pennell Director for Commissioning, Performance and Business Support	Ongoing
P Q 8	<b>Workforce recruitment and retention</b> within Children's services- capacity to undertake workforce planning; shortages of key skills/workers/leaders; low levels of workforce well-being & poor retention; lack of key leadership competencies; lack of training & development opportunities	<b>3</b>	<b>3</b>	<ul style="list-style-type: none"> <li>• Children's Workforce Strategy in place. Implementation underway</li> <li>• Common workforce data collection undertaken</li> <li>• Leadership development programme underway</li> <li>• Development of career pathways across sections of the Directorate</li> <li>• Range of initiatives in place for work-based recruitment – teachers (GRTP), social workers, apprentices &amp; graduate trainees</li> <li>• Range of training &amp; development opportunities to support retention and progression</li> <li>• Flexible working arrangements in place</li> <li>• Range of staff well-being schemes across Directorate</li> <li>• Talent Pool programme in place.</li> </ul>	<b>2</b>	<b>1</b>	<ul style="list-style-type: none"> <li>• Continue development and implementation of Children's Workforce Strategy</li> <li>• Implement change programme projects</li> <li>• Managing budget/staffing reductions through a managed process of restructuring</li> <li>• Transition CYP Change Programme to Continuous Improvement Programme</li> </ul>	Dave Carr, Head of Efficiency and Business Support	Ongoing
CYP	<b>Inspection failure</b> in limiting judgement area	<b>4</b>	<b>3</b>	Post inspection action plans in place monitored by DLT	<b>3</b>	<b>2</b>	Partnership Board with other agencies being established to look	Ann Pennell Director for	Ongoing

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	relating to services to children, young people and families which leads to failure in performance of the County Council as a whole			Inspection preparation groups in place Mock inspections being undertaken Service plan and performance management framework in place Audit team established			at undertaking multi-agency mock inspections	Commissioning, Performance and Business Support	
OCE	<b>Equal Pay Review</b>  leading to: <ul style="list-style-type: none"><li>- serious industrial action;</li><li>- significant numbers of tribunal claims;</li><li>- difficulties in retaining staff;</li></ul>	4	5	A Collective Agreement has now been signed by the main trade unions agreeing to most of the new terms and conditions introduced wef 1 August 2010.  On-going dialogue with trade unions and continuing communication with staff.  Ongoing communications with schools to keep them engaged and informed	2	2	Continue communication with staff groups affected and trade unions.  Continue engagement of senior managers to ensure consistent messages are given and communicated to staff.  Continue and complete the JE appeals process.  Complete JE for special and chief officer grades.  Complete JE for other staff groups e.g. soulbury grades.	Deputy County Secretary and Solicitor	Quarterly
ENV	<b>Surface water flooding.</b>  LAs now responsible for surface water management (Flood and Water Management Act April 2010)	2	4	Ongoing development of Surface Water Management Plan for Lancashire. Development of prioritised and targeted action to reduce risk.	2	3	Re-prioritise capital funding. Develop in-house expertise.	Jo Turton, Executive Director	Six - Monthly
ENV	<b>Loss of highway infrastructure due to flooding</b>	3	2	Regular inspections currently being undertaken on all highway bridges. "Structures at Risk Register" being developed with increased frequency of inspections on these highway structures. Special Inspections of "at-risk" highway structures being undertaken immediately following localised high rainfall events.	3	1	Close monitoring of risk via service risk register (ongoing)	Jo Turton, Executive Director	Annually
ENV	<b>Failure of Waste PFI Contract</b> - financial and reputation risk.	2	2	Weekly, Monthly, Quarterly and Annual monitoring and reconciliation of data and performance against both diversion and financial targets.	2	1	Close monitoring of risk via service risk register (ongoing)	Jo Turton, Executive Director	Six - Monthly

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				Maximising throughputs and exploring commercial opportunities from various sectors will aid in the challenge to effectively manage baseline costs.					
ENV	Corporate Manslaughter on highway	<b>1</b>	<b>1</b>	Highway safety inspections (3,6 or 12-monthly as appropriate) .Annual skid resistance surveys. Bi-annual bridge inspections. Monitoring of highway slopes and embankments.	<b>1</b>	<b>1</b>	Close monitoring of risk via service risk register (ongoing)	Jo Turton, Executive Director	Six - Monthly
ENV	Failure of Public Transport Contracts - financial and reputation risk	<b>2</b>	<b>2</b>	Public transport operators closely monitored. Where appropriate, contingency measures are put in place allow us to replace contracts quickly and efficiently should the need arise.	<b>2</b>	<b>1</b>	No further action proposed	Jo Turton, Executive Director	Six - Monthly

## Appendix B

### CORPORATE RISK ASSESSMENT

#### Impact

Score	What's the worst that could happen?
1	<ul style="list-style-type: none"><li>• Insignificant disruption with no loss of service to citizens</li><li>• No harm to life or limb</li><li>• No reputation damage</li><li>• No or insignificant environmental damage</li><li>• Low financial loss</li></ul>
2	<ul style="list-style-type: none"><li>• Some disruption to non-critical citizen service</li><li>• LCC liable for disruption to key partner but no loss of service</li><li>• Minor injury to third parties (requiring first aid treatment)</li><li>• Minimal reputation damage (minimal adverse coverage in local press)</li><li>• LCC responsible for minor damage to local environment</li><li>• Medium financial loss</li></ul>
3	<ul style="list-style-type: none"><li>• Noticeable disruption to critical service not exceeding 48 hours</li><li>• LCC responsible for disruption to key partner resulting in loss of their service not exceeding 48 hours</li><li>• Violence or threat of serious injury (medical treatment required)</li><li>• Adverse coverage in national tabloid press and/or extensive front page coverage in local press or TV</li><li>• LCC liable for moderate damage to local environment</li><li>• High financial loss</li></ul>
4	<ul style="list-style-type: none"><li>• Serious disruption LCC's ability to provide a critical service to citizens (loss of service between 2 and 7 days)</li><li>• LCC responsible for major disruption to key partner resulting in a loss of their service lasting between 2 and 7 days</li><li>• Adverse coverage in national broadsheet press and/or low level national TV reporting</li><li>• Extensive and multiple injuries</li><li>• LCC liable for major damage to local environment</li><li>• Major financial loss</li></ul>
5	<ul style="list-style-type: none"><li>• Central Government intervention in running of LCC / Directorate</li><li>• Loss of critical citizen service for more than 7 days</li><li>• Business failure of partner or loss of service delivery of over 7 days</li><li>• Multiple injuries including loss of life</li><li>• Extensive coverage in national press and broadsheet editorial and/or national TV item</li><li>• Significant local, national or international environment damage</li><li>• Enormous financial loss</li></ul>

### Likelihood

Score	Descriptors
5	Almost Certain. Expected to occur in most circumstances or more than a 75% chance of occurrence.
4	Likely. Potential of occurring several times in 10 years or has occurred recently. Between 50% and 75% chance of occurrence.
3	Moderate. Could occur more than once in 10 years. History of occurrence or near miss. Less than a 50% chance of occurrence.
2	Unlikely. May occur over a 10 year period. Less than 10% chance of occurrence.
1	Rare. Has not occurred. May occur in exceptional circumstances. Less than 2% chance of occurrence.

### Impact / Likelihood matrix

		Impact				
		1	2	3	4	5
Likelihood	5	1/5	2/5	3/5	4/5	5/5
	4	1/4	2/4	3/4	4/4	5/4
	3	1/3	2/3	3/3	4/3	5/3
	2	1/2	2/2	3/2	4/2	5/2
	1	1/1	2/1	3/1	4/1	5/1

Level of Concern	Action Required
Very concerned	Urgent attention required at senior level to ensure risk is reduced to an acceptable level. Action planning should start without delay. Progress on actions should be reported to ELT.
Concerned	Minimum of robust contingency plan plus early warning indicators. Some control measures likely to be necessary. Progress on actions should be reported on at directorate senior management team.
Uneasy	Acceptable with some mitigation and contingency planning. Routine reviews should be carried out to ensure there has been no change which will make them more severe.
Content	Acceptable, but keep under review. No further action required unless risk becomes more severe.

# Agenda Item 5

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected:  
All

### Update on treasury management activity

Appendix 'A' refers

Contact for further information:

Mike Jensen, 01772 534742, Resources Directorate  
[mike.jensen@lancashire.gov.uk](mailto:mike.jensen@lancashire.gov.uk)

#### Executive Summary

The revised treasury management policy 2009-10 was approved by full Council on 17<sup>th</sup> December 2009. Full Council approved the Annual Treasury Management Strategy 2010/11 on 25<sup>th</sup> February 2010. Implementation of the new strategy began on 4<sup>th</sup> of January 2010 and this report updates the progress made under the new strategy in terms of de-risking the investment portfolio whilst improving investment returns. As part of the Comprehensive Spending Review the Government increased the cost of borrowing to Local Authorities. The implications for future financing of capital expenditure is that borrowing from the market will be cheaper than from the Public Works Loans Board. Consequently plans are now being developed to raise funds in capital markets.

#### Recommendation

The Committee is asked to note the report on recent treasury management activities in Appendix 'A'.

#### Background and advice

At the meeting of the Cabinet on 9 July 2009 it was agreed that in order to strengthen members' oversight of the County Council's treasury management activities, the Audit Committee should monitor and scrutinise regular updates on treasury management issues. Reports on treasury activity are discussed on a monthly basis with the Executive Director for Resources and the content of these reports is used as a basis for this report to the Committee. The aim of the report is to inform members of the general economic environment surrounding treasury management activities and to set out the position on the borrowing and lending activities of the County Council.

The overall position set out in the report at Appendix 'A' is one where the County Council is reducing credit risk whilst maintaining investment income rates and also making plans to raise future capital financing funds in capital markets.

## **Consultations**

Sector Treasury Services Limited provides advice on treasury management.

## **Risk management**

The County Council's treasury strategy and review set out a policy in respect of borrowing and lending activity and how risks associated with these activities are managed and monitored.

## **Alternative options to be considered**

N/A

**Implications:** e.g. Financial, Legal, Personnel, Human Rights, Crime and Disorder or Other

This item has the following implications:

N/A

## **Local Government (Access to Information) Act 1985**

### **List of Background Papers**

Paper	Date	Contact/Directorate/Ext
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N/A

## **Appendix A**

### **Update on Treasury Management activity**

#### **Background**

This is the latest report on the conduct of the Council's Treasury Management activities which allows the Audit Committee to exercise its responsibilities for oversight of this area of the Council's business. Reports on treasury activity are discussed on a monthly basis with the Executive Director for Resources and the content of these reports is used as a basis for this report to the Committee.

#### **Economic Overview**

Much of the detail around fiscal tightening has now been announced but little has actually been introduced yet so it is a little early to gauge the likely results in terms of the interest rate landscape and the effects on the UK economy at large.

It is likely that changes in taxation, in particular VAT, will continue to put short term pressure on inflation and that in combination with general fiscal tightening the consumer is likely to remain under strain. Discretionary spending should be most at risk. Wage freezes and redundancies in the public sector may be offset by increased activity in private industry but relative impacts of these two opposing forces will take time to evaluate. Although headline inflation will certainly remain high for the near future leading some to call for an increase in interest rates, recent poor employment and average earnings data suggests the Monetary Policy Committee (MPC) will resist the increase until the recovery is more evident in the economic data.

The sensitivity of the UK economy as a whole to interest rate movements is larger now than previously and consequently we believe the Bank of England will be very cautious in shifting monetary policy. The Governor of the Bank has made it clear that the current high levels of inflation are likely to be transitory and that fiscal tightness and the output gap will most likely bring this overshoot down in the medium term. In fact the Monetary Policy Committee is still very nervous that deflation could be the outcome of government policy combined with world events (core inflation excluding tax changes is well below the 2% CPI target). The MPC is aware that periods of deflation are much more difficult for monetary authorities to deal with than inflation.

Economic data has remained mixed overall, although in recent weeks data has generally been more supportive of the recovery thesis but as little of the announced fiscal tightening has taken effect yet, caution is still advised.

The major market risks currently come from two sources:

- Sovereign credit issues especially around peripheral Europe and the impact of these on the banking systems in Europe
- Global trade, growth and currency imbalances; Emerging World growth is being heavily relied on by the developed world and many bellicose noises are being made on currency values with hints of trade protectionism

Should either of these issues develop badly then the risks to the whole markets are very large.

## Major Developments

On the same day as the Comprehensive Spending Review, the Treasury announced that, with immediate effect, the Public Works Loans Board would increase the cost of loans to Authorities by an average of 1.00% per annum across all maturities, whilst retaining its draconian early repayment penalty charge (now 1.33% per annum). This change will lead to a fundamental re-appraisal of Local Government capital financing.

The intention of the Government is clearly that there should be a very significant reduction in the overall level of local authority "self financed" capital expenditure (i.e. expenditure financed by means other than grant). In addition this move creates a push for Authorities to fund either in the capital markets or the money markets, or a combination of the two. The capital markets are most appropriate for larger authorities given that they are most likely to be able to deal with the required size of issuance and professionalism of approach. There is, however, a very large **BUT**; in order to properly manage such a process and the concomitant risks, Authorities will need to have access to a number of tools not currently used by Local Government.

This move has the potential to add further costs to local authority borrowing. However, although funding through the capital markets may add further layers of complexity and difficulty to the treasury management function it also could present many opportunities to improve performance and reduce costs.

At the same time as PWLB rates became uneconomic; the traditional banking alternatives have evaporated. Changes to bank's funding and reserve cost regimes have made it either prohibitively expensive to lend or regulatorally impossible. Therefore the capital markets are the likely solution for Local Authorities and the County Council is actively developing plans in this area in order to minimise future costs and risks, whilst at the same time maximising opportunities. There is substantial demand in the UK for Sterling denominated bond issues in either long dated (over 30yrs) fixed rate or index linked format, but such deals will need to fulfil certain requirements,

- Local Authorities will need to be credit rated by at least one of the two main agencies (Moodys, or Standard and Poor).
- Institutional investors need to have the confidence that they can buy and realise their investment easily and this depends upon the market being able to absorb the supply and demand that their positions generate. For this reason bond issues in Sterling will need to be above a critical size to qualify as liquid (£150m minimum.) and therefore give institutional investors the confidence needed.
- Bonds will need to be issued via special purpose vehicles for tax reasons.
- A strong group of market makers will need to be involved in the issuance of such bonds in order to provide buyers with the liquidity they need. Market makers quote bid and offer prices (ie make a market) for securities and crucially are prepared and able to buy or sell those securities at any time on

their own account, so ensuring that prices and buying and selling opportunities are always available to investors.

There will also be good demand for Local Authority bonds issued in other currencies and in other formats (hedged back into Sterling) with the added benefit that such issues will not need to be so large.

The best mechanism for such issuance will be in the form of a Medium Term Note (EMTN) programme, a coverall documentation that allows for multiple issuances of bonds without the need to repeat legal and contractual work and under which various type of debt and currency instruments can be created. In the past each time an issuer came to the market to raise funds a separate set of legal documents would be produced, new legal and listing opinions sought (and paid for). The development of the EMTN mechanism (an ongoing listing and legal framework) was driven by the need to streamline and simplify the legal process. It is now the norm for any borrower who is likely to raise debt more than once over the period of a few years. The single route is still available but completely inflexible.

Similar programmes for money market issuance can be created, Commercial Paper Programme (ECP) which will allow for access to short term cash held by corporation and money funds, these institutions are still concerned about credit risk with much of the European banking system but will only lend to rated institutions via formalized programmes.. This will reduce the Council's reliance on bank funding or loans from other Authorities.

**The Treasury Management team will engage the Moodys credit rating agency with a view to acquiring both short and long term credit ratings, the indicated ratings are P1 (top short term rating) and Aaa (top long term rating). If these ratings are achieved the next step will be to negotiate the construction of EMTN and ECP programmes with a group market makers.**

### **Advisory Services**

The current contract with Sector Treasury Services is due to be re-tendered and in light of the above mentioned opportunities to change our approach to capital financing, an area in which Sector have very limited expertise, timing for such an exercise is propitious. We are preparing documentation in conjunction with the procurement team with a view to seeking an enhance quality and scope of service, while also allowing other Council's in Lancashire to access the services provided under the contract as part of the shared services agenda. It is intended that the new contract will begin in early May. In the meantime a 6 month contract extension has been agreed with Sector.

### **Local District Councils**

The Audit Commission and CLG reports following the Icelandic Banking Crisis both highlighted the particular problems District Councils face in their treasury management activities. In order to gain an acceptable rate of interest they need to go to the market with a sizeable sum for investment. Due to the size of the overall

budget, this would represent a large proportion of the available balances and therefore an unacceptable credit risk.

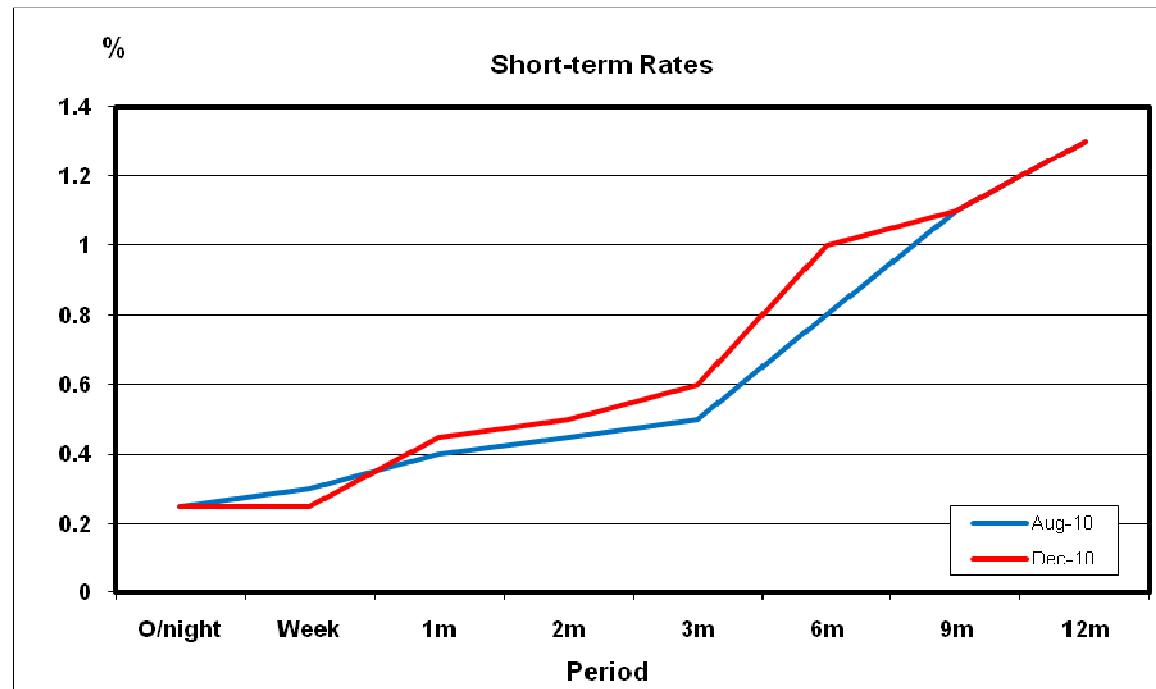
In response to this and as part of the shared service agenda, the County Council offers an investment opportunity on a call account basis to the Lancashire Districts with a view to reducing their counterparty risk whilst still providing a good level of interest. The facility was opened in mid June 2010 and to date 10 Districts have taken advantage with funds totalling to £36m. The benefit to the Districts is that they have earned approximately twice as much interest on their balances compared with the UK Government's Debt Management Account whilst maintaining a comparable very low credit risk.

In conjunction with the call deposit the Treasury Management Team also provides a fixed deposit facility enabling local Authorities to invest funds for a longer period of time.

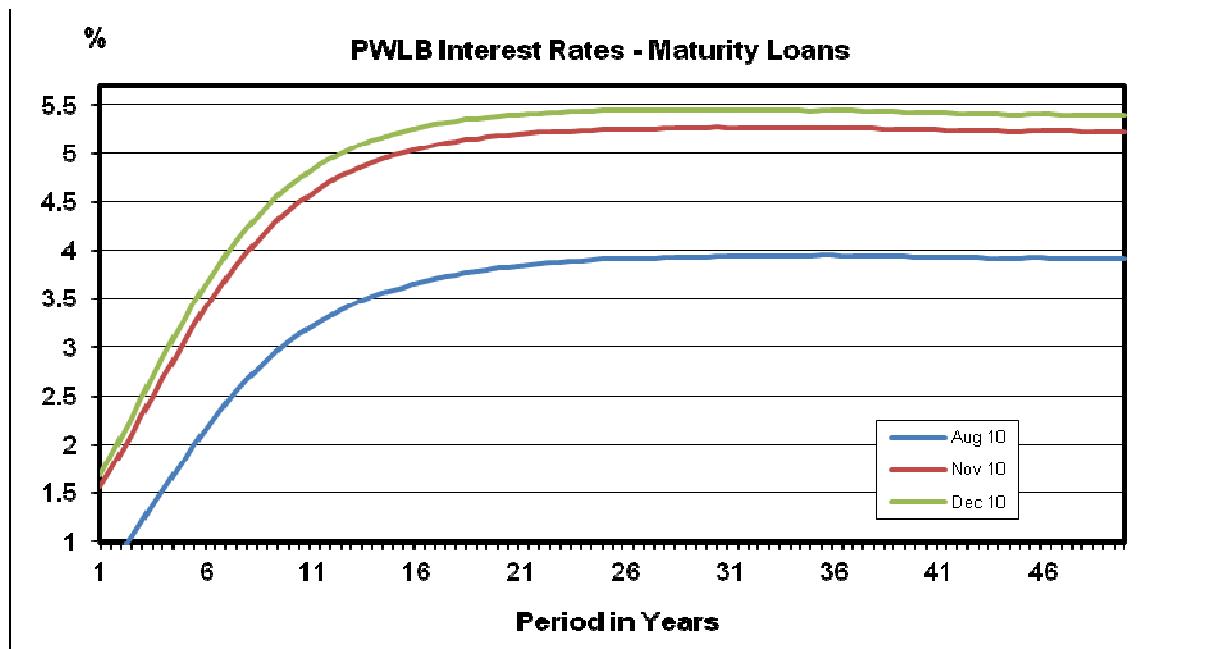
In both cases the funds invested count against the County Council's overall borrowing requirement.

### Borrowing and Investments

Short term interest rates continue at the very low levels since the Bank of England reduced the base rate to 0.5% in March 2009. The chart below shows the current levels.



Current longer term PWLB rates are shown below:



The current PWLB rates and revised forecast of interest rates, published recently, are as follows:

#### Economic Forecasts – Sector Treasury November 2010

	End Q4 2010	End Q1 2011	End Q2 2011	End Q3 2011	End Q4 2011	End Q1 2012	End Q2 2012	End Q3 2012
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%
5yr PWLB rate	3.00%	3.00%	3.10%	3.20%	3.30%	3.50%	3.80%	4.10%
10yr PWLB rate	4.10%	4.10%	4.10%	4.20%	4.30%	4.40%	4.60%	4.80%
25yr PWLB rate	5.00%	5.10%	5.20%	5.30%	5.30%	5.40%	5.40%	5.40%
50yr PWLB rate	5.10%	5.20%	5.30%	5.40%	5.40%	5.50%	5.50%	5.50%

#### Economic Forecasts – Capital Economics November 2010

	End Q4 2010	End Q1 2011	End Q2 2011	End Q3 2011	End Q4 2011	End Q1 2012	End Q2 2012
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%
5yr PWLB rate	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
10yr PWLB rate	3.75%	3.75%	3.75%	3.75%	3.75%	3.75%	3.75%
25yr PWLB rate	4.80%	4.80%	4.80%	4.80%	4.80%	4.80%	4.80%
50yr PWLB rate	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%

#### Economic Forecasts – UBS November 2010

	End Q4 2010	End Q1 2011	End Q2 2011	End Q3 2011	End Q4 2011	End Q1 2012	End Q2 2012
Bank Rate	0.50%	0.50%	0.50%	0.75%	1.00%	N/A	N/A
10yr PWLB rate	4.00%	4.10%	4.30%	4.50%	4.60%	N/A	N/A
25yr PWLB rate	5.10%	5.10%	5.10%	5.20%	5.30%	N/A	N/A
50yr PWLB rate	5.10%	5.20%	5.20%	5.30%	5.40%	N/A	N/A

## Borrowing activity

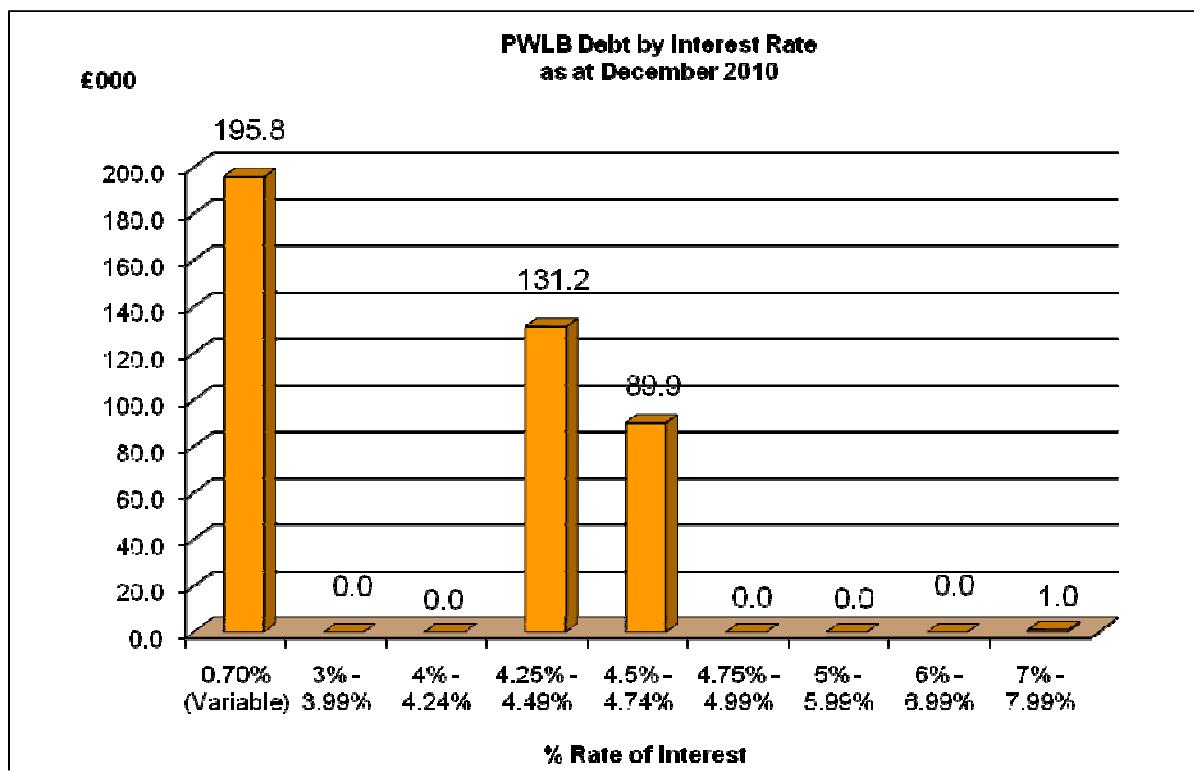
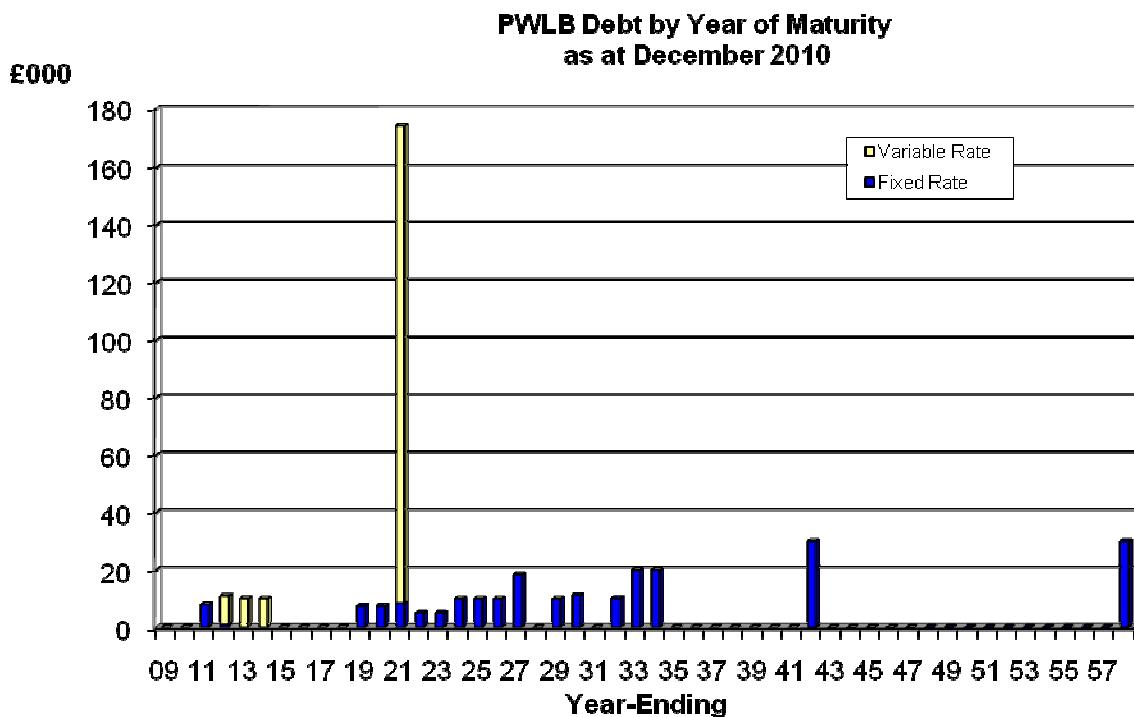
The actual 2009-10 borrowing position compared with the estimate based on the revised capital program is shown in the following table:

	2009-10 Estimate £000	2009-10 ACTUAL £000	2010-11 Estimate £000	2011-12 Estimate £000
Supported Borrowing	54,214	43,627	39,814	27,900
Unsupported Borrowing	44,998	21,335	41,136	42,714
Maturing Long Term Debt	15,029	15,029	9,029	20,514
Less transferred debt repayments	-4,069	-4,069	-4,069	-4,069
Less Minimum Revenue Provision	-21,175	-22,465	-24,272	-26,339
Less advance borrowing brought forward from previous years	-17,459	-17,459	-10,000	
Total requirement 2009/10	<b>71,538</b>	<b>35,998</b>	51,638	60,720
Actual short term borrowing 09-10		<b>98,000</b>		
Actual long term borrowing 09-10		<b>10,000</b>		

The 2009/10 borrowing requirement stands at £35.998m after taking into account the advance borrowings brought forward from 2008/09 and the decisions taken by Cabinet in September 2009 in respect of switching revenue contributions to the capital programme to prudential borrowing. This is less than initially anticipated due to slippage in the Capital Programme and the application of grants rather than anticipated borrowing on the BSF project.

The policy in place since investment rates have been falling has been to use internal cash balances in lieu of borrowing to fund capital expenditure, as this had been the least expensive option, but recently short term borrowings from the market have become cheaper than "self funding", consequently in order to secure the Authority's liquidity position £108m has been borrowed from other Local Authorities with a range of short maturities from 9months to 15months at an average cost of 0.65%. Our view is that UK rates will stay low for longer than the market expects and that longer rates will fall from current levels – should this view be confirmed we will refinance accordingly.

The following graphs highlight the interest rates payable on the County Council's long term PWLB borrowings along with the maturity profile.



During the period we have taken £50m of long term finance (50yr maturity with calls each 5yrs) in structured format such that if 10yr rates rise the cost of this borrowing falls proportionately. This was a risk management decision, to diversify our interest rate sensitivity exposure.

## **Investments**

Following the formal approval of the revised investment policy at Council on 17th December 2009, the County Council is now operating a credit de-risking strategy using information from the credit default swap market in addition to credit ratings to assess counterparty reliability and by increasing our exposure to sovereign credit at the expense of bank risk.

It has been our view since the beginning of 2010 that market expectations of early and sharp rises in base rate were too aggressive and that the steepness of the forward interest rate curve would have to be pegged back. We have continued to express this view via purchases of government, government guaranteed and supranational bonds as well as looking to more closely match our reserve characteristics.

With the current financial instruments available to Local Government, it is impossible to fully protect a portfolio against inflation and interest rate increases whilst at the same time providing a reasonable return in the present. Without access to the derivatives market, to be able to respond quickly to changes in the environment, investments must be highly liquid; if interest rates rise investments can be switched quickly to take advantage of the higher rates. However, liquidity is expensive and to access reasonable rates in the present environment investment maturities must be pushed out and liquidity given up. One of the tasks of the Treasury Management Section is to balance these two conflicting risks. As a partial offset to hedge against a rising inflation environment we have made purchases of inflation linked bonds issued by European Investment Bank (AAA) and Network Rail (UK govt guaranteed bonds). These bonds perform well in high inflation environments since although the coupon payments are fixed, the principal repayment is index linked as long as they are held to maturity. However the value of the bonds rises and falls depending on the markets view of future inflation expectations.

### **Strategic Medium Term Investments under New Treasury Management Policy**

<b>Maturity Range</b>	<b>Amount £M</b>	<b>Average Rate</b>
1-2 Years	3.00	1.60%
2-3 Years	167.60	2.92%
3-5 Years	25.00	3.30%
Local Authority Bonds	28.00	4.84%
Bonds	113.00	3.70%
Index Linked Bonds	87.40	5.05%
<b>Totals</b>	<b>424.00</b>	<b>3.71%</b>

In terms of credit risk, the Local Authority Bond portfolio along with the Bonds and Index linked bonds are all either UK Government or Supra-national (ie Multi- national Investment Bank) backed securities. The majority of the rest of the portfolio is made up of bank deposits with UK Government owned banks. The only other institutions with which the County Council has funds with a maturity period longer than overnight are Barclays and Santander Banks.

For the portfolio overall this represents a much reduced credit risk compared with the previous policy.

One of the items on the Treasury team's workplan for 2011 is to look into formal models of risk management.

### **Landsbanki**

At the time the Icelandic banks collapsed in October 2008, the County Council had an investment of £10.0m with Landsbanki.

In November 2009 the Landsbanki Winding Up Committee confirmed that wholesale depositors, including local authority deposits, would be treated as preferential creditors within the administration process. This decision was expected and was the basis of estimates that creditors could expect an eventual payout of around 83p in the pound. However, the Winding Up Committee of another Icelandic bank, Glitnir, later decided the wholesale depositors were not preferential creditors in their administration process. At this moment in time there is no direct connection between the Glitnir and Landsbanki decisions but clearly they are inconsistent. Both decisions have been appealed, and if the Landsbanki decision is overturned, the County Council can expect a much lower return from the administration process, current estimates vary between 23 - 27p in the pound. The appeals process continues with the Authority being represented by the Local Government Association and legal advisors Bevan Brittan. Currently all information is subject to legal privilege due to commercial confidentiality and although there is considerable uncertainty around the expected date of a conclusion to the appeals process the committee will be kept informed of developments.

### **Recommendation**

The Committee is asked to note the above report on treasury activity.



# Agenda Item 6

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected:  
All

### **Overview of the implementation of International Financial Reporting Standards for the accounts of the County Council (Appendices A & B refer)**

Contact for further information:

George Graham, 01772 538102, Resources Directorate,  
[george.graham@lancashire.gov.uk](mailto:george.graham@lancashire.gov.uk)

#### **Executive Summary**

The 2010/11 Statement of Accounts for Local Authorities must be completed under International Financial Reporting Standards (IFRS). Authorities must use a transitional date of 1<sup>st</sup> April 2009, in order to include comparative 2009/10 figures under the new standards within the 2010/11 Statement of Accounts. Preparation for the transition must be made now to ensure that accurate and comparative figures are in place for the changeover.

A Project Team and Project Plan have been established to review the impact of the transition to IFRS from the current reporting standards on our current arrangements and to ensure that the implementation is achieved satisfactorily.

Progress continues to be made, and the project team is on track to implement IFRS in accordance with the statutory deadlines. Close liaison with the District Auditor is being maintained throughout the process.

Audit Committee agreed at the meeting on 25<sup>th</sup> January 2010 that the Committee would receive regular progress reports on the implementation of IFRS.

#### **Recommendation**

That the report be noted.

#### **Background and Advice**

Local Authorities currently prepare their annual statement of accounts under United Kingdom Generally Accepted Accounting Practice (UK GAAP). However, in order to allow comparability and consistency with the private sector, it was announced in the 2008 Central Government Report that from 2010/11 Local Authorities are required to produce their annual statement of accounts under International Financial Reporting Standards (IFRS).

Appendix A gives an overview of the key facts relating to the implementation of IFRS, and progress made on those aspects. Appendix B is an updated copy of the project plan that the IFRS Project Group is working to and will be reported back to Audit Committee on a quarterly basis until implementation is complete.

### **Consultations**

Not applicable

### **Risk Management**

This item has the following implications, as indicated:

Financial – Significant existing resources within Finance Teams will need to be utilised to deliver the transition to IFRS. The project plan and regular project team meetings should enable staff to plan the time they need to dedicate to the transition process.

Legal – The production of the statement of accounts under IFRS is a statutory requirement.

### **Local Government (Access to Information) Act 1985 List of Background Papers**

Paper	Date	Contact/Directorate/Tel
N/A	N/A	N/A

Reason for inclusion in Part II, if appropriate

N/A

## **Progress report on the implementation of International Financial Reporting Standards for the accounts of the County Council**

**24<sup>th</sup> January 2011**

### **1. Executive Summary**

- 1.1 Local Authorities are required to adopt International Financial Reporting Standards (IFRS) from 2010/11 onwards. Although IFRS is fully implemented from 1 April 2010, the transition date is 1 April 2009. The transition process from current financial reporting standards to IFRS will have a significant impact on the accounts of the County Council; therefore a project plan has been put in place to ensure a successful transition and to maintain both the quality and integrity of the County Council's accounts.
- 1.2 The report aims to provide the Audit Committee with assurance that the implementation is progressing well, and that the County Council is on track to successfully implement IFRS on time with no compromise to the quality of the County Council's accounts.

### **2. Background**

- 2.1 Local Authorities are currently required to prepare their annual Statement of Accounts in accordance with United Kingdom Generally Accepted Accounting Practice (UK GAAP).
- 2.2 In the 2008 Pre Budget Report it was announced that Local Government must implement IFRS from 2010/11 onwards. The aim of the change in financial reporting standards is to bring comparability and consistency between financial reports in the global economy and to follow private sector best practice.
- 2.3 As part of the 2010/11 Statement of Accounts process Local Authorities are required to fully re-state their 2009/10 UK GAAP accounts under IFRS.
- 2.4 Central Government and NHS have an earlier implementation date of 2009/10, therefore Local Authorities can learn from both their successes and the challenges faced during the transition process.

### **3. Progress to Date**

- 3.1 The IFRS Project Group has continued to monitor progress since the last Audit Committee. Work has been done to prepare for the production of the Council's transition accounts but this has been limited by the late release of the technical guidance manual which provides the main tool in determining the accounting treatment to be utilised in producing these accounts.

## **Appendix A**

- 3.2 The delayed issue of the guidance has meant that the deadline for the production of the transition accounts has had to be extended and it now coincides with the statutory deadline for the production of the council's 2010/11 accounts in June.
- 3.3 It should be made clear that work on the transition accounts has commenced and the resulting output will be shared with the Audit Commission as much as is possible over the 3 months before the traditional closure work commences. It is believed to be appropriate however, to set a realistic deadline and due to the limit of resource available for both the council and audit commission in the next three months it can be guaranteed that the transition work will definitely be completed, therefore it would appear sensible to set the final deadline for June when all such work must be completed.
- 3.4 The next stage is to focus on the production of the transition accounts as soon as possible and a work plan has been created by the Central Finance team to achieve this. The team is in regular contact with our colleagues at the audit commission to ensure that the approach adopted by LCC is in compliance with the IFRS regulations. It is intended to have the majority of this work completed by the end of March and progress towards this will be closely monitored by the group.
- 3.5 The next report to the committee will highlight progress made in the production of the council's transition accounts and the production of the council's final accounts.

### **4. Summary**

- 4.1 The IFRS Project Group is continuing to monitor the progress towards the completion of the transition onto a statement of accounts produced under IFRS for 2010/11, with regular liaison with the District Auditor.
- 4.2 The revised project plan aims to ensure that the County Council continues to make good progress towards meeting the necessary deadlines associated with the transition process.
- 4.3 The IFRS Project group continues to work closely with the District Auditor and have agreed that they will review the restated accounts over the next three months where possible, ensuring that as much transition work as possible is completed before the traditional final accounts process begins.
- 4.4 The IFRS project group remains confident that full implementation of IFRS accounting standards for the 2010/11 statement of accounts will be achieved

## **Appendix A**

within the statutory timeframe. Progress against the project plan will continue to be closely monitored and reported to this committee.

- 4.5 It is anticipated that the implementation of IFRS will give rise to a greater than usual number of queries from the audit commission during the closure process and final audit. This has been an issue that has been discussed nationally by local authorities as being an expected outcome of this year's closure. It is appropriate therefore to highlight that there may be a number of minor issues that will be raised in the 2010/11 audit but that these will not be issues have that a material effect on the accounts.



Project Plan IFRS Implementation for Lancashire County CouncilKEY DATES

Task	Name of Accountable Officer	CIPFA Target Date	LCC Target Date	Revised Target Date	Date Completed	Additional Information
Create Project Team		May 09	Nov-09		Nov-09	
High level impact assessment & completion of associated tasks :						
<u>IFRIC 12 - Service Concession Arrangements</u>		May 09	Dec-09	14/05/2010	14/05/10	All work completed for closure pack submission for 2009/10 Statement of Accounts
<u>Leases (IAS 17)</u>		May 09	Dec-09	Mar-10	Mar-10	Required for both when we are a lessor & a lessee
<u>Embedded Leases (IFRIC 4)</u>		May 09	Procurement Jan 10 CFTs Feb 10	Jun-10	30.06.10	Full review of GL to identify embedded leases
<u>Property, Plant &amp; Equipment (IAS 16)</u>		May 09	Ongoing	Ongoing	In Progress	
<u>Employee Benefits (IAS 19)</u>		May 09	Dec-09	Jun-10	30.06.10	Details of staff annual leave not taken as at 31/03/08
<u>Segmental Reporting (IFRS 8)</u>	IFRS Project Group	May-09	Ongoing	Ongoing	In Progress	An income statement and a balance sheet for each directorate
<u>Investment Properties (IAS 40)</u>		May-09	Jan-10	Jun-10	30.06.10	List of properties held and the reason for holding them
<u>Intangible Assets (IAS 38)</u>		May-09	Jan-10	Jun-10	30.06.10	Identification of any intangible assets that are not currently recognised (only currently software licences >1 Year)
<u>Accounting Policies (IAS 8)</u>	IFRS Project Group	May-09	Ongoing	Ongoing	In Progress	All the County Council's current accounting policies
1. Expand task list with detailed deadlines for delivery of transition accounts	Senior Acct - Special Projects, ICT & CFTs			Nov-10	Dec-10	Expand tasks below into workstreams that can be assigned to project group members for delivery
2. Expand task list with detailed deadlines for development of Accounting policies	Senior Acct - Special Projects, ICT & CFTs			Dec-10	Dec-10	Expand tasks below into workstreams that can be assigned to project group members for delivery
3. Key staff trained on IFRS transition		ASAP	Ongoing	Jun-11	In Progress	
4. Identify systems and procedural changes (including Chart of Accounts changes) required		Jul-09	Ongoing	Ongoing	In Progress	Chart of Accounts, Asset Register, Annual Leave & Flexi Time systems/data
5. Develop skeleton SOA under IFRS (including Notes and Policies)		Sep-09	Dec-09	Jun-11	In Progress	CIPFA guidance on layout of accounts
6. Identify likely impact on budgets (if any)		Sep-09	Feb/Mar 10	Ongoing	In Progress	
7. Implement systems and procedural changes		Jan-10	Ongoing	Ongoing	In Progress	
8. Training for all relevant staff and members		Ongoing	Ongoing	Ongoing	In Progress	
9. Restate 1 April 2009 balance sheet (including reconciliations between UK GAAP and IFRS)		Dec-09	Feb/Mar 10	Jun-11	In Progress	
10. Testing of systems and procedural changes		Mar-10	Ongoing	Ongoing	In Progress	
11. Restate 2009/10 accounts & disclosure notes		Dec-10	Dec-10	Jun-11	In Progress	
12. Produce 2010/11 accounts on IFRS basis		Jun-11	Jun-11	Jun-11	In Progress	



# Agenda Item 7

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected:  
All

### CIPFA's statement on 'The role of the head of internal audit' (Appendix A refers.)

Contact for further information:  
Ruth Lowry, (01772) 534898, Resources Directorate

#### Executive summary

The Chartered Institute of Public Finance and Accountancy (CIPFA) issued a statement on 'The role of the head of internal audit' in December 2010 that is intended to be helpful to a wide audience including audit committees as well as chief executives and local authority leadership teams.

The foreword to this statement states:

'The Head of Internal Audit (HIA) occupies a critical position in any organisation, helping it to achieve its objectives by giving assurance on its internal control arrangements and playing a key role in promoting good corporate governance. The aim of this Statement is to clarify the role of the HIA in public service organisations and to raise its profile.' (Appendix A)

#### Recommendation

The Audit Committee is asked to note this statement.

#### Background

CIPFA is the professional institute that sets the professional framework for internal audit in local government, and this statement should be taken as informing the council of current best practice. Ruth Lowry, head of internal audit for Lancashire County Council is a member of CIPFA's Audit Panel, which has endorsed this statement.

The Institute of Internal Auditors frames professional practice for the internal audit profession more widely and its framework of internal audit standards is also applicable to the work of the council's internal audit service.

#### Consultations

Not applicable.

#### Advice

Not applicable.

#### Alternative options to be considered

Not applicable.

**Implications:** e.g. financial, legal, personnel, human rights, crime and disorder or other.

This statement should be read within the wider context of the council's corporate governance arrangements.

### **Risk management**

This report supports the Audit Committee in undertaking its role; there are no risk management issues associated with it.

### **Local Government (Access to Information) Act 1985**

#### **List of Background Papers**

Paper	Date	Contact
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Not applicable.

**Reason for inclusion in Part II, if appropriate:** Not applicable.



# the role of the head of internal audit

in public service organisations

2010

## **CIPFA Statement on the role of the Head of Internal Audit in public service organisations**

**The Head of Internal Audit in a public service organisation plays a critical role in delivering the organisation's strategic objectives by:**

- 1** championing best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments; and
- 2** giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.

**To perform this role the Head of Internal Audit:**

- 3** must be a senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee;
- 4** must lead and direct an internal audit service that is resourced to be fit for purpose; and
- 5** must be professionally qualified and suitably experienced.

## **Contents**

Foreword	<b>1</b>
Definitions used throughout the document	<b>2</b>
Introducing the CIPFA statement	<b>4</b>
Using the CIPFA Statement	<b>5</b>
Principle 1	<b>7</b>
Principle 2	<b>10</b>
Principle 3	<b>15</b>
Principle 4	<b>18</b>
Principle 5	<b>21</b>
Appendix	<b>23</b>

# \ foreword

The Head of Internal Audit (HIA) occupies a critical position in any organisation, helping it to achieve its objectives by giving assurance on its internal control arrangements and playing a key role in promoting good corporate governance. The aim of this Statement is to clarify the role of the HIA in public service organisations and to raise its profile.

Organisations need to know that they have strong arrangements for controlling their resources and for delivering their objectives. CIPFA believes that HIAs have a unique role to play here. They are senior managers whose business is objectively assessing these arrangements and the risks that organisations face and giving appropriate assurances. HIAs must also provide leadership, promoting and helping organisations achieve good governance and address future challenges.

HIAs need to review the whole system of control, both financial and non-financial, and focus on the areas where assurance is most needed. In most public service organisations the HIA has to give an annual opinion on the organisation's governance arrangements, which is used by Chief Executives as a primary source of evidence for their annual governance report.

HIAs must also be able to show that they can meet the needs of stakeholders such as Chief Executives and Audit Committees adding value by helping to

improve services whilst retaining their objectivity. They also need to work well with partners and other auditors.

The Statement is principles based and should be relevant for all public service organisations and their HIAs. It is intended to be helpful to a wide audience including Leadership Teams, including Chief Executives, Audit Committees, other stakeholders as well as HIAs themselves.

We believe organisations should see the Statement as best practice and use it to assess their HIA arrangements to drive up audit quality and governance arrangements.

We also commend the Statement to individual internal audit professionals. It articulates the core responsibilities of the HIA, as well as the personal and professional skills that they need.

**Mike More**  
Chair  
CIPFA Steering Group on the role of the Head of Internal Audit in public service organisations

December 2010

**Steve Freer**  
Chief Executive  
CIPFA

# \ definitions used throughout the document

The public services have a wide variety of organisational structures and governance arrangements. The definitions used in this document are primarily based on those used in CIPFA's Role of the Chief Financial Officer Statement and in CIPFA's Code of Practice for Internal Audit in Local Government. These definitions are broadly consistent with those used by the Institute of Internal Auditors (IIA) and reflected in the standards used in central government and the NHS. Where there are some differences (marked as \*) then the alternative IIA definition should be considered when applying the Statement in these sectors.

## **Head of Internal Audit (HIA)**

The executive responsible for the organisation's internal audit service, including drawing up the internal audit strategy and annual plan and giving the annual audit opinion. This could be someone from another organisation where internal audit is contracted out or shared with others.

## **Leadership Team**

Comprises the Board and Management Team.

## **Board**

The group of people charged with setting the strategic direction for the organisation and responsible for its achievement.

## **Management Team**

The group of executive staff comprising the senior management charged with the execution of strategy.

## **Chief Executive**

The most senior executive role in the organisation.

## **Chief Financial Officer**

The organisation's most senior executive role charged with leading and directing financial strategy and operations.

## **Managers**

The staff responsible for the achievement of the organisation's purpose through services/businesses and delivery to its clients/customers.

## **Governance<sup>1</sup>**

The arrangements in place to ensure that an organisation fulfils its overall purpose, achieves its intended outcomes for citizens and service users and operates in an economical, effective, efficient and ethical manner.

## **Control environment\***

Comprises the systems of governance, risk management and internal control. The key elements include:

- establishing and monitoring the achievement of the organisation's objectives
- the facilitation of policy and decision-making ensuring compliance with established policies, procedures, laws and regulations – including how risk management is embedded
- ensuring the economical, effective and efficient use of resources and for securing continuous improvement
- the financial management of the organisation and the reporting of financial management
- the performance management of the organisation and the reporting of performance management.

## **System of internal control**

The totality of the way an organisation designs, implements, tests and modifies controls in specific systems, to provide assurance at the corporate level that the organisation is operating efficiently and effectively.

<sup>1</sup> The Good Governance Standard for Public Services (Independent Commission chaired by Sir Alan Langlands, 2004)

## **Risk management\***

A logical and systematic method of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating the risks associated with any activity, function or process in a way that will enable the organisation to minimise losses and maximise opportunities.

## **Risk based audit\***

An audit that:

- identifies and records the objectives, risks and controls
- establishes the extent to which the objectives of the system are consistent with higher-level corporate objectives
- evaluates the controls in principle to decide whether or not they are appropriate and can be reasonably relied upon to achieve their purpose, addressing the organisation's risks
- identifies any instances of over and under control and provides management with a clear articulation of residual risks where existing controls are inadequate
- determines an appropriate strategy to test the effectiveness of controls ie through compliance and/or substantive testing
- arrives at conclusions and produces a report, leading to management actions as necessary and providing an opinion on the effectiveness of the control environment.

## **Audit Committee**

The governance group charged with independent assurance of the adequacy of the internal control environment and the integrity of financial reporting.

## **Internal audit\***

An assurance function that provides an independent and objective opinion to the organisation on the control environment, by evaluating its effectiveness in achieving the organisation's objectives. It objectively examines, evaluates and reports on the adequacy of the

control environment as a contribution to the proper, economic, efficient and effective use of resources.

## **Consultancy**

Advisory and related client service activities, the nature and scope of which are agreed by the client, are intended to add value and improve an organisation's governance, risk management and control processes without the internal auditor assuming management responsibility.

## **Annual governance report**

The mechanism by which an organisation publicly reports on its governance arrangements each year.

## **Public service organisation**

One or more legal bodies managed as a coherent operational entity with the primary objective of providing goods or services that deliver social benefits for civic society, are not privately owned and receive public and/or charitable funding.

## **Assurance**

A confident assertion, based on sufficient, relevant and reliable evidence, that something is satisfactory, with the aim of giving comfort to the recipient. The basis of the assurance will be set out and it may be qualified if full comfort cannot be given. The HIA may be unable to give an assurance if arrangements are unsatisfactory.

Assurance can come from a variety of sources and internal audit can be seen as the 'third line of defence' with the first line being the organisation's policies, processes and controls and the second being managers' own checks of this first line.

## **Head of Internal Audit Opinion**

The opinion issued each year by the HIA on the adequacy and effectiveness of the organisation's control environment and which is used by the Chief Executive in some public service organisations as a key source in drafting the annual governance report.

# introducing the CIPFA statement

## The public service context

Citizen, service user and taxpayer: all of us occupy one or other of these roles at different times. We all have different priorities and needs, but our common ground is that we expect high standards of service within affordable tax levels. And we demand exemplary standards of behaviour where public money is spent.

The public services also face frequent structural changes and changing models of service delivery and partnerships. Expectations of contestability and competition as drivers of value for money are also blurring the boundaries between the public and private sectors. This has increased the variety of governance arrangements, even among similar types of bodies.

## Good governance

The changing political environment within which decisions are taken and services delivered creates a range of stakeholders whose interests and influences must be acknowledged, understood, managed and balanced.

The demand for better public services within a complex environment has strengthened the need for effective governance. Good governance in a public service organisation requires a focus on the organisation's purpose and its intended outcomes. It also carries a specific obligation in relation to citizens, taxpayers and service users to make best use of resources and ensure value for money.

## The key role played by the HIA

Internal audit is one of the cornerstones of effective governance. The HIA is responsible for reviewing and reporting on the adequacy of their organisation's control environment, including

the arrangements for achieving value for money. Through the annual internal audit opinion and other reports the HIA gives assurance to the Leadership Team and others, and makes recommendations for improvement.

The HIA's role is a unique one, providing objective challenge and support and acting as a catalyst for positive change and continual improvement in governance in all its aspects. The role is particularly important when organisations are facing uncertain or challenging times. Fulfilling the role requires a range of personal qualities. The HIA has to win the support and trust of others, so that he/she is listened to, and the HIA's role as a critical friend means that sometimes difficult messages must be given and acted on.

It is these expectations, combined with the professional, personal and leadership skills required, that have shaped the CIPFA Statement on the role of the HIA in public service organisations.

## Primary audience

The primary audience for this Statement is those who rely on the HIA's assurances – the Leadership Team and the Audit Committee. CIPFA recommends that they should examine their own organisation against this Statement to satisfy themselves that they have effective HIA arrangements in place.

# using the CIPFA statement

## Statement approach and structure

The Statement sets out the five principles that define the core activities and behaviours that belong to the role of the HIA in public service organisations and the organisational arrangements needed to support them.

Successful implementation of each of the principles requires the right ingredients in terms of:

- the organisation;
- the role; and
- the individual.

For each principle the Statement sets out the governance arrangements required within an organisation to ensure that HIAs are able to operate effectively and perform their core duties. The Statement also sets out the core responsibilities of the HIA.

Summaries of personal skills and professional standards then detail the leadership skills and technical expertise organisations can expect from their HIA. These include the requirements of CIPFA and the other professional bodies' codes of ethics and professional standards to which the HIA as a qualified professional is bound. The personal skills described have been aligned with the most appropriate principle, but in many cases support other principles as well.

## Demonstrating compliance

The Statement supports CIPFA's work to strengthen governance, risk management and internal audit across public services. It is intended to allow the Leadership Team of a public service organisation, whether executive, non-executive or elected, to benchmark its existing arrangements against a defined framework.

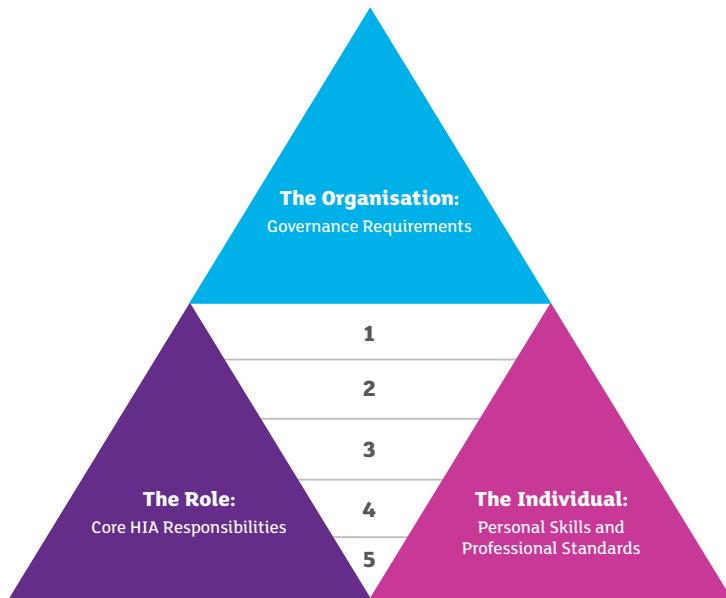
Public service organisations operate within a variety of legal and regulatory structures, and there is a huge range in size and scope of services delivered. The Statement therefore focuses on the principles that capture the essential characteristics of the HIA role in any public service organisation.

CIPFA recommends that organisations should use the Statement as the framework to assess their existing arrangements (linked to any sector specific guidance or standards), and that they should report publicly on compliance to demonstrate their commitment to good practice. CIPFA also proposes that organisations should report publicly where their arrangements do not conform to the compliance framework in this Statement, explaining the reasons for this, and how they achieve the same impact.

## Status of the Statement

The Statement sets out what CIPFA considers to be best practice for HIAs. It does not have the status of a CIPFA code, nor does it replace the sector-specific guidance or the codes and professional standards that underpin accountancy and internal audit bodies' competency and disciplinary frameworks. The aim is that standard setters and regulators across public services should draw on the Statement when reviewing their own guidance.

The Statement should also help guide both current and aspiring HIAs, by providing a summary of the core responsibilities entailed in the role as well as the personal skills and professional standards necessary to succeed. It should therefore provide a focus for audit professionals' own personal development at all stages of their careers.



### **CIPFA Statement on the role of the Head of Internal Audit (HIA) in public service organisations**

**The Head of Internal Audit in a public service organisation plays a critical role in delivering the organisation's strategic objectives by:**

- 1 championing best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments; and
- 2 giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.

**To perform this role the Head of Internal Audit:**

- 3 must be a senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee;
- 4 must lead and direct an internal audit service that is resourced to be fit for purpose; and
- 5 must be professionally qualified and suitably experienced.

# \ principle 1



The HIA in a public service organisation plays a critical role in delivering the organisation's strategic objectives by championing best practice in governance, objectively assessing the adequacy of governance and management of existing risks, commenting on responses to emerging risks and proposed developments.

## Promoting good governance

Good governance is fundamental to establishing confidence in public services. All managers have a responsibility for good governance but the HIA has a role in promoting this and spreading good practice. The internal audit strategy must set out how the HIA will fulfil this role.

The Leadership Team collectively needs to set the tone that good governance is core to achieving strategic aims and in demonstrating that public money is used well. The HIA is not responsible for good governance but they do have a role in helping to raise standards. This can be done by promoting the benefits of good governance as well as reporting on system failures. There are also benefits for the HIA in taking such an approach as this helps staff and others see the wider purpose of internal audit's work and the support that they can provide.

There are many ways to champion good governance across the organisation. In many organisations others such as the Chief Financial Officer will lead on promoting good governance. The HIA needs to assess the state of the organisation's governance and what others with an interest are doing. They then need to clarify their role in promoting good governance and how they can make most impact. Benchmarking with other organisations can be helpful and case studies from similar organisations can be useful. The aim should be to show the benefits of good governance for staff and others and using training and guidance to do this. The role of champion also extends to the significant partnerships that the organisation is part of.

## Assessing governance and management of existing risks

HIs must review and make a judgement on the whole range of controls including those relating to achieving value for money and the prevention and detection of fraud and corruption. In reaching the judgement the HIA might want to look at corporate arrangements, for example those regarding data quality and performance management arrangements. They may also want to test how these arrangements work by examining specific topics, for example major projects, decision making and implementation of programmes. Overall, internal audit's objectives must be aligned to the organisation's and should help improve the effectiveness of public service delivery.

There can often be many agencies reviewing controls within organisations. Internally there may be management consultants reviewing operational management. Externally there is a range of inspectors and other review agencies and service delivery partners. The HIA must understand the governance arrangements and assess the strengths of each of the parts. They then need to set out what reliance has been placed on the different elements and why they believe the reliance to be well placed. Setting out this framework should also help in explaining to others how internal audit fits into the wider governance picture.

## Advising on proposed developments

HIs must be asked to consider the impact of proposed policy initiatives, programmes

and projects as well as responses to emerging risks. HIAs should be made aware of major new systems and proposed initiatives to help ensure risks are properly identified and evaluated and appropriate controls built in. The HIA should consider what if any audit work needs to be done and also how the proposals fit with the organisation's strategic objectives. The HIA should be involved at the outset to ensure any advice they give can be actioned. Giving advice over proposed developments is inevitably a less precise business than giving assurances on existing systems. Managers and the HIA must therefore be clear on the scope of any internal audit work here and of the kind of advice that is given.

Internal audit sometimes provide advice on current or proposed arrangements. This is an important role – it makes good use of internal audit's analytical skills and brings value to the organisation. But for this to work well the HIA must ensure that staff carrying out the work have suitable skills and that internal audit's objectivity is not compromised. The HIA must also ensure that there are sufficient resources to do the work and that other work and the HIA annual opinion is not compromised.



## Governance requirements

## Principle 1

- Set out the HIA's role in good governance and how this fits with the role of others.
- Ensure that the importance of good governance is stressed to all in the organisation, through policies, procedures and training.
- Ensure that the HIA is consulted on all proposed major projects, programmes and policy initiatives.



## Core HIA responsibilities

## Principle 1

- Helping to promote the benefits of good governance throughout the organisation.
- Working with others in the organisation who have a responsibility for promoting good governance.
- Giving advice to the Leadership Team and others on the control arrangements and risks relating to proposed policies, programmes and projects.
- Promoting the highest standards of ethics and standards across the organisation based on the principles of integrity, objectivity, competence and confidentiality.
- Demonstrating the benefits of good governance for effective public service delivery and how the HIA can help.
- Offering consultancy advice where the HIA considers that it is appropriate, drawing up clear terms of reference for such assignments.



## Personal skills and professional standards

## Principle 1

- Provide leadership by giving practical examples of good governance that will inspire others.
- Deploy effective facilitating and negotiating skills.
- Build and demonstrate commitment to continuous improvement.
- Demonstrate consultancy skills as appropriate – analytical, problem solving, influencing and communicating.

# \ principle 2



The HIA in a public service organisation plays a critical role in delivering the organisation's strategic objectives by giving an objective and evidence based opinion on all aspects of governance, risk management and internal control.

## **Objectivity**

The Leadership Team is responsible for the organisation achieving its objectives and for underlying good governance, risk management and internal control. Managers are responsible for this in the areas for which they have responsibility. The HIA's unique role is to provide assurance and guidance on these arrangements and so it is important that the HIA is independent of operational management and is seen to provide objective views and opinions.

Whilst the HIA needs to be objective it is important that they understand the organisation and are pragmatic in their working relationships. The HIA should be concerned with effective action to improve the control environment. They must work to develop strong and constructive working relationships with managers and non-executive directors/elected representatives, creating mutual respect and effective communication. Providing objective information and advice to non-executive directors, elected representatives and others requires an understanding of ethics and the wider public interest as well as diplomacy.

To enable the HIA to be objective, he/she should have no operational responsibilities. In cases where the HIA does have operational responsibilities then alternative assurance arrangements must be made. In particular, the impact of this work and the audit planning and reporting arrangements for these areas must be reported to and agreed by the HIA's line manager and the impact reported to the Audit Committee.

## **Whole range of controls**

The Leadership Team need regular assurance that the organisation has good governance arrangements. The framework that provides this will have a number of sources including line management, external inspectors and agencies and external auditors, but the main objective source is the HIA.

The HIA needs to give the organisation a range of assurances, including reports on specific systems or work areas, new or developing systems (and the risks in areas being considered), partnerships and the overall annual opinion.

The annual HIA opinion is the most important output from the HIA. This is one of the main sources of objective assurance that Chief Executives have for their annual governance report. This opinion must reflect the work done during the year and it must summarise the main findings and conclusions together with any specific concerns the HIA has. Audit planning must be comprehensive and consider the whole control environment, so that the opinion is based on a picture of the whole organisation. The audit work should address key risk areas and draw attention to significant concerns and what needs to be done. The HIA must express concerns where they exist.

## **Evidence based assurance**

The HIA's assurance must be well founded if it is to give proper comfort to those who ask for it, and to improve governance arrangements. This means that internal audit planning must be well

focused. Individual audits must be carried out in a logical and systematic way, based on sufficient, relevant and reliable evidence and with the work being subject to proper supervision and review. HIAs must also ensure that their reports are balanced, focusing on key risks and issues and making practical recommendations.

The HIA may look to partners and other agencies for assurance. Here the HIA must understand the basis for the assurance and its adequacy, and therefore whether the HIA needs to carry out any additional review work.

Sometimes the HIA will be asked to give assurances to partners or other organisations such as government departments on the organisation's own arrangements. The HIA should carefully consider, taking advice as necessary, the scope and extent to which reliance should be placed on it and any potential reputational risks.

In both circumstances the scope and purpose of assurances given and received should be agreed by the Audit Committee. A summary of assurances given and relied upon should also be included in the HIA's annual report.

One of the HIA's key relationships must be with the external auditor. The roles of internal and external audit are different and they must be independent of each other. But both are concerned with the organisation's control environment and both use an objective, risk based approach in coming to their conclusions. The HIA must liaise closely with external audit in drawing up strategies and plans and understand where and how the external auditor will be relying on the HIA. This should help ensure that audit resources are used most effectively.

## **Develop and implement a risk based audit strategy**

Risk management is key to the effective delivery of public services. Organisations are taking a more positive view of risk and are becoming more mature in how they identify, measure, and manage risks.

The HIA must ensure that the internal audit strategy reflects risk management best practice. The starting point is to review the organisation's strategic objectives and how it plans to achieve these. The risks to achieving these must be considered and the HIA needs to review how the risks are captured in risk registers and the action plans that are in place. The HIA will draw on the organisation's risk register when drawing up the internal audit strategy and plans. The extent to which he or she does this will depend on how mature the organisation is at identifying key risks and taking appropriate action to address them.

The audit strategy must identify the priorities for internal audit based on an assessment of the key risks to the organisation and the extent of alternative sources of assurance, as well as the resources and skills needed to deliver it. The responsibility for effective governance arrangements (including risk management) remains with managers; the HIA cannot be expected to prevent or detect all weaknesses or failures in internal control nor can the internal audit strategy cover all areas of risk across the organisation.



## Governance requirements

## Principle 2

- Set out the responsibilities of the HIA, which should not include the management of operational areas.
- Ensure that internal audit is independent of external audit.
- Where the HIA does have operational responsibilities the HIA's line manager and the Audit Committee should specifically approve the IA strategy for these and associated plans and reports and ensure the work is independently managed.
- Establish clear lines of responsibility for those with an interest in governance (eg Chief Executive, Chief Legal Officer, Chief Financial Officer, Audit Committee, non-executive directors/elected representatives). This covers responsibilities for drawing up and reviewing key corporate strategies, statements and policies.
- Establish clear lines of reporting to the Leadership Team and to the Audit Committee where the HIA has significant concerns.
- Agree the terms of reference for internal audit with the HIA and the Audit Committee as well as with the Leadership Team.
- Set out the basis on which the HIA can give assurances to other organisations and the basis on which the HIA can place reliance on assurances from others.
- Ensure that comprehensive governance arrangements are in place, with supporting documents covering eg risk management, corporate planning, anti fraud and corruption and whistleblowing.
- Ensure that the annual internal audit opinion and report are issued in the name of the HIA.
- Include awareness of governance in the competencies required by members of the Leadership Team.
- Set out the framework of assurance that supports the annual governance report and identify internal audit's role within it. The HIA should not be responsible for preparing the report.
- Ensure that the internal audit strategy is approved by the Audit Committee and endorsed by the Leadership Team.



## Core HIA responsibilities

## Principle 2

- Giving assurance on the control environment. This includes risk and information management and internal controls across all systems.
- Reviewing the adequacy of key corporate arrangements including eg risk strategy, risk register, anti fraud and corruption strategy, corporate plan.
- Producing an evidence based annual internal audit opinion on the organisation's control environment.
- Working closely with others to ensure that sufficient and relevant evidence is used. Where relying on others, clarifying the degree and basis for the reliance.
- Reviewing significant partnership arrangements and major services provided by third parties and the controls in place to promote and protect the organisation's interests. Assessing whether lines of responsibility and assurance are clear.
- Liaising closely with the external auditor to share knowledge and to use audit resources most effectively.
- Producing an internal audit strategy that fits with and supports the organisation's objectives.
- Reviewing the organisation's risk maturity (including the organisation's own assessment) and reflecting this in the strategy.
- Consulting stakeholders, including senior managers and non-executive directors/elected representatives on the internal audit strategy.
- Setting out how the HIA plans to rely on others for assurance on the organisation's controls and risks and taking account of any limitations in assurance given by others.
- Liaising with external inspectors and review agencies where appropriate when drawing up the internal audit strategy.
- Liaising with the external auditor on the internal audit strategy, but not being driven by external audit's own priorities.



## Personal skills and professional standards

## Principle 2

- Give clear, professional and objective advice.
- Report on what is found, without fear or favour.
- Demonstrate integrity to staff and others in the organisation.
- Exercise sound judgement in identifying weaknesses in the organisation's control environment and a balanced view on how significant these are.
- Work well with others with specific responsibilities for internal control, risk management and governance including (as appropriate to the sector) Chief Executive, Chief Legal Officer, Chief Financial Officer, Audit Committee, non-executive directors/elected representatives.
- Be concerned for action - influencing the Leadership Team, Audit Committee and others to ensure that the HIA's recommendations are implemented.
- Be a role model, dynamic, determined, positive, robust and with resilient leadership, able to inspire confidence and respect and exemplify high standards of conduct.

# \ principle 3



The HIA in a public service organisation must be a senior manager with regular and open engagement across the organisation, particularly with the Leadership Team and with the Audit Committee.

## **Senior manager**

HIAs face increasing challenges and higher expectations from stakeholders, especially in helping organisations look forward. The HIA must be at the heart of the organisation, challenging and supporting the Leadership Team with authority and credibility. He or she should also be seen as a leader, promoting improvement and good governance. To do this effectively, making an impact and adding value, the HIA position must be a senior manager.

There is a range of guidance concerning line management responsibility for the HIA<sup>2</sup>. What is paramount is that the reporting line must leave the HIA free from interference in setting the scope of internal audit's work, in coming to conclusions and in reporting the results. They must also have unfettered access across the organisation, especially to the Chief Executive, Board and Audit Committee Chair. In practice this is most likely to be achieved by the HIA reporting to the Chief Executive or to the Chief Financial Officer.

The HIA role must be filled by a nominated individual so that all are clear about lines of responsibility. Where the service is provided in-house this should be straightforward. Where the service is contracted out or shared with others then the organisation must decide whether the HIA should come from within the organisation or from the supplier of the audit service. In the latter case the relationship between the HIA and the organisation, including the Audit Committee, must be clearly set out as part of the organisation's governance framework. In practice it is likely that the HIA should be the person who is responsible for drawing up the internal audit strategy and plan and for issuing the HIA annual internal audit opinion.

## **Engagement with the Leadership Team**

The Leadership Team in public service organisations takes many forms, with different mixes of executive and non-executive members, as well as elected representatives. Collectively the Leadership Team is responsible for setting the strategic direction for the organisation, its implementation and the delivery of public services. The HIA must also have a right of access to individual members of the Leadership Team. Whilst it is not appropriate for the HIA to be a member of the Leadership Team it is vital that the HIA attends key meetings where they consider it necessary. The HIA should be well placed to support the Leadership Team in understanding the governance, risk management and control arrangements. Examples of this might include presenting the internal audit strategy or the annual internal audit opinion or taking part in discussions about the annual governance report or planned major policies, projects or system changes.

## **Engagement with the Audit Committee**

The HIA's relationship with the Audit Committee and especially the Chair is crucial. They should be mutually supportive in their aim to be objective and to provide challenge and support across the organisation and improve governance, risk management and internal control. The HIA must work closely with the Audit Committee Chair so that they are clear about their respective roles and make best use of the available resources. For some areas of the public services it may be appropriate for the Audit Committee Chair to have a role in the appointment of the HIA.

<sup>2</sup> For example, in central government and the NHS, internal audit standards state that the HIA should report to the Chief Executive. In local government CIPFA's Code of Practice for internal audit states that the HIA should report to a member of the Management Team.



## Governance requirements

## Principle 3

- Designate a named individual as HIA in line with the principles in this Statement. The individual could be someone from another organisation where internal audit is contracted out or shared. Where this is the case then the roles of the HIA and the client manager must be clearly set out in the contract or agreement.
- Ensure that where the HIA is an employee that they are sufficiently senior and independent within the organisation's structure to allow them to carry out their role effectively and be able to provide credibly constructive challenge to the Management Team.
- Ensure that where the HIA is an employee the HIA is line managed by a member of the Management Team. Where the HIA is not an employee then the reporting line must be clearly set out in the contract or agreement with the internal audit supplier.
- Establish an Audit Committee in line with guidance and good practice.
- Set out the HIA's relationship with the Audit Committee and its Chair, including the Committee's role (if any) in appointing the HIA.
- Ensure that the organisation's governance arrangements allow the HIA:
  - to bring influence to bear on material decisions reflecting governance;
  - direct access to the Chief Executive, other Leadership Team members, the Audit Committee and external audit; and
  - to attend meetings of the Leadership Team and Management Team where the HIA considers this to be appropriate.
- Set out unfettered rights of access for internal audit to all papers and all people in the organisation, as well as appropriate access in (significant) partner organisations.
- Set out the HIA's responsibilities relating to partners including joint ventures and outsourced and shared services.



## Core HIA responsibilities

## Principle 3

- Escalating any concerns through the line manager, Chief Executive, Audit Committee and Leadership Team, legal officers, external auditor as appropriate.
- Supporting the Audit Committee in reviewing its own effectiveness and advising the Chair and line manager of any suggested improvements.
- Consulting stakeholders, including senior managers and non-executive directors/elected representatives on the internal audit strategy.

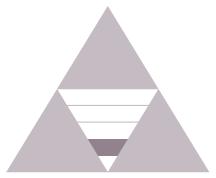


## Personal skills and professional standards

## Principle 3

- Network effectively to raise the profile and status of internal audit.
- Adopt a flexible style, being able to collaborate and advise but also able to challenge as appropriate.
- Build productive relationships both internally and externally.
- Work effectively with the Leadership Team and Audit Committee with political awareness and sensitivity.
- Be seen to be objective and independent but also pragmatic where appropriate.

# \ principle 4



The HIA in a public service organisation must lead and direct an internal audit service that is resourced to be fit for purpose.

## **Meeting the needs of the business**

Effective governance is critical in public service organisations and internal audit needs to play its part. The HIA must have a clear but wide ranging brief. This includes reviewing the key underlying systems and controls, reviewing arrangements for preventing fraud and corruption and also the arrangements for achieving value for money.

The HIA must have a firm grasp and understanding of the organisation's business as well as its control environment. This will allow HIAs to give an opinion to the Leadership Team on how well these arrangements are working. The HIA must ensure that there is sufficient depth of internal audit expertise and experience to do this well, so that he/she is able to engage effectively with managers and others and challenge where appropriate.

The internal audit resources available must be proportionate to the size, complexity and risk profile of the organisation and must be enough for the HIA to give a reliable opinion on the organisation's control environment. Responsibility for ensuring that an effective and appropriately resourced internal audit service is in place rests with the organisation. The organisation needs independent assurance over the quality of internal audit's work and should ensure that a regular external assessment is carried out.

The HIA must ensure that the Audit Committee has a clear understanding of the requirement for internal audit to review the whole system of internal control. The HIA must set out the audit coverage and audit resources needed to give a sound, evidence based annual audit opinion. The HIA must advise the Audit Committee and the Leadership Team where the available resources are inadequate and the consequences for the level of assurance that the HIA is able to give.

## **Appropriately developed internal audit skills**

A great deal of reliance is placed on the work of internal audit and the HIA must ensure that all the work, including planning and individual assignments, is consistently of a high quality and in line with professional standards. The HIA must also ensure that all staff demonstrate the highest ethical standards. The HIA therefore has a responsibility to ensure that internal audit staff have appropriate qualifications, knowledge, skills and competencies and are continuously developed. The HIA must assess the staffing needed to make sound judgements on the whole range of the organisation's governance arrangements.

The HIA needs well developed, motivated staff to make an impact at senior levels in the organisation. There may also be a need to buy in specialist skills which are not frequently used. The challenge for the HIA is to have the right mix and for the service to operate as a team, with staff being effective ambassadors for internal audit. The HIA has a particular responsibility to promote internal audit as a good career development opportunity.

The HIA must provide clear guidance for internal audit staff with appropriate quality assurance for internal audit as a whole and for each audit assignment. The HIA has a duty to see that their staff comply with the relevant internal audit standards and must have systems to verify this. More widely the HIA should work with colleague HIAs and others to ensure that they and the team are up to date on current issues affecting their organisation and on internal audit techniques and developments.



## Governance requirements

## Principle 4

- Provide the HIA with the resources, expertise and systems necessary to perform their role effectively.
- Ensure that the Audit Committee sets out a performance framework for the HIA and their team and assesses performance and takes action as appropriate.
- Ensure that there is a regular external review of internal audit quality.
- Ensure that where the HIA is from another organisation that they do not also provide the external audit service.



## Core HIA responsibilities

## Principle 4

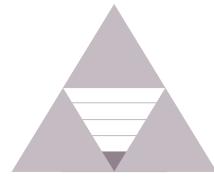
- Leading and directing the internal audit service so that it makes a full contribution to and meets the needs of the organisation and external stakeholders.
- Determining the resources, expertise, qualifications and systems for the internal audit service that are required to meet internal audit's objectives; using a full range of resourcing options including consultancy, working with others and buying in where appropriate.
- Informing the Leadership Team and Audit Committee if there are insufficient resources to carry out a satisfactory level of internal audit, and the consequence for the level of assurance that may be given.
- Implementing robust processes for recruitment of internal audit staff and/or the procurement of internal audit services from external suppliers.
- Ensuring that the professional and personal training needs for staff are assessed and seeing that these needs are met.
- Developing succession plans and helping staff with their career progression.
- Establishing a quality assurance and improvement programme that includes:
  - Ensuring that professional internal audit standards are complied with.
  - Reviewing the performance of internal audit and ensuring that the service provided is in line with the expectations and needs of its stakeholders.
  - Providing an efficient and effective internal audit service – demonstrating this by agreeing key performance indicators and targets with the line manager and Audit Committee; annually reporting achievements against targets.
  - Putting in place adequate ongoing monitoring and periodic review of internal audit work and supervision and review of files, to ensure that audit plans, work and reports are evidence based and of good quality.
  - Ensuring that any internal auditors declare any interests that they have.
  - Seeking continuous improvement in the internal audit service.
- Keeping up to date with developments in governance, risk management, control and internal auditing, including networking with other HIAs and learning from them, implementing improvements where appropriate.
- Demonstrating how internal audit adds value to the organisation.



## Personal skills and professional standards

## Principle 4

- Demonstrate leadership and be an ambassador for internal audit.
- Create, communicate and implement a vision for the internal audit service.
- Create a customer focused internal audit service.
- Establish an open culture, built on effective coaching and a constructive approach.
- Promote effective communication within internal audit, across the broader organisation and with external stakeholders.
- Set and monitor meaningful performance objectives for staff.
- Manage and coach staff effectively.
- Comply with professional standards and ethics.
- Require the highest standards of ethics and standards within internal audit based on the principles of integrity, objectivity, competence and confidentiality. In particular, ensuring that internal auditors identify and report any conflicts of interest and act appropriately.
- Ensure, when necessary, that outside expertise is called upon for specialist advice not available within the internal audit service.
- Promote discussion on current governance and professional issues and their implications.



# \ principle 5

The HIA in a public service organisation must be professionally qualified and suitably experienced

## Demonstrating professional and interpersonal skills

The HIA must be able to demonstrate his/her own professional credibility to exercise influence throughout the organisation. The HIA must be professionally qualified. In the UK, for example, this means holding a full Consultative Committee of Accountancy Bodies (CCAB) qualification or being a chartered member of the Chartered Institute of Internal Auditors (CIIA). As a member of a professional body, the HIA's skills, knowledge and expertise will have been tested by examination and must be continuously developed in a structured and monitored context. The HIA must adhere to the professional values of accuracy, honesty, integrity, objectivity, impartiality, transparency, confidentiality, competence and reliability and promote these throughout the internal audit service.

The HIA must communicate complex information in a clear and credible way. He/she must be able to operate effectively in different modes including directing, influencing, evaluating and informing. The HIA must be able to give objective opinions and advice even if this may be unwelcome, and be sufficiently forceful to intervene with authority if governance or ethical principles need to be asserted or defended. The HIA must work in partnership with a wide range of people and organisations and winning their confidence is key. He/she must be able to challenge the status quo and be a catalyst for change, achieving results through influence, without direct authority.

The HIA must be sensitive to the complexities and pressures facing organisations. He/she must build effective working relationships with the Audit Committee without damaging relationships with the Leadership Team. This requires tact and diplomacy.

## Applying business and professional experience

The HIA must have an understanding and commitment to the organisation's wider business and its delivery objectives, to inspire respect, confidence and trust amongst colleagues, with the Leadership Team, the Audit Committee and other stakeholders.

The HIA must have a good understanding of business processes and governance including strategic planning and performance, and financial and risk management. He/she must also be aware of current issues facing organisations and internal auditors. The HIA should be seen as a catalyst in improving governance and internal control and also supporting the organisation in its wider business objectives. To do this the HIA needs to look forward as well as at the organisation as it currently operates. The HIA must demonstrate leadership by personally setting a tone for the organisation that good governance, risk management and internal control matter to everyone in the organisation.



## Governance requirements

## Principle 5

- Appoint a professionally qualified HIA whose core responsibilities include those set out under the other principles in this Statement and ensure that these are properly understood throughout the organisation.
- Ensure that the HIA has the skills, knowledge, experience and resources to perform effectively in his or her role.



## Personal skills and professional standards

## Principle 5

- Be a full member of an appropriate professional body and have an active programme for personal professional development.
- Adhere to professional internal auditing (and where appropriate accounting and auditing) standards.
- Demonstrate a range of skills including communicating, managing and influencing, as well as an understanding of IT and consultancy.
- Have prior experience of working in internal audit.
- Understand and have experience of strategic objective setting and management.
- Understand the internal audit and regulatory environment applicable to public service organisations.
- Demonstrate a comprehensive understanding of governance, risk management and internal control.
- Undertake appropriate development or obtain relevant experience as appropriate in order to demonstrate an understanding of the full range of the organisation's activities and processes.

# \ appendix

## **Membership of the CIPFA Steering Group on the Role of the Head of Internal Audit in public service organisations**

<b>Mike More (Chair)</b>	Westminster City Council
<b>Anthony Barrett</b>	Wales Audit Office
<b>Chris Bowring</b>	NHS Fife
<b>Jackie Cain</b>	Institute of Internal Auditors
<b>Ian Carruthers</b>	CIPFA
<b>Mike Clarkson</b>	Deloitte
<b>Tim Crowley</b>	Mersey Internal Audit Agency
<b>Colin Langford</b>	CIPFA
<b>Paul Manning</b>	Department for International Development
<b>Justin Martin</b>	PricewaterhouseCoopers LLP
<b>Stephanie Mason</b>	Baker Tilly
<b>Jon Pittam</b>	Hampshire County Council
<b>Tim Pouncey</b>	Leeds City Council
<b>Duncan Savage</b>	East Sussex County Council
<b>Philip Winter</b>	Tenant Services Authority
<b>Chris Wobschall</b>	HM Treasury
<b>Clive Darracott (Secretary)</b>	CIPFA
<b>Diana Melville (Technical support)</b>	CIPFA

CIPFA is grateful to all the members of the Steering Group for their invaluable contributions and also to CIPFA's Audit Panel for their input and endorsement. The Statement was widely circulated for comment during its drafting and CIPFA is also grateful to the many individuals and organisations who responded, giving us additional insights into how the HIA operates in practice across the public services.







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# Agenda Item 8

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected: All
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### Internal Audit Progress Report

(Appendices A and B refer.)

Contact for further information:

Ruth Lowry, (01772) 534898, Resources Directorate

#### Executive Summary

In the context of fulfilling its responsibility to monitor the adequacy and effectiveness of the internal Audit Service, the committee is asked to consider the Audit Service's progress report for the year to date (Appendix A) and the supporting information regarding resource inputs (Appendix B).

#### Recommendation

The Audit Committee is asked to consider the internal audit progress report for the nine months to 31 December 2010.

#### Background

The Audit Committee's terms of reference state that the head of internal audit will provide a progress report summarising the following, and this has been achieved as follows:

Matters to be included in the progress report	How these matters have been addressed
i) work performed (and a comparison with work planned);	Please see Appendices A and B to this report.
ii) key issues emerging from internal audit work;	The issues arising from the reports that have been finalised to date are reported in Appendix A to this report.
iii) management response to audit recommendations;	We have begun to follow up the matters raised in our audit work in previous years to confirm that agreed recommendations have been implemented, and our findings are reported in Appendix A.



<b>Matters to be included in the progress report</b>	<b>How these matters have been addressed</b>
iv) changes to the audit plan for the period; and	We are not proposing any significant changes to our audit plan but some minor adjustments have been made where work is no longer appropriate, and where the resource inputs and timing of some assignments have altered. Appendix B to this report shows progress against the original audit plan agreed in March 2010.
v) any resourcing issues affecting the delivery of Internal Audit objectives.	The Audit Service establishment is being reduced to contribute to the council's cost saving targets, and a small amount of planned work will therefore slip into the first quarter of 2011/12 but, subject to any significant sickness absences, the Audit Service's objectives and annual plan will be achieved.

### **Consultations**

Not applicable.

### **Advice**

Not applicable.

### **Alternative options to be considered**

Not applicable.

**Implications:** e.g. financial, legal, personnel, human rights, crime and disorder or other.

None

### **Risk management**

This report supports the Audit Committee in undertaking its role, which includes advising the Council on the adequacy of the Authority's strategic risk management processes.

### **Local Government (Access to Information) Act 1985**

#### **List of Background Papers**

Paper

Date

Contact

Not applicable.

**Reason for inclusion in Part II, if appropriate:** Not applicable.

**Appendix A**

## **1 Introduction**

- 1.1 This report summarises the progress made by the council's internal Audit Service against the internal audit plan for 2010/11 to 31 December 2010, and some of the findings arising from this work. The findings included in this report have been agreed with executive directors and highlights were shared with the Executive Leadership Team (ELT) on 12 January 2011.

### **Overview of progress**

- 1.2 We continue to make good progress with our work on the 2010/11 audit plan. A number of reviews have now been completed or are being discussed with the management teams responsible and an indication of the work that has been completed under each area of the audit plan is set out below.

### **Resource inputs to the plan**

- 1.3 The Audit Service has continued to concentrate hard on managing our performance, in particular our focus on chargeable work for our clients rather than other non-chargeable tasks. For the nine months of the year to 31 December 2010 we have more than achieved (by 258 days) the overall inputs to our client work that we intended.
- 1.4 As a result of the councils' need to make cost savings, the Audit Service establishment has recently been reduced by three staff and a further team member will leave during 2011/12. Some work is likely to slip into the first quarter of 2011/12 (work relating to the county's schools in particular) but, subject to any unforeseen sickness during the remainder of the year we expect to be able to complete this year's plan appropriately.

### **Audit assurance**

- 1.5 Audit assurance is stated in the following terms, some of which are used below:

**Full assurance:** there is a sound system of internal control which is designed to meet the council's objectives and controls are being consistently applied.

**Substantial assurance:** there is a generally sound system of internal control, designed to meet the council's objectives, and controls are generally being applied consistently. However some weakness in the design and/ or inconsistent application of controls put the achievement of particular objectives at risk.

**Limited assurance:** weaknesses in the design and/ or inconsistent application of controls put the achievement of the council's objectives at risk.

**No assurance:** weaknesses in control and/ or consistent non-compliance with controls could result/ have resulted in failure to achieve the council's objectives.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

## **2 Progress in relation to cross-cutting and corporate risks**

### **Risk management**

- 2.1 This area is unchanged: the council is continuing to consider how best to use risk management as a tool to support its business processes.

### **Governance arrangements**

- 2.2 We reported in September 2010 that we have completed a review of members' expenses. We have provided substantial assurance over the operation of the members' allowances scheme, although the wording of the scheme could be made more specific in relation to the retention of documentation to support claims made under the scheme.

### **Selection of a strategic partner**

- 2.3 The selection of a strategic partner is central to achieving the council's overall objectives. The Audit Service has now provided full assurance that the whole procurement process was in accordance with EU and UK procurement rules, recognised procurement good practice, and fair to all bidding organisations.

- 2.4 In support of the council's director of finance we have also undertaken a substantial and detailed review of the figures provided by the council to BT plc relating to the budgets that will be managed by the joint venture company as the strategic partnership begins. We focussed specifically on the budgets for the costs of staff being seconded to the joint venture, the non-staff costs of supplies and services including external contracts, and income streams to provide assurance that the information provided was complete, current and accurately or reasonably valued where definitive information was not available. We provided substantial assurance that this was the case across each of the areas we reviewed.

### **Safeguarding**

- 2.5 We are currently assessing some of the controls in place to manage the wide range of risks related to safeguarding the children and vulnerable adults in the county council's care.
- 2.6 We have recently completed fieldwork assessing controls over the finances of adults in the care of the Adult and Community Services (ACS) Directorate, and we will be in a position to report our findings to the next Audit Committee meeting. We are also starting to consider the systems and controls in place to ensure that the monitoring and review functions across ACS teams are appropriately aligned and complement each other. Given the depth of the recent Care Quality Commission inspection, this review is limited in its scope.
- 2.7 A separate review of the corporate arrangements relating to vetting and barring and the enforcement of Criminal Records Bureau (CRB) checks has recently begun. Further audit work is also planned within the Directorate for Children and Young People (CYP) regarding the arrangements surrounding the Safeguarding Board.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- 2.8 In addition, a specific review of safeguarding arrangements relating to the transport of children is underway.

### **Health and safety of the public**

- 2.9 Our work on this cross-cutting theme is centred firstly upon the council's highways responsibility under legislation relating to corporate manslaughter, and secondly in relation to petroleum safety of closed sites.
- 2.10 We have recently completed fieldwork in relation to the council's highways responsibilities and are discussing our findings with the Environment Directorate's management team.
- 2.11 The management team is also considering our draft report relating to petroleum safety arrangements. We propose to provide substantial assurance over the arrangements in place, although we have made several recommendations regarding consistency of data quality, the need to update documented procedures to reflect current arrangements, and contingency plans to mitigate the possible loss of expertise in this area as efficiency savings are implemented.

### **Health and safety of council staff**

- 2.12 A review is currently underway of the arrangements in place to ensure the continued wellbeing of lone workers employed throughout the council and that risk exposure to both employer and employee is appropriately managed.
- 2.13 We have finalised our work on the council's overall arrangements in relation to the health and safety of the council's staff. At the time of our review a new structure had recently been implemented by the Corporate Health, Safety and Wellbeing team, a corporate champions group had been established and directorate service level agreements put in place. However we found that there is no process in place to ensure that all corrective actions and recommendations (CARs) raised are carried forward and followed up by the Corporate Health, Safety and Wellbeing team: in August 2010 58% of the CARs raised in 2009/10 remained outstanding. Our audit also reviewed a number of controls operating in each of the directorates and we have raised some minor recommendations to ensure a standard and consistent approach is taken across the council.

### ***Compliance with the European Working Time Directive***

- 2.14 We reported in September that the council does not have arrangements in place to enable it adequately to comply with, and monitor compliance with, the European Working Time Directive and related British law, the European Working Time Regulations.
- 2.15 The corporate Human Resources team has now produced guidance notes for managers which will be communicated to all managers shortly. These guidance notes cover all of the recommendations raised in our report and include a number of management actions covering key areas such as working hours, young workers and night workers.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

### **Customer contact centre**

- 2.16 Our work on the ACORN customer relationship management system is still underway. This system is a key tool to support the delivery of the Corporate Customer Access Strategy and our work is focussed on the management and infrastructure of the system, to ensure effective and continual services are maintained and that there are effective controls to secure the application and its data.

### **The council's role as accountable body – Performance Reward Grant**

- 2.17 We have recently verified the details of performance data submitted by the county council and its district council partners as part of the certification process for the remaining funded elements of Performance Reward Grant. The council has recently claimed final grant funding in excess of £3.3m.

## **3 Progress in relation to corporate or common controls**

### **Financial control systems**

- 3.1 The Audit Commission again plans to place reliance on our work as part of their assessment of the council's overall risk and control environment, and their audit evidence over the systems by which the council's financial reports are generated. We are working together to ensure that our revised sampling methodology and testing meet the Audit Commission's revised audit approach and its compliance with the Clarified International Auditing Standards.
- 3.2 Whilst we are not yet in a position to report our detailed findings on all the key financial systems, we are on target to complete the reviews by the end of the financial year. The current position of the individual key financial system reviews is identified in the table below.

<b>System</b>	<b>Position</b>	<b>Opinion</b>
Accounts payable	Our fieldwork is complete and we have issued a draft report for management consideration.	Substantial assurance over the operation of the system.
Accounts receivable	Our fieldwork is complete and we have issued a draft report for management consideration.	Substantial assurance over the operation of the system.
VAT	Our fieldwork is complete and we are currently drafting a report of our findings.	We are not yet in a position to report our findings.
Payroll	Our fieldwork is ongoing.	
Expenses	Our fieldwork is ongoing.	
General ledger	Our fieldwork is ongoing.	
Treasury management	Fieldwork began in January.	
Cash and banking	Fieldwork began in January.	

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

### **Information governance**

- 3.3 There has been significant progress in information management and security across the council and, based upon this progress, we have now provided substantial assurance over the development of the council's information governance framework.
- 3.4 In September we noted that significant achievements and examples of good practice include the establishment of the Corporate Information Governance Group (CIGG) as the decision making body on all information governance issues and policy for the council which has strengthened the council's information security framework. Data on all laptops and memory sticks has been encrypted and all members of staff have been provided with information assurance training. Annual information risk reviews now inform the council's business plans.
- 3.5 In addition to these corporate achievements there are some important initiatives and examples of good practice within directorates and specific services, generally attributable to the work of the CIGG representatives. These individuals are essential in adapting corporate policies and objectives to their service areas, providing support and raising awareness on a day to day basis.
- 3.6 However the council's information governance arrangements are still developing and considerable effort is still required if the council is to continue to effectively mitigate its information risks and utilise the information it holds in a secure manner. As noted in September, information breaches continue to occur and one severe incident in particular has highlighted a number of issues relating to the reporting, management and investigation of such incidents. Action has already been taken by management to amend these processes.

### **ICT controls**

- 3.7 We postponed our work on ICT controls until the third quarter of the year to enable ICT Services' management to focus on the development of the strategic partnership.
- 3.8 However we have completed a review of Government Connect. This is a programme which enables local authorities in England and Wales to share sensitive information between themselves, central government departments and other national bodies. We have provided substantial assurance over the current control environment and assessors from the Department of Work and Pensions have approved and authorised the council's connection for 2010/11.
- 3.9 We are currently undertaking work to review the security of the council's network and data under new operational arrangements which have come into effect over the last few years. This work will include a focus on how network access is assigned, managed and terminated across the council.
- 3.10 A review of the arrangements for asset management and disposal will also begin in this quarter.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

### **Procurement and tendering**

- 3.11 We have completed two reviews of procurement arrangements across the council. We have been able to provide only limited assurance for both of these. Draft reports have been issued and discussed with the director of finance and the head of procurement who have agreed the findings and will be working with the strategic partner where appropriate to implement the recommendations. We will also work with the head of procurement to produce a report for the Procurement Board, which involves the directors responsible for procurement across the council, to enable them to drive forward the changes required to strengthen procurement arrangements.
- 3.12 Our review of procurement arrangements across the council identified a number of issues regarding the i-procurement system user hierarchy, which is not consistently updated as users leave the council or change their role. Some approval permissions have been inappropriately established, so that requests by senior staff for goods and services may be approved by their subordinates, and some staff may self-approve orders up to £50,000. Approval limits on i-procurement are in a number of cases higher than the approval limits in the scheme of delegation.
- 3.13 During our review on tendering arrangements throughout the council we sought documentation relating to a number of tender exercises which could not be located by the relevant directorates. We also found cases of non-compliance with the tendering procedures including the award and extension of contracts.

### **Controls over the council's estate**

- 3.14 The Property Group acts as the council's corporate landlord, for example developing the asset management plan, and supports the council in the practical management of its estate. In particular this involves managing the risk of corporate manslaughter through premises management controls. The council has adopted a policy framework developed by the Property Group, where a local premises manager should be designated to provide overall control on site and make an annual statement of compliance with corporate policy requirements.
- 3.15 We have completed a review of the premises management framework operated within the council's directorates, and intend to review the arrangements for schools as part of next year's audit plan. We are currently drafting our report and we will be in a position to share our findings at the next meeting of the Audit Committee.
- 3.16 We continue to provide assurance on the final accounts with contractors on a sample basis; there are no issues to report at this time.

### **Human resources controls**

#### ***Attendance management***

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- 3.17 We have completed our review of attendance management and have provided substantial assurance over the controls now operated by the council. There were no significant issues arising from this review although we have made several minor recommendations to improve the control environment and standardise procedures across the council.
- 3.18 This substantial assurance is corroborated in practice by the council's performance in terms of reduced sickness absence which has now been sustained over the last three years.

### ***Equal Pay Review***

- 3.19 We have continued to provide support to the Equal Pay Review, in particular testing pay protection arrangements and assimilation of staff to the new grading structure. We identified no concerns from this work and we are able to provide substantial assurance over this area of the Equal Pay Review.

### ***Employees on the payroll also receiving pensions***

- 3.20 Following a query by a member of the Audit Committee and at the request of the executive director for resources and the director of finance, we made enquiries about county council employees in receipt of both payroll and pension payments. All individuals receiving a gross salary of over £34,000 and a pension were selected for detailed testing and this resulted in a sample of 32 employees.
- 3.21 We identified one instance where flexible retirement does not appear to meet the stipulations of the Local Government Pension Scheme since there has been no reduction in either hours or grade, and three that, whilst technically meeting its requirements, did not appear reasonable. We have discussed these cases with the director of finance.

## **4 Progress in relation to service specific controls**

- 4.1 As work has progressed on the audit plan for 2010/11 it is appropriate to share the outcomes with ELT and the Audit Committee.

### **Direktorate for Children and Young People (CYP)**

#### ***Data quality***

- 4.2 As noted in September, we have completed our audit of data quality in relation to a sample of 10 national performance indicators but we were able to provide only limited assurance over the accuracy of the indicators because there were significant discrepancies between the source data (from ISSIS) and the data used to calculate several of the performance indicators. Although use of the national indicator set will cease on 31 March 2010, the same points will be applicable to other performance data monitored by the directorate. The issues of the reliability of ISSIS data will be addressed in the review of Children's Social Care systems to be undertaken by the Council's strategic partnership.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- 4.3 The staff involved in preparing this data have since begun to investigate the use of the same data interrogation software used by the Audit Service, and the auditors have provided some training.

### **ContactPoint accreditation**

- 4.4 As required by the former Department for Children, Schools and Families we provided a certificate confirming the council's compliance with accreditation criteria for 2009/10 in relation to the integrated ContactPoint database. However this database was subsequently closed during August 2010.

### **Sure Start, Early Years and Childcare Services commissioning arrangements**

- 4.5 We have followed up the recommendations made in our previous report, dated March 2010, in which we raised several significant recommendations and allocated the system limited/ no assurance. We are pleased to report that our recommendations have been implemented.
- 4.6 As we reported in September, commissioning agreements for the current year have been signed by each of the Sure Start providers and action to monitor expenditure to ensure it is eligible is scheduled to begin in January 2011. A further recommendation relating to the new commissioning agreement for the financial year 2011/12 can be implemented only when the new commissioning agreements are issued with effect from 1 April 2011.

### **Graduate Leader Fund**

- 4.7 The county council has been awarded funding of £1.79m for 2009/10 and £2.45m for 2010/11 relating to the costs of educating and training staff in leadership positions within nurseries to graduate level.
- 4.8 Due to the lack of controls and non-compliance with some of the existing controls we were unable to provide assurance over the controls in place for the operation of the Graduate Leader Fund and related support funding.
- 4.9 However many of the weaknesses in this area had already been identified by the Sure Start, Early Years and Childcare management team and a number of actions had been initiated. A member of this team has begun the task of improving the control environment around the Graduate Leader Fund, and the actions taken will be subject to a further internal audit review during 2011/12.

### **Schools**

- 4.10 We reported in September that we had been able to provided no or only limited assurance over the controls operating in four of the six schools we had then visited. We have now completed 21 school audit visits and a summary of the assurance levels is provided in the table below.

Level of assurance	Full	Substantial	Limited	None
Number of schools	0	11	8	2

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- 4.11 It should be noted that both of the schools given no assurance, and one of those given only limited assurance, were selected for audit on the basis of concerns raised either by the headteacher or the area finance office. These have not therefore been selected on any random basis and cannot reasonably be regarded as representative of schools generally.
- 4.12 Our audits have highlighted some common issues covering schools' income and letting arrangements. We have shared these assurance reports with our colleagues in the CYP Combined Finance Team who are in the process of providing additional support and guidance to these schools where appropriate. The Audit Service will provide support to the Schools Finance Team to inform and update schools' administrators and bursars of the control issues relating to their role.
- 4.13 We had begun to assess the county's schools against the Department for Education's Financial Management Standard in Schools (FMSiS) and had put considerable effort into establishing arrangements to make these assessments across all of the county's schools every three years. However the Secretary of State for Education announced the decision on 15 November 2010 to end the current FMSiS regime with immediate effect and to develop a simpler standard as a replacement. It is not yet clear what this simpler standard will be or whether it will require external assessment.
- 4.14 As at 31 December, we had expended 102 audit days on this FMSiS work.

### **Environment Directorate**

- 4.15 As noted above, cross-cutting reviews involving the directorate are at various stages of completion; health and safety in relation to both petroleum safety and corporate manslaughter, and safeguarding in relation to the transport of children and vulnerable adults. Other cross-cutting work focussed on the directorate and planned for later in the year includes arrangements for accessible transport, project management arrangements (specifically relating to the Heysham-M6 link and Guild Wheel projects), and the removal of the client-contractor split between the directorate and LCCG.
- 4.16 We continue to work with the directorate in relation to the Accrington Eco Station project and wider European Interreg programme for which the county council is the lead partner: this work will be on-going for some time.

### **Closed landfill sites**

- 4.17 A review of arrangements relating to the management of closed landfill sites has been completed. Whilst we have given substantial assurance over the controls in place, we have suggested improvements to the way in which some urgent work is procured and to ensure that monitoring data is kept up to date.

### **Development control**

- 4.18 Two reviews relating to different aspects of development control are near to completion. Firstly, Section 278 agreements refer to

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

developments affecting the strategic highway network. The audit work we have undertaken allows us to provide substantial assurance in respect of s278 agreements, and specifically the collection of associated fees and advanced payments, the design review process, scheme manager supervision, contractor selection, and the certification of defects correction and substantial completion. We are able to give limited assurance regarding the council's compliance with the s278 agreement in respect of invoicing or refunding a developer any excess balances at scheme completion.

- 4.19 The second development control area relates to section 106 agreements where the council may recover sums from developers to mitigate the impact of development upon local infrastructure. Whilst the council in its role as highways authority is a statutory consultee to such agreements, other councils' teams contribute to such agreements on a non-statutory basis. There is, therefore, a significant reliance upon planning functions within the district councils to ensure that the county council's interests are protected. Fieldwork in this area has been completed and a report is being drafted for consideration. The outcome of this review will be reported to a subsequent meeting of the Audit Committee.

### **Adult and Community Services Directorate (ACS)**

#### ***Case management***

- 4.20 Our work on adult social care case management is still under way, focussing on the allocation of cases, the creation and closure of user records, workload management and supervision, and the use of ISSIS.

#### ***Transforming Community Equipment Service: retail model***

- 4.21 Under the retail model equipment assessors prescribe simple equipment aids that can be fulfilled for service users by any accredited retailer. The model has been operated by the county council in east Lancashire since August 2008, in partnership with Blackburn with Darwen Council, Blackburn with Darwen Primary Care Trust (PCT) and East Lancashire PCT. More complex or bespoke equipment aids are made available to service users through the loan stores service. The development of this model is part of a national response to the impetus to provide person-centred care services.
- 4.22 We have assessed the effectiveness of the existing processes and controls and have provided substantial assurance over their adequacy and effectiveness.

#### **Joint work on Adult and Community Services Directorate and Lancashire County Commercial Group (LCCG)**

#### ***Reablement***

- 4.23 We have recently completed a review of the reablement service, which is commissioned by ACS and provided by LCCG. The fieldwork was undertaken between April and July 2010. We have considered both the effectiveness of the overall management of the service by

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- both ACS and LCCG, and the controls within LCCG that ensure that the needs of service users are met.
- 4.24 We can provide only limited assurance over the effectiveness of the overall management of service delivery. A service level agreement is needed to set out the service delivery and monitoring arrangements between ACS and LCCG. Weaknesses remain in the effectiveness of their joint operations – both referral arrangements within both bodies and the utilisation of care hours – since we last reviewed this area in November 2008. There was significant under-utilisation of care hours and under-achievement of the target number of referrals across the county at the time of this review, although the target has increased significantly.
- 4.25 LCCG has responded positively to these concerns by rationalising the duty system for staff, increasing the availability of administrative support and by seeking to employ more staff on contracts which better serve the needs of the business by supplying care at peak demand periods. A review of the performance monitoring information as at November 2010 indicates a significant improvement in the delivery of the target number of referrals processed by the service and the effective utilisation of available care hours.
- 4.26 Improvements in the quality of management information available to both LCCG and ACS has been slow to materialise, with the result that neither party is yet in a position to quantify how many referrals, considered appropriate for a reablement package of care by ACS, are subsequently refused and returned by LCCG due to capacity issues or because they are considered by LCCG as inappropriate for reablement care. Without a clearer understanding of the cause of the capacity constraints, it will be extremely difficult to implement operational or management changes that will result in the required improvements needed to service delivery and staff utilisation.
- 4.27 ACS and LCCG have established a project board and drawn up a comprehensive action plan to address these issues. Whilst the project board is not yet in a position to report that action has been taken to address every issue, there is now a robust process to review the issues raised.
- 4.28 We can however, provide substantial assurance over the adequacy and effectiveness of the controls within LCCG that ensure that the needs of service users are met once a decision has been made to provide care, and that controls are in place to ensure that service delivery complies with professional care standards.
- 4.29 One of the key outcome indicators of the success of the reablement service is the number of service users who are still in receipt of some form of home care service three months after the service has ceased. As at 31 May 2010, only a third of service users were receiving some form of ongoing care. Furthermore, ongoing customer satisfaction surveys continue to show very positive results suggesting that service users are very pleased with the quality of care they receive from the service.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

- 4.30 Our detailed examination of a sample of cases also indicated that the quality of service provision is high, as evidenced by staff compliance with service requirements and in terms of the maintenance of care records and documentation, both within and outside the ISSIS environment.

### **Lancashire County Commercial Group (LCCG)**

- 4.31 As noted above, we have undertaken a review of the reablement service commissioned by ACS and provided by LCCG. Also noted above, we have completed an audit of the council's compliance with the European Working Time Directive. In addition, we have undertaken work to follow up the work we reported in 2009/10 on residential care establishments, and have undertaken a considerable amount of work arising from whistle-blowing calls.

### ***Residential care establishments***

- 4.32 During 2009/10 we raised several concerns following visits to five care establishments relating to the administration of medication and preparation of care plans for residents. We have now followed-up the recommendations arising from that work and assessed the progress made by management in improving the care planning and medication processes.
- 4.33 Considerable progress has been made since the previous review to source and evaluate a single supplier of medication to all 17 care homes. A contract is expected to be signed early in 2011. Following this, management will work to review the policies and guidance in place.
- 4.34 LCCG's Care Services team has also developed key performance indicators covering care planning, which are monitored on a monthly basis and reported to the care home managers for action.
- 4.35 Some of our previous recommendations remain outstanding and management is still working to firmly establish some of the recent control improvements and we are discussing the outstanding issues with management.

### ***Whistle-blowing issues***

- 4.36 We have completed an investigation at one of the engineering depots following a number of whistle-blowing calls. A report has been submitted to the director of LCCG and a disciplinary hearing is scheduled for January 2011. Further information will be provided to the Audit Committee following the conclusion of the disciplinary action. Our investigation identified a number of control weaknesses which will also be addressed following the disciplinary process.

### **Economic development**

- 4.37 Reviews relating to income protection arrangements and cash management processes are scheduled to be undertaken in the latter part of the financial year.

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

### **Regenerate Pennine Lancashire (RPL) – the accountable body role**

- 4.38 The council remains the accountable body for the Housing Market Renewal Pathfinder partnership in the face of significant changes to the nature and amount of current and future funding. Audit work will continue to ensure that any risks to the council are robustly dealt with in this changing environment.
- 4.39 At the request of the RPL Board we are undertaking specific assurance work relating to the eligibility and accuracy of any redundancy payments the partnership will be required to make as a result of its reduced funding. The first phase of this work has been to confirm with the relevant funding bodies any eligibility criteria associated with their funding, and these details have been recently reported to the RPL Board.

### **Pension Fund**

- 4.40 We have completed a review of the pension fund's property fund and a draft report has been issued to management for consideration. Whilst we are not in a position to report our detailed findings, we have noted that the current fund manager has managed the fund for over 25 years. Although performance of the property portfolio can be compared to benchmark returns and compared to other local authority property portfolio returns, we do not have assurance that the charges being paid are currently competitive. This issue has already been identified by senior managers who are intending to re-tender the contract in the near future.
- 4.41 During this quarter we will undertake basic compliance testing on the current global custodian arrangements. Our intended review of the new global custodian arrangements has been deferred until next year, after completion of the on-going tender exercise.
- 4.42 We have kept a watching brief of the planned arrangements for the new bank account which are in hand, and it is the intention to review these as part of next year's audit plan.
- 4.43 We have continued to provide ongoing support and advice to management on the implementation of the new pension administration system during the year and a comprehensive review of this application, considering both manual and ICT controls will be undertaken during this quarter.

### **Investigations and counter fraud work**

- 4.44 Our work supporting the council's management of the risk of fraud falls broadly into responsive work, where allegations have been made or fraud suspected, and proactive work to enhance the council's controls and to consider areas of the council's activities that may be susceptible to the risk of fraud.

### **Responsive work**

- 4.45 We continue to undertake special investigations across the council and its schools and a number have begun recently. One has resulted in the resignation of an employee, who has received a conditional

## **Internal Audit progress against plan 2010/11**

Audit Committee meeting 24 January 2011

caution from the police. One has resulted in the employee being suspended pending disciplinary action and the matter has also been referred to the police. We continue to support Warwickshire Police with a national fraud investigation regarding bogus invoices from recruitment firms.

- 4.46 Other investigations are continuing and some work has been under way for a considerable period as the disciplinary process moves into employee tribunals and appeals.

### ***Proactive counter fraud work***

- 4.47 As part of our counter fraud work we have performed a series of unannounced visits to a number of the council's establishments that handle cash. All cash checked has been accounted for, but we are in the process of making some recommendations to improve controls over cash handling.
- 4.48 Through our professional counter fraud networks we have identified a number of scams which are being operated nationally. We have taken appropriate steps to prevent and minimise any losses to the council and have communicated these scams throughout the council and via the schools portal.
- 4.49 As part of the Audit Commission's National Fraud Initiative we will be receiving reports from the Audit Commission in February 2011 providing details that will require investigation. We will work with the relevant areas of the council to take appropriate action.

Audit area	Planned audit days		Audit work undertaken *			
	Annual plan	9 months pro-rated	Relating to 2009/10	Relating to 2010/11	Total days	Variance to date
<b>Cross-cutting issues</b>						
Corporate governance	25	19	1	26	27	8
Information governance	30	23		40	40	18
Risk management	15	11		3	3	(8)
Issues arising from the formation of a strategic partnership	20	15		113	113	98
Safeguarding	105	79		77	77	(2)
Health and safety of the public	35	26		40	40	14
Health and safety of staff	60	45		89	89	44
Integrated service delivery	70	53		5	5	(47)
The customer service centre	80	60		52	52	(8)
The accountable body role	30	23		13	13	(9)
Procurement	25	19		91	91	72
Performance Reward Grant	15	11		15	15	3
<b>Sub-total</b>	<b>510</b>	<b>383</b>	<b>1</b>	<b>563</b>	<b>564</b>	<b>182</b>
<b>Service-specific controls</b>						
Adult and Community Services Directorate	255	191	78	149	227	35
Directorate for Children and Young People	260	195	49	165	214	19
Schools	350	263	11	105	116	(147)
Environment Directorate	240	180	75	166	241	61
Lancashire County Commercial Group	100	75	9	68	76	1
Economic development	35	26	3	15	18	(8)
Regenerate Pennine Lancashire - accountable body	30	23		3	2	(19)
Pension Fund	120	90	8	44	52	(38)
<b>Sub-total</b>	<b>1,390</b>	<b>1,043</b>	<b>233</b>	<b>714</b>	<b>947</b>	<b>(95)</b>

\* Note that minor rounding differences can occur as figures are summed from the underlying data.

**Internal Audit Service: progress report**  
 Audit Committee meeting 24 January 2011

Audit area	Planned audit days		Audit work undertaken *			
	Annual plan	9 months pro-rated	Relating to 2009/10	Relating to 2010/11	Total days	Variance to date
<b>Corporate or common controls</b>						
Financial controls	455	341	90	368	458	117
Human resources controls	30	23	7	73	80	57
ICT controls	175	131	7	94	101	(30)
Property management controls	100	75	12	60	72	(3)
<b>Sub-total</b>	<b>760</b>	<b>570</b>	<b>115</b>	<b>595</b>	<b>710</b>	<b>140</b>
<b>Response to the risk of fraud</b>						
Management and proactive work	210	158		46	46	(112)
Responsive work/ whistle-blowing	290	218		394	394	176
<b>Sub-total</b>	<b>500</b>	<b>375</b>		<b>439</b>	<b>439</b>	<b>64</b>
<b>Management of the audit service</b>						
Audit and Standards Committees reporting and attendance	6	5		6	6	1
Audit planning processes	15	11		8	8	(4)
Audit reporting processes	15	11		19	19	7
Audit Commission liaison	4	3		3	3	0
Support to management	10	8		6	6	(2)
<b>Sub-total</b>	<b>50</b>	<b>38</b>		<b>42</b>	<b>42</b>	<b>4</b>
Contingency	50	38				(38)
<b>Total audit days</b>	<b>3,260</b>	<b>2,445</b>	<b>350</b>	<b>2,353</b>	<b>2,703</b>	<b>258</b>

\* Note that minor rounding differences can occur as figures are summed from the underlying data.

# Agenda Item 9

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected: All
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### Sure Start, Early Years and Childcare Services

Contact for further information:

Ian Rushworth, (01772) 534779, Resources Directorate

#### Executive Summary

At its meeting on 27 September 2010 the Audit Committee requested an update on the progress made by the council in addressing the issues identified in an internal audit report on Sure Start, Early Years and Childcare Services commissioning arrangements and specifically in relation to Sure Start Hyndburn.

The issues have been addressed as far as possible at this time.

#### Recommendation

The Audit Committee is asked to consider this report.

#### Background

The Audit Committee received an internal audit report on the Sure Start, Early Years and Childcare Services (SSEYCS) commissioning arrangements at its meeting on 29 March 2010. This report provided limited assurance over the financial accounting, monitoring and reporting systems in place relating to the Sure Start children's centres which had signed a commissioning agreement, due to the inconsistent application of controls. We were able to provide no assurance over the controls in place over children's centres that had not signed a commissioning agreement.

#### Sure Start, Early Years and Childcare Services (SSEYCS) commissioning arrangements

As noted in the Audit Service progress report, our recommendations have now been implemented. In particular, commissioning agreements for the current year have been signed by each of the Sure Start providers. Action to monitor expenditure to ensure it is eligible (including sample checks by the Combined Finance Team) is scheduled to begin in January 2011. A further recommendation, relating to monitoring expenditure against agreed funding, can be implemented only when the new commissioning agreements are issued with effect from 1 April 2011.

#### Sure Start Hyndburn (SSH)

The Audit Committee received a report on Sure Start Hyndburn at its meeting on 29 March 2010. Copies of correspondence between all parties following a meeting in April



2010 were also provided to the committee. This addressed three key themes, and the actions agreed are set out below, with an update on the current position.

#### ***Commissioning agreement***

SSEYCS requested that SSH sign the revised commissioning agreement and this was done in September 2010.

#### ***Financial management***

SSEYCS and SSH agreed regular timescales to prepare and submit quarterly financial returns: SSH agreed to submit financial returns with details of all 'other' expenditure by the end of the month following each quarter. Quarterly financial reports have been received from SSH on a timely basis containing the required information.

#### ***Use of grant funding***

Both parties were to continue to seek advice from central government regarding the use of the grant to support the nurseries, cafe and Space Centre. SSH were informed by SSEYCS that the grant should not be used to support these activities from April 2011 onwards. Discussions have been held between SSEYCS and SSH regarding the use of the grant to support the nurseries, cafe and Space Centre. The use of the grant will be clarified before any funding for April 2011 onwards is allocated.

#### **Consultations**

Not applicable.

#### **Advice**

Not applicable.

#### **Alternative options to be considered**

Not applicable.

**Implications:** e.g. financial, legal, personnel, human rights, crime and disorder or other.

None

#### **Risk management**

This report supports the Audit Committee in undertaking its role, which includes advising the Council on the adequacy of the Authority's strategic risk management processes.

#### **Local Government (Access to Information) Act 1985**

#### **List of Background Papers**

Paper	Date	Contact
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Not applicable.

**Reason for inclusion in Part II, if appropriate:** N/A

# Agenda Item 10

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected:  
All

### Annual audit letter 2009/10 – Audit Commission Report

Appendix A refers.

Contact for further information:

Clive Portman, 0844 798 7038, Audit Commission, c-portman@audit-commission.gov.uk

#### Executive Summary

The report sets out the Audit Commission's annual audit letter for 2009/10.

#### Recommendation

The Committee are asked to consider the Audit Commission's Annual Audit Letter for 2009/10.

#### Background and Advice

The Audit Commission's annual audit letter for 2009/10 is attached at Appendix A. The letter summarises for members the more important matters arising from the 2009/10 audit and is also a public document published on the Council's and Audit Commission's websites. The letter has also been considered by Cabinet at its meeting on 2<sup>nd</sup> December 2010.

Clive Portman, District Auditor, will attend the meeting to present the report and respond to questions.

#### Consultations

The report was agreed with the Council's Chief Executive and Executive Director of Resources. In accordance with the regulations the letter will be made available for public inspection on the Council's website.

#### Implications:

N/A

#### Risk management

N/A

**Local Government (Access to Information) Act 1985**  
**List of Background Papers**

Paper	Date	Contact/Directorate/Tel
Annual governance report	September 2010	Clive Portman 0844 798 7056

Reason for inclusion in Part II, if appropriate

N/A

# Annual Audit Letter

Lancashire County Council

Audit 2009/10

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

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

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

# Contents

<b>Key messages .....</b>	<b>2</b>
Audit opinion and financial statements .....	2
Value for money.....	2
Current and future challenges .....	3
<b>Financial statements and annual governance statement .....</b>	<b>4</b>
Overall conclusion from the audit .....	4
Internal control .....	4
IFRS in local government .....	5
Investment in Landsbanki .....	5
National Fraud Initiative .....	5
<b>Value for money .....</b>	<b>7</b>
2009/10 use of resources assessments .....	7
VFM conclusion .....	7
Managing Finances .....	8
Governing the Business.....	9
Managing Resources.....	11
Approach to local value for money work from 2010/11.....	12
<b>Current and future challenges.....</b>	<b>13</b>
<b>Closing remarks .....</b>	<b>14</b>
<b>Appendix 1 – Glossary .....</b>	<b>15</b>

# Key messages

**This report summarises my findings from the 2009/10 audit. My audit is made up of two elements: the audit of your financial statements (pages 4 to 5) and my assessment of your arrangements to achieve value for money in your use of resources (pages 6 to 11).**

## Audit opinion and financial statements

**1** My 2009/10 audit is now complete and I have concluded the accounts give a true and fair view of the financial position of the Council and its spending and income for 2009/10. I issued an unqualified audit opinion on 30 September 2010.

## Value for money

**2** I am required to assess whether the Council has put in place adequate arrangements for securing economy, efficiency and effectiveness in its use of resources. I concluded the Council has adequate arrangements in place and I issued an unqualified VFM conclusion on 30 September 2010.

**3** The Council has continued its good performance and has improved its arrangements in several areas. This includes developing further its approach to financial planning, commissioning and procurement which will be important to help the Council address the financial challenges ahead. It recognises the need to develop in specific areas and has plans in place to do so. These include:

- improving the value for money achieved from the Council's significant purchasing power;
- supporting directorates in reviewing the existing arrangements for providing services;
- strengthening corporate risk management; and
- additional support for officers and members to deliver and monitor the more complex treasury management strategy.

## **Current and future challenges**

4 Like all councils, Lancashire faces significant financial pressures. The full extent of necessary spending reductions resulting from the Autumn 2010 Comprehensive Spending Review and allocation of grant funding from 2011/12 and beyond needs to be assessed. The Council has already started to address the potential implications of the spending review and will need to continue to review priorities, service standards and how services are delivered as the extent of the spending reductions become clearer.

# Financial statements and annual governance statement

**The Council's financial statements and annual governance statement demonstrate how the Council accounts for its stewardship of public funds.**

**I gave an unqualified opinion on the Council's 2009/10 financial statements on 30 September 2010 within the statutory target date.**

## Overall conclusion from the audit

**5** The financial statements were prepared to a good standard and supported by comprehensive working papers. This was again a challenging year for preparing the financial statements following the introduction of new accounting requirements. This has included bringing onto the Council's balance sheet the full value of assets it uses under the Private Finance Initiative (PFI) for the first time, totalling £118 million.

**6** While some amendments were needed to the accounts following their submission to the June 2010 Audit Committee, none of these were material. None of the amendments impacted on the financial position of the authority. The annual governance statement reflected our understanding of the Council's arrangements to ensure effective stewardship of public monies and the outcome of its review of their effectiveness.

**7** Following the completion of my audit I concluded that the amended accounts give a true and fair view of the financial position of the Council and its spending and income for 2009/10. I issued an unqualified audit opinion on 30 September 2010.

## Internal control

**8** The overall control environment is adequate although there are examples of inconsistency between departments in the application of controls. For a Council of this size and diversity, this is not unusual. Internal audit have reported identified weaknesses and action plans have been agreed to improve the consistent application of controls.

- 9** I have made recommendations in two areas about internal control of the Pension Fund and an action plan has been agreed. These relate to
- action needed by officers to obtain greater assurance over private equity investment valuations; and
  - continued effort by officers to achieve effective implementation of a separate bank account for the pension fund by 1 April 2011.

## **IFRS in local government**

**10** The 2008 Budget included an announcement that all public bodies would follow international financial reporting standards (IFRS). Local authorities will prepare financial statements based on IFRS for 2010/11.

**11** A failure to achieve successful transition to IFRS would cause significant reputational damage to individual local authorities and the local government sector as a whole. Poor preparation will heighten the risk that accounts will not meet requirements and so attract a qualified auditor's opinion or be published late. At a practical level, there is a risk that extra and unnecessary costs will be incurred.

**12** I have liaised with key finance staff on the key changes required and the plans in place to address them. I have also undertaken a number of surveys on the Council's progress towards IFRS. I assessed the Council as making good progress although there remains a significant amount of work. This is being closely monitored and managed by the Council's IFRS project group.

## **Investment in Landsbanki**

**13** As previously reported, the Council has investments in Landsbanki Iceland pf totalling £10 million. (This includes investments on behalf of the Pension Fund and Police and Fire Authorities). Latest guidance received is that councils should recover 95 per cent of these investments. This however assumes that the Council will be classed as a priority creditor, which will be decided by the Icelandic courts with the judgement expected late in 2011. If priority status is not confirmed it is estimated that recovery could fall to 38 per cent.

## **National Fraud Initiative**

**14** The Audit Commission plays an important role in the fight against fraud. It runs a data matching exercise every two years to help detect and prevent fraud: the National Fraud Initiative (NFI). The total fraud, overpayments and errors detected across the country in the latest completed exercise covering 2008/2009 amount to £215 million. Since the exercise began in 1996, cumulative national savings total £614 million.

**15** The NFI is a data matching exercise comparing information held by different organisations, including some from the private sector, to identify potentially fraudulent claims and overpayments. Examples of data matching undertaken include pension payments being checked to records of deceased persons and council tax records being matched to the electoral register. The Council participates in this bi-annual exercise. Savings identified by the Council as part of this latest exercise, including estimated forward savings, amount to £1.096 million. Most of this relates to the identification of pensions being paid to deceased pensioners.

## Value for money

**I considered whether the Council is managing and using its money, time and people to deliver value for money.**

**I assessed your performance against the criteria specified by the Audit Commission and have reported the outcome as the value for money (VFM) conclusion.**

### **2009/10 use of resources assessments**

**16** At the end of May 2010, the Commission wrote to all chief executives to inform them that following the government's announcement, work on CAA would cease with immediate effect. As a result the Commission would no longer issue scores for its use of resources assessments.

**17** However, I am still required by the Code of Audit Practice to issue a value for money conclusion. I have therefore used the results of the work completed on the use of resources assessment up to the end of May 2010 to inform my 2009/10 conclusion.

**18** I report the significant findings from the work I have carried out to support the vfm conclusion.

### **VFM conclusion**

**19** I assessed your arrangements to achieve economy, efficiency and effectiveness in your use of money, time and people against criteria specified by the Audit Commission. The Audit Commission specifies each year which Key Lines of Enquiry (KLOE) are the relevant criteria for the VFM conclusion at each type of audited body.

**20** This is a summary of my findings.

Criteria	Adequate arrangements?
Managing finances	
Planning for financial health	Yes
Understanding costs and achieving efficiencies	Yes
Financial Reporting	Yes
Governing the business	
Commissioning and procurement	Yes
Use of information	Yes
Good governance	Yes
Risk management and internal control	Yes
Managing resources	
Workforce	Yes
Strategic asset management	Yes

**21** I issued an unqualified conclusion stating the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources. I reported the findings of my work in relation to the VFM conclusion to members of the Audit Committee in my Annual Governance Report on 28 September 2010 and this is set out below.

## Managing Finances

**22** In previous years we have identified this as an area where the Council performs well. Arrangements in 2009/10 continue to be sound and the Council is responding well to the new financial pressures it is facing.

**23** The Council has robust financial arrangements in place that effectively support the delivery of strategic objectives. It is in sound financial health and has a strong track record of managing spending within budgets. However, like all councils, it currently faces significant financial pressures. The Authority's financial strategy focuses on planning for future reductions in public spending, while continuing to make efficiency savings that will help to protect investment in priority services and meet increased costs in areas such as waste disposal. The Council's approach to Treasury Management has changed in response to the increased risks within global markets. The new strategy plans to reduce the risk to the Council while maintaining returns where possible.

**24** The Authority has a good understanding of its relative costs and performance. During 2009/10 it has used comparative information to identify scope for future efficiencies in areas such as youth services. The streamlined Business Improvement Programme is now more effective for reconfiguring services. Outcomes from the Programme during 2009/10 include an increase of £1.7 million in recovered debt, £430,000 savings from a more efficient approach to internal mail, and improved quality outcomes from a dedicated mobile minute-taking service for adult and children's statutory social care meetings. More significant outcomes are planned for future years. For example, the cost of the Council's Human Resources function is comparatively high and this is a focus for the developing Strategic Partnership.

### **Areas for future focus and development**

**25** The County Council faces an additional £22 million fall in government funding in 2010/11. In addition, it has already programmed over £20 million of efficiency savings from a wide range of sources. Given the scale and scope of the required savings, close monitoring will be important to ensure they are fully delivered. Detailed monitoring and reporting on the delivery of planned efficiency savings during 2010/11 is already planned. The full extent of necessary spending reductions will become clearer after the Comprehensive Spending Review and the settlement of revenue grant funding for 2011/12 and beyond.

**26** The Council's new treasury management strategy introduces more complex decision making and loans and investments. To support its implementation, effective skills development and training for relevant staff and members will be important. Monitoring reports also need to more clearly measure the impact of decisions on the changing risk profile of the Council's loans and investments.

**27** The Authority can improve value for money from its significant purchasing power. To achieve this, it needs to develop a better understanding of procurement and transaction costs. An internal review of procurement is currently underway; we would expect this to create a clear picture of where and how money is spent, and where scope for efficiencies is greatest. Reporting of procurement outcomes, including benefits for service users and compliance with corporate policies, also needs to be strengthened. Some progress has already been made, with improved management information leading to more effective challenge of procurement decisions.

## **Governing the Business**

**28** Over the past year the Council has built on its existing strengths in the areas of governance, performance management, use of information and data quality. Some progress has been made in addressing weaknesses previously identified in commissioning and procurement but it is too soon to discern significant outcomes from this. Corporate risk management arrangements need to be strengthened.

**29** The Council is improving its approach to strategic service commissioning. The recent restructure of the Environment Directorate reflects commissioning principles - for example, integrated working with district councils on streetscene. These changes are expected to deliver both cost reductions and improvements for the public. The Council is also in the process of setting up a strategic partnership with a private sector partner to provide key support services, including human resources and information technology. At the local strategic partnership, (LSP), level, partners are reviewing their activity and impact on the four 'big ticket' issues - economy, health, housing and climate change - to identify scope for reconfiguring resources.

**30** During 2009/10, information management arrangements have been strengthened by officer workshops and the completion of encryption and data security e-learning programmes. The Council has a robust framework to oversee data quality. Performance management is strong, and information is well presented to support decision making. As in previous years, the Council's network has been penetration tested by external specialists

**31** Strong ethical and governance arrangements are in place. Member training and development is good and, in 2009/10, included extensive training for 48 new councillors. The Audit Committee is challenging and effective. Arrangements for monitoring Pension Fund performance by members has also improved. This has enabled members to more effectively challenge performance.

**32** Numerous examples of effective risk management exist across the Council. These include the actions taken to manage the significant in-year spending pressures during 2009/10 and to reduce the risk of the Council's exposure to financial markets.

## **Areas for future focus and development**

**33** The maintenance and use of a corporate risk register has not been effective during 2009/10. Internal Audit has also identified inconsistencies in the effectiveness of risk management across the Council. The need to improve the Council's corporate risk management arrangements has been accepted by the Council and is reflected within its annual governance statement.

**34** Some concerns remain over the security of the Council's network. Penetration testing of key corporate IT systems found several weaknesses, including unauthorised access to payroll data (read-only) and the fact that many networked servers do not have up to date security patches installed, making them more vulnerable to hacking. Steps have subsequently been taken to close off unauthorised access to payroll data, and improved patch management processes/software will be introduced during 2010/11. Arrangements for network access by staff working from home do not meet the security standards currently required by Government Connect. This is

the subject of disagreement and further discussion between the Council and Government Connect.

**35** There remains scope for the Council to more clearly articulate its approach to strategic service commissioning. Directorates are beginning to undertake reviews of their commissioning activity in the light of the new financial position and would benefit from clearer guidance on the key issues to be addressed.

## Managing Resources

**36** During 2009/10, we re-examined the Authority's arrangements for securing value for money from its physical assets and found that these remain effective. We also looked, for the first time, at how the Council is managing its workforce to meet current and future needs.

**37** The Council has a strong approach to asset management that is helping to deliver strategic priorities. Through comprehensive property data and an ongoing process of property review, the Council challenges whether all its assets are required, fit for purpose and providing value for money. The Council continues to enthusiastically pursue office rationalisation, particularly in Preston city centre. The Preston offices review has so far generated £2.4 million in capital receipts, released nine leased and three owned buildings, and reallocated retained workspace at a more efficient 8.5 square metres per work station. County-wide, office rationalisation has realised revenue savings in excess of £50 million over the past five years. The Council continues to promote joined-up asset management with district councils through 'aligned asset management plans', although this has so far produced few tangible outcomes. A joint portfolio review with Central Lancashire Primary Care Trust (PCT) is underway, covering Children's Centres, GP surgeries and the PCT estate.

**38** Workforce planning and people management arrangements support the Council's strategic objectives well. Effective systems are in place to attract, retain and develop the right people. This includes good use of apprenticeships and a strong approach to skills development. The Council can show evidence of improving productivity through service reconfiguration and reducing absence. It has a good track record of involving staff in organisational change. Sickness absence fell by 4 per cent in 2009/10 as a result of improved occupational health and absence intervention, although the ambitious target reduction was not met. Skill shortages exist in some areas – for example, children's social work and some engineering services – and these are being addressed. Workforce planning has been variable in quality across the organisation but should become more robust and consistent as a new corporate template is launched. For example, the Children and Young People's Directorate has a clear workforce strategy, linking challenges to improvement measures, and can demonstrate positive outcomes such as greater success in filling vacancies for primary headships on the first attempt. The Authority has refreshed its approach to promoting equality and diversity. Its new 'Narrowing the Gaps' strategy includes plans

to strengthen partnership working and to support managers in better understanding the profile of their service users.

### **Areas for future focus and development**

**39** Despite the County Council's efforts to co-ordinate asset management with district councils, there remain disappointingly few examples of joint property use that transform access to services for the public. In the context of the financial pressures facing the public sector, the County Council should continue to lead this agenda, seeking more active support from local partners.

**40** The new corporate model for workforce planning needs to be implemented consistently across directorates to ensure that the Authority knows in the medium to longer term what staff it will need, with what skills, and has plans to achieve this.

### **Approach to local value for money work from 2010/11**

**41** Given the scale of pressures facing public bodies in the current economic climate, the Audit Commission has been reviewing its work programme for 2010/11 onwards. This review has included discussions with key stakeholders of possible options for a new approach to local value for money (VFM) audit work. The Commission aims to introduce a new, more targeted and better value approach to our local VFM audit work.

**42** My work will be based on a number of reporting criteria, specified by the Commission, concentrating on:

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

**43** I will determine a local programme of VFM audit work based on my audit risk assessment, informed by these criteria and my statutory responsibilities. I will no longer be required to provide an annual scored judgement relating to my local VFM audit work. Instead I will report the results of all my local VFM audit work and the key messages for the Council in my annual report to those charged with governance and in my annual audit letter.

## Current and future challenges

**44** The economic downturn and banking crisis is having a very significant impact on public finances and the bodies that manage them. There are implications for treasury management strategies and there are likely to be wider and more fundamental impacts on the ability of public sector bodies to fund service delivery and capital programmes, in particular, pressures on income streams.

**45** The Council faces perhaps its toughest ever period financially. In order to meet increasing demand from the local population, drive up quality and respond to rising expectations the Council will have to do more with its money. It is, therefore, inevitable that the shape of some services will have to change.

**46** As the Council moves forward it will need to continue to develop robust arrangements to:

- ensure resilience in medium term financial strategies;
- deliver efficiencies and future plans;
- update treasury management strategies;
- assess the funding requirements and re-prioritise capital programmes;
- review income streams; and
- identify patterns of changing demand profiles and shift priorities accordingly.

## Closing remarks

**47** I have discussed and agreed this letter with the Chief Executive and the Executive Director of Resources. I will present this letter at the Cabinet on 2 December 2010 and will provide copies to all members.

**48** Full detailed findings, conclusions and recommendations in the areas covered by our audit were included in the reports I issued to the Council during the year.

Report	Date issued
Audit Opinion Plan	June 2010
Annual Governance Report	September 2010
Opinion on the financial statements	September 2010
Value for Money conclusion	September 2010
Audit Letter	November 2010

**49** The Council has taken a positive and helpful approach to our audit. I wish to thank the Lancashire County Council staff for their support and cooperation during the audit.

Clive Portman  
District Auditor

November 2010

# Appendix 1 – Glossary

## **Annual governance statement**

Governance is about how local government bodies ensure that they are doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner.

It comprises the systems and processes, cultures and values, by which local government bodies are directed and controlled and through which they account to, engage with and where appropriate, lead their communities.

The annual governance statement is a public report by the Council on the extent to which it complies with its own local governance code, including how it has monitored the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.

## **Audit opinion**

On completion of the audit of the accounts, auditors must give their opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question;
- whether they have been prepared properly, following the relevant accounting rules; and
- for local probation boards and trusts, on the regularity of their spending and income.

## **Financial statements**

The annual accounts and accompanying notes.

## **Qualified**

The auditor has some reservations or concerns.

## **Unqualified**

The auditor does not have any reservations.

## **Value for money conclusion**

The auditor's conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of money, people and time.

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**0844 798 7070**

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

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



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November 2010

# Agenda Item 11

## Audit Committee

Meeting to be held on 24 January 2011

Electoral Division affected: None
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## Audit Commission – Lancashire County Council and Pension Fund 2010/11

### Audit Plans

(Appendix A and B refer).

Contact for further information:

Fiona Blatcher, 0844 798 7056, Audit Commission,  
[f-blatcher@audit-commission.gov.uk](mailto:f-blatcher@audit-commission.gov.uk)

### Executive Summary

In June the Audit Committee received proposed fee letters for the audit of the County Council and Pension Fund for 2010/11. Since then, the 2009-10 audit has been completed and detailed audit plans have now been produced setting out in particular the key audit risks for 2010/11 and the planned audit strategy.

These plans set out the audit work the Audit Commission propose to undertake in relation to the audit of the financial statements 2010/11 and the provision of a VFM conclusion for Lancashire Council (Appendix A) and the audit of the pension fund financial statements (Appendix B). The plan is based on the Audit Commission's risk-based approach to audit planning which assesses:

- current national risks relevant to your local circumstances; and
- your local risks and improvement priorities.

It includes a summary of the key risks for the financial statements and VFM conclusion identified through this process together with the auditor's planned response.

### Recommendation

The committee is asked to note the Audit Commission's reports.

### Background and Advice

Clive Portman, District Auditor, will attend the meeting to present the reports and respond to questions.

### Consultations

These reports have been agreed with the Director of Finance.

**Implications:**

N/A

**Risk management**

N/A

**Local Government (Access to Information) Act 1985**  
**List of Background Papers**

Paper	Date	Contact/Directorate/Tel
Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies		Fiona Blatcher Audit Commission 0844 798 7056
Audit Commission Act 1998		
Code of Audit Practice		
Reason for inclusion in Part II, if appropriate		
N/A		

# Audit plan

Lancashire County Council

Audit 2010/11

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

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

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

# Contents

<b>Introduction .....</b>	<b>2</b>
<b>Responsibilities .....</b>	<b>3</b>
<b>Fee for the audit .....</b>	<b>4</b>
Specific actions Lancashire County Council could take to reduce its audit fees .....	5
<b>Auditors report on the financial statements.....</b>	<b>6</b>
Materiality .....	6
Identifying opinion audit risks.....	6
<b>Identification of specific risks.....</b>	<b>7</b>
<b>Testing strategy .....</b>	<b>9</b>
<b>Value for money conclusion .....</b>	<b>10</b>
Value for money risks .....	10
<b>Key milestones and deadlines.....</b>	<b>11</b>
<b>The audit team.....</b>	<b>12</b>
Independence and objectivity .....	12
Meetings .....	12
Quality of service .....	12
Planned outputs.....	13
<b>Appendix 1 Basis for fee .....</b>	<b>14</b>
Assumptions .....	14
<b>Appendix 2 Independence and objectivity .....</b>	<b>15</b>
<b>Appendix 3 Working together.....</b>	<b>17</b>
Meetings .....	17
Sustainability.....	17
<b>Appendix 4 Glossary .....</b>	<b>18</b>

# Introduction

**This plan sets out the audit work that I propose to undertake for the audit of financial statements and the value for money conclusion 2010/11.**

- 1** The plan is based on the Audit Commission's risk-based approach to audit planning. It reflects:
  - audit work specified by the Audit Commission for 2010/11;
  - current national risks relevant to your local circumstances; and
  - your local risks.

# Responsibilities

**The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out the respective responsibilities of the auditor and the audited body. The Audit Commission has issued a copy of the Statement to every audited body.**

**2** The Statement summarises where the different responsibilities of auditors and of the audited body begin and end and I undertake my audit work to meet my responsibilities.

**3** I comply with the statutory requirements governing our audit work, in particular:

- the Audit Commission Act 1998; and
- the Code of Audit Practice.

## Fee for the audit

**The fee for the audit is £279,000 as indicated in my letter of 15 April 2010.**

**4** The Audit Commission scale fee for Lancashire County Council is £338,150. The fee proposed for 2010/11 is 17 per cent below the scale fee and is within the normal level of variation specified by the Commission.

**5** As noted in my letter of 15 April 2010, the above fee included a 6 per cent increase to cover the costs of additional audit work arising from the introduction of International Reporting Standards. In July 2009, the Commission confirmed it would subsidise the 'one-off' element of the cost of transition to International Financial Reporting Standards (IFRS) for local authorities from 2010/11. As a result the Council has received a rebate from the Audit Commission of £20,496 in April 2010.

**6** The Commission wrote to all audited bodies, on 9 August 2010 about its proposed new arrangements for local value for money audit work. This indicated the impact on audit fees for 2010/11 would be considered as part of the Commission's consultation on its work programme and scales of fees for 2011/12. The recently issued consultation paper proposes a further rebate of the 2010/11 fee of 3.5 per cent of the scale fee. The consultation period ends on 7 January and final fees will be notified in February 2011.

**7** The Commission will also not charge inspection fees for work carried out during 2010/11 on the managing performance part of the organisational assessment. This is because there was no value to the work once CAA ended.

**8** In setting the fee, I have assumed that:

- the level of risk in relation to the audit of accounts is consistent with that for 2009/10;
- good quality, accurate working papers are available at the start of the financial statements audit;
- the Council will supply good quality working papers to support the restatement of 2009/10 balances to comply with International Financial Reporting Standards (IFRS)]; and
- Internal Audit undertakes appropriate work on all material systems and this is available for our review by 30 April 2011.

**9** Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee. Where this is the case, I will discuss this first with the County Treasurer and I will issue supplements to the plan to record any revisions to the risk and the impact on the fee.

**10** Further information on the basis for the fee is set out in Appendix 1.

## **Specific actions Lancashire County Council could take to reduce its audit fees**

**11** The Audit Commission requires its auditors to inform audited bodies of specific actions it could take to reduce its audit fees. As in previous years, I will work with staff to identify any specific actions that the Council could take and to provide ongoing audit support.

# Auditors report on the financial statements

**I will carry out the audit of the financial statements in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board (APB).**

**12** I am required to issue an audit report giving my opinion on whether the accounts give a true and fair view of the financial position of the Council as at 31 March 2011.

## **Materiality**

**13** I will apply the concept of materiality in both planning and performing the audit, in evaluating the effect of any identified misstatements, and in forming my opinion.

## **Identifying opinion audit risks**

**14** I need to understand fully the audited body to identify any risk of material misstatement (whether due to fraud or error) in the financial statements. I do this by:

- identifying the business risks facing the Council, including assessing your own risk management arrangements;
- considering the financial performance of the Council;
- assessing internal control - including reviewing the control environment, the IT control environment and Internal Audit; and
- assessing the risk of material misstatement arising from the activities and controls within the Council information systems.

# Identification of specific risks

**I have considered the additional risks that are appropriate to the current opinion audit and have set these out below.**

Table 1: **Specific risks**

Specific opinion risks identified

Risk area	Audit response
Some material assets under the waste PFI scheme may need to come on to the Council's balance sheet for the first time in 2010/11 depending on the date the sites became fully operational. This will require complex estimations of contract values and allocations within the accounts.	We will review the management controls used to ensure the resultant figures are materially correct and will carry our tests of detail on the technical calculations and accounting entries.
2010/11 is the first year of full implementation of the new international financial reporting standards, (IFRS). This is likely to result in some material changes to the accounts and requires detailed work to ensure no material items are missed.	We will continue to review the Council's management controls in place to ensure effective implementation of IFRS and continue to discuss with accountants any specific issues. We will carry out tests of detail on the restated opening position for 2010/11 as early as possible and will complete further testing of in-year movements and year end balances.
Audit work in previous years has identified inconsistent application of controls across the Council around payroll, creditors, schools and journals. This lessens our ability to rely on testing of controls in these areas. Additional workload pressures in payroll during 2010/11 increase the inherent risk of error around payroll.	Where Internal Audit work shows the same issues apply for 2010/11, we will perform tests of detail rather than taking a controls based approach. Testing of detail for payroll will use larger sample sizes to reflect the higher risk identified.

Risk area	Audit response
<p>The Council may need to produce group accounts for 2010/11 for the first time in some years. This will depend upon the Council's assessment of the impact of the changes under IFRS and the creation of the Strategic Partnership.</p>	<p>We will review the Council's assessment of the position. If group accounts are needed we will prepare a specific testing strategy. This is likely to include planned reliance on the work of other auditors of the components of the group.</p>
<p>New financial systems and processes have been introduced during 2010/11 for accounts receivables and treasury management.</p>	<p>We will plan to place reliance on the work of internal audit for these systems. Independent confirmation of year-end investments and borrowings will be obtained as in previous years.</p>
<p>The Council's new approach to Treasury Management could result in the Council having more complex financial instruments on its balance sheet by 31/3/2011. Valuation of such instruments is likely to be less straight forwards and require estimation of values. As the new strategy involves greater complexity, the need for a stronger skill set for both officers and members and closer management of risk profiles exists. This includes the need for careful review to ensure there is no borrowing to lend on.</p>	<p>For a sample of more complex financial instruments we will test in detail the validity of any estimation assumptions. We will continue to review the detailed application of the new treasury management strategy. This will include review of compliance with prudential guidelines, clarity of reporting to members and reviewing the Council's analysis of its investments and borrowings against its reserves, provisions and borrowing need.</p>

# Testing strategy

**On the basis of risks identified above I will produce a testing strategy which will consist of testing key controls and/or substantive tests of transaction streams and material account balances at year end.**

**15** I can carry out the testing both before and after the draft financial statements have been produced (pre- and post-statement testing).

**16** Wherever possible, I will complete some substantive testing earlier in the year before the financial statements are available for audit. I have identified the following areas where substantive testing could be carried out early.

- Bank reconciliation.
- Borrowing and investments - independent confirmation.
- Fixed assets - existence and ownership.
- Restated opening balances and comparatives under IFRS.
- Estimation of values for Waste PFI.
- Group accounts - assessment of need for group accounts.
- Payroll, creditors and SIMs testing of detail transactions.

Where I identify other possible early testing, I will discuss it with officers.

**17** Wherever possible, I will seek to rely on the work of Internal Audit to help meet my responsibilities. For 2010/11, I expect to be able to use the results of the following pieces of work:

- Accounts payable.
- Accounts receivable.
- Cash and bank.
- Treasury Management.
- General ledger.

**18** I will also seek to rely on the work of other auditors and experts, as appropriate, to meet my responsibilities. For 2010/11, I plan to rely on the work of other auditors for Group Accounts if they need to be produced. I also plan to rely on the work of experts in the following areas:

- actuarial assessment of the Council's proportion of pension fund assets and liabilities
- property valuers estimates of Council assets at 31 March 2011.

# Value for money conclusion

## I am required to give a statutory VFM conclusion on the Council's arrangements to secure economy, efficiency and effectiveness.

**19** This is based on two criteria, specified by the Commission, related to your arrangements for:

- securing financial resilience – focusing on whether the Council is managing its financial risks to secure a stable financial position for the foreseeable future; and
- challenging how the Council secures economy, efficiency and effectiveness – focusing on whether the Council is prioritising its resources within tighter budgets and improving productivity and efficiency.

**20** I will plan a programme of VFM audit work based on my risk assessment.

## Value for money risks

**21** I will undertake my risk assessment for the vfm conclusion over the next few months and will communicate with you then. An early consideration of potential VFM risks has identified the following areas that are likely to require a more detailed review:

- Waste PFI contract - actions taken to ensure the contract delivers value for money.
- Strategic partnership - work to understand in more detail the nature of the arrangement, business case including assessed costs and benefits and arrangements to manage performance and ensure effective governance of the partnership.
- Savings plans - realism and robustness of planned savings over the next three years.

# Key milestones and deadlines

**The Council is required to prepare the financial statements by 30 June 2011. I am required to complete the audit and issue the opinion and value for money conclusion by 30 September 2011.**

**22** The key stages in producing and auditing the financial statements are in Table 2.

**23** I will agree with you a schedule of working papers required to support the entries in the financial statements. The agreed fee is dependent on the timely receipt of accurate working papers.

**24** During the audit, the audit team will meet with the key contact and review the status of all queries. The frequency of such meetings will be agreed with the key contact and depend on the need and the number of issues arising.

Table 2: **Proposed timetable**

Activity	Date
Control and early substantive testing	February - May 2011
Receipt of accounts	June 2011
Sending audit working papers to the auditor	Early July 2011
Start of detailed testing	July 2011
Progress meetings	as required
Detailed risk assessment for VFM conclusion	January to March 2011
Any detailed work arising from VFM risk assessment	April to July 2011
Present report to those charged with governance at the audit committee	September 2011
Issue opinion and value for money conclusion	By September 2011

# The audit team

**Table 3 shows the key members of the audit team for the 2010/11 audit.**

Table 3: Audit team

Name	Contact details	Responsibilities
Clive Portman District Auditor	c-portman@audit-commission.gov.uk 0844 798 7038	Responsible for the overall delivery of the audit including the quality of outputs, signing the opinion and conclusion, and liaison with the Chief Executive.
Fiona Blatcher Senior Audit Manager	f-blatcher@audit-commission.gov.uk 0844 798 7056	Manages and coordinates the different elements of the audit work. Key point of contact for the County Treasurer.

## Independence and objectivity

**25** I am not aware of any relationships that may affect the independence and objectivity of the District Auditor and the audit staff, which I am required by auditing and ethical standards to communicate to you.

**26** I comply with the ethical standards issued by the APB and with the Commission's requirements in respect of independence and objectivity as summarised in Appendix 2.

## Meetings

**27** The audit team will ensure we have knowledge of your issues to inform our risk-based audit through regular liaison with key officers. Our proposals are set out in Appendix 3.

## Quality of service

**28** I aim to provide you with a fully satisfactory audit service. If, however, you are unable to deal with any difficulty through me and my team please contact Chris Westwood, Director of Professional Practice, Audit Practice, Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ (c-westwood@audit-commission.gov.uk) who will look into any complaint promptly and to do what he can to resolve the position.

**29** If you are still not satisfied you may of course take up the matter with the Audit Commission's Complaints Investigation Officer (The Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol BS34 8SR).

## Planned outputs

**30** My team will discuss and agree reports with the right officers before issuing them to the Audit Committee.

Table 4: Planned outputs

Planned output	Indicative date
Annual governance report	September 2011
Auditor's report giving an opinion on the financial statements and value for money conclusion	30 September 2011
Final accounts memorandum [if needed]	November 2011
Annual audit letter	November 2011

# Appendix 1 Basis for fee

The Audit Commission is committed to targeting its work where it will have the greatest effect, based upon assessments of risk and performance. This means planning work to address areas of risk relevant to our audit responsibilities and reflecting this in the audit fees.

The risk assessment process starts with the identification of the significant financial and operational risks applying to the Council with reference to:

- my cumulative knowledge of the Council;
- planning guidance issued by the Audit Commission;
- the specific results of previous and ongoing audit work;
- interviews with Council officers; and
- liaison with Internal Audit.

## Assumptions

In setting the fee, I have assumed that:

- the level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2009/10;
- you will inform me of significant developments impacting on the audit;
- Internal Audit meets the appropriate professional standards;
- Internal Audit undertakes appropriate work on all systems that provide material figures in the financial statements sufficient that I can place reliance for the purposes of our audit;
- you provide:
  - good quality working papers and records to support the financial statements by 8th July 2011;
  - information asked for within agreed timescales;
  - prompt responses to draft reports; and
- there is no allowance for extra work needed to address questions or objections raised by local government electors.

Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee.

## Appendix 2 Independence and objectivity

Auditors appointed by the Audit Commission are required to comply with the Commission's Code of Audit Practice and Standing Guidance for Auditors, which defines the terms of the appointment. When auditing the financial statements, auditors are also required to comply with auditing standards and ethical standards issued by the Auditing Practices Board (APB).

The main requirements of the Code of Audit Practice, Standing Guidance for Auditors and the standards are summarised below.

International Standard on Auditing (UK and Ireland) 260 (Communication of audit matters with those charged with governance) requires that the appointed auditor:

- discloses in writing all relationships that may bear on the auditor's objectivity and independence, the related safeguards put in place to protect against these threats and the total amount of fee that the auditor has charged the client; and
- confirms in writing that the APB's ethical standards are complied with and that, in the auditor's professional judgement, they are independent and their objectivity is not compromised.

The standard defines 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case, the appropriate addressee of communications from the auditor to those charged with governance is the Audit Committee. The auditor reserves the right, however, to communicate directly with the Council on matters which are considered to be of sufficient importance.

The Commission's Code of Audit Practice has an overriding general requirement that appointed auditors carry out their work independently and objectively, and ensure that they do not act in any way that might give rise to, or could reasonably be perceived to give rise to, a conflict of interest. In particular, appointed auditors and their staff should avoid entering into any official, professional or personal relationships which may, or could reasonably be perceived to, cause them inappropriately or unjustifiably to limit the scope, extent or rigour of their work or impair the objectivity of their judgement.

The Standing Guidance for Auditors includes a number of specific rules.

The key rules relevant to this audit appointment are as follows.

- Appointed auditors should not perform additional work for an audited body (ie work over and above the minimum required to meet their statutory responsibilities) if it would compromise their independence or might give rise to a reasonable perception that their independence could be compromised. Where the audited body invites the auditor to carry out risk-based work in a particular area that cannot otherwise be justified as necessary to support the auditor's opinion and conclusions, it should be clearly differentiated within the Audit and Inspection Plan as being 'additional work' and charged for separately from the normal audit fee.
- Auditors should not accept engagements that involve commenting on the performance of other auditors appointed by the Commission on Commission work without first consulting the Commission.
- The District Auditor responsible for the audit should, in all but the most exceptional circumstances, be changed at least once every seven years, with additional safeguards in the last 2 years.
- The District Auditor and senior members of the audit team are prevented from taking part in political activity on behalf of a political party, or special interest group, whose activities relate directly to the functions of local government or NHS bodies in general, or to a particular local government or NHS body.

The District Auditor and members of the audit team must abide by the Commission's policy on gifts, hospitality and entertainment.

# Appendix 3 Working together

## Meetings

The audit team will ensure we have knowledge of your issues to inform our risk-based audit through regular liaison with key officers.

My proposal for the meetings is as follows.

Table 5: **Proposed meetings with officers**

Council officers	Audit Commission staff	Timing	Purpose
Chief Executive	District Auditor (DA) and Senior Audit Manager (SAM)	Quarterly	General update
County Treasurer	DA and SAM	Monthly	General update plus: January - audit plan March - VFM risk assessment July - accounts progress September - annual governance report
Senior accountancy staff	AM and Teamleader	As necessary	Update on audit and accounting issues.
Internal audit	DA and SAM	Tri-annually	General update
Audit Committee	DA and SAM	As determined by the Committee	Formal reporting of: Audit Plan Annual governance report Other issues as appropriate

## Sustainability

The Audit Commission is committed to promoting sustainability in our working practices and I will actively consider opportunities to reduce our impact on the environment. This will include:

- reducing paper flow by encouraging you to submit documentation and working papers electronically;
- use of video and telephone conferencing for meetings as appropriate; and
- reducing travel.

# Appendix 4 Glossary

## **Annual audit letter**

Report issued by the auditor to an audited body that summarises the audit work carried out in the period, auditors' opinions and conclusions and significant issues arising from auditors' work.

## **Audit of the accounts**

The audit of the accounts of an audited body comprises all work carried out by auditors in accordance with the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

## **Audited body**

A body to which the Audit Commission is responsible for appointing the external auditor, comprising both the members of the body and its management (the senior officers of the body). Those charged with governance are the members of the audited body. (See also 'Members' and 'Those charged with governance'.)

## **Auditing Practices Board (APB)**

The body responsible in the UK for issuing auditing standards, ethical standards and other guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

## **Auditing standards**

Pronouncements of the APB, which contain basic principles and essential procedures with which auditors are required to comply, except where otherwise stated in the auditing standard concerned.

## **Auditor(s)**

Auditors appointed by the Audit Commission.

## **Code (the)**

The Code of Audit Practice.

## **Commission (the)**

The Audit Commission for Local Authorities and the National Health Service in England.

## **Ethical Standards**

Pronouncements of the APB that contain basic principles that apply to the conduct of audits and with which auditors are required to comply, except where otherwise stated in the standard concerned.

## **Financial statements**

The annual statement of accounts or accounting statements that audited bodies are required to prepare, which summarise the accounts of the audited body, in accordance with regulations and proper practices in relation to accounts.

## **Internal control**

The whole system of controls, financial and otherwise, that is established in order to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

## **Materiality (and significance)**

The APB defines this concept as ‘an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor’s report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’.

The term ‘materiality’ applies only in relation to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, in addition to their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

The concept of ‘significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

## **Members**

The elected, or appointed, members of local government bodies who are responsible for the overall direction and control of the audited body. (See also ‘Those charged with governance’ and ‘Audited body’.)

## **Statement on internal control/Annual Governance Statement**

Local government bodies are required to publish a statement on internal control (SIC) with their financial statements (or with their accounting statements in the case of small bodies). The disclosures in the SIC are supported and evidenced by the body's assurance framework. At local authorities the SIC is known as the Annual Governance Statement and is prepared in accordance with guidance issued by CIPFA.

### **Those charged with governance**

Those charged with governance are defined in auditing standards as 'those persons entrusted with the supervision, control and direction of an entity'.

In local government bodies, those charged with governance, for the purpose of complying with auditing standards, are:

- for local authorities – the full council, audit committee (where established) or any other committee with delegated responsibility for approval of the financial statements;
- for police or fire authorities – the full authority, audit committee (where established) or other committee with delegated responsibility for approval of the financial statements;
- for local probation boards and trusts – the board or audit committee; and
- for other local government bodies – the full authority or board or council, audit committee (where established) or any other committee with delegated responsibility for approval of the financial statements

Audit committees are not mandatory for local government bodies, other than police authorities and local probation trusts. Other bodies are expected to put in place proper arrangements to allow those charged with governance to discuss audit matters with both internal and external auditors. Auditors should satisfy themselves that these matters, and auditors' reports, are considered at the level within the audited body that they consider to be most appropriate.

### **Whole of Government Accounts**

The Whole of Government Accounts initiative is to produce a set of consolidated financial accounts for the entire UK public sector on commercial accounting principles. Local government bodies, other than probation boards and trusts, are required to submit a consolidation pack to the department for Communities and Local Government which is based on, but separate from, their statutory accounts.

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**0844 798 7070**

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

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



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January 2011



# Audit opinion plan

Lancashire Pension Fund

Audit 2010/11

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

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

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

# Contents

<b>Introduction .....</b>	<b>2</b>
<b>Responsibilities .....</b>	<b>3</b>
<b>Fee for the audit .....</b>	<b>4</b>
Specific actions Lancashire Pension Fund could take to reduce its audit fees .....	5
<b>Auditors report on the financial statements.....</b>	<b>6</b>
Materiality .....	6
Identifying opinion audit risks.....	6
<b>Identification of specific risks.....</b>	<b>7</b>
<b>Testing strategy .....</b>	<b>10</b>
Audit Commission IAS 19 protocol .....	11
<b>Key milestones and deadlines.....</b>	<b>12</b>
<b>The audit team.....</b>	<b>13</b>
Independence and objectivity .....	13
Meetings .....	13
Quality of service .....	14
Planned outputs.....	14
<b>Appendix 1 Basis for fee .....</b>	<b>15</b>
Assumptions .....	15
<b>Appendix 2 Independence and objectivity .....</b>	<b>16</b>
<b>Appendix 3 Working together.....</b>	<b>18</b>
Meetings .....	18
Sustainability.....	18
<b>Appendix 4 Glossary .....</b>	<b>19</b>

# Introduction

**This plan sets out the audit work that I propose to undertake for the audit of financial statements of the pension fund.**

- 1** The plan is based on the Audit Commission's risk-based approach to audit planning, which assesses:
  - current national risks relevant to your local circumstances; and
  - your local risks.
- 2** I will discuss and agree this plan, and any reports arising from the audit, with the Pension Fund Committee. However, as the pension fund accounts remain part of the financial statements of Lancashire County Council as a whole, the Audit Committee will retain ultimate responsibility for receiving, considering and agreeing the audit plans, as well as receiving and considering any reports arising from the audit.

# Responsibilities

**The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out the respective responsibilities of the auditor and the audited body. The Audit Commission has issued a copy of the Statement to every audited body.**

**3** The Statement summarises where the different responsibilities of auditors and of the audited body begin and end and I undertake my audit work to meet my responsibilities.

**4** I comply with the statutory requirements governing our audit work, in particular:

- the Audit Commission Act 1998; and
- the Code of Audit Practice.

**5** Specifically, the work of auditors on pension fund accounts is defined by the Auditing Practices Board practice note 15 on the audit of pension fund accounts.

## Fee for the audit

**The indicative fee for the audit is £61,795, as noted in my letter of 7 June 2010.**

**6** The Audit Commission scale fee for Lancashire Pension Fund is £49,437. The fee proposed for 2010/11 is 25 per cent above the scale fee and is within the normal level of variation specified by the Commission.

**7** In setting the fee, I have assumed that:

- the level of risk in relation to the audit of accounts is consistent with that for 2009/10;
- good quality, accurate working papers are available at the start of the financial statements audit; and
- Internal Audit undertakes appropriate work on all material systems and this is available for our review by 30 April 2011.

**8** Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee. Where this is the case, I will discuss this first with the Treasurer of the Pension Fund and I will issue supplements to the plan to record any revisions to the risk and the impact on the fee.

**9** Further information on the basis for the fee is set out in Appendix 1.

## **Specific actions Lancashire Pension Fund could take to reduce its audit fees**

**10** The Audit Commission requires its auditors to inform audited bodies of specific actions it could take to reduce its audit fees. As in previous years, I will work with staff to identify any specific actions that the Pension Fund could take and to provide ongoing audit support.

**11** Specific actions already noted during 2010 include the effective operation of a separate bank account for the pension fund and ensuring all fund managers can provide independent confirmation of their controls over processing and valuation. Action is already in hand to have a separate bank account from April 2011.

**12** A report to the Pension Fund Committee on 10 December set out proposed changes to the Fund's Investment Strategy going forwards. These will have a significant impact on the nature of the investment portfolio and its management going forwards. Such changes are likely to increase the audit procedures needed in future and could therefore result in increased audit fees. We will work with staff to understand the detailed changes and identify any specific actions around these changes that could help to lessen the impact on audit fees.

# Auditors report on the financial statements

**I will carry out the audit of the financial statements in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board (APB).**

**13** I am required to issue an audit report giving my opinion on whether the accounts give a true and fair view of the financial position of the Pension Fund as at 31 March 2011.

**14** I am also required to review the pension fund annual report according to the LGPS regulations 1997.

## **Materiality**

**15** I will apply the concept of materiality in both planning and performing the audit, in evaluating the effect of any identified misstatements, and in forming my opinion.

## **Identifying opinion audit risks**

**16** I need to understand fully the audited body to identify any risk of material misstatement (whether due to fraud or error) in the financial statements. I do this by:

- identifying the business risks facing the Pension Fund, including assessing your own risk management arrangements;
- considering the financial performance of the Pension Fund;
- assessing internal control - including reviewing the control environment, the IT control environment and Internal Audit; and
- assessing the risk of material misstatement arising from the activities and controls within the Pension Fund information systems.

# Identification of specific risks

**I have considered the additional risks that are appropriate to the current opinion audit and have set these out below.**

Table 1: Specific risks

Specific opinion risks identified

Risk area	Audit response
Implementation of International Financial Reporting Standards (IFRS). This requires disclosure in the pension fund accounts of future pension liabilities as well as current liabilities. This will require liaison with the actuary to ensure sufficient and appropriate information is available to meet the requirements. Actuarial estimates involve a wide range of uncertainty because of the variety and range of assumptions made within the estimation process.	We will: <ul style="list-style-type: none"><li>■ review the information provided to the actuary by the Pension Fund to support their estimation process;</li><li>■ obtain independent expert advice on our ability to rely on the actuaries estimates; and</li><li>■ ensure the actuarial information is shown correctly in the financial statements.</li></ul>
Changes in key staff. This increases the inherent risk of material error or non-compliance with accounting standards within the Pension Fund financial statements.	Standard audit procedures on the whole should be sufficient to cover this risk including a detailed early review of the draft financial statements. In addition we will increase the level of sample testing we will undertake on individual items of account.

Risk area	Audit response
<p>Pensions administration. During 2010/11 a new financial system for calculating and paying pensions has been implemented. The Pensions team has also been dealing with increased workloads following the implementation of redundancy/early retirement programmes of admitted bodies. These changes both increase the inherent risk of material error in pension payments and could also impact on the accuracy of information provided to the actuary.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>■ plan to rely on the work of internal audit around introducing the new pensions system;</li> <li>■ review the management controls in place to ensure the various changes have not resulted in a significant weakening in pensions processing</li> <li>■ carry out tests of detail on the accuracy of pension calculations and processing during the year including carrying out predictive analytical review procedures.</li> </ul>
<p>Private Equity, (PE) Investment Values. The pension fund has over £100 million invested in private equity funds. These are not traded on an open market and therefore their valuations are estimated by the private equity fund operators. The Pension Fund have agreed to complete more detailed checking of these valuations following recognised industry guidance for 2010/11. As the Pension Fund investment strategy is developing there may be an increase in other more complex investment instruments during 2010/11.</p>	<p>We will review the actions taken by the Pension Fund to gain assurance about the valuations provided and plan to place reliance on these controls if possible. If this does not provide sufficient assurance we will complete sample testing of PE values by reference to audited accounts and communications with relevant auditors of the Funds. Should other more complex investments have become more significant in 2010/11, for example the use of derivatives, we will follow a similar approach to that noted above.</p>

Risk area	Audit response
<p>Lack of a separate bank account.</p> <p>During 2010/11 the pension fund has continued to use the County Council's bank account. This raises a potential risk of misallocation of money between the Pension Fund and the County Council. During the period actions have been taken in to prepare for the introduction of a separate bank account by April 2011. These include reducing the amount of cash going through the Council's bank account for pension fund investments. In addition a full reconciliation of the Pension Fund cash position will be available to support the opening of the new bank account.</p>	<p>We will:</p> <ul style="list-style-type: none"> <li>■ review the actions taken to implement the new bank account;</li> <li>■ test in detail the year end reconciliation of the pension fund cash held within the County Council's bank account as at 31/3/2010; and</li> <li>■ consider the implications of this work on the cash balance recorded during the year and its use to calculate the interest due to or from the pension fund during the year.</li> </ul>

# Testing strategy

**On the basis of risks identified above I will produce a testing strategy which will consist of testing key controls and substantive tests of transaction streams and material account balances at year end.**

**17** I can carry out the testing both before and after the draft financial statements have been produced (pre- and post-statement testing).

**18** Wherever possible, I will complete some substantive testing earlier in the year before the financial statements are available for audit. I have identified the following areas where substantive testing could be carried out early:

- estimated future pension liabilities;
- reconciliation of Pension Fund year end cash invested in Lancashire County Council; and
- investments.

Where I identify other possible early testing, I will discuss it with officers.

**19** Wherever possible, I will seek to rely on the work of Internal Audit to help meet my responsibilities. For 2010/11, I expect to be able to use the results of the following pieces of work:

- pensions payment system including the transfer of data from the old to the new pensions system;
- accounts payable;
- accounts receivable, and
- general ledger.

**20** I will also seek to rely on the work of other auditors and experts, as appropriate, to meet my responsibilities. For 2010/11, I plan to rely on the work of other auditors for the accuracy and completeness of pensions contributions from admitted bodies.

**21** I also plan to rely on the work of experts in relation to the actuarial estimates of future pension fund liabilities:

## Audit Commission IAS 19 protocol

**22** To avoid unnecessary duplication, the Audit Commission requires the auditors of local government pension funds to undertake a work programme as part of a protocol to provide opinion audit assurance on admitted bodies' LGPS pension fund assets and liabilities. Auditors are then required to report the outcome of this work to the auditors of the admitted bodies. This work relates to those assets and liabilities that arise as a result of applying International Accounting Standard 19 (IAS19). This assurance work includes:

- reviewing the actuary's analysis of the pension fund's assets to establish whether the asset value attributed to the admitted bodies' accounts are consistent with the total scheme assets considered in the audit of the pension fund's accounts, and
- making enquiries of the actuary in relation to their work in calculating IAS19 assets and liabilities.

# Key milestones and deadlines

**The Pension Fund is required to prepare the financial statements by 30 June 2011. I am required to complete the audit and issue the opinion by 30 September 2011.**

**23** The key stages in producing and auditing the financial statements are in Table 2.

**24** I will agree with you a schedule of working papers required to support the entries in the financial statements. The agreed fee is dependent on the timely receipt of accurate working papers.

**25** During the audit, the audit team will meet with the key contact and review the status of all queries. The frequency of meetings will depend on the need and the number of issues arising.

Table 2: **Proposed timetable**

Activity	Date
Control and early substantive testing	February-May 2011
Receipt of accounts	June 2011
Sending audit working papers to the auditor	June 2011
Start of detailed testing	July 2011
Progress meetings	As required
Present report to those charged with governance at the audit committee	September 2011
Issue opinion	By 30 September 2011

# The audit team

**Table 3 shows the key members of the audit team for the 2010/11 audit.**

Table 3: Audit team

Name	Contact details	Responsibilities
Clive Portman District Auditor	c-portman@audit-commission.gov.uk 0844 798 7038	Responsible for the overall delivery of the audit including the quality of outputs, signing the opinion, and liaison with the Treasurer
Fiona Blatcher Senior Audit Manager	f-blatcher@audit-commission.gov.uk 0844 798 7056	Manages and coordinates the different elements of the audit work. Key point of contact for the Head of Pension Fund and Senior Accountant.

## Independence and objectivity

**26** I have identified the following relationship that might affect objectivity and independence and have put appropriate safeguards in place.

Table 4: Relationships and safeguards

Relationship	Safeguard
A member of our audit team is related to a member of the pensions administration team.	Our member of staff does not undertake, or is responsible for the review of, any of our work which assesses the work of the pensions team.

**27** I comply with the ethical standards issued by the APB and with the Commission's requirements in respect of independence and objectivity as summarised in Appendix 2.

## Meetings

**28** The audit team will ensure we have knowledge of your issues to inform our risk-based audit through regular liaison with key officers. Our proposals are set out in Appendix 3.

## **Quality of service**

**29** I aim to provide you with a fully satisfactory audit service. If, however, you are unable to deal with any difficulty through me and my team please contact Chris Westwood, Director of Professional Practice, Audit Practice, Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ (c-westwood@audit-commission.gov.uk) who will look into any complaint promptly and to do what he can to resolve the position.

**30** If you are still not satisfied you may of course take up the matter with the Audit Commission's Complaints Investigation Officer (The Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol BS34 8SR).

## **Planned outputs**

**31** My team will discuss and agree reports with the right officers before issuing them to the Audit Committee.

Table 5: **Planned outputs**

Planned output	Indicative date
Annual governance report	September 2011
Auditor's reports giving an opinion on the financial statements	30 September 2011
Final accounts memorandum [if needed]	November 2011

# Appendix 1 Basis for fee

The Audit Commission is committed to targeting its work where it will have the greatest effect, based upon assessments of risk and performance. This means planning work to address areas of risk relevant to our audit responsibilities and reflecting this in the audit fees.

The risk assessment process starts with the identification of the significant financial and operational risks applying to the Pension Fund with reference to:

- my cumulative knowledge of the Pension Fund;
  - planning guidance issued by the Audit Commission;
  - the specific results of previous and ongoing audit work;
- interviews with Pension Fund officers; and
- liaison with Internal Audit.

## Assumptions

In setting the fee, I have assumed that:

- the level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2009/10;
- you will inform me of significant developments impacting on the audit;
- Internal Audit meets the appropriate professional standards;
- [Internal Audit undertakes appropriate work on all systems that provide material figures in the financial statements sufficient that I can place reliance for the purposes of our audit];
- you provide:
  - good quality working papers and records to support the financial statements by [date];
  - information asked for within agreed timescales;
  - prompt responses to draft reports; and
- there is no allowance for extra work needed to address questions or objections raised by local government electors.

Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee.

## Appendix 2 Independence and objectivity

Auditors appointed by the Audit Commission are required to comply with the Commission's Code of Audit Practice and Standing Guidance for Auditors, which defines the terms of the appointment. When auditing the financial statements, auditors are also required to comply with auditing standards and ethical standards issued by the Auditing Practices Board (APB).

The main requirements of the Code of Audit Practice, Standing Guidance for Auditors and the standards are summarised below.

International Standard on Auditing (UK and Ireland) 260 (Communication of audit matters with those charged with governance) requires that the appointed auditor:

- discloses in writing all relationships that may bear on the auditor's objectivity and independence, the related safeguards put in place to protect against these threats and the total amount of fee that the auditor has charged the client; and
- confirms in writing that the APB's ethical standards are complied with and that, in the auditor's professional judgement, they are independent and their objectivity is not compromised.

The standard defines 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case, the appropriate addressee of communications from the auditor to those charged with governance is the Audit Committee. The auditor reserves the right, however, to communicate directly with the Council on matters which are considered to be of sufficient importance.

The Commission's Code of Audit Practice has an overriding general requirement that appointed auditors carry out their work independently and objectively, and ensure that they do not act in any way that might give rise to, or could reasonably be perceived to give rise to, a conflict of interest. In particular, appointed auditors and their staff should avoid entering into any official, professional or personal relationships which may, or could reasonably be perceived to, cause them inappropriately or unjustifiably to limit the scope, extent or rigour of their work or impair the objectivity of their judgement.

The Standing Guidance for Auditors includes a number of specific rules.

The key rules relevant to this audit appointment are as follows.

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- The District Auditor responsible for the audit should, in all but the most exceptional circumstances, be changed at least once every seven years, with additional safeguards in the last two years.
- The District Auditor and senior members of the audit team are prevented from taking part in political activity on behalf of a political party, or special interest group, whose activities relate directly to the functions of local government or NHS bodies in general, or to a particular local government or NHS body.

The District Auditor and members of the audit team must abide by the Commission's policy on gifts, hospitality and entertainment.

# Appendix 3 Working together

## Meetings

The audit team will ensure we have knowledge of your issues to inform our risk-based audit through regular liaison with key officers.

My proposal for the meetings is as follows.

Table 6: Proposed meetings with officers

Council officers	Audit Commission staff	Timing	Purpose
Treasurer	District Auditor (DA) and Senior Audit Manager (SAM)	Monthly	General update plus: January - audit plan July - accounts progress September - annual governance report
Head of Pensions and Senior Accountant	Senior Audit Manager and Teamleader	Quarterly	Update on audit, accounting and governance issues
Internal Audit	DA and SAM	Tri-annually	Update on audit issues
Audit Committee and Pension Fund Committee	DA and SAM	As determined by the Committee	Formal reporting of: Audit Plan Annual governance report Other issues as appropriate

## Sustainability

**32** The Audit Commission is committed to promoting sustainability in our working practices and I will actively consider opportunities to reduce our impact on the environment. This will include:

- reducing paper flow by encouraging you to submit documentation and working papers electronically;
- use of video and telephone conferencing for meetings as appropriate; and
- reducing travel.

# Appendix 4 Glossary

## **Audit of the accounts**

The audit of the accounts of an audited body comprises all work carried out by auditors in accordance with the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

## **Audited body**

A body to which the Audit Commission is responsible for appointing the external auditor, comprising both the members of the body and its management (the senior officers of the body). Those charged with governance are the members of the audited body. (See also 'Members' and 'Those charged with governance'.)

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## **Financial statements**

The annual statement of accounts or accounting statements that audited bodies are required to prepare, which summarise the accounts of the audited body, in accordance with regulations and proper practices in relation to accounts.

## **Internal control**

The whole system of controls, financial and otherwise, that is established in order to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

## **Materiality (and significance)**

The APB defines this concept as ‘an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor’s report; likewise a misstatement is material if it would have a similar influence. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’.

## **Those charged with governance**

Those charged with governance are defined in auditing standards as ‘those persons entrusted with the supervision, control and direction of an entity’.

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