Portsmouth City Council

Audit Committee Summary

For the year ended 31 March 2015

Audit Results Report – ISA (UK and Ireland) 260

September 2015

EY

Building a better working world

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Section 1

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Audit results and other key matters

The Audit Commission's Code of Audit Practice (the Code) requires us to report to those charged with governance – the Governance Audit and Standards Committee – on the work we have carried out to discharge our statutory audit responsibilities together with any governance issues identified.

This report summarises the findings from the 2014/2015 audit which is substantially complete. It includes the messages arising from our audit of your financial statements and the results of the work we have undertaken to assess your arrangements to secure value for money in your use of resources.

Financial statements

- As of 28 September 2015, we expect to issue an unqualified opinion on the financial statements. Our audit results demonstrate, through the few matters we have to communicate, that the Council has prepared its financial statements adequately.

Value for money

- We expect to conclude that you have made appropriate arrangements to secure economy, efficiency and effectiveness in your use of resources. However we have raised concerns that current plans will not be sufficient to enable the identification and delivery of savings to the scale required, in the time available .

Whole of Government Accounts

- We have not reported any significant matters to the National Audit Office (NAO) regarding the Whole of Government Accounts submission.

Audit certificate

- The audit certificate is issued to demonstrate that the full requirements of the Audit Commission's Code of Audit Practice have been discharged for the relevant audit year. We expect to issue the audit certificate at the same time as the audit opinion.

Section 2

Extent and purpose of our work

Extent and purpose of our work

The Council's responsibilities

- The Council is responsible for preparing and publishing its Statement of Accounts, accompanied by the Annual Governance Statement. In the Annual Governance Statement, the Council reports publicly on the extent to which it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.
- The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Purpose of our work

- Our audit was designed to:
  - Express an opinion on the 2014/2015 financial statements and the consistency of other information published with them
  - Report on an exception basis on the Annual Governance Statement
  - Consider and report any matters that prevent us being satisfied that the Council had put in place proper arrangements for securing economy, efficiency and effectiveness in the use of resources (the Value for Money conclusion)
  - Discharge the powers and duties set out in the Audit Commission Act 1998 and the Code of Audit Practice

In addition, this report contains our findings related to the areas of audit emphasis and any views on significant deficiencies in internal control or the Council's accounting policies and key judgments.

As a component auditor, we also follow the NAO group instructions and report the results on completion of the WGA work through the Assurance Statement to the NAO and to the Council..

This report is intended solely for the information and use of the Council. It is not intended to be and should not be used by anyone other than the specified party.

Section 3

Addressing audit risks

Addressing audit risks – significant audit risks

We identified the following audit risks during the planning phase of our audit, and reported these to you in our Audit Plan. Here, we set out how we have gained audit assurance over those issues.

A significant audit risk in the context of the audit of the financial statements is an inherent risk with both a higher likelihood of occurrence and a higher magnitude of effect should it occur and which requires special audit consideration. For significant risks, we obtain an understanding of the entity's controls relevant to each risk and assess the design and implementation of the relevant controls.

Audit risk identified within our audit plan	Audit procedures performed	Assurance gained and issues arising
Significant audit risks (including fraud risks)		
As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of their ability to directly or indirectly manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively	► Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements; ► Reviewed accounting estimates for evidence of management bias; and ► Evaluated the business rationale for significant unusual transactions.	► Journals testing did not identify any instances that suggested management override. ► Our review of accounting estimates did not identify any examples of management bias ► No unusual items were identified.

Addressing audit risks – other audit risks

- We identified the following audit risks during the planning phase of our audit, and reported these to you in our Audit Plan. Here, we set out how we have gained audit assurance over those issues.

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
Other audit risks		
The Council has made a number of changes to the layout of the Property plant and Equipment note to the accounts, which will involve restating the 2013/14 note and then following the same format for 2014/15 onwards. Last year we made some recommendations about streamlining the Council's fixed asset accounting and valuation processes. In 2014/15, the Council has revised the valuation procedures and begun to rationalise its fixed asset register (FAR).	Our testing involved: ► Reviewing the controls the Council implements to oversee transition to the revised disclosures and amendments to the fixed asset register; ► testing the accuracy of the restatement exercise and rationalisation of the fixed asset register; and ► testing the operation of the revised valuation processes	► We found the Council had implemented appropriate controls to oversee the transition to the revised disclosures and confirmed appropriate amendments had been made. ► We found the restatement exercise was completed accurately. ► We found the revised valuation process to be appropriate but that work is on-going to complete rationalisation of the FAR.

Section 4

Financial statements audit – issues and findings

Financial statements audit – issues and misstatements arising from the audit

Progress of our audit

- The following areas of our work programme remain to be completed. We will provide an update of progress at the Governance Audit and Standards Committee meeting:
  - Receipt of a Letter of Representation,
  - Responses to assorted sundry queries to enable us to conclude our testing on PPE, leases and reserves, and
  - Completion of our WGA work
- Subject to the satisfactory resolution of the above items, we propose to issue an unqualified audit report on the financial statements.

Uncorrected misstatements

- We have identified no misstatements within the draft financial statements that management has chosen not to adjust.

Corrected misstatements

- Our audit identified a number of misstatements in disclosure notes, which our team have highlighted to management for amendment. These have been corrected during the course of our work and are not considered significant enough to report.

Other matters

- As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we are required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Council's financial reporting process including the following:
  - Qualitative aspects of your accounting practices; estimates and disclosures;
  - Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions;
  - Any significant difficulties encountered during the audit; and
  - Other audit matters of governance interest

We noted there are still a large number of assets within the Fixed Asset Register (FAR) that are not depreciated currently. While this could not lead to a material misstatement in the accounts, officers need to review these carefully and ensure that all assets are depreciated in accordance with the Council's accounting policy.

There are also a number of assets held at nil value on the FAR, one of those at nil value at 31/03/14 was revalued in 2014/15 to £1m. Again, while we are satisfied any potential value of other such assets would not lead to a material misstatement in the accounts. officers need to ensure that there are no other assets with a value that should be recognised in the accounts.

Further work is also needed to cleanse the FAR by removing redundant asset lines and identifying groups of small and similar assets that could be aggregated..

The Department for Transport has indicated Harbour Accounts for the Commercial Port should be submitted within nine months of the balance sheet date, but that this has not been officially communicated to the Council yet. This would mean the 2012/13, 2013/14 and 2014/15 accounts will need to be prepared and audited to meet this statutory duty. We have been appointed auditors and will prepare separate audit plans for these audits when the accounts are available for audit.

Financial statements audit – application of materiality

Our application of materiality

- When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	
Planning Materiality and Tolerable error	We determined planning materiality to be £11.5 million (2014: £11.8 million), which is 2% of gross expenditure reported in the accounts of £534.5 million adjusted for certain items within other operating expenditure and financing and investment expenditure. We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council. We set a tolerable error for the audit. Tolerable error is the application of planning materiality at the individual account or balance level. It is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds planning materiality. The level of tolerable error drives the extent of detailed audit testing required to support our opinion. We have set tolerable error at the upper level of the available range because there were no corrected significant errors in the Council's 2013/2014 financial statements and no uncorrected errors.
Reporting Threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.6 million (2014: £0.6 million)

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

Financial statements audit – internal control, written representations and whole of government accounts

Internal control

- It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.
- We have tested the controls of the Council only to the extent necessary for us to complete our audit. We are not expressing an opinion on the overall effectiveness of internal control.
- We have reviewed the Annual Governance Statement and can confirm that:
  - It complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
  - It is consistent with other information that we are aware of from our audit of the financial statements.
- We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements of which you are not aware.
- However, we noted a number of issues associated with reconciliations between the general ledger and sub-ledgers. Reconciliations are not done between SWIFT and the General Ledger throughout the year and should be done monthly. Also our review of the Accountants Receivable reconciliation identified an unreconciled difference that was not being investigated and cleared on a monthly basis.

Request for written representations

- We have requested a management representation letter to gain management's confirmation in relation to a number of matters.

Whole of Government Accounts

- Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the National Audit Office.
- We are currently concluding our work in this area and will report any matters that arise to the Audit Committee.

Section 5

Arrangements to secure economy, efficiency and effectiveness

Arrangements to secure economy, efficiency and effectiveness

The Code of Audit Practice (2010) sets out our responsibility to satisfy ourselves that Portsmouth City Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. In examining the Council's corporate performance management and financial management arrangements, we have regard to the following criteria and focus specified by the Audit Commission.

Criteria 1 – arrangements for securing financial resilience

- 'Whether the Authority has robust systems and processes to manage financial risks and opportunities effectively, and to secure a stable financial position that enables it to continue to operate for the foreseeable future'
- We did not identify any significant risks in relation to this criteria in our Audit Plan but did identify a risk around the Council's longer term financial strategy in light of reducing government funding and increasing demand for services.
- As financial pressures in the public sector continue to mount, there is increased focus on the financial resilience of Local Government. Portsmouth City Council has a good track record of managing its finances, and our previous reviews have highlighted no concerns in this area. However, the Chancellor has asked DCLG to come up with savings plans of 25% and 40% of their budget in his spending review and we decided that we should highlight this area as a significant risk, explain the work we have undertaken and report our current conclusions to you.
- We focused on:
  - monitoring action taken in 2014/15 to address any forecast overspending;
  - reviewing the assumptions used in setting the 2015/16 budget and driving the savings requirements in future years, and assessing their reasonableness;
  - monitoring progress in the development of corporate transformation workstreams, co-ordination of planning across services and the identification of savings needed in service budgets

Criteria 2 – arrangements for securing economy, efficiency and effectiveness

- 'Whether the Authority is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity'
- We did not identify any significant risks in relation to this criteria but we set out in our plan that we would follow-up progress in two areas that we looked at in our 2013/14 VFM work but were still on-going at the time of our reporting
  - Adult Social Care performance management arrangements, and
  - Better Care Fund planning and delivery
- We set out in our plan that we would:
  - discuss the Council's progress in addressing these issues with officers;
  - review Council, committee and meeting papers and minutes; and
  - assess the adequacy of supporting evidence as appropriate.

Our findings are set out in the following slides.

Our work did not identify any other matters relating to aspects of your corporate performance and financial management framework which are not covered by the scope of the two specified criteria above.

Addressing audit risks – significant VFM risks

VFM risk identified within our Audit Plan
Longer –term financial strategy

Monitoring action taken in 2014/15 to address any forecast overspending

- In 2014/15 the principal overspending service was again Children's Social Care because, despite investment in additional posts, it has not proved possible to reduce the numbers of Looked After Children (LAC) as planned, against a backdrop of increasing demand. The Council has analysed its costs and performance against others and instigated remedial plans and close financial monitoring, but the service is still forecasting overspends in 2015/16. As the Council continues to deliver savings year on year, it will become increasingly sensitive to fluctuations in demand for statutory services. The cost of LAC has been the root cause of overspending in the portfolio since at least 2010/11, and so the Council needs to reconsider how it deals with such instances in the future. Ensuring issues are identified early and that remedial actions are implemented responsively is part of the solution but, where this cannot deliver a balanced budget, the Council will also need to consider providing additional corporate support to help services identify transformational opportunities that will enable them to deliver the savings needed while avoiding unnecessary performance management of an intractable issue. The continued use of demand, cost and quality benchmarking will be important to target management efforts.

Reviewing the assumptions used in setting the 2015/16 budget and driving the savings requirements in future years, and assessing their reasonableness

- The 2015/16 budget setting process was robust and involved sensible assumptions about changes in funding and expenditure over the medium-term. It was however the most difficult in recent years for the Council, as there are no easy solutions left and little scope to continue protecting front-line services in the wake of delivering £75m of savings since 2010/11. The Council succeeded in identifying the £13.1m of savings required and managed to protect Children's Services, but other front-line services are having to take increasingly difficult decisions about what they can cease delivering to reduce costs. The budget gap for 2016/17 to 2018/19 will require at least another £31m of savings to be identified, as the Council's share of the larger than budgeted 2014/15 deficit on the Collection Fund will need to be reflected in the medium-term savings requirement.

Monitoring progress in the development of corporate transformation workstreams, co-ordination of planning across services and the identification of savings needed in service budgets

- We reported last year that the Council needed to give proper attention to the longer-term issues and challenges it faces and approach these in a planned and strategic manner using benchmarking . The difficulty in doing this is compounded by an annual local election cycle that essentially drives a short-term planning horizon; capacity restraints that limit the investment in, and pace of, transformation plans; new legislative burdens on Councils, and the need to work with partners to integrate health and social care. While the Council is taking action to become more commercial in the way it is run, we have concerns that the current plans and available management capacity will not be sufficient to enable the identification and delivery of savings/efficiencies to the scale required, in the time available.

Addressing audit risks – significant VFM risks

VFM risk identified within our Audit Plan
Longer –term financial strategy (continued)
The Council has recently piloted the use of the Systems Thinking approach and has decided to apply this methodology across all services. Interventions will be led by the Systems Development Service, which is a small team of people from across the Council who have previous experience of the principles and approach. It will operate as an internal consultancy, working with services to run interventions, and, in doing so, build wider knowledge of the approach so it can become a part of business-as-usual. Following an initial assessment phase, the initial interventions are planned in Revenues & Benefits and Finance, and then in the operation of the integrated locality teams. These first interventions are focused on process-driven aspects of the Council's business, where the methodology has more of a proven track-record, rather than on the people-centred services where the bulk of the Council's expenditure is. Proof of concept in this area will be critical in securing officer buy-in to the approach. To this effect, the Council has separately commissioned Vanguard Consulting to review the Adult Social Care assessment process. However, in light of the elapsed time from intervention to delivery of financial savings, the Council should consider how this programme of work could be further accelerated and holistic benefits realised. The Council has ambitious plans to improve contract management by introducing practices from the private sector. Following successful reviews of certain key contracts, it has used the learning to set up a small central team who have commissioned training for key staff to build wider skills. They have procured bespoke software to enable better analysis and aggregation of spend across the Council, to highlight contracts coming up for re-procurement and improve oversight. Officers are in the process of populating this and cleansing the data. They have separately identified the strategic contracts that account for the majority of lifetime spend, and are analysing them against best practice to target a series of reviews on those assessed as highest risk. Again the team will operate on an internal consultancy basis and work with officers in services, but only has a limited capacity. Again, the Council should consider how this process could be accelerated to drive out the potential savings at the pace needed. Officers are also working with partners to maximise the use of the pooled estate and release surplus properties, and to share back office services, which will both grow income and spread the existing support services overhead. Further consideration should be given to other shared services opportunities. In recent years the Council has taken advantage of the non-recurrent Council Tax freeze grant. This means the local council tax base has stood still against decreasing central government revenue funding and on-going cost and demand pressures on services. Unless the Council can accelerate the pace of change above, or introduce additional strategic initiatives, it will need to consider how it can increase income further as it will not be sustainable to draw on available reserves. There is limited headroom in the general fund, the MTRS is largely committed, the PFI reserve is already underfunded, and other earmarked funds are generally prudent and held for particular expected eventualities. While there is some flexibility available in certain areas should policy be changed, these offer limited protection over the medium term.

Addressing audit risks – significant VFM risks

VFM risk identified within our Audit Plan
Follow-up of 2013/14 VFM work - Adult Social Care
Adult Social Care is the Council's second highest spending portfolio representing just over 1/3 of the Council's net cost of services. However, Public Sector Audit Appointments' VFM profiles show the Council's spend on adult social care per adult is in the lowest 20% when compared to its statistical nearest neighbours. While it has been protected to some degree from its proportionate share of the savings targets in recent years, it was asked to deliver portfolio savings of £2.9m in 2014/15, which it achieved only by use of portfolio reserves. This meant it went into 2015/16 with an underlying deficit and further savings to identify. At Q1 they are forecasting a £2.9m overspend, £2.4m of which represents an underlying deficit. Adult Social Care needs to identify a further £10m of savings in the three years to 2018/19. This needs to be done against a background of increasing demand, additional legislative burdens, the introduction of the minimum living wage and a 37% vacancy rate that is already impacting on waiting lists. As the majority of expenditure is on packages of care, this is therefore likely to involve cuts in the level of care that can be provided and additional pressure on staff in post. In light of this, effective performance management arrangements that will provide early intelligence about trajectory to business plan targets and against national indicators will be critical. In 2013/14 we concluded that Adult Social Care performance management arrangements were still developing. A new business information tool was being tailored to ensure it met local operational needs and to help track progress against objectives set out in the service's business plan. We also noted that the service did not have a three year business plan and was focussed on addressing an underlying deficit, identifying the savings needed in 2015/16, implementing new legislative requirements and managing increasing demand. Over the last year, the additional local performance indicators have been built into the new business information tool but system stability issues meant its rollout was delayed. It is now considered stable and is currently available to managers, with plans to extend to all staff soon. Work to bring together finance and performance information, which currently has to be done manually, has stalled because of the planned move to System One as part of the integration agenda. System One does not currently have the functionality to align the money to activity, but this is being worked on. Officers have re-joined the ADASS South East group, which allows them to better compare Portsmouth's performance against other councils and to assess progress against business plan objectives. Operational performance monitoring appears to be working effectively with reports going to the management team monthly and corporately quarterly. In conclusion, it is clear progress has been made in the year with performance management in the service but plans to produce a fully integrated approach will not be completed because of the planned move to TPP System One.

Addressing audit risks – significant VFM risks

VFM risk identified within our Audit Plan
Follow-up of 2013/14 VFM work – Better Care Fund
We reported last year that the Better Care Fund implementation had been slower than initially expected and that further work was needed on the financial and operational implications of planned changes, alongside the development of a vision for sustainable integrated care services in Portsmouth. In light of the previous slide there is a pressing need to deliver fundamental efficiencies through BCF plans to enable Adult Social Care to operate within its budget constraints. The programme of work is generally progressing in line with planned milestones but there are some important areas that are not: Whilst the plans for establishment of three integrated locality teams are on track for September/October, these are essentially limited to co-location at present and further work is needed on integrating the underlying processes. This is complicated by structural issues with the commissioning and provision of services and the operation of pooled budgets. Clarification is needed of the role of the Integrated Commissioning Unit in commissioning adult social care and further thought needs to be given to the operation of the pooled budget. Once teams are integrated there will need to be alignment of money and accountability, with a single process for operational decision-making. At present Adult Social Care decisions are taken by a different route to NHS ones and respective contributions to the pool remain badged as either health or social care, and expenditure is separately accounted for. Urgent consideration is needed of increased financial delegation and de-badging, so that funds can be spent via a single integrated approach. Other key workstreams that are behind schedule are Need and Demand Profiling and Risk Stratification, Care Homes, and Prevention. The first is about understanding the holistic care needs of the population and how they are expected to change over time, which is clearly important to understand in redesigning the care system. This work was anticipated to have been concluded in 14/15 but is still on-going due to difficulties in aligning health and social care data. The second is about improving the quality and range of work in care homes to enable better preventative work by upskilling care home staff. At present this is only just starting and at the investigation stage, but with full mobilisation due to start in April 2016 for completion by March 2017 work needs to be accelerated. Finally prevention is the critical enabler for a system that will be unable to deliver the care needs for a changing population in the historic way. Tackling the primary causes of long-term conditions and earlier intervention to prevent avoidable deterioration are critical in managing the future demand for care. The launch of the Well-being service in October is the first key milestone but the principles need to be built into the operational practices of locality teams and into future commissioning decisions The Council will wish to ensure appropriate focus is given to ensuring these critical workstreams are accelerated.

Section 6

Independence and audit fees

Independence and audit fees

Independence

- We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated 18 February 2015.
- We have already separately notified the Governance Audit and Standards Committee that the 2014/15 audit year is the sixth year that Kate Handy has led the audit of Portsmouth City Council. We assessed this relationship prior to the commencement of the audit period and concluded that there are no considerations that compromise, or could be perceived to compromise, Kate's independence or objectivity. The Audit Commission has approved this continued appointment
- We complied with the Auditing Practices Board's Ethical Standards for Auditors and the requirements of the Audit Commission's Code and Standing Guidance. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.
- We confirm that we are not aware of any relationships that may affect the independence and objectivity of the firm that we are required by auditing and ethical standards to report to you.
- We consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the Governance Audit and Standards Committee on 25 September 2015.
- We confirm that we have met the reporting requirements to the Governance Audit and Standards Committee , as 'those charged with governance' under International Standards on Auditing (UK and Ireland) 260 – Communication with those charged with governance. Our communication plan to meet these requirements were set out in our Audit Plan of 18 February 2015.

Audit fees

- The table below sets out the scale fee and our final proposed audit fees.

	Proposed final fee 2014/2015	Scale fee 2014/2015	Variation comments
	£	£	
Audit Fee: Code work	201,014	199,250	Time spent dealing with elector correspondence
Certification of claims and returns	20,060	20,060	
Non-Audit work	0	0	

- Our actual fee has slightly increased (£1,764) because of time spent considering issues raised by electors and responding to them, but is otherwise is in line with the agreed fee at this point in time - subject to the satisfactory clearance of the outstanding audit work and dependent on not receiving any objections to the accounts.
- In our audit plan we indicated that the fee for the certification of claims and returns would be £24,460 as we had understood that the certification of TRA11 *Local transport Plan – Major Projects* claims would be included within the Audit Commission grant regime. It is no longer.
- We confirm that we have not undertaken any non-audit work outside of the Audit Commission's Audit Code requirements.

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ED None

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