

Annual Audit Letter

London Borough of Tower Hamlets

Audit 2008/09

December 2009



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Status of our reports

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

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

This report summarises the findings from my 2008/09 audit. It includes messages arising from the audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.

Audit opinion

- 1 I gave an unqualified opinion on the Council's financial statements and Pension Fund on 30 September 2009. I also issued a certificate closing the audit on this date.
 - 2 I issued an unqualified opinion on the Council's Whole of Government Accounts submission to Communities and Local Government on 26 October 2009.
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Financial statements

- 3 The accounts were submitted for audit in accordance with the statutory timetable and were supported by adequate working papers. The accounts were complete but contained two material errors which were subsequently corrected. I reported the significant findings from my audit of the financial statements to the Audit Committee on 29 September 2009.
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Value for money

- 4 I issued an unqualified conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in the use of resources on 30 September 2009.
 - 5 I also assessed how well the Authority uses its resources in line with the new methodology developed by the Audit Commission. I concluded that the Authority demonstrated sound performance in managing its use of resources.
 - 6 The Council has adequate arrangements across all nine areas assessed and these are delivering good outcomes in five key areas:
 - financial planning;
 - understanding costs and achieving efficiencies;
 - commissioning and procurement;
 - data quality and the use of information; and
 - risk management and internal control.
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Audit fees

- 7 To meet my responsibilities under the Audit Commission Act, I had to undertake extra work which was not included in my audit plan. To meet the cost of this I increased my audit fee by £12,500.

Actions

- 8 Recommendations are shown within the body of this report and have been agreed with officers. The Council should monitor progress against the action plan in Appendix 2.

Independence

- 9 I can confirm that the audit has been carried out in accordance with the Audit Commission's policies on integrity, objectivity and independence.

Financial statements and annual governance statement

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

Significant issues arising from the audit

- 10** My audit identified two material misstatements in the draft financial statements, which were corrected by management.
- Following a verification exercise of its fixed asset database, the Council identified £120m of fixed assets that were incorrectly included in its balance sheet. The majority of this balance, £100m, related to voluntary aided schools. In the draft financial statements, these assets were removed in year via an entry for losses on disposal of fixed assets in the Income and Expenditure Account. Because the value of the assets removed was fundamental to the value of the Council's opening balance sheet, this should have been disclosed as a prior period adjustment.
 - £24.4m of long term debt in relation to deferred consideration for PFI had been incorrectly classified as a short-term debtor.
- 11** My audit also identified three non-trivial errors which I reported to the Audit Committee. All of the errors were corrected by management and none had an impact on the Council's available resources.
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Material weaknesses in internal control

- 12** I have not identified any weakness in the design or operation of an internal control that might result in a material error in your financial statements of which you are not aware. However, I found the following weaknesses in the operation of controls.
- My testing of a total sample of 40 journals found that in five cases, no evidence could be provided of appropriate authorisation.
 - My documentation of the payroll system found that there were no systematic checks in place to ensure that leavers are removed from the payroll correctly.
 - The Council has an internal target of issuing invoices within five days of receiving an invoice request. My testing of a sample of 20 invoices found that in five cases, this target was not met (in two of these cases, the invoices were not issued within 14 working days).

Accounting practice and financial reporting

- 13 I considered the qualitative aspects of your financial reporting. The Council has undertaken reviews of key aspects of its accounts and closedown arrangements and this work has led to improvements in the quality of the financial statements. However there remain some important areas where further work is required:
- not all working papers are subject to a robust quality review;
 - I identified un-reconciled items in control account reconciliations which indicates that authorisation controls are weak; and
 - I experienced some delays in receiving requested working papers, which resulted in audit work being completed late in the process.

Whole of government accounts

- 14 The Council is required to submit a Whole of Government Accounts (WGA) consolidation pack to Communities and Local Government (CLG). This is to support the central government objective of producing a set of accounts for the public sector as a whole. The Council is a schedule 1 body which means that its accounts are significant to the consolidation process. As such, it is important that the audited consolidation pack is submitted to CLG by the deadline.
- 15 The deadline for the submission of the audited pack to CLG was 1 October 2009. Due to late work on the accounts and amendments being made at a late stage, I received the un-audited consolidation pack on 25 September 2009. I issued my opinion on the consolidation pack on 26 October 2009.

International Financial Reporting Standards

- 16 The introduction of International Financial Reporting Standards (IFRS) into the public sector raises significant challenges for local government. Authorities must ensure arrangements are in place if they are to publish timely and accurate IFRS compliant accounts in 2010/11.
- 17 Our experience in other sectors has shown that despite a long lead-in time, it is important for organisations to have robust well managed plans to make the necessary adaptations.
- 18 The Council is making progress in the move to IFRS, however the work still has a limited profile and there is a risk that not all work will be completed on time.

Recommendations	
R1	Strengthen internal quality control procedures to facilitate a more efficient closedown and audit process.
R2	Raise the profile of the IFRS transition exercise and closely monitor the progress of the project against key milestones, taking remedial action where necessary.

Value for money and use of resources

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

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

Use of resources judgements

- 19 In forming my scored use of resources judgements, I have used the methodology set out in the [use of resources framework](#). Judgements have been made for each key line of enquiry (KLOE) using the Audit Commission's current four point scale from 1 to 4, with 4 being the highest. Level 1 represents a failure to meet the minimum requirements at level 2.
- 20 I have also taken into account, where appropriate, findings from previous use of resources assessments (updating these for any changes or improvements) and any other relevant audit work.
- 21 The Council's use of resources theme scores are shown in Table 1 below. The key findings and conclusions for the three themes, and the underlying KLOE, are summarised in Appendix 1.

Table 1 Use of resources theme scores

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

VFM conclusion

- 22 I assessed your arrangements to secure economy, efficiency and effectiveness in your use of resources against criteria specified by the Audit Commission. The three themes of the framework are:
- managing finances;
 - governing the business; and
 - managing resources.

- 23 From 2008/09, the Audit Commission will specify each year, which of the use of resources KLOE are the relevant criteria for the VFM conclusion at each type of audited body. My conclusions on each of the areas are set out in Appendix 1.
- 24 I issued an unqualified conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources.

Managing finances

- 25 The Council has demonstrated good outcomes from its financial planning and its understanding of costs. For example, the Council's Service and Resource Planning Process fully integrates service and financial planning and achieve robust financial plans. In addition, the Council continually challenges service delivery and efficiency savings of £6.2m were achieved in 2008/09.
- 26 PWC were commissioned by the Council to undertake a review of the Council's central finance function to ensure that it will support the Council in moving to World Class Financial Management. Improvements are being made as a result of the review, however work is at an early stage and has not yet delivered the expected outcomes.
- 27 In light of recent turbulence in the financial markets and national pressures on funding, the Council should continue to keep its finances under review. In particular, it should ensure that the level of available reserves is commensurate with the risks it faces.

Governing the business

- 28 The Council has a clear vision for procurement to deliver better and sustainable outcomes. Effective joint working has translated this vision into tangible value for money improvements. The Council has a clear approach to commissioning and staff and service users are involved in service design.
- 29 Data quality and the use of information is managed well by the Council. My work on the Council's accounts, financial systems, grants claims and housing benefits has not identified concerns regarding data quality. There is an integrated approach to performance information to inform strategic, partnership and operational planning. Performance against priorities is monitored well.
- 30 The Council has an embedded ethical framework and generally constructive Member/Officer relations. It is accepted that the departure of the previous Chief Executive could have been handled better.
- 31 Risk management and internal control is sound. Risk management is linked to strategic priorities and is used to secure improvements in all services including those delivered through partnerships. The Council's effective internal audit function delivers against its plan and satisfies CIPFA standards. Zero tolerance is demonstrated for fraud and there is an embedded anti-fraud culture.

Managing resources

- 32 In the past the Council did not consider its use of natural resources a priority. However, during 2008/09 the agenda has moved forward significantly. While there have been some 'quick wins', there is not yet sustained and improved performance in how the Council reduces its own environmental impact.

Value for money and use of resources

- 33** In previous years' assessments, asset management had been identified as only meeting minimum requirements. In 2008/09, the Council appointed a new Head of Corporate Property and improved resource allocation to the department. An improvement agenda has been driven forward but many of the benefits will not be realised until 2009/10 and beyond.

Recommendation

- R3** Continue to closely monitor the Council's financial position to ensure the Council retains a robust level of reserves commensurate with the risks it faces.

National Fraud Initiative

- 34** The Audit Commission's National Fraud Initiative (NFI) matches data across different organisations and identifies matches of data which could indicate fraudulent activity. The Authority has sound arrangements for responding to the results of the NFI project and has made good progress investigating the matches.

Your business at risk

- 35** IT security is a high profile issue in the public sector after a number of well publicised cases of poor management of electronic information. I undertook a survey of a sample of the Authority's staff to assess the strength of its IT security. The overall perception of most staff is that IT security at the London Borough of Tower Hamlets is adequate or better than adequate but staff are less clear about the precise role that they have to play in it.
- 36** Regular reminders to staff about all of the issues covered in our survey will be of benefit to the Council. The survey indicates that there are a number of key areas where the Council particularly needs to raise staff awareness.

Recommendation

- R4** Monitor the implementation of the recommendations in my Use of Resources report and in my Your Business at Risk report .

Closing remarks

- 37** I have discussed and agreed this letter with the Chief Executive and the Director of Finance. I will present this letter at the Audit Committee on 30 March 2010 and will provide copies to all committee members.
- 38** Further detailed findings, conclusions and recommendations in the areas covered by our audit are included in the reports issued to the Council during the year.

Table 2

Report	Date issued
Audit plan	June 2008
Supplementary opinion plan letter	February 2009
Your business at risk	August 2009
Annual governance report	September 2009
Use of resources report	December 2009

- 39** The Council has taken a positive and constructive approach to our audit. I wish to thank the Council staff for their support and co-operation during the audit.

Jon Hayes
 District Auditor
 December 2009

Appendix 1 – Use of resources key findings and conclusions

The following tables summarise the key findings and conclusions for each of the three Use of Resources themes.

Managing finances

Theme score	3
KLOE 1.1 (financial planning)	3
<p>The Council fully integrates service and financial planning via a Service and Resource Planning (SARP) process. This is informed by a stock take of financial, human and capital asset use and related performance indicators. The corporate challenge process includes Members and enables resources to be targeted to priority areas to improve performance. SARP also achieves the following outcomes:</p> <ul style="list-style-type: none"> • efficient and timely approval of the annual budget; • a stable planning framework to take informed decisions over the medium-to-long term; • corporate efficiency gains; • a corporate ownership of service; and • robust financial planning. <p>The 2009/10 statutory budget consultation, in which Members played a lead role, identified concerns about the impact of the credit crunch. Further engagement takes place through the participatory budgeting process, for which the Council has been invited by Government to act as a South East learning hub. Community events were held at Local Area Partnership level. The turnout at the events has been high and feedback is very positive.</p>	

Appendix 1 – Use of resources key findings and conclusions

KLOE 1.2 (understanding costs and achieving efficiencies)	3
<p>The Council continually challenges efficiency and service delivery and efficiency savings of £6.2m were achieved in 2008/09. The Council routinely challenges its costs and performance and demonstrates a sound understanding of their relationship. Benchmarking is an embedded process and helps prioritise areas for review. A major improvement project has been set up to re-engineer 'back-office' functions such as HR and IT.</p>	
KLOE 1.3 (financial reporting)	2
<p>The Council engaged PWC to undertake a review of its central finance function to ensure that it is fit for purpose and will support the Council in moving towards World Class Financial Management. While the review found no underlying system weaknesses, it did find that budget-holders rely heavily on directorate based finance officers to support budget-monitoring, because the general ledger is not user-friendly. This causes inefficiencies because finance officers spend a high proportion of their time on administrative activities. The review also found scope to increase the profile of Finance within the Council and to adopt a more 'business partnering' approach. The Council is taking this forward in 2009/10 and will be creating a dedicated financial reporting section and making improvements to the reporting tools on the ledger.</p> <p>The Council is making progress on preparing for implementation of IFRS. The draft 2008/09 accounts were presented on time, although there was slippage against the internal timetable, which impacted on internal quality checks. The draft accounts were approved by the Audit Committee, although the level of challenge was inhibited by the fact that a time limit was imposed on the meeting.</p>	

Governing the business

Theme score	3
KLOE 2.1 (commissioning and procurement)	3
<p>The Council has a clear vision for procurement to deliver better and sustainable outcomes. Effective joint working has translated this vision into tangible value for money improvements. The Council has a clear approach to commissioning and staff and service users are involved in service design.</p> <p>The Council works well with suppliers to further develop its understanding of the supply market. There is proactive ongoing evaluation of procurement options, including sustainability. The Competition Board commissions detailed options appraisals and business cases and drives cashable procurement savings. A systematic approach is in place to review service competitiveness. There is an emphasis on achieving efficiencies and savings.</p>	

Appendix 1 – Use of resources key findings and conclusions

KLOE 2.2 (data quality and use of information)	3
<p>Our spot check of a sample of four performance indicators found that there are effective systems in place for producing robust information. There is a risk-based review mechanism which incorporates internal audit and the corporate performance team. All indicators reviewed were found to be fairly stated demonstrating that these arrangements work in practice. Our work found that data provided by third parties is subject to challenge and internal review. Our work on the Council's accounts, financial systems, grants claims and housing benefits has not identified concerns regarding data quality.</p> <p>There is an integrated approach to performance information to inform strategic, partnership and operational department/service planning. Performance against priorities is monitored well. The SARP process integrates financial and performance planning and draws on benchmarking, satisfaction surveys and trends. Actions from the meetings of the Performance Review Group confirm a sound peer challenge approach. This addresses strategic and priority indicators which are off target in the Performance Digests.</p>	
KLOE 2.3 (good governance)	2
<p>The Council has an embedded ethical framework and generally constructive Member/Officer relations. A shared vision was apparent from interviews. The quality of governance is dependent on member and staff attitudes, behaviours and culture and work to ensure the arrangements continue to produce the right outcomes is in hand.</p>	
KLOE 2.4 (risk management and internal control)	3
<p>The Council has risk champions in every department and members demonstrated good risk awareness. Risk registers are in place at a departmental and corporate level and these link to the Council's priorities. The Council actively uses risk management to secure improvements in all services including those delivered through partnerships. Business continuity plans are in place and these are tested with Partner agencies.</p> <p>The Council has an embedded anti-fraud culture and demonstrates zero tolerance of fraud. The culture is underpinned by relevant codes, policies and strategies. The Council has completed an assessment of its anti-fraud arrangements against the Red Book and is implementing an action plan to address the few areas for improvement. There is also an active network of North East London internal auditors to share good practice on anti-fraud arrangements. A review of the NFI database demonstrates that the Council is proactive in working through the matches from NFI.</p> <p>The Council has an effective internal audit function that delivers against its plan on a timely basis and satisfies CIPFA standards. The Council's Audit Committee provides an effective contribution to the control environment. It is objective and asks challenging questions. The reports presented to the Committee allow it to discharge its role effectively. The Council's Annual Governance Statement is a concise and honest self-assessment of its arrangements and Members demonstrated ownership of the Statement.</p>	

Managing resources

Theme score	2
KLOE 3.1 (use of natural resources)	2
<p>In the past the Council did not consider its use of natural resources a priority. However, during 2008/09 the agenda has moved forward significantly. While there have been some quick wins there is not yet sustained and improved performance in how the Council reduces its own environmental impact.</p> <p>Additional funding of £150,000 has been allocated in 2008/09 to quantify the Council's use of natural resources and then develop plans to reduce the impact of its activities on the environment. Performance management of the green agenda has improved during 2008/09 by increased emphasis on data collection. Recycling and waste management, which had been an area of long-standing poor performance, is showing the benefits of additional investment and increased partnership working with the ALMO and Registered Social Landlords.</p> <p>Sustainability issues are starting to be mainstreamed, both in internal and external plans. Team planning events should now incorporate sustainability issues. The Council is establishing systems and processes to manage its own use of natural resources.</p>	
KLOE 3.2 (strategic asset management)	2
<p>In previous years' assessments, asset management had been identified as only meeting minimum requirements. In 2008/09, the Council appointed a new Head of Corporate Property and improved resource allocation to the department. An improvement agenda has been driven forward recently, although many of the benefits will not be realised until 2000/10 and beyond.</p> <p>The Council has a designated property department and Head of Service. Assets are now considered as 'corporate' rather than 'service' assets, replacing the fragmented approach that existed previously. This permits flexibility in asset use and helps identify estate rationalisation opportunities, leading to a more rigorous and unified approach to determining when assets are surplus to requirements. The quality of housing stock remains a key issue and the Council is not expected to reach the Decent Homes Standard by the target date, although the Council has been successful in recently securing funding to improve its stock.</p>	

Appendix 2 – Action plan

Page no.	Recommendation	Priority 1 = Low 2 = Med 3 = High	Responsibility	Agreed	Comments	Date
6	R1 Strengthen internal quality control procedures to facilitate a more efficient closedown and audit process.	3	Head of Corporate Finance	Yes	Work is in hand to achieve this for 2009/10.	30 September 2010
6	R2 Raise the profile of the IFRS transition exercise and closely monitor the progress of the project against key milestones, taking remedial action where necessary.	3	Head of Corporate Finance	Yes	The project team is being strengthened.	31 March 2010
9	R3 Continue to closely monitor the Council's financial position to ensure the Council retains a robust level of reserves commensurate with the risks it faces.	2	Director of Resources	Yes	This will be address as part of the budgeting process for 2009/10.	31 March 2010
9	R4 Monitor the implement of the recommendations in my Use of Resources report and in my Your Business at Risk report .	2	Director of Resources	Yes	This is being done.	30 September 2010

The Audit Commission

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

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

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

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