

Annual Audit and Inspection Letter

January 2006



Annual Audit and Inspection Letter

Royal Borough of Kingston Upon Thames

Audit 2004-2005

External audit is an essential element in the process of accountability for public money and makes an important contribution to the stewardship of public resources and the corporate governance of public services.

Audit in the public sector is underpinned by three fundamental principles:

- auditors are appointed independently from the bodies being audited;
- the scope of auditors' work is extended to cover not only the audit of financial statements but also value for money and the conduct of public business; and
- auditors may report aspects of their work widely to the public and other key stakeholders.

The duties and powers of auditors appointed by the Audit Commission are set out in the Audit Commission Act 1998 and the Local Government Act 1999 and the Commission's statutory Code of Audit Practice. Under the Code of Audit Practice, appointed auditors are also required to comply with the current professional standards issued by the independent Auditing Practices Board.

Appointed auditors act quite separately from the Commission and in meeting their statutory responsibilities are required to exercise their professional judgement independently of both the Commission and the audited body.

Status of our reports to the Council

Our reports are prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission. Reports are prepared by appointed auditors and addressed to members or officers. They are prepared for the sole use of the audited body, and no responsibility is taken by auditors to any member or officer in their individual capacity, or to any third party.

Copies of this report

If you require further copies of this report, or a copy in large print, in Braille, on tape, or in a language other than English, please call 0845 056 0566.

© Audit Commission 2006

For further information on the work of the Commission please contact:

Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ

Tel: 020 7828 1212 Fax: 020 7976 6187 Textphone (minicom): 020 7630 0421

www.audit-commission.gov.uk

Contents

Key messages	5
Council performance	5
Accounts and governance	5
Action needed by the Council	5
Performance	6
CPA scorecard	6
Direction of travel report	8
Best value performance plan and performance information	9
Working with other inspectorates and regulators	10
Accounts and governance	11
Use of resources judgements	11
Audit of 2004/05 accounts	13
Matters arising from the final accounts audit	13
Report to those with responsibility for governance in the Council	13
Financial standing	13
Systems of internal financial control	15
Standards of financial conduct and the prevention and detection of fraud and corruption	17
National Fraud Initiative	17
Legality of transactions	17
Kingston Theatre	17
Grant claims	18
Looking forward	20
Future audit and inspection work	20
Revision to the Code of Audit Practice	20
Closing remarks	21
Availability of this Letter	21
Appendix 1 – Background to this Letter	22
The purpose of this Letter	22
Audit objectives	22

Appendix 2 – Audit reports issued	24
Appendix 3 – Audit fee	25
Inspection fee update	25

Key messages

Council performance

- 1 The Council's overall CPA category is three stars (the range is zero stars to four stars) and the direction of travel judgement is 'improving well'. The Council provides generally high-quality services at relatively low cost. It actively pursues efficiency savings and has a good track record of redirecting resources saved in this way.

Accounts and governance

- 2 The Council's financial position is sound. In previous Letters, we have commented on the low level of reserves. However, at 31 March 2005 the Council has built up the general fund reserve balance to £4 million and met the target set by the Council.
- 3 We gave an unqualified opinion on the 2004/05 accounts on 31 October 2005.

Action needed by the Council

- 4 The Council's challenge is to continue to improve services from a strong base and to focus efforts on areas of underperformance.

Performance

The Council's overall CPA category is three stars (the range is zero to four stars) and the direction of travel judgement is 'improving well'. The Council provides generally high-quality services at relatively low cost. It actively pursues efficiency savings and has a good track record of redirecting resources saved in this way.

CPA scorecard

- 5 The Audit Commission published its Comprehensive Performance Assessments of all single and upper tier councils on 15 December 2005. Each council's 'scorecard' and more background on Comprehensive Performance Assessment (CPA) can be found on the website: www.audit-commission.gov.uk.
- 6 The CPA 'score' is based on service performance (including a new use of resources) and corporate assessment but there is a new methodology, based on the Audit Commission's publication '*CPA - the harder test*'. As the title implies, CPA is now a more stringent test with more emphasis on outcomes for local people and value for money. The summary categories have changed and a star rating introduced. There is also a more comprehensive assessment of the Council's use of resources. This examines the Council's arrangements for financial reporting, financial management, financial standing, internal control and (new for this year) value for money.
- 7 The Audit Commission has also introduced new scoring categories of 'direction of travel' to reflect the extent to which councils are improving services. The Council's CPA scorecard is set out in Table 1 below.

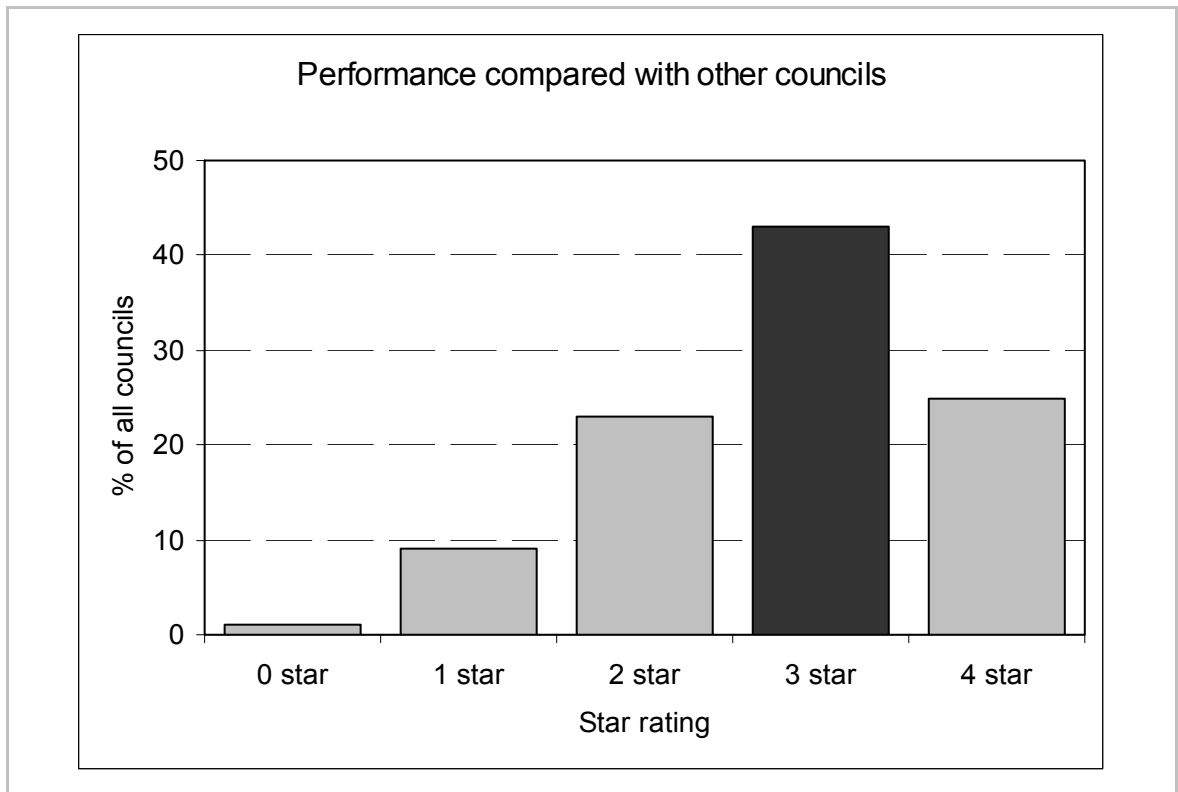
Table 1 CPA scorecard

Element	Assessment
Direction of travel judgement	3
Overall	3 stars
Current performance	
Children and young people	4
Social care (adults)	3
Use of resources	3
Housing	3
Environment	2
Culture	3
Benefits	3
Corporate assessment/capacity to improve (not reassessed in 2005)	3

(Note: 1=lowest, 4=highest)

- 8 Figure 1 shows how the Council's three-star rating compares with other councils in England.

Figure 1 CPA 2005 star ratings



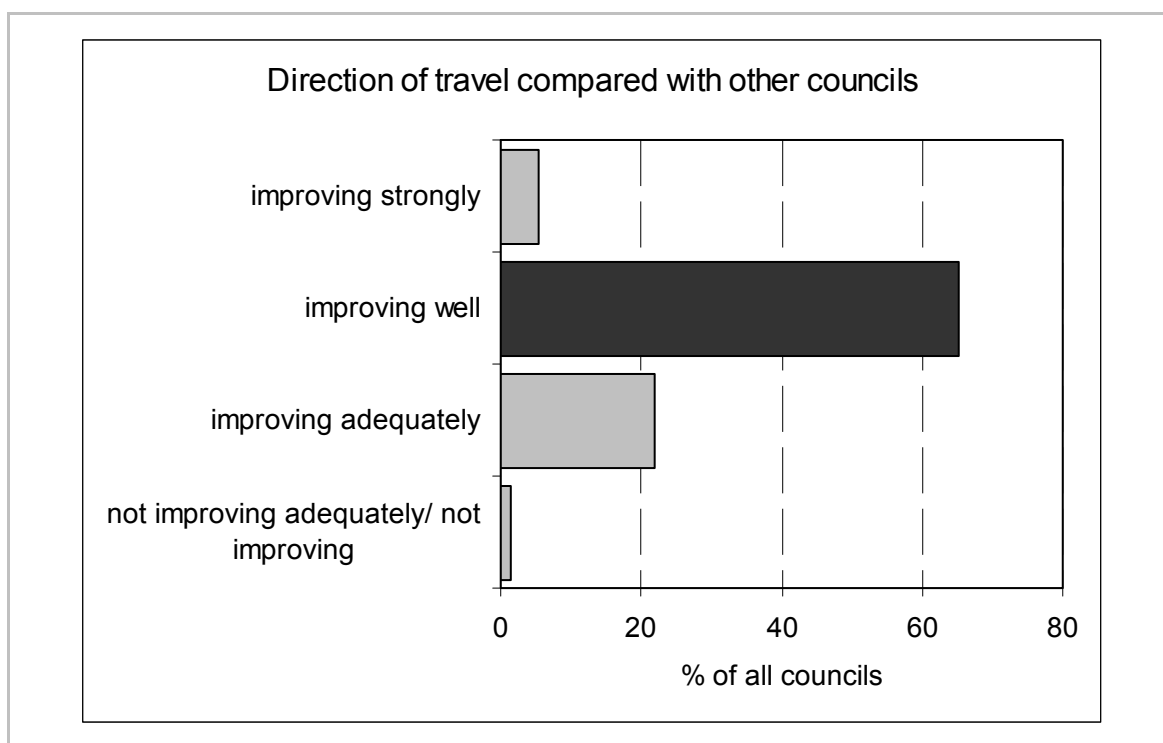
Source: Audit Commission

Direction of travel report

- 9 We carried out an assessment of the Council's progress in improving services in October 2005. Our assessment was that the Council is improving well and we have given the Council a direction of travel score of 3 out of 4. The direction of travel report, which has now been published on the Audit Commission website, is set out below.

'The Council is maintaining high performance levels in social care and educational attainment is improving from a strong base. There is better access to services for people with disabilities through improvements to Council buildings. Waste management and road conditions have improved in response to public concern. Wider community achievements include reductions in crime and the creation of the first Business Improvement District in the country. Services that remain a challenge for the Council include recycling. Satisfaction levels have improved in weaker service areas but remain low in cultural services. Partnership working and long-term contractual relationships are resulting in improved value for money such as the joint procurement of school improvement services. The independent Improvement and Development Agency peer review highlighted a commitment to achieving excellence and improvement across the Council. Improvements in scrutiny are being addressed through its constitutional review. Progress against plans is managed through the Policy and Improvement Programmes and an embedded performance management framework. The Council has a clear corporate commitment, good capacity and overall strong governance arrangements to sustain future improvement.'

- 10 Figure 2 shows how the Council's 'improving well' assessment compares with other councils in England.

Figure 2 2005 Direction of travel ratings

Source: Audit Commission

Best value performance plan and performance information

- 11 The Council's best value performance plan (BVPP) is a well-presented document and complies with statutory requirements. We issued an unqualified opinion on the Council's BVPP on 19 December 2005.
- 12 We completed our review of the Council's best value performance indicators (BVPIs) on 5 September 2005, the deadline set by the Audit Commission. Our review focused on high risk BVPIs and included Audit Commission selected indicators that are used in assessing the Council's CPA rating.
- 13 This year, we made amendments to five indicators. This is a significant decrease compared to the previous year when we made amendments to 17 indicators.
- 14 The Audit Commission selected 12 core indicators to form part of the Council's CPA assessment, not all of these were required to be shown in the BVPP. We reported a reservation on one indicator, relating to library stock turnover.

Working with other inspectorates and regulators

- 15 To ensure that councils receive a tailored seamless service, integrated with the work of other inspectorates, the Audit Commission has appointed a Relationship Manager for each council. The Council's Relationship Manager is Derek Elliott who is also the Council's District Auditor. An important aspect of the role of the Relationship Manager is to work with other inspectorates and regulators who also review and report on the Council's performance. These include:
- Ofsted;
 - Commission for Social Care Inspection (CSCI);
 - Benefits Fraud Inspectorate (BFI);
 - DfES; and
 - Local Government Office contact.
- 16 We share information and seek to provide 'joined up' regulation to the Council. There were no service inspections by either the Audit Commission or the above regulators during 2005.

Accounts and governance

The Council's financial position is sound. In previous letters we have commented on the low level of reserves. However, at 31 March 2005 the Council has built up the general fund reserve balance to £4 million and has met the target set by the Council.

We gave an unqualified opinion on the 2004/05 accounts on 31 October 2005.

- 17 We carried out a use of resources assessment for the first time this year. The assessment focuses on financial management and links to the strategic management and governance of the Council. It looks at how financial management is integrated with strategy and corporate management, supports Council priorities and delivers value for money. It will be carried out annually, as part of each council's external audit. For single tier and county councils, the use of resources assessment forms part of the CPA framework.
- 18 We set out below the main findings from our work on use of resources and set out more detailed comments on our work on accounts and governance in separate sections on:
 - audit of the 2004/05 accounts;
 - financial standing;
 - systems of internal financial control;
 - standards of financial conduct and the prevention and detection of fraud and corruption; and
 - legality of transactions.

Use of resources judgements

- 19 We have assessed the Council's arrangements and scored each on a scale of 1 to 4 against descriptors called 'key lines of enquiry'. A score of 2 represents adequate performance and 3 good performance with embedded arrangements. A score of 4 is only given for exceptionally good performance.
- 20 The overall use of resources score for the Council was 3, as shown in Table 2.

Table 2 Use of resources assessment

Use of resources area	Assessment
Financial reporting	2
Financial management	3
Financial standing	3
Internal control	2
Value for money	3
Overall	3

(Note: 1=lowest, 4=highest)

- 21 The scores for the Council show that sound arrangements are in place. The key issues we would like to draw to your attention are set out in Table 3 below.

Table 3 Use of resources key issues

Use of resources area	Key issues
Financial reporting	The Council has sound arrangements for making information available to the public. There are good communication links with the community. Accounts and supporting papers are generally satisfactory. There is some scope for improvement, particularly in support of capital accounting.
Financial management	The Council has a good track record of controlling spending within budgets. There are reliable arrangements for monitoring and reporting performance against budgets. There are adequate arrangements for managing the Council's asset base. The Council should consider preparing a comprehensive asset management plan.
Financial standing	The Council has maintained its spending within the overall budget in the last three years. It has established a target level for the general fund reserve which is being achieved with the general fund balance of £4 million at 31 March 2005.
Internal control	The Council has sound arrangements in place for maintaining its system of internal control. Information about fraud prevention is disseminated to staff on a regular basis. The Council should consider establishing an audit committee in line with CIPFA guidance.

Use of resources area	Key issues
Value for money	Overall the Council is providing good quality services at a relatively low cost. The Council has a strong commitment to improving services and is tackling areas of under-performance.

Audit of 2004/05 accounts

- 22 We gave an unqualified opinion on the Council's accounts on 31 October 2005.

Matters arising from the final accounts audit

- 23 The published accounts are an essential means by which the Council reports its stewardship of the public funds at its disposal and its financial performance in the use of those resources.
- 24 The 2004/05 accounts were approved by members on 19 July 2005. We received the draft accounts and most of the supporting papers at the start of the audit. We received good co-operation from officers during the audit.
- 25 The Council will be required to meet the Government's 'Whole of Government Accounts' target of getting the 2005/06 accounts approved by members by 30 June next year and for the audit to be completed by 30 September. This will be a challenging target. We will work closely with officers to help achieve this target.

Report to those with responsibility for governance in the Council

- 26 We are required by professional standards to consider reporting to those charged with governance certain matters before we give an opinion on the accounts, for the Royal Borough of Kingston this is the full Council.
- 27 We reported to members on 4 October 2005 and noted that a number of issues relating to capital accounting and disclosures in the accounts need to be addressed. We will work closely with officers to help address these issues during 2005/06.

Financial standing

- 28 The Council's financial position is sound. The Council has a good track record of spending within available resources. The balance on the general fund reserve at 31 March 2005 was £4 million and achieves the target level set by the Council.

General fund spending and balances

- 29** Net expenditure on the general fund amounted to £163.8 million for 2004/05. This represents an underspend of £1.2 million. The Council has set a target for general fund reserves of 2 per cent of net expenditure. With the balance at 31 March 2005 of £4 million this target has now been achieved.
- 30** The Council has set a net expenditure budget for 2005/06 of £167.8 million. The Director of Finance's report to the Executive of 15 November 2005 shows that there is a projected overspend of £1.2 million for the year. Action is being taken to maintain expenditure within the budget.

Income collection and arrears

- 31** The Council's income collection rates are above the average for London boroughs, as shown in Table 4 below.

Table 4 Income collection rates

Income	2004/05 target	2004/05 actual	2004/05 outer London average	2004/05 England average
Council tax	96.5%	96.7%	95.1%	96.6%
National non-domestic rates	99.0%	99.7%	98.3%	98.3%
Housing rents	97.8%	98.5%	n/a	n/a

Pension fund

- 32** The Council's pension fund is invested world wide with about 62 per cent in equities and the remainder in fixed interest securities and property. The net assets of the fund increased in 2004/05 to stand at £233 million at 31 March 2005. This increase is largely due to increases in the value of fund investments which reflects the recovery in stock values globally. Fluctuations in the value of world stock markets have a significant effect on the overall value of the fund. Table 5 shows recent movements in the net assets of the fund.

Table 5 Net pension fund assets

Net assets	2004/05 £ million	2003/04 £ million	2002/03 £ million	2001/02 £ million
Start of year	208	164	200	202
Movements	25	44	-36	-2
End of year	233	208	164	200

- 33** Investment performance achieved by the Council's fund managers in 2004/05 was poor compared to the average return for all local authorities. The Council uses WM Performances Services to compare the returns achieved by its fund managers to the 'WM Local Authority Universe' benchmark. The return on investments in 2004/05 for the Council's pension fund amounted to 8.6 per cent, compared to the average for all local authorities of 11.6 per cent. The average return on investments for the Council's pension fund over the three-year period from April 2002 to March 2005 was 2.0 per cent, this is significantly below the average return for all local authorities of 3.5 per cent. The Council has now appointed new fund managers.
- 34** A full triennial actuarial valuation was carried out in 2004 and assessed the pension fund's assets and liabilities accrued in respect of pension benefits as at 31 March 2004. The valuation assessed the pension fund as being 64 per cent funded to meet future liabilities, this is one of the lowest funding levels of councils in England. The funding position had deteriorated since the previous actuarial valuation, at 31 March 2001, which assessed the fund as being 80 per cent funded. The deterioration in the funding position, according to the fund actuary, is largely due to poor returns on fund investments. The Council will increase employer contributions following the actuarial valuation from 20.6 per cent to 24.4 per cent. The increase will be phased over a period of three years from 1 April 2005.

Systems of internal financial control

We have not identified any significant weaknesses in the overall control framework.

Internal Audit

- 35** Our audit is carried out on a managed audit basis whereby we seek to place reliance, as far as possible, on the work of Internal Audit. Our 2004 letter commented that Internal Audit had not carried out reviews of four of the Council's twelve core financial systems. There has been some improvement in 2005 and all core systems have been reviewed. However, some of this work was not completed at the planned date due to slippage. Internal Audit resource planning needs to build in realistic assumptions regarding staff availability to carry out planned audit work.

- 36 We carried out a review of Internal Audit work on the Council's key financial systems. Our review confirmed that the work had been carried out to a satisfactory standard and that their findings and recommendations had been reported on a timely basis. We will continue to work closely with Internal Audit to ensure there is efficient use of audit resources.

Statement on internal control

- 37 As part of the statement of accounts, it is now a requirement for the Leader and Chief Executive to sign a statement on internal control. The areas identified in the 2004/05 statement where improvements can be made are:

- risk management;
- business continuity and disaster recovery planning;
- corporate project management; and
- internal audit coverage.

Action plans are being prepared to address these areas of weakness.

Ethical governance

- 38 There is an increased emphasis on good conduct in public life and on the standards of behaviour of elected members. One of the common aspects of governance failures is not the absence of frameworks, controls and arrangements but the absence of appropriate behaviours and values amongst members and officers. We carried out a review of the Council's arrangements for promoting high standards of ethical governance and issued a report in May 2005.
- 39 Our overall conclusion is that the Council's arrangements for maintaining high standards of ethical behaviour are sound, and comply with legislative requirements. We found the Council to be compliant with legislation, as well as meeting some good practice standards:
- a Standards Committee was established in 1999, three years before the legislative requirement to do so;
 - there is proportionate political representation on the Standards Committee and it is chaired by an independent person;
 - a code of conduct for members has been adopted and all members have received training; and
 - a register of members' interests is maintained which is available for public inspection.

Standards of financial conduct and the prevention and detection of fraud and corruption

- 40 The overall arrangements for maintaining high standards of financial conduct and for the prevention and detection of fraud and corruption are generally satisfactory.

National Fraud Initiative

- 41 In 2004/05, the Council took part in the Audit Commission's National Fraud Initiative (NFI). The NFI is undertaken every two years and aims to help identify and reduce fraud by bringing together data from NHS bodies, local authorities and government departments and other agencies, to detect a wide range of frauds against the public sector. These include housing benefit, occupational pension, tenancy and payroll fraud.
- 42 We carried out a review in March 2005 of the arrangements at the Council to follow up and investigate potential frauds identified by the NFI. Our overall conclusion was that a structured approach is in place to manage, monitor and control the investigation of cases identified by the NFI. Officers are clear about their responsibilities and the approach to be taken to the investigations.
- 43 The Audit Commission collects information from councils on the levels of fraud identified by the NFI. The latest NFI return submitted by the Council, December 2005, shows savings of £205,000 have been identified. These savings relate mainly to fraudulent housing benefit claims.

Legality of transactions

- 44 We have not identified any significant weaknesses in the framework established by the Council for ensuring the legality of its significant financial transactions.
- 45 We made responses to correspondence from local government electors. We have yet to conclude our correspondence with one local government elector. There are no issues arising from our correspondence that we wish to bring to your attention.

Kingston Theatre

- 46 The Council would like a theatre in Kingston which would help develop a more balanced night time economy and has for a number of years been providing support to Kingston Theatre Trust (the Trust) with its plans to build and run a theatre.

- 47 The Council has to date provided funding of £0.85 million to the Trust and an unsecured loan facility of £0.9 million. The cost of fitting out the Theatre is currently estimated at £6.0 million. The Council's Executive members agreed at their meeting on 7 June 2005 a funding plan for providing a fully fitted out theatre. The main elements of the plan are:
- a property company would be set up to which the Council would transfer ownership of the Theatre at a valuation of £2 million;
 - an external investor would take up 51 per cent of the shareholding of the property company for a contribution of £3 million towards the fitting out of the Theatre;
 - a second external investor would take a 4 per cent shareholding in the property company and take up a lease on the studio within the Theatre for which a premium would be payable;
 - the Council would take up the unallocated shares in the property company for £0.5 million and underwrite a further £0.6 million of fitting out costs;
 - the Council would purchase approximately £1.3 million of theatre equipment and lease that equipment back to the Trust at a cost of £10,000 in the first year which would rise to £30,000 per annum by year 5; and
 - the Council would continue to provide an interest free loan facility of up to £0.9 million to the Trust.
- 48 The project, as stated in our previous Letters, is high-risk. The Theatre was scheduled to open in September 2005 but this has not been achieved as sufficient funding for fitting out the Theatre was not available. The Council is currently in the process of finalising funding arrangements with the external investors in the project. The Council must continue to exercise robust scrutiny of all risks and benefits of the project.

Grant claims

- 49 The Audit Commission's aim is to be more strategic in its approach to regulation. In line with this we have taken a more risk-based approach to the certification of grant claims. We have reduced our audit of these claims and the Council's fee but our ability to reduce further depends on the adequacy of the Council's control environment.
- 50 We have now certified most of the claims submitted for audit. A summary of the results of our work on grant claims is set out in Table 6.

Table 6 Grant claims submission and certification

	Yes	No
Claims received on time	13	5
Claims amended by officers following audit work	9	7
Qualification letter issued	5	11

Looking forward

Future audit and inspection work

- 51 We have an agreed plan for 2005/06 and we have reported in this Letter those aspects that have already been completed. The remaining elements of that plan, including our audit of the 2005/06 accounts, will be reported in next year's Letter. Our planned work, together with that of other inspectorates, is included on both the Audit Commission and LSIF (Local Services Inspectorates Forum) websites.
- 52 We have sought to ensure, wherever possible, that our work relates to the improvement priorities of the Council. We will continue with this approach when planning our programme of work for 2006/07. We will seek to reconsider, with you, your improvement priorities in the light of the latest CPA assessment and your own analysis, and develop an agreed programme by 31 March 2006. We will continue to work with other inspectorates and regulators to develop a co-ordinated approach to regulation.

Revision to the Code of Audit Practice

- 53 The statutory requirements governing our audit work, are contained in:
- the Audit Commission Act 1998; and
 - the Code of Audit Practice (the Code).
- 54 The Code has been revised with effect from 1 April 2005. Further details are included in our Audit Plan which has been agreed with the Director of Finance. The key changes include:
- the requirement to draw a positive conclusion regarding the Council's arrangements for ensuring value for money in its use of resources; and
 - a clearer focus on overall financial and performance management arrangements.

Closing remarks

- 55 This Letter has been discussed and agreed with the Chief Executive. A copy of the Letter will be presented at the Executive on 21 February 2006 and the Community Leadership and Overview Panel on 13 April 2006.
- 56 The Council has taken a positive and constructive approach to our audit and inspection I would like to take this opportunity to express my appreciation for the Council's assistance and co-operation.

Availability of this Letter

- 57 This Letter will be published on the Audit Commission's website at www.audit-commission.gov.uk and also on the Council's website.

Derek Elliott
Relationship Manager and District Auditor
January 2006

Appendix 1 – Background to this Letter

The purpose of this Letter

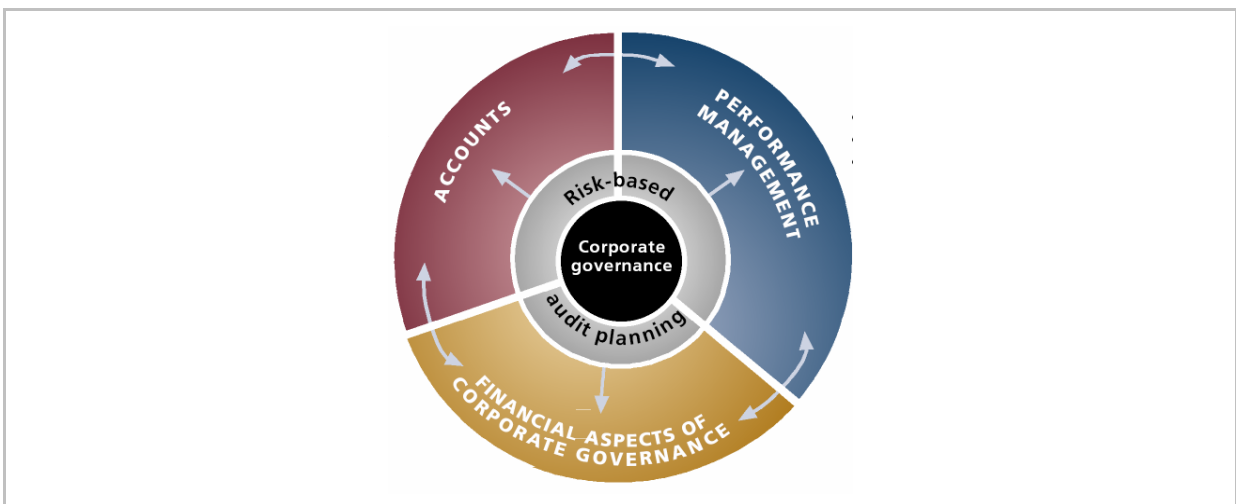
- 1 This is our Annual Audit and Inspection Letter for members which incorporates the Annual Audit Letter for 2004/05, which is presented by the Council’s Relationship Manager and District Auditor. The Letter summarises the conclusions and significant issues arising from our recent audit and inspections of the Council.
- 2 We have issued separate reports during the year setting out the findings and conclusions from the specific elements of our programme. These reports are listed at Appendix 2 for information.
- 3 The Audit Commission has circulated to all audited bodies a statement that summarises the key responsibilities of auditors. Our audit has been conducted in accordance with the principles set out in that statement. What we say about the results of our audit should be viewed in the context of that more formal background.
- 4 Appendix 3 provides information about the fee charged for our audit and inspections.

Audit objectives

- 5 Our main objective as your appointed auditor is to plan and carry out an audit that meets the requirements of the Code of Audit Practice. We adopt a risk-based approach to planning our audit, and our audit work has focused on your significant financial and operational risks that are relevant to our audit responsibilities.
- 6 Central to our audit are your corporate governance arrangements. Our audit is then structured around the three elements of our responsibilities as set out in the Code and shown in Figure 3 below.

Figure 3 Code of Audit Practice

Code of practice responsibilities



Accounts

- Opinion.

Financial aspects of corporate governance

- Financial standing.
- Systems of internal financial control.
- Standards of financial conduct and the prevention and detection of fraud and corruption.
- Legality of transactions.

Performance management

- Use of resources.
- Performance information.
- Best value performance plan.

Appendix 2 – Audit reports issued

Table 7

Report title	Date issued
Audit Plan	May 2005
Interim Audit Report	November 2005
Report on the 2004/05 Financial Statements to Those Charged with Governance (SAS 610)	October 2005
Ethical Governance Arrangements	June 2005
Final Accounts Audit Report	November 2005

Appendix 3 – Audit fee

Table 8 Audit fee update

Audit area	Plan 2004/05 (£)	Actual 2004/05 (£)
Accounts	89,840	89,840
Financial aspects of corporate governance	73,980	73,980
Performance	59,780	59,780
Total Code of Audit Practice fee	233,600	233,600

Inspection fee update

- 7 The full year inspection fee is £46,117 for Relationship Management and some aspects of CPA. The work reported in this Letter has been funded by an element of the fee covering 2004/05 and by an element of the fee covering 2005/06. In both years the actual fee will be in line with that planned.