

Annual Audit Letter

City of Salford

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DISTRICT AUDIT

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KEY MESSAGES

Introduction

This has been another demanding year for the Council. However, despite continuing financial pressures, there have been a number of significant achievements including:

- recognition by the Department of Health that the Social Services Directorate is one of the best 15 performers in the country
- being awarded Pathfinder status for the Council's e-government work
- continuing the regeneration of the Salford Quays area of the City
- restructuring of the refuse collection service to improve its efficiency.

2000/2001 is the first year that we have carried out a truly risk based audit under the new Code of Audit Practice. We have therefore placed emphasis on the two potential risk areas of financial standing and Best Value.

Financial standing

The Authority has completed the first year of its financial recovery plan and has achieved the level of reserves anticipated at this stage of the plan. However the difficult financial climate continues and the budgetary position will remain tight for the foreseeable future. Much remains to be done to stabilise the longer term position.

The out-turn for 2001/2002 was better than expected and the Council has been able make the planned £2m contribution to reserves. A balanced budget has also been set for 2001/2002 and the latest monitoring reports show that this should be achieved. It is important that the Council continues to closely monitor performance against the budget and takes prompt action if there is slippage in the delivery of savings or other pressure areas look likely to cause a problem.

The Council's current capital proposals for 2002/2003 significantly exceed the capital resources available. There are plans to bring the two into line primarily by reducing the capital schemes planned for the year. We would stress the importance of taking this action to ensure

that an overspend on the capital programme does not arise.

The current year's capital financing strategy places significant reliance on capital receipts. The date of receipt is difficult to predict with any certainty and the Council was left with a significant element of unfinanced capital expenditure at the end of 2000/2001. We understand that capital receipts are being closely monitored in 2001/2002 to ensure that expenditure is not incurred until the means to finance it are available. It is essential that this continues.

Best Value

The Council's 2001/2002 Best Value Performance Plan met the minimum statutory requirements in all areas apart from the omission of some performance indicators. In addition the Summary Plan did not provide a fair and accurate reflection of the main plan. We qualified our opinion in respect of both of these items and the Summary Plan was subsequently re-issued.

We made a number of formal recommendations to which the Council responded positively and agreed a comprehensive series of actions. These mainly related to the need to consistently apply the Authority's performance management system, reviewing the approach to Best Value reviews and adopting a more proactive approach to challenge.

Our recent review of progress against the action plan indicates that significant progress has been made in some areas, particularly around performance monitoring and increasing the robustness of challenge at the scoping stage of the review process.

However, a lot remains to be done and we are still concerned about the Council's capacity to deliver robust reviews and implement changes which will improve service delivery within an acceptable timeframe.

It is important that the impetus for change continues and begins to have an impact on the quality of the services delivered. We will re-visit Best Value early in the new year to continue to monitor the progress made.

The purpose of this Letter

This Annual Audit Letter summarises for Members the more important matters arising from our audit for 2000/2001 and comments on other current issues. We have produced separate reports during the year on completion of specific aspects of our work which have been discussed in detail with Officers. The reports are listed at the end of this Letter for Members' information.

The Audit Commission has circulated to all audited bodies a statement, which 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.

Audit objectives

Audit work is based on the significant financial and operational risks that the Council faces and is structured around three main elements:

EXHIBIT 1

The three main elements of audit objectives



Accounts

- Opinion
- Regularity

Financial Aspects of Corporate Governance

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

Performance Management

- Best Value Performance Plans
- Performance information
- Use of resources – performance studies

Our audit has addressed the requirements of the Code of Audit Practice and we have worked with the Council to maximise the benefits of the integrated audit approach. We have reviewed your arrangements for dealing with risks and we have undertaken more detailed work in selected areas of higher audit risk.

Accounts

- Opinion
- Regularity

We anticipate being able to give an audit opinion by 31 December 2001. This opinion will contain an emphasis of matter paragraph due to the level of unfinanced capital expenditure at the year end.

The Authority was late in preparing its accounts this year and they were only approved by Council on the 21 November 2001. As a result we commenced our audit one month later than usual although we are still aiming to give our opinion by 31 December 2001.

During 2000/2001 the Council planned to use a £13.6m capital receipt from the sale of Salford Precinct to finance its capital programme. The completion of the sale was delayed until the end of May 2001 which meant that a significant part of the capital programme was unfinanced at the year end.

The capital controls regulations make it clear that the Council is only able to incur capital expenditure in so far as it has the necessary 'credit cover' which includes capital receipts. The 2000/2001 accounts therefore do not comply with these regulations. We will be referring to this failure to comply in our opinion and the Authority must introduce measures to ensure that a funding shortfall does not arise again in the future.

Financial aspects of corporate governance

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

Financial standing

The Council has made some progress in putting its financial standing back on a sound footing. However the Council's financial health remains difficult and much remains to be done to stabilise the longer term position.

Financial standing – revenue

In the recent past the Council has faced significant financial difficulties. During 1999/2000 a sudden increase in the number of children in care meant that urgent measures had to be taken to avoid a deficit. One of these measures was to use all of the Council's remaining reserves in that year. The increasing cost of children in care is a problem that is now being faced by many other authorities nationally.

The difficulties in 1999/2000 showed that the underlying levels of expenditure were £13m greater than underlying resources. The scale of the pressures meant that it was unreasonable to achieve financial stability in just one year. Consequently the Council's plan was to produce a balanced budget by the year 2001/2002 and to increase reserves in phases to £7m (3%) by 2002/2003.

The Council had to implement some radical changes in 2000/2001 to achieve the planned savings. The out-turn for the year was better than expected and the Council has been able to set up two new earmarked reserves totalling £1m as well as making the planned £2m contribution to general reserves. A balanced budget has also been set for 2001/2002 and the latest monitoring report shows that the Council is on target to achieve this.

The Council's longer term projections show that finances are going to be tight for the foreseeable future. It is anticipated that savings of approximately £3m will have to be made in 2002/2003 although this could increase if the Council decides to bring back to revenue some of the costs it has capitalised in the past to ease the financial pressures.

The Council views capitalisation as a temporary measure to help to overcome the immediate financial difficulties. We support the Council's longer term plans which show the level of capitalisation reducing in future years.

Financial standing - capital

During 2001/2002 it was found that the capital expenditure proposals exceeded the available finance by £7.5m and the two were brought into line through the following measures:

- deferring £5.7m of expenditure into 2002/2003
- identifying £1.8m of reductions in capital expenditure.

The Council's longer term capital proposals significantly exceed the resources available. The latest estimates of the 2002/2003 capital programme show that the cost of potential schemes exceeds the financial resources by £15.4m. As mentioned above, one factor that has contributed to the potential over programming is capitalisation to support the revenue budget. If this was to continue at the same rate as in 2001/2002, the under-funding would be almost £21m or 25% of the programme.

The Council intends to tackle this over programming by:

- examining the potential for alternative sources of finance such as PFI
- continuing to prioritise and reduce capital proposals to bring them into line with resources.

We would stress the importance of taking these measures to ensure that capital expenditure does not exceed the funding available.

The Council's capital financing strategy places significant reliance on capital receipts, many of which have not yet been realised. The problems experienced last year with the sale of Salford Precinct illustrate the difficulties that can be experienced with property disposals. It is therefore important that the Council continues to carefully monitor capital receipts and does not incur capital expenditure until it is certain that the means to finance it are available.

We are pleased to note that the level of capital receipts included in future capital projections now reflects the normal annual level of such receipts. Whilst this will have contributed to the potential over programming, it means that the risks associated with having to generate high levels of receipts have been reduced.

Legality of financial transactions

We have identified issues that need to be addressed on the Council's homeswaps scheme.

We reviewed the Council's overall arrangements for monitoring the legality of its transactions. There are plans to strengthen the Legal Services Division so that these arrangements can be carried out in a more structured manner.

During the year we have reviewed a number of specific legal issues including:

- transfer of residential care homes to a trust
- homeswaps scheme.

The transfer of residential care homes is still on-going. We were asked to review the homeswaps scheme due to its innovative nature and sensitivity with the local community.

We concur with the Council's view that there appear to be legislative powers to enable implementation of the scheme. A comprehensive report outlining the legal position is currently being prepared. However we found that there was a need to be more clear and rigorous in relation to the eligibility criteria, procedures and documentation. Recommendations have been made which are currently being considered.

As mentioned above, the homeswaps scheme is an innovative approach to solving a very difficult problem. If it is successful it may become a regeneration model that it replicated in other parts of the country. It is therefore essential that the scheme does not become discredited because of weaknesses in the detailed operational procedures.

Systems of internal financial control

The newly implemented financial systems contain some control weaknesses that are currently being addressed.

We reviewed internal financial controls in business critical systems. In April 2000 the Authority introduced a new main accounting system. This included new payroll, creditors and debtors systems that were phased in over the course of the year.

We found that, due to the demands of introducing a new system, some key controls in the main accounting system had not been carried out regularly throughout the year. In addition, at the time of our audit, there was some confusion between officers as to where the controls over systems feeding into the ledger should be exercised.

The lapse in controls does not necessarily mean that the ledger is wrong but could lead to errors going undetected and so uncorrected for longer than necessary. We understand that since our audit action has been taken to address these problems. The Council is aiming to be up to date with all the reconciliations by January 2002.

As part of an integrated audit approach we rely as much as possible on the work of Internal Audit. Internal Audit are currently carrying out in-depth reviews of the new payroll, creditors and debtors systems and will be reporting their findings in the near future. Initial indications are that some controls could be strengthened. It is important that the Council addresses any weaknesses that may be identified by these Internal Audit reviews.

Fraud and corruption

There are no significant issues arising.

The Authority has implemented arrangements to help to ensure that its affairs are managed in accordance with proper standards of financial conduct. These include a Code of Conduct for Members and registers for pecuniary interests and gifts and hospitality received. The Staff Code of Conduct is to be issued shortly.

There are also arrangements for the prevention and detection of fraud and corruption. These include an anti-fraud and corruption policy and 'whistle blowing' arrangements set up in response to the Public Interest Disclosure Act.

Salford have also taken part in the National Fraud Initiative which is a key data matching exercise operated throughout the public sector to prevent and detect misappropriation of public funds. This exercise enabled the Council to successfully detect instances of fraud and overpayment with a consequent saving of £74,000. In common with most similar authorities, these cases relate predominantly to housing benefits. This activity supports the corporate anti-fraud and corruption strategy.

Performance management

- Best Value Performance Plan
- Performance information
- Use of resources

Best Value

Although committed to the concept of Best Value the Council has struggled to implement it effectively because of capacity constraints. As part of our BVPP audit we made a number of formal recommendations to which the Council responded positively and agreed a comprehensive series of actions. These mainly related to the need to consistently apply the Authority's performance management system, reviewing the approach to Best Value reviews and adopting a more proactive approach to challenge. However there has also been some slippage against the action plan.

The Council's 2001/2002 Best Value Performance Plan (BVPP) met the minimum statutory requirements in all areas apart from the omission of some performance indicators. In addition the Summary Plan did not provide a fair and accurate reflection of the main plan. We qualified our opinion in respect of both of these items and the Summary Plan was subsequently re-issued.

Our audit showed that Best Value was not sufficiently integral to day to day management arrangements and was sometimes seen as an 'add on'. There were examples of dynamic good practice but these need to be replicated across the Authority.

The Council has had many elements of a performance management system in place for a number of years but the absence of a strong corporate lead has resulted in variations in its application between directorates.

The first year Best Value review programme has resulted in little identifiable improvement in services largely due to a combination of slippage in completing reviews and action plans that lack clarity and specific, measurable actions. The lessons learnt from the Year 1 review process need to be taken on board to secure better processes and outcomes in Year 2.

Since our audit the Council has responded positively to our recommendations. Significant progress has been made in a number of areas including:

- production of a comprehensive performance monitoring report for Quarter 1 in November. For every indicator showing below target performance comprehensive details were provided including identification of any barriers to improvement and what action was needed to address these
- alignment of performance information, objectives and targets under the six Council pledges and initial moves to link budget allocations to pledges. This should feed through into individual service plans which are currently under preparation
- regular meetings between the Leader and Chief Executive and leading members and Directors to discuss progress and ensure commitment to the developing agenda
- challenge sessions for reviews nearing completion and visioning challenges for new reviews have been initiated and driven by the Chief Executive.

However, the agenda remains considerable and there are still issues around capacity. There has been some slippage in the agreed action plan and areas that have not progressed as well as originally anticipated include:

- preparatory work on improving the quality and coverage of the 2002/2003 BVPP
- individual Best Value reviews with no new reviews being completed since our audit
- assessment of the workload associated with Best Value and staffing levels needed to resource it
- project management training for the officers involved in the review process

- comprehensive application of the staff appraisal scheme across the Authority.

It is important that the impetus for change continues and begins to have an impact on the quality of the services delivered. We will re-visit Best Value early in the new year to continue to monitor the progress made.

Performance information

There have been significant problems with the collation of reliable performance information resulting in a qualified opinion being issued. Measures are being taken to address these problems.

During our Best Value audit tests on the accuracy of a selection of the performance indicators showed that 58% of the estimates tested were not soundly based. Supplementary work by the Authority proved that, in terms of the accuracy of the estimates compared to the year end actuals, 50% were significantly different. We therefore qualified our Best Value opinion in respect of these inaccuracies.

We also encountered a number of problems with the working papers supporting the performance indicator calculations including:

- failure to keep working papers
- insufficient supporting documentation
- delays in producing working papers for audit.

Since then we have audited the performance indicators actual figures for the year and whilst some areas had improved others had not.

In order to assist in the production of accurate information District Audit has recently held a series of workshops designed to explain to staff how to set targets and produce clear audit trails. In addition the Authority are developing a quality assurance system with Directors to ensure auditing and checking at all levels and stages and this work is on target for delivery in December 2001.

This work should continue so that eventually performance indicators become an integrated part of the Authority's overall management arrangements with officers taking ownership of the performance indicator data.

Use of resources

We have reported issues in a number of specific areas and, in particular, we draw Members' attention to our findings on school budgets, housing management arrangements and the collection of income.

School budgets

Schools have had control over their own budgets since the introduction of local management in schools in 1990 but recent developments such as Fair Funding and the Standards Fund present new challenges for their budget management. Our audit reviewed the way in which the LEA supports financial and resource management in schools.

We found many examples of good practice within the Authority's approach. In particular we identified as strengths the risk-based frameworks developed by the Inspection/Advisory Service and Internal Audit to focus their work, and the LEA's co-ordinated response to schools causing concern.

We also found that:

- although a Fair Funding Review Group meets regularly to consider the funding formula, there have been no fundamental revisions since its inception in 1990
- there were some areas in which better management information could be provided to schools eg earlier communication of budget allocations, regular reconciliation of schools' systems to their bank accounts
- there is little flexibility in the traded financial services offered to schools.

We have agreed an Action Plan aimed at addressing these issues.

Housing management arrangements

We carried out this review at the request of the Authority following similar reviews in the Education and Social Services Directorates. We reviewed the Housing Directorate's management arrangements in the following three areas:

- strategic decision making
- performance management
- management of void properties.

We concluded the audit with an action planning workshop at which the Council's response to our recommendations was agreed.

With regard to the future housing strategy, we found that the Housing Directorate had collected a lot of information to help inform future decisions but had still to act on it. We agreed that the best way forward would be for the newly developed area actions plans, prepared as part of the Unitary Development Plan, to form the basis of the future housing strategy. These have the advantage of covering all the services in an area, whether provided by the Council or external partners, and will ensure that housing is not considered in isolation.

In the case of performance management we agreed that the Housing Directorate would make a number of improvements to their current arrangements including:

- developing action plans to achieve service plans
- translating key objectives into performance targets that cascade through the Directorate in the form of service and individual targets
- introducing a staff appraisal system across the Directorate.

Finally, in the third area of void management, we found that there was a need to reduce the number of social housing units across the City. We agreed that short, medium and long term targets for the level of council owned housing would be set as part of the area based planning process.

Collection of income

We reported in last year's management letter that the level of debt outstanding was a significant risk for the Council and was high in comparison to other authorities. This year's review concentrated on the Council's performance in collecting income for:

- council tax
- sundry debtors.

We found that in recent years council tax and sundry debtor recovery procedures have not been rigorous in their design and application. However during the last twelve months the Council has introduced some changes in its procedures aimed at improving the collection rates in these two areas.

These developments have generally taken place as departmental initiatives rather than as part of an overall strategy on income collection. To significantly improve the collection of income overall there needs to be a comprehensive corporate income collection policy across the board. Without a clear corporate lead, the initiatives taken so far will not be effective in meeting the new demands placed on the Council.

Our review also showed that:

- there is a need to explore the options for reducing the number of small value invoices, including a much greater emphasis on prepayments and aggregated invoices
- the new procedures are just beginning to have a positive impact on collection rates but need to continue to be rigorously enforced
- the administration of old sundry debts is hindering the effective performance of the new measures taken by the Council
- the Council has a high level of outstanding transactions with some of its own schools and other public bodies, particularly Salford University
- the Council has not had an active policy for write-offs with many accounts lying dormant on the system although work on reviewing these has recently commenced
- the bad debt provision needs to be re-appraised as this does not currently reflect the level of arrears.

We are currently discussing our report with officers and will be agreeing an Action Plan to take our recommendations forward in the near future. Resolution of some of these items, such as the write-offs and bad debts provision, is particularly important due to their potential impact on the Council's financial health.

New democratic arrangements

The Council responded to the democratic renewal agenda in advance of the Local Government Act 2000 by operating pilot arrangements since December 1999.

As required by legislation and guidance the Council has this year:

- carried out comprehensive public consultation around the three options for the new executive arrangements
- submitted proposals, based on the results of the consultation, setting out the intention to proceed with the Leader and Cabinet model
- prepared a new constitution which was adopted by full Council on 19 September 2001.

The experience gained from the pilot arrangements has been used positively to develop the final proposals and constitution. The Council has been open to advice and assistance from other parties including ourselves. We are pleased to see that the intention is to maintain this approach with the new constitution being seen as a living document which will be subject to regular review to secure its fitness for purpose.

In common with other authorities the priority now will be to ensure that the new arrangements work in practice and deliver the improvements expected of them. In particular the following issues will need to be addressed:

- the effective operation of the scrutiny function
- the development of the Forward Plan into a useful and meaningful document
- arriving at a proper balance between collective executive management and delegation to both Lead member and officers
- agreeing financial regulations that meet new requirements
- the operation of the new ethical arrangements once final guidance has been issued.

We are aware that work is in hand in all of these areas and will be reviewing progress as part of next year's audit.

Other service reviews

We carried out six other reviews during the year, some of which were following up the progress

made on recommendations from past studies. The key findings are summarised in Exhibit 2.

EXHIBIT 2

Key issues arising from use of resources reviews

Service reviewed/key findings	Progress/Further action needed
Health Act flexibilities At the time of our review, in May 2001, the Council was in the early stages of developing a partnership for the provision of services for adults with learning disabilities.	District Audit has developed a checklist covering the areas that should be considered when establishing partnerships. The Authority is continuing to address the outstanding issues highlighted by the checklist. We intend to re-visit this area to review progress early in the new year.
Information Society The Council has committed substantial investments in ICT facilities to enable modernisation through electronic service delivery. There have been a number of achievements during the year including continuing implementation of the office automation project and call centre services.	The Council has been awarded Pathfinder status for its electronic government project. The detailed plans that have been prepared to support the Pathfinder objectives have now to be implemented. Engagement with and ownership by service managers is likely to be a critical success factor in the delivery of overall programme objectives.
Planning school places The secondary school review is underway and surplus places should be no more than 8% by the time this exercise is concluded.	Work is progressing on the plans to reduce the number of surplus places in primary schools although there has been some slippage in the programme. Securing funding to finance any structural changes to school buildings that may be required as a result of the review may be a problem.
School attendance and exclusion The Authority has succeeded in reducing the cost and improving the effectiveness of the Education Welfare Service.	The Authority has worked hard to improve the inclusiveness of its provision but despite these efforts the exclusion rate, particularly in secondary schools, has remained high. Further work is required to understand the effectiveness of different approaches.
Asset management The Council has developed its asset management arrangements including producing an Asset Management Plan in accordance with the DTLR timetable.	Work is continuing in the following areas: <ul style="list-style-type: none"> • linking the Asset Management Plan to the six pledges • calculating the on-going cost of maintaining the asset base • undertaking phase two of the property Best Value review • developing benchmarking for running costs.
Probity in planning Good progress has been made in addressing key improvement areas identified last year.	The only issue still outstanding is the need to include certain policies in the new Unitary Development Plan when it is published in 2002.

Future audit work

We are currently considering the significant operational and financial risks facing the Council that will need to be addressed in next year's audit.

We will discuss our risk assessment with your officers before producing an audit plan.

Closing remarks

Finally, I would like to take this opportunity to express my appreciation for the assistance received from officers during the course of our work. Our aim is to provide a high standard of audit service which makes a practical and positive contribution to the work of the Council. We recognise the value of your co-operation and support.



Sue Sunderland
District Auditor
December 2001

Reports issued during the audit

- School Budgets (May 2001)
- Best Value Reports (June 2001)
- Review of Management Arrangements in Housing (July 2001)
- Health Act Flexibilities – Learning Disabilities (August 2001)
- Core Process and Corporate Governance Arrangements (September 2001) -draft
- Collection of Income (October 2001) - draft
- General Financial Standing (October 2001) - draft
- Homeswaps (November 2001) - draft