

# Annual Governance Report

Dudley Metropolitan Borough Council

Audit 2008/09

24<sup>th</sup> September 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 the 2008/09 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess how well you use and manage your resources to deliver value for money and better and sustainable outcomes for local people.

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Financial Statements	Results	Pages
Unqualified audit opinion	Yes	6
Financial statements free from error	Yes	6 - 8
Adequate internal control environment	Yes	8
<b>Use of resources</b>		
Use of resources judgements	Yes	9 - 10
Arrangements to secure value for money	Yes	10

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## Audit opinion and financial statements

- 1 I plan to issue an unqualified audit opinion following the adoption of the accounts by the Audit Committee and the clearance of any outstanding matters. I will not be able to certify the completion of the audit until I have considered matters brought to my attention by a member of the public.
- 2 I am required to report all items that are 'non trivial' that we have identified during our audit before I issue my opinion. Our definition of 'trivial' has been revised this year and I am reporting any issues above £71,000.
- 3 There are three issues that I wish to draw to your attention:
  - Impairment of Council Dwellings – the valuation of Council Dwellings has been reduced by £85.1m from the draft financial statements to reflect the impact of general economic changes.
  - Restatement of prior period adjustments – most items that were adjustments to the opening position in the draft financial statements are now included within the 2008/09 financial transactions
  - Pension fund asset valuation – the accounts have been amended to reflect a £3.7m fall in pension fund asset valuations between December 2008 and March 2009.

**Value for money Conclusion and use of resources**

- 4 I plan to issue an unqualified value for money conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in its use of resources in 2008/09.
- 5 My conclusion is based on work carried out to inform my scored use of resources judgement. Overall I assessed the Council as having good arrangements in place for managing finances and governing the business and adequate arrangements for managing resources.

# Next steps

**This report identifies the key messages that you should consider before I issue my financial statements opinion, value for money conclusion, and audit closure certificate. It includes only matters of governance interest that have come to my attention in performing my audit. My audit is not designed to identify all matters that might be relevant to you.**

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**6** I ask the Audit Committee to:

- consider the matters raised in the report before approving the financial statements (pages 6 to 8);
- take note of the adjustments to the financial statements which are set out in this report (Appendix 2);
- take note of the VFM Conclusion and Use of Resources score;
- approve the letter of representation on behalf of the Council before I issue my opinion and conclusion (Appendix 3).

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# Financial statements

**The Council's financial statements and annual governance statement are important means by which the Council accounts for its stewardship of public funds. As Council members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.**

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## Opinion on the financial statements

- 7 Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the financial statements. Appendix 1 contains a copy of my draft audit report.
- 8 A member of the public has exercised their rights under the Audit Commission Act 1998 to question me about the accounts. I will not be able to issue a certificate of closure until I have considered this matter on the 30<sup>th</sup> September 2009.

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## Errors and uncertainties in the financial statements

### Impairment of council dwellings

- 9 I noted that the valuation of Council Dwellings included in the accounts was not reduced as a consequence of changes in economic conditions. As part of the audit I requested that the Council's Valuer reconsidered this. Following further consideration of the impact of falling property prices he determined that an 8% fall in the value of Council Dwellings was appropriate. The overall impact of this is to reduce the value of Council Dwellings by £85.1m in the restated accounts.
- 10 Independent expert valuation advice provided to the Audit Commission indicates that residential property values fell by 13% in the West Midlands during 2008/09. The Council's Valuer has based his judgment on factors more local to Dudley. I have concluded that the reduction in values of 8% is reasonable.

### Restatement of prior period adjustments

- 11 The accounts presented for audit restated the Council's opening financial position for 2008/09. This included adjustments relating to demolition of Council Houses (£7.8m), the inclusion of Oldswinford Hospital School's assets and liabilities (£1.4m) and a change in how the Council's share of quoted securities held by the pension fund are valued (£0.6m)
- 12 The change in pension fund asset values is an appropriate adjustment, as it results from a change in the Council's accounting policies. The adjustments for demolished Council Houses and Oldswinford Hospital School did not meet the requirements for restatement. The revised accounts have been adjusted to only include restatement for the change in pension fund asset values. Items that were initially adjustments to the opening position are now included in the accounts.

## Financial statements

### Pension fund asset valuation

- 13** The change in economic conditions has also had an impact on pension fund assets. The auditors of the pension fund administered by Wolverhampton City Council concluded that the value of assets fell by 0.8% between December 2008 and March 2009. This reduction was not reflected in the fund's year end asset valuations.
- 14** This issue was notified to me during the course of my audit and the Council were not aware of it when the accounts were prepared. I assessed the impact of this change as £3.7m. The accounts have been amended to reflect this change.

### Other issues

- 15** Two other issues were identified by my audit which I am reporting to you:
- Fixed assets - the Springfields Neighbourhood Centre Lions Boxing Club asset value was incorrect and it was included in the wrong category of fixed assets (£136,000)
  - Receipts in advance - misclassification of capital funding as a receipt in advance (£100,000).
- 16** There is no impact on the Council's revenue reserves from the issues identified during the course of my audit.

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### Letter of representation

- 17** Before I issue my opinion, auditing standards require me to obtain appropriate written representations from you and management about your financial statements and governance arrangements. Appendix 3 contains the draft letter of representation I seek to obtain from you.

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### Key areas of judgement and audit risk

- 18** In planning my audit I identified specific risks and areas of judgement that I have considered as part of my audit. These areas and my findings are set out in Table 1.

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**Table 1**      **Key areas of judgement and audit risk**

<b>Issue or risk</b>	<b>Finding</b>
Accounting for equal pay settlements	The provision for equal pay settlements complies with the Statement of Recommended Practice. I also made enquires to confirm that the amount of the provision had not changed significantly since 31 March 2009.

Issue or risk	Finding
Valuation of investment in Birmingham Airport	The valuation of the Council's shareholding is consistent with the advice I have received.
The accounting treatment of the Dudley Grid for Learning contract needed to be re-considered in the light of contract renewal.	The revised accounting treatment for the extended service contract is appropriate.
The recession has had a negative impact on asset values. There is a risk that the Council's assets may not have been appropriately impaired and are overvalued.	Council Dwelling values have been amended to reflect the change in economic conditions.

**Adequate internal control environment**

**19** There are no issues regarding the Council's internal control environment that I wish to bring to your attention.



# Use of resources

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

I am also required to conclude 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

- 20** 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.
- 21** 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.
- 22** The Council's use of resources theme scores are shown in Table 2 below. The KLOE scores are summarised in Appendix 4.

**Table 2 Use of resources theme scores**

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

## Managing finances

- 23** Overall, the Council performs well at managing its finances. The annual budget process is completed and approved in a timely manner with strong emphasis on medium term financial planning. The capital programme is linked to priorities and supporting service improvements. Public consultation results in changes to spending priorities and resources have been shifted from low to high priority areas. The Council continues to show strong performance whilst keeping costs within budget.
- 24** Directorates have authority to identify their areas for efficiency but are called to account on their achievement and on their comparative outcomes on cost and performance. Efficiency targets are regularly achieved although this is recognised as a particular future challenge given increasingly tight budgets. The Council's processes for regular financial monitoring and forecasting throughout the year enables them to

maintain a good track-record for prompt and accurate closedown, with draft accounts provided by the end of May.

### Governing the business

- 25** The Council has good arrangements in place to govern its business. It seeks to maximise efficiencies through procurement and promotes this through its procurement strategy and practices, a lean supply chain and a partnership approach with its contractors.
- 26** The Council is proactive in reviewing its data quality and has sound systems in place to support its decision making. The Corporate Improvement group is developing its scrutiny of performance indicators. Data quality is a focus area for the Council to strengthen further.
- 27** The Council is an ethical Council, which regularly refreshes governance policies and procedures. It puts a strong emphasis on good governance in partnership working and has a well established and effective Partnership Evaluation Tool (PET). The Audit Committee plays an effective role in ensuring governance policies and procedures are up to date. Risk Management is embedded in the Council's business practices and strong anti fraud and corruption arrangements are in place.

### Managing resources

- 28** The Council meets the minimum requirements in managing its resources. It takes a corporate, co-ordinated and proactive approach to making effective use of natural resources, which extends into its partnership working and leadership roles. Sound progress is already demonstrable in schools on transport plans and achievement of Eco Schools status, and in the establishment of Council baselines for energy consumption, staff travel and energy consumption.
- 29** The Council has a well established and sound approach to asset management. Asset management plans are in place at all levels of the organisation with ranking systems to establish priorities and a robust monthly monitoring system is in place. The Council recognises its estate is outdated and is now developing a business transformation strategy which may impact on its premises needs.

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### Value for money conclusion

- 30** I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against criteria specified by the Audit Commission. 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 4.
- 31** I intend to issue an unqualified conclusion stating that the Council had adequate arrangements to secure economy, efficiency and effectiveness in the use of resources.
- 32** Appendix 1 contains the wording of my draft report.

# Appendix 1 – Independent auditor’s report to Members of Dudley Metropolitan Borough Council

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## Opinion on the financial statements

I have audited the Authority accounting statements and related notes of Dudley Metropolitan Council for the year ended 31 March 2009 under the Audit Commission Act 1998. The accounting statements comprise the Income and Expenditure Account, the Statement of Movement on the General Fund Balance, the Balance Sheet, the Statement of Total Recognised Gains and Losses, the Cash Flow Statement, the Housing Revenue Account, the Statement of Movement on the Housing Revenue Account, the Collection Fund and the related notes. These accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of Dudley Metropolitan Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 49 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by the Audit Commission.

## Respective responsibilities of the Responsible Financial Officer and auditor

The Responsible Financial Officer’s responsibilities for preparing the financial statements in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2008 are set out in the Statement of Responsibilities for the Statement of Accounts.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the accounting statements present fairly, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2008 the financial position of the Authority and its income and expenditure for the year.

I review whether the governance statement reflects compliance with ‘Delivering Good Governance in Local Government: A Framework’ published by CIPFA/SOLACE in June 2007. I report if it does not comply with proper practices specified by CIPFA/SOLACE or if the statement is misleading or inconsistent with other information

I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered, whether the governance statement covers all risks and controls. Neither am I required to form an opinion on the effectiveness of the Authority's corporate governance procedures or its risk and control procedures

I read other information published with the accounting statements, and consider whether it is consistent with the audited accounting statements. This other information comprises the Explanatory Foreword. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the accounting statements. My responsibilities do not extend to any other information.

### **Basis of audit opinion**

I conducted my audit in accordance with the Audit Commission Act 1998, the Code of Audit Practice issued by the Audit Commission and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the accounting statements and related notes. It also includes an assessment of the significant estimates and judgments made by the Authority in the preparation of the accounting statements and related notes, and of whether the accounting policies are appropriate to the Authority's circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the accounting statements and related notes are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the accounting statements and related notes.

### **Opinion**

In my opinion the Authority's financial statements present fairly, in accordance with relevant legal and regulatory requirements and the Code of Practice on Local Authority Accounting in the United Kingdom 2008, the financial position of the Authority as at 31 March 2009 and its income and expenditure for the year then ended.

## **Appendix 1 – Independent auditor’s report to Members of Dudley Metropolitan Borough Council**

### **Conclusion on arrangements for securing economy, efficiency and effectiveness in the use of resources**

#### **Authority’s Responsibilities**

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance and regularly to review the adequacy and effectiveness of these arrangements.

#### **Auditor’s Responsibilities**

I am required by the Audit Commission Act 1998 to be satisfied that proper arrangements have been made by the Authority for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion in relation to proper arrangements, having regard to relevant criteria specified by the Audit Commission for principal local authorities. I report if significant matters have come to my attention which prevent me from concluding that the Authority has made such proper arrangements. I am not required to consider, nor have I considered, whether all aspects of the Authority’s arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

#### **Conclusion**

I have undertaken my audit in accordance with the Code of Audit Practice and having regard to the criteria for principal local authorities specified by the Audit Commission and published in May 2008 and updated in February 2009, and the supporting guidance, I am satisfied that, in all significant respects, Dudley Metropolitan Borough Council made proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2009.

# Appendix 2 – Adjusted amendments to the accounts

The following misstatements were identified during the course of my audit and the financial statements have been adjusted by management. I bring them to your attention to assist you in fulfilling your governance responsibilities.

**Table 3**

		Income and Expenditure Account		Balance Sheet	
Adjusted misstatements	Nature of Adjustment	Dr £000s	Cr £000s	Dr £000s	Cr £000s
Impairment of Council Dwellings	Reduction in valuation due to change in economic conditions			85,097	85,097
Net pension liability	Reduction in valuation due to change in economic conditions			3,683	3,683
Fixed asset restatement	Omission of updated asset value and re-designation as surplus asset			136	136
Receipts in advance	Misclassification of capital funding as a receipt in advance			100	100

It should also be noted that items initially shown as prior period adjustments have been restated as in year transactions.

# Appendix 3 – Draft letter of representation

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To:

Tony Corcoran  
District Auditor  
Audit Commission  
Ground Floor, Suite 1,  
Observer House  
Horsefair,  
Abbey Forge  
Shrewsbury,  
SY2 6BL

## **Dudley Metropolitan Borough Council - Audit for the year ended 31 March 2009**

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Dudley Metropolitan Borough Council, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2009. All representations cover the Council's accounts included within the financial statements.

### **Compliance with the statutory authorities**

I acknowledge my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom: A Statement of Recommended Practice which present fairly the financial position and financial performance of the Council and for making accurate representations to you.

### **Supporting records**

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Council have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Council meetings, have been made available to you.

### **Irregularities**

I acknowledge my responsibility for the design and implementation of internal control systems to prevent and detect fraud or error.

There have been no:

- irregularities involving management or employees who have significant roles in the system of internal accounting control;
- irregularities involving other employees that could have a material effect on the financial statements; or
- communications from regulatory agencies concerning non-compliance with, or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements; and
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

### Law, regulations, contractual arrangements and codes of practice

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the Council.

The Council has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

### Fair Values

I confirm the reasonableness of the significant assumptions within the financial statements. For the valuation of land and buildings, residual interest in the Council's PFI contracts, long term investments, debtors, creditors and provisions assumptions, I confirm:

- the appropriateness of the measurement method;
- the basis used by management to overcome the presumption under the financial reporting framework;
- the completeness and appropriateness under the financial reporting framework; and
- subsequent events do not require adjustment to the fair value measurement.

### Assets

The following have been properly recorded and, where appropriate, adequately disclosed in the financial statements:

- losses arising from sale and purchase commitments;
- agreements and options to buy back assets previously sold; and
- assets pledged as collateral.



## Appendix 3 – Draft letter of representation

### Compensating arrangements

There are no formal or informal compensating balancing arrangements with any of our cash and investment accounts. Except as disclosed in the financial statements we have no other lines of credit arrangements.

### Contingent liabilities

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements; and
- no financial guarantees have been given to third parties.

### Related party transactions

I confirm the completeness of the information disclosed regarding the identification of related parties.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements

### Post balance sheet events

Since the date of approval of the financial statements by the Audit Committee, no additional significant post balance sheet events that have occurred which would require additional adjustment or disclosure in the financial statements.

The Council has no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

### Specific representations:

The Council's contractual dispute regarding the value of the unitary payment for a PFI scheme referred to in note 28 to the financial statements. This dispute with Newmount Limited concerning the Paragon contract continues to be subject to negotiation. In particular any final settlement sum cannot yet be quantified.

I confirm that there has been no change to the risk transfer profile relevant to ongoing PFI contracts and that the 'off balance sheet' accounting treatment of these contracts is an appropriate interpretation of UK Generally Accepted Accounting Principles under Financial Reporting Standard 5 'Substance over Form'.

I confirm that this letter has been discussed and agreed by the Audit Committee on 24 September 2009.

Signed on behalf of Dudley Metropolitan Borough Council

Bill Baker  
Interim Director of Finance  
24 September 2009

Councillor Alan Taylor  
Chair of the Audit Committee  
24 September 2009

# Appendix 4 – Use of resources key findings and conclusions

The following tables summarise the three use of resources themes.

## Managing finances

<b>Theme score 3</b>	
<b>1.1 Does the organisation plan its finances effectively to deliver its strategic priorities and secure sound financial health?</b>	
Score	3
VFM criterion met	Yes
<b>1.2 Does the organisation have a sound understanding of its costs and performance and achieve efficiencies in its activities?</b>	
Score	3
VFM criterion met	Yes
<b>1.3 - Is the organisation’s financial reporting timely, reliable and does it meet the needs of internal users, stakeholders and local people?</b>	
Score	3
VFM criterion met	Yes

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## Governing the business

<b>Theme score 3</b>	
<b>2.1 - Does the organisation commission and procure quality services and supplies, tailored to local needs, to deliver sustainable outcomes and value for money?</b>	
Score VFM criterion met	3 Yes
<b>2.2 - Does the organisation produce relevant and reliable data and information to support decision making and manage performance?</b>	
Score VFM criterion met	2 Yes
<b>2.3 - Does the organisation promote and demonstrate the principles and values of good governance?</b>	
Score VFM criterion met	3 Yes
<b>2.4 - Does the organisation manage its risks and maintain a sound system of internal control?</b>	
Score VFM criterion met	3 Yes

## Appendix 4 – Use of resources key findings and conclusions

### Managing resources

<b>Theme score</b>	
<b>3.1 - Is the organisation making effective use of natural resources?</b>	
Score	2
VFM criterion met	Yes
<b>3.2 - Does the organisation manage its assets effectively to help deliver its strategic priorities and service needs?</b>	
Score	2
VFM criterion met	Yes

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# The Audit Commission

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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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