Minutes of the Audit and Standards Committee Meeting held on 26 September 2016

Present: Martyn Tittley (Chairman)

Attendance

Mike Davies (Vice-Chairman)	Philip Jones
William Day	Robert Marshall
Brian Edwards	David Smith
Michael Greatorex	Alison Spicer
Derrick Huckfield	Mike Worthington

Apologies: Councillors Derek Davis, OBE, Kevin Jackson, Diane Todd and Caroline Wood

PART ONE

33. Declarations of Interest

Councillor Alison Spicer declared an interest as a member of Staffordshire Pension Fund.

34. Minutes of the Meeting held on 27 June 2016.

The Chief Accountant explained that the meeting had had to be rescheduled to take place on the 26 September due to this being the first audit undertaken by the new external auditors and a couple of technical notional adjustments being made to the accounts.. The Committee were thanked for moving the meeting whilst the adjustments were finalised and it was noted that the meeting was still being held within the deadline of the 30 September.

The Chairman suggested that the September meeting in 2017 should take place towards the end of September to ensure that paperwork would be available beforehand.

There was a discussion in respect of ongoing concerns about the value for money that the council receives from external contracts/partnerships. Whilst there are a number of ways that this assurance is obtained the members asked that concerns in respect of Infrastructure + be followed up with the appropriate scrutiny chairman.

Resolved: That the
- minutes of the meeting held on the 27 June 2016 be confirmed and signed by the Chairman.
- Committee Chairman write to the Chairman of the Prosperous Staffordshire Select Committee seeking reassurances regarding the scrutiny of the contract with Amey and Infrastructure Plus.

35. Joint Annual Governance Statement

The Chief Internal Auditor discussed the Annual Governance Statement prepared in line with guidance issued by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Society of Local Authority Chief Executives and Senior Managers (SOLACE) which detailed what the Committee was responsible for, the aim of the governance framework, the governance framework itself, the review of how effective the governance framework was and to highlight any significant governance issues. The document was required on an annual basis.

Section three of the report detailed the systems, policies, procedures and operations in place to ensure an effective governance framework. The report detailed the review undertaken to ensure that effective governance was operational. Actions contained within the 2014/15 Statement were outlined within the report and the annex to the report contains there actions taken. An unqualified annual audit letter for 2014/15 had been received and the outturn report from internal audit had been received which gave an adequate opinion. Other reasons to have confidence that there was effective governance in place included; no issues having been reported through to the Monitoring Officer or the Chief Financial Officer under their official powers, effective scrutiny in place through the Select Committees, appropriate action plans implemented to strengthen controls, the risk register continued to be revised as the operating model continued to develop and a low number of complaints. Significant governance issues highlighted for 2015/16 would be taken forward by the officer Corporate Governance Working Group included seven key pieces of work as detailed within the report. These significant issues would be monitored by the Group and where appropriate included in the Strategic Risk Register.

Whilst the work in respect of governance arrangements was praised there remained a concern that there are risks in the number of decisions that are taken by individual Cabinet members as opposed to all the information being made available to and the decision being made by the full Cabinet. This was a concern raised previously by Corporate Review but remained a concern to date.

The Director of Finance and Resources explained that the rational behind Delegated decisions was about being more effective and efficient in decision making. In addition to matters that are delegated to each Cabinet member there are occasions when a collective decision of the whole Cabinet was required in respect of overarching direction and intent but for reasons of effective and efficient decision making the detail in respect of that decision is considered and the decision made by the appropriate Cabinet Member. This was in accordance with the County Council's arrangements which were consistent with good practice guidance.

Whilst there are, in addition, informal ways that decisions are discussed by all Cabinet members the concerns for individual Cabinet members remained using the issues around the Better Care Fund (BCF) as an example.

Concerns were also raised in respect of the quantity and complexity of the issues that the County Council needed to respond to within limited resources, particularly time.

The Sustainability and Transformation Plan (STP) in respect of how local authorities and Clinical Commissioning Groups (CCGs) could spend NHS money was one example but there are many others.

Resolved: That the

- Audit and Standards Committee approve the Annual Governance Statement.
- Chairman of the Audit and Standards Committee write to the Leader of the Council regarding the Committee's concerns in relation to delegating decisions to one Cabinet Member, in particular making reference to recommendations made previously by Corporate Review and concerns regarding the BCF.

36. Statement of Accounts

The report was introduced and the slides circulated to the Committee prior to the meeting explained the format, content and the rules that existed for the Statement of Accounts and highlighted some of the key points in relation to the 2015/16 accounts.

The County Council had £1.2 billion yearly gross expenditure. To comply with the rules of local government accounting the accounts have to apply with international standards and a range of notional transactions had had to be included to demonstrate compliance with international standards. These notional transactions are then reversed out, complicating the accounts.

In response to a question, the Chief Accountant clarified that there were two schools funded through PFI mechanisms in the 2015/16 year of account, neither of which had transferred to academy status. Looking to the future, one school was likely to move to an academy and the implications of this were being considered. The arrangements would be dependent on who would continue to receive the funding for the borrowing. If this went to the academy the liability under the contract would also move to the academy. It was uncertain if this would be the case however as two schools were let as one contract and this contract would therefore need to be separated. The funding for borrowing would follow where the liability fell so there would be no impact on the Council however there would be notional adjustments to be made which would then need to be reversed out.

In response to a question, the Director of Finances and Resources explained that although it was too early to say what the impact of Brexit would be, the Pension Fund since Brexit had increased in its value because of increased stock market valuations. There was uncertainty about the impact in the medium term but in the short term the biggest impact of Brexit had been on exchange rates rather than the value of assets. Most commentators anticipated that there would be a negative impact in medium term growth but the long term impact would depend on the alternative arrangements secured with the markets in Europe post Brexit.

In response to a further question in respect of PFI, the Chief Accountant reassured the Committee that the previous accounting treatment which was based on a set of assumptions and judgements on the contract was correct. The accounting was not wrong but the interpretation of the clauses in the PFI contract had changed as the external auditors had had a slightly different view of the assumption around the operator's income from third parties. Any waste to resource plant would generate electricity and the income from this had to be treated as either due from the County Council or from users. The interpretation of what was a user had been questioned. The external auditor's interpretation of a user of the plant meant that the notional liability needed to be split. The PFI asset was shown notionally in the County Council's assets and this had to be balanced against a finance lease. The interpretation placed by the external auditors meant that the liability had to be split between that which was related to the finance lease and that which was related to other third party operators. The issue came down to the interpretation of how the notional asset was funded, how much from the County Council and how much from the third party user. This resulted in many debates and the cost of service and cost of financing having to be split, however this was purely notional as the PFI asset was not yet the County Council's. By the time the decision had to be made, the papers had had to be sent out to the Committee so the decision was made to defer the date of the Committee. The process would be much more straightforward next year as the interpretation had now been agreed.

In response to a question regarding the moving of un-useable reserves to useable reserves to cover the loss on the transfer of school premises for example, the Chief Accountant explained that un- useable reserves were the opposite entries for the notional accounting adjustments that had to be put through. For example the pensions liability did not, under the rules, have to be funded one hundred percent as there was time under the Local Government Pension Scheme to put the pension contributions aside, however, in reflecting the notional entry on the balance sheet there had to be an opposite entry. The same applied for asset accounting as this was a notional transaction which needed an opposite entry. The un-useable reserves were not cash backed. Within the cash backed reserves, money was earmarked for specific periods. For example where the County Council had to pay out on claims or pay for other capital obligations money had been put into earmarked reserves. Earmarked reserves were for a specific purpose in accordance with the scheme of management. The surplus from previous years was called a general reserve. There was never a transfer between cash backed and non cash backed reserves.

A question was asked whether the general fund balance of £11.9 million was adequate considering that CIPFA had previously recommended that a 3-5% of managed turnover should be what was reserved.

The Chief Accountant explained that the general balance had to be spent when required. It was acceptable to spend on any deficit from general balances provided that there was a credible plan to repay the balances over a reasonable period. Due to overspend on care services general balances had gone down, however in 2016/17 the Council had budgeted for a contribution to go back into the balances of around £6 million. Taking a long term view, the general balance would be brought back more in line with the assessed requirement. However rather than a 3-5% in balances a better approach to determine this amount was to consider the risk associated. The better the risk assessment, the more money could be put into earmarked reserves and the less money was needed in general balances. An assessment had been undertaken of unknown risks and this had suggested that the County Council needed in the region of £18 - £20 million of available resources to fund these issues. When the contribution back into balances in 2016/17 was taken into account, together with an in year contingency provision of £2 million a year, over a five year period this was an addition

£10 million of available resource. There was satisfaction that there was enough general resource to address risks assessed as part of the medium term financial strategy.

In response to a question, the Corporate Finance Manager explained that where schools converted to academies in legal terms the building and land was let on a long term lease of one hundred years or one hundred and twenty five years to the academy. The Council therefore no longer controlled the asset and the building was removed from the balance sheet. The land was kept on the balance sheet however as the Council still legally owned this but the value of the land was reduced to £1 to represent that the County Council could not have any say in how the land was used.

In response to questions in respect of the County Council's interest in Entrust the Chief Accountant confirmed that in 2015/16 there was no dividend from Entrust. The Corporate Review MTFS Working Group would be considering when there was likely to be a dividend and how much that was likely to be. This would depend on the trading activity and performance of the company. Regarding the investment in Entrust, this was contained within long term investments on the balance sheet at Note 12 to the Accounts. The £53.7 million was made up of the Treasury Cash Investment of £30.4 million and the investment which the County Council held in Entrust which was £23.3 million.

Resolved: That

- Approval be given to the 2015/2016 Statement of Accounts as included in the Committee papers.
- Approval be given to the letters of representation from the Director of Finance and Resources.

37. Report to those charged with Governance

Steve Clark, Ernst and Young LLP, explained that the document presented concluded the first year of Ernst and Young's appointment as auditors to the County Council and Pension Fund. Thanks were expressed to the County Council's team in supporting the process. Overall the audit had gone well. He highlighted in terms of the opinions, an unqualified audit opinion was being issued in both financial statements in accounts terms and the value for money statement. This did not happen everywhere. Once the Committee had approved the accounts and the letters of representation the accounts could be signed. The auditors had not received any objections from members of the public and there were no unadjusted audit differences. There had been a number of audit adjustments, the major one relating to the PFI scheme which had been explained in detail earlier in the meeting by the Chief Accountant. In terms of materiality, the level to which the audit work was focussed had been discussed with the Committee previously and was referred to in the report under the scope and materiality section and there was no change to this. The external auditors had initially identified two significant risks, the risk of management override and the risk of revenue and expenditure recognition. These were standard significant risks identified in any audit of any organisation. As a result of going through the detail of the PFI, the PFI had also been classed as a significant risk because of the level of focus on this. This matter had been dealt with however and it was not anticipated this would be an issue in the future. The other area of significant work undertaken was in relation to value for money. A number of procedures had been undertaken to understand the arrangements that the County

Council had in place to secure value for money. The external auditors had examined a number of things specifically related to the BCF up until the 31 March 2016 and the auditors had concluded that they were satisfied with the arrangements that the County Council had in place.

Mark Surridge, Ernst and Young LLP, explained that the audit had commenced with two significant risks over the financial statement. The extent of the work that the external auditors planned to perform in relation to the significant risks was set out in the report, and the Committee could take assurances from work that the external auditors had undertaken. Assurance was given that there was no issues to report in relation to the significant risk that management may override controls and manipulate the financial statement in a way that they should not. Secondly, regarding the significant risk around expenditure recognition which was essentially the undercounting of expenditure to manage the financial position incorrectly, a variety of procedures had been undertaken to give the Committee assurance that the expenditure in the financial statement was not materially misstated. The PFI work was very technical and took time to conclude due to the nature of interpretation and judgement required. There were some adjustments to the accounts but none of the adjustments impacted on the County Council's general fund as they were all financial reporting technical adjustments that mostly moved figures around the accounts but did not affect the overall financial resilience of the organisation.

A Member referred to the Governance Statement which had stated that to achieve savings and do more and better for less, a Challenge Board had been set up including the Deputy Leader, Chief Executive and Director of Finance and Resources. This Board was responsible for finding savings and value for money. The auditors' key findings however identified significant risk that insufficient arrangements were in place to identify savings to bridge the financial gap. It was queried if the present arrangements were insufficient or if the governance system was working well in finding these savings?

It was explained that because of the scale of the savings that the Council was working towards and the challenges that the Council faced this had been identified as a significant risk that the Council may not have had arrangements for. The auditors however had looked at the arrangements in place and operating up until the 31st March 2016 and concluded that the arrangements were adequate at that point in time.

The Member raised concern that the term insufficient had been used and the auditor clarified that the information meant that there was a significant risk that the arrangements may not be in place. Further work was undertaken to determine if the arrangements were adequate and the auditors believed that they were. This did not mean that there was not a significant risk but that the arrangements in place were adequate.

Caroline Davies, Ernst and Young LLP, discussed the high level messages in the audit report for the Pension Fund. At the time of writing the auditors were awaiting the Pension Fund's Annual Report which had now been received and it was anticipated that audit procedures would be completed in time for the Pensions Committee in October. There were no unadjusted differences that auditors wished to present. There were however two minor changes to the statements, one in regard to the contributions and one in regard to an updated valuation. One significant risk had been identified which was in relation to management override and there was nothing the auditors needed to bring to the Committee’s attention regarding the work undertaken on that particular risk. One further risk was identified in regard to the valuation of complex investments which were more judgemental in nature, for example hedge funds and private equity. The detailed work to give assurance in this area was detailed in the report and there was nothing that needed to be brought to the Committee’s attention.

In response to a question in respect of BCF income, the Director of Finance and Resources reported that the Council was still in an escalation process with the Department of Health around the BCF. Nothing had been received through the BCF in the current financial year and the Cabinet had therefore put in place controls on non essential spending to compensate. The resolution of the escalation process had not concluded but from a financial planning point of view a Cabinet report, which had been Called In by scrutiny, identified a series of savings to compensate if the money was not received going forward. There were £4 million in savings in the current year, rising to £14 million in a full year. Financially the assumption was that the County Council would get nothing out of the BCF after the current financial year because it was prudent to do so, but if the escalation did secure some money for the Council this would enable money to be put back into the Council for health and care or other priorities. Over the medium term the Sustainable Transformation Plan process was the mechanism in which the Council, in accordance with national guidance, could get greater NHS contributions towards adult social care.

In response to a member question in respect of whether the council tax increase had been sufficient to cover the shortfall in funding from the health economy the Director of Finance and Resources clarified that the extra 2% on Council Tax was the Staffordshire taxpayers contribution to adult social care. This was separate to the BCF monies which were intended to be the the NHS contribution towards adult social care.

Resolved: That the Committee
- Note the Staffordshire County Council Audit Results Report – ISA (UK and Ireland) 260 for the year ended 31 March 2016.
- Note the Staffordshire Pension Fund Audit Results Report – ISA (UK and Ireland) 260 for the year ended 31 March 2016

38. Code of Corporate Governance

The Head of Democracy acknowledged the work undertaken on the item by the Chief Internal Auditor. Previously it had been brought to the Committee’s attention that there had been changes to the guidance around corporate governance and the County Council was looking to introduce these changes. The assessment of the old principles compared to the new principles was included in the report. A new single page diagram of the key methods by which the Council assures itself that all was working properly was also included. There was more work to do to assure that the evidence was available to show how well the arrangements were embedded, where there were issues that needed to be reflected on and the development of a new action plan to address any such issues. . Members were asked to note that there was more work to do and that there would be further report to the Committee on progress.

Resolved: That the Committee

- Note the updated Code of Corporate Governance and the revised Single Sheet Local Framework.
- Note the progress on developing the Corporate Governance Action Plan 2016/17.

39. Future External Audit Procurement

The Chief Internal Auditor referred to reports previously shared with the Committee following the decision to close the Audit Commission and to end its role in appointing the external auditor. Original transitional arrangements for the appointment of all external auditors within the public sector and for the setting up of audit fees were extended, for one more year – 2017/18. , The Council had received confirmation that Ernst and Young LLP would continue as the external auditor for that period. When the transitional arrangements end on the 31 March 2018 each Council has the ability to move to local appointment of the external auditor. The County Council and Pension Fund should appoint an external auditor for the 2018/19 financial year by December 2017. There were three broad options available, firstly to make a stand alone appointment via an auditor panel, secondly to set up a joint auditor panel or undertake joint procurement arrangements with other public sector bodies within the particular area or thirdly to opt into a sector led body arrangement. The Local Government Association had lobbied for a sector led body to be established to potentially procure future audit contracts. This body would have the ability to negotiate contracts nationally, potentially maximising opportunities to procure sustainable external audit arrangements on behalf of the whole sector. In July 2016 it was announced by the Department for Communities and Local Government that Public Sector Audit Appointments Limited had been named as the sector led body and that the first appointments made by this body would be for 2018/19. The advantages and disadvantages of each option were outlined in the Committee paper, including a detailed question and answer paper published by Public Sector Audit Appointments Limited. CIPFA had produced guidance on setting up an auditor panel which organisations would need to adhere to when making their own appointments and also if a joint auditor panel was set up. A sector led body could provide the opportunity to potentially obtain greater scales of economy. The County Council had until 2017/18 to make an appointment but in practical terms this meant that one of the options had to be deemed as the favourable route by December 2016. Public Sector Audit Appointments Limited would be looking to issue the invitation to join the sector led body by December 2016 which would give organisations eight weeks to decide whether to go down this route. Contract negotiations would then commence in Spring 2017. Over two hundred and seventy public sector bodies had said that they would prefer the Public Sector Audit Appointments route to do the procurement on their behalf when consulted. The Council is required to take action to appoint the external auditor from April 2018. The appropriate route for the organisation would need to be approved by Full Council following a decision by the Audit and Standards Committee. The recommendation to the Committee was for the Council to opt for the forthcoming cycle of appointments to be undertaken by the Public Sector Audit Appointments route.

Resolved:
That the Committee recommend that Full Council 'opt-in' to the Local Government Association Sector Led Body approach via Public Sector Audit Appointments Ltd for the procurement of the External Audit contract for the financial year commencing April 2018.

40. Work programme 2016-17 for the Audit and Members Standards Committee

A Member asked if the Committee could consider if the Council should have an appeals process for decisions made by Officers in the field of licensing or contracts. It was suggested that there should be some further right of appeal as people currently could only make a complaint to the Council and then take the matter to the Local Government Ombudsman or to Judicial Review. It was requested that the possibility of setting up an appeals panel could be explored.

The Committee Chairman clarified that for the normal taxi driver function, taxi drivers had a right of appeal to the Magistrates Court. The regulated work referred to scenarios when drivers were carrying vulnerable people. He understood that in this scenario there was an appeals panel of two people who played no part in the decision making process, however this panel did not include Members of the Council. He undertook to discuss this matter with Officers.

A Member referred to a letter from the Committee to the Leader of the Council asking him to consider setting up a position of a Cabinet Member without a portfolio to focus on the financial position of the Council and Entrust. It was queried if a response had been received.

The Chairman confirmed that a reply had been received and it had been considered that there were enough checks and balances in place, including the Overview and Scrutiny Committees, and the Council therefore did not require a Cabinet Member without a portfolio.

There was a discussion in respect of the optimum time for training members in respect of changes to local government funding. It was agreed that this training was best arranged for after the elections and when there was sufficient detail available as to what was to change, how these changes affected the County Council and when the changes would be coming into force.

Resolved:
That the Committee Chairman discuss the process for appeals in relation to regulated work with Officers and report back to the Committee on this matter.

41. Exclusion of the Public

The Chairman moved that the public be excluded from the meeting for the following items of business which involved the likely disclosure of exempt information as defined in the paragraphs of Schedule 12A (as amended) of Local Government Act 1972.

42. Internal Audit Reports - Limited Assurance Review Update

Exemption under Paragraph 3

Chairman