

<b>AUDIT AND ASSURANCE COMMITTEE</b>	<b>Paper No.</b>
<b>Meeting date: 26 September 2012</b>	
<b>From: CORPORATE DIRECTOR – RESOURCES AND ACTING ASSISTANT DIRECTOR - FINANCE</b>	

## **STATEMENT OF ACCOUNTS 2011/12 – CUMBRIA COUNTY COUNCIL AND CUMBRIA LOCAL GOVERNMENT PENSION SCHEME**

### **1.0 EXECUTIVE SUMMARY**

- 1.1 *The Unaudited Accounts for the County Council and the separate Cumbria Local Government Pension Scheme (CLGPS) 2011/12 were published on 29<sup>th</sup> June, having been authorised by the Acting Assistant Director – Finance in line with the Accounts and Audit Regulations 2011, after consultation with the Chair and Vice-Chair of the Committee.*
- 1.2 *The Audit Commission has now substantially completed its audit work. The Audit Commission will present their Annual Governance Reports to the meeting (Agenda Items 7 and 8). This report presents for both sets of accounts:*

*Letters of Representation  
providing assurance to the  
Audit Commission*

*Appendix 1a – County Council  
Appendix 1b – CLGPS*

*The Statements of Accounts  
(as amended for the audit  
findings)*

*Appendix 2 — Note: CLGPS from  
page 165 to 216*

*Actions Plans in response to  
the Annual Governance  
Reports' recommendations*

*Appendix 3a – County Council  
Appendix 3b – CLGPS*

## **Key Messages**

- 1.3 ***The key messages of the Annual Governance Reports are that the District Auditor intends to issue an unqualified (clean) audit opinion on both sets of 2011/12 Accounts.***
- 1.4 ***The District Auditor also intends to issue an unqualified Value for Money conclusion for Cumbria County Council in respect of securing economy, efficiency and effectiveness in the use of resources.***
- 1.5 ***The Annual Governance Report for the County Council's accounts comments on the further improvement in the quality of the accounts with fewer amendments than in previous years and much improved supporting working papers to a good standard. There was particular improvement on capital accounting, which had been an issue in recent years. Overall, the limited number and the nature of the amendments reflect the significant improvements that have been made in the Council's closedown processes and the strengthening of technical accounting capacity.***
- 1.6 ***The draft accounts contained only one material error in the primary statements (in the Cash Flow Statement) and one material classification error within the Group Accounts. This was the first year that the Council's three PFI/PPP schemes had to be fully accounted for and these required some non-material amendments to the Comprehensive Income and Expenditure Account. None of the changes affected the final General Fund balance or Earmarked Reserves, which remain as reported to Council at its meeting of 21st June at £15.756m and £88.261m respectively.***
- 1.7 ***There were a small number of other adjustments to the unaudited accounts published in June, which in the main relate to improvements in presentation. There were a few corrections to amounts in the disclosure notes but with no net overall impact. While the aim is to provide a completely "clean" set of accounts, it would be exceptional for any authority not to have some amendments to their unaudited accounts given the scale of the exercise resulting in a 225 page document, the complex requirements of the International Financial Reporting Standards and the short time period for completion.***
- 1.8 ***The Annual Governance Report for the Cumbria Local Government Pension Scheme comments that the accounts were again prepared ahead of the statutory deadline and were supported by working papers prepared to a high standard. The accounts contained no material errors to the primary statements. Some material amendments were required to the detailed disclosures on investments, but these did not affect the overall net investment position for the 2011/12 year.***
- 1.9 ***The Audit Committee will be required to approve the audited set of accounts at this meeting in accordance with the Accounts and Audit Regulations 2011.***

- 1.10 *The Committee is also asked to consider the Letters of Representation (Appendices 1a and 1b), which provide the Audit Commission with assurance on the financial statements and governance arrangements upon which they will base their audit opinion. The Regulations require the letters to be signed by the Acting Assistant Director – Finance, as the S151 Officer on behalf of the Authority.*
- 1.11 *The Action Plans arising from the Audit Commission's findings (Appendices 3a and 3b) will contribute to the continuous improvement in the quality of the accounts and value for money for 2012/13. The Action Plan for the County Council will be reported to the Committee at its meeting on 7<sup>th</sup> December, 2012.*

## **2.0 POLICY POSITION, BUDGETARY AND EQUALITY IMPLICATIONS, AND LINKS TO COUNCIL PLAN**

- 2.1 *The delivery of action plans in response to the findings of audit reviews is essential to ensure the improvement in internal control systems and to ensure that the Council's resources are properly applied, risks are appropriately managed and Council Plan outcomes are achieved.*

## **3.0 RECOMMENDATION**

- 3.1 *Members are asked to:*

- a) Note the contents of this report.*
- b) Consider the matters set out by the District Auditor in the Annual Governance Report in relation to Cumbria County Council (Agenda Item 7). In particular, to note:*
  - i) The Key Messages (Page 3)*
  - ii) Appendix 2 of that report – Uncorrected errors and uncertainties, together with the associated comments of the Acting Assistant Director -Finance in the Letter of Representation (Appendix 1a)*
  - iii) Appendix 3 of that report – Corrected errors*
- c) Consider the matters set out by the District Auditor in the Annual Governance Report – Cumbria Local Government Pension Scheme Audit 2011/12 (Agenda Item 8). In particular, to note:*
  - i) The Key Messages (Page 3)*
  - ii) Appendix 2 of that report – Uncorrected errors and uncertainties, together with the associated comments of the Acting Assistant Director -Finance in the Letter of Representation (Appendix 1b).*

**iii) Appendix 3 of that report – Corrected errors.**

- d) Approve the Letters of Representation on behalf of the Council in respect of the two sets of accounts to enable the District Auditor to issue audit opinions on the accounts. (Appendices 1a and 1b).**
- e) Authorise the Acting Assistant Director –Finance, as the Council's Section 151 (Local Government Act 1972) Officer to sign the two sets of accounts on behalf of the Council. (Appendix 2).**
- f) Approve the Cumbria County Council Accounts 2011/12 which incorporates the Cumbria Local Government Pension Scheme Accounts (Appendix 2).**
- g) Authorise the completed Action Plan to the Annual Governance Report for the CLGPS (Appendix 3b) and note the proposal for the County Council Action Plan (Appendix 3a) to be reported to the Audit & Assurance Committee at its meeting on 7<sup>th</sup> December, 2012.**

## **4.0 BACKGROUND**

- 4.1 The Unaudited Accounts for the County Council and the Cumbria Local Government Pension Scheme (CLGPS) were published on 29<sup>th</sup> June, having been authorised by the Acting Assistant Director – Finance in line with the Accounts and Audit Regulations 2011. The Chair and Vice-Chair of the Committee have been briefed throughout the accounts closure process and were consulted before the publication in June.
- 4.2 The Audit Commission has now substantially completed its audit work and at this meeting will present the Annual Governance Reports for 2011/12 in respect of the two sets of accounts. This covering report summarises the Audit Commission's findings. It does not add commentary or further explanation to their reports, but summarises key messages and provides some context.

### **Statement of Accounts – Cumbria County Council**

- 4.3 2011/12 is the second year that the accounts have been prepared under a full International Financial Accounting Standards (IFRS) basis. The Audit and Assurance Committee will note the length of the accounts has continued to increase and it totals 225 pages. The Council's accounts contain 55 disclosure notes in support of the four statutory statements. While the changes in accounting requirements were not as extensive as those required by the introduction of IFRS last year, there were some changes. These included the introduction of a separate asset class for heritage assets and componentisation of additions to property, plant and equipment, as well as the need to account fully for the Council's three Private Finance Initiative (PFI/PPP) schemes which came into fruition this year.
- 4.4 In summary, the Annual Governance Report (contained at Agenda Item 7 on today's Agenda) comments on the continuing improvement in the quality of the accounts and the supporting working papers, with fewer amendments

than in previous years and much improved supporting working papers prepared to a good standard. There was particular improvement on capital accounting, which had been an issue in recent years. The draft accounts contained only one material error in the primary statements (on the Cash Flow Statement) and one material classification error within the group accounts, discussed below.

- 4.5 The Auditor's findings on the financial statements are set out on pages 6 to 11 of the Annual Governance Report and in its appendices 2 and 3. These include "Uncorrected Errors" that are commented upon by the Council in the Letter of Representation (Appendix 1a). The Auditor highlights one of the unadjusted items that relates to a liability arising from historic claims on the Municipal Mutual Insurance (MMI) scheme of arrangement, under which the Council shares the risk on potential insurance claims for events prior to MMI's dissolution in 1992. A recent decision in the Supreme Court has increased the likelihood that MMI will no longer be able to achieve a solvent run-off which would mean that MMI Scheme Creditors such as the Council would become liable for a proportion of the liabilities. At the time of writing the scheme of arrangement had not been triggered and neither the amount nor the timing of the Council's share of the liability are known. Estimates based on the latest published accounts from MMI indicate a liability in the region of £0.560m. This is not a material sum in the Council's overall accounts and if it arises will be funded from the Insurance Reserve, which exists to cover insurance uncertainties, and consequently will have no direct impact on the General Fund balance.
- 4.6 The Audit Commission report highlights other "Corrected Errors"; errors that have resulted in changes to the accounting statements. These include one material error in the primary statements; this was in the Cash Flow Statement and arose from some errors in classifying long term debtors and investment transactions that although less significant in themselves became material when accumulated. The other material error was identified in the Group Accounts and arose from the presentation of the Exceptional Items in the County Council Accounts not being fully followed through to the Group Accounts.
- 4.7 Accounting for the Council's three PFI/PPP schemes for the first time in 2011/12, was recognised in the Council's planning as a particularly complex area and PWC were employed as recognised experts to advise. It is disappointing that there were nevertheless some amendments required to the Primary Statements, in particular an adjustment of £6.5m between the net cost of services and an equivalent reduction in capital expenditure funded from revenue. The errors arose from a combination of factors including errors in the accounting models, mis-interpretation for the specific accounting entries required and the complexity of the area reducing the opportunity for quality review by others not directly engaged in the work, as happens for other aspects of the accounts. The auditor also identified that within the disclosure notes, the increase in PFI liability (£71.6m) was wrongly shown as reducing the Capital Financing Requirement i.e the amount of spending incurred but not yet financed. This was simply due to the entry being on the wrong line within a disclosure note table and it had no impact on the reported value of the Council's net assets or the assessment of

financing requirements. None of the PFI changes affected the General Fund balance or Earmarked Reserves and the models provided by PWC will support the ongoing accounting treatment for these schemes in future years.

- 4.8 Other adjustments to the unaudited accounts published in June mainly relate to improvements in presentation. A few are corrections to amounts but with no net overall impact on the primary statements. While the aim is to provide a completely “clean” set of accounts, these adjustments should be seen in the context of a 225 page document and the complex accounting requirements of the International Financial Reporting Standards.
- 4.9 Overall, the limited number and the nature of the amendments reflect the significant improvements that have been made in the Council’s closedown processes and the strengthening of technical accounting capacity. The capital accounting arrangements were flagged by the Audit Commission in its report to the Committee in June as a significant risk for the Council in completing its accounts. However, the arrangements put in place, using a spreadsheet rather than the e5 asset module as agreed by the Committee in March, proved a solid basis for the handling the complex asset accounting requirements. While it is disappointing to have any errors, the planning of the accounts process and adherence to timetable allowed more quality review than previous years. The introduction of electronic working papers assisted both the closedown work and the ready access to information for the Audit Commission. These improvements provide a strong basis for next year.
- 4.10 The Audit Commission’s report includes only one recommendation regarding the Statement of Accounts. This relates to valuation and lifecycle cost information for the PFI schemes. It is proposed to establish what information is required to be provided by the contracts and to come to an agreement with the operators, subject to consideration of any cost implications.
- 4.11 The key messages of the Council’s Accounts 2011/12 are set out in the Explanatory Foreword to the Statement of Accounts (Appendix 2, pages 1-13 ). Some headlines from the Accounts are as follows:-
- Increase in General Fund Balances of £0.889m
  - Increase in Earmarked Revenue Reserves of £19.203m, which includes:
    - £10.670m for grants that have been received in 2011/12 but which will not be applied until future years (mainly PFI)
    - £12.700m for school and DSG reserves that are ring-fenced for future spending on schools
    - -£6.016m utilisation of the Equal Pay and Modernisation Reserve
  - Increase in the net book value of Property, Plant and Equipment of £79.161m which includes additions of £182.020m (of which £87.036m relates to PFI schemes), disposals of £69.168m and revaluation decreases of £31.145m.

- Two exceptional items within the Comprehensive Income & Expenditure Statement with a net effect of £6.988m. These relate to pension costs as a result of staff transferring to academy schools and the closure of the former Capita contract. These transactions have not affected the General Fund balance.
- Post Balance Sheet Event - The new West Lakes Academy building was handed over to the governors on 12th April.

### **Statement of Accounts – Cumbria Local Government Pension Scheme**

- 4.12 The Council's Accounts contain the Statement of Accounts of the Cumbria Local Government Pension Scheme. The separate Annual Governance Report for the CLGPS (Agenda Item 8) summarises the findings from the Audit Commission's review of the draft CLGPS Accounts for 2011/12.
- 4.13 CIPFA produced guidance on a new format for the Pension Scheme Accounts for 2011/12, which involved a major re-ordering of the financial statements and the disclosure checklist increasing from 6 to 17 pages. Where appropriate the new formats have been adopted. The draft format was discussed and agreed with the Audit Commission during March and April 2012 and the CLGPS accounts have increased from 28 pages in 2010/11 to 52 in 2011/12 as a consequence.
- 4.14 The Auditor's Annual Governance Report finds that the Accounts for 2011/12 were prepared and available for audit ahead of the statutory deadline and that they were supported by working papers, that were, as in previous years, prepared to a high standard.
- 4.15 The accounts contained no material errors affecting the primary statements. However, there were some material amendments required to the analysis within the investment disclosure notes. These amendments included the reclassification of investments and the removal of statutory debtors, creditors and certain provisions from the financial instruments disclosures. There was no affect on the overall total net investment position for the 2011/12 year.
- 4.16 The Annual Governance Report notes one "Uncorrected Error" which is commented upon by the Council in the Letter of Representation (Appendix 1b). The error relates to Managed Funds of £2.581m that were incorrectly classified as Equities in the 2010/11 accounts. Correction for the closing balance in 2011/12 results in the movement between years not reflecting the true movement, which is regarded as an uncorrected error.
- 4.17 The amendments that have been made to the unaudited accounts are set out on pages 20-23 of the Annual Governance Report.
- 4.18 The Auditor's report makes three recommendations to strengthen processes for future years. These are set out in the report and in the Action Plan for the CLGPS. (Appendix 3b). The recommendations relate to extending the reconciliation of investment classifications between the disclosure notes and the holdings recorded in the Custodian's report; retaining evidence of values as well as the number of units when there are transfers between portfolio's;

and the publication of extended information on compensation paid to key managers. The last of these includes publication of information on accrued pension benefits, which goes beyond what is required for the County Council accounts and is the subject of contention nationally among local government pension schemes. There is no consensus on this at present.

4.19 A comprehensive report on the performance of the Cumbria Local Government Pension Scheme in 2011/12 will be provided in the Annual Report which is to be published by December 2012 and will be available on the Council's website before this. Key headlines from the CLGPS accounts are as follows:-

- Net assets increased by £66m to £1,466m.
- The Fund returned 5.3% for the twelve month period, which was a little below the scheme benchmark of 6.5%, but above the LGPS average of 2.6% resulting in the annual Pension Scheme investment performance being ranked in the top quartile at 13th out of 100 in the WM LGPS Universe as at 31st March 2012.
- Performance over the mid (5 years) to longer term (10 years) ranks within the top 40% of Local Government Schemes in the country.
- A funding level of 70% at the interim valuation at 31<sup>st</sup> March 2012, reflecting the ongoing turbulence in financial markets and the inflationary impact on the scheme liability.
- Post balance sheet event - Management of the global equity portfolio with Newton Investment Management Ltd was discontinued in April 2012. The assets will be held on a passive basis while a full procurement process is undertaken to appoint a new manager.

### **Value for Money**

4.20 The Annual Governance Report – Cumbria County Council sets out audit findings in relation to the Value for Money assessment (pages 12 to 18). The District Auditor intends to issue an unqualified conclusion stating that the Council had adequate arrangements in place to secure economy, efficiency and effectiveness in the use of resources during 2011/12. The commentary sets out several recommendations for further improvement, which require further consideration by Corporate Management Team to develop a completed Action Plan. This will be reported to the next meeting of the Audit and Assurance Committee on 7<sup>th</sup> December, 2012.

4.21 While the report recognises the Council's achievement in delivering £44m savings in 2011/12 two recommendations are made to improve the monitoring and reporting of savings. Improvements are already being considered for the way large value savings are monitored and reported within the quarterly Corporate and Directorate Scorecards. The Quarter 1 report for 2011/12 noted that work is being carried out to improve the



tracking of savings for Quarter 2. These arrangements will be given further consideration in the light of the audit findings.

- 4.22 Several Audit recommendations relate to contract management. These mainly reflect issues referred to in the Annual Governance Statement 2011/12 and Action Plan 2012/13. An update on progress in delivery of these actions is contained elsewhere on today's agenda. The recommendations in the Audit Commission's Annual Governance Report will be considered by the Corporate Management Team and an Action Plan will be developed and reported to the Committee in December. This will include consideration of how to strengthen the reporting to Members of contract performance within the existing reporting framework for budget monitoring, performance and risk management and Internal Audit report coverage on individual contracts and themes.

### **Letter of Representation**

- 4.23 Before issuing the opinion upon the Council's Accounts, in accordance with auditing standards, the Auditor is required to ask the Council for its written representations about the Council's financial statements and governance arrangements. The Audit and Assurance Committee is asked to confirm on behalf of the Council that the letter has been discussed and agreed, and authorise the Acting Assistant Director – Finance to sign the letter on behalf of the Council. The Letters of Representation in respect of the two sets of Accounts are attached as Appendix 1a and 1b.
- 4.24 A full copy of the updated, audited Statement of Accounts 2011/12 are attached to this report (Appendix 2) as a hard copy for Members attending the Committee. (Subs have been emailed a pdf copy). The draft, unaudited Accounts were published on the Council's website in June. The Audited Accounts 2011/12 will also be published on the website by the end of the week, upon receipt of the Auditor's opinion.

**Diane Wood**  
**Corporate Director – Resources**

**Julie Crellin**  
**Acting Assistant Director – Finance**

*21 September 2012*

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### **APPENDICES**

***Appendix 1a - Letter of Representation to the Audit Commission – Cumbria County Council***

***Appendix 1b - Letter of Representation to the Audit Commission – Cumbria Local Government Pension Scheme***

***Appendix 2 - Audited Statement of Accounts 2011/12 Cumbria County Council***

***Appendix 3a – AGR Action Plan Report - Cumbria County Council Audit 2011/12***

***Appendix 3b – AGR Action Plan Report - Cumbria Local Government Pension Scheme***

**BACKGROUND PAPERS**

N/A

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