

# AUDIT COMMITTEE

29 JUNE 2006

## STATEMENT OF ACCOUNTS 2005/2006 AND STATEMENT ON INTERNAL CONTROL 2005/2006

Director: Neil Davies, Director of Finance and Corporate Services

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### 1. Purpose of item

- 1.1 This report requests the Audit Committee to approve the Council's draft Statement of Accounts and the Statement on Internal Control for 2005/2006.

### 2 Recommendations

- 2.1. Members are requested to approve the Statement on Internal Control for signature and inclusion in the Council's Statement of Accounts for the financial year 2005/2006.
- 2.2. Members are requested to approve the draft Statement of Accounts for 2005/2006.

### 3 Background

- 3.1. The Accounts and Audit Regulations 2003 (the Regulations) require these accounts to be formally approved by the authority before 30 June 2006.
- 3.2. The Local Authorities (Functions and Responsibilities) (England) Regulations 2000 places a duty on Council or a designated committee to approve the statement of accounts which is a function that cannot be delegated to Cabinet. In accordance with CIPFA recommendations, Members recently agreed to set up this Committee with terms of reference including approval of the Statement of Accounts. In the first instance they are being presented to Cabinet on 27 June 2006, as the body charged with the executive management of the Council's budget, to make comment and recommend approval by this Committee. Members will be given an update at the meeting of the Cabinet's recommendation.
- 3.3. Local authorities are required under the Regulations to produce an annual statement of accounts that is subject to scrutiny by the external auditors. The auditor will give an opinion on the accounts and additionally interested persons have the right to inspect the accounts and make representations to the auditor. PricewaterhouseCoopers is responsible for the audit of accounts that must be completed by 30 September 2006.
- 3.4. Since the 2003/2004 final accounts there has been a requirement for the Council to comply with the standards and codes of corporate governance, and to report on the effectiveness of the Council's systems for risk management and internal control.

The Statement on Internal Control (SIC) has been updated annually to report on issues raised in previous audits and identify any new areas to be addressed.

- 3.5. Although incorporated within the Statement of Accounts there is a requirement that Members formally agree the contents of the SIC which must be signed by the Leader of the Council and the Chief Executive. The SIC also requires formal acceptance by Members and a separate recommendation is incorporated in this report for that purpose.

#### **4. Statement of accounts**

- 4.1 These documents are subject to detailed requirements as to content and style mainly prescribed by the Code of Practice on Local Authority Accounting and the Best Value Accounting Code of Practice (BVACOP).

- 4.2 In accordance with proper accounting practice, the statement of accounts includes the following elements which are subject to scrutiny by the appointed auditor:

- an explanatory introduction and statement by the chief financial officer;
- a statement of responsibilities which outlines responsibility for efficiently managing the affairs of the Council;
- a statement on internal control. As discussed above, this is a relatively new requirement designed to ensure effective systems of internal control;
- the auditor's opinion which is given at the completion of the audit and must occur by 30 September 2006;
- a statement of accounting policies which highlights practices adopted by the authority;
- the consolidated revenue account (CRA) which summarises the major items of expenditure and income, and shows further analysis where required;
- the housing revenue account (HRA) which summarises the major items of expenditure and income relevant to the account with supplementary notes where required;
- the collection fund which records council tax and business rate income and disbursements to precepting authorities (the council's own requirement, Kent Police Authority, Kent Fire and Rescue Service and parish councils) and payments to central government in respect of the contribution to the business rates pool;
- the consolidated balance sheet which shows the assets, liabilities and net worth of the authority. Explanatory notes are required for certain headings; and
- the cash flow statement which summarises the total transactions of the authority in cash terms.

- 4.3 The draft statement of accounts is attached as Appendix 1 to this report. The elements that may be of most interest to Members are the consolidated revenue account (CRA) and consolidated balance sheet which can be found on pages 14 and 28 respectively.

- 4.3 As stated previously, the presentation of the CRA is prescribed and is not the familiar format that Members are used to for the regular monitoring reports. In addition a number of technical adjustments have to be made to service headings to reflect the accounting requirements that are designed to make the accounts more compatible with general accounting practice throughout both public and private sectors. More significant amongst these adjustments are those in respect of

accounting for pension costs and the costs of capital. Both of these sets of adjustments have a net nil effect on the CRA overall but require costs to be allocated to service headings that are subsequently netted out through the appropriation or other 'below the line' adjustments. To assist Members in making the comparison to the more familiar format as shown on page 3, note 8 on page 18 provides a reconciliation between the CRA 'deficit' and the revenue summary.

- 4.4 Paragraph 3.1 refers to the audit of the statements being completed by the 30 September 2006. The actual audit of the statements is scheduled to commence at the end of July and clearly the statement of accounts that is presented for approval does not reflect any changes that this audit may require. If there are significant amendments to the statement of accounts these will need to be reported back to Members prior to formal publication.

## **5. Summary financial position for 2005/2006 (General Fund)**

- 5.1 Throughout the year, regular monitoring reports have identified the major variations from approved budgets. Earlier monitoring reports had forecast an overspending peaking at approximately £3m in September 2005. The final accounts now show a revenue underspend of £37,000 (summary on page 3 of appendix 1) and clearly, against this backdrop, the final position is a significant achievement. However, this achievement must be viewed against a backdrop of continuing overspends for Children's Services, Community Services and Corporate Provisions, approaching £3m, offset by underspendings in all other directorates and, in particular, an extremely favourable outturn for interest and financing. For Members information, some of the more significant variations to agreed budgets were:

### 5.1.1 Chief Executive

- The division met its vacancy saving target of £111,000 and achieved an underspend of £220,000 mainly as a result of staff vacancies contributing to the corporate aim of achieving a balance to budget.

### 5.1.2 Finance and Corporate Services

Despite facing considerable overspends predominantly as a result of increased benefit payments (£341,000), pay and grading allowances within Community Services Directorate (£207,000) and falling income from land charges and licensing (£236,000) the directorate has achieved significant compensating savings from Human Resources, ICT business units and staff vacancies to achieve a net underspend of £402,000.

### 5.1.3 Children's Services

- The gross overspend for the directorate is approaching £2.7m predominantly occurring in the following areas:
  - SEN Recoupment £567,000;
  - SEN Home to School Transport £631,000;
  - Independent/non-maintained schools & joint services provision group (JSPG) £272,000;
  - Independent Fostering £351,000; and
  - Looked after Children £204,000.

- The following major underspends have partially offset the above, resulting in a net overspend for the directorate of £736,000:
  - Children's staffing (ex Rochester Team) £370,000;
  - Policy Team £178,000;
  - Adoption service £156,000;
  - Section 17 – Children with Disabilities £126,000; and
  - Early Years Team £100,000.

#### 5.1.4 Community Services

- The gross overspend for the directorate is approaching £2.4m predominantly occurring in the following areas:
  - Physical Disability £675,000;
  - Leisure budget shortfall and trading deficit £481,000;
  - Learning Disability £299,000;
  - Adult and Community Learning £199,000;
  - Older People £157,000;
  - Community Centres £129,000; and
  - Homelessness £123,000.
- The following major underspends have partially offset the above, resulting in a net overspend for the directorate of £1.005m:
  - Adult Assessment and related services £318,000;
  - Private Sector Housing overheads £206,000;
  - Training £190,000;
  - Procurement and Exchequer £133,000;
  - Support services £129,000; and
  - Property and access points £108,000.

#### 5.1.5 Regeneration and Development

- The directorate has exercised tight control over those budgets with a history of volatility such as car parking income and expenditure and has not recorded any significant overspendings. However, Highways have recorded a £79,000 overspend due, in the main, to higher costs on winter gritting and maintenance costs of the Pentagon bus station. As previously reported there has been a constant pressure on the budget due to unplanned remedial works and the uncertainty of the weather.
- The directorate has achieved a net underspend of £523,000 from various budget headings but, more significantly, the following are one-off savings which will not be repeated in future years:
  - Insurance contributions £132,000 (saving taken as part of 2006/2007 budget setting); and
  - Concessionary Fares £198,000 from retrospective rebates of charges now incorporated in the base budget.

#### 5.1.6 Interest and Financing

- Treasury and cash management during 2005/2006 performed above expectations, generating a healthy surplus. Effective cash management ensured that during the period there were always cash balances to invest,

yielding returns that compared favourably with those of the authority's professional fund managers. As cash forecasting eliminated the necessity to borrow to cover the Council's cash flow, savings accrued from not having to incur overnight borrowing, nor pay brokers' fees to secure these funds. Coupled with earlier years' good practices in developing a wide range of options for short-term investments to suit differing economic outlooks, the in-house team were able to secure the best return against cash investments, whilst maintaining a risk averse strategy. The treasury outturn report also reveals that the 'in-house' treasury team outperformed both the professional fund managers we employ.

#### 5.1.7 Corporate Provisions

- This budget incorporates anticipated savings from the review of management and other staffing, unallocated savings target and income from PSA Reward Grant. The full year staff savings target and other savings were not achieved to the extent of the £642,000 previously reported. In addition the impact of the amending report for 2003/2004 has had to be incorporated in respect of the Government 'clawback' in 2005/2006 of grant for that year amounting to £558,000. Redundancy and early retirement pension costs of £1.8m arising from the re-organisation have been met by a contribution from general reserves. The summary overspend position is as follows:
  - Staff savings £497,000;
  - Corporate savings £145,000;
  - Revenue Support Grant Clawback £558,000

5.2 The above paragraphs highlight the major variations from the approved budget. The general pattern of variation remains as reported in previous monitoring reports with the overspending in Children's services, Community Services and Corporate Provisions being offset by savings within the remaining directorates and Interest and Financing.

#### Summary revenue outturn position

Directorate	Approved Budget £000s	Actual Expenditure £000s	Variation £000s
Chief Executive	3,037	2,817	(220)
Regeneration & Development	49,003	48,480	(523)
Children's Services	198,596	199,332	736
Finance & Corporate Services	11,738	11,336	(402)
Community Services	63,587	64,592	1,005
Interest & Financing	(42,639)	(44,413)	(1,774)
Levies	765	706	(59)
Corporate Provisions	(1,245)	(45)	1,200
<b>Total</b>	<b>282,842</b>	<b>282,805</b>	<b>(37)</b>

5.3 The 2005/2006 revenue underspend has been applied to the General Fund balance and the Consolidated Balance Sheet (page 28 of Appendix 1) shows this balance at £7.7 million. This represents 5.8% of the non-schools budget for the council. The Chartered Institute of Public Finance and Accountancy (CIPFA) and the Audit Commission have declined to be prescriptive on a guideline level of reserves but

5% is the figure that is generally quoted as a prudent guide. Clearly we remain within this tolerance.

## **6. Summary financial position for 2005/2006 (HRA)**

6.1 The Housing Revenue Account (HRA) is a ring-fenced account to record the 'landlord' costs and income associated with the maintenance of our housing stock. It includes costs of management and maintenance for the property portfolio, housing benefit costs in the form of rent rebates and capital financing costs, offset by housing rents and government grant. The summary of that account is set out at page 21 of Appendix 1 and reveals a surplus for the year of £831,000. This is then incorporated into the balance shown at the foot of the Consolidated Balance Sheet (page 28) as the Housing Revenue Account balance that now stands at just over £2.0m. This is only available for housing purposes and cannot be used to support General Fund (council tax) costs.

## **7. Summary financial position for 2005/2006 (Delegated Schools Budget)**

7.1 A significant proportion of the overall budget of the council is delegated to schools (£162m out of the £283m) and is then ring-fenced for that purpose. Any surplus or deficit is 'rolled-forward' as part of the schools' balances. The effect of this in the table at paragraph 5.2 is therefore to assume that for this £162m there is neither an over or under spending against the budget.

7.2 The reality of the spending position is reflected in the movement in the schools' balances figure at the foot of the Consolidated Balance Sheet (page 28). This shows that the schools balances have reduced considerably from £11.244m as at 31 March 2005 to £6.717m as at 31 March 2006. This is after the LEA received an additional £1.290m in transitional support grant, all of which has been passed to schools. In addition:

- Net revenue reserves have fallen significantly, as a percentage of the total resources available, from 6.7% to 4.1%;
- There has been a reduction of £4.4m in the level of reserves held by schools with positive balances;
- There has been an increase of £0.1m in the level of deficits held by schools;
- The number of schools in deficit has increased from 3 to 4; and
- The number of schools with reserves over 10% has fallen from 40 to 8.

## **8. Summary financial position for 2005/2006 (Capital)**

8.1 The final capital expenditure for 2005/2006 was £63.150m against the programmed expenditure for the year of £75.597m, a variation of £12.447m predominantly due to a roll forward of compensation claims in respect of Rochester Riverside. This outcome continues an established pattern of steadily increasing value of capital investment delivered year on year. Indeed, in 2005/2006, almost £40m more was invested than was the case in 1999/2000. The tables below exemplify the spend across directorates and the funding streams and section 8.3 highlights the major achievements during 2005/2006.

### Summary capital outturn position

Directorate	Approved programme 2005/2006 and beyond £000	Anticipated Spend for 2005/2006 £000	Provisional Outturn 2005/2006 £000	Variance £000
Chief Executive	3,838	2,062	2,155	93
Children's Services	30,655	19,657	19,901	244
Community Services	9,980	6,874	6,874	0
Finance & Corporate Services	6,215	2,985	2,917	(68)
Regeneration & Development	89,418	44,019	31,303	(12,706)
<b>Total</b>	<b>140,106</b>	<b>75,597</b>	<b>63,150</b>	<b>(12,447)</b>

Funding Source	Funding of expenditure £000's
Borrowing through the Single Capital Pot	15,647
Government Grants	33,382
Major Repairs Allowance	1,372
Capital Receipts	3,818
General and Earmarked Reserves	3,377
Developer and Other Contributions	5,554
<b>Total</b>	<b>63,150</b>

- 8.2 Borrowing through the single capital pot represents the total supported capital expenditure (revenue) for the Council in 2005/2006, (SCE(R)). Government grants represents the proportion of the supported capital expenditure (grant) in 2005/2006, (SCE(C)), used in financing spend in the year. The balance of government grants that haven't been spent during 2005/2006 will roll forward to support spend in later years. These grants include certain education grants linked to the academic year, and thus available to the end of the summer term, and ODPM sustainable communities grant.
- 8.3 The capital investment of £63.150m represents significant achievement towards the planned outputs of the capital programme. These will have featured in the regular monitoring reports to Cabinet and Overview and Scrutiny, the latest of which, in April 2006, forecast a spend of £75.597m. Key outputs were:
- 8.3.1 Chief Executive
- Completion of first phase of Customer First project and opening of new Contact Centre in June 2005;
  - Funding for Universities at Medway.
- 8.3.2 Children's Services
- Opening of Community Hub at New Brompton College;

- Opening of Fairview All Through Primary School;
- Completion of Phase I of Twydall Junior school;
- New classrooms;
- Interactive whiteboards;
- Kitchen adaptations;
- Extensions to facilities;
- Learning support units and
- Improved security and sports facilities.

#### 8.3.3 Community Services

- Improvements to housing stock;
- Improvements to private sector housing through renovation grants etc;
- Property adaptations for disabled persons;
- Refurbishment of Rochester Adult Education Centre;
- Opening of Ranscombe Farm Park and
- Relocation of Chatham Library.

#### 8.3.4 Finance & Corporate Services

- Continuing programme or maintenance of Council buildings;
- Introduction of Digi TV;
- Completion of the 'Wired Medway' project and
- Works required for Disabilities Discrimination Act.

#### 8.3.5 Regeneration & Development

- Completion of A228 Main Road to Ropers Lane Dualling;
- Remedial works to Grain Sea Wall;
- Various projects from Liveability Fund;
- Introduction of Rural Community Transport Programme;
- Significant progress of Rochester Riverside development and
- Upgrade of Gillingham Library.

### 9. Reserves

- 9.1 The council's reserves have diminished substantially in recent years, largely as a result of financing capital investment but also in supporting revenue expenditure. The budget setting process for 2006/2007 forecast available general reserve of £1.7m at 1 April 2007. However, this anticipated the use of £9.0m to support the capital programme in 2005/2006 and future years and, as the table above indicates, only £3.8m was required with the balance being rolled forward to future years. In addition, during the budget setting process Members transferred some £2.6, of funding from reserves to capital receipts but introduced a further £2m of capital expenditure to be funded from released reserves. As a consequence, £5m from the General Reserve is committed to fund the capital programme.
- 9.2 The General Reserve at 31 March 2006 stands at £7.0m and assuming that the remaining balance of reserves to finance the capital programme is spent in 2006/2007, the estimated balance of the General Reserve at 31 March 2007 will be approximately £2m which is broadly consistent with the forecast at budget setting.



## **10. Financial and legal implications**

- 10.1 The financial implications are contained within the body of the report.
- 10.2 The Local Authorities (Functions and Responsibilities) (England) Regulations 2000 places a duty on Council or a designated committee to approve the statement of accounts and it is a function that cannot be delegated to Cabinet.
- 10.3 Regulation 4 (2) of the Accounts and Audit Regulation 2003 require authorities to “conduct a review at least once in a year of the effectiveness of its systems of internal control” and include a statement on internal control with their statement of accounts.

### **Background papers**

Revenue and Capital budget monitoring reports to Cabinet during 2005/2006  
Medway Council’s draft statement of accounts for 2005/2006.

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