



cutting through complexity™

Appendix 1

Report to those charged with governance (ISA 260) 2010/11

Leeds City Council

30 September 2011

The contacts at KPMG in connection with this report are:

Mike McDonagh

Partner

KPMG LLP (UK)

Tel: 0207 694 5546

Mobile : 07747 757 173

michael.a.mcdonagh@kpmg.co.uk

Steve Clark

Director

KPMG LLP (UK)

Tel: 0113 254 2910

Mobile: 07876 390 524

stephen.clark@kpmg.co.uk

Alison Ormston

Senior Manager

KPMG LLP (UK)

Tel: 0113 231 3444

Mobile: 07833 400 887

alison.ormston@kpmg.co.uk

Sam Bradford

Manager

KPMG LLP (UK)

Tel: 0113 231 3624

Mobile: 07554 116 255

sam.bradford@kpmg.co.uk

Page

Report sections

- Introduction 2
- Headlines 3
- Financial Statements 8
- VFM conclusion 13

Appendices

1. Issues and Recommendation 17
2. Follow-up of prior year recommendations 18
3. Declaration of independence and objectivity 20

This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Mike McDonagh the appointed engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by email to complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421.

This report summarises:

- the key issues identified during our audit of Leeds City Council's ('the Authority's) financial statements for the year ended 31 March 2011; and
- our assessment of the Authority's arrangements to secure value for money (VFM) in its use of resources.

We do not repeat matters we have previously communicated to you. In particular, we draw your attention to our *Interim Audit Report 2010/11*, presented to you on 23 June 2011, which summarised our planning and interim audit work.

Financial statements

Our audit of the financial statements can be split into four phases:



We previously reported on our work on the first two stages in our Interim Audit Report 2010/11 issued in June.

This report focuses on the final two stages: substantive procedures and completion.

Our final accounts visit on site took place between 18 July and 30 September. During this period, we carried out the following work:

Substantive Procedures

- Planning and performing substantive audit procedures.
- Concluding on critical accounting matters.
- Identifying audit adjustments.
- Reviewing the Annual Governance Statement.

We are now in the final phase of the audit. Some aspects are also discharged through this report:

Completion

- Declaring our independence and objectivity.
- Obtaining management representations.
- Reporting matters of governance interest.
- Forming our audit opinion.

VFM conclusion

We have also now completed our work in respect of the 2010/11 VFM conclusion. This included:

- work to address the specific risk areas identified in our VFM Audit Approach presented to you on 17 April 2011.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out the key findings from our audit work in relation to the 2010/11 financial statements.
- Section 4 outlines the key findings from our work on the VFM conclusion.

We have reviewed your progress in implementing prior year recommendations and this is detailed in Appendix 2.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

This table summarises the headline messages. The remainder of this report provides further details on each area.

Audit Progress	<p>At the date of this report our audit of the financial statements is still to be completed, until this point we are unable to issue our opinion. We anticipate issuing the audit opinion on 30 September.</p>
Audit adjustments to date	<p>Our audit identified no significant audit adjustments, there were a small number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2010.</p> <p>Management have however identified one 'event after the reporting date' with a total value of £8.4m. This related to the fact that in the Authority's draft accounts a contingent asset, which is an asset where the possibility of receipt depends solely upon a future event, was identified in respect of a VAT claim for Trade Waste. Since the year end HMRC have confirmed to the Authority, in writing, that this claim will be paid. Therefore in accordance with accounting standards, the receipt of this letter confirms that the money from HMRC will be received and so this is classed as an 'adjusting event'. This means that this income has now been recognised in the 2010-11 accounts and a corresponding debtor raised with HMRC.</p> <p>The impact of this was to:</p> <ul style="list-style-type: none"> ▪ Increase the balance on the general fund account as at 31 March 2011 by £8.4m; ▪ Increase the surplus on provision of services for the year by £8.4m; and ▪ Increase the net worth of the Authority as at 31 March 2011 by £8.4m.
Critical accounting matters	<p>We have worked with officers throughout the year to review the specific risk areas highlighted during the planning stages of our audit. These specific risks included:</p> <ul style="list-style-type: none"> ▪ Financial Standing – The Authority has delivered a surplus of £13.5m against its budgeted position for the year. This is against a backdrop of overspends totalling £10.3m in directorates. The main areas of overspend, again this year, are in Adults and Children's services, with both directorates continuing to face demand pressures. These overspends have been offset by corporate savings of £23.8m. The savings include: <ul style="list-style-type: none"> ○ Interest payable savings (£4.7m) due to the Bank of England interest rate remaining at a lower level than budgeted. ○ Changes in the accounting treatment of PFI schemes (£8.4m) which have meant that an element of the PFI payment is recognised as capital spend and, in accordance with legislation, can therefore be funded from capital receipts. ○ A successful VAT claim (£8.4m) which the Authority were notified about post year end. ○ Other net savings (£2.3m).

This table summarises the headline messages. The remainder of this report provides further details on each area.

<p>Critical accounting matters (cont.)</p>	<ul style="list-style-type: none"> ▪ Valuation of Council Assets – In the prior year we identified two issues in respect of the valuation of fixed assets. There had been three assets which had been revalued during the year however these revaluations had not been reflected on the fixed asset register and there had been six properties which had been revalued and included on the fixed asset register when they should not have been. In addition to the risks as a result of these historical errors there are a number of additional risk factors this year. These risks include the fact that the Authority changed to solely rely upon their internal valuer this year and there has also been significant changes in the accounting treatment for assets as a result of the adoption of IFRS. This year we are pleased to state that we have found no issues as a result of our work in this area which has included reviewing: <ul style="list-style-type: none"> ○The independence and objectivity of the Authority's in-house valuer. ○The valuations of fixed assets for complete and accurate recording on the fixed asset register. ○The methodology and accounting entries in relation to component accounting as adopted by the Authority. ▪ IFRS implementation – Throughout the year we have kept in regular contact with the finance team discussing emerging issues and current guidelines. The Authority have handled the implementation of IFRS well and have demonstrated that they have a team who are flexible and adaptable in their approach.
<p>Accounts production and audit process</p>	<p>The quality of the accounts and the supporting working papers has remained strong. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.</p> <p>We submitted our prepared by client list to the Authority in April and officers delivered a full set of working papers in line with our requirements and within the timescales agreed. This year we have asked for a number of items to be made available electronically and the officers have done this wherever possible.</p> <p>The Authority has implemented all of the recommendations in our ISA 260 Report 2009/10 relating to the financial statements and continue to take action against our recommendations on a timely basis.</p>
<p>Fees</p>	<p>As per the Audit Fee Letter issued at the beginning of the year our indicative fee for the 2010/11 audit was set at £570,000, although a rebate number of £39,617 was provided to subsidise the 'one-off' element of the cost of transition to International Financial Reporting Standards, reducing the fee to £530,383. This was significantly below the recommended Audit Commission mid point fee of £598,500.</p> <p>In year we have also provided additional services to the Authority at no additional cost. This has included employment tax advice relating to the Early Leavers Initiative (ELI) and advice from our business intelligence team on the design of the financial dashboard monitoring that the Authority are looking to introduce.</p> <p>At the request of the Corporate Governance and Audit Committee and in recognition of the financial pressures the Authority is under we agreed to review this fee upon completion of our audit to identify whether any efficiencies gained throughout the audit process could be passed back to the Authority. We are pleased to report that KPMG have agreed to provide the Authority with a rebate of £3,000 as a result of the audit efficiencies we delivered.</p>

This table summarises the headline messages. The remainder of this report provides further details on each area.

<p>Completion</p>	<p>At the date of this report our audit of the financial statements is still to be completed. However before we can issue our opinion we also require a signed management representation letter. This year, in parallel with the work we have done, we are asking for an additional, specific representation in relation to the calculation of the Authorities Equal Pay provision.</p> <p>The Equal Pay provision is an amount of money set-aside by the Authority to settle claims made against it in relation to the Equal Pay Act. The amount of the provision has increased substantially during the year (from £4.3m to £36.1m) and is subject to a greater number of claimants and claimant groups to which an estimation applies than in prior years. This is because the Authority must estimate the number and value of claimants who have been disadvantaged over the past 4 years in relation to protected pay agreements. The Authority have received a capitalisation direction from the government so that this value will be funded over 20 years.</p> <p>Due to the significance of the value and the amount of judgement required in setting this provision we are seeking the specific assurance of management that this value is materially correct.</p> <p>We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.</p>
<p>VFM conclusion</p>	<p>We have yet to finalise our VFM opinion as to whether the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources and we are continuing to assess the Authority against the two criteria identified by the Audit Commission:</p> <ul style="list-style-type: none"> ▪ Securing financial resilience; and ▪ Securing economy, efficiency and effectiveness. <p>To date we have held meetings with officers and reviewed a wide range of documentation and arrangements across the Authority in order to come to our conclusion. In addition to this we have considered 3 specific risks relevant to the Authority which are discussed below .</p>

This table summarises the headline messages. The remainder of this report provides further details on each area.

VFM risk areas

We have considered the specific VFM risks we set out in our VFM audit approach 2010-11:

Managing with Less - The Authority has put in place arrangements following the Comprehensive Spending Review (CSR) to ensure that it achieves its objectives. Achievement of the 2010-11 budget, and strong uptake on the Early Leavers Initiative has shown the Authority is responding to the challenges it faces. The Authority has delivered a surplus of £13.5m against its budgeted position for the year and 1,500 staff have left the Authority to date. This is against a backdrop of overspends totalling £10.3m in directorates, which are mainly in Adults and Children's, which the Authority has identified as risk areas and where they continue to seek early intervention throughout the year. These overspends have been offset by corporate savings of £23.8m.

The Authority has achieved this £13.5m underspend with a relative low level of reserves (including earmarked reserves) as a percentage of spending power (LCC 4% average core city 14%) whilst facing funding reductions which are relatively greater than other Authority's. The Authority has always operated within a level of reserves it has felt prudent and has added to these with the surplus reported this financial year.

The results of the Audit Commission financial resilience survey did not identify any areas for major concern when assessing the VFM arrangements at the Authority.

The scale of the challenge ahead is not to be underestimated and key to this will be managing the overspends in Adults and Children's which as at month 4 of 2011/12 are showing overspends of £10.6m.

The Authority therefore need to ensure that they continually monitor their Medium Term Financial Plan and take appropriate early interventions to manage their financial pressures. See recommendation in Appendix 1.

Early Leavers Initiative (ELI) - As a result of the significant financial pressures faced by the Authority, the Executive Team approved an early Council wide ELI. The rationale for the introduction of this scheme was to provide the Authority with a mechanism to help respond to the financial challenges it faced.

Initial targets for the first phase of the ELI was for 1,000 employees to leave the Authority achieving around £20m of savings. These figures were determined to support a balanced budget rather than being through a review of future service delivery. The Authority however maximised the VFM achieved through this initiative by not simply stopping when they reached their target of 1,000. The Authority continued reviewing individual applications against the business case criteria and drove through extra savings as a result. In total 1,159 employee posts have been saved as at 31 March 2011. The number of ELI approved cases was 890, with the remainder achieved through not recruiting as employees have left the Authority.

The Authority are also in a second phase of the ELI and have target figures of between 350 – 400 early leavers to be achieved through this process in the current financial period. This is also a continual journey for the Authority and going forward, due to the continual improvements in service planning the Authority plan to move to an approach whereby the resourcing team will look at the future delivery method of the services and use this to identify the future structure of the directorates. This method will be utilised as a tool to identify the target numbers for staffing numbers within the Authority based on the most effective, efficient method of service delivery.

This table summarises the headline messages. The remainder of this report provides further details on each area.

VFM risk areas
 (continued)

Waste Management – The Authority currently sends over 50% of the waste produced by the residents of Leeds to landfill, for which the costs keep escalating. For a number of years, the Authority have been reviewing a more cost effective method of waste management. To achieve this, the Authority plans to continually improve its recycling targets and have developed a ‘residual waste’ strategy. To manage this ‘residual waste’ strategy the Authority commenced the procurement of a contract to treat the Authority’s residual waste in 2008 . Currently the Authority have short listed the participants down to two bidders who have both submitted their final tenders and the Authority are now completing the final tender evaluation with proposed recommendations to go to the Executive Board in November. It is expected that the facility will become fully operational in March 2016.

Throughout the life of this project the Authority have sought technical, legal and financial advice from external advisors including, DLA, PwC and Jacobs and the internal team within the Public Private Partnership Unit (PPPU). This expert advice has been called upon to undertake a technical review of the technology to be used in this facility and the Authority were satisfied with the assumptions used to underpin this work.

The Authority have also sought external advice to determine what the cost would be for the Authority to do nothing and to continue as they are. The costs of the ‘do nothing’ model are significantly higher than the costs of the ‘residual waste’ strategy. The objective of this project overall is to at least achieve a break even position and if possible achieve a saving in net terms.

There remain some potential risks that need to be managed by the Authority including the fact that the facility has the potential to be either a combined heat and power (CHP) enabled or deliverable scheme.

Our audit did not identify any audit adjustments.

One adjustment has been made by the Authority in relation to an ‘event after the reporting date’.

The impact of this was to:

- Increase the balance on the general fund account as at 31 March 2011 by £8.4m;
- Increase the surplus on provision of services for the year by £8.4m; and
- Increase the net worth of the Authority as at 31 March 2011 by £8.4m.

The wording of your Annual Governance Statement accords with our understanding.

Proposed audit opinion

At the date of this report our audit of the financial statements is still to be completed, until this point we are unable to issue our opinion. We anticipate issuing the audit opinion on 30 September.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

Our audit did not identify any audit adjustments.

The tables on the right illustrate the total impact of the event after the reporting date on the Authority’s movements on the General Fund and the Balance Sheet as at 31 March 2011.

The net impact on the General Fund as is to increase the balance as at 31 March 2011 by £8.4m.

The event after reporting date, related to the fact that in the Authority’s draft accounts a contingent asset, which is an asset where the possibility of receipt depends solely upon a future event, was identified in respect of a VAT claim for Trade Waste.

Since the year end HMRC have confirmed to the Authority, in writing, that this claim will be paid. Therefore in accordance with accounting standards, the receipt of this letter confirms that the money from HMRC will be received and so this is classed as an ‘adjusting event’.

This means that this income has now been recognised in the 2010-11 accounts and a corresponding debtor raised with HMRC.

Annual Governance Statement

We have reviewed the Annual Governance Statement and confirmed that :

- It complies with *Delivering Good Governance in Local Government:*

A Framework published by CIPFA/SOLACE in June 2007; and

- It is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Movements on the General Fund 2010/11		
£m	Pre-audit	Post-audit
Surplus or (deficit) on the provision of services	69,798	75,224
Adjustments between accounting basis & funding basis under regulations	(49,611)	(46,605)
Transfers to/ (from) earmarked Reserves	(15,132)	(15,132)
Increase/(decrease) in General Fund	5,055	13,487

Balance Sheet as at 31 March 2011		
£m	Pre-audit	Post-audit
Property, plant and equipment	3,482,646	3,482,646
Other long term assets	89,637	89,637
Current assets	122,360	130,792
Current liabilities	(363,685)	(405,519)
Long term liabilities	(2,620,445)	(2,581,617)
Net worth	710,513	715,939
General Fund	(21,131)	(29,563)
Other reserves	(689,382)	(686,376)
Total reserves	(710,513)	(715,939)

We have worked with officers throughout the year to discuss specific risk areas. The Authority addressed the issues appropriately.

Further details and findings are documented here.

In our *Financial Statements Audit Plan 2010/11*, presented to you on 21 March 2011 we identified the key risks affecting the Authority's 2010/11 financial statements.



In our *Interim Audit Report 2010/11* we commented on the Authority's progress in addressing these key risks. We highlighted that we had completed our initial work to assess the Authority's financial resilience following the funding settlement for 2011-2013 and that the Authority

had made considerable progress in the restatement of its 2009/10 financial statements under IFRS.

We have now completed our testing of these areas and set out our final evaluation following our substantive work.

The table below sets out our detailed findings for each risk.

Key audit risk	Issue	Findings
	<p>Financial standing / medium term financial planning</p> <p>Following the Government's spending review the Authority announced that it was required to make £90 million savings in the financial year to address the twin constraints of reduced funding and increasing demographic and demand pressures. The final settlement has since confirmed the figure to be accurate.</p> <p>In order to deliver the required savings, the Authority will be undertaking some significant change programmes across all services.</p>	<p>The Authority has delivered a surplus of £13.5m against its budgeted position for the year.</p> <p>This has been achieved by offsetting overspends totalling £10.3m in directorates against corporate savings of £23.8m.</p> <p>The major corporate savings include:</p> <ul style="list-style-type: none"> ▪ Interest payable (£4.6m). ▪ Changes in the accounting treatment, which result in non cashable savings, on PFI schemes (£8.4m). ▪ A successful VAT claim (£8.4m). ▪ Other net savings of (£2.3m). <p>Financial performance to date in 2011/12 demonstrates the continued pressures within adults and children's and the management of these pressures will be critical in the future financial standing of the Authority.</p>

Key audit risk	Issue	Findings
	<p>Valuation of Council Assets</p> <p>Valuation of Council Assets is considered to be a key audit risk for the following reasons:</p> <p>During 2009/10 audit we found a small number of errors relating to fixed asset valuations.</p> <p>There is a change in the valuation process during 2010/11 as the Authority are changing the number of Valuers from five to one, bringing all valuations in house.</p> <p>There are added complications in the valuation of Authority assets during 2010/11 due to componentisation as a result of the transition to IFRS.</p>	<p>We have found no issues as a result of our work in this area. The work has included reviewing:</p> <ul style="list-style-type: none"> ▪ The independence and objectivity of the Authority's in-house valuer. ▪ The valuations of fixed assets for completeness and accuracy. ▪ The methodology and accounting entries in relation to component accounting as adopted by the Authority.
	<p>IFRS conversion process</p> <p>The Authority will require a lot of planning and resources to ensure a smooth and successful transition to IFRS.</p> <p>The Authority have an IFRS Work Plan in place with lead officers being allocated responsibility for individual work areas. The finance team have involved us at an early stage in the conversion process and are keeping us up to date with progress against the Work Plan as well as seeking clarification on specific issues.</p>	<p>We completed a review of the IFRS conversion process as part of our interim work and updated this at the final visit.</p> <p>The Authority has worked well in this area and tackled the issues raised by this major change in a timely and effective manner.</p>

The quality of the accounts and the supporting working papers continue to be of a good standard.

Officers dealt efficiently with audit queries so the audit process could be completed within the planned timescales.

The Authority has implemented all of the recommendations in our ISA 260 Report 2009/10 relating to the financial statements.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the qualitative aspects of the Authority's accounting practices and financial reporting. We also assessed the Authority's process for preparing the accounts and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Authority has a strong financial reporting process and we consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 30 June. The Authority made a number of amendments of a presentational nature during the audit.
Quality of supporting working papers	Our <i>Prepared By Client List</i> , which we issued on 14 April 2011 and discussed with Chris Blythe, set out our working paper requirements for the audit. The quality of working papers provided was good and met the standards specified in our <i>Prepared By Client List</i> .
Response to audit queries	Officers resolved our audit queries in a timely manner.

Prior year recommendations

In our *Interim Audit Report 2010/11* we commented on the Authority's progress in addressing the recommendations in our *ISA 260 Report 2009/10*.

The Authority has now implemented all of the recommendations in our *ISA 260 Report 2009/10* relating to the financial statements.

Appendix 2 provides further details.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of the Authority for the year ending 31 March 2011, we confirm that there were no relationships between KPMG LLP and the Authority, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 3 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Director of Resources and Acting Deputy Chief Executive. We require a signed copy of your management representations before we issue our audit opinion.

We have requested representation over the following area of material judgement:

- Equal Pay Provision – The Authority are confident that the estimated equal pay costs and associated probability underpinning volume of claims is reasonable and does not provide a material under or over provision based upon available information.

Other matters

ISA 260 requires us to communicate 'audit matters of governance interest that arise from the audit of the financial statements' to you which includes:

- material weaknesses in internal control identified during the audit;
- matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. issues relating to fraud, compliance with laws and regulations, subsequent events etc.); and
- other audit matters of governance interest.

There are no matters which we wish to draw to your attention.

Our VFM conclusion considers how the Authority secures financial resilience and challenges how it secures economy, efficiency and effectiveness.

Overview of the new VFM audit approach

For 2010/11, auditors are required to give their statutory VFM conclusion based on two criteria specified by the Audit Commission. These consider whether the Authority has proper arrangements in place for:

- securing financial resilience: looking at the Authority's financial governance, financial planning and financial control processes; and
- challenging how it secures economy, efficiency and effectiveness: looking at how the Authority is prioritising resources and improving efficiency and productivity.

We follow a risk based approach to target audit effort on the areas of greatest audit risk. We consider the arrangements put in place by the Authority to mitigate these risks and plan our work accordingly.

Our VFM audit draws heavily on other audit work which is relevant to our VFM responsibilities and the results of last year's VFM audit.

The key elements of the VFM audit approach are summarised in the diagram below.



Conclusion

We have yet to finalise our VFM opinion as to whether the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources and we are continuing to assess the Authority against the two criteria identified by the Audit Commission.

VFM criterion	Met
Securing financial resilience	TBC
Securing economy, efficiency and effectiveness	TBC


The following pages include further details on the specific risk-based work.

Specific value for money risks


We have considered the specific VFM risks we set out in our VFM audit approach 2010/11.

We have assessed the Authority's arrangements in regard to these risks and found them to be adequate.

Our risk assessment was included in our Value for Money audit approach 2010/11 and we set out our preliminary findings in respect of these risks in our Interim Audit Report 2010/11. We have completed our work on these risk areas and summarise our findings below.


VFM risk	Focus of work	Update
	<p>The Audit Commission published a national study in May 2011 on the impact of the 2011/12 local government settlement on councils' finances. The study examined the approaches taken by councils in responding to the need to make savings and to manage with less.</p> <p>To support the study, we completed a survey which captured:</p> <ul style="list-style-type: none"> information on the financial stability of the Authority following the 2011/12 settlement, focusing in particular on the capacity of the Authority's 2011/12 draft budgets to secure this stability; and actions used by the Authority to secure the necessary savings in its 2011/12 draft budget and any resulting implications for service provision. <p>We also critically assessed the Authority's financial standing to ensure that its Medium Term Financial Plan and planning has duly taken into consideration the potential funding reductions and that it is sufficiently robust to ensure that the Authority can continue to provide services effectively.</p> <p>The information collected in the survey is closely based on the financial resilience criterion of the VFM conclusion and forms a mandatory part of auditors' work programmes at all single-tier, county and district councils.</p>	<p>The Authority has put in place arrangements following the CSR to ensure that it achieves its objectives despite the funding reductions it is facing.</p> <p>Achievement of the 2010-11 budget and strong uptake on the Early Leavers Initiative has shown the Authority is responding to the challenges it faces.</p> <p>As part of the new VFM work programme we have held meetings with officers and reviewed a wide range of documentation and arrangements the Authority has put in place to ensure it remains financially resilient.</p> <p>We have completed the Audit Commission financial resilience survey and the results of this confirmed that the Authority is performing adequately. This is in the context of the Authority having relative low level of reserves (including earmarked reserves) as a percentage of spending power (LCC 4%, average core city 14%) and funding reductions which are relatively greater than other Councils.</p> <p>Throughout the year we have discussed with officers the arrangements for managing the Medium Term Financial Plan and these arrangements appear appropriate. However the scale of the funding challenge is large and should not be under-estimated, especially since the Authority continues to face demand and cost pressures within Adults and Children's Social Care.</p> <p>The Authority are in the process of implementing a key performance dashboard to give early warning/indication of possible budget issues and have also implemented monthly monitoring of budget information by Members</p>

Section four – value for money conclusion
Specific value for money risks - continued

VFM risk	Focus of work	Update
		<p>(previously quarterly) to improve awareness and increase responsiveness.</p> <p>The scale of the challenge ahead is not to be underestimated, but we feel the Authority has a good understanding of this and to date have responded appropriately.</p>
	<p>We will consider how the Authority has ensured that its decision on cost reductions and service cuts reflect local priorities and will achieve long-term sustainable savings.</p> <p>This work is relevant to both the financial resilience and economy, efficiency and effectiveness criteria of the VFM conclusion</p>	<p>As a result of the significant financial pressures faced by the Authority following the Comprehensive Spending Review, the Executive Team approved an early Council wide ELI. The rationale for the introduction of this scheme was to provide the Authority with a mechanism to help respond to the financial challenges it faced.</p> <p>Employees were asked to express an interest in Voluntary Severance (VS) or Voluntary Early Retirement (VER) by completing an individual business case.</p> <p>Initially 1,866 business cases were received from employees and whilst 486 were withdrawn these were reviewed initially within Directorates and then by a Corporate Approval Panel. This review process of the individual business cases ensured that the specified criteria were achieved with regards to reducing costs and yet still maintaining service delivery in line with priorities.</p> <p>Initial targets of ELI numbers were set to enable a balanced budget. The initial target was 1,000, however the Authority tried to maximise the VFM achieved through this initiative by not simply stopping when they reached their target. The Authority continued reviewing individual applications against the business case criteria and drove through extra savings as a result.</p> <p>In total 1,159 employee posts have been saved as at 31 March 2011. The number of ELI approved cases was 890, with the remainder achieved through not recruiting as employees have left the Authority.</p>

Section four – value for money conclusion

Specific value for money risks - continued

VFM risk	Focus of work	Update
		<p>The Authority are currently in a second phase of the ELI and have target figures of between 350 – 400 early leavers to be achieved through this next stage of the process. This is also a continual journey for the Authority and going forward, due to the continual improvements in service planning the Authority plan to move to an approach whereby the resourcing team will look at the future delivery method of the services and use this to identify the future structure of the directorates and staff numbers required.</p>
	<p>We will take into consideration how the Authority ensures that the waste management plan is affordable and tailored to local needs, delivering value for money.</p> <p>This work is particularly relevant to the economy, efficiency and effectiveness criterion of the VFM conclusion.</p> <p>This project is an example of a large scale procurement exercise and a review of the procedures followed for this project may indicate further risks and lead to additional work.</p>	<p>Currently the Authority have short listed the original nine bidders down to two through using an evaluation framework which was made publically available back in 2008. The Authority are now completing this final tender evaluation on the final two bidders with proposed recommendations going to the Executive Board in November. Throughout this evaluation process the Authority have ensured that local needs and value for money have been factored in.</p> <p>Throughout the life of this project the Authority have sought technical, legal and financial advice from external advisors including, DLA, PwC and Jacobs and the internal team within the Public Private Partnership Unit (PPPU). This expert advice has been called upon to undertake a technical review of the technology to be used in this facility and the Authority were satisfied with the assumptions used to underpin this work.</p> <p>The Authority have also sought external advice to determine what the cost would be for the Authority to do nothing and to continue as they are. The costs of the 'do nothing' model are significantly higher than the costs of the 'residual waste' strategy. The objective of this project overall is to at least achieve a break even position and if possible achieve a saving in net terms.</p>

We have given each recommendation a risk rating and agreed what action management will need to take.

The Authority should closely monitor progress in addressing specific risks and implementing our recommendations.

We will formally follow up these recommendations next year.

Priority rating for recommendations		
● Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	● Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	● Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

No.	Risk	Issue and recommendation	Management response/ responsible officer/ due date
1	● (two)	<p>Medium Term Financial Plan</p> <p>The results of the Audit Commission financial resilience survey did not identify any areas for major concern when we were assessing the VFM arrangements at the Authority.</p> <p>However, the scale of the challenge ahead is not to be underestimated and key to this will be managing the overspends in Adults and Children's which, as at month 4 of 2011/12, are showing overspends of £10.6m.</p> <p>The Authority need to ensure that they continually monitor their Medium Term Financial Plan and take appropriate early interventions to manage their financial pressures.</p>	<p>Monthly in year budget monitoring is undertaken via the Executive Board. The Medium Term Financial Plan will be reviewed as part of the 2012/13 budget process.</p> <p>Responsible officer: Chief Officer Financial Management</p> <p>Due date: February 2012</p>

Appendix 2: Follow up of prior year recommendations

The Authority has implemented all of the recommendations in our ISA 260 Report 2009/10.

This appendix summarises the progress made to implement the recommendations identified in our ISA 260 Report 2009/10 and reiterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	2
Implemented in year or superseded	2
Remain outstanding	0

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at 30 September 2010
1	● (two)	<p>Fixed Asset Disposals</p> <p>Our review of Fixed Asset revaluations found there were six properties which were revalued in the year which were included on the fixed asset register which should not have been.</p> <p>Of these, five of the properties had been disposed of in prior years and one asset had been duplicated on the fixed asset register.</p> <p>The value of these properties was £3.2m, this had already been adjusted by the Authority in the accounts approved by Committee and is therefore not included within Appendix D where we show our audit adjustments.</p> <p>We recommend that the Authority reviews all items within the Fixed Asset register which have not been revalued recently to ensure that these assets are still owned by the Authority. This indication of control weakness is considered serious but mitigated as the Authority were aware of this prior to our audit.</p>	<p>Principle Accountant - Corporate Financial Management</p> <p>April 2011</p>	<p>Our work this year has included a review of a sample of property revaluations to ensure all assets are correctly included on the fixed asset register.</p> <p>From the sample we selected for testing we did not find any discrepancies.</p>

Appendix 2: Follow up of prior year recommendations - continued

The Authority has implemented all of the recommendations in our *ISA 260 Report 2009/10*.

No.	Risk	Issue and recommendation	Officer responsible and due date	Status as at 30 September 2010
2	<p>● (two)</p>	<p>Fixed Asset Valuations</p> <p>During our work we identified three assets which had been revalued during the year, however these revaluations (upwards) had not been reflected in the fixed asset register.</p> <p>Further review found two more assets where the same situation occurred. This has resulted an increase to the Fixed Asset balance in the accounts of £1.942m.</p> <p>The Authority should ensure that all fixed asset valuations are updated to the Fixed Asset Register each year.</p>	<p>Principle Accountant - Corporate Financial Management</p> <p>April 2011</p>	<p>We have sample tested revaluations undertaken during the year to identify if any revaluations have not been reflected in the 2010/11 fixed asset register.</p> <p>From our sample selected we did not identify any cases where the revaluation performed had not been appropriately reflected.</p>

The Code of Audit Practice requires us to exercise our professional judgement and act independently of both the Commission and the Authority.

Requirements

Auditors appointed by the Audit Commission must comply with the *Code of Audit Practice* (the Code) which states that:

“Auditors and their staff should exercise their professional judgement and act independently of both the Commission and the audited body. Auditors, or any firm with which an auditor is associated, should not carry out work for an audited body that does not relate directly to the discharge of auditors’ functions, if it would impair the auditors’ independence or might give rise to a reasonable perception that their independence could be impaired.”

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Audit Commission’s Standing guidance for local government auditors (Audit Commission Guidance) and the requirements of APB Ethical Standard 1 *Integrity, Objectivity and Independence* (Ethical Standards).

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Audit Commission Guidance requires appointed auditors to follow the provisions of ISA (UK & I) 260 Communication of *Audit Matters with Those Charged with Governance* that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor’s objectivity and independence.
- The related safeguards that are in place.

- The total amount of fees that the auditor and the auditor’s network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor’s professional judgement, the auditor is independent and the auditor’s objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor’s objectivity and independence may be compromised and explaining the actions which necessarily follow from his. These matters should be discussed with the Corporate Governance and Audit Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Audit Partner and the audit team.

General procedures to safeguard independence and objectivity

KPMG’s reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's financial statements.

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the Ethics and Independence Manual ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual Ethics and Independence Confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of Leeds City Council for the financial year ending 31 March 2011, we confirm that there were no relationships between KPMG LLP and the Leeds City Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.



cutting through complexity™

© 2011 KPMG LLP, a UK public limited partnership, is a subsidiary of KPMG Europe LLP and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative, a Swiss entity. All rights reserved.

The KPMG name, logo and 'cutting through complexity' are registered trademarks or trademarks of KPMG International Cooperative (KPMG International).