

Ms R Pritchard-Wooles
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05 March 2014

Dear Ms Pritchard-Wooles

Understanding how the Civic Affairs Committee gains assurance from management

I am writing in response to your letter of 11 February 2014 in my capacity as Chair of the Civic Affairs Committee.

I have considered the questions that you raised, consulted appropriate officers and set out responses on behalf of the Committee below.

1. How does the Civic Affairs Committee, as 'those charged with governance' at the Authority, exercise oversight of management's processes in relation to:

- *Undertaking an assessment of risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments)*

Management's overall assessment of the risks that the financial statements may be materially misstated is reflected by the inclusion, in the corporate risk register, of identified risks, control measures in place and any additional actions required to mitigate those risks. Members of Civic Affairs have the role of overseeing the effective management of risk by officers. In effect this means that they agree the Strategy, framework and process put forward by officers. The Risk Management Strategy was last formally presented to the Committee in March 2013. Updates, for example arising from internal audit work, are provided as necessary.

Civic Affairs also approves the Internal Audit Plan (usually presented in March each year) and receives reports on the Annual Review of the Effectiveness of Internal Audit and the Annual Opinion of the Head of Internal Audit (in June each year) to review and challenge. In addition, the Committee receives a mid-year audit opinion progress report.

The Council's financial statements are prepared substantially from information held in its Financial Management System together with information held on other systems which feed into it. The Internal Audit work, which the Committee approves and receives reports upon, includes review of the Council's key financial systems and processes in order to gain assurance that appropriate systems of control are in place and operating effectively.

- *Identifying and responding to risks of fraud in the Authority, including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist*

The work of Internal Audit includes identifying those systems or transactions which may be more susceptible to fraud and these areas are appropriately covered by the Internal Audit Plan which Civic Affairs approves. Any significant issues which arise from audit reports may be reported either to the committee or direct to the relevant scrutiny committee, as appropriate.

- *Communicating to employees its view on business practice and ethical behaviour (for example by updating, communicating and monitoring against the Authority Code of Conduct)*

Employees are required to follow the Council's Employee Code of Conduct (available on the intranet), the latest version of which was approved by Civic Affairs in March 2011. Further specific amendments in relation to gifts and hospitality were approved by the Committee in June 2013.

Fraud and irregularity investigations are reported annually in June to Civic Affairs in the Annual Report on Prevention of Fraud and Corruption Policy. This includes a summary of investigations into benefit fraud, theft and any whistleblowing allegations.

- *Encouraging employees to report their concerns about fraud*

There is a whistleblowing policy, which staff are made aware of and which is available on the intranet. Civic Affairs receives a summary of whistleblowing activity as part of the Annual Report on Prevention of Fraud and Corruption Policy.

- *Communicating to you the processes for identifying and responding to fraud or error?*

Fraud and irregularity investigations are normally reported annually to Civic Affairs. This covers Internal Audit work as well as that of the Revenue and Benefits Service Fraud Prevention Team.

The Leader of the Council and relevant Executive Councillor receive copies of the final versions of all Internal Audit reports. In addition, final reports are available on

request to other Councillors and arrangements are being made to enable secure access to these via the intranet.

2. How does the Committee oversee management processes for identifying and responding to the risk of fraud and possible breaches of internal control?

As outlined above, the Committee oversees management processes in relation to the risk of fraud and weaknesses in internal control through the monitoring of Internal Audit activity and the setting of risk management strategy.

3. Is the Committee aware of any:

- *Breaches of, or deficiencies in, internal control;*

Internal Audit report on any identified deficiencies in internal control as part of their audit work. The outcome of this work in respect of 2012/13 was summarised and reported to Civic Affairs as part of the Head of Internal Audit's Annual Audit Opinion at the meeting in June 2013. The overall conclusion was that Cambridge City Council has a fundamentally sound governance framework from which those charged with governance can gain assurance. The only significant control weakness identified related to the arrangements for the management of contracts and projects and this is reflected in the Annual Governance Statement (AGS) action plan.

The Committee also critically reviews the AGS and associated action plan to ensure any significant governance issues are appropriately addressed.

The outcome of internal audit's work in respect of 2013/14 will be summarised and reported to Civic Affairs as part of the Head of Internal Audit's Annual Audit Opinion and Annual Governance Statements (AGS) at the meeting in June 2014. The mid-year audit opinion progress report (reported in November 2013) identified no critical actions arising from audit findings.

In December 2012 Council officers identified errors in the budget forecasts contained within the September 2012 Medium Term Strategy (MTS), which understated the Council's spending requirements. As a result, the process and key systems which underpin the budgeting and forecasting process were reviewed by both Council officers and the Council's external auditors, Ernst & Young.

The reviews provided assurance with regard to the process followed to produce revised estimates, and established an action plan to further strengthen the Council's control processes for the future. These actions have been implemented, and Internal Audit have reviewed the process adopted for the 2014/15 Budget to provide additional assurance.

- *Actual, suspected or alleged frauds during 2013/14?*

Investigations into alleged fraud are summarised in the Annual Report on the Prevention of Fraud and Corruption Policy presented annually to the Committee.

The Committee and Internal Audit are not aware of any frauds which would have a material impact on the financial statements.

4. Is the Committee aware of any organisational or management pressure to meet financial or operating targets?

The Council uses a number of financial and operating targets; for example, Cost Centre Managers and Directors are expected to manage their budgets within cash limits. However, targets are flexed as appropriate and there is a revised budget process in each financial year which is designed to identify and manage unavoidable budget variances and agree appropriate remedial actions.

5. How does the Committee gain assurance that all relevant laws and regulations have been complied with? Are you aware of any instances of non-compliance during 2013/14?

There are specific legal responsibilities on the Council's Statutory Officers (Head of Paid Service, Monitoring Officer and Section 151 Officer) to report on aspects of compliance with relevant laws and regulations.

Internal Audit's annual plan contains a programme of work that includes reviews of compliance with policies, procedures, laws and regulations. In addition, work is carried out by other inspection agencies.

The process for compiling the Annual Governance Statement includes consideration of compliance with laws and regulations.

The Committee is not aware of any non-compliance which could have a material impact on the financial statements.

6. Is the Committee aware of any actual or potential litigation or claims that would affect the financial statements?

The Committee is not aware of any actual or potential litigation or claims that would have a material impact on the financial statements. As part of the preparation of the financial statements for 2013/14 officers will consider the accounting treatment of such items and any which are significant will be reported to the Committee.

7. How does the Committee satisfy itself that it is appropriate to adopt the going concern basis in preparing the financial statements?

Local Authorities derive their powers from statute. The assumption that a local authority's services will continue to operate for the foreseeable future is made because local authorities carry out functions essential to the local community and are themselves revenue-raising bodies (albeit within certain limits set by statute/central government). If an authority were in financial difficulty, the prospects are thus that alternative arrangements might be made by central government for the continuation of the services.

In addition the financial position of the Council also indicates that the going concern basis is appropriate:

- The Council has significant income-generating net assets (£485 million at 31 March 2013). These net assets include a significant property portfolio.
- Cash deposits and short term investments exceeded £88 million at 21 February 2014.
- The Council has significant usable reserves (£60 million at 31 March 2013).
- The Council has a detailed medium term financial strategy which ensures the achievement of a balanced budget and financial position across a five year period and provides for a minimum and target level of General Fund Reserves. Similar financial planning is undertaken for the Housing Revenue Account.
- Longer term projections are also made to demonstrate sustainability over a 25 year period and to highlight any significant longer-term implications of budget proposals and decisions.

Yours sincerely

Councillor Colin Rosenstiel
Chair of Civic Affairs Committee

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20 March 2014

Dear Ms Pritchard-Wooles

Understanding Management Processes and Arrangements

I am writing in response to your letter of 11 February 2014 regarding the above.

I have considered the questions that you raised, consulted appropriate colleagues, and to the best of my knowledge set out below my responses to each of the points in turn.

(1) What are management processes in relation to:

- *Undertaking as assessment of the risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments)*

The Council's overall assessment of the risks that the financial statements may be materially misstated is reflected by the inclusion, in the corporate risk register, of identified risks, control measures in place and any additional actions required. The Council's risk register provides a real-time overview of all risks identified, and the register is formally reviewed at key stages in the year. This oversight helps ensure that any changes to control measures are identified and / or actions agreed and delivered to mitigate risks.

The Internal Audit Plan is designed to allow Internal Audit to offer an opinion on the adequacy and effectiveness of the Council's risk management, control and governance processes. The plan has been broken down into a number of areas:

- Core systems assurance work. This work covers the Council's key financial systems and provides external audit with assurance on their control.
- Annual governance and assurance work;
- Corporate/cross cutting audit;
- Key contracts and projects; and
- Departmental specific audits.

The programme of audit work for 2013/14 was agreed by Civic Affairs in March 2013.

The Council's financial statements are prepared substantially from information held in its Financial Management System together with information held on other systems which feed into it.

Internal Audit's work includes review of the Council's fundamental financial systems in order to gain assurance that the systems of financial control are in place and operating effectively.

Cumulative monthly budgetary control reports are prepared and distributed electronically to cost centre managers and Directors. Variances from budget over £10,000 are highlighted. Overall budget variances, together with explanations of individual major variances (those over £20,000) are reported to Senior Leadership Team and to Executive Councillors at key points throughout the year.

The financial statements are reconciled to the Oracle Financial Management system and the outturn reports distributed to management to ensure the consistency and integrity of the data.

- *Identifying and responding to risks of fraud in the Authority, including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist*

The work of Internal Audit includes identifying those systems or transactions which may be more susceptible to fraud and these areas are appropriately covered by the Internal Audit Plan.

The corporate risk register will also reflect areas where there is a greater susceptibility to fraud, and actions taken to mitigate such risks.

This is supplemented by the work undertaken as part of the National Fraud Initiative (NFI), using data matching to identify issues for investigation.

- *Communicating to employees its views on business practice and ethical behaviour (for example by updating, communicating and monitoring against the Authority's code of conduct)*

Employees are required to follow the Council's Employee Code of Conduct which is available on the intranet. A number of minor updates will be published and publicised to staff in March 2014. Employees are further governed by the Council's HR policies which are also available on the intranet.

All offers of gifts and hospitality, regardless of whether the offer was accepted or declined, must be recorded and the records are regularly reviewed. Additional guidance on this topic is available to employees in the form of a set of 'Frequently Asked Questions'.

Guidance and training is available in areas where there may be specific ethical/probity considerations such as procurement.

- *Encouraging employees to report their concerns about fraud*

There is a Whistleblowing policy which staff are made aware of and which is available on the intranet. This is supplemented by other HR policies which are all available on the intranet.

Third parties are also able to report concerns through the Council's complaints procedure which includes an Independent Complaints Investigator.

- *Communicating to the Audit Committee (i.e. those charged with governance) the processes for identifying and responding to fraud and error.*

Fraud and Irregularity investigations are normally reported annually to Civic Affairs and will next be reported in June 2014. This covers Internal Audit work as well as that of the Revenue and Benefits Services Fraud Prevention Team.

The Head of Internal Audit, Directors, the Leader of the Council, relevant Executive Councillor and the Council's External Auditors receive copies of the final versions of all Internal Audit reports. Copies of Executive Summaries are sent to the Chief Executive and the Council's Monitoring Officer; in addition, final reports are available on request to other Councillors and arrangements are being made to enable secure access to these via the intranet.

(2) What are Management's views about whether there are areas within the organisation that are at risk of fraud?

Management ensures that there is appropriate internal control and segregation of duties over areas which are considered to be at a higher risk of fraud.

For example:

Treasury Management transactions require authorisation by two senior officers using bank security devices. Monthly treasury management activity is reported to the Executive Councillor for Customer Services and Resources and Leader of the Council.

There are specific controls over the input and validation of invoices for payment and strict segregation of these duties from cheque and BACS payment authorisations, which are undertaken by authorised senior managers. There are also specific controls over the creation of new suppliers records within the financial management system.

The payment of Council Tax and Housing benefits is also an area susceptible to fraud and the Council has a specific Revenue and Benefits Fraud Prevention Team.

(3) Does Management have knowledge of any actual or suspected or alleged instances of fraud?

Management is not aware at this time of any actual, suspected or alleged instances of fraud which are likely to have a material effect on the council's financial statements.

(4) Is Management satisfied that internal controls to prevent and detect fraud, including segregation of duties, exist and work effectively?

The Internal Audit Plan is designed to give assurance that internal controls are working effectively. The Head of Internal Audit will report his opinion in relation to 2013/14 to Civic Affairs in June 2014. However, based on the audit opinion progress report presented to Civic Affairs in November 2013 and Internal Audit Reports finalised and issued since that date, Management is not aware of any significant concerns.

(5) Are there any deficiencies in internal control?

Internal Audit report on deficiencies in internal control as part of their audit work. The outcome of this work in respect of 2013/14 will be summarised and reported to Civic Affairs as part of the Head of Internal Audit's Annual Audit Opinion and Annual Governance Statements (AGS) at the meeting in June 2014. The mid-year audit opinion progress report identified no critical actions arising from audit findings and at this time there are no further finalised audit reports with critical actions.

In December 2012 Council officers identified errors in the budget forecasts contained within the September 2012 Medium Term Strategy (MTS), which understated the Council's spending requirements. As a result, the process and key systems which underpin the budgeting and forecasting process were reviewed by both Council officers and the Council's external auditors, Ernst & Young.

The reviews provided assurance with regard to the process followed to produce revised estimates, and established an action plan to further strengthen the Council's control processes for the future. These actions have been implemented, and Internal Audit have reviewed the process adopted for the 2014/15 Budget to provide additional assurance.

(6) Are you aware of any instances where controls have been overridden?

Management is not, at this time, aware of any deliberate overriding of controls which could have a material effect on the financial statements.

(7) Is there any organisational or management pressure to meet financial or operating targets?

The Council uses a number of financial and operating targets. For example, Cost Centre Managers and Directors are expected to manage their budgets within cash limits. However, targets are flexed as appropriate and there is a revised budget process in each financial year which is designed to identify unavoidable budget pressures and agree appropriate remedial actions.

(8) Are there any particular areas of the accounts that are more susceptible to false entries or omissions or other forms of manipulation? Are management aware of any such manipulation having occurred?

There are no particular areas of the accounts that Management considers to be susceptible to manipulation. No officers are incentivised on the basis of financial performance. Management is not aware of any such manipulation having occurred.

(9) How does management gain assurance that all relevant laws and regulations have been complied with? Have there been any instances of non-compliance during 2013/14?

The Council's Constitution sets out how budgetary and policy decisions are made. Officers are required to ensure compliance with relevant laws and regulations and all reports include a section on legal implications which must be completed.

There are specific legal responsibilities on the Council's Statutory Officers (Head of Paid Service, Monitoring Officer and Section 151 Officer) to report on aspects of compliance with relevant laws and regulations.

Internal Audit's annual plan contains a programme of work that includes reviews of compliance with policies, procedures, laws and regulations. In addition, work is carried out by other inspection agencies.

(10) Are there any actual or potential litigation or claims that would affect the financial statements?

As part of the closedown process the Council will assess the adequacy of provisions for liabilities arising from current or potential future litigation and claims. The Council will also consider whether there are any contingent liabilities which may require disclosure.

(11) How does management satisfy itself that is appropriate to adopt the going concern basis in preparing the financial statements?

Local Authorities derive their powers from statute. The assumption that a local authority's services will continue to operate for the foreseeable future is made because local authorities carry out functions essential to the local community and are themselves revenue-raising bodies (with limits on their revenue-raising powers arising only at the discretion of central government). If an authority were in financial difficulty, the prospects are thus that alternative arrangements might be made by central government either for the continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year.

The abolition of an authority or the transfer of some of its services could bring the going concern assumption into question. However, the Code of Practice on Local Authority Accounting makes clear that combinations of public sector bodies are not to be taken as negating the presumption of going concern. Even if assets are to be taken from an authority, with perhaps no compensation, the continued use of the property for the public benefit means that the authority does not need to consider the restriction on its own ability to make use of the property from the going concern perspective.

In addition to these statutory considerations, the financial position of the Council also indicates that the going concern basis is appropriate:

- The Council has significant net assets (£485 million at 31 March 2013.) These net assets include a significant property portfolio.
- Cash deposits and short term investments exceed £88 million at 21 February 2014.
- The Council has significant usable reserves (£60 million at 31 March 2013.)
- The Council has a detailed Medium Term Financial Strategy which ensures the achievement of a balanced budget and financial position across a five year period and provides for a minimum and target level of General Fund Reserves. Similar financial planning is undertaken for the Housing Revenue Account.
- Longer term projections are also made to demonstrate sustainability over a 25 year period and to highlight any significant longer-term implications of budget proposals and decisions.

Yours sincerely

Alex Colyer
Section 151 Officer