



cutting through complexity

Report to those charged with governance (ISA 260) 2014/15 – supplementary report

Rutland County Council

September 2015

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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 issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on Public Sector Audit Appointment's website (www.psa.co.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.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Tony Crawley the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Trevor Rees (on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

This document updates the Audit and Risk Committee on:

- **our audit of the financial statements for the year ended 31 March 2015 for the Authority, and our proposed opinion; and**
- **our work in assessing the Authority's arrangements to secure value for money and our proposed conclusion based on that work.**
- **The status of our Audit Certificate.**

Scope of this report

This report updates the Audit and Risk Committee on the key findings arising from:

- our audit work at Rutland County Council ('the Authority') in relation to the Authority's 2014/15 financial statements; and
- the work to support our 2014/15 conclusion on the Authority's arrangements to secure economy, efficiency and effectiveness in its use of resources ('VFM conclusion').

The report supplements our first report to the Committee and is to be discussed with the Audit and Risk Committee on 22 September 2015.

This report also updates the Audit and Risk Committee on the status of our Audit Certificate

Financial statements and Annual Governance Statement

We have completed the remaining audit procedures and there are no additional items that we need to report to you. The explanatory foreword to the draft financial statements has been updated to reflect the impact on the Council's medium term financial outlook of the estimated additional costs arising from the loss of Section 106 developer contributions for the Oakham North Development.

The Annual Governance Statement, which is published alongside the financial statements, has also been updated to reflect the significant control matters relating to the Oakham North Development issue, and the actions taken by the Council.

VFM conclusion

Our *External Audit Plan 2014/15* explained our risk-based approach to VFM work. Our work to support our 2014/15 VFM conclusion has included:

- assessing the potential VFM risks and identifying the residual audit risks for our VFM conclusion;
- considering the results of any relevant work by the Authority and other inspectorates and review agencies in relation to these risk areas;
- carrying out additional risk based work.

As part of the additional risk based work carried out we have considered the issues regarding the Oakham North Development, and the reported loss of an estimated total £1.88m in Section 106 developer contributions. In Section 3 we have reported our findings and proposed conclusion. Based on the findings of our work, we plan to issue a qualified VFM conclusion.

Audit Certificate

We have considered the matters identified during our audit in relation to our broader external audit statutory responsibilities and at this stage are proposing to delay the issue of our Audit Certificate that closes the audit.

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 from this report for the Authority. The remainder of this report provides further details on the proposed Value for Money Conclusion and the status of the Audit Certificate.

Proposed audit opinion	<p>We anticipate issuing an unqualified audit opinion on the Authority's amended financial statements by 30 September 2015. We expect to confirm that the updated Annual Governance Statement included with the amended financial statements is consistent with our understanding.</p>
Value for Money Conclusion	<p>Based on the findings of our work, we plan to issue a qualified VFM conclusion. We anticipate that it will be an 'except for' opinion in respect of the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources. This is based on the issues identified in relation to the Oakham North Development Section 106 Agreement and weaknesses in the Authority's arrangements which led to the estimated loss of developer contribution funding. We have set out in detail the basis of our conclusion in section three.</p>
Audit Certificate	<p>We are proposing to delay the issue of our Audit Certificate closing the audit. This is to enable us to complete our consideration of the Oakham North Development Section 106 Agreement issues in relation to our broader external audit statutory responsibilities. We will update officers and the Audit and Risk Committee when we are able to do so.</p>

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

We have considered the impact of the reported mistake made by the Council in relation to the Section 106 agreement for the Oakham North Development.

Background

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.

Work completed

In line with the risk-based approach set out in our *External Audit Plan* we have:

- assessed the Authority's key business risks which are relevant to our VFM conclusion;
- identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- considered the results of relevant work by the Authority, inspectorates and review agencies in relation to these risk areas; and
- completed specific local risk based work.

Key findings

In our *External Audit Plan 2014/15* issued in April 2015 we did not highlight any specific significant risks to the value for money conclusion. We reported that we would continue to keep our risk assessment up to date and take any additional factors into account before issuing our final value for money conclusion.

In the rest of this section of this report, we have highlighted a significant risk which was identified after our External audit Plan 2014/15 was issued and which has led us to propose a qualified conclusion for this year.

Oakham North Development and Section 106 Contributions

In June 2015 the Chief Executive and Director of Resources brought to our attention significant issues which were relevant to our auditor responsibilities relating to the Oakham North development.

In response to matters raised by the developer in April 2015, officers had concluded that following a mistake by the Planning Team there was no Section 106 Agreement in place for the new planning permission issued in 2012. This new permission was issued following the processing of an application for a variation to the original 2011 planning permission. The developer had informed the Council that it considered that it was not legally liable for any Section 106 contributions for the development carried out under the new permission and was therefore refusing the Council's request for payment.

Officers investigated the matter and following discussions with their legal advisors, and the developer concluded that the existing Section 106 Agreement was not enforceable under the new permission. Up to £7.6m in contributions was potentially due to the Council and its partners (Police, Fire and health bodies) under the original Agreement over the life of the development.

Council members were briefed in private in July 2015 on the issues and the steps being taken by officers to resolve the matter in hand.

The Full Council meeting of 14 September 2015 received an update report from the Chief Executive on the relevant issues, and progress made to date. The Council considered the report in open session and:

- Approved the settlement of £4.8m negotiated with the developer; and
- Delegated authority to the Chief Executive and Portfolio Holder for Places (Development and Economy) to sign on behalf of the Council the final agreement to allow the proposed arrangements to take effect. The Agreement has now been signed.

The report provided a detailed background to the issues and the sequence of events leading up to these recommendations, including acknowledging that errors were made. The Authority has also brought the public's attention to the issue and its report through press releases and notices on its website. We have not therefore repeated the full detail in this report.

We have considered the impact of the reported mistake made by the Council in relation to the Section 106 agreement for the Oakham North Development.

We have proposed a qualified Value for Money Conclusion for 2014/15.

We have examined relevant background documentation to the report, including:

- Correspondence between the Council and the developer's representatives
- the independent QC legal advice obtained by the Council;
- the independent investigator's review of the actions of officers and to identify any conflicts of interest or other probity concerns.

The report states that, due to changes in the development since the date of the original permission, the recalculated maximum contribution due under the Agreement was £6.68m. The financial loss to the Council by accepting the developer's £4.8m offer is estimated therefore (net of indexation) at £1.88m. The report sets out the potential medium term financial impact on the Council of this loss. Should the Authority need to fund the gap of £1.88m the additional revenue costs resulting from the internal financing of the capital spend (including the opportunity cost of lost investment interest) is estimated at around £79,000 per annum.

Officers are revisiting the Council's Medium Term Financial Strategy (MTFS) and the identified priority infrastructure needs, so that they can look to manage effectively the financial and service impact on residents. Managers have also taken the expected steps to investigate the circumstances which led to the mistakes being made and introduced safeguards designed to ensure they will not be repeated.

Value for Money Conclusion assessment

We have considered the impact of the matters described above in relation to our statutory Value for Money Conclusion and the two criteria specified by the Audit Commission, that is:

- Securing financial resilience; and
- Challenging how it secures economy, efficiency and effectiveness.

This development was large in the context of the Authority as a whole. The value of the estimated loss to the Council is significant and managers will need to deliver the projects required within the new total contribution or revise the MTFS to manage the ongoing financial impact. The financial planning and other financial control arrangements during

2014/15 were though consistent with established practices, although the anticipated level of Section 106 funding available to the Council was based on inaccurate assumptions and is now less than anticipated.

At this stage officers expect to be able to accommodate the estimated additional cost to the Council, should it be required, of this lost funding within the revised MTFS. This has yet to be fully evaluated though and the revised plan will need member approval. We will continue to monitor progress on this during 2015/16.

Officers have incurred additional expense in order to investigate the issue, negotiate a settlement with the developer, and had to take steps in 2015/16 to strengthen the arrangements which led to this loss occurring. This has included:

- new planning applications being reviewed by a dedicated Section 106 officer to identify any impact on existing agreements and whether further action is required; and
- a programme of retraining to ensure the Planning Team has the appropriate skills and knowledge levels to carry out their duties effectively.

Our overall assessment is that in relation to the management of the Section 106 agreement for this significant development, the arrangements in place during 2014/15 were not sufficient to secure economy, efficiency and effectiveness. This is of sufficient concern to conclude that a qualified Value for Money Conclusion in respect of this specified criterion is appropriate for 2014/15.

We are not at this stage proposing to issue the Audit Certificate.

Audit Certificate

The Audit Commission Act 1998 requires us to certify whether we have completed the audit in accordance with the requirements of the Act and the Code of Audit Practice. The effect of the certificate is to close the audit, and marks the point when the auditor's responsibilities in respect of the audit of the period covered by the certificate have been discharged.

The Code of Audit Practice recognises that there are occasions when the auditor is able to issue the audit report, including the accounts opinion and Value for Money Conclusion, but cannot certify completion of the audit as certain non-material issues remain outstanding. In these circumstances, the auditor may decide to issue their audit report ahead of certifying closure of the audit.

We are satisfied that the issues relating to the Oakham North Development Section 106 Agreement identified above are not material to the accounts opinion and have been taken into account in our proposed Value for Money Conclusion. We are though at this stage proposing to delay the issue of our Audit Certificate to enable us to complete our consideration of the issues in relation to broader audit responsibilities. We will update officers and the Audit and Risk Committee when we are able to do so.



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