

Annual Governance Report

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# Annual Governance Report

**Southampton City Council**

**Audit 2006/07**

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## Purpose of this document

- 1 In accordance with the Audit Commission's Code of Audit Practice (the Code), this report provides a summary of the work we have carried out during our 2006/07 audit of accounts, the conclusions we have reached and the recommendations we have made to discharge our statutory audit responsibilities to those charged with governance (in this case the Standards and Governance Committee) at the time they are considering the financial statements.
- 2 In preparing our report, the Code requires us to comply with the requirements of International Standards on Auditing (United Kingdom & Ireland) – ISA (UK&I) - 260 'Communication of Audit Matters to Those Charged With Governance', by reporting to you matters relating to the audit of the financial statements. Other auditing standards require us to communicate with you in other specific circumstances including:
  - where we suspect or detect fraud;
  - where there is an inconsistency between the financial statements and other information in documents containing the financial statements; and
  - non-compliance with legislative or regulatory requirements and related authorities.
- 3 We are also required to communicate to you the Audit Commission's requirements in respect of independence and objectivity, and these are set out at Appendix 2.
- 4 This report has been prepared for presentation to the Standards and Governance Committee on 28 September 2007. Members are invited to:
  - consider the matters raised in the report before the financial statements are approved;
  - approve the representation letter on behalf of the Council and those charged with governance before we issue our opinion; and
  - consider the recommendations for improvement in the action plan at Appendix 1.
- 5 Our work during the year was performed in line with the plan that we presented to you on 18 April 2006. We have issued separate reports during the year having completed specific aspects of our programme, which are listed in Appendix 3.

## Key messages

- 6 Our work on the financial statements is substantially complete, although there are still outstanding issues to be resolved. In particular, our work on agreeing social care income and debtors has yet to be concluded. Should any further matters arise in concluding the outstanding work that need to be reported, we will raise them at the meeting of the Standards and Governance Committee. In the absence of any significant issues arising from our remaining work, we expect to issue an unqualified audit opinion on 28 September 2007 (a draft report is attached at Appendix 4).
- 7 We have concerns about two key financial systems, which the Council has been unable to fully reconcile. Our assurance on the figures derived from these systems is therefore limited, although we are satisfied that any misstatements of the figures reported in the financial statements are unlikely to be material.
- 8 In our view, the Statement on Internal Control (SIC) has been prepared in accordance with proper practice specified by CIPFA and is consistent with the findings from our audit. However, it makes no reference to the reconciliation problems referred to above.
- 9 Our work on the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources is now complete. We propose issuing an unqualified conclusion on the use of resources on 28 September 2007 (a draft report is attached at Appendix 4).

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## Audit status

- 10 At the date of issue of this report, our detailed audit is substantially complete, and we expect to provide our audit certificate on 28 September 2007.
- 11 The Council has taken a positive and constructive approach to our audit and we would like to take this opportunity to express our appreciation for the assistance and co-operation of the Council and its officers.

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## Accounts and Statement on Internal Control

- 12 We will issue our audit report on the financial statements shortly once outstanding queries have been resolved.
- 13 Auditors are required to obtain written confirmation of certain representations from management and those charged with governance before an audit report is issued, such as acknowledgement of responsibility for the fair presentation of the financial statements in accordance with the applicable financial reporting framework and responsibility for the design and implementation of internal control to prevent and detect error.
- 14 The auditor should also obtain written representations from management on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist.
- 15 The final draft of the letter of representation for 2006/07 has been attached as Appendix 5.

### Unadjusted misstatements

- 16 We are required to report to you all unadjusted misstatements that we have identified during the course of our audit, other than those that are clearly trivial. There are no unadjusted misstatements for us to bring to the attention of members.

### Adjustments to the financial statements

- 17 We are also required to bring to your attention misstatements that have already been corrected by management where we consider them relevant to your wider governance responsibilities.
- 18 We have asked for a small number of adjustments to be made as a result of our audit work, and for changes to some disclosure notes, but we do not regard any of these as relevant to your wider governance responsibilities. If there are any adjustments required as a result of our remaining work, we will add details here and set out the adjustment in Appendix 6.

### Accounting practices

- 19 We are also required to report to you our view on the qualitative aspects of the Council's accounting practices and financial reporting and have set out below our observations on key issues affecting the Council.



- 20 Since the balance sheet date, the Council has entered into an agreement with Capita for a strategic service partnership. This will result in significant changes to the Council's operations, including transfer of staff, assets and responsibilities that resided with the Council during 2006/07. We therefore judged this to be a material non-adjusting post-balance sheet event, which should be disclosed in a note to the core statements. A note to this effect has now been added.
- 21 The quality of the supporting documentation for the Council's accounts was significantly improved again this year and we identified no errors of any significance in the financial statements. This is a commendable achievement, particularly viewed against the standard we found only two years ago.

## Systems of internal control

- 22 As part of our audit, we consider the systems of accounting and financial control and report to you any material weaknesses identified.
- 23 Reconciliations between the Council's Agresso main accounting system and the Academy system for council tax, non-domestic rates and benefits are carried out only at the end of each financial year. Significant discrepancies have arisen from these reconciliations, many of which officers have not been able to resolve. While we are satisfied that there is unlikely to be a material impact upon the figures reported in the financial statements, the assurance we have on them is limited. There is a need to ensure that monthly reconciliations are carried out, so that discrepancies can be rectified promptly. Officers are working to simplify procedures so that this can be achieved without undue impact upon staff resources.
- 24 The PARIS system, which processes income and expenditure associated with social care packages, cannot be reconciled with the Agresso main accounting system. Poor manual records have also meant that there is uncertainty about some of the data held on the PARIS system. While we have obtained a reasonable level of assurance on the expenditure figures, we have limited assurance to support the Council's reported figures for 2006/07 social care income and debtors. We are satisfied that it is unlikely these figures will be materially misstated in the financial statements. However, there is an urgent need to put this system on a sound footing, and to ensure by regular checks that it is consistent with other associated records. Only then can the Council have confidence that the income is being properly controlled and that clients are being appropriately billed for the services provided. We recognise that your officers are currently giving high priority to resolving these problems.
- 25 We have not provided a comprehensive statement of all weaknesses that may exist in internal control or of all improvements that may be made, but have addressed only those matters that have come to our attention as a result of the audit procedures we have performed.

- 26 We have also reviewed whether the SIC has been prepared in accordance with proper practice specified by CIPFA and is consistent with the findings from our audit. The only matter arising is that it makes no reference to the problems with reconciliation of the PARIS social care system and the Academy revenues and benefits system.

***Recommendations***

*R1 Ensure that processes are put in place for monthly reconciliations of the Academy and Agresso systems and for resolving any differences.*

*R2 Ensure that the outstanding problems with social care services invoicing are resolved, and that records are correct and regularly reconciled with Agresso.*

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## Use of resources

### Work performed

- 27 The Code requires us to reach a conclusion on whether we are satisfied that the Council has proper arrangements in place for securing economy, efficiency and effectiveness in its use of resources – the value for money conclusion. In meeting this responsibility, we review evidence that is relevant to the Council's corporate performance management and financial management arrangements across a range of criteria specified by the Audit Commission. Our work to support our conclusion comprised the following elements:
- use of resources assessment;
  - data quality work; and
  - the best value performance plan.

### Conclusion

- 28 We have now completed our work on the Council's arrangements. We aim to issue our VFM conclusion on 28 September 2007, stating that we are satisfied the Council made proper arrangements to secure value for money in its use of resources during 2006/07. The auditor's report is attached at Appendix 4.
- 29 We have reached our conclusion for 2006/07 by assessing the Council's arrangements against twelve criteria specified by the Audit Commission, eight of which are linked directly to related judgements in our CPA Use of Resources assessment. Our conclusions for each of the criteria are set out in Appendix 7 and the key issues of note are summarised below.

### Summary

- 30 Last year we qualified the Council's VFM Conclusion in relation to its arrangements to maintain a sound system of internal control and to manage its significant business risks. Since that time the Council has taken appropriate action to resolve these weaknesses. In particular it has:
- strengthened its risk management arrangements. Business plan key priorities are now risk assessed and the processes for reviewing and updating risk registers are embedded. Responsibility for risk management has now been formally assigned to an appropriate member group;
  - made some significant improvements in the systems of internal control. There is now an Audit Committee in place, and greater status is accorded to the audit function. There is stronger management of the Internal Audit team and sound audit processes are being developed;

- significantly strengthened the management of housing benefits, and the problems that have beset the service in recent years are now being resolved; and
  - taken action to strengthen capital project management, which should help to ensure much better control over capital spending.
- 31 In other areas the Council has sustained and improved its performance since our 2005/06 assessment. In particular it has:
- worked with its partners to secure a Local Area Agreement commencing in April 2007. This is a key mechanism for delivery of many of the Council's and its partners' objectives over the next three years;
  - further strengthened its culture of performance management. Senior officers and members consider regular monitoring reports, focused on the Council's priorities and making use of a corporate scorecard and traffic-light indicator approach;
  - tackled weaknesses in its management of the 'organisational futures' initiative, the capital programme and performance management of partnerships;
  - strengthened its approach to achieving value for money through its use of cost and performance benchmarking and targeting of resources to poorly performing services; and
  - improved its procurement arrangements, although this is still work in progress and procurement savings planned for 2006/07 were not all achieved.

## Use of resources assessment

- 32 We are currently finalising our report arising from our use of resources assessment. When finalised, we will discuss this with the relevant officers, and will report our conclusions and assessments in our Annual Audit and Inspection Letter in early 2008.

## Data quality work

- 33 We are currently finalising our data quality review and will report our findings to officers shortly.
- 34 We have completed our review of the Council's arrangements for managing data quality. Our conclusions have informed our judgement on one criterion of the VFM conclusion reported in Appendix 7 and our risk assessment for spot checks of performance indicators.

## Best value performance plan

- 35 Our work in respect of the Council's 2006/07 Best Value Performance Plan (the Corporate Improvement Plan) was reported in the 2006 annual audit and inspection letter. No recommendations were made to the Audit Commission or the Secretary of State. The 2007/08 Best Value Performance Plan audit will be reported in the Annual Audit and Inspection Letter in early 2008.

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## Audit fee update

- 36 We reported our fee proposals as part of the Audit Plan for 2006/07. The table below reports the outturn fee against that plan:

	<b>Plan 2006/07</b>	<b>Expected Actual 2006/07</b>
Financial statements and Statement on Internal Control	£171,480	£171,480
Use of Resources	£ 84,720	£ 84,720
Total Audit Fees	£256,200	£256,200
Other work	n/a	n/a

- 37 The analysis above shows that our audit fee has been contained within the totals you agreed in April 2006.
- 38 The outturns for inspection and grant claims fees will be reported in the annual audit and inspection letter.

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## Appendix 1 – Action plan

Page	Recommendation	Priority 1 = Low 2 = Medium 3 = High	Responsibility	Agreed	Comments	Anticipated Implementation Date
10	R1 Ensure that processes are put in place for monthly reconciliations of the Academy and Agresso systems and for resolving any differences.	3				
10	R2 Ensure that the outstanding problems with social care services invoicing are resolved, and that records are correct and regularly reconciled with Agresso.	3				

## Appendix 2 – The Audit Commission’s requirements in respect of independence and objectivity

- 1 We are required to communicate the following matters to those charged with governance:
  - the principal threats, if any, to objectivity and independence identified by the auditor, including consideration of all relationships between the Council, directors and the auditor;
  - any safeguards adopted and the reasons why they are considered to be effective;
  - any independent partner review;
  - the overall assessment of threats and safeguards; and
  - information about the general policies and processes for maintaining objectivity and independence.
- 2 We are not aware of any relationships that may affect the independence and objectivity of the audit team and which are required to be disclosed under auditing and ethical standards.



## Appendix 3 – Audit reports issued

Planned output	Planned date of issue	Actual date of issue	Addressee
Audit plan	March 2006	March 2006	S&G Committee
Interim audit memorandum	May 2007	June 2007	Strategic Director of Resources
Annual governance report	September 2007	September 2007	S&G Committee
Opinion on financial statements	September 2007	September 2007	S&G Committee
Use of resources conclusion	September 2007	September 2007	S&G Committee
Final accounts memorandum	October 2007	Not yet due	Strategic Director of Resources
BVPP report	October 2006	December 2006	Chief Executive
Data quality report	September 2006	January 2007	Chief Executive
Performance reports - SSP	Not specified	September 2006 & March 2007	Chief Executive
Annual audit letter	December 2007	Now due February 2008	S&G Committee

## **Appendix 4 – Proposed auditor's report**

### **Auditor's report to the Members of Southampton City Council**

#### **Opinion on the financial statements**

I have audited the financial statements of Southampton City Council for the year ended 31 March 2007 under the Audit Commission Act 1998, which comprise the Explanatory Foreword, Income and Expenditure Account, Statement of the Movement on the General Fund Balance, the Balance Sheet, the Statement of Total Recognised Gains and Losses, the Cash Flow Statement, the Housing Revenue Account, the Collection Fund and the related notes. These financial statements have been prepared under the accounting policies set out within them.

This report is made solely to Southampton City Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 36 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by the Audit Commission.

#### **Respective responsibilities of the Chief Finance Officer and auditors**

The Chief Finance Officer's responsibilities for preparing the financial statements in accordance with applicable laws and regulations and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2006 are set out in the Statement of Responsibilities.

My responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

I report to you my opinion as to whether the financial statements present fairly the financial position of the Council in accordance with applicable laws and regulations and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2006.

I review whether the statement on internal control reflects compliance with CIPFA’s guidance: ‘The statement on internal control in local government: meeting the requirements of the Accounts and Audit Regulations 2003’ issued in April 2004. I report if it does not comply with proper practices specified by CIPFA or if the statement is misleading or inconsistent with other information I am aware of from my audit of the financial statements. I am not required to consider, nor have I considered, whether the statement on internal control covers all risks and controls. I am also not required to form an opinion on the effectiveness of the Council’s corporate governance procedures or its risk and control procedures

## Basis of audit opinion

I conducted my audit in accordance with the Audit Commission Act 1998, the Code of Audit Practice issued by the Audit Commission and International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the Council in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Council’s circumstances, consistently applied and adequately disclosed.

I planned and performed my audit so as to obtain all the information and explanations which I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements.

## Opinion

In my opinion the financial statements present fairly, in accordance with applicable laws and regulations and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2006, the financial position of the Council as at 31 March 2007 and its income and expenditure for the year then ended.

**Stephen Taylor, District Auditor**

Audit Commission, North Wing, Southern House, Sparrowgrove, Otterbourne, Winchester, SO21 2RU

Date

## **Conclusion on arrangements for securing economy, efficiency and effectiveness in the use of resources**

### **Council's Responsibilities**

The Council is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to regularly review the adequacy and effectiveness of these arrangements.

Under the Local Government Act 1999, the Council is required to prepare and publish a best value performance plan summarising the Council's assessment of its performance and position in relation to its statutory duty to make arrangements to ensure continuous improvement in the way in which its functions are exercised, having regard to a combination of economy, efficiency and effectiveness.

### **Auditor's Responsibilities**

I am required by the Audit Commission Act 1998 to be satisfied that proper arrangements have been made by the Council for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion in relation to proper arrangements, having regard to relevant criteria specified by the Audit Commission for principal local authorities. I report if significant matters have come to my attention which prevent me from concluding that the Council has made such proper arrangements. I am not required to consider, nor have I considered, whether all aspects of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

I am required by section 7 of the Local Government Act 1999 to carry out an audit of the Council's best value performance plan and issue a report:

- certifying that I have done so;
- stating whether I believe that the plan has been prepared and published in accordance with statutory requirements set out in section 6 of the Local Government Act 1999 and statutory guidance; and
- where relevant, making any recommendations under section 7 of the Local Government Act 1999.

## Conclusion

I have undertaken my audit in accordance with the Code of Audit Practice and having regard to the criteria for principal local authorities specified by the Audit Commission and published in December 2006, I am satisfied that, in all significant respects, Southampton City Council made proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2007.

## Best Value Performance Plan

I issued my statutory report on the audit of the Council’s best value performance plan (the Corporate Improvement Plan) for the financial year 2006/07 on 14 December 2006. I did not identify any matters to be reported to the Council and did not make any recommendations on procedures in relation to the plan.

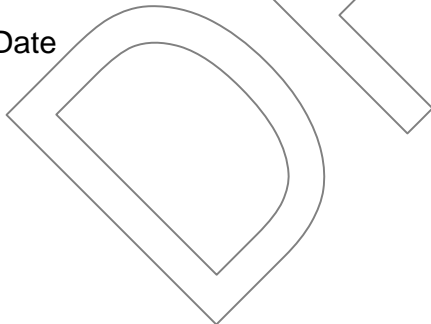
## Certificate

I certify that I have completed the audit of the accounts in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

**Stephen Taylor, District Auditor**

Audit Commission, North Wing, Southern House, Sparrowgrove, Otterbourne, Winchester, SO21 2RU

Date



## Appendix 5 – Management representation letter

To: Stephen Taylor  
District Auditor  
Audit Commission  
North Wing  
Southern House  
Sparrowgrove  
Otterbourne  
Winchester  
Hampshire  
SO21 2RU

### Southampton City Council - Audit for the year ended 31 March 2007

We confirm to the best of our knowledge and belief, having made appropriate enquiries of Directors and other officers of Southampton City Council, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2007.

We acknowledge our responsibilities under the relevant statutory authorities for preparing the financial statements which present fairly and for making accurate representations to you. We acknowledge our responsibilities under the relevant statutory authorities to prepare the Council's accounts in accordance with proper practices as defined in relevant legislation or guidance.

The Council has no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

### Specific representations

Sufficient controls have been established, and have operated, to identify, classify and record correctly transactions processed via the Council's bank account.

There are no other material amounts relating to unfunded liabilities, curtailments or settlements of past service costs relating to pension provision other than those which have been properly recorded and disclosed in the financial statements.

The Council considered the data provided by the actuary for the FRS17 calculations and has concluded that it represents a true and fair view for the purposes of the calculations produced.

## **Supporting records**

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Council have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Councillors meetings, have been made available to you.

## **Related party transactions**

We confirm the completeness of the information provided regarding the identification of related parties.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements

## **Contingent liabilities**

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements; and,
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements;
- no financial guarantees have been given to third parties
- there are no significant claims from employees for back-pay relating to single status or equal pay arrangements.

## **Law, regulations and codes of practice**

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the Council.

We acknowledge our responsibility for the design and implementation of internal control systems to prevent and detect error.

There have been no:

- irregularities involving management or employees who have significant roles in the system of internal accounting control;
- irregularities involving other employees that could have a material effect on the financial statements;
- communications from regulatory agencies concerning non-compliance with or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

**Post balance sheet events**

Since the date of approval of the financial statements by Members of the Council, no additional significant post balance sheet events have occurred which would require additional adjustment or disclosure in the financial statements.

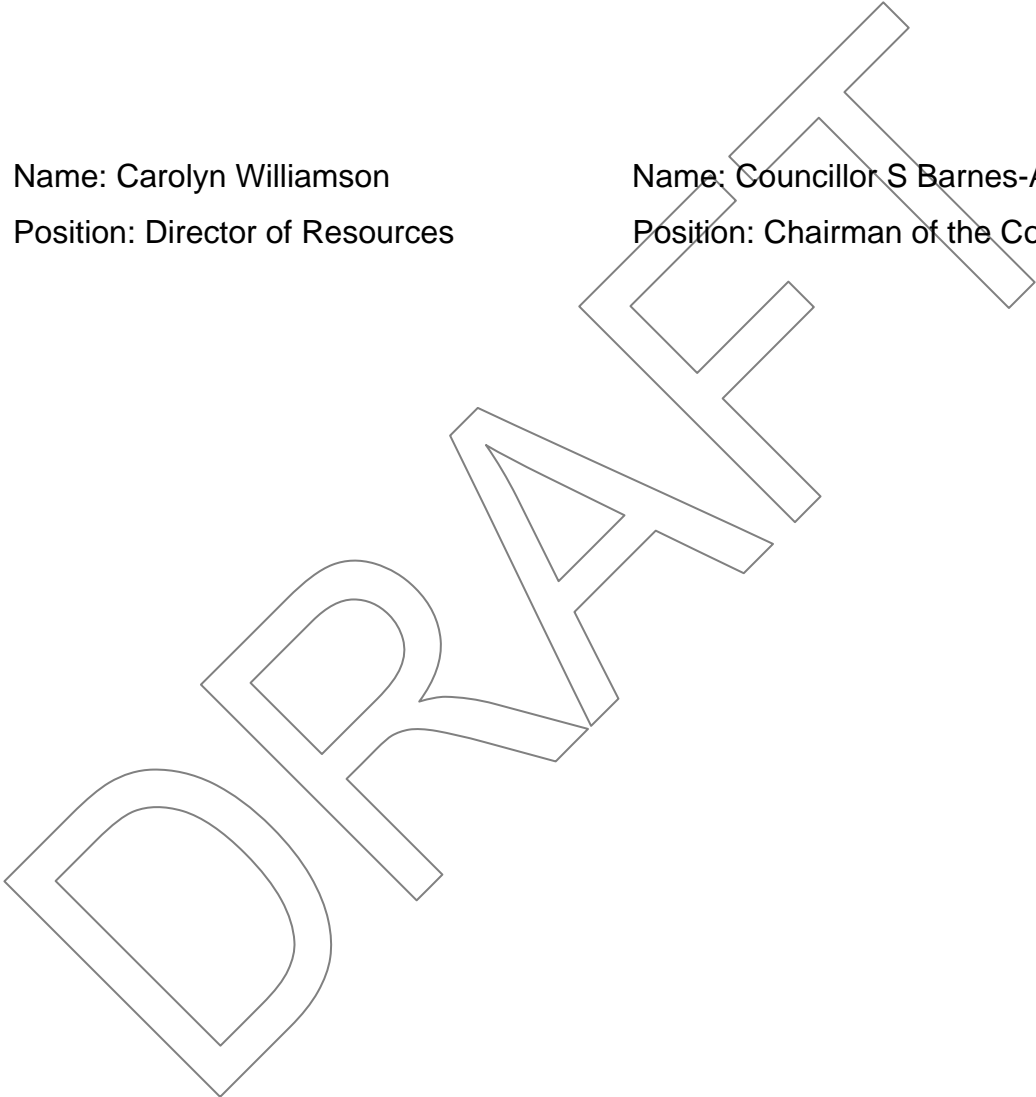
Signed on behalf of Southampton City Council

Signed

Signed

Name: Carolyn Williamson  
Position: Director of Resources

Name: Councillor S Barnes-Andrews  
Position: Chairman of the Council

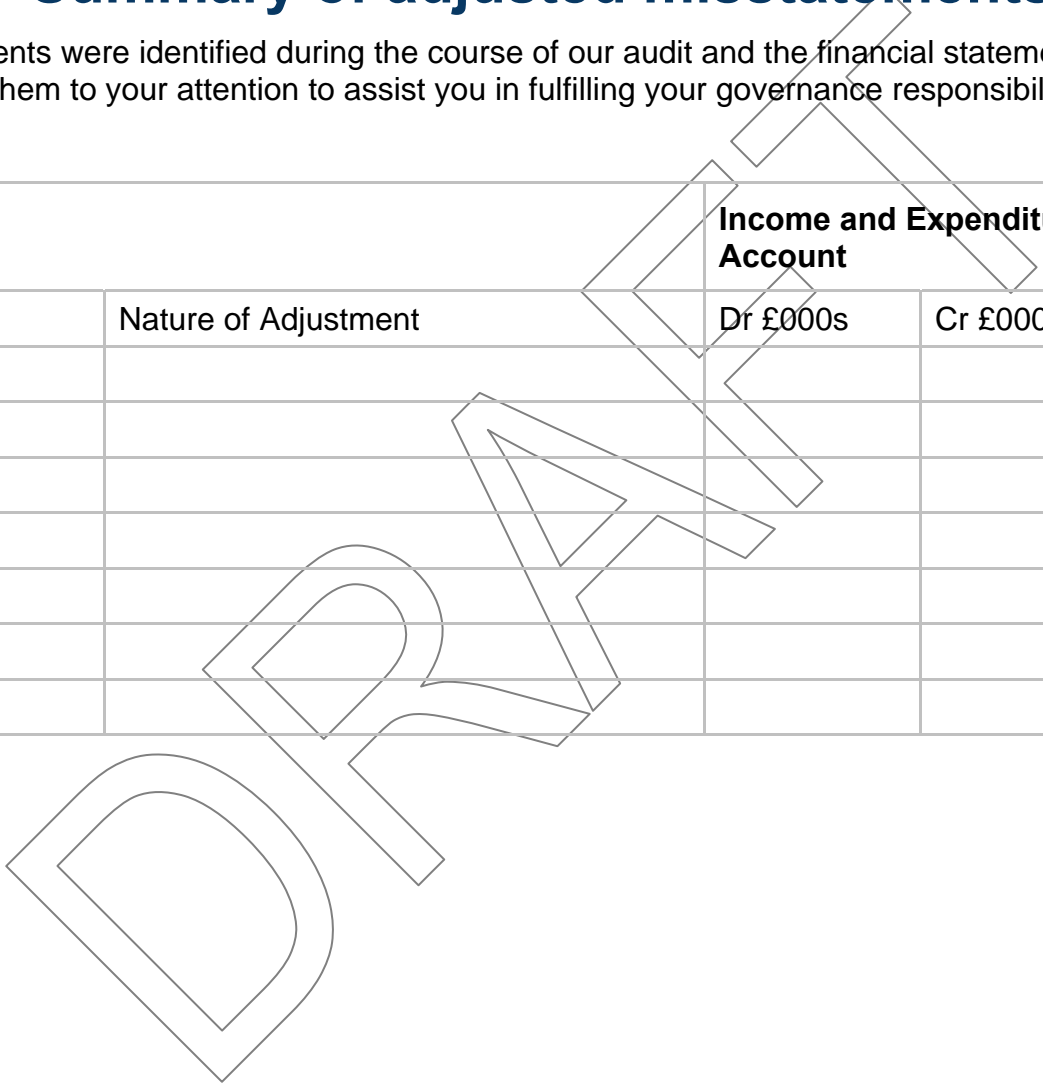




## Appendix 6 – Summary of adjusted misstatements

The following misstatements were identified during the course of our audit and the financial statements have been adjusted by management. We bring them to your attention to assist you in fulfilling your governance responsibilities.

Adjusted misstatements	Nature of Adjustment	Income and Expenditure Account		Balance Sheet	
		Dr £000s	Cr £000s	Dr £000s	Cr £000s
[None at this stage]					



## Appendix 7 – Value for money conclusion

The Audit Commission has published, in accordance with the Code of Audit Practice, 12 criteria on which auditors are required to reach a conclusion on the adequacy of an audited body’s arrangements for economy, efficiency and effectiveness in its use of resources.

The Code criteria are linked to the use of resources assessment (UoR) key lines of enquiry (KLoEs). A score of Level 2 or higher under the KLoEs will result in an assessment that the Council has adequate arrangements in place for the purposes of the Code criteria. The Code criteria and the linked KLoEs are show in the table below.

Code Criteria	Description	Associated UoR KLoE	UoR Score	VFM Conclusion
1	The body has put in place arrangements for setting, reviewing and implementing its strategic and operational objectives.	N/A	N/A	Yes
2	The body has put in place channels of communication with service users and other stakeholders including partners, and there are monitoring arrangements to ensure that key messages about services are taken into account.	N/A	N/A	Yes
3	The body has put in place arrangements for monitoring and scrutiny of performance, to identify potential variances against strategic objectives, standards and targets, for taking action where necessary, and reporting to members.	N/A	N/A	Yes
4	The body has put in place arrangements to monitor the quality of its published performance information, and to report the results to members.	LG DQ KLoEs	N/A	Yes
5	The body has put in place arrangements to maintain a sound system of internal control.	4.2	Not yet finalised	Yes

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6	The body has put in place arrangements to manage its significant business risks.	4.1	Not yet finalised	Yes
7	The body has put in place arrangements to manage and improve value for money.	5.2	Not yet finalised	Yes
8	The body has put in place a medium-term financial strategy, budgets and a capital programme that are soundly based and designed to deliver its strategic priorities.	2.1	Not yet finalised	Yes
9	The body has put in place arrangements to ensure that its spending matches its available resources.	3.1	Not yet finalised	Yes
10	The body has put in place arrangements for managing performance against budgets.	2.2	Not yet finalised	Yes
11	The body has put in place arrangements for the management of its asset base.	2.3	Not yet finalised	Yes
12	The body has put in place arrangements that are designed to promote and ensure probity and propriety in the conduct of its business.	4.3	Not yet finalised	Yes

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