# The Audit Findings for Birmingham City Council

**Year ended 31 March 2016**

September 2016


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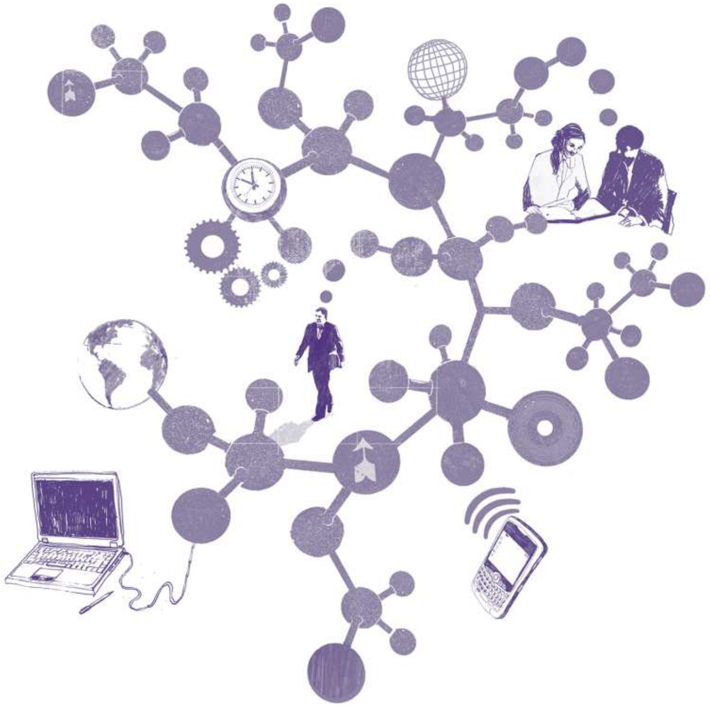

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12 September 2016

Dear Members of the Audit Committee

**Audit Findings for Birmingham City Council for the year ending 31 March 2016**

This Audit Findings report highlights the key findings arising from the audit for the benefit of those charged with governance (in the case of Birmingham City Council, the Authority's Cabinet), as required by International Standard on Auditing (UK & Ireland) 260, the Local Audit and Accountability Act 2014 and the National Audit Office Code of Audit Practice. Its contents have been discussed with officers.

As auditors we are responsible for performing the audit, in accordance with International Standards on Auditing (UK & Ireland), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements and giving a value for money conclusion. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

We would like to take this opportunity to record our appreciation for the kind assistance provided by the finance team and other staff during our audit.

Yours sincerely

Phil W Jones

Engagement lead

# Contents

# Section 1: Executive summary

## Purpose of this report

This report highlights the key issues affecting the results of Birmingham City Council ('the Council') and the preparation of the group and Council's financial statements for the year ended 31 March 2016. It is also used to report our audit findings to management and those charged with governance in accordance with the requirements of International Standard on Auditing (UK & Ireland) 260, and the Local Audit and Accountability Act 2014 ('the Act').

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Council's financial statements give a true and fair view of the financial position of the Council and its income and expenditure for the year and whether they have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting.

We are also required to consider other information published together with the audited financial statements, whether it is consistent with the financial statements and in line with required guidance.

We are required to carry out sufficient work to satisfy ourselves on whether the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion').

Auditor Guidance Note 7 (AGN07) clarifies our reporting requirements in the Code and the Act. We are required to provide a conclusion whether in all significant respects, the Council has put in place proper arrangements to secure value for money through economic, efficient and effective use of its resources for the relevant period.

The Act also details the following additional powers and duties for local government auditors, which we are required to report to you if applied:

- a public interest report if we identify any matter that comes to our attention in the course of the audit that in our opinion should be considered by the Council or brought to the public's attention (section 24 of the Act);
- written recommendations which should be considered by the Council and responded to publicly (section 24 of the Act);
- application to the court for a declaration that an item of account is contrary to law (section 28 of the Act);
- issue of an advisory notice (section 29 of the Act); and
- application for judicial review (section 31 of the Act)

We are also required to give electors the opportunity to raise questions about the accounts and consider and decide upon objections received in relation to the accounts under sections 26 and 27 of the Act. There are no matters relating to our additional powers and duties that we need to bring to your attention.

## Introduction

In the conduct of our audit we have not had to alter or change our audit approach, which we communicated to you in our Audit Plan dated 15 March 2016.

Our audit is substantially complete although at the time of drafting we are finalising our procedures in the following areas:

- completion and review of audit work including property plant and equipment, pensions and operating expenditure
- review of the final version of the financial statements
- obtaining and reviewing the management letter of representation
- updating our post balance sheet events review, to the date of signing the opinion
- Whole of Government Accounts

We received draft financial statements on 13 June 2016 more than two weeks in advance of the statutory deadline. The draft accounts were well presented. The delivery of working papers was also improved compared to previous years. Most were available at the commencement of our audit, and the remainder were delivered in accordance with the agreed timetable.

It is pleasing to report that we have seen further improvement in both the timeliness and quality of the accounts production process. We noted in particular that the information to provided by group entities was delivered more promptly, enabling group accounts to be completed in line with the Council's accounts.

We have worked closely with the Financial Accounts Team throughout the audit and we would like to express our gratitude and thanks for their hard work and support. From 2018 the statutory deadline for accounts production will be 31 May and the Financial Accounts Team is committed to delivering to this deadline in 2017. We will continue to work with the team to help embed the further process changes necessary to meet the earlier deadlines required in future.

## Key audit and financial reporting issues

**Financial statements opinion**

There are no adjustments affecting the Council's overall reported financial position, although adjustments and disclosure changes have been made to the accounts presented for audit (details are recorded in section two of this report). The draft financial statements for the year ended 31 March 2016 recorded net expenditure of £870 million; the audited financial statements show net expenditure of £853 million. This change is primarily driven by changes made to the historical cost of Grand Central prior to its revaluation. We have also agreed adjustments to improve the presentation of the financial statements.

We anticipate providing an unqualified audit opinion in respect of the financial statements (see Appendix B).

The key comments arising from our audit of the Council's financial statements concern:

- the extent of disclosures relating to disposal of the NEC and Grand Central
- our consideration of the going concern assessment
- the equal pay provision

Further details are set out in section two of this report and are summarised below.

**NEC and Grand Central**

The disclosures relating these transactions have been challenging for the Council due to the sensitive nature of these commercial transactions. Our initial review of the draft accounts concluded that there were insufficient disclosures of these two highly material transactions to meet the requirements of the Local Authority Accounting Code and IFRS (International Financial Reporting Standards).

We discussed our concerns about the disclosure for the NEC and Grand Central disposals with the Financial Accounts Team. Amendments were proposed to both the narrative report, notes to the accounts and the group accounts. These changes were agreed by the Strategic Director, Finance and Legal and the final version of the accounts have been amended.

The disposal of the NEC in particular was a highly complex transaction requiring key judgements to be made about accounting treatment. During the disposal process the Council obtained professional accounting advice. We focused our attention on ensuring that the accounting treatment applied was consistent with the advice and reasonable. We have concluded that it is.

Accounting advice was also obtained at the start of the Grand Central project to support the accounting treatment during the construction phase. This was updated to reflect the disposal of the asset and we have concluded that the accounting treatment in the final version of the 2015/16 accounts is consistent with this advice and Code and IFRS requirements.

**Going concern**

We have considered whether it is appropriate for the Council to prepare its accounts on a 'going concern' basis. In previous years the key issue has been the Council's ability to generate sufficient cash resources to meet its equal pay obligations. The capital receipts generated by asset sales, including the NEC and Grand Central ensured that there is sufficient cash to meet current equal pay obligations.

Our assessment this year has considered the impact of the savings challenge over the 12 month period from our opinion date. We have noted the size of the challenge and the scope that balances provide to temporarily cover shortfalls in savings delivery.

We have concluded that balances provide sufficient cover for the next 12 months and there is no material uncertainty that the Council will continue as a going concern in this period. We do however emphasise that we are not expressing an opinion that balances should be used for this purpose and stress the importance of the actions currently being taken by the Council to respond to the savings challenge.

**Equal pay provision**
During 2015/16 equal pay claims were settled and the value and volume of new claims reduced. This has resulted in the provision for equal pay claims decreasing from £562 million at 31 March 2015 to £310 million at 31 March 2016.

In previous years we have included an emphasis of matter paragraph in our opinion with regard to the Council's equal pay liability, due to the difficulties in accurately estimating equal pay liabilities. We are not proposing to include this paragraph in this year's audit opinion.

The purpose of the emphasis of matter paragraph has been to draw the readers' attention to the risk of material misstatement of the equal pay provision due to uncertainty about the impact of court judgements, the potential for a high volume of claims and the outcomes of negotiating settlements. Although these are still risks, we do not now consider that these are significant enough to draw specific attention to them in our audit opinion.

**Other financial statement responsibilities**
As well as an opinion on the financial statements, we are required to give an opinion on whether other information published together with the audited financial statements is consistent with the financial statements. We report by exception if in our opinion the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the information of which we are aware from our audit.

We are not proposing to report any Annual Governance Statements issues in our opinion, but bring the following points to your attention.

- The management of schools has not been included as a significant governance issue in this year's Annual Governance Statement due to the assessment of the progress made with the single integrated improvement plan. Although we are not challenging this assessment we are proposing to qualify our value for money conclusion with respect to schools management.

- Group governance arrangements are considered as part of the Annual Governance Statement assessment process. These are not referred to in the Statement and we have suggested that this is included in future.

## Controls

**Roles and responsibilities**
The Council's management is responsible for the identification, assessment, management and monitoring of risk, and for developing, operating and monitoring the system of internal control.

Our audit is not designed to test all internal controls or identify all areas of control weakness.  However, where, as part of our testing, we identify any control weaknesses, we report these to the Council.

We reported one internal control issue in our Audit Plan. This related to IT automated notifications about leavers as this is currently a manual process. IT service management have agreed to take action on this. There are no other internal control issues that we need to bring to your attention.

## Value for Money

We propose issuing a qualified 'except for' conclusion on your arrangements for securing economy, efficiency and effectiveness in your use of resources.

Our review has highlighted the following issues which give rise to our proposed qualified value for money conclusion.

- Savings challenge – due to the impact of non-recurrent savings in 2015/16 and the weaknesses in the People Directorate's savings plan delivery
- Services for vulnerable children – due to the concerns reported by Ofsted following their monitoring visit and the continuing need for the Council to have external oversight of its arrangement by the Children's Commissioner
- Management of schools – due to Ofsted feedback indicating that there are significant governance issues in some schools and concerns reported by Ofsted on the pace of change
- Improvement Panel – due to continuation of the Panel's appointment

Further detail of our work on Value for Money is set out in section three of this report.

## Other statutory powers and duties

We have not identified any issues that have required us to apply our statutory powers and duties under the Act.

## Grant certification

In addition to our responsibilities under the Code, we are required to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. At present our work on this claim is in progress and is not due to be finalised until 30 November 2016. We will report the outcome of this certification work through a separate report to Audit Committee which is due in February 2017.

## Matters arising

Matters arising from the financial statements audit and our review of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources have been discussed with the Strategic Director, Finance and Legal.

We have made a number of recommendations, which are set out in the action plan at Appendix A.

## Acknowledgement

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

**Grant Thornton UK LLP**
**September 2016**

# Section 2: Audit findings

# Materiality

In performing our audit, we apply the concept of materiality, following the requirements of International Standard on Auditing (UK & Ireland) (ISA) 320: Materiality in planning and performing an audit. The standard states that 'misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements'.

As we reported in our audit plan, we determined overall materiality to be £45.126 million (being 1.5 per cent of gross Cost of Service expenditure). We have considered whether this level remained appropriate during the course of the audit and (have made no changes to our overall materiality.

We also set an amount below which misstatements would be clearly trivial and would not need to be accumulated or reported to those charged with governance because we would not expect that the accumulated effect of such amounts would have a material impact on the financial statements. We have defined the amount below which misstatements would be clearly trivial to be £2.256 million. This remains the same as reported in our audit plan.

As we reported in our audit plan, we identified the following items where we decided that separate materiality levels were appropriate. These remain the same as reported in our audit plan.

| Balance/transaction/disclosure | Explanation | Materiality level |
|---|---|---|
| Cash and cash equivalents | Although the balance of cash and cash equivalents may not be material at year end, all transactions made by the Council affect the balance and it is therefore considered to be material by nature. | This is treated as a sensitive item although no specific materiality value is set. |
| Disclosures of officers' remuneration, salary bandings and exit packages in notes to the statements | Due to public interest in these disclosures and the statutory requirement for them to be made. | £2.256 million |
| Disclosure of auditors' remuneration in notes to the statements | Due to public interest in these disclosures and the statutory requirement for them to be made. | £2.256 million |

# Audit findings against significant risks

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, either due to size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty" (ISA (UK&I) 315).

In this section we detail our response to the significant risks of material misstatement which we identified in the Audit Plan. As we noted in our plan, there are two presumed significant risks which are applicable to all audits under auditing standards

| | Risks identified in our audit plan | Work completed | Assurance gained and issues arising |
|---|---|---|---|
| 1. | **The revenue cycle includes fraudulent transactions**<br>Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.<br>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition. | Having considered the risk factors set out in ISA240 and the nature of the revenue streams at Birmingham City Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:<br>• there is little incentive to manipulate revenue recognition<br>• opportunities to manipulate revenue recognition are very limited; and<br>• the culture and ethical frameworks of local authorities, including Birmingham City Council, mean that all forms of fraud are seen as unacceptable. | Our audit work has not identified any issues in respect of revenue recognition. |
| 2. | **Management over-ride of controls**<br>Under ISA (UK&I) 240 it is presumed that the risk of management over-ride of controls is present in all entities. | We have undertaken<br>• review of entity controls<br>• testing of journal entries<br>• review of accounting estimates, judgements and decisions made by management<br>• review of unusual significant transactions | Our audit work has not identified any evidence of management over-ride of controls. In particular the findings of our review of journal controls and testing of journal entries has not identified any significant issues. |

# Audit findings against significant risks continued

We have also identified the following significant risks of material misstatement from our understanding of the entity. We set out below the work we have completed to address these risks.

| | Risks identified in our audit plan | Work completed | Assurance gained and issues arising |
|---|---|---|---|
| 3 | **Sale of the NEC and Grand Central**<br>Risk that complex accounting entries are not correctly posted in the accounts | We have<br>• gained an understanding of the transactions including a review of supporting documentation<br>• carried out testing of the transactions in the financial statements to ensure they were consistent with our understanding<br>• reviewed the accounting entries to ensure they complied with the requirements of the CIPFA Code of Practice.<br>• reviewed of accounting treatment of sale proceeds.<br>• completed substantive testing to ensure the lease/investment arrangements have been correctly eliminated from the accounts<br>• completed substantive testing of sale proceeds | Our audit work has not identified any accounting issues that we wish to bring to your attention.<br>We have agreed further disclosure to enhance information relating to the disposals and ensure compliance with the Local Authority Accounting Code and IFRS. Further details are given later in this report on pages 29 to 31.<br>Our work has also considered the Grand Central profit share payment of £72.9 million, disclosed as an exceptional item. We have concluded that the payment is in accordance with the agreement with Network Rail. |
| 4 | **Actuarial Valuation of LGPS pension liability**<br>Under ISA 540 (Accounting Estimates and Related Disclosures), the auditor is required to make a judgement as to whether any accounting estimates with a high degree of estimation uncertainty give rise to a significant risk. | We have<br>• reviewed documentation of the key controls that were put in place by management to ensure that the pension fund liability was not materially misstated.<br>• completed walkthrough of the key controls to assess whether they were implemented as expected and mitigate the risk of material misstatement in the financial statements.<br>• reviewed of the competence, expertise and objectivity of the actuary who carried out the Council's pension fund valuation.<br>• gained an understanding of the basis on which the IAS 19 valuation was carried out, undertaking procedures to confirm the reasonableness of the actuarial assumptions made.<br>• reviewed of the consistency of the pension fund asset and liability and disclosures in notes to the financial statements with the actuarial report from your actuary. | At the time of drafting this report our audit work was subject to final review. We have not identified any issues at this stage that we wish to bring to your attention. |

# Audit findings against significant risks continued

| | Risks identified in our audit plan | Work completed | Assurance gained and issues arising |
|---|---|---|---|
| 5. | **Equal Pay Provision**<br>Under ISA 540 (Auditing Accounting Estimates, including Fair Value Accounting Estimates and Related Disclosures), the auditor is required to make a judgement as to whether any accounting estimates with a high degree of estimation uncertainty give rise to a significant risk. | • We reviewed the assumptions on which the estimate was based<br>• We considered events or conditions that could change the basis of estimation<br>• We checked the calculation of the estimate<br>• We checked that the estimate has been determined and recognised in accordance with accounting standards<br>• We determined how management has assessed estimation uncertainty<br>• We considered the impact of subsequent transactions | The Council recognises equal pay claims and estimates the potential cost when they are received. It does not forecast future claims on the basis that a significant number of variables impact on the number and value of future claims.<br>Our audit work has not identified any significant issues in relation to the risk identified.<br>Our audit plan identified a potentially high level of estimation uncertainty with respect to the £310 million provision in the accounts.<br>We noted that estimated future cash flows relating to the provision have not been discounted and we are satisfied that the Council's assessment that this would not be material is reasonable.<br>The impact of claims received since 31 March 2016 was also assessed. New claims received between February and August totalled £3.9 million. We concluded that there was not a risk of material estimation uncertainty from not including these claims in the provision.<br>On the basis of our work, we concluded that the level of estimation uncertainty does not present material uncertainty in the accounts. |

# Audit findings against significant risks continued

| | Risks identified in our audit plan | Work completed | Assurance gained and issues arising |
|---|---|---|---|
| 6 | **Valuation of property, plant and equipment**<br>The Council revalues its assets on a rolling basis over a five year<br>The Code requires that the Council ensures that the carrying value at the balance sheet date is not materially different from the current value. This represents a significant estimate by management in the financial statements. | We have:<br>• reviewed of management's processes and assumptions for the calculation of the estimate.<br>• reviewed of the instructions issued to valuation experts and the scope of their work<br>• discussed with the Council's valuer the basis on which the valuation was carried out, challenging the key assumptions.<br>• review and challenge of the information used by the valuer to ensure it was robust and consistent with our understanding.<br>• tested revaluations made during the year to ensure they were input correctly into the Council's asset register<br>• evaluated the assumptions made by management for those assets not revalued during the year and how management satisfied themselves that these were not materially different to current value. | Our audit work has not identified any significant issues in relation to the risk identified.<br>The valuer's report for both HRA and General Fund land and buildings is dated 1 April 2015, but is included in the accounts as if the valuation was at 31 March 2016.<br>To ensure that the valuation is not materially misstated the valuer reviewed the potential movement in values during the year. As part of this, the valuer also carried out a desktop review of all DRC (Depreciated Replacement Cost) valued assets, not subject to formal revaluation to assess whether they were materially misstated. He concluded that they were and the carrying value of assets were adjusted to reflect this. This resulted in an increase of £38.5m for assets fully revalued in 2015/16, and £164.3m for assets not revalued during 2015/16.<br>We are satisfied that the accounts are consistent with the valuation and assessment and that this demonstrates that there is a low risk of material misstatement. |
| 7. | **Better Care Fund**<br>Risk that transactions are not accounted for correctly | We have<br>• obtained an understanding of the nature of any Better Care Fund agreements in place, and documented the control environment.<br>• reviewed the accounting treatment of significant agreements<br>• agreed the accounting entries and disclosures in the financial statements | Our audit work has not identified any issues regarding accounting treatment that we wish to bring to your attention.<br>Further detail is provided in section three of this report around the value for money aspects of the Better Care Fund. |

# Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses are attached at appendix A.

| Transaction cycle | Description of risk | Work completed | Assurance gained & issues arising |
|---|---|---|---|
| **Property, Plant and Equipment** | Risk that property, plant and equipment activity is not valid | We have<br>• updated our documentation and undertaken a walkthrough of the controls in place to ensure that PPE activity is valid<br>• tested agreement of the fixed asset register to the accounts and supporting notes<br>• tested a sample of PPE additions and disposals including compliance with capitalisation requirements | Our audit testing of the Grand Central project identified a £15 million credit included within the balance of Assets Under Construction (AUC) at year end. This related to Pallasades rental income.<br>This credit should have been included within the Grand Central asset when it was transferred out of AUC. This would have reduced the historic cost of Grand Central and therefore decreased the loss on revaluation. This omission impacted the CIES and the Balance Sheet (PPE and Reserves) as well as the related notes.<br>The final version of the accounts has been adjusted for this item. |
| **Property, Plant and Equipment** | Risk that property, plant and equipment allowance for depreciation is not adequate | We have<br>• updated our documentation and undertaken a walkthrough of the controls in place to ensure that depreciation is adequate<br>• tested depreciation and impairments, including evidence of review of useful economic lives and mathematical accuracy<br>• tested surplus or deficit on disposal | Our audit work has not identified any significant issues in relation to the risk |

# Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses are attached at appendix A.

| Transaction cycle | Description of risk | Work completed | Assurance gained & issues arising |
|---|---|---|---|
| **Employee remuneration** | Employee remuneration accruals understated (Remuneration expenses not correct) | We have:<br>• documented our understanding of processes and key controls over the transaction cycle<br>• undertaken walkthrough testing of the key controls to assess the whether those controls were in line with our documented understanding<br>• tested the reconciliation of the annual payroll to the ledger and to the segmental analysis note in the accounts<br>• completed trend analysis of monthly and weekly payroll payments covering 2015/16 and comparing to 2014/15<br>• reviewed the payroll accrual processes<br>• substantively tested of the completeness of IAS19 pension liabilities<br>• agreed employee remuneration disclosures in the financial statements to supporting evidence | Our audit work has not identified any significant issues in relation to the risk identified. |

# Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses are attached at appendix A.

| Transaction cycle | Description of risk | Work completed | Assurance gained & issues arising |
|---|---|---|---|
| **Operating expenses** | Creditors understated or not recorded in the correct period (Operating expenses understated) | We have<br>• documented our understanding of processes and key controls over the transaction cycle<br>• undertaken walkthrough of the key controls to assess the whether those controls were in line with our documented understanding<br>• reviewed the application of the year end closedown process for capturing creditor accruals<br>• undertaken substantive testing of year end creditors including after date payments<br>• tested Goods Received not Invoiced listing to confirm appropriate accruals<br>• reviewed control account reconciliations covering the agreement of creditor payments to the ledger | At the time of drafting this report our audit work is subject to final review. We have not identified any issues at this stage that we wish to bring to your attention. |

# Audit findings against other risks

| Transaction cycle | Description of risk | Work completed | Assurance gained & issues arising |
|---|---|---|---|
| **Early closure of the accounts** | Risk that issues may arise due to the earlier closure of the accounts compared to prior years, an increased use of estimations, and a potential reduction in quality assurance capacity due to senior staff secondments. | We have<br>• gained an understanding of the process for ensuring compliance with early closure<br>• documented the techniques used for the increased use of estimates in the accounts including any changes from prior year<br>• undertaken specific testing of significant estimates | Our audit work has not identified any significant issues in relation to the risk identified.<br><br>It is pleasing to report that further progress has been made with the earlier closure of accounts. The accounts were provided for audit on the 13 June 2016, more than two weeks before the statutory deadline of 30 June 2016. This was the agreed deadline for submission in the accounts production project plan.<br><br>We were briefed by the Financial Accounts Team throughout the closedown process and also provided our views on the increased use of estimates.<br>Our testing has confirmed that the increased use of estimates has not resulted in an increased risk of material misstatement in the accounts.<br><br>There were further improvements in the quality of supporting working papers and the process to resolve audit quires was efficient. We noted in particular that group entities provided their information more promptly than in previous years. This enabled group accounts to be completed by the 13 June 2016.<br><br>We did note however that the information provided to Financial Accounts Team to support the NEC and Grand Central disposals was not complete. We recognise that information relating to these transactions, and for other major redevelopment schemes is sensitive, but the preparers of the accounts must have full information to ensure appropriate accounting treatment and disclosures.<br><br>We will continue to work with the Financial Accounts Team to support further efficiencies in the closedown process and our audit. |

# Group audit scope and risk assessment

ISA (UK&I) 600 requires that as Group auditors we obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

| Component | Significant? | Level of response required under ISA 600 | Risks identified | Work completed | Assurance gained & issues raised |
|---|---|---|---|---|---|
| NEC Group Ltd | No | Analytical | Subsidiary – discontinued operation | Review of accounting treatment of disposal transactions in group consolidation.<br>Review of disclosure relating to discontinued operations | Our audit work has confirmed that the accounting treatment adopted is consistent with the accounting advice obtained and is a reasonable application of the Local Authority Accounting Code and IFRS requirements.<br><br>In our view the disclosures in the draft accounts were not sufficient and have been amended. |
| NEC (Developments) PLC | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| Innovation Birmingham Ltd | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| Performances (Birmingham) Ltd | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| Acivico Ltd | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| PETPS (Birmingham) Ltd | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues.<br><br>The company is a new entity set up following the completion of the disposal of NEC Group Ltd. Its purpose is to assume the continuing liability for the NEC's closed defined benefit pension liability. The Council has assumed the continuing funding obligation. The company therefore has nil net assets and net nil impact on the group accounts. |

# Group audit scope and risk assessment (continued)

| Component | Significant? | Level of response required under ISA 600 | Risks identified | Work completed | Assurance gained & issues raised |
|---|---|---|---|---|---|
| Birmingham Museums Trust | No | Analytical | Subsidiary | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues, but audited accounts were not available for the preparation of the draft consolidation. |
| Paradise Circus Limited Partnership | No | Analytical | Joint Venture | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| Service Birmingham Ltd | No | Analytical | Associate | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |
| Birmingham Airport Holdings Ltd | No | Analytical | Associate | Agreement of consolidation using audited accounts and analytical approach | Our audit work has not identified any material issues. |

# Accounting policies, estimates and judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Council's financial statements.

| Accounting area | Summary of policy | Comments | Assessment |
|---|---|---|---|
| **Revenue recognition** | The Council has adopted the following revenue recognition policy<br>• Service activity is accounted for in the year it takes place, not simply when cash payments are made or received<br>• Revenue from the sale of goods is recognised when the Council transfers the significant risks and rewards of ownership to the purchaser and it is probable that economic benefits or service potential associated with the transaction will flow to the Council<br>• Revenue from the provision of services is recognised when the Council can reliably measure the percentage of completion of the transaction and it is probable that economic benefits or service potential associated with the transaction will flow to the Council<br>• Interest receivable on investments is accounted for as income on the basis of the effective interest rate for the relevant financial instrument rather than the cash flows fixed or determined by the contract<br>• When income has been recognised but cash has not been received, a debtor for the relevant amount is recorded in the Balance Sheet. Where debts may not be settled, the balance of debtors is written down and a charge made to revenue for the income that might not be collected | We are satisfied that the Council's disclosure note on revenue recognition is adequate and is consistent with the requirements of the CIPFA Code of Practice on Local Authority Accounting | ● Green |

**Assessment**
● Marginal accounting policy which could potentially attract attention from regulators
● Accounting policy appropriate but scope for improved disclosure
● Accounting policy appropriate and disclosures sufficient

# Accounting policies, estimates and judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Council's financial statements.

| Accounting area | Summary of policy | Comments | Assessment |
|---|---|---|---|
| **Judgements and estimates** | Key estimates and judgements include the<br>• required level of provisions, specifically with respect to equal pay liabilities and business rates valuation appeals<br>• the valuation, impairment and remaining useful life of Property Plant and Equipment<br>• assessment of PFI schemes and other arrangements as to whether they fall within the scope of IFRIC 12.<br>• valuation of long term liabilities for PFI and leasing<br>• present value of pension obligations<br>• estimate of provision required for bad debts | Our findings from our review of judgements and estimates are set out below:<br>We have reviewed the Council's accounting policies with regard to judgements and estimates and are satisfied that they are appropriate and in accordance with the recommendations of the CIPFA Code of Practice on Local Authority Accounting.<br>Our consideration of the equal pay provision is summarised under "audit findings significant risks" on page 12<br>Note 32 Provisions includes a £25 million provision for business rate valuation appeals. The settlement of business rate valuation appeals is determined by the Valuation Office Agency (VOA). We reviewed the Council's approach to estimating its provision including its consideration of the impact of the settlement of appeals since the balance sheet date. We are satisfied that the estimate has been made on a reasonable basis, but in our view that there is a need for the adequacy of this provision to be kept under review.<br>Our consideration of property plant and equipment valuations issues is considered under "audit findings significant risks" on page 13<br>The Council has a number of PFI schemes. The finance liability is disclosed in the balance sheet at £457 million. Revenue and interests payments are also disclosed in Note 43. We are satisfied that the PFI liabilities are consistent with the Council's financial models and that the allocation between interest, service and capital repayments is materially correct.<br>The Council's estimated pension liability has decreased by £206 million compared to the 2014/15 balance sheet. This change is largely due to the actuaries reassessment of the Council's future pension liability.<br>We are satisfied that the Council Tax bad debt provision is calculated on a reasonable basis, but in our view that there is a need for the adequacy of this provision to be kept under review. | ● Green |

**Assessment**

● Marginal accounting policy which could potentially attract attention from regulators
● Accounting policy appropriate but scope for improved disclosure
● Accounting policy appropriate and disclosures sufficient

# Accounting policies, estimates and judgements continued

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| Accounting area | Summary of policy | Comments | Assessment |
|---|---|---|---|
| **Going concern** | The Strategic Director, Finance and Legal, has a reasonable expectation that the services provided by the Council will continue for the foreseeable future. Members concur with this view. For this reason, the Council continue to adopt the going concern basis in preparing the financial statements. | We have considered whether it is appropriate for the Council to prepare its accounts on a 'going concern' basis. In making our assessment we considered the Council's financial forecast for 2017/18 and the forecast savings within its business plan especially in relation to health and social care element. We have also considered the risk of the Council's level of borrowing and its pension liability.<br>If the Council does not generate the required savings it will need to utilise reserves to manage any revenue consequences. In terms of liquidity, the Council would need to increase its borrowing or reduce its short term lending to meet its cash requirements.<br>On the basis of our review we are satisfied that the Council remains a 'going concern'. | ● Amber |
| **Other accounting policies** | | We have reviewed the Council's policies against the requirements of the CIPFA Code of Practice. The Council's accounting policies are appropriate and consistent with previous years. | ● Green |

**Assessment**
● Marginal accounting policy which could potentially attract attention from regulators
● Accounting policy appropriate but scope for improved disclosure
● Accounting policy appropriate and disclosures sufficient

# Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

| | Issue | Commentary |
|---|---|---|
| 1. | **Matters in relation to fraud** | • We have previously discussed the risk of fraud with the Audit Committee. We have not been made aware of any other incidents in the period and no other issues have been identified during the course of our audit procedures |
| 2. | **Matters in relation to related parties** | • From the work we carried out, we have not identified any related party transactions which have not been disclosed |
| 3. | **Matters in relation to laws and regulations** | • You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work. |
| 4. | **Written representations** | A letter of representation has been requested from the Council that includes specific representations on the following:<br>• the receipt of the claim is the appropriate point to recognise a liability for equal pay<br>• it is not possible to accurately estimate the volume, type or value of future equal pay claims<br>• the fair values of property, plant and equipment, and the equal pay provision are appropriate<br>• there are no onerous contracts for Academy Schools with a PFI agreement in place at the transfer<br>• the Council holds no investment properties other than those disclosed on the balance sheet<br>• there are no further issues requiring section five of the Annual Governance Statement to be amended<br>• the Council does not consider that it needs to make additional provision for uncollected Council Tax debt<br>• the Council considers that it remains a 'going concern' for the foreseeable future<br>• the Council is satisfied that it will be able to deliver sufficient savings or utilise reserves to enable it to meet its 'financial duties'. |
| 5. | **Confirmation requests from third parties** | • We sought direct confirmations for all material and a sample of non-material loans. All confirmations were received.<br>• We also requested from management permission to send confirmation requests for bank and all material and a sample of non-material investment balances. This permission was granted and the requests were sent. All of these requests were returned with positive confirmation. |
| 6. | **Disclosures** | • We have summarised the disclosure amendments included in the final version of the accounts on pages 29 to 31. |

# Other communication requirements continued

| | Issue | Commentary |
|---|---|---|
| 7. | **Matters on which we report by exception** | We have not identified any issues we would be required to report by exception in the following areas. If:<br>• the Annual Governance Statement not meeting the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the information of which we are aware from our audit; or<br>• the information in the narrative report is materially inconsistent with the information in the audited financial statements or our knowledge of the Council and group acquired in the course of performing our audit, or is otherwise misleading |
| 8. | **Specified procedures for Whole of Government Accounts** | We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions.<br>As the Council exceeds the specified group reporting threshold of £350m we are required to examine and report on the consistency of the WGA consolidation pack with the Council's audited financial statements.<br>At the time of drafting this report our audit work is not yet complete. We plan to complete the work before signing our audit opinion. |

# Internal controls

The purpose of an audit is to express an opinion on the financial statements.

Our audit included consideration of internal controls relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. We considered and walked through the internal controls for Employee Remuneration Operating Expenses and Property Plant and Equipment.

The matters that we identified during the course of our audit are set out in the table below. These and other recommendations, together with management responses, are included in the action plan attached at Appendix A.

| | Assessment | Issue and risk | Recommendations |
|---|---|---|---|
| 1. | ● Amber | IT - one recommendation has been identified, relating to an automated notifications about leavers as this is currently a manual process. | IT service management has agreed to take action on this. |
| 2. | ● Amber | Group accounts have been produced from unaudited accounts for all the group entities included in the consolidated balance sheet. Audited accounts were being received by the Finance Team throughout the audit process. | The Audit Committee needs assurance that group entities provide sufficient information by the end of May to ensure materially accurate group accounts can be produced and that audited accounts are received before the completion of the Council's audit. |

**Assessment**
- ● Significant deficiency – risk of significant misstatement
- ● Deficiency – risk of inconsequential misstatement

The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

# Adjusted misstatements

A number of adjustments to the draft accounts have been identified during the audit process. We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management. The table below summarises the adjustments arising from the audit which have been processed by management.

### Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the key statements and the reported net expenditure for the year.

| | Detail | Comprehensive Income and Expenditure Statement<br>£m | Balance Sheet<br>£m | Impact on total net expenditure<br>£m |
|---|---|---|---|---|
| 1 | A £15m credit relating to the Pallasades rental income was incorrectly offsetting the Asset Under Construction This error impacted on the I&E and notes 19 and 20. | 15.7 | 15.7 | 15.7 |
| 2 | A capital grant of £8m relating to Growth Fund – Metro had been incorrectly credited in total to grants received . This grant was made by Growth Fund to CENTRO and therefore BCC was acting as an agent rather than a principal for £7.55m of the grant. Therefore grant income and REFCUS were both overstated by £7.55m. | Overstated Grant received (7.6)<br>Overstated expenditure 7.6 | | Nil |
| 3 | 2 assets were revalued down to a Gross Book Value (GBV) of nil in error. This resulted in an understated GBV of £3.3m. | 1.4 | 3.3 | 1.4 |
| | **Overall impact on single entity accounts** | £17.1 | £19.0 | £17.1 |
| | **Impact on usable reserves** | Nil | Nil | Nil |

# Adjusted misstatements

| | Detail | Comprehensive Income and Expenditure Statement<br>£m | Balance Sheet<br>£m | Impact on total net expenditure<br>£m |
|---|---|---|---|---|
| 4 | Restatement of group gain on disposal of NEC from 'Other (Gains)/Losses to Discontinued Operations' – from Items that will not be reclassified to the (Surplus)/Deficit on the Provision of Services, to (Surplus) / Deficit on Provision of Services. | (145.6)<br>145.6 | | Nil |
| 5 | Restatement of single entity loss on disposal of NEC from Other Operating Expenditure to Discontinued Operations | 59.2<br>(59.2) | | Nil |
| | **Overall impact on group accounts** | Nil | Nil | Nil |

# Misclassifications and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

| | Adjustment Type | Issue |
|---|---|---|
| 1 | Disclosure | Further narrative has been provided to indicate where 2014/15 comparative figures have been restated within the notes to the accounts. |
| 2 | Disclosure | Narrative Report<br>Detail within the Narrative Report in relation to Grand Central and the NEC disposal has been enhanced to quantify the capital receipt and explain the structure of the sale. The expanded narrative gives a clearer explanation of the impact of the disposal, including the impact on the group structure.<br>The Narrative Report has also been amended to explain the reason for the movement in usable reserves and to include reference to the potential impact as a result of the EU referendum. |
| 3 | Disclosure | Note 1 Accounting Policies<br>Accounting policies have now been expanded to include a policy which refers to acquired operations for the single entity and the group. This was required as the Public Health acquisition was material to the financial statements. |
| 4 | Disclosure | Note 3 Critical Judgements<br>The summary regarding the Better Care Fund only included the accounting treatment adopted. The note has been amended to make clear what the critical judgements were in relation to Better Care Fund accounting.<br>We noted that the accounting treatment of the NEC disposal includes two judgements relating to NEC Developments accounting for transactions. These are:<br>• the application of regulation 30(d) of the Capital Finance Regulations (regarding soft loans) does not apply to the principal and interest contractually committed to be paid by the Council to NEC Developments; and<br>• The treatment of the consideration of £21 million for the Hall 17 -20 lease re-assignment as a capital receipt.<br>We reviewed both of these judgements and concluded that they are reasonable. Note 3 has been amended to include these judgements. |
| 5 | Disclosure | Note 8 Usable Reserves<br>Capital Receipts Reserve shows a net movement of £296m. This is in line with expectations but an expanded explanation now supports the movement and explains the key sources of capital receipts and their application.<br>Further explanation has been provided in relation to the increase of £38m in other Earmarked Reserves. |

# Misclassifications and disclosure changes

| | Adjustment Type | Issue |
|---|---|---|
| 6 | Disclosure | Note 12 Material Items of Income and Expense and Acquired Operations<br>The note has been amended to include a description of the NEC sale transaction. |
| 7 | Disclosure | Note 13 Other Operating Expenditure<br>Analysis added to the note which states that the loss on disposal is £59.2 million for NEC and gain on disposal for Gateway is £112.1 million |
| 8 | Misclassification | Note 19 (Single Entity) / Note G17 (Group). Amendment was required to the Directorate Analysis, reducing 'fees, charges and other service income' and increasing 'support service recharges' by £40.4m. There was a net nil movement overall. |
| 9 | Disclosure | Note 20 Property Plant and Equipment<br>Summary by revaluation date. This table showed all Vehicles, Plant, Furniture and Equipment as being held at cost. This was incorrect. Additionally the years of valuation shown for some items were incorrect. These have been amended. |
| 10 | Disclosure | Note 24 Long Term Investments<br>Narrative has been amended to include the following:<br>*The increase in Investments in Subsidiary and Associated Companies reflects the crystallisation of the Council's guarantee to meet the loans entered into by the National Exhibition Centre (Developments) Plc following the sale of the NEC Group.* |
| 11 | Disclosure | Note 27 Assets Held for Sale<br>Amended to include narrative that explains that the reduction in PPE held for sale assets relates to assets that formed part of the NEC disposal. |
| 12 | Disclosure | Note 33 Contingent Liabilities and Contingent Assets<br>There was no recognition within the financial statements to reflect the potential future receipts from the sale of the NEC. These have now been included as contingent assets. |
| 13 | Disclosure | Note 39 Financial Instruments<br>The fair value table has been restated to include the valuation basis for financial instruments and provide explanation for those financial instruments approximated by carrying value. |
| 14 | Disclosure | Note 42 Leases<br>A narrative explanation has now been included in note 42 of the impact of the NEC disposal on the Council's leases. It explains that the previous portfolio of operating and finance leases relating to the NEC have been terminated and replaced. |

# Misclassifications and disclosure changes

| | Adjustment Type | Issue |
|---|---|---|
| 15 | Disclosure | Housing Revenue Account<br>An exceptional item had been included within the HRA. This was not exceptional by scale and did not require separate disclosure. Item has now been removed from this line. |
| 16 | Disclosure | Group Note G1 Accounting Policies<br>An accounting policy has also been included on disposals of subsidiaries. This states:<br>*When a subsidiary company is disposed of the assets and liabilities of the subsidiary are derecognised at their carrying value at the time of disposal and the value of any consideration received is recognised. The transactions plus any resulting differences are identified in the Profit/Loss on disposal of a subsidiary and forms part of the Surplus/Deficit on Provision of Services within the Group Comprehensive Income and Expenditure Statement.* |
| 17 | Disclosure | Group Note G4 Discontinued Operations<br>Note expanded to provide an analysis of discontinued operations, including the gain on disposal of the NEC. |
| 18 | Disclosure | Group Note G16 Cash Flow Statement - Investing Activities and Note G17 Cash Flow Statement - Financing Activities<br>The cash flows from discontinued operations in 2014/15 have been included in notes G16 and G17 |

# Section 3: Value for Money

## Background

We are required by section 21 of the Local Audit and Accountability Act 2014 ('the Act') and the NAO Code of Audit Practice ('the Code') to satisfy ourselves that the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the Value for Money (VfM) conclusion.

In a change to previous years, the Act and the Code require us only to report by exception where we are not satisfied that the Council has proper arrangements in place to secure value for money. We must, however, carry out sufficient work to satisfy ourselves that proper arrangements are in place at the Council.

In carrying out this work, we have to follow the NAO's Auditor Guidance Note 3 (AGN 03) issued in November 2015. AGN 03 identifies one single criterion for auditors to evaluate:

> *In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.*

AGN03 provides examples of proper arrangements against three sub-criteria but specifically states that these are not separate criteria for assessment purposes and that auditors are not required to reach a distinct judgement against each of these.

## Risk assessment

We carried out our initial risk assessment in February 2016 and identified the significant risks that we would investigate. These were communicated to you in our Audit Plan which we presented to the Audit Committee on 15 March 2016.

We identified risks in respect of specific areas of proper arrangements using the guidance contained in AGN03.

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We have continued our review of relevant documents up to the date of giving our report, and have not identified any further significant risks where we need to perform further work.

We carried out further work only in respect of the significant risks we identified from our initial and ongoing risk assessment. Where our consideration of the significant risks determined that arrangements were not operating effectively, we have used the examples of proper arrangements from AGN 03 to explain the gaps in proper arrangements that we have reported in our VfM conclusion.

## Significant qualitative aspects

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risks that we identified in the Council's arrangements. In arriving at our conclusion, our main considerations were:

- the scale of the Council's overall savings challenge and the actions being taken to deliver it
- the views of other regulators on the implementation of improvements for services for vulnerable children
- the pace of change in improving the management of schools in the City
- feedback from the Council's Improvement Panel
- the progress with the Future Council programme
- how the Council is working with its partners to deliver health and social care services
- the continuing impact of the Council's equal pay liabilities.

We have set out more detail on the risks we identified, the results of the work we performed and the conclusions we drew from this work later in this section.

## Overall conclusion

Based on the work we performed to address the significant risks, we propose a qualified 'except for' conclusion on your arrangements for securing economy, efficiency and effectiveness in your use of resources. The text of our proposed report can be found at Appendix B.

The arrangements in respect of the following significant risks were not sufficient for an unqualified VfM conclusion.

- Savings challenge – due to the impact of non-recurrent savings in 2015/16 and the weaknesses in the People Directorate's savings plan delivery
- Services for vulnerable children – due to the concerns reported by Ofsted following their monitoring visit and the continuing need for the Council to have external oversight of its arrangement by the Children's Commissioner
- Management of schools – due to Ofsted feedback indicating that there are significant governance issues in some schools and concerns reported by Ofsted on the pace of change
- Improvement Panel – due to continuation of the Panel's appointment

We concluded that except for the matters above, the Council had proper arrangements in all significant respects.

We qualified our 2014/15 VfM Conclusion with respect to services for vulnerable children, management of schools and Improvement Panel. Although we have concluded that there is not sufficient progress to remove these qualifications for 2015/16 we do recognise that the Council is making progress with its improvement agenda for children's service, including the management of schools. We have also noted that the Improvement Panel has reduced the level of its intervention since March 2016.

The scale of the Council's savings challenge is unprecedented. The impact of these pressures on the People Directorate in particular presents a major management issue for the Council. We recognise that this issue is being given the highest priority by Cabinet and the Corporate Leadership Team. There is however uncertainty about the Council's ability to deliver its savings plans for 2016/17 and the potential cumulative impact on the following two years' savings programme.

In previous years we have qualified our VfM conclusion with respect to the impact of the Council's equal pay liabilities, but we have not done so for 2015/16. Although the Council still had £310 million of equal pay liabilities at 31 March 2016 it has generated sufficient resources to meet these commitments. From our perspective this is a significant step forward for the Council and we recognise the commitment there has been and continues to be to make sure the Council meets its obligations.

The Future Council programme is at the heart of reshaping the Council and the delivery of services. We have noted the progress being made with this and have concluded that effective management arrangements are in place to deliver it.

Delivery of health and social care outcomes depends upon effective partnership arrangements with Health bodies. We concluded that there are adequate arrangements in place. We did however note with concern that the joint commissioning board for the learning disabilities and mental health services pooled budget has not met since April 2015.

## Recommendations for improvement

We discussed findings arising from our work with management and have agreed recommendation for improvement as follows.

The Council needs to ensure the following.

- Effective plans are put in place to respond to the under delivery of savings plans and emergent budget pressures, particularly in the People Directorate. These need to include a realistic assessment of the use of reserves to enable sufficient lead time for savings plans to be implemented.
- Plans for services to vulnerable children, including the options for setting up a Children's Trust, need to deliver significant and measureable improvement promptly.
- The implementation of the Birmingham Education Delivery and Improvement Plan needs to demonstrate that the issues raised by Ofsted, including children missing from education, are being addressed promptly and effectively.
- The pace of change and the impact of new political and corporate leadership arrangements need to demonstrate to the Improvement Panel that this intervention is no longer required.
- The Council and its health partners need to either reinstitute the joint commissioning board for the learning disabilities and mental health services pooled budget, or agree alternative arrangements.

## Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

| Significant risk | Findings and conclusions |
|---|---|
| **Savings challenge**<br>The Council has identified an overall savings challenge of over £251 million to be delivered in the four years to 2019/20. The five largest savings schemes proposed over the period account for just under half of the savings target. They are challenging and include health and social care service redesign, efficiency improvements and workforce changes. The key risk is that these schemes will not deliver the required recurrent savings, or will take longer to implement than planned. | The Council reported a 2015/16 revenue budget underspend of £2.8 million on a net revenue budget of £874.5 million. This included the delivery of a £110.3 million savings programme. Delivery of the budget and a savings programme of this scale was a notable achievement. There was however a significant dependence on non-recurrent savings to do this.<br><br>The Council's Business Plan 2016+ identifies continuing savings pressures, with a requirement of £251.2 million of savings to be delivered by the end of 2019/20; 2016/17 (£88.2 million) and 2017/18 (£75.1 million) are the two years with the greatest savings demand. The Business Plan includes a detailed analysis of savings schemes across the four year period. We focused our work on the delivery risks for the major savings schemes.<br><br>The Corporate Revenue Monitoring Report up to the end of May 2016/17 was presented to Cabinet on 26 July 2016. It identifies the following:<br>• the overall savings challenge for 2016/17 is much larger than originally anticipated due to £34.8 million of non-recurrent savings carried forward from 2015/16<br>• at the end of May 2016 there were £63.2 million of budget risks and pressures (£51.6 million of savings programme actions not yet in place and £11.6 million of budget pressures)<br>• the financial pressures are most severe in the People Directorate - £44.7 million of the total £51.6 million savings pressures, and £6.1 million of the £11.6 million budget pressures.<br><br>The largest savings programme is £60 million relating to health and social care service redesign and Better Care Fund funding. Of this, £28 million was due to be delivered in 2016/17. This savings programme assumed that funding would be released by central government and health partners would direct this to the Council. This has not yet happened for 2016/17 and there is uncertainty about how much of this funding the Council will receive in the following two years.<br><br>Savings of £14.8 million were also planned from the redesign of adult social care packages which are not being realised and budget pressures of £7.1 million have now been identified for adult social care provision.<br><br>The Corporate Revenue Monitoring Report states in the first paragraph that:<br><br>"It is recognised that this is an exceptional level of challenge at this stage in the year, and the position is receiving the full attention of senior management and the Cabinet." |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Savings challenge (continued)** | Budget monitoring arrangements have been strengthened and there is an intense focus from Corporate Leadership Team and Cabinet on actions to find alternative savings. This includes fortnightly 'challenge' meetings with People Directorate leads involving both the Cabinet member for Health and Social Care and the Deputy Leader. We recognise that this is a major management pressure for the Council and it is acting promptly to rectify the situation.<br><br>The Council is also working with the Birmingham and Solihull Sustainability and Transformation Plan programme board to ensure there is clarity about both the amount and timing of financial support for service redesign and Better Care Fund funding in future years.<br><br>We identified in our initial risk assessment that the key risk was that the major savings schemes will not deliver the required recurrent savings, or will take longer to implement than planned. The £34.8 million shortfall in recurrent savings brought forward from 2015/16 and the delivery difficulties with the largest savings scheme in 2016/17 means that this risk is not sufficiently mitigated. In our view savings planning arrangements did not sufficiently take into account the impact of the level of non-recurrent savings or adequately assess the vulnerability of the largest proposed savings scheme.<br><br>We have concluded that these weaknesses in the Council's arrangements relate to the adequacy of financial planning VfM criteria as part of sustainable resource deployment. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Services for vulnerable children**<br>The Council's services for vulnerable children are assessed as inadequate by Ofsted and subject to an Improvement Notice. The Secretary of State has appointed a second Children's Commissioner. The key risk is that the service does not show demonstrable improvement and continues to be subject to external intervention. | The Council was subject to an Ofsted monitoring visit in early June 2016 and the inspector wrote to the Council summarising her findings on 28 June 2016. The visit focused on safeguarding arrangements in schools, children missing from education, children being educated at home and the application of Prevent in schools.<br><br>The inspector's letter lists 13 areas where the Council was found to be under performing. The issues identified include:<br>• failure of senior management to promptly and effectively implement change,<br>• a lack of consistent improvement,<br>• failing to ensure children are always kept safe and not enough is being done to protect children from potential harm,<br>• significant numbers of children missing from education; and<br>• Weak strategic leadership of safeguarding children in schools that lacks sufficient rigour.<br><br>Sir Michael Wilshaw, the Chief Inspector of Schools, wrote an advisory letter to the Secretary of State on the 8 July 2016 concerning Birmingham City Council's children's services, its support for vulnerable schools and wider issues around safeguarding. The letter is headed " Birmingham City Council is still failing its children - particularly the most vulnerable" and is highly critical of the Council.<br><br>We understand that Ofsted plan to carry out a full inspection in September 2016, which is likely to report by December. It is clearly important that the Council can demonstrate sufficient improvement to be assessed as adequate.<br><br>The Council announced in May 2016 its intention to investigate a children's trust model as part of its improvement planning. A report was presented to Cabinet in July 2016 supported by a 'case for change' analysis. An appraisal process and timetable was agreed at that meeting and a preferred option will be presented to Cabinet in September.<br><br>The Secretary of State appointed Andrew Christie as the Council's Children's Commissioner in December 2015. He is the second post holder and was appointed as the Council was not performing to an adequate standard and meeting all of its responsibilities under the Education Act 1996 and the Children's Act 2004. We have met with the Children's Commissioner twice during the course of this year's audit. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Services for vulnerable children (continued)** | We identified in our initial risk assessment that the key risk was that services for vulnerable children do not show demonstrable improvement and continue to be subject to external intervention. The findings of the Ofsted monitoring report and the continuation of external intervention by the Children's Commissioner means that this risk is not sufficiently mitigated.<br><br>We concluded that these weaknesses in the Council's arrangements relate to managing risks effectively and maintaining a sound system of internal control, demonstrating and applying the principles and values of good governance, as part of informed decision making and planning, organising and developing the workforce effectively to deliver strategic priorities as part of strategic resource deployment. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Management of schools**<br>The Council's management of the governance of schools was found to be weak and an Education Commissioner was appointed by the Secretary of State. This appointment is continuing and the Birmingham Education Partnership (BEP) has responsibility for implementing the improvement plan. The key risk is that plan implementation will be slower than envisaged and underlying issues will not be effectively addressed. | The Birmingham Education and Schools' Strategy and Improvement Plan (2015-16) was subject to an LGA peer challenge which reported to the Council in December 2015. The peer challenge considered five work streams. Its findings included the following:<br>• the Council has made good progress across the five work streams<br>• there is confidence amongst members, officers and partners that the basics for strong effective city wide system of school improvement are in place<br>• stronger professional leadership is making a significant impact and governance is now high on the agenda<br>• the Birmingham Education Partnership (BEP) is widely regarded as the right vehicle for school improvement and has good buy-in from schools.<br><br>These findings are not wholly consistent with the Ofsted monitoring visit findings, which indicated that there are continuing and serious weaknesses in the management of schools. In particular, arrangements for ensuring children with special educational needs receive full time education, weak links with independent schools and ensuring appropriate suitability checks are carried out for potential governors of schools not maintained by the Council. In his advisory letter to the Secretary of State, Sir Michael Wilshaw also concluded that there is more the Council needs to do to support headteachers in schools at risk of radicalisation.<br><br>As part of the assessment of schools governance improvement Birmingham Audit (internal audit) have been commissioned to carry out a programme of audits over a two year period. Their findings so far have shown that there are a range of governance issues to address across the schools visited. Eleven of the 48 schools visited have been assessed as 'level 3' assurance (specific control weaknesses of a significant nature noted, and/or the number of minor weaknesses noted was considerable).<br><br>We identified in our initial risk assessment that the key risk was that plan implementation will be slower than envisaged and underlying issues will not be effectively addressed. Although it is clear that progress has been made with the establishment of the BEP and the implementation of the improvement plan there is still work to do. The pace of school improvement is the key issue affecting our judgement.<br><br>We concluded that these weaknesses in the Council's arrangements relate to managing risks effectively and maintaining a sound system of internal control, demonstrating and applying the principles and values of good governance, as part of informed decision making and planning, organising and developing the workforce effectively to deliver strategic priorities as part of strategic resource deployment. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Improvement Panel**<br>The Improvement Panel has been in place since January 2015, following the publication of Lord Kerslake's report on the Council's governance. The Panel has reported to the Secretary of State on the progress made by the Council, but has also noted its concerns. The key risk is that the Panel will conclude that the Council is not making sufficient progress in implementing the changes needed. | We have met with the Vice Chair of the Improvement Panel on a frequent basis throughout the year and been briefed on the Panel's view of the progress being made. The Panel wrote to the Secretary of State in November 2015, January 2016 and March 2016.<br><br>The Panel's March 2016 letter referred to the positive improvement that the change in political leadership was having, the strengthening of corporate leadership and the Council's gap analysis of what it needs to do in the next six months. The Panel noted that:<br><br>"…., much has been done, progress continues to be made, the pace of change is picking up, but the required impact is not yet sufficient. The Panel is hopeful about the prospects for further improvement, but the robustness, resilience and sustainability of the Council's progress is yet to be evidenced."<br><br>The Panel's letter also refers to the development of the long term financial strategy and raises concerns about the scale and nature of the 2017/18 savings plans in particular. The letter concludes:<br><br>"….., the Panel believes it would now be appropriate for the political and managerial leadership to be given the chance to work together and demonstrate the Council's ability to deliver the actions outlined in the Council's recent gap analysis, without the current level of intervention. The Panel therefore considers it should stand back for a period, undertaking a review of further progress in the autumn, drawing again on feedback from residents, partners, elected members and staff."<br><br>The Secretary of State agreed to this course of action in his response.<br><br>We identified in our initial risk assessment that the key risk is that the Panel will conclude that the Council is not making sufficient progress in implementing the changes needed. We have considered whether the stepping back of the Panel is sufficient for us not to qualify our VfM conclusion. In our view it is not. The Panel was fully engaged with the Council during 2015/16 and it is yet to conclude that sufficient progress has been made in implementing the changes needed.<br><br>We concluded that the Panel's continuing engagement is evidence that the significant governance failings previously identified have not been fully addressed as part of the arrangements to support informed decision making. |

## Key findings

| Significant risk | Findings and conclusions |
| --- | --- |
| **Health and Social Care funding**<br>The Council has a good track record of controlling health and social care spend and has extensive partnership arrangements with Health bodies. Delivery of service outcomes is dependent on effective partnership working with Clinical Commissioning Groups. The key risk is that partnership arrangements do not fully deliver service outcomes and improvements. | We have considered the governance arrangements for the Better Care Fund and other pooling agreements. In particular, the clarity of lines of accountability to the Council. We have also considered the risk sharing arrangements in place and the partnership arrangements.<br><br>The Birmingham Better Care Fund totals £100 million for 2015/16 with contributions from the Council and its Health partners. The main decision making forum for the Better Care Fund is the 'Commissioning Executive'. Whilst our work has shown that the governance of the fund is operating effectively and appropriately it is clear that the partnership has not achieved the forecast efficiencies envisaged by the fund inception. This does not reflect a weakness in the Better Care Fund governance arrangements but is indicative of the weaknesses nationally in the fund implementation.<br><br>The Council also works with its Health partners through the Learning Disabilities and Mental Health pooled budget. The Council contributed £93.0 million of the total pooled spending of £259.3 million in 2015/16. When reviewing the governance arrangements for the pooled budget we were told that the joint commissioning board has not met since April 2015.<br><br>Without this board in place, which has been absent for the full financial year, there has been inadequate reporting of performance or financial information to all pooled budget members collectively. At the time of writing we are not aware of any plans to address this. We are however aware that the Council has continued to lead on Learning Disabilities services and its Health partners commission and delivering Mental Health services.<br><br>We identified in our initial risk assessment that the key risk is that partnership arrangements do not fully deliver service outcomes and improvements. We have noted that the Better Care Fund has not fully delivered due to weaknesses in national implementation. We have also considered the impact of the failure to maintain the joint commissioning board for the pooled budget. The lack of oversight may have resulted in ineffective working with third parties and needs to be rectified. However, we have seen no evidence that service outcomes and improvements have not been delivered. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Future Council**<br>The programme is ambitious and extensive. It has five work streams and it is essential that delivery is effectively managed. The key risk is that deliverables are not clearly identified, project and risk management arrangements are not effective, and as a result changes are not implemented as intended. | The Future Council programme has now moved to its second phase. The programme started in June 2015 and the first phase focused on the 'Whole Council' programme structure. This had five sub-programmes focusing on the Council's operating model, its political governance, integrated support services, the workforce strategy and working with partners.<br><br>A Programme Transition Report was presented to Corporate Leadership Team in June 2016. This identified the key outcomes of the first phase and the objectives and approach for the second phase. The report highlights the outcomes achieved, but also notes that there is outstanding activity to be carried forward to phase two. It also notes that the programme governance was thoroughly thought through and generally worked well. Performance against 134 key actions derived from the Kerslake report were tracked and the report identifies that 109 of these were delivered by June 2016. There is also a clear focus on risk management.<br><br>A briefing document was sent to all staff on the 26 July 2016, providing an outline of the progress made with the Future Council Programme and how it is being developed. This includes five key outcomes from phase one and eight areas where improvements are still needed. Four supporting programmes for phase two; creating an improvement hub, developing the people strategy, implementing the IT and digital strategy and designing services from a citizen perspective through the citizen access strategy.<br><br>A clear project management structure is outlined, with the establishment of a programme management office. This will have a key role in ensuring that the Council's leadership is clearly sighted on progress and risk management.<br><br>We identified in our initial risk assessment that the key risk is that deliverables are not clearly identified, project and risk management arrangements are not effective, and as a result changes are not implemented as intended. We have concluded that this risk is effectively mitigated by the arrangements in place during phase one of the programme. |

## Key findings

| Significant risk | Findings and conclusions |
|---|---|
| **Equal Pay**<br>The Council has a settlement plan for Equal Pay claims that is dependent on utilising capital receipts. The key risk is that there will be insufficient resources available to meet these commitments. | We have reviewed the settlement plan and are satisfied that the capital receipts generated are sufficient to meet the Council's anticipated equal pay commitments. During 2015/16 over £200 million of claims have been settled resulting in a reduced provision in the 2015/16 financial statements of £310 million.<br><br>In previous years there has been greater uncertainty about the extent of the Council's liabilities for the claims as this is dependent on complex law against the particular circumstances at each authority. As more local cases have been settled and information about claims has become clearer, the extent of the Council's liabilities can be determined with greater certainty.<br><br>We have concluded that the receipt of funds from asset sales and the continuing fall in the Council's liabilities contribute to sufficient resources being available to meet the Councils equal pay commitments. |

# Section 4: Fees, non-audit services and independence

We confirm below our final fees charged for the audit and provision of non-audit services.

## Fees

| | Proposed fee £ | Final fee £ |
|---|---|---|
| Council audit | 314,168 | 314,168 |
| Grant certification | 17,594 | TBC |
| **Total Council audit fees (excluding VAT)** | **331,762** | **TBC** |

## Fees for other services

| Service | Fees £ |
|---|---|
| Certification of grant claims (outside Audit Commission/PSAA requirements) | **16,700** |
| Finance Birmingham | **22,125** |
| | **38,825** |

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA).

### Grant certification

Our fees for grant certification cover only housing benefit subsidy certification, which falls under the remit of Public Sector Audit Appointments Limited. Fees in respect of other grant work, such as reasonable assurance reports, are shown under 'Fees for other services'.

### Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

# Section 5: Communication of audit matters

# Communication to those charged with governance

International Standards on Auditing ISA (UK&I) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

The Audit Plan outlined our audit strategy and plan to deliver the audit, while this Audit Findings report presents the key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

## Respective responsibilities

The Audit Findings Report has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by Public Sector Audit Appointments Limited (http://www.psaa.co.uk/appointing-auditors/terms-of-appointment/)

We have been appointed as the Council's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England at the time of our appointment. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice ('the Code') issued by the NAO (https://www.nao.org.uk/code-audit-practice/about-code/). Our work considers the Council's key risks when reaching our conclusions under the Code.

It is the responsibility of the Council to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Council is fulfilling these responsibilities.

| Our communication plan | Audit Plan | Audit Findings |
|---|---|---|
| Respective responsibilities of auditor and management/those charged with governance | ✓ | |
| Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications | ✓ | |
| Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought | | ✓ |
| Confirmation of independence and objectivity | ✓ | ✓ |
| A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence.<br>Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged<br>Details of safeguards applied to threats to independence | ✓ | ✓ |
| Material weaknesses in internal control identified during the audit | | ✓ |
| Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements | | ✓ |
| Non compliance with laws and regulations | | ✓ |
| Expected modifications to auditor's report | | ✓ |
| Uncorrected misstatements | | ✓ |
| Significant matters arising in connection with related parties | | ✓ |
| Significant matters in relation to going concern | | ✓ |
| Significant matters in relation to the Group audit including:<br>Scope of work on components, involvement of group auditors in component audits, concerns over quality of component auditors' work, limitations of scope on the group audit, fraud or suspected fraud | ✓ | ✓ |

# Appendices

# Appendix A: Action plan

**Priority**
**High** - Significant effect on control system
**Medium** - Effect on control system
**Low** - Best practice

| Rec No. | Recommendation | Priority | Management response | Implementation date & responsibility |
|---|---|---|---|---|
| | **Accounts** | | | |
| 1 | Narrative report – the draft report did not include sufficient commentary on the two major material disposals that had taken place during the year. For future years it is important to ensure that there is sufficient narrative about redevelopment schemes such as the Paradise project. | Medium | | |
| 2 | Major schemes, supporting information – during our audit we became aware that key information relating to the NEC and Grand Central disposals had not been shared with the Financial Accounts Team when they were preparing the accounts. Key information relating to the Paradise project and other major schemes needs to be provided to the Financial Accounts Team to enable them ensure that the accounting treatment adopted is appropriate. | High | | |

# Appendix A: Action plan

| Rec No. | Recommendation | Priority | Management response | Implementation date & responsibility |
|---|---|---|---|---|
| 3 | Annual Governance Statement – we noted that group governance arrangements were not included in the AGS. In future the AGS should include narrative on group governance arrangements. | Medium | | |
| 4 | IT internal controls – a control weakness relating to the automation of leaver notification was reported to IT management. Management need to ensure that our recommendation is implemented by Service Birmingham. | Medium | | |
| 5 | Group accounts, entity accounts – group accounts are drafted using unaudited financial information provided by group entities. In future the Audit Committee need assurance that group entities provide sufficient information by the end of May to ensure materially accurate group accounts can be produced and that audited accounts are received before the completion of the Council's audit. | Medium | | |

# Appendix A: Action plan

| Rec No. | Recommendation | Priority | Management response | Implementation date & responsibility |
|---|---|---|---|---|
| | **Value for Money Conclusion** | | | |
| 6 | Savings challenge – effective plans need to be put in place to respond to the under delivery of savings plans and emergent budget pressures, particularly in the People Directorate. These need to include a realistic assessment of the use of reserves to enable sufficient lead time for savings plans to be implemented. | High | | |
| 7 | Services for vulnerable children – the Council needs to demonstrate how the plans for services to vulnerable children, including the options for setting up a Children's Trust, will deliver specific and measureable improvements promptly. | High | | |
| 8 | Management of schools – the implementation of the Birmingham Education Delivery and Improvement Plan needs to demonstrate that the issues raised by Ofsted, including children missing from education, are being addressed promptly and effectively. | High | | |
| 9 | Improvement Panel – the Council needs to demonstrate to the Improvement Panel that the pace of change and the impact of new political and corporate leadership arrangements are sufficient to address the concerns previously raised by the Panel. | High | | |

# Appendix A: Action plan

| Rec No. | Recommendation | Priority | Management response | Implementation date & responsibility |
|---|---|---|---|---|
| 10 | Health and social care – the Council and its health partners need to either reinstitute the joint commissioning board for the learning disabilities and mental health services pooled budget, or agree alternative arrangements. | High | | |

# Appendix B: Audit opinion

**We anticipate we will provide the Council, including the Group with an unqualified audit report**

**INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF BIRMINGHAM CITY COUNCIL**

We have audited the financial statements of Birmingham City Council (the "Authority") for the year ended 31 March 2016 under the Local Audit and Accountability Act 2014 (the "Act"). The financial statements comprise the Movement in Reserves Statement, the Group Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Group Comprehensive Income and Expenditure Statement, the Balance Sheet, the Group Balance Sheet, the Cash Flow Statement, the Group Cash Flow Statement, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement, the Collection Fund Income and Expenditure Account and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

This report is made solely to the members of the Authority, as a body, in accordance with Part 5 of the Act and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

**Respective responsibilities of the Strategic Director, Finance and Legal and auditor**
As explained more fully in the Statement of Responsibilities for the Financial Statements, the Strategic Director, Finance and Legal is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16, which give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

**Scope of the audit of the financial statements**
An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Authority and Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Strategic Director, Finance and Legal; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Narrative Report, the Group Narrative Report, and the Annual Governance Statement to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

**Opinion on financial statements**
In our opinion the financial statements:
- present a true and fair view of the financial position of the Authority and Group as at 31 March 2016 and of the Authority's and Group's expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 and applicable law.

**Opinion on other matters**
In our opinion, the other information published together with the audited financial statements in the Narrative Reports, and the Annual Governance Statement is consistent with the Group audited financial statements.

**Matters on which we are required to report by exception**
We are required to report to you if:
- in our opinion the Annual Governance Statement does not comply with the guidance included in 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007; or
- we issue a report in the public interest under section 24 of the Act; or
- we make a written recommendation to the Authority under section 24 of the Act; or
- we exercise any other special powers of the auditor under the Act.

We have nothing to report in these respects.

**Conclusion on the Authority's arrangements to secure value for money through economic, efficient and effective use of its resources**
**Respective responsibilities of the Authority and auditor**
The Authority 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 review regularly the adequacy and effectiveness of these arrangements.

We are required under Section 20(1)(c) of the Act to be satisfied that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

**Scope of the review of the Authority's arrangements to secure value for money through economic, efficient and effective use of its resources**

We have undertaken our review in accordance with the Code of Audit Practice prepared by the Comptroller and Auditor General as required by the Act (the "Code"), having regard to the guidance on the specified criteria issued by the Comptroller and Auditor General in November 2015, as to whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The Comptroller and Auditor General determined these criteria as those necessary for us to consider under the Code in satisfying ourselves whether the Authority put in place proper arrangements to secure value for money through the economic, efficient and effective use of its resources for the year ended 31 March 2016.

We planned our work in accordance with the Code. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether in all significant respects the Authority has put in place proper arrangements to secure value for money through economic, efficient and effective use of its resources.

**Basis for qualified conclusion**

In considering the Authority's arrangements for securing efficiency, economy and effectiveness we identified the following matters:

*Financial planning arrangements*

The Authority's 2015/16 budget included the requirement to deliver £110.3 million of recurrent savings. During 2015/16 the Authority also updated its Long Term Financial Plan and Efficiency Statement for the period 2016/17 - 2025/26, which includes the requirement to deliver a further £88.3 million of recurrent savings in 2016/17.

The planned delivery of savings is not being achieved and there were weaknesses in the delivery of recurrent savings in 2015/16, resulting in £34.8 million of the savings being non-recurrent. The largest savings plan relates to health and social care service redesign and Better Care Fund funding, which was planned to deliver £60 million of savings over the three years to 2018/19. This plan assumed that in 2016/17 £28 million of funding would be released by Government and Health partners to support the Authority in this service redesign. This funding has not yet been secured and there is uncertainty about whether any of it will be received in 2016/17 and how much will be received in future years. The Authority has yet to fully secure alternative savings actions to replace this plan for 2016/17.

This matter is evidence of weaknesses in the adequacy of financial planning to support sustainable resource deployment.

*Managing risks effectively and organising and developing the workforce*

In May 2014 the Office for Standards in Education (Ofsted) issued a report on its inspection of services for children in need of help and protection, children looked after and care leavers in Birmingham. It assessed the services as inadequate and identified a number of serious weaknesses in the Authority's arrangements for looking after vulnerable children and young people.

In July 2014 significant failings in the Authority's management of schools were identified in a review by Peter Clarke in July 2014. Since this review the Authority has taken and continues to take action to improve its management of schools through the implementation of its improvement plan.

However, an Ofsted monitoring visit in June 2016 identified 13 areas of underperformance, where they stated that arrangements were not yet adequate. The issues identified included:

- a lack of consistent improvement;
- failure of senior management to promptly and effectively implement change;
- failure to ensure children are always kept safe and not doing enough to protect children from potential harm;
- significant numbers of children missing from education; and
- weak strategic leadership of safeguarding children in schools that lacks sufficient rigour.

**Qualified conclusion**

On the basis of our work, having regard to the guidance on the specified criteria issued by the Comptroller and Auditor General in November 2015, except for the effects of the matters described in the Basis for qualified conclusion paragraph, we are satisfied that, in all significant respects, the Authority put in place proper arrangements to secure value for money through economic, efficient and effective use of its resources for the year ended 31 March 2016.

**Certificate**

We certify that we have completed the audit of the accounts of the Authority in accordance with the requirements of the Act and the Code.

Phil Jones
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

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