

Annual Audit and Inspection Letter

Herefordshire Council

The Audit Commission is an independent body responsible for ensuring that public money is spent economically, efficiently and effectively, to achieve high-quality local services for the public. Our remit covers around 11,000 bodies in England, which between them spend more than £180 billion of public money each year. Our work covers local government, health, housing, community safety and fire and rescue services.

As an independent watchdog, we provide important information on the quality of public services. As a driving force for improvement in those services, we provide practical recommendations and spread best practice. As an independent auditor, we ensure that public services are good value for money and that public money is properly spent.

Status of our reports

This report provides an overall summary of the Audit Commission's assessment of the Council, drawing on audit, inspection and performance assessment work and is prepared by your Relationship Manager.

In this report, the Commission summarises findings and conclusions from the statutory audit, which have previously been reported to you by your appointed auditor. Appointed auditors act separately from the Commission and, in meeting their statutory responsibilities, are required to exercise their professional judgement independently of the Commission (and the audited body). The findings and conclusions therefore remain those of the appointed auditor and should be considered within the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission.

Reports prepared by appointed auditors are:

- prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission; and
- addressed to members or officers and prepared for the sole use of the audited body; no responsibility is taken by auditors to any member or officer in their individual capacity, or to any third party.

Copies of this report

If you require further copies of this report, or a copy in large print, in Braille, on tape, or in a language other than English, please call 0845 056 0566.

© Audit Commission 2007

For further information on the work of the Commission please contact:

Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ

Tel: 020 7828 1212 Fax: 020 7976 6187 Textphone (minicom): 020 7630 0421

www.audit-commission.gov.uk

Contents

| | |
|--|-----------|
| Our overall summary | 4 |
| Performance issues | 4 |
| Other accounts and governance issues | 5 |
| Action needed by the Council | 5 |
| How is Herefordshire Council performing? | 7 |
| The improvement since last year - our Direction of Travel report | 8 |
| Performance information | 13 |
| Working with other inspectorates and regulators | 13 |
| Performance management | 14 |
| Local Area Agreements | 15 |
| Pooled budgets | 15 |
| Financial management and value for money | 17 |
| Financial reporting - audit of 2005/06 accounts | 18 |
| Financial management | 18 |
| Financial standing | 19 |
| Systems of internal financial control | 20 |
| Value for money | 21 |
| Other work | 23 |
| Waste management | 23 |
| Herefordshire Connects Programme | 23 |
| Grant claims | 24 |
| Conclusion | 25 |
| Availability of this letter | 25 |

Our overall summary

- 1 This report provides an overall summary of the Audit Commission's assessment of the Council. It draws on the findings and conclusions from the audit of the Council and from a wider analysis of the Council's performance and its improvement over the last year, as measured through the Comprehensive Performance Assessment (CPA) framework.
- 2 The report is addressed to the Council, in particular it has been written for councillors, but is available as a public document for stakeholders, including members of the community served by the Council. The main messages included in this report for the Council are set out below.

Performance issues

- 3 Our Direction of Travel assessment is that the Council is improving adequately.
- 4 Overall the Council is maintaining its performance and has made improvements in priority areas including safeguarding vulnerable children and helping more elderly adults to live at home. Further progress in children's and adult services has been limited by skills shortages which are now being resolved.
- 5 Performance in both benefits and homelessness dipped in 2005/06 but is recovering well. There have been improvements in planning, recycling and the amount of household waste collected, but environmental health and trading standards have deteriorated. The Council has worked effectively with its partners to reduce crime and improve the health of children and young people.
- 6 The improvement plan drawn up following the Audit Commission's corporate assessment has been strengthened. The business transformation programme, Herefordshire Connects, continues to be developed, but still presents some risks for the Council. Corporate resource management has improved significantly and services continue to provide good value for money. Although there has been an improvement in public satisfaction with most Council services and in public access to services, overall satisfaction with the Council has fallen and is low compared with similar councils.
- 7 The Council is making steady progress in strengthening its performance management arrangements and in embedding a performance culture.

Other accounts and governance issues

- 8 Accounts production was good and timely. We were able to issue an unqualified audit opinion by the earlier deadline of 30 September 2006.
- 9 Systems of internal control and financial management have improved significantly in the year. Your arrangements for the acceptance of gifts and hospitality have been strengthened now.
- 10 Changes to the waste management PFI agreement, which is being negotiated in partnership with Worcestershire County Council, are slow and still not agreed. There continues to be a risk of contract termination.
- 11 The overall financial position of the Council was sound at the 31 March 2006, with the accounts showing a £4.1m under spend and £28.4m of balances. The Council has a good historical track record of keeping expenditure within budget but agrees that unexpected under-spending is not acceptable and the range of reserves it holds needs reviewing. The Council's pension fund deficit reduced slightly to £101m, but is still a cause for concern.
- 12 The Council's arrangements for pooling budgets with the local Primary Care Trust (PCT) were found in need of development. In particular agreements were out of date and risk sharing is very limited. We noted in our September Governance Report that the Council was owed over £1 million by the PCT in relation to pooled budget contributions. This has still not been resolved. This area significant given the current moves towards the development of a Public Service Trust together with the PCT.
- 13 The business transformation programme Herefordshire Connects continues to be developed. This ambitious programme is a key element of the Council's medium term financial strategy and is planned to deliver significant financial savings. However there are also significant risks attached to this both now in getting the specification right for the Council's future needs and subsequently in terms of delivering the benefits expected.

Action needed by the Council

- 14 Members need to take the following actions.
 - Focus on improving service outcomes and ensure that actions recommended by our recent performance management report are delivered.
 - Before awarding a contract for Herefordshire Connects, formally consider what other options are still open to the Council and the costs, benefits and risks of each option. The Council should then agree a process to monitor whether the expected financial and other benefits are delivered.
 - Monitor the improvement of joint working arrangements with the PCT in preparation for a forthcoming decision on whether to set up a Public Service Trust in Herefordshire.

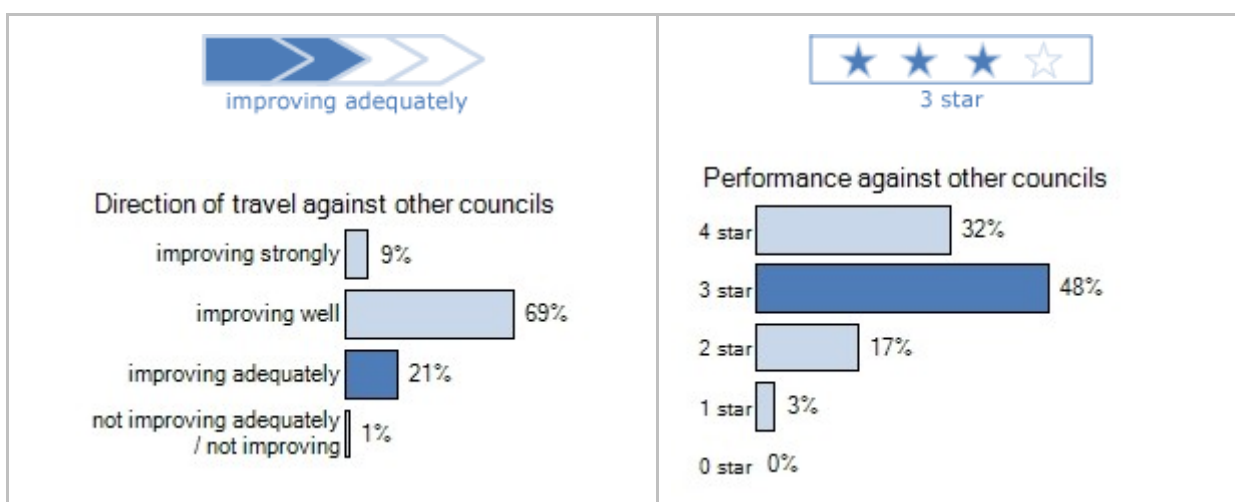
6 Annual Audit and Inspection Letter | Our overall summary

- Ensure that the necessary changes to the waste management contract are resolved promptly.
- Further develop the ethical governance and anti-fraud culture within the Council.
- Ensure that improvements in value for money are accounted for in a straightforward and transparent way, by improving service planning and reporting arrangements.
- Monitor the development of corporate approaches to procurement.
- Ensure robust approaches to benchmarking in all service areas, and ensure that challenge (eg Scrutiny) is robust.

How is Herefordshire Council performing?

- 15 The Audit Commission's overall judgement is that Herefordshire Council is improving adequately and the Council is classified as a three star in its current level of performance under the Comprehensive Performance Assessment. These assessments have been completed in all single tier and county councils with the following results.

Table 1



Source: Audit Commission

- 16 The detailed assessment for Herefordshire Council is as follows.

Our overall assessment - the CPA scorecard

Table 2 CPA scorecard

| Element | Assessment |
|---|----------------------|
| Direction of Travel judgement | Improving adequately |
| Overall | 3 star |
| Current performance | |
| Children and young people | 2 |
| Social care (adults) | 2 |
| Use of resources | 3 |
| Housing | 2 |
| Environment | 2 |
| Culture | 3 |
| Benefits | 2 |
| Corporate assessment/capacity to improve | 2 |
| Previous corporate assessment/capacity to improve, as included in overall CPA judgement in 2006 | 3 |

(Note: 1=lowest, 4= highest)

The improvement since last year - our Direction of Travel report

Herefordshire Council is improving adequately.

- 17 Overall, the Council is maintaining its performance and has made improvements in priority areas including safeguarding vulnerable children and helping more elderly adults to live at home. Further progress in children's and adult services has been limited by skills shortages which are now being resolved.
- 18 Performance in both benefits and homelessness dipped in 2005/06 but is recovering well. There have been improvements in planning, recycling and the amount of household waste collected, but environmental health and trading standards have deteriorated. The Council has worked effectively with its partners to reduce crime and improve the health of children and young people.

- 19 The improvement plan drawn up following the Audit Commission's corporate assessment has been strengthened. The business transformation programme, Herefordshire Connects, continues to be developed, but still presents some risks for the Council. Corporate resource management has improved significantly and services continue to provide good value for money. Although there has been an improvement in public satisfaction with most Council services and in public access to services, overall satisfaction with the Council has fallen and is low compared with similar councils.

Evidence of improving outcomes

- 20 The Council is maintaining overall performance levels with 58 per cent of comparable service performance indicators improving (compared with the average for similar Councils of 67 per cent) but 38 per cent deteriorating.¹
- 21 The Council has had some success in improving outcomes in its priority areas of adult social care and children's services. The external inspectorate, CSCI, assessed both of these areas as providing adequate services for local people, the same score as in 2005. However, the Council has made significant progress in improving its arrangements for safeguarding vulnerable children, moving from an assessment of inadequate to good. In addition, there have been some improvements in educational achievement, particularly at GCSE level.
- 22 In Adult Social Care the Council has made some improvements in helping more vulnerable people to live at home and in increasing the number of direct payments made. There is a mixed picture of progress in other key service areas. In the Council benefits service, the external inspection score dropped from 3 to 2, with an increase in the time taken to assess benefits claims due to changes in the Council's benefits IT systems. However Council figures for the first three quarters of 2006/07 indicate that performance has improved strongly since then. Performance in the environment service area is generally strong, with improvements in the priority areas of, recycling and the amount of waste collected from households as well as in the speed of determining planning applications but a downward trend in environmental health and trading standards. Finally, the Council's homelessness service is improving in recent months after a worsening performance in 2005/06 when indicators showed an increase in both the number of households in temporary accommodation and the length of time spent in bed and breakfast.
- 23 The Council makes an effective contribution to wider community outcomes and has strengthened its overall approach to partnership working as a key member of the Herefordshire Partnership. This has been most evident in the work the Council has done in developing the Local Area Agreement and in working with partners to improve outcomes in such areas as crime, children's health and economic development. In the area of crime, there have been decreases in the number of domestic burglaries, theft of motor vehicles and violence against the person. CSCI assessed the Council's contribution to children's health as good, despite a small increase in the rate of teenage pregnancies, with the specific health needs of looked after children being met effectively. There have been reductions in the numbers of people killed and injured on the roads. Finally, in the area of economic regeneration, the Council, with its partners, is progressing ambitious schemes such as the Edgar Street Grid, the Leominster Enterprise Park, the Rotherwas Futures and the Herefordshire Learning Village.

¹ These statistics exclude indicators for children's, young people's and older people's services.

Access and the quality of service

- 24** The Council is making steady improvements in improving access to its services for local people. It has information points in four key market towns where customers can access all Council services, and a further centre is opening in Hereford in 2007. Front line staff are being integrated and provided with customer service training with a view to breaking down barriers between traditional service areas and providing customers with a one-stop solution to their enquiries. There are some key areas of increased satisfaction, both around Council services and quality of life. There is good satisfaction with recycling and civic amenity sites, sports and leisure facilities and libraries. In terms of quality of life, residents are more positive about anti-social behaviour and environmental vandalism, but are increasingly critical of public transport provision. However, overall satisfaction with the Council, has fallen slightly and is among the lowest in comparable Councils.
- 25** In the area of equalities, although the Council has only reached level 1 of the national equality standard, it has improved the steps it is taking to progress to the next level. An example of this improved approach can be seen in the way the Council is addressing the issue of the large number of migrant workers in the county. It is developing, with the Police and PCT, a website for such workers to provide them with information and advice. More is needed to be done, however, in specific service areas with CSCI commenting that the adult social care service has not done enough to focus on the specific needs of minority ethnic groups. The Council is addressing this with its partners and hopes to use its improved demographic data to ensure that services are appropriate and relevant for all sections of the community.

Value for money

- 26** The Council maintained its value for money rating of 3 in the annual use of resources assessment. The overall low spend, linked to a reasonable level of performance across all services is providing good value for local people. The Council is improving its management of value for money with a better integration of data on resources and performance, service and financial planning are now much better linked. The Council has also put in place robust processes to assess the capacity of specific service areas to resource its planned improvement activity. The Council has introduced annual efficiency statements and has set itself challenging targets for efficiency gains, particularly in respect of releasing cash. It reports achievement of 87 per cent of its efficiency targets in 2005/06.
- 27** The constant pressure on budgets and the need to improve performance mean that the Council needs to demonstrate value for money particularly in children's services and adult social care in future.

- 28 The Council is making good progress in strengthening its arrangements for securing continuous improvement. Good performance management processes have been put in place at a corporate level and this is leading to improvements in both processes and culture in key service areas. Significant improvement has taken place in the integration of the Council's service and financial planning processes. The Council has an improved medium-term financial strategy and has established a performance improvement cycle that is robust and has the potential to drive improvement. The Council is aware of the need to improve the role of overview and scrutiny in performance management and the scrutiny improvement plan is being implemented.

Improvement plans

- 29 The Council has strengthened its improvement planning over the past year after responding satisfactorily to the findings of the corporate assessment and the joint area review (JAR) in late 2005. The initial response by the Council was to put in place an overall improvement plan which, among things, contained a discrete JAR action plan. The overall improvement plan was a good attempt to identify the full range of challenges facing the Council and the actions coming out of these, but it needed to be sharper in terms of outcomes, indicators and targets to ensure that it could be robustly monitored. The Council recognised this and has strengthened its approach, having developed a set of six discrete improvement plans (both service specific and corporate) as part of its business transformation programme. This programme has clear terms of reference and is due to be managed under well-established project management guidelines.
- 30 One of the six areas is Herefordshire Connects, the Council's overall plan to modernise its ICT infrastructure. This programme, which is moving towards the implementation stage with a provider being chosen by February 2007, contains both risks and potential benefits for the Council. The most important risk is that the project may not deliver the expected efficiencies and service improvements within the planned cost envelope. Further risks are referred to later in this letter. In both children's services and adult social care the Council has been developing good building blocks for future improvement by commissioning work from external consultants which has identified key issues and areas of work.
- 31 Herefordshire has had some capacity problems in the past that have hampered its attempts to improve. Since the 2005 corporate assessment, the Council has been assessing its own ability to make the improvements needed. It has used help available from government departments effectively and has engaged consultants where necessary to speed progress in key areas eg the plan for adults' services. It is ensuring that there is adequate capacity to implement its improvement plans, both for corporate issues and in specific services, by measuring the specific requirements being made on key corporate services – ICT, project management and HR. This process has led to the Council being better placed to deliver its improvement plans than it has been for some time.

- 32** In children's services the Council was judged as having adequate capacity by CSCI and is building on this by more partnership working, and by investing in additional performance management posts and systems. In adult social care CSCI's assessment was that there were 'uncertain prospects' for improvement, but there are a number of more recent developments that indicate a more positive outlook. These include the completion of a comprehensive needs assessment, externally commissioned work around such issues as performance management and commissioning, and the setting up of a change team to drive forward improvement.
- 33** Negotiations, in partnership with Worcestershire County Council, for a new long term waste disposal contract have been slow. The waste PFI continues to be a risk for the Council and it is not yet clear whether the contract will deliver value for money. To ensure the continued economic and efficient disposal of waste in future it is important that a contract with a new provider is established soon.

Performance information

- 34** The Audit Commission approach to the audit of statutory performance information changed this year, with a 'lighter touch' being applied. This meant that we reviewed your overall management arrangements to develop the quality of data and only tested a limited number of performance indicators. There were five themes for us to consider as part of our work on Data Quality; Governance and Leadership, Policies, Systems and Processes, People and Skills and Data Use.
- 35** The Council continues to develop and improve its management arrangements for ensuring the quality of data. The Integrated Performance Reporting methodology has improved the focus of performance indicators within the Council, the collection and reporting of performance information across the Council has led to more attention being paid to all indicators.
- 36** There are, however, areas for further improvement. In particular there should be a formal strategy for data quality put in place which should be agreed to by Members. Specific data quality policies should be put in place to support the current guidance and regular formalised training for relevant staff would support the Data Quality process.

Working with other inspectorates and regulators

- 37** An important aspect of the role of the Relationship Manager is to work with other inspectorates and regulators who also review and report on the Council's performance. Relationship Managers share information and seek to provide 'joined up' regulation to the Council. During the last year the Council has received the following assessments from other inspectorates.
- 38** CSCI's Annual Assessment has concluded that social care for adults is 'serving some adults well' with 'uncertain prospects for improvement', whereas social care for children is 'delivering an adequate service for children' and has 'adequate capacity for improvement'.

- 39 The Benefits Fraud Inspectorate's annual assessment the Council's Benefits service concluded that it is 'fair'.

Performance management

- 40 The last Corporate Assessment of the Council in late 2005, assessed the Council's performance management arrangements as being adequate, but this remained the weakest area of the Council's overall arrangements. The assessment stated that the corporate performance management approach was not yet fully embedded and that there were some serious weaknesses in some important areas including children's social care. As a result we followed up the Council's progress in this area in the Autumn of 2006.
- 41 We concluded that the Council is making steady progress in strengthening its performance management arrangements and in embedding a performance culture. A new network of improvement managers is beginning to result in a more consistent, corporate approach to managing performance, individual performance management (the SRD process) is having a greater impact and there are some robust plans to improve the links between resources and performance. In addition, there is a greater focus on the collection and reporting of performance information across the Council which is leading to more attention being paid to poor or under-performance. However, because the Council's baseline position was relatively low, these improvements are not yet sufficient to meet the standard that the Council aspires to and are not yet embedded across the organisation.
- 42 In line with the trends at a corporate level, arrangements for managing performance in the two social care service areas, which have been criticised by a number of inspectorates, are steadily improving. A key factor in this improvement has been the involvement of the corporate performance management officers. There is a growing culture among staff at all levels in these service areas of the importance of performance management, improving data collection processes and a determination by managers to analyse performance information in a timely fashion. The result of this is that it is less likely than it was a year ago, in both service areas, that serious under-performance will go unreported. However, as with the arrangements at a corporate level, more is needed to be done, particularly in children's social care to ensure that the improvements are sustained, in line with overall corporate policy, and embedded across the service.
- 43 Arrangements for managing performance in the Benefits service have improved significantly over the past year with particular strengths around workload monitoring and the setting of individual targets.
- 44 Although the Council is continuing to develop a range of specific processes and initiatives designed to improve the way in which performance is managed, these components have not been brought together in a single, high-level model that clearly identifies how the Council plans to measure its performance and levels of improvement. The result of this is that it is not clear to many officers and members, how the various components fit together into a coherent whole and which aspects of the arrangements have a greater priority.

- 45 There is clear evidence of an improving culture of performance across the Council. Staff and managers in all the service areas we examined are becoming increasingly aware of the importance of performance management and managers are offering stronger leadership around performance and improvement issues. However, this trend is characterised by an ad hoc, unplanned approach to communication and there is no high-level consistent programme or strategy designed to identify and cascade what the Council means by a performance management culture and to enthuse and motivate staff into focussing on performance improvement. The lack of such a corporate strategy (distinct from the Council's overall improvement plan) may result in some service areas developing at a slower rate than others as managers do not have a robust, shared approach to refer to.
- 46 The Council has developed a very comprehensive action plan to address the recommendations in our detailed report.

Local Area Agreements

- 47 We carried out a high level overview of potential risk areas in the developing governance for the pilot local area agreements. In carrying out the work, it was agreed that we would liaise closely with the Government Office for the West Midlands to avoid duplication with their six-monthly review. Good progress is being made by the Council and its partners in addressing, to a greater or lesser extent, all of the issues set out above in the key risk areas. There are no serious weaknesses or gaps in the arrangements being developed and the Council's arrangements compare well to those we have reviewed elsewhere. There is clear enthusiasm among partners to make the LAA process work for the area and an obvious commitment to continuing the good work achieved to date. However, within each of the risk areas, particularly financial management, there is still more work to do before the overall arrangements can be said to be sufficiently robust and embedded. Specifically in financial management, the Council needs to work with Government Office to develop a plan to formalise how the issue of increasing the Single Pot is to be taken forward. We have since provided additional good practice guidance around financial management in LAAs to your officers. The Council has drawn up an action plan to address the recommendations in our full report.
- 48 Government office has recognised the good progress the Council has made and has given the Council two "green lights" ratings for achievement and prospects for improvement.

Pooled budgets

- 49 A year ago we carried out an overview assessment of the arrangements in place to manage the performance and ensure effective use of resources and integrated provision in the services covered by the pooled budget agreements for learning disabilities and mental health.

- 50 Our overall conclusion is that the integration of health and social care services for mental health and learning disabilities are delivering some benefits to service users. Further potential benefits could be realised by treating the budget more as a pooled resource. Some parts of the budget were being managed as separate health and social care elements.
- 51 In response to the overspend in learning disabilities, a fundamental review of key elements of service provision was being carried out with the aim of providing more targeted and cost effective services. In mental health, efficiencies are being achieved across the integrated services, but we felt a more strategic approach to managing the pooled fund was needed to ensure that resources are appropriately targeted. In both areas these needed to be supported by strengthened commissioning arrangements and stronger partnership agreements which incorporate clear measurable outcomes, with associated monitoring mechanisms.
- 52 We felt that the PCT and Council needed to ensure that the pooled budget arrangements were supported by clear and updated agreements to reflect progress and new strategic priorities. Our main recommendation to strengthen their partnership working through the pooled budget arrangements, was that the PCT and Council should update the agreements for each service area to reflect developments since the original agreements were made. These should include:
- joint strategic priorities and expected benefits for service users;
 - specific details of which resources are to be pooled and for what;
 - financial management arrangements including risk sharing and reporting;
 - performance management arrangements including joint targets and indicators and how and when they should be reported;
 - arrangements for ensuring feedback from service users including joint complaints systems; and
 - arrangements for ensuring value for money.
- 53 Delivery of the joint action plan addressing the recommendations in our detailed report is still planned for this spring. This issue is particularly significant given the Council's proposal to form a Public Service Trust with the local Primary Care Trust this year.

Financial management and value for money

- 54 As your appointed auditor, I have reported separately to your Audit and Corporate Governance Committee on the issues arising from our/the 2005/06 audit and have provided:
- an unqualified opinion on your accounts;
 - a conclusion on your VFM arrangements to say that these arrangements are adequate; and
 - a report on the Best Value Performance Plan confirming that the Plan has been audited.
- 55 The findings of the auditor are an important component of the CPA framework described above. In particular the Use of Resources score is derived from the assessments made by the auditor in the following areas.
- Financial Reporting (including the preparation of the accounts of the Council and the way these are presented to the public).
 - Financial management (including how the financial management is integrated with strategy to support council priorities).
 - Financial Standing (including the strength of the Council's financial position).
 - Internal Control (including how effectively the Council maintains proper stewardship and control of its finances).
 - Value for money (including an assessment of how well the Council balances the costs and quality of its services).
- 56 For the purposes of the CPA we have assessed the Council's arrangements for use of resources in these five areas as follows.

Table 3

| Element | Assessment |
|---|-------------------|
| Financial reporting | 3 out of 4 |
| Financial management | 3 out of 4 |
| Financial standing | 2 out of 4 |
| Internal control | 2 out of 4 |
| Value for money | 3 out of 4 |
| Overall assessment of the Audit Commission | 3 out of 4 |

(Note: 1=lowest, 4=highest)

- 57 The key issues arising from the audit, as reflected in the above judgements where appropriate, are as follows.

Financial reporting - audit of 2005/06 accounts

- 58 We assessed the Council's production of accounts as good and an improvement on the previous year. The accounts were produced by 30 June and were well supported with working papers. The Council also produced a good summary annual review of the accounts for the public. To achieve further improvement the accounts presented for audit should have no non-trivial errors and analytical review needs to be further developed.
- 59 We are required by professional standards to report to those charged with governance (in this case the Audit and Corporate Governance Committee) certain matters before we give an opinion on the financial statements. We reported four matters.
- There was difficulty in reconciling end of year balances with the PCT. There have been protracted delays in the PCT settling invoices with the Council. In September the Council was owed over £1 million by the PCT in relation to pooled budget contributions.
 - The valuation of Hillside intermediate Care Centre.
 - Two balance sheet errors which the Council subsequently corrected for in relation to long term loans and tangible assets.
 - Governance arrangements around a severance payment made in 2005/06. These have subsequently been revised.

Financial management

- 60 Our overall conclusion on financial management is that there are good arrangements in place but these now need to be fully embedded.
- 61 The Council has made very good progress over the last year in improving the quality and reliability of financial management arrangements particularly in adult social care. Particularly significant was the production of a robust Medium Term Financial Plan which is focussed on the achievement of the Council's objectives. The Council need to continue this improvement and fully embed the new financial management arrangements. We also note that training is being developed for Members and officers.
- 62 We also considered how the Council manages its asset base. The Council demonstrates some good practice in this area. The Council is taking action to improve the capacity of the asset management and property services team and to recruit a permanent head of this service. This is important given the level of input required in key areas such as the reconsideration of the Council's Accommodation strategy.

Financial standing

- 63 We concluded that the Council's financial standing meets the minimum requirements for the Use of Resources assessment.
- 64 Achieving financial balance is an important element of financial standing and historically the Council has been successful at this. Good financial standing is also about effectively managing activities and their associated budgets to avoid significant under-spending and the non-achievement of objectives. It is also about setting aside prudent but not excessive levels of reserves in relation to risks. For the last three years the Council has started the year forecasting the need to use approximately £3m of its general reserve. However, due to large unplanned under-spending within a number of departments a contribution has been made to reserves of between £3 and 4m. Capital reserves have remained static at approximately £20m.
- 65 We have seen significant improvements in this financial year. Until recently the Council has had high levels of general reserves for which there was no clear strategy on how they would be used. As part of the production of the medium term financial plan, revenue reserves were reviewed and significant amounts of reserves were earmarked against specific risks. Further improvement is still needed, including a reappraisal of the level of reserves that the Council should now hold.
- 66 The Council's financial position reported in the 2005/06 accounts shows revenue balances (earmarked and general) of £28.4m and a net under spend of £4.1m against budget. Much of this under-spending and the resultant increase in the level of balances was due to the operation of the Council's previous committed expenditure rules and carry over rules. The Council continues to work to a target of £3.0m for unallocated balances. The Council has revised these arrangements for carrying forward under-spends. There were overspends in two areas of Adult and Community Services. Adult Social Care overspent by £828k and there was an overspending of £593k on homelessness. These overspends were mitigated by an under-spending on community services of £430k. The planned overspend on Adult and Community Services in 2006/07 has been reduced by concerted action from £3.6 million to £1 million. The most recent forecasts of the Council show a significant under-spend against the 2006/07 budget of around £2.5 million.
- 67 Schools balances were £8.7m at the end of 2005/06 and although this is a small drop from the previous year, it is recognised that this level of balances is high. The Council is seeking to reduce this.
- 68 The Council's pensions liability (the amount liabilities exceeded assets) at the 31 March 2006 was £100m. Though a small fall from 2005, the level of this deficit is a cause for concern as the Council is not currently in a position to meet its future pension liabilities for its workforce.
- 69 The Medium Term Financial Plan identifies very significant savings deriving from the Herefordshire Connects transformation programme which is discussed later in this Letter. It will be vital that these savings are robustly monitored.

Systems of internal financial control

- 70 The Council's systems of internal control meet the minimum requirements for the Use of Resources assessment.
- 71 There have been significant improvements this year in risk management arrangements. The Council has put in place a risk register which assigns key individuals to risk. The register is actively managed as can be seen from the movement of the waste disposal risk into the corporate log. Champions have been put in place to drive risk forward and Members have been trained. However there is still scope for improvement. The Council now needs to demonstrate that it actively manages risk and there are outputs from that management. Officers need to be trained in risk awareness and the Council need to demonstrate that they have adequately considered partnerships in their risk assessments.
- 72 There have also been significant improvements in the internal control arrangements of the Council. The Audit and Corporate Governance Committee has been in operation for over 12 months, having had five meetings and has been improving with each meeting. The Committee now provides a focus for audit reports and governance issues, giving these a greater profile. It also has started to track progress on previous internal and external audit reports, an area which is developing. The Statement of Internal Control (SIC) is reviewed by the Audit Committee and there is much wider involvement in the process than previously. Issues raised during the 2005/06 audit are being or have been addressed. To improve further, the elements that have been put in place over the last year need to embed. The assurance framework needs to embed and the links between the Council's objectives and risks could be clearer. Reconciliations of key feeder systems need to occur monthly. Partnership arrangements need to be developed with standing orders showing how good governance and partnerships relate.
- 73 Probity and propriety arrangements have not progressed in the same way as other parts of this assessment. The process in relation to gifts and hospitality is being strengthened following our review. The whistle blowing policy has not been communicated to those who contract with the Council. The Council has been proactive in trying to raise awareness concerning ethical behaviour but it also needs to raise awareness of whistle blowing procedures and the anti fraud and corruption policy. This can be done by providing leaflets and placing posters where they would be seen and giving presentations to staff.
- 74 We carried out a survey of Members and Senior Officers to assess the adequacy of your ethical governance arrangements. The results showed a reasonable level of awareness and in most instances the survey results were favourable. There are some areas where the Council will need to take some action.
- More improved training is required, specifically around understanding of what the Standards Board is and when issues should be reported and a more informed knowledge of Statutory Acts which affect the Council.
 - The communicating of your high ethical standards to the General Public needs improvement.

- The work of the Standards Committee was not well known amongst respondents.
- Communicating the whereabouts of public documents to the Public could be improved upon.

75 We plan to assist the Council in developing these arrangements after the forthcoming elections by delivering training to officers and members.

Value for money

76 We considered both the Council's achievement of value for money and the arrangements to manage and improve value for money. Overall we concluded that both good achievement and good arrangements are demonstrated.

77 Overall spend on services is below average when compared with similar councils. Service outcomes in some areas are good and some improvements have been achieved (eg speed of processing planning applications), however the Council has also seen a decline in performance in some significant areas. The capital programme is linked to priorities, and is reasonably well managed. In broad terms, the Council still achieves a lot for its level of resourcing.

78 The Council's understanding of its cost pressures is improving, with a more robust and rigorous approach to medium term planning. There is a more robust approach to integrating service and resource planning. Areas of overspending are identified and a range of steps are being taken to address them. The key area is Adult Social Care which has significant projected overspends and will present a continuing challenge over the medium term. There is a better grasp on costs and benchmarking information in some services, but this is still not consistent across all service areas. Corporate approaches to procurement are still not well developed.

79 Arrangements for challenging and driving better value for money (VFM) and more efficient ways of working are improving, but many of these improvements are still at an early stage and have yet to show their impact. For example, the Council believes the Herefordshire Connects programme to have the potential to deliver significant improvements in both customer service and cash-releasing efficiencies. This programme, and the more robust approaches to medium term planning, is already having an impact on the organisation's culture. However, a VFM culture is still not well developed or embedded across all service areas. A consistent pattern of under-spending in most service areas indicates that there is still scope in service budgets to drive further efficiencies, and the lack of targets in a significant number of 2005/06 performance indicators meant that the Council's capacity to assess improved VFM was weakened. There is room for improvement in the challenge provided by Scrutiny.

- 80** There is a lack of straightforward and transparent accounting for how well services are doing in their delivery of value for money. It is not always clear from service plans and performance reports how improved value for money has been achieved. The Council has set itself challenging targets for efficiency gains, but it does not always have assurance that non-cashable efficiency gains are being robustly stated.

Other work

Waste management

81 The Council continues, together with Worcestershire County Council, to seek to reach an agreement with its PFI partner on arrangements for delivering the recycling requirements of the contract. It is disappointing that progress has been slow and the implementation of national recycling targets and penalties mean that there is an urgent need to resolve this issue.

82 We noted in our 2003/04 letter that:

‘Until the discussions with the contractor are finally concluded, there remains a risk that the contract could terminate. Contract termination could have a significant impact on the financial standing of the Councils, because:

- termination clauses in the original contract will require the Councils to repay the contractors shareholder equity in exchange for bringing waste management assets and facilities back in-house;
- the Councils are likely to have to enter into a new contract in order to achieve the objectives of the Waste Management Strategy. Re-procurement costs are likely to be significant and the Councils would be unlikely to secure the level of government PFI funding that was made available for the existing contract; and
- the inherent delay in putting new contract arrangements in place would expose both councils to potential future financial penalties under the Waste Emissions and Trading Act for failing to meet landfill diversion targets.

Members need to be mindful of these significant financial risks in particular, in considering the Council’s medium term financial strategy’.

83 This continues to be our view. Members should also be aware of the financial and environmental risks that the recycling arrangements present before they are approved.

Herefordshire Connects Programme

84 Herefordshire Connects is a fundamental part of the Council transformation plan. It is expected to cost over £25 million over five years and is currently at the procurement phase. Due to the scale of this commitment we carried out a very short overview whilst the project was progressing.

- 85 Based on the limited work undertaken, we found several strengths in the approach taken by the Council including project management and the procurement approach. We have raised several important issues which need to be considered by Members at this stage. These include the following.
- Extent to which the contract will deal with proposed Public Service Trust.
 - The need for a risk assessment for the contract when it goes live.
 - The lack of an options appraisal.
 - The capacity of staff to deal with work needed now such as a benefits realisation and subsequently in managing the contract.
 - The extent to which the contract specification has limited the choice of a technical solution.
- 86 We are currently discussing our draft report with your officers.

Grant claims

- 87 In accordance with Strategic Regulation, the Audit Commission has continued with a more risk-based approach to the certification of grant claims. We have reduced our audit of these claims but our ability to reduce further depends on the adequacy of the Council's control environment.
- 88 The Council's arrangements for managing and quality assuring grant claims submitted for audit has improved in the past year partly as a result of a new protocol and setting up a grant claims co-ordinator. To help improve arrangements further the Council needs to be more proactive in chasing departments where claims are outstanding.

Conclusion

- 89 This letter has been discussed and agreed with the Chief Executive and Director of Resources and presented at the Cabinet.
- 90 The Council has taken a positive and constructive approach to our audit and inspection I would like to take this opportunity to express my appreciation for the Council's assistance and co-operation.

Availability of this letter

- 91 This letter will be published on the Audit Commission's website at www.audit-commission.gov.uk, and also on the Council's website.

Elizabeth Cave

District Auditor and Relationship Manager