

Annual Governance Report

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# Annual Governance Report

London Borough of Lewisham

Audit 2006/07

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- any third party.

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## Purpose of this document

- 1 In accordance with the Audit Commission's Code of Audit Practice (the Code), this report provides a summary of the work we have carried out during our 2006/07 audit of accounts, the conclusions we have reached and the recommendations we have made to discharge our statutory audit responsibilities to those charged with governance (in this case the Audit Panel and the Urgency Sub Committee of the Full Council) at the time they are considering the financial statements.
- 2 In preparing our report, the Code requires us to comply with the requirements of International Standards on Auditing (United Kingdom & Ireland) – ISA (UK&I) - 260 'Communication of Audit Matters to Those Charged With Governance', by reporting to you matters relating to the audit of the financial statements. Other auditing standards require us to communicate with you in other specific circumstances including:
  - where we suspect or detect fraud;
  - where there is an inconsistency between the financial statements and other information in documents containing the financial statements; and
  - non-compliance with legislative or regulatory requirements and related authorities.
- 3 We are also required to communicate to you the Audit Commission's requirements in respect of independence and objectivity, and these are set out at Appendix 2.
- 4 This report has been prepared for presentation to the Audit Panel on 20 September 2007. Members are invited to:
  - consider the matters raised in the report before the financial statements are approved;
  - approve the representation letter on behalf of the Council and those charged with governance before we issue our opinion; and
  - consider amending the financial statements for unadjusted misstatements, significant qualitative aspects of financial reporting and any recommendations for improvement in the action plan.
- 5 Our work during the year was performed in line with the plan that was presented to the Public Accounts Committee on 30 May 2006. We have issued separate reports during the year having completed specific aspects of our programme, which are listed in Appendix 3.

## Key messages

- 6 Our work on the financial statements is substantially complete although there are still outstanding issues to be resolved. In particular, our work on the St John's loan guarantee has yet to be concluded. Should any further matters arise in concluding the outstanding work that need to be reported, we will raise them with the Chair of the Audit Panel and the Chair of the Council. Subject to the satisfactory conclusion of the outstanding issues we propose issuing an unqualified audit opinion on 26 September (a draft report is attached at Appendix 4).
- 7 In our view, the financial statements of the pension fund do present fairly the financial transactions of the pension fund.
- 8 In our view, the Statement on Internal Control (SIC) has been prepared in accordance with proper practice specified by CIPFA and is consistent with the findings from our audit.
- 9 Our work on the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources is now complete. We propose issuing a qualified conclusion on the use of resources on 26 September (a draft report is attached at Appendix 4). We draw members attention to the following recommendation.

### **Recommendation**

*R1 Maintain current focus on internal audit and ensure that the Council's internal audit function operates in accordance with the CIPFA Code of Practice for Internal Audit in Local Government.*

## Audit status

- 10 At the date of issue of this report our detailed audit is substantially complete.
- 11 The Council has taken a positive and constructive approach to our audit and we would like to take this opportunity to express our appreciation for the Council's assistance and co-operation.

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## Accounts and Statement on Internal Control

- 12 Our work on the financial statements is substantially complete although audit work on accounting for the loan guarantee to Hyde Housing for the St John's development is on-going.
- 13 Auditors are required to obtain written confirmation of certain representations from management and those charged with governance before an audit report is issued, such as acknowledgement of responsibility for the fair presentation of the financial statements in accordance with the applicable financial reporting framework and responsibility for the design and implementation of internal control to prevent and detect error.
- 14 The auditor should also obtain written representations from management on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist.
- 15 The final recommended draft of the letter of representation has been attached as Appendix 5.

### Unadjusted misstatements

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

### Adjustments to the financial statements

- 17 We are also required to bring to your attention misstatements that have already been corrected by management where we consider them relevant to your wider governance responsibilities.
- 18 The draft Statement of Accounts submitted for audit and approved by Council included a provision of £29.4 million relating to the transfer of properties at the St John's Housing estate. This resulted from the Council acting as a guarantor for the loans raised by Hyde Housing Association, as disclosed in previous years' accounts as a contingent liability.
- 19 We have been involved in discussions with officers and an in depth review of this matter. We recognise that the accounts were produced based on the best information at the time. However, subsequent information arose during the course of the audit that meant the provision was not required in the 2006/07 accounts. The accounts have therefore been appropriately adjusted to remove the provision from the balance sheet. This amendment does not have any impact on the Council's reported outturn position.

- 20** Capital expenditure with a value of £2.6 million relating to the Silwood development was incorrectly classified as a fixed asset addition in the Council's balance sheet. However, the asset did not belong to the Council and the accounts were amended to record the £2.6 million as a deferred charge on the face of the Housing Revenue Account Income and Expenditure account. There is no impact on the HRA balance as deferred charges are required by statute to be excluded from the movement on the HRA Balance for the year.
- 21** Whilst we consider the amount involved is not material to the Council's balance sheet and there is no impact on the HRA balance in the balance sheet, this represents a significant adjustment in the HRA Income and Expenditure account and therefore we bring it to your attention.

## Accounting practices

- 22** We are also required to report to you our view on the qualitative aspects of the Council's accounting practices and financial reporting and have set out below our observations on key issues affecting the Council.
- 23** The Council provided a comprehensive statement of accounts and working papers for audit in accordance with the agreed timetable. The accounts prepared were of a high standard and officers generally responded promptly to audit queries and requests for further information. Over the past few years we have seen a continued marked improvement in the quality of the accounts and the accompanying working papers.
- 24** The Audit Commission's approach for 2006/07 accounts has required an enhanced focus on audit testing of the existence and ownership of fixed assets. As part of our audit we tested a sample of fixed assets back to ownership documentation. The Council was unable to provide supporting documentation for one of the 22 assets selected for testing. Whilst this indicates a system weakness, we recognise that this asset has been in the Council's accounts for many years and the documentation may have been misplaced. Officers are aware of the issue and are looking to locate the missing documentation.

## Systems of internal control

- 25** As part of our audit, we consider the systems of accounting and financial control and report to you any material weaknesses identified. We have no significant issues that we wish to bring to your attention.
- 26** We have not provided a comprehensive statement of all weaknesses which may exist in internal control or of all improvements which may be made, but have addressed only those matters which have come to our attention as a result of the audit procedures we have performed.
- 27** We have also reviewed whether the SIC has been prepared in accordance with proper practice specified by CIPFA and is consistent with the findings from our audit. There are no matters arising.



## Use of resources

### Work performed

- 28** The Code requires us to reach a conclusion on whether we are satisfied that the Council has proper arrangements in place for securing economy, efficiency and effectiveness in its use of resources – the value for money conclusion. In meeting this responsibility, we review evidence that is relevant to the Council's corporate performance management and financial management arrangements across a range of criteria specified by the Audit Commission. Our work to support our conclusion comprised the following elements:
- use of resources assessment;
  - data quality work; and
  - the best value performance plan.
- 29** Details of our conclusion for each of the criteria specified by the Audit Commission are set out in Appendix 6. We have assessed Code Criteria 5, 'the body has put in place arrangements to maintain a sound system of internal control' as not adequate. Within internal control, one of the issues we consider is whether there is an internal audit function that operates in accordance with the CIPFA Code of Practice for Internal Audit in Local Government.
- 30** Our concerns about the Council's Internal Audit section have been well documented over the past few years and have been regularly reported to and discussed by the Public Accounts Select Committee and more recently the Audit Panel. We reviewed Internal Audit in early 2007 and reported to the Public Accounts Select Committee on 2 May that much progress had been made, especially in the second half of the year. However, assessing the year as a whole we concluded that Internal Audit was still not fully compliant with the CIPFA Code. We were, at that time, confident that with a continued improvement during 2007/08, there was every indication that Internal Audit will be able to gain a 'compliant with the Code' assessment in 2007/08.
- 31** At the request of the Council's Internal Control Board we reviewed a sample of Internal Audit files in August 2007. It was intended that this work would help provide assurance to us and the Council's Executive Director of Resources that the anticipated improvements were materialising.
- 32** We reviewed a sample of six files and consider that three had weaknesses relating to the management of audit assignments, the quality of audit work and quality assurance procedures. We therefore concluded that we consider that Internal Audit still falls short of the required CIPFA Code in several areas at this time but we do note that they have made improvements.

- 33 We recognise that there are some strong and innovative elements of internal control at Lewisham, for example, a challenging Internal Control Board. We also acknowledge that the Council recognises the weaknesses in its internal audit section and has disclosed this as a high risk issue in its Statement of Internal Control.
- 34 However, It is our view that internal audit is fundamental in maintaining a sound system of internal control and therefore propose to issue a report including a value for money conclusion qualified on the grounds of internal control.
- 35 We recognise the Council's disappointment in light of the investment that it has made in trying to improve the internal audit function. This investment has included both additional resources and senior staff input in addressing the concerns we have raised. In particular, we commend the Executive Director of Resources personal commitment in trying to improve this service and recognise that the problems are due to basic practices not being applied consistently within the Internal Audit section.

## Use of resources assessment

- 36 We are currently finalising our report arising from our use of resources assessment. When finalised, we will discuss this with the relevant officers and present this report to the Audit Panel.

## Data quality work

- 37 We are currently finalising our data quality review and will report our findings to the relevant officers and present this report to the Audit Panel.

## Best value performance plan

- 38 Our work in respect of the Council's 2006/07 Best Value Performance Plan (BVPP) was reported in the 2006 annual audit and inspection letter. No recommendations were made to the Audit Commission or the Secretary of State.

## Audit fee update

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

	<b>Plan 2006/07 (£'000)</b>	<b>Actual 2006/07</b>
Financial statements and Statement on Internal Control	296	296
Use of Resources	116	116
Total Audit Fees	412	412
Grants certification work	160	TBC

- 40 The analysis above shows that our audit fee has been contained within the totals you have already agreed.
- 41 Our grants certification work for 2006/07 is ongoing. The outturn of fees for this work will be reported in the Annual Audit and Inspection Letter.
- 42 The outturn on inspection fees will be reported in the annual audit and inspection letter.

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## Appendix 1 – Action plan

Page	Recommendation	Priority 1 = Low 2 = Medium 3 = High	Responsibility	Agreed	Comments	Anticipated Implementation Date
5	R1 Maintain current focus on internal audit and ensure that the Council's internal audit function operates in accordance with the CIPFA Code of Practice for Internal Audit in Local Government.	3	Executive Director of Resources	Yes	We will continue to maintain focus on this with a view to obtaining compliance with the CIPFA code.	31 March 2008

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

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

## Appendix 3 – Audit reports issued

Planned output	Planned date of issue	Actual date of issue	Addressee
Audit plan	April 2006	May 2006	Public Accounts Committee
Opinion audit plan	June 2006	July 2006	Executive Director for Resources
Annual governance report	September 2007	September 2007	Audit Panel, Council Urgency Sub Committee
Opinion on financial statements	September 2007	September 2007	Audit Panel, Council Urgency Sub Committee
Use of resources conclusion	September 2007	September 2007	Audit Panel, Council Urgency Sub Committee
Final accounts memorandum	October 2007		Executive Director for Resources
BVPP report	December 2006	December 2006	Chief Executive and reported in Annual Audit and Inspection letter in early 2007
Data quality report	December 2007		Audit Panel
Performance reports	On-going	On-going	Audit Panel
Annual audit letter	March 2008		Audit Panel

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

## **Independent auditor’s report to the Members of Lewisham Council**

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

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

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

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

The Chief Finance Officer’s responsibilities for preparing the financial statements, including the pension fund accounts, in accordance with applicable laws and regulations and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2007 are set out in the Statement of Responsibilities.

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

I report to you my opinion as to whether the financial statements and the pension fund accounts present fairly, in accordance with applicable laws and regulations and the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2007:

- the financial position of the Council and its income and expenditure for the year; and

- the financial transactions of its pension fund during the year and the amount and disposition of the fund's assets and liabilities, other than liabilities to pay pensions and other benefits after the end of the scheme year.

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

I read other information published with the financial statements, and consider whether it is consistent with the audited financial statements. This other information comprises only the Explanatory Foreword. I consider the implications for my report if I become aware of any apparent misstatements or material inconsistencies with the financial statements. My responsibilities do not extend to any other information.

### **Basis of audit opinion**

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

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

### **Opinion**

In my opinion:

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



The pension fund accounts present fairly, in accordance with the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom 2006, the financial transactions of the Pension Fund during the year ended 31 March 07, and the amount and disposition of the fund's assets and liabilities as at 31 March 07, other than liabilities to pay pensions and other benefits after the end of the scheme year.

Signed

Philip Johnstone  
District Auditor  
Audit Commission  
1st Floor  
Millbank Tower  
Millbank  
London SW1P 4HQ

September 2007

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

### **Council's Responsibilities**

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

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

### **Auditor's Responsibilities**

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

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

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

### **Conclusion**

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

## **Best Value Performance Plan**

I issued my statutory report on the audit of the Council's best value performance plan for the financial year 2006/07 on 20 December 2006. I did not identify any matters to be reported to the Council and did not make any recommendations on procedures in relation to the plan.

## **Certificate**

The audit cannot be formally concluded and an audit certificate issued until I have completed my consideration of matters brought to my attention by local authority electors. I am satisfied that these matters do not have a material effect on the financial statements.

Signed

Philip Johnstone  
District Auditor  
Audit Commission  
1st Floor  
Millbank Tower  
Millbank  
London SW1P 4HQ

September 2007

## Appendix 5 – Management representation letter

To: Philip Johnstone  
Audit Commission  
1st Floor Millbank Tower  
Millbank  
London  
SW1 4HQ

### London Borough of Lewisham - Audit for the year ended 31 March 2007

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Lewisham Council, the following representations given to you in connection with your audit of the council's financial statements and the pension fund accounts for the year ended 31 March 2007.

I acknowledge my responsibility under the relevant statutory authorities for preparing the financial statements which present fairly and for making accurate representations to you.

I confirm that there are no uncorrected financial statements misstatements, of which we are aware, which would have a material effect on the accounts, either individually or in aggregate.

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

### Representations

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

### Supporting records

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

## **Ownership Testing**

For the three assets in your sample where you were unable to obtain appropriate documentation to support ownership, I can confirm that to the best of my knowledge, these assets belong to Lewisham Council.

## **Related party transactions**

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

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

## **Contingent liabilities**

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

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements; and
- no financial guarantees have been given to third parties.

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

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

## **Irregularities**

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

There have been no:

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

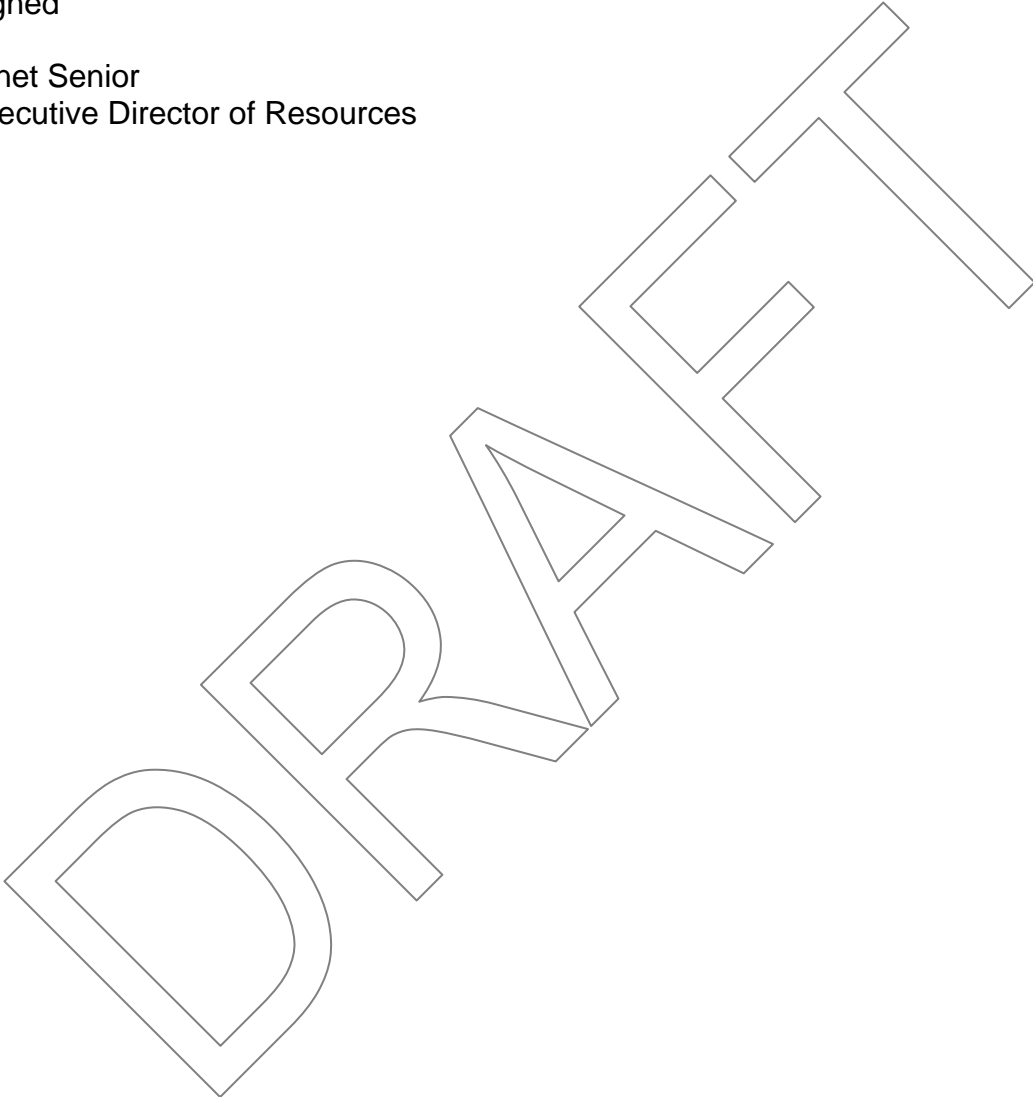
**Post balance sheet events**

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

Signed on behalf of the London Borough of Lewisham

Signed

Janet Senior  
Executive Director of Resources



## Appendix 6 – Value for money conclusion

- 3 The Audit Commission has published, in accordance with the Code of Audit Practice, 12 criteria on which auditors are required to reach a conclusion on the adequacy of an audited body's arrangements for economy, efficiency and effectiveness in its use of resources.
- 4 The Code criteria are linked to the use of resources assessment (UoR) key lines of enquiry (KLoEs). A score of Level 2 or higher under the KLoEs will result in an assessment that the Council has adequate arrangements in place for the purposes of the Code criteria. The Code criteria and the linked KLoEs are show in the table below.

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

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6	The body has put in place arrangements to manage its significant business risks.	4.1	3	Adequate
7	The body has put in place arrangements to manage and improve value for money.	5.2	3	Adequate
8	The body has put in place a medium-term financial strategy, budgets and a capital programme that are soundly based and designed to deliver its strategic priorities.	2.1	3	Adequate
9	The body has put in place arrangements to ensure that its spending matches its available resources.	3.1	3	Adequate
10	The body has put in place arrangements for managing performance against budgets.	2.2	3	Adequate
11	The body has put in place arrangements for the management of its asset base.	2.3	3	Adequate
12	The body has put in place arrangements that are designed to promote and ensure probity and propriety in the conduct of its business.	4.3	4	Adequate

