Auditor’s Annual Report on Mid Devon District Council

2022/23

8 May 2024

Contents

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the National Audit Office (NAO) requires us to report to you our commentary relating to proper arrangements.

We report if significant matters have come to our attention. We are not required to consider, nor have we considered, whether all aspects of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

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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 for the purpose of completing our work under the NAO Code and related guidance. Our audit is not designed to test all arrangements in respect of value for money. However, where, as part of our testing, we identify significant weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all irregularities, or to include all possible improvements in arrangements 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.

Executive summary

Value for money arrangements and key recommendation(s)

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to consider whether the Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Auditors are required to report their commentary on the Council's arrangements under specified criteria and 2022/23 is the third year that we have reported our findings in this way. As part of our work, we considered whether there were any risks of significant weakness in the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources. Where we identify significant weaknesses in arrangements, we are required to make recommendations so that the Council may set out actions to make improvements. We set out our VFM risk assessment to the Council in our audit plan in June 2023. Our initial VFM conclusions for 2022/23 are summarised in the table overleaf, and include two key recommendations linked to significant weaknesses we identified in the Council's arrangements for that year.

We have completed our audit of your 2022-23 financial statements and issued our final audit findings report to the Council. This was presented to Audit Committee on 30 April 2024. This updated the position that was reported to the committee on 5 December 2023.

Following the Council's decision to close its arm's length company (3 Rivers Development Ltd) in August 2023, updated group and subsidiary accounts required preparation to reflect the realisable value of assets and liabilities of the company within the consolidated group accounts for Mid Devon District Council. This, coupled with some delays encountered in the receipt of outstanding working papers, informed our decision to pause the audit of the Council's financial statements in December 2023.

Our audit work recommenced in April 2024, following receipt of updated consolidated group accounts for Mid Devon District Council. We have now concluded the outstanding audit work and issued our audit report, including the audit certificate on 8 May 2024.

Further information on our audit of the financial statements is set out on pages 38 and 39.

We have now concluded our VFM assessment and this Annual Auditor's Report summarises the findings and conclusions reached. We have raised no further significant weaknesses to those reported in the interim Auditors Annual Report and have not identified the need to issue additional recommendations, including written recommendations to the Council under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014.

The key recommendations raised in the interim report remain in place and are set out on page 4 of this report.

Executive summary (continued)

Our interim assessment of the Council's value for money arrangements is summarised in the table below.

Other than in relation to the Council's management of 3 Rivers, we did not identify significant weaknesses in the Council's arrangements. Within the financial sustainability area we highlight the need for the Council to follow a clear timeline and plan for soft closure of the Company. We consider the Council could set out more clearly, in a way that can be tracked and monitored over time, a clear plan of savings and income generation activities to bridge its medium-term funding gaps. Our improvement recommendations in relation to Governance and Improving Economy, Efficiency and Effectiveness are designed to support the Council in continuing to refine existing arrangements.

We have identified two significant weaknesses in relation to the Council's management of its arm's length company, 3 Rivers Development limited (see page 5). These relate to the Council's oversight and discharge of its shareholder role; and to the way in which the debate around the Company's business plan was conducted. We raise a Key recommendation in relation to each identified significant weakness (see pages 8 and 9).

Criteria	2022/23 Risk assessment		2022/23 Auditor judgement on arrangements		2021/22 Auditor judgement on arrangements	Direction of travel
Financial sustainability	Significant risk identified in relation to financial sustainability	A	No significant weakness identified, but improvement recommendation made.	A	No significant weaknesses in arrangements identified, but improvement recommendations made	↔
Governance	Significant risk identified in relation to group governance	R	Significant weakness in arrangements identified in relation to the conduct of the debate around a business plan for 3 Rivers Development Limited and the subsequent impact on setting the 2023/24 budget. Key Recommendation made. One further improvement recommendation made.	A	No significant weaknesses in arrangements identified, but improvement recommendations made	↓
Improving economy, efficiency and effectiveness	No significant risks identified	R	Significant weakness in arrangements for managing 3 Rivers Development Limited, and a Key Recommendation made. One further improvement recommendation made.	A	No significant weaknesses in arrangements identified, but improvement recommendations made	↓

G	No significant weaknesses in arrangements identified or improvement recommendation made.
A	No significant weaknesses in arrangements identified, but improvement recommendations made.
R	Significant weaknesses in arrangements identified and key recommendations made.

Executive summary (continued)

Findings in relation the Council's management of 3 Rivers Development Limited in 2022/23

Background and Context

In 2017, Mid Devon District Council (the Council) established a company, 3 Rivers Development Limited (the Company) with the aim of developing housing to provide a financial return to the Council. During our 2021/22 review of the Council's VFM arrangements, carried out during January and February 2023, it became clear that the approval timeline for the Company's annual business plan had been significantly delayed. In issuing our report on the Council's Value for Money (VFM) arrangements covering the 2021/22 year, we noted these events and undertook to return to the issue in our review of the Council's arrangements covering 2022/23, when the events took place.

In September 2023, after considering on external specialist advice on the company's trading position and future prospects, the Council decided to "soft close" the Company. Soft closure will certainly result in a significant financial loss to the Council, which it currently estimates a gross loss of £9 million and a net loss of £6 million. The Council's quarter 2 financial monitoring report for 2023/24 indicated that the Council had, at that point, made a further £1.3 million of loans to 3 Rivers in 2023/24 and indicated that the net drawdown to completion was a [further] £2.7 million, giving a total of around £25m loaned to the Company. Set against this is a forecast £16 million returns from sales. The Council notes that this does not include interest receipts and recharges of c£3 million, which would set the net total loss to the Council of around £6 million. Either figure is a significant amount for a Council the size of Mid Devon District Council.

We identified two key, overarching significant weaknesses in the Council's arrangements in 2022/23. Within each of these headings are a number of issues that the Council will need to consider as it learns lessons from its experience with 3 Rivers. We set out our detailed findings in relation to the Council's management of 3 Rivers over pages 13 to 20, and our Key Recommendations on pages 8 and 9.

Assessment of the Council's arrangements

Improving economy, efficiency and effectiveness

Significant Weakness 1: The Council did not exercise its shareholder role effectively, contributing to the failure of its arm's length company and a significant financial loss. In particular, it did not maintain clear strategic direction for the Company, make effective and timely decisions to in a changing operating context, or ensure there was clear and effective strategic reporting on performance and risk.

In its 2017 business case, the Council set only one objective for the Company: a sustainable, positive financial return. By 2022/23, however, the Company was clearly not delivering against this objective. At an early stage, the Council assigned the Company a large regeneration site, which, while the initial business case included a profit, was later identified as a clear example of a site that would not have been taken on by an organisation whose primary purpose was to make a profit. There had also been "mission creep" by this stage, with statements of the Company's objectives in both its own and Council documentation increasingly referring to objectives related to housing supply, housing quality and regeneration, which were explicitly excluded as objectives in setting up the Company in 2017.

Executive summary (continued)

Further, in April 2023, changes to Public Works Loan Board criteria meant the Company would not (as had been expected) be able to develop sites outside the District. As the Company itself identified at the time, this further challenged its financial viability. Even without existing underperformance, a fundamental change in the operating context such as this should have triggered the Council to review promptly its overall business case for the Company, to establish if its objective (i.e. making a positive financial return) was still deliverable and, if so, whether an arm's length property development company remained the right vehicle to do so. The Council instead delayed any decision on the Company's future until a decision was made on its November 2022 business plan, resulting in a lack of clear direction.

Governance, including financial governance

Significant weakness 2: The Council conducted the debate around approval of the Company's 2022 business plan in a way that damaged the Council's reputation and meant the Council was not able to set its budget in a robust and timely manner.

Given the lack of clear direction, it can be understood that Members had queries about the Company's performance and the Council's oversight. It is reasonable to expect Members and Officers to have robust and constructive debate on this topic, given the financial, operational and reputational risks involved. As we have already reported in our 2021/22 Auditor's Annual report, the Council as a whole was unable to maintain the normal good relations that are essential to effective decision-making and governance. Disagreements over the Company's business case escalated and eventually, normal processes broke down, leading to public allegations of fraud and a breakdown in decision-making capacity. During February 2023, several members left the Cabinet, which was then not able to exercise its key decision-making functions, including setting the Council's annual budget. Ultimately, this led to the resignation of the Council Leader.

Adverse media reports highlighting the extent of disruption for the Council during this period will, inevitably, have adversely affected its reputation.

As a result of delays in decision-making and the ultimate rejection of the Company's business plans, as well as the disruption to normal decision-making processes, the Council had to delay setting its Budget until March 2023 as it had been unable to do so as planned in February. It also had to rely on an unplanned and significant one-off use of reserves to plug the £625,000 gap left by the removal of loan interest payments from the company. Although this amount was not sufficient in itself to challenge the Council's overall financial sustainability, it left the Council's forecast General Reserve substantially below its own £2 million recommended minimum level and substantially increased the Council's medium-term budget gap.

It is positive that the Council's Scrutiny Committee recently published its own lessons learned review into the Council's management of the Company, going back to its inception in 2017. We note this review also identifies a number of lessons and makes recommendations for the Council to consider in the event it again wishes to deliver its objectives through an arm's length company or similar organisation. The Council should ensure relevant lessons and recommendations from this report, as well as our Auditor's Annual Report, are implemented to ensure future debates around strategic decisions are conducted in a robust, but constructive manner.

Executive summary (continued)

Financial sustainability

We did not identify significant weaknesses in relation to the Council's arrangements for securing financial sustainability in 2022/23. The Council delivered a small overspend in 2022/23. In setting the 2023/24 budget, as previously set out, it had to rely on an unplanned and significant one-off use of reserves to plug the £625,000 gap left by the removal of loan interest payments from the company. Although this amount was not sufficient in itself to challenge the Council's overall financial sustainability, it left the Council's forecast General Reserve substantially below its own £2 million recommended minimum level and substantially increased the Council's medium-term budget gap.

The gap in the Council's medium term financial planning is made more acute by the removal of assumed payments from 3 Rivers. The Council needs to ensure there is a clear programme of savings, efficiencies and income generation measures to address this gap, that can be robustly monitored and tracked. We make an improvement recommendation in this area. We also note that at the time of undertaking our review, the Council's eventual financial loss is not yet clear and the impact on the Council's preparation of group and subsidiary accounts had contributed to us not being able to complete our audit of the Council's 2022/23 financial statements in a timely manner. The Council needs to follow a clear timeline to closure of 3 Rivers Development Limited, assess the ultimate scale of financial loss and adapt its financial plans accordingly, and to prepare group accounts on an appropriate basis for audit.

Governance

Other than with relation to the events surrounding 3 Rivers Development Limited, we did not identify significant weaknesses in the Council's governance arrangements. The Council generally maintained appropriate arrangements to govern standards and behaviours, and to make informed decisions. Neither the Council nor its internal auditors identified significant shortcomings in the Council's control environment. We raise an improvement recommendation related to positive assurance over the Council's compliance with key governance policies.

Improving economy, efficiency and effectiveness

Other than with relation to the events surrounding 3 Rivers Development Limited, we did not identify significant weaknesses in the Council's arrangements to improve economy, efficiency and effectiveness. The Council has improved its performance reporting to Cabinet, building on work it had started earlier in the 2023 calendar year. As set out under the financial sustainability heading, above, the Council's financial reporting would benefit from a more systematic delivery of savings and efficiency measures, though there are examples the Council can build on, such as the scrutiny of waste and recycling efficiency measures. We cover this area under our financial sustainability improvement recommendations.

Financial Statements opinion

We have completed our audit of your 2022-23 financial statements and issued our final audit findings report to the Council. This was presented to Audit Committee on 30 April 2024. This updated the position that was reported to the committee on 5 December 2023.

Following the Council's decision to close its arm's length company (3 Rivers Development Ltd) in August 2023, updated group and subsidiary accounts required preparation to reflect the realisable value of assets and liabilities of the company within the consolidated group accounts for Mid Devon District Council. This, coupled with some delays encountered in the receipt of outstanding working papers, informed our decision to pause the audit of the Council's financial statements in December 2023.

Our audit work recommenced in April 2024, following receipt of updated consolidated group accounts for Mid Devon District Council. We have now concluded the outstanding audit work and issued our audit report, including the audit certificate on 8 May 2024.

Our findings are set out in further detail on pages 38 and 39.

Key recommendations

Key Recommendation 1	The Council should learn lessons from the debate over 3 Rivers Development Limited's business plan and ensure future discussions around key strategic financial and operational decisions are conducted in a robust but constructive manner. This includes ensuring relevant actions and recommendations from internal and external reviews of its management of the Company, including this AAR report and the recent report of the Scrutiny Committee Working Group review, are monitored and implemented.
Identified significant weakness in arrangements	The Council conducted the debate around approval of the Company's 2022 Business Plan in a way that damaged the Council's reputation and meant the Council was not able to set its budget in a robust and timely manner.
Summary findings	Given the lack of clear direction, it can be understood that Members had queries about the Company's performance and the Council's oversight. It is reasonable to expect Members and Officers to have robust and constructive debate on this topic, given the financial, operational and reputational risks involved. However, disagreements over the approval of the Company's November 2022 business plan became protracted and the Council's processes did not effectively resolve disagreements. Eventually, normal processes broke down to the extent that Cabinet was then not able to exercise its key decision-making functions (including setting the budget) and adverse media reports.
Criteria impacted by the significant weakness	Financial sustainability; Governance; Improving economy, efficiency and effectiveness
Auditor judgement	Based on the work undertaken, we are not satisfied that the Council has proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources in 2022/23, in relation to its management of its arm's length company. We have therefore identified a significant weakness in these arrangements.
Management comments	All external recommendations from previous reviews of 3Rivers have been implemented. The 3Rivers soft closure timetable is agreed and progressing well and should transfer all assets back to the Council before the end of March 2024. The lessons learnt report has been considered and agreed by Scrutiny. Already delivered necessary savings to offset use of reserves in 2023/24 and balanced 2024/25 budget without the use of any reserves. Remaining write off of losses to be funded from underspend / reserves without any short-term implication on service delivery.

Progressing the actions management has identified to address the recommendations made will support the Council in addressing the weaknesses identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place.

The range of recommendation s that external auditors can make is explained in Appendix B.

Key recommendations

Key Recommendation 2	The Council needs to ensure it follows an action plan with a clear timeline and allocation of responsibilities for the Company's closure, and to work effectively to ensure the closure is conducted in a way that minimises its financial loss. The Council should also ensure its decisions are based on high quality expert advice as necessary. When working through this or any other significant partnerships, the Council should ensure both members and officers uphold effective political and management oversight of key partnerships and commercial entities. It must ensure it maintains a clear focus on the Council's objectives, ensures high quality reporting on performance and risk to inform key decisions, and acts promptly on information and significant changes of circumstances, that challenge the basis for establishing the partnership, supported by a clear exit strategy where necessary.		
Identified significant weakness in arrangements	The Council did not exercise its shareholder role effectively, contributing to the failure of its arm's length company and a significant financial loss. At the time of compiling this report, however, the exact scale of this loss was is not yet clear but it was expected to be significant.		
Summary findings	The Council did not maintain clear strategic direction for the Company, make effective and timely decisions on the Company's role in a changing operating context, or ensure there was clear and effective strategic reporting on Company performance and risk. We have seen a high level plan for the closure of the company but at the time of compiling this report this work was not complete.		
Criteria impacted by the significant weakness	Financial sustainability	Governance	Improving economy, efficiency and effectiveness
Auditor judgement	Based on the work undertaken, we are not satisfied that the Council has proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources in 2022/23, in relation to its management of its arm's length company. We have therefore identified a significant weakness in these arrangements.		
Management comments	Excluding 3Rivers, the council has no other significant partnerships. In respect of 3Rivers, a clear plan is in place and being followed that will ensure the soft closure of the company. 3Rivers financial losses clearly need to be reconciled against a backdrop of: Cost of Living Crisis Covid-19 (material and contract availability and prices) A challenging political environment Planning Committee decisions Major contractor failure Government geographical restrictions.		

Progressing the actions management has identified to address the recommendations made will support the Council in addressing the weaknesses identified from our work. We consider that the timescales provided by management are appropriate and encourage the
Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place.

Use of auditor's powers

We bring the following matters to your attention:

	2022/23
Statutory recommendations Under Schedule 7 of the Local Audit and Accountability Act 2014, auditors can make written recommendations to the audited body which need to be considered by the body and responded to publicly.	We do not make any written recommendations under Schedule 7 of the Local Audit and Accountability Act 2014 within this interim report and will consider whether this would be appropriate in issuing our final report in due course.
Public Interest Report Under Schedule 7 of the Local Audit and Accountability Act 2014, auditors have the power to make a report if they consider a matter is sufficiently important to be brought to the attention of the audited body or the public as a matter of urgency, including matters which may already be known to the public, but where it is in the public interest for the auditor to publish their independent view.	We did not issue a public interest report.
Application to the Court Under Section 28 of the Local Audit and Accountability Act 2014, if auditors think that an item of account is contrary to law, they may apply to the court for a declaration to that effect.	We did not make an application to the Court.
Advisory notice Under Section 29 of the Local Audit and Accountability Act 2014, auditors may issue an advisory notice if the auditor thinks that the authority or an officer of the authority: • is about to make or has made a decision which involves or would involve the authority incurring unlawful expenditure, • is about to take or has begun to take a course of action which, if followed to its conclusion, would be unlawful and likely to cause a loss or deficiency, or • is about to enter an item of account, the entry of which is unlawful.	We did not issue any advisory notices.
Judicial review Under Section 31 of the Local Audit and Accountability Act 2014, auditors may make an application for judicial review of a decision of an authority, or of a failure by an authority to act, which it is reasonable to believe would have an effect on the accounts of that body.	We did not make an application for judicial review.

Securing economy, efficiency and effectiveness in the Council's use of resources

All councils are responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness from their resources. This includes taking properly informed decisions and managing key operational and financial risks so that they can deliver their objectives and safeguard public money. The Council's responsibilities are set out in Appendix A.

Councils report on their arrangements, and the effectiveness of these arrangements as part of their annual governance statement.

Under the Local Audit and Accountability Act 2014, we are required to be satisfied whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

The National Audit Office's Auditor Guidance Note (AGN) 03, requires us to assess arrangements under three areas:

Financial sustainability

Arrangements for ensuring the Council can continue to deliver services. This includes planning resources to ensure adequate finances and maintain sustainable levels of spending over the medium term
(3-5 years).

Governance

Arrangements for ensuring that the Council makes appropriate decisions in the right way. This includes arrangements for budget setting and management, risk management, and ensuring the Council makes decisions based on appropriate information.

Improving economy, efficiency and effectiveness

Arrangements for improving the way the Council delivers its services. This includes arrangements for understanding costs and delivering efficiencies and improving outcomes for service users.

As the Council's management of its arm's length company is relevant to all three areas, we report our assessment of arrangements in this area separately over pages 13 to 20. Our further findings on the Council's arrangements in each of the three areas above, is set out on pages 21 to 37.

In addition to our financial statements audit work, we perform a range of procedures to inform our value for money commentary:

- Review of Council, Cabinet and committee reports
- Regular meetings with senior officers
- Interviews with other members and management
- Attendance at Audit Committee
- Considering the work of internal audit
- Reviewing reports from third parties where appropriate
- Reviewing the Council's Annual Governance Statement and other publications

The current Local Government landscape

Context

Mid Devon District Council serves a population of around 83,000 (as at the 2021 Census) across a number of towns, including the area's largest town, Tiverton and surrounding rural areas. The Council currently operates a 'leader and Cabinet' model and has been under Liberal Democrat majority control since the 2023 local government elections, having previous been "no overall control".

The Council, along with the wider local government sector in England continues to face significant challenges. These include a high level of uncertainty over future levels of government funding, alongside delays to the Government's plans for reform of the local government finance system, impacting on medium-term financial planning. The 2022/23 financial year was also a time of significant inflation – the UK inflation rate was 7.8% in April 2022, rising to a 41-year high of 11.1% in October 2022, then reducing to 10.1% in March 2023. Inflation put pressure on councils' revenue and capital expenditure, and the associated cost of living crisis has affected local communities and businesses, leading to an increase in demand for council services. Increases in the costs of finance, labour and materials are relevant to the Council's own services and those of its arm's length property development company, 3 Rivers Development Limited. Areas of council income such as car parking and the collection rates of council tax, business rates and rents have also been affected. This follows a significant period of funding reductions by Government (2012 to 2017) and the impacts of Brexit and the COVID-19 pandemic which, for example, have contributed to workforce shortages in a number of council service areas, as well creating supply chain fragility risks.

The local government finance settlement for 2023/24 was better than many in the sector anticipated demonstrating an understanding by Government of the financial challenges being faced by the sector. However, the Local Government Association, in July 2023, estimated that the costs to councils of delivering their services will exceed their core funding by £2bn in 2023/24 and by £900m in 2024/25. This includes underlying cost pressures that pre-date and have been increased by the pandemic, such as demographic pressures increasing the demand for services such as social care and homelessness.

Over the past decade many councils have sought to increase commercial activity as a way to generate new sources of income which has increased the nature of financial risk, as well as the need to ensure there is appropriate skills and capacity in place to manage such activities. Mid Devon District Council in 2017 set up 3 Rivers Development Limited, the Council's management of which in 2022/23 is the subject of detailed review in this report. Local government is coming under an increased spotlight in terms of how the sector responds to these external challenges, including the Government establishing the Office for Local Government (Oflog) and there has been an increase in the number of councils who have laid a Section 114 Notice, or are commenting on the likelihood of such an action, as well as continued Government intervention at a number of councils.

There has also been an increase in the use of auditors using their statutory powers, such as public interest reporting and statutory recommendations. The use of such auditor powers typically derive from Value for Money audit work, where weaknesses in arrangements have been identified. These include:

- a failure to understand and manage the risks associated with commercial investments and council owned companies
- a failure to address and resolve relationship difficulties between senior officers and members
- significant challenges associated with financial capability and capacity
- a lack of compliance with procurement and contract management processes and procedures
- ineffective leadership and decision-making.

Value for Money audit has an important role in providing assurance and supporting improvement in the sector.

The Council's management of 3 Rivers development limited

Background and context

In 2017, Mid Devon District Council (the Council) established a company, 3 Rivers Development Limited (the Company) with the broad aims of developing housing and delivering a financial return to the Council. The Council has funded the company by making it commercial loans, on which the Company has paid interest back to the Council. It was also intended that the Company would also pay an annual dividend once it made a profit, though in the event the Company never achieved a sufficient level of profit to pay this dividend.

During our 2021/22 review of VFM arrangements, carried out during January and February 2023, it became clear that: the usual approval timeline for the Company's annual business plan had been significantly delayed, impacting the Council's budget-setting process; and that relationships between members and between members and officers had become increasingly strained, leading to adverse media reports, public allegations of fraud and a breakdown in decision-making to the extent that, during February 2023, Cabinet was not able to exercise its key decision-making functions (including setting the budget).

Scope

Our role in assessing the Council's arrangements for securing value for money are set out in the Local Audit and Accountability Act 2014 and the 2020 Code of Audit Practice. The subject matter of auditors' work under the Code is a local body's arrangements "to secure economy, efficiency and effectiveness in its use of resources".

Our review of the Council's VFM arrangements covering the 2020/21 financial year (reported in March 2022) found that the Council had improved governance arrangements to address a number of weaknesses identified in two external reviews and a report of the Devon Audit Partnership, as well as our own reports covering the 2018/19 and 2019/20 financial years. Therefore, in this report, we have undertaken sufficient work to identify whether there was evidence of significant weaknesses in the Council's arrangements in regard to financial sustainability, governance, and improving economy, efficiency and effectiveness in the 2022/23 financial year.

We did not re-perform audits or assess reviews undertaken by other bodies that have already reported on either the Company's performance or the Council's management of it, including those of the Devon Audit Partnership or the various external reviews undertaken in earlier years and in 2023. We do, however, consider the Council's use of and response to such reviews, where relevant. Where we refer to events in prior years, this is because we consider them relevant to the events that occurred in 2022/23; for example, because a weakness in arrangements in setting up the company a contributed to issues occurring in 2022/23.

Key Findings

Establishing and maintaining focus on the Company's core objectives

The Council's 2017 business case set out very clearly that the Company's sole purpose was to deliver a financial return to the Council. It set a need to "*create revenue streams that can be used to fund the standard of front line services that this Council believes are vital for its residents*" and that "*it should be clearly understood that this company is not intended as a mechanism to deliver affordable housing; the company is being formed to create revenue which will be reinvested into the Council.*"

Later articulations of the Company's objectives reflect a significant degree of "mission creep" from this initial objective. We identified three different articulations of the Company's objectives within 2022/23 and a further one in 2023/24, all of which included aims such as delivering economic regeneration and increasing the level and quality of housing within Mid Devon. A well-reported example of this is the Company's largest development site at St George's Court. The Company noted in its 2021 business plan, endorsed by Cabinet in November 2021 that, prior to setting up the Company, the Council intended to regenerate this area of Tiverton and recognised it would need to provide some financial support to do so. An external review commissioned by the Council meanwhile described the site as "*one which no commercially minded property developer would have taken on in normal circumstance*". In August 2023, the Council's advisors reported that the Council was at that point currently anticipating a £3.94m loss on this site, the scale of which outweighed any profit expected from the Company's other, smaller sites.

The Council's management of 3 Rivers Development Ltd.

Figure 1 – examples of the Company's statement of objectives in 2022/23 and 2023/24

Business Plan objectives reported to Cabinet in August 2022:	• 3 Rivers Developments Limited's primary objective is to generate future returns in order to grow the business and to recycle monies made back to the Council to mitigate some of the cuts in Government funding.
Business Plan objectives referred to in a report to Cabinet report 6th September 2022:	• Generate future returns in order to grow the business, • Recycle monies made back to the Council to mitigate some of the cuts in Government funding, • Increase the level and quality of housing units within the district, • Look to help regenerate sites/areas in need of assistance.
Business plan objectives referred to in a Cabinet report, 2nd November 2022:	• Housing to meet Local Authority needs, • Economic regeneration by building private and social homes, • Commercial lets for sale or rent, • Other social economic activities.
Business plan objectives referred to in a report to Cabinet 18th January 2023	• Increase level and quality of housing units within the district, • Look to help regenerate sites/areas in need of assistance, • Generate future returns in order to grow the business, • Recycle monies made back to the Council to mitigate some of the cuts in government funding.
Company objectives referred to in an Option Appraisal report to Cabinet, 16th August 2023	• Higher levels of property numbers, • Enhanced quality of build, • More affordable housing numbers, • Financial return to the Council.

The Council's management of 3 Rivers development limited (continued)

Key findings (cont.)

Reporting on Company Performance and Risk

The Council used a range of formal and informal mechanisms to monitor Company performance. These included monthly liaison between the 3 Rivers Finance Director and the Councils 151 officer; monthly meetings with Cabinet Members with responsibility at Cabinet level to review the project progress of 3 Rivers and discuss any risks/ issues and bi-monthly PowerPoint presentation detailing project progress and risk assessment is provided to Cabinet on a bi-monthly basis internal management accounts and individual project financial performance.

Key performance indicators (KPIs) reported in formal progress reports did not provide an assessment of long-term progress towards the Council's objectives. For example, the Company's annual report to the Council in August 2022, covering the 2021/22 financial year, did not compare financial performance to expectation, or contain KPIs relating to any regeneration or housing quality objectives that may have been extant at this point. The Council's covering paper for the same report lists a number of 'highlights' but similarly did not include a systematic analysis of financial or non-financial performance relative to its own expectations or targets. For example, officers reported to Cabinet that *"The company has increased its overall borrowing by £3.4m to £13.5m"*; and that *"During 2021/22 the company paid the Council interest of £0.638m"* but did not set out whether this was in line with the Council's expectations or its forward forecast.

Some audit recommendations related to risk management were not fully implemented and strategic risk reports in routine performance reports from the Company to Cabinet (as shareholder) were of limited utility.

- In our 2020/21 Auditor's Annual Report, we recommended the Council address weaknesses identified by internal audit in relation to the Company's risk register. It is not clear, however, that any progress was made against this recommendation.
- The Company provided, as part of its performance reporting, a schedule of project risks as part of the "project report". This report provided useful narrative on the progress of specific projects and also included, as a final slide, a summary of its the key strategic risks. Between May 2021 and March 2022, this summary was provided at least four times. The assessment of risk was identical in each case, with the exception that the 'Overall risk' moved from "watch" (amber-red) to "Ok" (amber-green) between May 2021 and October 2021, though the basis of this assessment is not clear. In the instructions for completing the risk slide within the project report it is reported that *" [the risk assessment] is subjective - there are no hard & fast rules. This is meant to close the discussion rather than stimulate more."* This is not in line with robust and transparent risk reporting, but we did not identify any instances of the Council challenging this risk view.
- Similarly, in the Company's annual report of August 2022, risks are covered in narrative on individual sites and not highlighted. For example the body of the report notes a key risk of not achieving expected returns on due to note winning a tender to develop a site at Post Hill, but this was not flagged prominently in the report's summary, nor in the Council's own covering paper provided to Cabinet covering the annual report.

Responding to a changing operating environment in 2022/23

In April 2022 the Company recognised there had been a further, fundamental shift in its operating environment. In its 2021 business plan, the Company made clear that due to the competitive nature of the market within Mid Devon, it was exploring plans to develop some sites outside the district, to enhance its profitability. Such developments could have helped to achieve the key objectives relating to income generation of income for the Council, but not regeneration and housing market development objectives the Council also stated later it wished to achieve. In 2022, however, the Company was informed that the Council could not support development outside the district following changes to the PWLB lending criteria. A subsequent external review completed in August 2023 by Francis Clark reported that the impact of this change was obviously significant. It notes: *"There is a limited supply of land in the Mid-Devon district which is a constraint that the company needs to operate in. It is understood there were circa 90 development opportunities in Devon, but only four of these were in Mid-Devon, meaning future development opportunities for the company are restricted."*

The Council's management of 3 Rivers development limited (continued)

Figure 2: performance against build and sales targets compared to business plan, reported in the Company's annual report to Cabinet, August 2022

Site	Stage reached on development project	Business plan Month	Forecast Month
St George's Court	Build Completion	Apr 22	Nov 22
Orchard House	Final Sale	Jul-21	Jun-21
Knowle Lane	Start on site	Jan-22	Jan-23
Park Road (Anticipated Project 1)	Start on site	Sep-21	Nov-21
Post Hill (Anticipated Project 2)	Start on site	Oct-21	Feb-23
Bampton - (Anticipated Project 3)	Start on site	Aug-21	Aug-21
Future Project 1 (Howton Road)	Site purchase	Jan-22	Now Lost

Performance summary from covering paper to Cabinet "The main highlights of the 2021/22 financial year were:

- *Generated £0.676m in sales from units at The Orchard, Halberton*
- *Ongoing delivery of St. Georges Court, Tiverton and took over direct management with effect from 1 April 2021*
- *Commence start on site on Bampton project August 2021*
- *Repaid the Council £1.064m of capital borrowing relating to the Threwstones, Tiverton and Orchard, Halberton sites.*
- *The company has increased its overall borrowing by £3.4m to £13.5m*
- *During 2021/22 the company paid the Council interest of £0.638m"*

The Council's management of 3 Rivers development limited (continued)

Responding to a changing operating context (continued)

Despite the fundamental change in the operating context and there is no evidence the Council considered, in line with good practice, a formal review its business case for the company in early 2022/23. Good practice would have been to establish if its key objective (a financial return) was still deliverable, and whether a housing development company remained the right vehicle through which to deliver that objectives, and whether the rewards on offer were worth the level of risk the council would need to take.

The Council therefore did not come to a clear view on the right balance between company autonomy, and Council control and oversight within this new context. In August 2022, the Company submitted a discussion paper to Cabinet noting that it now had a very limited marketplace to seek new development sites. In the Company's view, a revised balance favouring more Company autonomy and agility was required for it to operate effectively. It proposed a more flexible working model based on autonomy within agreed funding envelopes. Officers' advice at the time recommended acceptance of the Company's linked funding request (see below) but deferred any discussion on the more fundamental question of the Council's relationship to the Company until at least that Autumn when the Council would usually be considering the company's latest Business Plan.

At the same time as requesting a clearer arm's length relationship, the Company highlighted immediate gaps in its funding, in the context of rising costs. During 2022/23, interest rates reached a 15-year high and the cost-of-living crisis intensified as inflation increased. The Consumer Prices Index ("CPI") rose by 8.7% in the 12 months to May 2023 and that meant that many potential buyers of new houses were delaying purchasing decisions. There was also pressure on the price and availability of construction materials. Based on a request from the Company, officers recommended (and Cabinet, in its role as Shareholder, agreed to) an increase in loan agreements of c£2.3 million in September 2022 to cover project overspends on two projects: St George's Court (£1.76 million) and Bampton (£0.23 million), plus £0.3 million working capital. The Cabinet approved this plus a further £0.6m "future projects fund" for the Company to replace abandoned plans for out-of-district projects.

Consideration of the Company's funding request and November 2022 business plan

Submission of the Company's funding request and the later business plan highlighted some Members' concerns about the Company's performance and the Council's oversight, exacerbated by the lack of a clear and agreed strategic direction.

- Cabinet on 6 September approved the Company's funding request.
- The Council's Overview and Scrutiny Committee resolved on 21 September 2022 that that the updates in the 6th September Cabinet papers (that is, the Cabinet decision to award additional funding in response to the Company's request for additional funding) were "*of such significance that the Committee believed that they constituted a new business plan*" and recommended Cabinet agree to an Audit Committee review of the business plan.
- Cabinet on 22 September resolved not to support the recommendation of the Scrutiny Committee and to remain consistent with its view taken on 6 September
- On 21 November considering the Company's business plan, the Scrutiny Committee recommended that the Audit Committee recommend to Cabinet that more detail about alternative options be sought from the S151 Officer and that Cabinet refer the matter to Full Council.
- At its own meeting of 22 November 2022, meanwhile, the Audit Committee recommended similarly that Cabinet seek more details, that more information on alternatives be included and that the Audit Committee itself recommend to cabinet that the business plan in its current form should not be supported due to the risk the Council may need to "impair loans on these projects with very narrow rates of return".

The Council's management of 3 Rivers development limited (continued)

Consideration of the Company's November 2022 business plan (continued)

Shareholder (particularly Cabinet) scrutiny of the Business Plan became increasingly detailed and operational, rather than strategic. Cabinet papers show that after reflecting on the meetings summarised on page 17, the Cabinet fed back to the Company and requested an amended business plan that restricted development to sites of 15 units or fewer. Accordingly, on 16th December 2022, the Company submitted an "addendum" to its November business plan reflecting "feedback provided [by] Cabinet" [that it is] "*seeking to support already approved schemes and those sites for development of up to 15 dwellings.*"

The Company pointed out that this challenged two large sites, Knowle Lane and Post Hill, and the proposed inclusion of a single, nominal 25-unit development site per annum that featured in the original November 2022 business plan. The Company argued that the latter was essential for it to be profitable. We note that the date at which the Company proposed it would be able to break even was now March 2026, some three years later than the date specified in the November 2021 business plan.

On 3rd January 2023, Cabinet considered the two business plans and associated site-level business cases but, unusually, referred the final decision to Full Council. Under the shareholder agreement, it is clear that decisions relating to the Company should be made by Cabinet.

Referring the decision to Full Council did not provide clarity to the Council's decision-making and decision-making on this issue became increasingly dysfunctional.

On 18th January, Full Council recommended to Cabinet that neither of the business plans or business cases be supported and set out its view and also that Cabinet should "*consider whether it should continue to fund the company and if so to what stage*" and that "*independent legal and financial advice be sought to help inform those considerations and explore what options are available.*"

On 27th January 2023, the Company submitted a third business plan for approval. The plan included a single nominal 25-unit development site per annum and a phased approach to Knowle Lane. The Post Hill site was to be abandoned. The projected break-even date was now March 2027.

On 31st January 2023, Cabinet approved the business plan of 27th January, along with two site-level business cases for Bampton (5 Levels) and Park Road. The Leader was not present at the meeting.

On 13th February 2023, the Overview and Scrutiny Committee called in Cabinet's decision to approve the 27th January business plan and supported Full Council's recommendation of 18th January not to support either business case and consider the Company's forward funding plans in the light of external advice. On 13th February 2023, four Cabinet members left their positions. Cabinet was not quorate and could not proceed.

On 22 February 2023, Full Council rejected all of the 3 Rivers business cases. On this date, the Council's Leader resigned, and a subsequent vote appointed an Independent Councillor, a member of the Council's Overview and Scrutiny and Planning Committees, as Leader until the then forthcoming elections in May 2023. The subsequent budget of 8th March was set on the basis of the recommendations made by Full Council (to not accept any of the 3 company business plans or the associated 2 business cases submitted by 3 Rivers Developments Ltd) but did include provision to fund to completion two of the company's existing development projects at St. Georges Court, Tiverton and at Bampton. The Council's subsequent external review, carried out by Francis Clark LLP, reported in August 2023 indicated that costs to complete St Georges Court and Bampton of around £1.8m, though noted that it is possible costs could be higher.

The Council's management of 3 Rivers development limited (continued)

Impact on the Council

As a result of the time taken to reach a decision, and the eventual decision not to approve any business case submitted by the Company, the Council was not able to set its budget in a robust and timely manner. The Council, like many others, typically sets its budget in February each year. Without a functioning Cabinet and agreement on a key part of the budget, the Council was not able to achieve this in setting its budget for 2023/24. The budget eventually set was not complete and relied on a significant one-off use of reserves to balance the 2023/24 financial plan.

While the original draft 2023/24 General Fund Budget recommended to Full Council on the 22nd February 2023 required only a temporary transfer of £58k from the New Homes Bonus Reserve, the budget approved by Full Council on 8 March 2023/24 included a number of changes:

- Transfers from General Reserves increased by £610,000, reflecting the removal of interest payments from the Company (assumed to be reversed in 2024/25 to reflect the replenishment of Reserves, though at the time of setting the budget the means to achieve this were not clear).
- Medium Term shortfalls increased by around £600k a year to reach £4 million by 2027/28.
- Interest Receivable (from 3 Rivers) reduced by £500k in 2023/24 (recurring)
- Car Parking revenue reduced by £120,000 in 2023/24 (recurring);
- Member's Allowances reduced by £40k (recurring); and
- £30,000 included for an external review of 3 Rivers Developments Ltd (one-off).

In August 2023, the Council decided to "soft close" the Company, resulting in a significant financial loss to the Council. As at quarter 2 2023/24, the Council estimated this at a gross loss of £9 million and a net loss of £6 million. The Council decided to soft close the company after considering external specialist advice on the company's trading position and future prospects. The Council's financial monitoring report for Quarter 2 of 2023/24 indicated that the Council had at that point made a further £1.3 million of loans to 3 Rivers in 2023/24 and indicated that the net drawdown to completion was a [further] £2.7 million, giving a total of around £25m loaned to the Company. Set against this is a forecast £16 million returns from sales. The Council notes that this does not include interest receipts and recharges of c£3 million, which would set the net total loss to the Council of around £6 million, which is a significant amount for a Council the size of Mid Devon District Council. At the time of compiling this report, work to progress the soft closure of the company was ongoing.

The Council's management of 3 Rivers development limited (continued)

Impact on the Council (continued)

Financial impact

The final financial loss to the Council may be higher (or lower) than forecast depending on the profit or loss on sales at completed sites, its exit strategy from remaining sites, and timely closure of the Company. As set out above, the Council in its budget of 8 March 2023 committed to completing two of the Company's ongoing projects – St George's Court and Bampton. The Council has committed to pay all creditors in full for these two projects up to completion. The Council based its forecasts on updates from the Company but, as the housing market is dynamic, it can currently only forecast the sales figures achievable from the completed sites. Given current housing market conditions, it is possible it will not realise the estimated returns set out earlier in the year. The Company also has operating monthly overheads of around £34,000.

As the Council notes, the implications of this are clearly negative from a value for money perspective. It identifies a combination of higher borrowing requirement for future capital projects and increased revenue costs for asset maintenance, vehicle replacements and essential property repairs as it has "significantly reduced these essential and prudent provisions" to meet these costs. On 29 August 2023, Cabinet resolved to approve the acquisition of the loss-making St Georges Court, by the Council's Housing Revenue Account, subject to an agreed valuation. It also agreed to a feasibility study on acquiring the Knowle Lane site. As this decision was taken in 2023/24, it does not present a risk of significant weakness in relation to 2022/23. The 2022/23 financial year is our final year as the Council's external auditor. We have brought this matter to the attention of the Council's new auditors for the 2023/24 financial year, for their consideration. **Impact on the Council's reputation**

Adverse media reporting illustrates how the poor decision-making and public disagreements can damage the Council's reputation. For example, we note that public allegations of fraud and incompetence were made by some members against other members and some officers at Full Council's meeting in January 2023. The report of an investigation by Devon Audit Partnership to the Audit Committee in May 2023 found that there was no substance to the allegations. The report set out the Auditor's judgement that the allegations were made based on an incomplete understanding of the issues involved. The debate has, however continued mistrust between officers, members and some members of the public continues.

Financial sustainability

We considered how the Council:

- identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds them into its plans
- plans to bridge its funding gaps and identify achievable savings
- plans its finances to support the sustainable delivery of services in accordance with strategic and statutory priorities
- ensures its financial plan is consistent with other plans such as workforce, capital, investment and other operational planning which may include working with other local public bodies as part of a wider system
- identifies and manages risk to financial resilience, such as unplanned changes in demand and assumptions underlying its plans.

Short and medium term financial planning

2022/23 financial performance

The General Fund Outturn in 2022/23 was a net overspend of £190,000 (1.38% on the Net Cost of Services Budget). There was also an underspend of £312,000 on the Housing Revenue Account (HRA), 2.90% of the Total Direct Expenditure Budget). This was improvement on the £436,000 overspend predicted at the end of Quarter 3. The Council funded the General Fund overspend from the General Fund Reserve, which decreased to £2.025m, still above the Council's minimum recommended level of £2m. The Council approved the transfer of the HRA surplus to the ring-fenced HRA earmarked reserve.

Along with many other local authorities, the Council identified staffing costs as a significant pressure area during 2022/23. During the year, the Local Government pay award of £1,925 per full-time equivalent was made (equivalent to around 6.5% per FTE on average). This was significantly in excess of the Council's budget assumption of a 2% increase and added £0.5m to the Council's staffing costs within the General Fund and £0.15m in the HRA.

Capital expenditure across the 2022/23 financial year was £17.1m - a variance of some £10.5m against the 2022/23 Deliverable Budget. Of the Council's total capital projects, £5.2m was underspent, £1.9m overspent, and £7.2m was slippage to future years. Of the underspend, the largest item by some margin related to the budget for 3 Rivers Development Limited projects, which underspent 100% of the planned £3.9m budget. At the time of reporting this underspend in June 2023, the Council had decided not to approve any business plan from 3 Rivers and the underspend is not surprising in this context, though illustrates the significant financial planning impact of decisions relating to 3 Rivers on the 2022/23 and 2023/24 budgets. The largest item of slippage (around £3.6m) related to the Cullompton town centre relief road, progress on which was subject to the Council securing additional external funding.

2023/24 financial planning

The Council set its budget for 2023/24 in March 2023, a delay to the usual timetable (see page 19). While the original draft 2023/24 General Budget recommended to Full Council on the 22nd February 2023 required a temporary transfer of £58k from the New Homes Bonus Reserve, the budget approved by Full Council on 8 March 2023/24 included a number of changes:

- Transfers from General Reserves increased by £610,000, reflecting the removal of interest payments from 3 Rivers Development Ltd (assumed to be reversed in 2024/25 to reflect the replenishment of Reserves, though at the time of setting the budget the means to achieve this were not clear.
- Medium Term shortfalls increased by around £600k a year to reach around £4 million by 2027/28.
- Interest Receivable (from 3 Rivers) reduced by £500k in 2023/24 (recurring)
- Car Parking revenue reduced by £120,000 in 2023/24 (recurring);
- Member's Allowances reduced by £40k (recurring); and
- £30,000 included for an external review of 3 Rivers Developments Ltd (one-off).

The final budget, in other respects, reflected key assumptions in line with national requirements and expectations, such as in respect of council tax increases with an increase of £6.56 or 2.99% from 2022/23, and did not display any clear deviation from prevailing understanding of legislation and policy as it stood at the time. The budget did, however, breach the Council's own policy on minimum General Reserve levels by setting a forecast level of around £1.4m at the end of 2023/24.

Financial sustainability (continued)

Short and medium term financial planning (continued)

As at November 2023 the Council was forecasting an overspend on the General Fund of £196,000 before the expected use of reserves set out on page 19, above. This means the Council is actually in a better position than it expected and, if it is able to deliver this position, then the general fund reserve would reduce to £1.8m, rather than £1.4m as forecast. This would still be below the recommended £2m minimum level, but much closer to it. However, this excludes any in-year write offs associated with the soft closure of 3 Rivers.

The Council generally has a well-established process for developing its view of medium-term and immediate funding requirements and gaps. On 1 November 2022, the first draft of the Medium Term Financial Plan (MTFP), covering the period 2023/24 to 2027/28 for the General Fund, Capital Programme and Housing Revenue Account (HRA), was presented to Cabinet. The General Fund budget indicated a deficit of over £5.2m by the end of the 5-year timeframe of the MTFP, with the increase largely due to the implications of the cost of living crisis. A November 2022 update focused more closely on the 2023/24 budget with a reduction in the projected shortfall for the General Fund to £960,000 and as at 3 Jan 2023, the draft budget deficit for 2023/24 was £905k. The proposed February Budget indicated an MTFP summary position of cumulative shortfall of £3,366k over the remaining four-years of the MTFP to 2027-28, which remained to be address. As set out on page 21, the final March 2023 MTFP position was a cumulative shortfall of around £4 million to 2027-28 reflecting shortfalls created by the removal of interest payments from 3 Rivers.

Developing savings plans

It is not clear from our review of 2023/24 budget setting that a more strategic approach to developing and monitoring delivery savings had been embedded. In our Auditor's Annual Report covering the 2020/21 financial year, we noted that the Council had not developed a strategic programme of savings to evolve its short-term use of reserves to balance the budget, though there were signs of a more strategic approach being developed. However, our discussions with the Council for our review of value for money arrangements in the 2021/22 financial year, and our review of the budget-setting for 2022/23 indicated that while the Council had progressed specific savings plans, it had not set these out as an identifiable 'programme' that could be monitored and tracked and the Council remained reliant on shorter-term tactical savings, such as underspends on staff budgets and contributions from reserves to balance the budget.

The late changes to the 2023/24 budget clearly necessitated a number of unplanned and short-term measures to arrive at a balanced budget but the work to recover a balanced position provides an opportunity to develop a true medium-term approach to savings plans. We note that one of the conditions of approving the 2023/24 budget on 8 March 2023 was that "work on strategic planning for delivering a balanced budget for 2024/25 […] commence immediately." We also note appetite expressed by Members during 2022/23 for a more "holistic" approach to savings plans. In discussing the MTFP in November 2022, Members noted that *"every year there seemed to be a budget gap. There was a need to have a strategy and for the gap to be managed. It was felt that the Policy Development Groups (PDGs) were compartmentalised and there was a need for a more holistic approach."* This again indicates that a strategic approach would be beneficial to the Council.

In balancing the 2023/24 budget, the Council set a vacancy management target of £400,000. In its 2023/24 budget submission the Council noted that *"The vacancy factor has been considered by all PDG's and Scrutiny. Although not ideal, Members understood the need for this and the potential implication for service delivery during 2023/24. Scrutiny requested regular progress updates against this target which will be provided."* This therefore provides a specific target that can be monitored. We reported in 2021/22 that the Council had a tendency to report vacancy-related underspends as savings and that while this is clearly true in terms of cost reduction, there may also be an erosion of value if the vacancies identified have a material impact on performance. Given the explicit focus on vacancy management, it is important that the Council understands the impact of vacancy management is at a granular level to ensure that the cost reductions achieved are not offset by a deterioration in performance.

We make a further improvement recommendation in relation to developing and monitoring medium term savings plans on page 27.

Financial sustainability (continued)

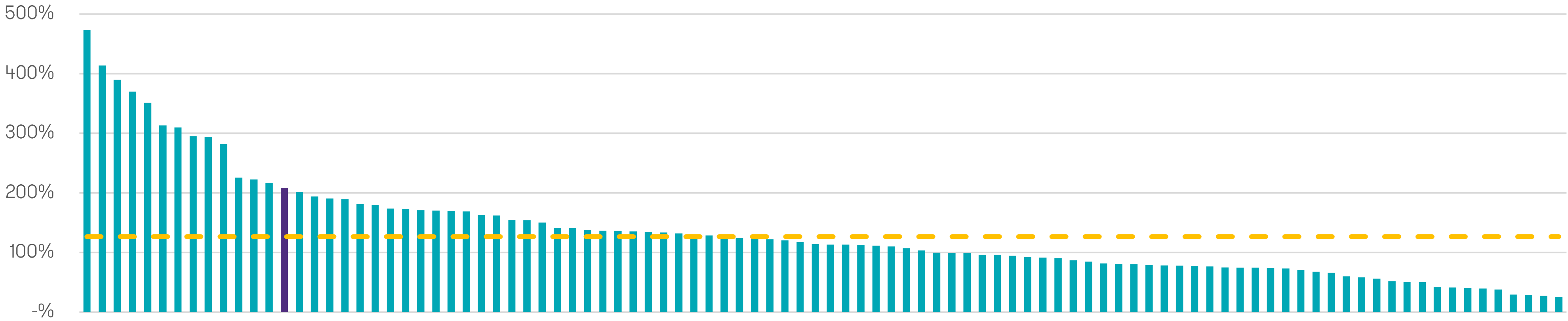
Managing risks to financial resilience and use of reserves

As set out above, we did not identify significant weaknesses in the Council's arrangements for financial sustainability in relation to 2022/23, including setting the 2023/24 budget. Given the ongoing financial pressure on all Councils, and the removal of forecast revenues and profits from 3 Rivers, it is important that the Council has a robust medium term plan that clearly sets out the gaps in its funding and how it plans to address these.

The Council's MTFP reporting clearly identifies risks and uncertainties within its financial planning, including both external factors (the lack of multi-year settlements, business rate reset and delay to fair funding review) and internal factors (such as the risk of achieving savings and income increases). As the Council highlights, not all of these risks can be mitigated and this means a level of uncertainty within its financial plan. The MTFP assumptions report sets out how the Council has addressed these risks within its financial plans. The report lists a range of assumptions and models the financial impact of a (+/- 1%) variance in each assumption. The 1% figure does seem arbitrary and does not fully reflect the actual level of risk in some areas, given the Council also notes a 40% increase in fuel prices. The Council rightly notes some costs are hard to predict and might have a higher degree of error - this being the case it would be helpful to see the impact of a broader spread of variation in each assumption. We raise an improvement recommendation in this regard on page 27.

The Council has a relatively high level of earmarked and General Reserves to meet the costs of unexpected events, relative to its net service budgets, compared to other District Councils (see chart below). As noted elsewhere, a result of the decision related to 3 Rivers, transfers from General Reserves increased by £610k in 2023/24 compared to the initially-budgeted amount (this is reversed in the Council's plans for 2024/25 to reflect its planned replenishment of that Reserve). This was an unforeseen risk and meeting it took the Council's General Reserve below its recommended minimum level of £2 million, though this was contingent on starting work to replenish this reserve. As with all Councils, continued monitoring of the level of risk relative to the level of available reserves is required to ensure reserves are maintained at an appropriate level.

Figure 3: General fund and non-schools earmarked general fund reserves as a percentage of net service revenue expenditure (%) – 2022/23; District Councils for which 2022/23 available at time of this report.)



Note: Data sourced directly from local authority draft Statements of Accounts published on council websites. As this data is taken from third parties, we cannot verify the accuracy of completeness of such information. Data is not available for all local authorities due to some delays in publications.

Financial sustainability (continued)

Capital strategy and borrowing

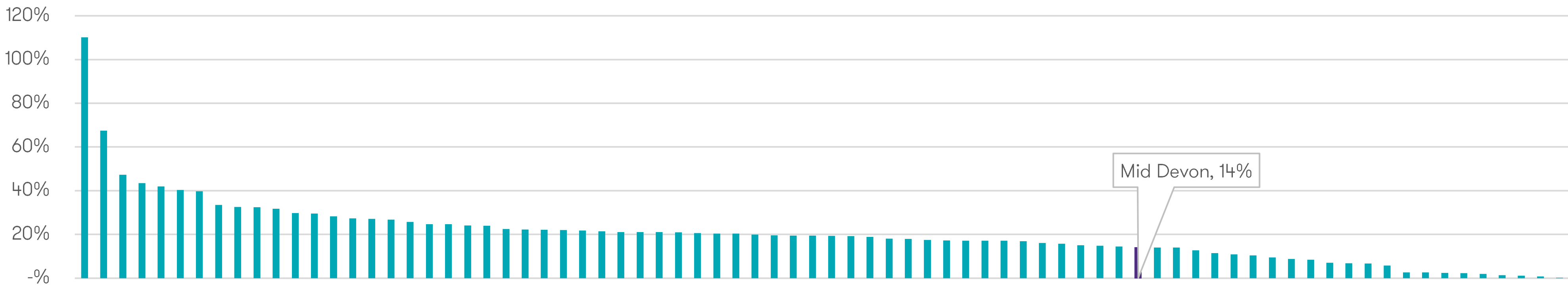
At the time it initially set its 2023/24 budget, the Council envisaged a significant capital programme with projects expected to start in 2023/24 totalling £98.4m and some £39.4m rolling forward from the 2022/23 programme. Some £64.8m of this was expected to be spent in 2023/24. The programme included significant investment in housing, either through the HRA Housing delivery programme (£15.7m) or through 3 Rivers (£26.1m).

Following the changes to the Council's plans, driven substantially by the Council's decision not to approve any business plans related to 3 Rivers, the actual capital programme in 2023/24 is considerably smaller than expected. As at the end of Quarter 2, there was a variance of £52.9m against the 2023/24 budget. Of this, only £1.1m was a forecast underspend, set against a £1.7m over-spend. There was slippage of £28.7m across various projects (including the Cullompton Town Centre Relief Road project) and various indicative HRA schemes, and £24.9m of spend no longer required, the majority reflects removal of future 3 Rivers development projects from the programme.

As shown in the chart below, the Council does not currently have an excessively high level of long-term borrowing, relatively to the value of to its long-term assets, compared to other District Councils. The Council reported in 2022/23 that it remained under-borrowed. This meant that the capital borrowing need (the Capital Financing Requirement) was not fully funded with loan debt. The Council considers that its policy of avoiding new borrowing by running down spare cash balances, has served it well over the last few years. However, as it also notes, this has been kept under review to avoid incurring higher borrowing costs in the future when the Council may not be able to avoid new borrowing to finance capital expenditure.

The Council has a clear Treasury Management Strategy that is presented to Cabinet alongside the Capital Strategy and Draft budget, typically in February each year. Total treasury investments fell from £32m to £21m with the main drawdown being from banks (£12m to £4m) and other local authorities (£15m to £12m). The absolute amount invested externally in property funds remained at £5m but this means it now represents 24% of investments (up from 16%). Due to interest rates over the year, the Council's return on its short-term investments increased significantly from £54,000 in 2021/22 to £539,000 in 2022/23.

Figure 4: Long-term borrowing as a proportion of long-term assets (%); 2022/23, District Councils for which 2022/23 available at time of this report.



Note: Data sourced directly from local authority draft Statements of Accounts published on council websites. As this data is taken from third parties, we cannot verify the accuracy of completeness of such information. Data is not available for all local authorities due to some delays in publications.

Financial governance

Annual budget setting and identifying savings

As we reported in our 2021/22 Auditor's Annual Report, the Council usually maintains adequate arrangements to set its annual budget. Budget proposals are considered by Cabinet in February each year having been were also circulated and considered by the Scrutiny Committee in January and also considered by the Council's Policy Development Groups in November and January.

As set out on page 19, the setting of the 2023/24 budget was significantly disrupted by the delays in decision-making on approval of the 3 Rivers business plan, and the associated fallout from the debate around this. This contributes to the significant weaknesses and key recommendations we have set out on pages 5-6 and pages 8 and 9. However, we do not consider that this specifically implies further underlying weaknesses in the basic budget setting arrangements that require further recommendations.

We noted in 2021/22 that the Council's Policy Development Groups did not identify any specific savings plans in 2022/23 and we made an improvement recommendation in relation to developing strategic savings plans. We note that PDGs did put forward options to consider in early drafts of the 2023/24 budget to identify options to bridge the budget gap estimated at that point. The first paragraph of the 29 November update to Cabinet, for example, makes clear that the recommendations of PDGs are key to approving and moving forward the budget. It is also clear that PDGs made specific suggestions to identify savings.

As we recommended in 2021/22 – and as the Council's PDGs themselves noted in considering the Council's MTFP in November 2022 – there remains scope for the Council to take a more strategic and holistic approach to setting a medium-term savings programme. We recommended the Council develops processes to identify and track key medium-term savings initiatives to help manage the ongoing risk of funding gaps. It would be good practice for its tracking to identify the target savings and payback period and whether any investment is affordable, and whether in-year and cumulative targets had been met. Our improvement recommendation on page 27 covers this.

Budgetary control

Cabinet receives quarterly updates during the year which reports financial performance in some detail. These include:

- a summary of the General Fund budget, including a full-year forecast, and actual spend against budgets, with key variances explained; and
- HRA summary performance, again with a schedule of major movements and reasons.

The main reports provide additional commentary on risks, impact on key reserves and treasury management activity including interest receivable and payable.

Financial update reports are presented to Cabinet separately from performance and risk reports, though sometimes these intersect, allowing non-financial performance to be considered at the same time as financial performance. In 2022/23 however, the outturn for performance was presented in July 2023, while the capital and revenue outturns as well as the Treasury Management Outturn were presented in June. We do not see this as a significant weakness given the reports themselves are of adequate quality and there is a regular drumbeat of reporting.

We note that the Council has been implementing changes to its performance framework through which it aims to streamline the number of indicators reported to allow members to focus more on the key indicators that are most important to their view of the Council's performance. We report on this further on page 32.

Financial governance (cont.)

Preparation and audit of the Council's 2022/23 financial statements

The Council submitted its draft group and Council financial statements for external audit in June 2023. The Council consolidates one subsidiary company, 3 Rivers Development Limited, into its group financial statements. The draft group financial statements presented for audit were prepared and consolidated on the basis that the company would continue to trade.

As set out earlier in our report, on 6 September 2023, the Council reached a decision to 'soft close' 3 Rivers Development Limited. This means that the subsidiary company accounts can no longer be prepared on a going concern basis and that the valuation of assets and liabilities within the subsidiary has required reassessment, along with any consequential impact on the Council's own and group financial statements. We raised this issue with management and facilitated a meeting of representatives from the Council and 3 Rivers Development Limited on 26 September 2023 to understand the Council and company's plans for it revised accounts preparations. At that stage, no arrangements had been made to reconsider the accounts at that time and it was agreed that the subsidiary's accounts would need to be revisited, to allow the subsidiary's audit to be undertaken.

Following the Council's decision to close its arm's length company (3 Rivers Development Ltd) in August 2023, updated group and subsidiary accounts required preparation to reflect the realisable value of assets and liabilities of the company within the consolidated group accounts for Mid Devon District Council. This, coupled with some delays encountered in the receipt of outstanding working papers, informed our decision to pause the audit of the Council's financial statements in December 2023.

Our audit work recommenced in April 2024, following receipt of updated consolidated group accounts for Mid Devon District Council. We have now concluded the outstanding audit work and issued our audit report, including the audit certificate on 8 May 2024.

Our Key Recommendation on page 8 made it clear the Council needs to continue to make progress on these issues. In our interim report, we set out that a failure to prepare updated accounts to allow for timely conclusion of our audit, prior to any backstop date would constitute a further risk of significant weakness in the Council's arrangements to secure value for money. We are pleased to report that the audit has now been concluded, within the revised timescales agreed. Further, a lack of clarity on the scale and timing of the financial loss may hinder the Council's ability to develop its financial plans accordingly.

Improvement recommendation

Improvement Recommendation 1	To support medium term financial planning the Council should • set out a medium-term programme showing how it will close its forecast medium-term gaps in its financial plans, including the contribution of savings plans and related activities, such as income generation. • revisit the sensitivity analysis it uses to illustrate divergence from key assumptions, as a 1% variance may not adequately capture the level of volatility or the Council's view of the degree of error possible in its estimates.
Improvement opportunity identified	We have previously recommended that the Council develop a more strategic approach to developing and reporting on savings proposals. More systematic monitoring of savings proposals, targets and progress would enable members to routinely track progress on key savings proposals. Some Councils set out such plans on a multi-year basis, recognising that invest-to-save activities, for example, may take more than one year to deliver a net saving.
Summary findings	It is not clear from our review of 2023/24 budget setting process that a more strategic approach to developing and monitoring delivery savings had yet been embedded. We also note there appears to have been some appetite expressed by Members for amore holistic approach to developing and tracking progress on savings plans.
Criteria impacted	Financial sustainability
Auditor judgement	Our work has enabled us to identify a weakness in arrangements which we do not consider to be significant, but have raised a recommendation to support management in making appropriate improvements.
Management comments	The Council will review best practice and consider any changes required for the 2025/26 budget process. However, it is worth reflecting how the council has successfully balanced budgets and increased its reserves set against a backdrop of government funding cuts.

Progressing the actions management has identified to address the recommendations made will support the Council in addressing the improvements identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place. The range of recommendations that external auditors can make is explained in Appendix B.

Governance

We considered how the Council:

- monitors and assesses risk and gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud
- approaches and carries out its annual budget setting process
- ensures effective processes and systems are in place to ensure budgetary control; communicate relevant, accurate and timely management information (including non-financial information); supports its statutory financial reporting; and ensures corrective action is taken where needed, including in relation to significant partnerships
- ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency
- monitors and ensures appropriate standards, such as meeting legislative/regulatory requirements and standards in terms of staff and member behaviour (such as gifts and hospitality or declaration of interests) and where it procures and commissions services.

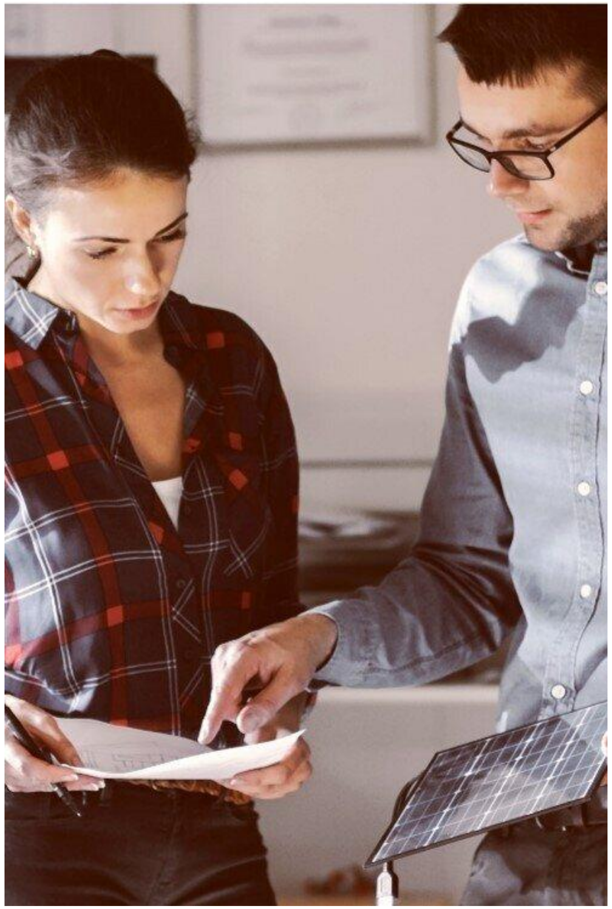
Risk management

The Council has a risk management policy that was approved by the Audit Committee in March 2022. The policy sets out its purpose, aims and objectives which is to embed risk management in the Council by establishing a risk management framework. The policy also sets out roles and responsibilities for risk management within the Council. The Audit Committee is responsible for approving the Risk management Policy and monitoring the operation of risk management. Cabinet also monitors the effective operation of risk management while the Leadership Team is responsible for setting risk appetite and identifying corporate strategic risks.

The Council maintained a corporate risk register which sets out its assessment of strategic risks in 2022/23. These are risks which are most likely to impact the corporate priorities of the Council. The risk register is reviewed at least quarterly by the corporate managers and the leadership team and updated as required. It is then presented to the Audit Committee and to Cabinet. The council uses a standard risk scoring matrix, where the scores of "impact x likelihood" equals the total risk score. Risk scoring between 15 and 25 would be classed as high risk (red) with 25 being the highest risk. Risk scoring between 6 and 12 would be classed as medium risk (amber) and risk scoring between 1 and 4 would be low risk (green).

The Audit committee received the performance and risk update reports in March, June, August, November 2022 and March and June 2023. The Cabinet received them in April, June, August, November 2022 and April and June 2023.

We note that the Council has revised its way of reporting from March 2023 and the risk report is now reported separately from the Corporate performance report. As at July 2023, unsurprisingly, the highest scoring risks related to the potential failure of 3 Rivers; and the Cullompton Town Centre Relief Road, which was contingent on funding from external sources being identified. This reflects a reasonable view of the key issues facing the Council at that time.



Governance (continued)

Internal Controls and the Audit Committee

The Council's internal audit service is delivered by the Devon Audit Partnership, a shared service arrangement with the founder councils of Torbay, Devon and Plymouth formed in April 2009. Public Sector Internal Audit Standards requires that an external assessment of Internal Audit is undertaken every five years. An external assessment on Devon Audit Partnership (DAP) was conducted at the end of 2021, by the Head of Southwest London Audit Partnership and the Chief internal Auditor of Orbis (a partnership organisation covering Brighton and Hove, East Sussex, and Surrey County Councils). The assessment result was that "“Based on the work carried out, it is our overall opinion that DAP generally conforms with the Standards and the Code of Ethics‘’.

The 2022/23 Internal audit charter and plan were approved by the Audit Committee on 22 March 2022 and covered an extensive range of reviews including audit governance with a total 345 audit days audit work planned.

Regular internal audit progress reports were presented to the audit committee. The Committee received updates in June, August, September and November 2022, and January and March 2023. The progress reports included executive summary of audit results, fraud prevention and detection update, audit coverage against the plan audit recommendation tracking.

The internal audit annual report indicates 89% audit plan coverage against a (90% target). The remaining audits were either cancelled, deferred by the Council, or rolled over into 2023/24.

The Internal Audit Annual report indicated that the head of internal audit’s opinion for the year was one of “reasonable assurance”. The report highlights that 24 of the reviews were assigned either substantial or reasonable assurance opinions and five were given a limited assurance opinion. These related to:

- Cyber Security: The need for more effective cyber governance commensurate with risk present in this area.
- Information Governance: further work is needed to implement and embed improvements.
- Environmental Health (Water): Problems with staff resourcing impacted on the team output and resultant income derived.
- Repairs and Maintenance: A reactive rather than proactive maintenance approach and the system to manage repairs is not effective.
- Culm Valley Sports Centre: Concerns including costs vs income, and Health and Safety responsibilities and monitoring.

	2022/23	2021/22
Annual Governance Statement (control deficiencies)	None	None
Head of Internal Audit opinion	Reasonable Assurance	Reasonable Assurance

The Council’s performance against key governance metrics is set out in the table above.

Governance (continued)

Standards and behaviours

As set out above, our findings in relation to 3 Rivers Development Limited highlight significant weaknesses in relation to the way the Council conducted the debate around approval of the Company's November 2022 Business Plan. We note that issues around the Company appear to have been a focal point for these behaviours and our review of the Council's arrangements more generally did not identify similar issues, and the Council has in place arrangements that we would usually expect to see to govern standards and behaviour.

The Council's constitution, reviewed in February 2023, incorporates codes of conduct for members and officers, both of which set out how these individuals are expected to conduct themselves.

It is the Monitoring Officer's responsibility to monitor compliance with legislation and regulatory standards. The Monitoring Officer reports annually to the Standards Committee on complaints under the Code of Conduct, most recently in October 2023, covering the 2022/23 Financial Year. This report highlighted that during 2022/23, a total of 12 formal complaints were made, 4 of which were withdrawn. None were referred for formal investigation, though the report notes that these cases still raised important questions about standards of behaviour. The core themes were respect, bullying, communication and reputational concerns. The complaints were made against parish and district councillors.

The report notes that workload and capacity has been an issue for the Monitoring Officer this year, which resulted in some of the complaints not being considered in as timely a manner as the Council would have wished, particularly when several complaints were under consideration at once.

The Council, through its Codes of Conduct and its Constitution maintains appropriate policies on standards and behaviours including the receipt of gifts and hospitality. However, there is scope to increase the level of monitoring of staff and Member awareness, and engagement and compliance with key policies. We make an improvement recommendation in this area on page 31.

Informed decision making

The Council's constitution, sets out how decisions are made within the Council. The Council currently operates a Cabinet system of governance where each Cabinet Member holds a separate portfolio, to include: Environment; Community Well-being; Finance; Housing and Property Services; Planning and Economic Regeneration; Working Environment and Support Services, and; more recently, Climate Change. Decisions concerning Council policies, plans, and strategies are taken by the Cabinet as a whole, which are reported to Full Council. The Cabinet and the decisions it takes are scrutinised by the Scrutiny Committee. The Audit Committee can challenge management over areas of concern identified in audit reports. We set out findings in around this process

The Council publishes on its website details of all Committee meetings, including Full Council and Cabinet. The details include agendas, minutes, and decisions made. The Council also maintains a forward plan, which shows key decisions that will be made over the next one to four months. This plan is published on the website and include a short description of the decision to be made, who will make it, when the decision will be taken, details of planned consultation with local people and other stakeholders and reports and background papers. Reports to Cabinet and Full Council provide space for finance, legal and services input before they are considered by members.

Beyond matters highlighted earlier in this report around the Council's subsidiary, we did not identify significant weaknesses in relation to the Council's arrangements for informed decision-making.

Improvement recommendation

Improvement Recommendation 2	The Council should put in place a mechanism to provide positive assurance that officers and members have complied with the Council's policies on receipt of gifts and hospitality during the year. This could be achieved through a periodic declaration, for example. The Council may wish to include in such a declaration confirmation that other key parts of the Code of Conduct had been read and complied with.
Improvement opportunity identified	The Council could increase the level of assurance it has that officers and members have reviewed, and complied with, the terms of key policies such as those governing the receipt of gifts and hospitality
Summary findings	The Council, through its Codes of Conduct and Constitution maintains appropriate policies on standards and behaviours including the receipt of Gifts and hospitality. However, there is scope to increase the level of monitoring of staff and Member awareness, and engagement and compliance with key policies.
Criteria impacted	Governance
Auditor judgement	Our work has enabled us to identify a weakness in arrangements which we do not consider to be significant, but have raised a recommendation to support management in making appropriate improvements.
Management comments	The Council will consider this recommendation and assess what mechanisms could be put in place that provide more positive assurance of compliance with such policies.

Progressing the actions management has identified to address the recommendations made will support the Council in addressing the improvements identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place. The range of recommendations that external auditors can make is explained in Appendix B.

Improving economy, efficiency and effectiveness

We considered how the Council:

- uses financial and performance information to assess performance to identify areas for improvement
- evaluates the services it provides to assess performance and identify areas for improvement
- ensures it delivers its role within significant partnerships and engages with stakeholders it has identified, in order to assess whether it is meeting its objectives
- where it commissions or procures services assesses whether it is realising the expected benefits.

Use of financial and performance information

Reporting performance to Members and stakeholders

The Council has improved the way it reports its performance to Cabinet.

We reported in 2021/22 that the Council had adequate arrangements for reporting performance to Cabinet including established arrangements for reporting key performance indicators (KPIs) periodically. At the time of our review in early 2023, the Council was in the early stages of a review of its performance frameworks, and we noted that this provided a good opportunity to consider whether it was reporting 'measures that matter' to Members and other stakeholders.

The Council has now adopted a new format for reporting its performance to Cabinet, in which the cover report has been enhanced to include summaries of key indicators of interest and includes more graphs and charts to highlight trends and bring the data to life. The summary report is accompanied by five appendices which cover: Homes, Environment, Economy, Community and Corporate. These map to the Council's Policy Development Groups, plus the overarching corporate update which provides useful statistics on corporate performance.

There is scope to include more information on cost-effectiveness and productivity performance reporting. We understand the Council maintains a subscription to external benchmarking websites and given members' interest in, for example, the cost effectiveness of waste collection (and that finance and performance continue to be reported separately), the Council could usefully supplement KPI reporting with some of this data. We raise an improvement recommendation in this regard (see page 35).

Data quality and completeness

The Council recognises the importance of data quality at an organisational level. The Council has a Data Quality Policy and associated data Quality standards; the most recent versions were presented to and approved by the Audit Committee in November 2022. The policy confirms that fit for purpose data is integral to performance management and should be accurate, valid, timely, relevant and complete. Roles and responsibilities are set out clearly, as well as the need for adequate controls over data input and verification of data.

As we noted in our 2021/22 AAR, internal audit has previously noted shortcomings in relation to the Council's use of service level management information. It noted these findings particularly in issuing its limited assurance opinion on care services, alarms but also in other areas, such as car parking, in which it gave a reasonable assurance rating overall. Our review of the audits completed by internal audit during the 2022/23 year did not identify any specific audits related to data quality such as reviews of performance indicator systems underpinning KPIs reported to Cabinet. However, the 2022/23 internal audit annual report highlight instances where performance information is not being collected or reported to allow effective monitoring and decision making, such as Repairs and Maintenance, Culm Valley Sport Centre and Housing Voids.

We therefore continue to note our existing improvement recommendation from 2021/22 that the Council should map its assurance framework for key contracts. This should include assuring itself that service managers have access to the information and data they need to monitor and report on service performance effectively and whether the links between service- level and strategic reporting to Members is clear, for example, when service managers should to escalate a service problem to a more strategic level.

Improving economy, efficiency and effectiveness (continued)

Using information to improve the cost-effectiveness of services

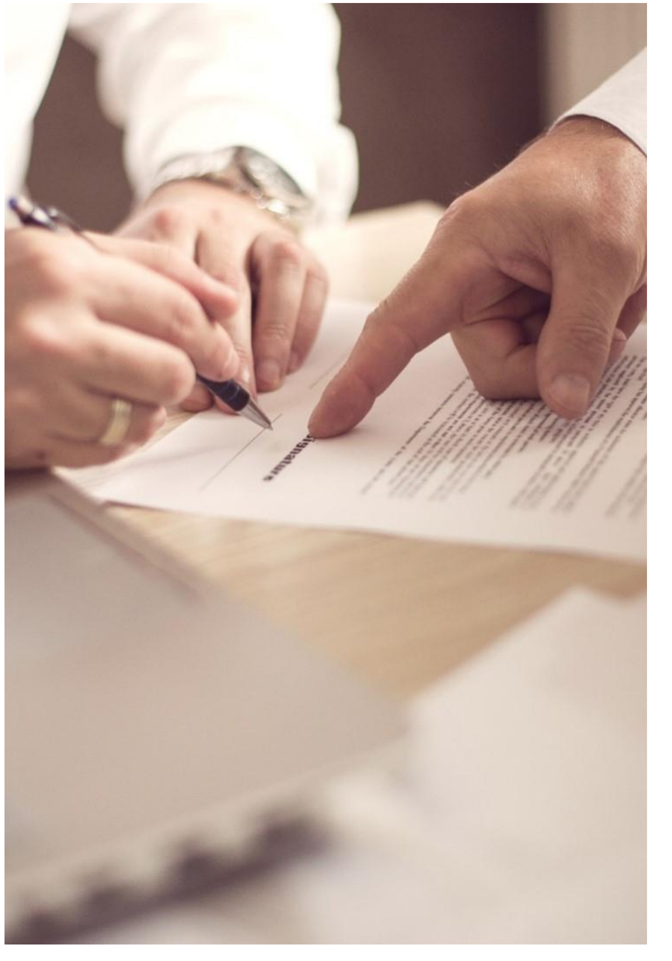
The Council did not make significant recurring service savings to balance 2022/23 budget, relying instead on transfers from reserves. The 2023/24 budget report recognises that while the Council has up to now secured savings without reducing services, this is becoming more difficult and a new strategic process is required to match service provision to available funding, with difficult decisions required that will alter the quality or frequency of services in the future. Members' preference remained to explore revenue raising options before cutting services. As set earlier in our report, we consider there is now an even greater need for a coherent and well-communicated medium-term savings plan (which could include income-generation measures) that can be discussed in the holistic way members have highlighted.

The 2023/24 budget process identified various options for service savings that will be considered for future years. This included potentially closing public conveniences, reducing waste collections and reducing grant payments. It is not clear that any of these were adopted as recurrent savings (barring the waste collection changes set out above, where the quantum of savings is not yet clear). One specific proposal considered as part of 2023/24 budget setting was a review of local paddling pools with a view to potential closure, saving £70,000. This was subject to intense discussion on 8 March 2023 with members of the public concerned about the impact of a potential closure.

While this was not a major potential financial saving, it does illustrate how potential changes to popular local services can affect residents, and the need for a clear and well-communicated strategy to achieve the MTFP savings required, particularly if services may be affected. This further underlines the benefit of a clear programme of potential savings to bridge medium-term gaps, as set out in our recommendation on page 27.

In common with other waste collection authorities, the Council has been attempting to make its waste collection service more efficient. This is an area in which the Council has struggled to recruit and retain permanent staff, and relies significantly on agency workers. In February 2022, Cabinet agree a move to 3-weekly waste collections (known as 1-2-3 Recycle, Reuse, Reduce). Part of that change was to provide households with a wheeled bin for their waste. Approval was sought to add a £750,000 one-off investment (previously estimated at £650,000) to the 2022/23 Revenue Budget, fully funded from Earmarked Reserves, for the purchase of the bins. The new service is expected to deliver savings from 2023/24.

Cabinet received updates on this initiative in August 2022 and again in August 2023. The latter indicated that the scheme had had a positive effect on recycling rates, but did not contain an analysis of the comparative costs of the service compared to the previous service. The paper notes that the environment PDG recommended that further trialled changes scheduled for 2023/24 be postponed to allow for an evaluation of the effectiveness of the current scheme against the metrics of recycling percentage achieved, residual tonnage reduction, and overall cost to the Council. This provides a good example of the use of information and effective challenge of an "invest to save" measure that the Council can build on.



Improving economy, efficiency and effectiveness (continued)

Partnership working

The Council's March 2022 LGA peer challenge report noted that it *"led an impressive response to the Covid pandemic"* and the follow up report from December 2022 noted that senior officers and members *"are continuing to play an active and visible role at the regional and sub-regional level"*.

The Council has a building control partnership with North Devon District Council (NMD Building Control). The costs of this partnership are reported through the Council's routine financial monitoring. NMD performance is reported as part of Corporate performance reports, comprising KPIs for full plan applications and building regulation applications determined within timescale. Internal Audit reviewed NMD Building Control in 2021/22 and provided a reasonable assurance opinion. The Council also operates a procurement partnership with Devon County Council which is governed via a service-level agreement.

The Council confirmed during our 2021/22 review of its VFM arrangements that it had not implemented our improvement recommendation from our 2020/21 Auditor's Annual Report to develop a partnership register. The Council considers that it relies more on contractual relationships with key suppliers to provide essential services than partnerships (other than building control). However, the Council committed to keeping this under review.

Commissioning and procurement

As we reported in 2021/22, the Council has in the past maintained a small in-house procurement team but, after staffing changes and struggling to recruit suitably skilled people, from June 2021, Devon County Council (DCC) provided interim reactive support, including procurement advice and guidance to services in undertaking procurements including contractual support. The Council then more formally outsourced procurement support to Devon County Council.

The Council has a procurement strategy covering 2023/24. The Audit Committee on 24 January 2023 considered a draft procurement strategy for 2023 to 2027, and the final strategy in February 2023.

Internal Audit's 2022/23 review of procurement found that the Council has a good procurement framework to support the effective and efficient procurement of goods and services. The procurement team includes an experienced and qualified Contracts Officer and a Procurement Officer, both of whom have access to specialist support provided by Devon County Council via its Devon Procurement Services team. This aligns with our own understanding of the Council's arrangements.

They also found that the Council provides good guidance on procurement and contracts and that the Procurement Strategy for 2023-27 is aligned with the Devon County Council Strategy. There were 11 waivers visible on the contracts register with a combined value of £569,000, which was comparable to peer councils. Internal Audit further noted that that the Councils should publish their Contracts Registers on a quarterly basis and a link to the database was clearly highlighted, along with a real-time list complying with the requirements.

Improvement recommendation

Improvement Recommendation 3	**The Council should include further information on the cost-effectiveness of services in its performance reporting to Cabinet, drawing on relevant benchmarks.**
Improvement opportunity identified	The Council has already improved its performance reporting regime and could develop this further to support delivery of key savings plans.
Summary findings	**There is scope to include more information on cost-effectiveness and productivity in performance reporting to Cabinet.** We understand the Council maintains a subscription to external benchmarking websites and given members' interest in, for example, the cost effectiveness of waste collection (and that finance and performance continue to be reported separately) the council could usefully supplement KPI reporting with some of this data.
Criteria impacted	Improving economy, efficiency and effectiveness
Auditor judgement	Our work has enabled us to identify a weakness in arrangements which we do not consider to be significant, but have raised a recommendation to support management in making appropriate improvements.
Management comments	The council has subscribed to CipfaStats+ and implemented the new performance reporting regime which will include national and local benchmarking for the 2024/25 financial year.

Progressing the actions management has identified to address the recommendations made will support the Council in addressing the improvements identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place. The range of recommendations that external auditors can make is explained in Appendix B.

Follow-up of previous recommendations

	Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
1	We recommend the Council develops process to identify and track key medium-term savings initiatives to help manage the ongoing risk of funding gaps. It would be good practice for its tracking to identify the target savings and payback period and whether any investment is affordable, and whether in-year and cumulative targets had been met.	Improvement	May 2023	It is not clear from our review of 2023/24 budget setting that a more strategic approach to developing and monitoring savings plans had yet been embedded. We also note appetite from Members for a more "joined-up" approach.	No	Yes – we set out a further improvement recommendation in this area (improvement recommendation 2)
2	When identifying salary underspends in its financial reporting the Council should be clearer whether the financial underspend has led to any reduction in quality or service level (such as reduced activity, backlogs or delays) or whether a genuine efficiency saving (where costs have been reduced without adversely impacting quality) is being identified.	Improvement	May 2023	We note that in balancing the 2023/24 budget, the Council introduced specific vacancy management targets which contributed £400,000. This provided a specific target that can be monitored. It is important that the impact of vacancy management is understood at a granular level to ensure that the cost reductions achieved are not offset by a deterioration in performance.	Yes	Yes – we set out a further improvement recommendation in this area (improvement recommendation 2)
3	In taking forward its review of its performance framework and KPI suite, the Council should: consider including more indicators that capture operational and customer-focused issues, which could be integrated into strategic reporting, to ensure key stakeholders' perspectives are represented.	Improvement	May 2023	The Council accepted this recommendation. We have noted ongoing improvement in this area, in line with the Council's response to our 2021/22 recommendation.	Yes	We make further suggestions for developing the Council's performance reporting to include more information on cost-effectiveness and productivity (improvement recommendation 4)

Follow-up of previous recommendations

	Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
4	The Council should map its assurance framework for key contracts. This should include assuring itself that service managers have access to the information and data they need to monitor and report on service performance effectively and whether the links between service- level and strategic reporting to Members is clear, for example, when service managers should to escalate a service problem to a more strategic level.	Improvement	May 2023	The Council accepted this recommendation. Internal Audit's 2022/23 review found existing good practice in some areas, including good guidance on procurement and contracts and that the Procurement Strategy 2023-27 is aligned with the Devon CC Strategy. IA highlighted as good practice the approach of another council to classify their contracts as Gold, Silver, and Bronze to support prioritisation of the contract management required. We did not identify specific improvements in this area, but given the timing of the recommendation and the scope of our review being to the year to April 2023.	Ongoing	The Council should continue to implement this recommendation.
5	We recommend the Council maps its key partnerships systematically and set outs: their aims and objectives, its financial commitment, the service improvement or other goals, and whether the intended goal are being achieved. This will enable it to identify clearly the value its ongoing partnerships add, and may assist in identifying where similar partnerships offer further opportunities for efficiencies to be made, including other areas in which collaboration could help the Council address skills gaps, particularly where it might otherwise struggle to recruit or retain skilled individuals.	Improvement	May 2023	The Council has chosen not to implement this recommendation but has noted that it will keep its position on this under review should its partnerships landscape change.	No	The Council should keep this in view in line with its management response to the recommendation from our 2021/22 Auditor's Annual Report.

Opinion on the financial statements

Grant Thornton provides an independent opinion on whether the Council's financial statements:

- give a true and fair view of the financial position of the Council and Group as at 31 March 2023 and of its expenditure and income for the year then ended, and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of practice on local authority accounting in the United Kingdom 2022/23
- have been prepared in accordance with the requirements of the Local Audit and Accountability Act 2014.

We conducted our audit in accordance with:

- International Standards on Auditing (UK)
- the Code of Audit Practice (2020) published by the National Audit Office, and
- applicable law

We are independent of the Council in accordance with applicable ethical requirements, including the Financial Reporting Council's Ethical Standard.

Opinion on the financial statements

Audit opinion on the financial statements

We have completed our audit of your 2022-23 financial statements and issued our final audit findings report to the Council. This was presented to Audit Committee on 30 April 2024. This updated the position that was reported to the committee on 5 December 2023.

Following the Council's decision to close its arm's length company (3 Rivers Development Ltd) in August 2023, updated group and subsidiary accounts required preparation to reflect the realisable value of assets and liabilities of the company within the consolidated group accounts for Mid Devon District Council. This, coupled with some delays encountered in the receipt of outstanding working papers, informed our decision to pause the audit of the Council's financial statements in December 2023.

Our audit work recommenced in April 2024, following receipt of updated consolidated group accounts for Mid Devon District Council. We have now concluded the outstanding audit work and issued our audit report, including the audit certificate on 8 May 2024.

Whole of Government Accounts

To support the audit of the Whole of Government Accounts (WGA), we are required to review and report on the WGA return prepared by the Council. This work includes performing specified procedures under group audit instructions issued by the National Audit Office. As the Council is below the stated national thresholds, no detailed procedures are required. Our shortform assurance statement was issued on 8 May 2024.

Preparation of the accounts

With the exception of the matters already highlighted in relation to the Group and subsidiary, the Council provided draft accounts in line with the national deadline and provided suitable quality working papers to support it.

Findings from the audit of the financial statements

The draft group financial statements, submitted for audit, were amended to reflect the revised subsidiary accounts. The key changes to the group accounts are summarised below. These predominantly relate to further impairment of Work In Progress:

Group Comprehensive Income and Expenditure Statement

• Expenditure increased from £1,376k to £3,713k an increase of £2,337k

Group Balance sheet

• Work in progress decreased from £13,946k to £11,632k

• Short-term creditors increased from £11,023k to £11,046k

• Usable reserves down from £51,964k to £49,627k

Other

• The Cashflow Statement, Movement in Reserves Statement and group notes have all been updated by these amounts.

Our audit work identified a small number of other matters:

- The Council do not have an in-built journals authorisation process in place. This means that users can post and authorise their own journals. A mitigating detective control exists wherein all journals above £25,000 posted in a month are reviewed by principal accountants in subsequent month has been put in place. Our testing of this control identified that this control did not operate as designed and the retrospective review was not undertaken until September 2023, once the evidence was requested. We have raised a recommendation to ensure that this key control operates as designed and is completed on a timely basis.
- As part of PPE work we noted that the valuation for Phoenix House, included in the financial statements was incorrect. This was due to the valuer not updating the rounding figure that was subsequently included in the Council fixed asset register. The value should have been £3.750m but was rounded in error to £3.550m. We are satisfied that this is an isolated error.

More detailed findings are set out in our Audit Findings Report, which was presented to the Council's Audit Committee on 30 April 2024. Requests for this Audit Findings Report should be directed to the Council.

Appendices

Appendix A: Responsibilities of the Council

Public bodies spending taxpayers' money are accountable for their stewardship of the resources entrusted to them. They should account properly for their use of resources and manage themselves well so that the public can be confident.

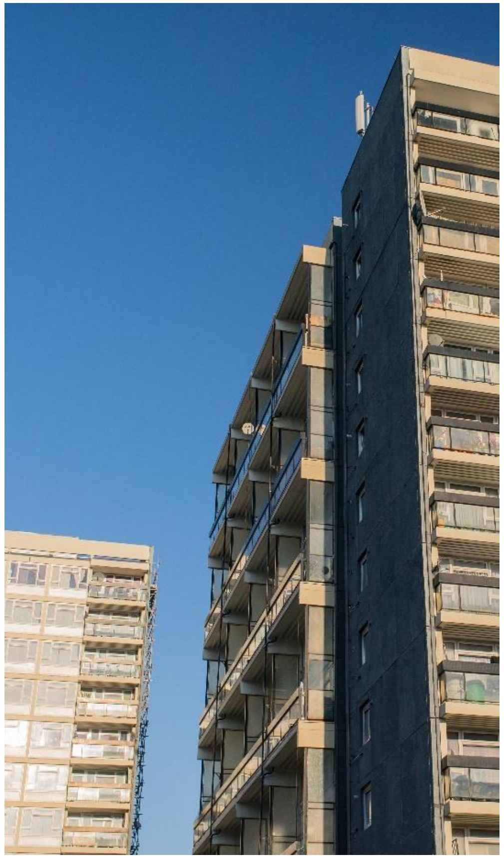
Financial statements are the main way in which local public bodies account for how they use their resources. Local public bodies are required to prepare and publish financial statements setting out their financial performance for the year. To do this, bodies need to maintain proper accounting records and ensure they have effective systems of internal control.

All local public bodies are responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness from their resources. This includes taking properly informed decisions and managing key operational and financial risks so that they can deliver their objectives and safeguard public money. Local public bodies report on their arrangements, and the effectiveness with which the arrangements are operating, as part of their annual governance statement.

The Chief Financial Officer (or equivalent) is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Chief Financial Officer (or equivalent) determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Chief Financial Officer (or equivalent) is required to prepare 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. In preparing the financial statements, the Chief Financial Officer (or equivalent) is responsible for assessing the Council's ability to continue as a going concern and use the going concern basis of accounting unless there is an intention by government that the services provided by the Council will no longer be provided.

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 review regularly the adequacy and effectiveness of these arrangements.



Appendix B:
An explanatory note on recommendations

A range of different recommendations can be raised by the Council's auditors as follows:

Type of recommendation	Background	Raised within this report	Page reference(s)
Statutory	Written recommendations to the Council under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014.	No	n/a
Key	The NAO Code of Audit Practice requires that where auditors identify significant weaknesses as part of the Council's arrangements to secure value for money they should make recommendations setting out the actions that should be taken by the Council. We have defined these recommendations as 'key recommendations'.	Yes	Pages 8 and 9
Improvement	These recommendations, if implemented, should improve the arrangements in place at the Council, but are not a result of identifying significant weaknesses in the Council's arrangements.	Yes	Pages 27, 31 and 35.

Grant Thornton

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