

Forest Heath District Council

Audit Committee Summary

For the year ended 31 March 2014

Audit Results Report – ISA (UK & Ireland) 260

12 September 2014



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Executive summary

Key findings

Audit results and other key matters

The Audit Commission's Code of Audit Practice (the Code) requires us to report to those charged with governance on the work we have carried out to discharge our statutory audit responsibilities together with any governance issues identified.

This report summarises the findings from the 2013/14 audit which is substantially complete. It includes the messages arising from our audit of your financial statements and the results of the work we have undertaken to assess your arrangements to secure value for money in your use of resources.

Financial statements

- ▶ As of 12 September 2014, we expect to issue an unqualified opinion on the financial statements. Our audit work raised a number of queries which resulted in amendments to the accounts. These were mainly classification adjustments which have all been agreed and amended by officers. We therefore have few matters to bring to your attention although we have still to fully complete work in a number of areas.

Value for money

- ▶ We expect to conclude that you have made appropriate arrangements to secure economy, efficiency and effectiveness in your use of resources.

Whole of Government Accounts

- ▶ We expect to issue an unqualified confirmation to the National Audit Office (NAO) regarding the Whole of Government Accounts submission.

Audit certificate

- ▶ The audit certificate is issued to demonstrate that the full requirements of the Audit Commission's Code of Audit Practice have been discharged for the relevant audit year. We expect to issue the audit certificate at the same time as the audit opinion.

Extent and purpose of our work

The Council's responsibilities

The Council is responsible for preparing and publishing its Statement of Accounts, accompanied by the Annual Governance Statement. In the Annual Governance Statement, the Council reports publicly on the extent to which it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Purpose of our work

Our audit was designed to:

- Express an opinion on the 2013/14 financial statements
- Report on any exception on the governance statement or other information included in the foreword
- Consider and report any matters that prevent us being satisfied that the Council had put in place proper arrangements for securing economy, efficiency and effectiveness in the use of resources (the Value for Money conclusion)

In addition, this report contains our findings related to the areas of audit emphasis, our views on the Council's accounting policies and judgments and significant deficiencies in internal control.

As a component auditor, we also follow the group instructions and send to the National Audit Office our group assurance certificate, audit results report and auditor's report on the consolidation schedule.

This report is intended solely for the information and use of the Council. It is not intended to be and should not be used by anyone other than the specified party.

Addressing audit risks

Significant audit risks

We identified the following audit risks during the planning phase of our audit, and reported these to you in our Audit Plan. Here, we set out how we have gained audit assurance over those issues.

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
Significant audit risks (including fraud risks)		
<p>1. As identified in ISA (UK & Ireland) 240, management is in a unique position to perpetrate fraud because of their ability to directly or indirectly manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p> <p>For district council's the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.</p>	<ul style="list-style-type: none"> We tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements; We reviewed accounting estimates for evidence of management bias; We evaluated the business rationale for any significant unusual transactions; and We reviewed capital expenditure on property, plant and equipment to ensure it met the relevant accounting requirements to be capitalised. 	<ul style="list-style-type: none"> We did not identify any material instances of fraud or error.
<p>2. There have been significant changes in the arrangements for business rate arrangements from April 2013. The detailed accounting arrangements for the new arrangement are not yet clear and this therefore presents a risk in terms of the financial statements.</p> <p>One of the main changes is that individual councils now need to provide for rating appeals. This includes not only claims from 1 April 2013 but claims that relate to earlier periods. As appeals are made to the Valuation Office, Councils may not be aware of the level of claims. Council's may also find it difficult to obtain sufficient information to establish a reliable estimate.</p>	<ul style="list-style-type: none"> We reviewed the detailed accounting for business rates to ensure the Council's accounts are materially accurate and compliant with the CIPFA Code of practice; and We reviewed the Councils provision for business rate appeals to ensure it was calculated on a reasonable basis in line with IAS37. We ensured the provision was supported by appropriate evidence and that the level of estimation uncertainty was adequately disclosed in the accounts. 	<ul style="list-style-type: none"> Our audit work confirmed that the accounting treatment adopted by the Council for business rates was appropriate and in compliance with the CIPFA Code of Practice. The business rates appeals provision accounted for by the Council was deemed to have been calculated on a reasonable basis in line with the requirements of IAS 37. The Council have amended their accounts to provide additional disclosure on the level of estimation and uncertainty with this provision, in particularly providing an estimate on what a "worst case" provision may be for the whole rateable value population, taking account of appeals not lodged.

Addressing audit risks

Significant audit risks

We identified the following audit risks during the planning phase of our audit, and reported these to you in our Audit Plan. Here, we set out how we have gained audit assurance over those issues.

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
Significant audit risks (including fraud risks) continued		
<p>3. Our planning work has identified that the Council is undertaking a significant general ledger upgrade to align itself with St Edmundsbury Borough Council as part of the Council's commitment to joint working and sharing key financial systems and processes. This presents a risk in terms of the completeness and accuracy of data transfer between the two systems.</p>	<ul style="list-style-type: none"> We utilised the work of internal audit as much as possible; We reviewed the integrity of the Agresso upgrade; and We performed additional early work on the relevant systems and key processes, the outcome of which fed into our testing strategy. 	<ul style="list-style-type: none"> Our review of the work of Internal Audit, as well as our own work on the general ledger system did not raise any issues over the completeness and integrity of the data transferred to the new system.
<p>4. The Council is the lead organisation for the proposed Home of Horseracing Trust (HoHT) project in Newmarket. This is a capital project to be funded by donations via the HoHT, national lottery monies and contributions from the Council. The project aims to restore the Palace House, Stables and Mews to form an educational and cultural racing heritage centre for ex race horses.</p> <p>5. Due to the size and nature of the scheme this represents potential material risk to the Council in a number of areas including abortive costs, incorrect recovery of VAT, incorrect recording of, and accounting for, transactions associated with the asset in the financial statements.</p>	<ul style="list-style-type: none"> We have undertaken a detailed review of the lease arrangements ensuring that accounting treatment is in line with applicable accounting standards and SORP requirements; We have ensured that disclosures within the financial statements are in line with expectations; and We considered the tax planning aspects 	<ul style="list-style-type: none"> Our review work is now complete. We have no issues to bring to the attention of Members.

Financial statements audit

Issues and misstatements arising from the audit

Progress of our audit

- ▶ The following areas of our work programme are in progress, but remain to be completed. We will provide an update of progress at the Performance and Audit Scrutiny Committee meeting:
 - ▶ Aspects of disclosure notes
 - ▶ Completion of debtors testing
 - ▶ Payables
 - ▶ Collection fund
 - ▶ Payroll disclosures
 - ▶ Whole of Government Accounts (WGA)
 - ▶ Receipt of a Letter of Representation
 - ▶ Director final review of audit work and financial statements
- ▶ Subject to the satisfactory resolution of the above items, we propose to issue an unqualified audit report on the financial statements.

Uncorrected Misstatements

- ▶ We have identified 1 error within the draft financial statements which management have chosen not to adjust. This error is brought forward from 2011/12.

We request that this uncorrected misstatement be corrected or a rationale as to why it is not corrected be considered and approved by the Performance and Audit Scrutiny Committee and provided within the Letter of Representation. Appendix 1 to this report sets out the uncorrected error.

Corrected Misstatements

Our audit identified several errors which the audit team have highlighted to management for amendment. All of these have been adjusted during the course of our work. We bring to your attention one amendment which is considered significant. This relates to £5.9million which was reclassified from cash and cash equivalents to short term investments.

Other Matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we are required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Council's financial reporting process including the following:

- ▶ Qualitative aspects of your accounting practices; estimates and disclosures;
- ▶ Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions; and,
- ▶ Any significant difficulties encountered during the audit; and
- ▶ Other audit matters of governance interest, We have no matters we wish to report.

Financial statements audit (continued)

Internal Control, Written Representations & Whole of Government Accounts

Internal Control

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

We have performed a substantive audit approach this year, and have therefore not tested the controls of the Council. We are not expressing an opinion on the overall effectiveness of internal control.

We have reviewed the Annual Governance Statement and can confirm that:

- ▶ It complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
- ▶ It is consistent with other information that we are aware of from our audit of the financial statements.

We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements of which you are not aware.

Request for written representations

We have requested a management representation letter to gain management's confirmation in relation to a number of matters, for which we do not currently have sufficient audit evidence. There were no additional specific representations required other than the standard representations.

Whole of Government Accounts

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the National Audit Office.

We are currently concluding our work in this area and will report any matters that arise to the Audit and Governance Committee.

Arrangements to secure economy, efficiency and effectiveness

The Code of Audit Practice (2010) sets out our responsibility to satisfy ourselves that Forest Heath District Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. In examining the Council's corporate performance management and financial management arrangements, we have regard to the following criteria and focus specified by the Audit Commission.

Criteria 1 - Arrangements for securing financial resilience

- ▶ *“Whether the Council has robust systems and processes to manage financial risks and opportunities effectively, and to secure a stable financial position that enables it to continue to operate for the foreseeable future”*
- ▶ We did not identify any significant risks in relation to this criteria.
- ▶ We have completed our work and plan to issue an unqualified value for money conclusion in relation to the Council's financial resilience. We do have some issues to report to those charged with Governance, as set out on the next page of this report.

Criteria 2 - Arrangements for securing economy, efficiency and effectiveness

- ▶ *“Whether the Council is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.”*
- ▶ We did not identify any significant risks in relation to this criteria.
- ▶ We have no issues to report in relation to this criteria

Arrangements to secure economy, efficiency and effectiveness (continued)

Financial resilience

Along with many other Council's, Forest Heath is facing significant financial challenges over the next three to four years.

The Council's external funding sources are reducing and are subject to change and uncertainty in future years. Some of the main areas of uncertainty relate to:

- ▶ Future levels of business rates income
- ▶ Future funding through the New Homes Bonus
- ▶ Level of Government funding through the Revenue Support Grant (RSG) and Baseline Funding (business rates)

The Council is acutely aware of the challenges it faces and is continually at looking at ways in which services can be provided more efficiently and effectively over the coming years. Officers are also considering how the Council can generate income by operating on a more commercial basis.

The Council has a good track record of delivering savings and meeting its budget and good progress has already been made on identifying savings to bridge the budget gap of around £1.1 million in 2015-16.

The Council's financial forecasts that have been reported to Members make clear the scale of the challenge being faced. Some of the key issues reported include:

- The Council has a cumulative budget gap of around £2.3 million over the next 4 years (to 2017-18) which will need to be bridged through savings and efficiencies or increased income.
- Over the past four successive years, Forest Heath has frozen its council tax in recognition of the difficult times faced by many of the Council's residents.

In light of the future financial pressures the Council is facing, Members need to consider carefully the impact of any decisions to freeze or reduce council tax or use reserves to support the Council's finances, on the ongoing sustainability of the Council's financial position and its ability to maintain service levels in future years.

Independence and audit fees

Independence

- ▶ We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated April 2014.
- ▶ We complied with the Auditing Practices Board's Ethical Standards for Auditors and the requirements of the Audit Commission's Code of Audit Practice and Standing Guidance. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.
- ▶ We confirm that we are not aware of any relationships that may affect the independence and objectivity of the firm that we are required by auditing and ethical standards to report to you.
- ▶ We consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you consider the facts of which you are aware and come to a view.

If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the Performance and Audit Scrutiny Committee on 25 September 2014.

- ▶ We confirm that we have met the reporting requirements to the Performance and Audit Scrutiny Committee, as 'those charged with governance' under International Standards on Auditing (UK&I) 260. Our communication plan to meet these requirements were set out in our Audit Plan of April 2014.

Audit fees

The table below sets out the scale fee and our final proposed audit fees.

	Proposed final fee 2013-14	Scale fee 2013-14	Variation comments
	£s	£s	
Total audit fee – Code work	61,845	61,845	Final fee to be confirmed.
Certification of claims and returns	23,700	23,700	No change proposed, however claims work is still in progress.
Home of Horse Racing Trust	3,345	N/A	Estimated scale fee variation for additional work agreed by management.

Independence and audit fees

- ▶ At present, our proposed final fee is in line with the scale fee. However, we have undertaken more work than anticipated in agreeing financial statement disclosures. We have also spent extra time in understanding the audit trail which supported the financial statements following the change in the general ledger and also tracking through all the amendments to the draft accounts, either from our audit work or those subsequently identified from the Council.
- ▶ We will need to consider the impact of this extra work on our final audit fee when we complete our work. Should we need to vary the final fee, we will discuss this with the Chief Financial Officer and report any variations to the Performance and Audit Scrutiny Committee.
- ▶ We confirm that we have not undertaken any non-audit work outside of the Audit Commission's Audit Code requirements.

Appendix 1 - Unadjusted Audit Errors

The following adjustments, which are greater than our trivial level, and less than our tolerable error, have been identified during the course of our audit.

These adjustments have not been made by management within the revised financial statements

Item of Account	Nature of Error Description	Error Type F, P, J	Statement of Comprehensive Income & Expenditure		Balance Sheet	
			Debit	(Credit)	Debit	(Credit)
General Fund	As noted in the 2011/12 AGR, the Authority has not valued an element of its property, plant and equipment in accordance with the Code of Practice on Local Authority Accounting ('the Code') by erroneously including Adjudication costs in its valuation. These costs are 'abnormal costs' which are not directly attributable to bringing the asset into use and so should be reported as a cost of service. £394k has been capitalised in previous years.	F			394,000	
Capital Receipts Reserve	As above	F				(394,000)
Balance sheet totals					394,000	(394,000)
Income effect of corrected adjustments						
Cumulative effect of uncorrected misstatement					394,000	(394,000)

Key

- ▶ F – Factual error
- ▶ P – Projected error based on audit sample error and population extrapolation
- ▶ J – Judgemental error

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In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

