

# Forest Heath District Council

Annual Audit Letter for the year ended 31 March 2017

October 2017

Ernst & Young LLP

## Contents

<b>Executive Summary</b> .....	<b>2</b>
<b>Purpose</b> .....	<b>5</b>
<b>Responsibilities</b> .....	<b>7</b>
<b>Financial Statement Audit</b> .....	<b>10</b>
<b>Value for Money</b> .....	<b>16</b>
<b>Other Reporting Issues</b> .....	<b>19</b>
<b>Focused on your future</b> .....	<b>22</b>
<b>Appendix A    Audit Fees</b> .....	<b>24</b>

Public Sector Audit Appointments Ltd (PSAA) have issued a “Statement of responsibilities of auditors and audited bodies”. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psaa.co.uk](http://www.psaa.co.uk))

The Statement of responsibilities serves as the formal terms of engagement between 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 “Terms of Appointment (updated 23 February 2017)” issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter 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.

A hand with white nail polish is writing on a document with a blue pen. In the background, there is a calculator, a laptop, and a white mug. A yellow rectangular box is overlaid on the left side of the image.

## Executive Summary

## Executive Summary

We are required to issue an annual audit letter to Forest Heath District Council (the Council) following completion of our audit procedures for the year ended 31 March 2017.

Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
<b>Opinion on the Council's:</b> ▶ Financial statements	Unqualified - the financial statements give a true and fair view of the financial position of the Council as at 31 March 2017 and of its expenditure and income for the year then ended.
▶ Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Statement of Accounts.
<b>Concluding on the Council's arrangements for securing economy, efficiency and effectiveness</b>	We concluded that you have put in place proper arrangements to secure value for money in your use of resources.

Area of Work	Conclusion
<b>Reports by exception:</b>	
▶ Consistency of Governance Statement	The Annual Governance Statement was consistent with our understanding of the Council.
▶ Public interest report	We had no matters to report in the public interest.
▶ Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Area of Work	Conclusion
<b>Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).</b>	The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the consolidation pack.

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 7 September 2017.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 22 September 2017.

In January 2017 we will also issue a report to those charged with governance of the Council summarising the certification work we have undertaken.

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Mark Hodgson

Associate Partner  
For and on behalf of Ernst & Young LLP

Purpose



## Purpose

### **The Purpose of this Letter**

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2016/17 Audit Results Report to the 21 September 2017 Performance and Audit Scrutiny Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.



# Responsibilities



## Responsibilities

### Responsibilities of the Appointed Auditor

Our 2016/17 audit work has been undertaken in accordance with the Audit Plan that we issued on 10 March 2017 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
  - ▶ On the 2016/17 financial statements; and
  - ▶ On the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
  - ▶ If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - ▶ Any significant matters that are in the public interest;
  - ▶ Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - ▶ If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the return.

## **Responsibilities of the Council**

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned 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.

# Financial Statement Audit



## Financial Statement Audit

### Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 22 September 2017.

Our detailed findings were reported to the 21 September 2017 Performance and Audit Scrutiny Committee.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
<p><b>Revenue Recognition</b></p> <p>Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue.</p> <p>In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.</p> <p>One area susceptible to manipulation is the capitalisation of revenue expenditure on Property, Plant and Equipment given the extent of the Council's Capital programme.</p>	<p>We did not identify any material weaknesses in the recognition of revenue.</p> <p>We did not identify any instances of inappropriate judgements or estimates being applied.</p>

Significant Risk	Conclusion
<p><b>Management override of controls</b>                      As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and to prepare fraudulent financial statements by overriding controls that otherwise seem to be operating effectively.</p> <p>We identify and respond to this fraud risk on every audit engagement.</p>	<p>We did not identify any material weaknesses in controls or evidence of material management override.</p> <p>We did not identify any instances of inappropriate judgements being applied.</p> <p>We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business.</p>
<p><b>Purchase of Greenheath Energy Ltd</b>                      The Council has purchased Greenheath Energy Ltd along with the associated solar farm for £14 million.</p> <p>The Council planned to transfer the company's assets and liabilities into the Council's Balance sheet, leaving Greenheath Energy Ltd as a dormant company.</p> <p>Due to the material nature and complexity of these transactions, there is a significant risk that the accounting treatment and entries in the Council's financial statements could be materially misstated.</p>	<p>The acquisition of Greenheath Energy was a complex transaction with a significant number of accounting entries to reflect the acquisition.</p> <p>Our audit work provided us with sufficient assurance over the accounting transactions and valuation for opinion purposes. However, we identified the following matters:</p> <p><u>Accounting Transactions</u>                      We identified one unadjusted misstatement of £75,000 relating to retention money, as a result of the acquisition, being included within Creditors, when the balance had been paid before the 31 March 2017. Officers chose not to amend the financial statements for this item.</p> <p><u>Valuation basis</u>                      The Council's valuation utilised the income approach, specifically by capitalising the net income received over the six months leading up to the valuation date into perpetuity. We employed our internal EY Valuation team and based on a corroborative review of calculations using the Council's Financial Model and recent market transactions, the Council's adopted project value of £14.15 million for the Solar Farm as at the 31 March 2017 sat within a reasonable range (£14.02 to £15.28 million).</p>

Other Key Findings	Conclusion
<p><b>Financial Statements Presentation</b></p> <p>Amendments have been made to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the Code) changing the way the financial statements are presented.</p> <p>The new reporting requirements impact the Comprehensive Income and Expenditure Statement (CIES) and the Movement in Reserves Statement, and include the introduction of a new Expenditure and Funding Analysis note as a result of the 'Telling the Story' review of the presentation of local authority financial statements.</p>	<p>We identified misstatements in regards to the treatment of overhead recharges which were corrected by management. The improper treatment of recharges led to the overstatement of total income and expenditure of net cost of services within the CIES and accompanying notes for the 2016/17 figures and 2015/16 comparatives.</p>
<p><b>Property, plant and equipment</b></p> <p>Property, Plant and Equipment represent a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges.</p> <p>Material judgemental inputs and estimation techniques are required to calculate the year-end fixed assets balances held in the balance sheet.</p> <p>The Council will engage an external expert valuer who will apply a number of complex assumptions. Annually assets are assessed to identify whether there is any indication of impairment.</p> <p>As the Council's asset base is significant, and the outputs from the valuer are subject to estimation, there is a risk fixed assets may be under/overstated or the associated accounting entries incorrectly posted.</p>	<p>We assessed and were satisfied with the competency and objectivity of the Council's valuer, the District Valuer.</p> <p>We undertook appropriate audit procedures to verify and critically challenge the basis of valuation adopted by the valuer in relation to the Council's fixed assets. We did not identify any issues that we need to report to you.</p>

Other Key Findings	Conclusion
<p><b>Pensions Liability - IAS19</b></p> <p>The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding the Local Government Pension Scheme (LGPS) in which it is an admitted body.</p> <p>The Council's current pension fund deficit is a material and sensitive item and the Code requires that this liability be disclosed on the Council's balance sheet. Accounting for this scheme involves significant estimation and judgement.</p> <p>The information disclosed is based on the IAS 19 report issued to the Council by the actuary to the administering body.</p>	<p>Assumptions used by the actuary and adopted by the Council are considered to be generally acceptable. The sensitivities surrounding these assumptions were correctly disclosed in Note 3 to the financial statements.</p> <p>We did not identify any misstatements in completing our work over the Council's pension liability, related balances and disclosures.</p>

## Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	We determined planning materiality to be £0.70 million, which is 2% of gross revenue expenditure on services reported in the group accounts of £35.1 million. We consider gross revenue expenditure on services to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.
Reporting threshold	We agreed with the Performance and Audit Scrutiny Committee that we would report to the Committee all audit differences in excess of £35,000.

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- Remuneration disclosures - reduced materiality level of £5,000 applied in line with bandings disclosed.
- Related party transactions, members' allowances and exit packages - reduced materiality level applied equal to the reporting threshold.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.



A close-up, shallow depth-of-field photograph of a stack of coins. The coins are stacked vertically, with some showing their edges and others showing their faces. The lighting is warm, highlighting the metallic texture and the ridges on the edges. A bright yellow rectangular box is overlaid on the left side of the image, containing the text "Value for Money".

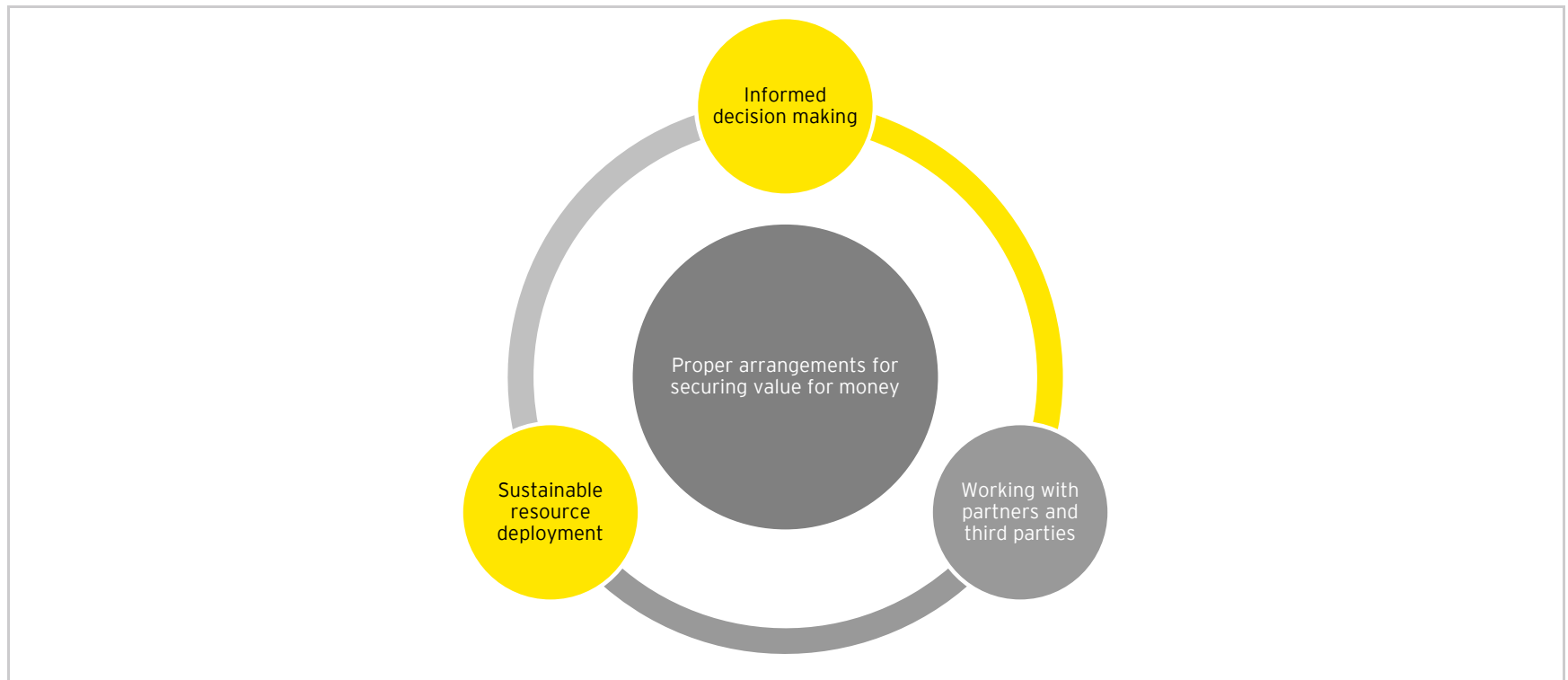
Value for Money

## Value for Money

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.



We identified one significant risks in relation to these arrangements. The table below presents the findings of our work in response to this risk.

We have performed the procedures outlined in our audit plan. We did not identify any significant weaknesses in the Authority's arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We therefore issued an unqualified value for money conclusion on 22 September 2017.

Significant Risk	Conclusion
<p><b>Purchase of Greenheath Energy Ltd</b></p> <p>The Council purchased Greenheath Energy Ltd and the associated solar farm with a view to providing energy at reduced rates throughout the district.</p> <p>Given that this is an unusual transaction, the Council's governance arrangements surrounding the business case to proceed with the acquisition should be adequate to ensure that these decisions are based on a sound assessment of the value for money that this strategy provides to the Council.</p>	<p>We undertook the following procedures:</p> <ul style="list-style-type: none"><li>▶ Review of the Council's business case for the transaction;</li><li>▶ Review of the Council's governance arrangements around the transactions; and</li><li>▶ Consideration of the impact on the Council's medium term financial position (MTFP).</li></ul> <p>The Council have taken appropriate advice at all stages. Due diligence reviews have been carried out at every stage, using a number of independent experts, in order to mitigate the risk associated with such a transaction. Our review of the Council's business case for these transactions, the governance arrangements put in place and the impact of the transaction on the Council's MTFP did not identify any significant matters.</p>



## Other Reporting Issues

## Other Reporting Issues

### Whole of Government Accounts

The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the consolidation pack.

### Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern.

### Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

### Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.

### Objections Received

We did not receive any objections to the 2016/17 financial statements from member of the public.

### Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

## **Independence**

We communicated our assessment of independence in our Audit Results Report to the Performance and Audit Scrutiny Committee on 21 September 2017. 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 regulatory and professional requirements.

## **Control Themes and Observations**

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

Our audit did not identify any controls issues to bring to the attention of the Performance and Audit Scrutiny Committee.

A close-up photograph of a person's face as they look through a pair of black binoculars. The person's eyes are focused on the lenses, and their hands are visible holding the device. The background is a soft, out-of-focus white. A bright yellow rectangular box is overlaid on the left side of the image, containing the text "Focused on your future".

Focused on your  
future

## Focused on your future

Area	Issue	Impact
<p><i>Earlier deadline for production and audit of the financial statements from 2017/18</i></p>	<p>The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. From that year the timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the audited accounts by 31 July.</p>	<p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p> <p>To prepare for this change the Council has reviewed and amended the closedown process to achieve draft accounts production by 31 May for 2016/17.</p> <p>We will work with the Council to engage early, to facilitate early substantive testing for 2017/18 and consider other steps the Council can take.</p>
<p><i>Forthcoming changes to accounting standards:</i></p> <p><i>IFRS 9 Financial Instruments</i></p> <p><i>IFRS 15 Revenue from Contracts with Customers</i></p> <p><i>IFRS 16 Leases</i></p>	<p>Revised accounting standards are expected to be applicable for local authority accounts from the 2018/19 (IFRS 9 and IFRS15) and 2019/20 financial year (IFRS 16).</p> <p>Transitional arrangements are included within the accounting standard, however as the 2018/19 and 2019/20 Accounting Code of Practice for Local Authorities have yet to be issued it is unclear what the impact on local authority accounting will be and whether any accounting statutory overrides will be introduced to mitigate any impact.</p>	<p>Some initial thoughts on the approach to adopting IFRS 9 and IFRS 15 have been issued by CIPFA, but until the Code is issued and any statutory overrides are confirmed there remains some uncertainty.</p> <p>For IFRS 16, it is clear is that the Council will need to undertake a detailed exercise to classify all of its leases and therefore must ensure that all lease arrangements are fully documented</p>



**Appendix A**

# **Audit Fees**



## Appendix A     Audit Fees

Our fee for 2016/17 is in line with the scale fee set by the Public Sector Audit Appointments Ltd (PSAA) and reported in our 7 September 2017 Audit Results Report.

Description	Final Fee 2016/17 £'s	Planned Fee 2016/17 £'s	Scale Fee 2016/17 £'s	Final Fee 2015/16 £'s
<b>Total Audit Fee - Code work (See Note 1)</b>	56,309	47,059	47,059	47,059
<b>Total Audit Fee - Certification of claims and returns</b>	TBC	15,203	15,203	12,442

Note 1: Our actual fee is £9,250 higher than the scale fee set by the Public Sector Audit Appointments (PSAA Ltd) due to additional work required to review the valuation and accounting transactions in relation to the acquisition of Greenheath Energy Ltd. The additional procedures required to gain sufficient assurance for opinion purposes were set out in our Audit Results Report. These additional fees are subject to final agreement with PSAA.

Our planned fee for the certification of claims and returns is based on the indicative scale fee set by the PSAA. The final fee will be reported to you in our annual certification report, upon completion of this work.

We confirm we have not undertaken any non-audit work outside of the PSAA's requirements.

EY | Assurance | Tax | Transactions | Advisory

Ernst & Young LLP

© Ernst & Young LLP. Published in the UK.  
All Rights Reserved.

ED None

The UK firm Ernst & Young LLP is a limited liability partnership registered in England and Wales with registered number OC300001 and is a member firm of Ernst & Young Global Limited.

Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

[ey.com](https://www.ey.com)