

Harlow District Council

Audit & Standards Committee Summary

For the year ended 31 March 2015

Audit Results Report – ISA (UK and Ireland) 260

September 2015



Building a better
working world

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Section 1

Executive summary

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 – the Audit and Standards Committee – 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 2014/15 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 9 September 2015, we expect to issue an unqualified opinion on the financial statements. Our audit results demonstrate, through the few matters we have to communicate, that the Council has prepared its financial statements well. The Council has strengthened capacity in its finance team and we have been able to complete the audit within a shorter timeframe than in previous years. This places the Council in a good position in preparation for the earlier statutory deadline of the end of July in 2017/18.

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

- ▶ 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. We have not yet completed our work on your Whole of Government Accounts return. However, we do not expect to identify any significant matters which will require reporting to the NAO.

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 along with our opinion on the financial statements once we have completed our work on the Whole of Government Accounts return.

Section 2

Extent and purpose of our work

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 2014/15 financial statements and the consistency of other information published with them
 - ▶ Report on an exception basis on the Annual Governance Statement
 - ▶ 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)
 - ▶ Discharge the powers and duties set out in the Audit Commission Act 1998 and the Code of Audit Practice

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

As a component auditor, we also follow the NAO group instructions and report the results on completion of the WGA work through the Assurance Statement to the NAO and to the Council.

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.

Section 3

Addressing audit risks

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.

A significant audit risk in the context of the audit of the financial statements is an inherent risk with both a higher likelihood of occurrence and a higher magnitude of effect should it occur and which requires special audit consideration. For significant risks, we obtain an understanding of the entity's controls relevant to each risk and assess the design and implementation of the relevant controls.

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
<p>Property asset valuation and accounting</p> <p>The Council undertakes an annual exercise to revalue property assets (including its social housing stock and investment property assets). The Council has also undertaken a specific exercise in 2014/15 to revalue its garage stock. This has resulted in a significant change to both the value of those garages, and their estimated useful life.</p> <p>The valuation of property assets represents a significant accounting estimate. The accounting entries arising from changes in value are complex and will have a significant impact on the Council's financial statements. The Council's Fixed Asset Register is unable to calculate the accounting entries arising from changes in the valuation of these assets. The Council is therefore reliant on excel-based spreadsheets to manually calculate the accounting entries, using data provided by the Council's valuer and historic data recorded on the Council's Fixed Asset Register.</p> <p>Taken together, these factors present a significant risk to the financial statements, and we will undertake specific testing to address this risk.</p>	<ul style="list-style-type: none"> ▶ Assessed the reliability of management's experts (placing reliance on our own valuation specialists where necessary). ▶ Tested the evidence underpinning changes in the valuation of property, plant & equipment. ▶ Tested the accounting treatment applied to changes in the valuation of property assets. 	<p>We have completed our testing in this area.</p> <p>We found that we could place reliance on the work undertaken by management's expert, that there was appropriate evidence underpinning changes in the valuation of property, plant and equipment, and that changes in the valuation had been accounted for correctly.</p> <p>We have no matters to report to you as a result of our work in this area.</p>

Addressing audit risks – significant audit risks (cont'd)

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
<p>Fraud Risks (Risk of Management Override)</p> <p>As identified in ISA (UK and 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.</p> <p>Given the extent of the Council's capital programme, an area particularly susceptible to manipulation is the capitalisation of revenue expenditure on property, plant and equipment.</p>	<ul style="list-style-type: none"> ▶ Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. ▶ Reviewed and tested estimates made in relation to pensions, appeals against the rateable value on business properties, and the valuation of and depreciation charges on property, plant and equipment. ▶ Evaluated the business rationale for any significant unusual transactions. ▶ Sample tested additions to property, plant and equipment to ensure they are properly classified as capital expenditure 	<p>We have completed our testing in this area. We found that journal entries recorded in the general ledger and other adjustments made in the preparation of the accounts were appropriate.</p> <p>We have reviewed the estimates made by management when preparing the financial statements and concluded they were appropriate. We found no evidence of management bias.</p> <p>We did not identify any significant or unusual transactions.</p> <p>We tested a sample of additions to property , plant and equipment and found that the expenditure was correctly classified as capital expenditure.</p>

Addressing audit risks – other 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
Group Accounting Standards		
<p>The 2014/15 CIPFA Code of Practice introduces new accounting practices in relation to:</p> <ul style="list-style-type: none"> • The specification of new control criteria under IFRS 10 (consolidated financial statements); • New classification requirements for joint arrangements under IFRS 11 (joint arrangements); and • The requirements of the new disclosures standard IFRS 12 (disclosures of interests in other entities). <p>The Council will therefore need to assess its group relationships in line with the new standards and as a result associated group boundary changes may need to be reflected in the accounts.</p>	<p>We reviewed management’s assessment of the group boundary against the requirements of the Code and International Financial Reporting Standards (IFRS), focussing in particular on the Council’s relationship with Kier Harlow.</p>	<p>We agreed with management’s assessment that the Council’s arrangement with Kier Harlow does not give it control over Kier Harlow, and that it was therefore not required to prepare group accounts under IFRS 11.</p> <p>We extended the assessment to consider whether the Council’s arrangement with Kier Harlow meant that the entity met the definition of an associate under IFRS 10. We concluded that the entity is an associate of the Council, but on the grounds of materiality there is no requirement for the Council to prepare group accounts. The Council has amended Note 2 to the financial statements to reflect this assessment.</p>

Section 4

Financial statements audit – issues and findings

Financial statements audit – issues and misstatements arising from the audit

Progress of our audit

- ▶ The following areas of our work programme remain to be completed. We will provide an update of progress at the Audit Committee meeting:
 - ▶ Complete our testing on the payment of housing benefits
 - ▶ Complete our testing on the Non-Domestic Rates appeals provision
 - ▶ Complete our testing on journal entries
 - ▶ Receipt of a Letter of Representation
 - ▶ Final Director review, closing procedures and sign off
- ▶ 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 one misstatement within the draft financial statements, which management has chosen not to adjust.
- ▶ We ask the Audit and Standards Committee to consider approving management's rationale as to why these corrections have not been made and, if approved, include this in the Letter of Representation.
- ▶ Appendix A to this report sets out the uncorrected misstatement.

Corrected misstatements

- ▶ Our audit also identified a limited number of disclosure matters which were highlighted to management for amendment. All of these have been adjusted during the course of our work. Details of the most significant of these are set out at Appendix B to this report.

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 Authority'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;
 - ▶ Any significant difficulties encountered during the audit; and
 - ▶ Other audit matters of governance interest

We have no matters that we wish to report to you.

Financial statements audit – application of materiality

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		Amount (£)
Planning Materiality	<p>We set planning materiality at 2% of gross expenditure of £138.281 million. Gross expenditure was calculated based on the cost of services as reported in the Comprehensive Income and Expenditure Statement, plus:</p> <ul style="list-style-type: none"> • Payments to housing capital receipts pool (£2.955 million) • Interest payable (£7.159 million) • Pensions Interest Cost (£3.684 million) <p>We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p>	£3.041 million (2014: £2.117 million)
Tolerable Error	<p>We set a tolerable error for the audit. Tolerable error is the application of planning materiality at the individual account or balance level. It is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds planning materiality. The level of tolerable error drives the extent of detailed audit testing required to support our opinion.</p> <p>We have set tolerable error at the lower level of the available range as we identified material errors in the Council's 2013/14 financial statements .</p>	
Reporting Threshold	We have set the threshold at which we report audit differences to the Committee at £0.152 million.	£0.152 million (2014: £0.105 million)

Financial statements audit – application of materiality (continued)

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:

Item	Strategy applied
Remuneration disclosures including any severance payments, exit packages and termination benefits	Our audit strategy was to check the bandings reported in Note 31 of the financial statements, test the completeness of the disclosure and compliance with the Code requirements. We sample checked transactions back to the payroll system and supporting documentation.
Related party transactions.	Our audit strategy was to obtain and review declarations from senior officers and members of the Council and review for any material disclosures. We also confirmed that the disclosure in Note 35 complied with the Code requirements. We undertook a sample check of contracts included on the Council's contracts register against Companies House records to identify whether any key decision makers within the Council had an interest in the companies with which the Council had contracts.
Members allowances	Our audit strategy was to test the completeness of the disclosures within Note 30 and make sure that the disclosure was compliant with the Code by sample checking transactions back to the payroll system.

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

Financial statements audit – internal control, written representations and 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 not tested the controls of the Corporation as we have adopted a fully substantive approach to our audit, as we have assessed this as the most efficient approach. We are therefore 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. We have not requested any specific representations from the Council that are not part of our standard representations.

Whole of Government Accounts

- ▶ 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 extent of our review and the nature of our report are specified by the National Audit Office.
- ▶ We have not yet completed our work on your Whole of Government Accounts return. We do not expect to identify any issues that will require us to report to the NAO. We will report any matters that arise to the next meeting of the Audit Committee.

Section 5

Arrangements to secure economy, efficiency and effectiveness

Arrangements to secure economy, efficiency and effectiveness

The Code of Audit Practice (2010) sets out our responsibility to satisfy ourselves that Harlow 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 Authority 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, but did identify financial resilience as an area that we would consider in more detail as part of our value for money conclusion. We have undertaken a review of the medium term financial plan and the assumptions included within it. We have also assessed the level of reserves (both general fund and earmarked) that the Council has at the 31 March 2015. Our findings and conclusions from this work are set out below:
 - ▶ The Council set a balanced budget for 2015/16 in February 2015, with no unmet budget gap to be addressed. The Council's latest Medium Term Financial Strategy identifies a cumulative budget gap in the financial years 2016/17 and 2017/18 of £2 million.
 - ▶ The assumptions made by the Council in determining its budget are appropriate, and that the Council does not rely on as yet uncertain funding streams to balance its base budget (for example funding from the New Homes Bonus). We are satisfied that the Council's has established appropriate budgetary control procedures, and that further work is planned over the summer of 2015 to address the budget gaps in future years.
 - ▶ The level of reserves held by the Council at 31 March 2015 covers the budget gap identified within the medium term financial plan to an appropriate level. However, the Council does need to formalise the savings plans it is developing in order to address the budget gap going forward and maintain its reserve balances.

Criteria 2 – arrangements for securing economy, efficiency and effectiveness

'Whether the Authority 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 completed our work in relation to this criteria and have no issues to report.
- ▶ Our work at the Council did not identify any other matters relating to aspects of your corporate performance and financial management framework which are not covered by the scope of the two specified criteria above.

Section 6

Independence and audit fees

Independence and audit fees

Independence

- ▶ We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated 19 February 2015.
- ▶ We complied with the Auditing Practices Board's Ethical Standards for Auditors and the requirements of the Audit Commission's Code 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 Audit and Standards Committee on 9 September 2015.

- ▶ We confirm that we have met the reporting requirements to the Audit and Standards Committee, as 'those charged with governance' under International Standards on Auditing (UK and Ireland) 260 – Communication with those charged with governance. Our communication plan to meet these requirements were set out in our Audit Plan of 19 February 2015.

Audit fees

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

	Proposed final fee 2014/2015	Scale fee 2014/2015
	£	£
Audit Fee: Code work	103,352	103,352
Certification of claims and returns	27,790	27,790

- ▶ Our actual fee is in line with the agreed fee at this point in time, subject to the satisfactory clearance of the outstanding audit work.
- ▶ Our work on the certification of claims and returns is not yet complete. We will report the final fee for this work in our Certification Report in January 2016.
- ▶ We confirm that we have not undertaken any non-audit work outside of the Audit Commission's Audit Code requirements.

Section 7

Appendices

Appendix A – uncorrected audit misstatements

The following misstatements, which are greater than £0.152 million have been identified during the course of our audit and in our professional judgement warrant communicating to you as those charged with governance.

These items have not been corrected by management.

Item of account	Nature	Type	Balance sheet	Comprehensive income and expenditure statement
	Description	F, P, J	Debit/(credit)	Debit/(credit)
Tangible Fixed Assets – Other Land & Buildings	Amounts capitalised as Intangible Fixed Assets were incorrectly categorised. This error is a classification error within the balance sheet only, there is no impact on the comprehensive income and expenditure statement	F	£275,000	
Intangible Fixed Assets			(£275,000)	
Cumulative effect of uncorrected misstatement			£0	

Key

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

Appendix B – corrected audit misstatements

The following matters were identified during the course of our audit and in our professional judgement warrant communicating to you. These items have been corrected by management within the revised financial statements

Disclosure	Description of misstatement
1. Note 2: Critical judgements in applying accounting policies.	Disclosure note updated to give greater explanation of the judgements made in establishing the potential liability to the Council arising from appeals against the rateable value on business premises.
2. Note 10: Taxation and Non-Specific Grant Income	Disclosure note has been amended to provide further disclosure on amounts received from taxation and non-specific grant income. There has been no change to the total amounts received. The need for this amendment was brought to our attention by management.
3. Note 37: Operating Leases	Amounts relating to minimum lease payments, and sublease payments receivable, have been corrected.

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