Thurrock Council

Audit Committee Summary

For the year ended 31 March 2015
Audit Results Report – ISA (UK and Ireland) 260

9 September 2015
## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 1</td>
<td>Executive summary</td>
<td>3</td>
</tr>
<tr>
<td>Section 2</td>
<td>Extent and purpose of our work</td>
<td>5</td>
</tr>
<tr>
<td>Section 3</td>
<td>Addressing audit risks</td>
<td>7</td>
</tr>
<tr>
<td>Section 4</td>
<td>Financial statements audit – issues and findings</td>
<td>10</td>
</tr>
<tr>
<td>Section 5</td>
<td>Arrangements to secure economy, efficiency and</td>
<td></td>
</tr>
<tr>
<td></td>
<td>effectiveness</td>
<td>15</td>
</tr>
<tr>
<td>Section 6</td>
<td>Independence and audit fees</td>
<td>18</td>
</tr>
<tr>
<td>Section 7</td>
<td>Challenges for the Coming Year</td>
<td>20</td>
</tr>
</tbody>
</table>

### Appendices

<table>
<thead>
<tr>
<th>Appendix</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appendix A</td>
<td>Uncorrected audit misstatements</td>
<td>22</td>
</tr>
</tbody>
</table>
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, Scrutiny and Transformation 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, subject to the completion of the outstanding work detailed on page 10. Our audit results demonstrate, through the few matters we have to communicate, that the Council has prepared its financial statements adequately.

Value for money
► At the time of drafting this report, we have not yet completed our work in this area. However, based on the work we have completed to date, 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.

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, once we have completed work on the Whole of Government Accounts.
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 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.

<table>
<thead>
<tr>
<th>Audit risk identified within our audit plan</th>
<th>Audit procedures performed</th>
<th>Assurance gained and issues arising</th>
</tr>
</thead>
<tbody>
<tr>
<td>Significant audit risks (including fraud risks)</td>
<td>► Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements; ► Reviewed accounting estimates for evidence of management bias; ► Evaluated the business rationale for any significant unusual transactions; and ► Reviewed capital expenditure on property, plant and equipment to ensure it met the relevant accounting requirements to be capitalised.</td>
<td>► We did not identify any material misstatements, evidence of management bias or significant unusual transactions in our testing. ► Our testing did not identify any expenditure which had been inappropriately capitalised.</td>
</tr>
</tbody>
</table>

Management override

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.

For local authorities the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.
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.

<table>
<thead>
<tr>
<th>Audit risk identified within our Audit Plan</th>
<th>Audit procedures performed</th>
<th>Assurance gained and issues arising</th>
</tr>
</thead>
<tbody>
<tr>
<td>Other audit risks</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Change in accounting for schools

In December 2014, CIPFA/LASAAC issued LAAP Bulletin 101 Accounting for Non-Current Assets Used by Local Authority Maintained Schools which provided further guidance on the practical application of the Accounting Code of Practice to non-current assets used by schools, where the assets are owned by a third party.

The Council will need to consider the nature of the agreements in place locally for each of their schools to determine the appropriate accounting approach and whether the land and buildings should be recognised in the Council’s accounts.

Our approach focussed on:

- The Council’s assessment of their accounting treatment for each relevant school against the LAAP bulletin;
- Review of accounting treatment for any changes required to balance sheet assets; and
- The valuation expertise used by the Council.

Our work confirmed that the Council’s assessment and treatment of Local Authority maintained schools was reasonable.
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 Standards and Audit Committee meeting:
  ► Investments and borrowings (receipt of outstanding bank confirmations, including schools)
  ► Capital expenditure, financing and minimum revenue provision (MRP) calculation
  ► Amounts reported for resource allocation decisions note
  ► Clearance of outstanding queries
  ► Completion of the work to support our value for money conclusion
  ► Whole of Government Accounts
  ► Manager and Director review of audit work and financial statements
  ► Receipt of a Letter of Representation

► 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 Standards and Audit 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 misstatements.

Corrected misstatements

► Our audit identified a number of further misstatements which our team have highlighted to management for amendment. These have been corrected during the course of our work. We do not consider any of the errors identified to be significant and therefore have not provided further details of these corrected misstatements.

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;
  ► Any significant difficulties encountered during the audit; and
  ► Other audit matters of governance interest

► We have one matter we wish to report to you.

► We had difficulty in reviewing and testing some year end estimates for debtor and creditors balances. This is due to the method used by the Council to account for these balances. Rather than raising a new debtor/creditor in year and reversing this out of the accounts after the year end when paid, the balance is continually rolled forward in the ledger. This led to difficulties in identifying which balances represented genuine current year assets or liability at year end for audit testing.

► We did not identify any specific errors in the year end debtor or creditor position. However, to facilitate a more timely process for the production and audit of accounts in future years, management should review the approach to raising year end debtors and creditors to ensure clear audit trails to support year end estimates for debtor and creditor balances can be provided for audit.
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.

<table>
<thead>
<tr>
<th>Item</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Planning materiality</td>
<td>We determined planning materiality to be £6.3 million (2014: £7.1 million), which is 2% of gross expenditure reported in the accounts of £317 million adjusted for losses on disposal of non-current assets and other investment and taxation income. We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</td>
</tr>
<tr>
<td>Tolerable error</td>
<td>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. We have set tolerable error at the upper level of the available range because there were no significant corrected errors in the Council’s 2013/14 financial statements and only two uncorrected errors, neither of which are likely to re-occur.</td>
</tr>
<tr>
<td>Reporting threshold</td>
<td>We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.32 million (2014: £0.35 million).</td>
</tr>
</tbody>
</table>
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:

<table>
<thead>
<tr>
<th>Area</th>
<th>Strategy applied</th>
</tr>
</thead>
<tbody>
<tr>
<td>Remuneration disclosures, including severance payments, exit packages and termination benefits</td>
<td>Our audit strategy was to check the bandings reported in the financial statements, test the completeness of the disclosures and make sure that the disclosures were compliant with the Code. We checked transactions back to the payroll system and supporting documentation.</td>
</tr>
<tr>
<td>Related party transactions</td>
<td>Our audit strategy was to obtain and review declarations from senior officers and members of the Council for any material disclosures and make sure that the disclosure was compliant with the Code. We carried out a sample check of Companies House searches on contracts from the Council’s contract register to identify whether any key decision-makers in the Council had an interest in the company, to test the completeness of the disclosure.</td>
</tr>
<tr>
<td>Members’ allowances</td>
<td>Our audit strategy was to test the completeness of the disclosure and make sure that it was compliant with the Code by sample checking transactions back to the payroll system and the Council’s Constitution.</td>
</tr>
</tbody>
</table>
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 tested the controls of the Council only to the extent necessary for us to complete our audit. The controls tested were for Accounts Payable, Accounts Receivable, Schools Balances and Housing Benefits. 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. In addition to the standard representations, we have requested the following specific representation:
  • The Council has reviewed their accounting treatment for non-current assets used by maintained schools and are satisfied that the changes made are appropriate.

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 completing our work in this area and will report any matters that arise to 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 Brentwood Borough 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 identified a significant risks in relation to this criteria in relation to the level of budget gap for future years reflected in the Council’s Medium Term Financial Strategy (MTFS). As part of out planning we noted that, to date the Council has responded well to the financial pressure resulting from the continuing economic downturn.

► However, the Council continues to face significant financial challenges over the next three to four years, due to loss of Central Government funding and pressures from inflation, demographics and the impact of new legislation.

► To address the specific risk we have identified, we have undertaken a more detailed review of the Council’s MTFS and the key assumptions within this. We have also looked at the level and planned use of reserves and the Council’s track record in delivering previous budgets and savings plans, as well as progress on addressing the budget gaps identified in the current MTFS. Our key findings in relation to these areas are set out on the next page of this report.

► At the time of drafting this report, we have not yet completed our work in this area.

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 and have no issues to report.

► Our work 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.
Arrangements for securing financial resilience

As noted in our conclusion, the Council has continued to respond well to the financial challenges it is facing. The size of that challenge is however increasing and there are a number of significant uncertainties that could have a significant impact on the Council’s future financial stability. We have set out below further details on how the Council has responded to the challenges it is facing along with our understanding of the current financial position - OUTSTANDING
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 2 March 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 Standards and Audit Committee on 24 September 2015.

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

<table>
<thead>
<tr>
<th>Proposed final fee 2014/2015</th>
<th>Scale fee 2014/2015</th>
<th>Variation comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Audit Fee: Code work</td>
<td>188,053</td>
<td>178,297</td>
</tr>
<tr>
<td>Certification of claims and returns</td>
<td>21,010</td>
<td>21,010</td>
</tr>
<tr>
<td>Non-Audit work</td>
<td>11,750</td>
<td>n/a</td>
</tr>
<tr>
<td></td>
<td>10,000</td>
<td>n/a</td>
</tr>
</tbody>
</table>

► We confirm that we have met the reporting requirements to the Audit, Scrutiny and Transformation 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 2 March 2015.

► We have incurred additional audit time in reviewing the Council’s proposed revised treatment of their Minimum Revenue Provision (MRP). This has resulted in an additional fee of £9,756 which has been agreed with the Head of Finance.
► We confirm that we have undertaken non-audit work outside of the Audit Commission’s Audit Code requirements, as shown above. We have adopted necessary safeguards in our completion of this work.
Section 7

Challenges for the Coming Year
Challenges for the coming year

Highways Network Asset (formerly Transport Infrastructure Assets)

- The Invitation to Comment on the Code of Accounting Practice for 2016/17 (ITC) sets out the requirements to account for Highways Network Asset under Depreciated Replacement Cost from the existing Depreciated Historic Cost. This is to be effective from 1 April 2016.

- This requirement is not only applicable to highways authorities, but to any local government bodies that have such assets.

- This may be a material change of accounting policy for the Council. It could also require changes to existing asset management systems and valuation procedures.

- Nationally, latest estimates are that this will add £1,100 billion to the net worth of authorities.

Action required

- CIPFA have produced LAAP bulletin 100, which provides a suggested timetable for actions to prepare for this change. This has been supplemented by the issue of the Code of Practice on Transport Infrastructure Guidance Notes (May 2015) and ITC (July 2015).

- The Council will need to demonstrate it has assessed the impact of these changes and undertaken work to:
  - Determine the completeness of base information, working closely with highways and other relevant departments.
  - Ensure that valuation information is appropriate to the Council, and that national valuation indicators are not used without consideration of their appropriateness locally.
  - Consider the Impact for the HRA or non-highways General Fund

- We will discuss the potential impact for the Council as part of our planning for 2015/16.
Section 8

Appendices
Appendix A – uncorrected audit misstatements

The following misstatements, which are greater than £0.32 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.

Balance sheet and statement of comprehensive income and expenditure

<table>
<thead>
<tr>
<th>Item of account</th>
<th>Nature</th>
<th>Type</th>
<th>Balance sheet</th>
<th>Comprehensive income and expenditure statement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Description</td>
<td>F, P, J</td>
<td>Debit/(credit)</td>
<td>Debit/(credit)</td>
</tr>
<tr>
<td>B/S - Fixed Asset Additions</td>
<td>Relates to expenditure on the construction of new housing. Regular invoices are received for payment based on completion of the work to date. We identified one invoice which was received in April for work done in 2014/15 which had been included in 2015/16. We extended out testing to review all construction invoices received in April relating to housing construction. We did not find any further issues.</td>
<td>F</td>
<td>£879,382</td>
<td>(£879,382)</td>
</tr>
<tr>
<td>B/S - Capital creditors</td>
<td>Relates to expenditure on the construction of new housing. Regular invoices are received for payment based on completion of the work to date. We identified one invoice which was received in April for work done in 2014/15 which had been included in 2015/16. We extended out testing to review all construction invoices received in April relating to housing construction. We did not find any further issues.</td>
<td>F</td>
<td>£879,382</td>
<td>(£879,382)</td>
</tr>
</tbody>
</table>

Cumulative effect of uncorrected misstatement

<table>
<thead>
<tr>
<th>Description</th>
<th>Type</th>
<th>Balance sheet</th>
<th>Comprehensive income and expenditure statement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>£0</td>
<td>£0</td>
</tr>
</tbody>
</table>

Key

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