

Tendring District Council

Annual Audit Letter for the year ended 31 March 2015

October 2015

Ernst & Young LLP



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The Members
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26 October 2015

Dear Members,

Annual Audit Letter 2014-15

The purpose of this annual audit letter is to communicate the key issues arising from our work to the Members and external stakeholders, including members of the public.

We have already reported the detailed findings from our audit work in our 2014-15 annual results report to the 24 September 2015 Audit Committee, representing those charged with governance, as updated under delegated arrangements for consideration by the Chair of the Audit Committee on 30 September 2015. We do not repeat these detailed finding here.

The matters reported here are those we consider most significant for Tendring District Council.

We would like to take this opportunity to thank officers for their assistance during the course of our work.

Yours faithfully

Neil A Harris
Audit Director
For and behalf of Ernst & Young LLP
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Contents

| | |
|--|-----------|
| 1. Executive summary | 1 |
| 2. Key findings | 3 |
| 3. Control themes and observations..... | 9 |
| 4. Looking ahead | 10 |
| 5. Fees | 11 |

Relevant parts of the Audit Commission Act 1998 are transitionally saved by the Local Audit and Accountability Act 2014 (Commencement No. 7, Transitional Provisions and Savings) Order 2015 for 2014/15 audits.

The Audit Commission's 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the accountable officer 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 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.

1. Executive summary

We have undertaken our 2014/15 audit work in accordance with the Audit Plan which we issued on 9 March 2015 to the 19 March 2015 Audit Committee.

We have conducted our audit work in accordance with the Audit Commission’s Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

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 having proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- Forming an opinion on the financial statements and on the consistency of other information published with them;
- Reviewing and reporting by exception on the Council’s AGS;
- Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources; and
- Undertaking any other work specified by the Audit Commission and the Code of Audit Practice.

Summarised below are the results of our work across all these areas:

| Area of work | Result |
|---|--|
| Audit of the financial statements of Tendring District Council for the financial year ended 31 March 2015 in accordance with International Standards on Auditing (UK & Ireland) | On 30 September 2015 we issued an unqualified audit opinion on the Council’s financial statements |
| Form a conclusion on the arrangements the Council has made for securing economy, efficiency and effectiveness in its use of resources | On 30 September 2015 we issued an unqualified value for money conclusion |
| Report to the National Audit Office on the accuracy of the consolidation pack the Council needs to prepare for the Whole of Government Accounts | We reported our findings to the National Audit Office on 30 September 2015 that the financial statements of Tendring District Council are below the threshold set and so do not require an audit. |
| Consider the completeness of disclosures on the Council’s AGS, identify any inconsistencies with other information which we know about from our work and consider whether it complies with CIPFA/ SOLACE guidance | Management amended the Annual Governance Statement to include and enhance specific references to the findings from Internal Audit reports high priority recommendations, the Council’s coastal protection scheme and how the Council is managing financial resilience. |

Consider whether we should make a report in the public interest on any matter coming to our notice in the course of the audit

We did not issue such a report.

Determine whether we need to take any other action in relation to our responsibilities under the Audit Commission Act

We did not issue such a report.

As a result of the above we have also:

Issued a report to those charged with governance of the Council with the significant findings from our audit.

Our Audit Results Report was issued to the 24 September Audit Committee, as updated under delegated arrangements for consideration by the Chair of the Audit Committee on 30 September 2015

Issued a certificate that we have completed the audit in accordance with the requirements of the Audit Commission Act 1998 and the Code of Practice issued by the Audit Commission.

On 30 September 2015 we issued our audit completion certificate.

In February 2016 we will also issue a report to those charged with governance of the Council summarising the certification of housing benefits grant claims work we have undertaken.

2. Key findings

2.1 Financial statement audit

The Council's Statement of Accounts is an important tool to show both how the Council 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 Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission. We issued an unqualified audit report on 30 September 2015.

Our detailed findings were reported to the 24 September Audit Committee, as updated under delegated arrangements for consideration by the Chair of the Audit Committee on 30 September 2015

The main issues identified as part of our audit were:

Significant risk 1: Risk of Management Override:

We plan our audit work to consider the risk of fraud. This includes consideration of the risk that management may override controls in order to manipulate the financial statements.

Management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly 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.

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 have completed our testing as set out in our Audit Plan. We did not identify any instances of management override.

Other key findings: Business rates appeals provision

The business rates appeals provision includes not only claims up to 31 March 2015 but claims that relate to earlier periods and is subject to estimation. As appeals are made to the Valuation Office, the Council may not be aware of the level of claims lodged. The Council may also find it difficult to obtain sufficient information to establish a reliable estimate.

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 on Local Authority Accounting and calculated on a reasonable basis.

However, as a result of a decision by the Valuation Tribunal of England in January 2015 to allow an appeal on the assessment of the rateable value of purpose built GP Surgeries, management has amended the financial statements to disclose an extra provision of £0.122 million in the Collection Fund. The Council has also updated the Movements in Reserves Statement, Balance Sheet and Note 16 Provisions to account for Tendring's share of the revised provision.

This amendment results in a deficit for Tendring's share of National Non-Domestic Rates but because of the technical nature of the accounting adjustment, the Council's useable reserves have increased by £25,000 for 2014/15.

Other findings: Uncorrected errors 2014/15

Management corrected several other misstatements we identified from our audit. However, there is one uncorrected misstatement for the 2014/15 financial year.

The asset values reported in the fixed asset register and hence note 10 Property, Plant and Equipment (PPE) do not agree to the valuer's report. The impact is that the Council has understated the value of its assets by £590,000, overstated expenditure in the Comprehensive Income and Expenditure Statement by £378,000 and understated the revaluation reserve by £213,000.

This error does not impact on useable reserves.

Management did not amend for this error as it is immaterial to the financial statements.

Those charged with governance and management set out in their letter of representation dated 30 September the reasons why the Council were not amending the financial statements.

Other findings: Uncorrected errors 2013/14

We reported upon three errors within our 2013/14 Audit Results report and Annual Audit Letter:

- The Council included a provision for land search charges under the Revenue Commitments Reserve at disclosure Note 6 Transfers To/From Earmarked Reserves. Had the Council amended the financial statements, useable reserves would have decreased by an immaterial sum of £114,300.
- The other two errors concerned netting off income and expenditure within Note 5: Adjustment between Accounting Basis and Funding Basis under Regulation and also within the Housing Revenue Account. Neither of these two corrections would have had an impact on the Council's useable reserves

Only the incorrect inclusion of land charges as a reserve instead of a provision impacted upon useable reserves in 2013/14. The Revenue Commitments Reserve of £12.4 million at Note 6 is overstated by £114,300 and Provisions at Note 17 is understated by £114,300. Therefore this amendment would decrease useable reserves by £114,300 in the 2013/14 comparative figures.

Management has amended for all three errors for the 2014/15 financial year.

Management did not amend for these errors in the 2013/14 comparative figures as they were immaterial to the financial statements.

Those charged with governance and management set out in their letter of representation dated 30 September the reasons why the Council were not amending the financial statements.

2.2 Value for money conclusion

As part of our work we must also conclude whether the Council has proper arrangements to secure economy, efficiency and effectiveness in the use of resources. This is known as our value for money conclusion.

In accordance with guidance issued by the Audit Commission, our 2014-15 value for money conclusion was based on two criteria. We consider whether the Council had proper arrangements in place for:

- Securing financial resilience, and
- Challenging how it secures economy, efficiency and effectiveness.

We issued an unqualified value for money conclusion on 30 September 2015. We noted the following issues as part of our audit.

Key finding 1: The Council's arrangements for the development of Jaywick

The September 2014 Report to Cabinet sought to progress the acquisition of various parcels of land at Jaywick. The aim is for the Council in its community leadership and housing provider roles, to encourage regeneration in Jaywick by direct housing development to improve housing conditions for local residents and stimulate a change in market conditions. There are financial and value for money risks associated with this project.

Our approach focused on:

- Reviewing the reports prepared by management to support the decision to acquire the land; and
- Considering whether the reports adequately address the risks associated with the project to form the basis for decision making.

We reported our findings to the Finance and Procurement Manager in March 2015. Whilst noting that the report covered financial, legal and value for money aspects we considered that any future reporting would be enhanced by the following:

- By statute a Council must secure best price when disposing of assets, but there are no similar rules in respect of land purchase. However, whilst the Council has assessed the purchase in terms of value for money, the Council must remain alert to the assessment of the powers available to the Council to purchase land at a price in excess of the market value. We have reviewed the arrangements for the land purchases and are not minded to challenge the transactions;
- Within the finance section of the report, an analysis of the impact on Housing Revenue Account (HRA) balances of the impairment arising from the difference in the market value paid for the land and its inclusion in the balance sheet at existing use value. Future reports could usefully state the size and overall purpose of the HRA balance and an assessment as to the impact on planned spending. We note that as part of Phase 2 of the project, management intends to review the HRA Business Plan;
- A concise summary to support the overall conclusion that effective use of resources can be demonstrated through the project. The paragraphs discussing the risks end inconclusively. A bullet point summary demonstrating how VFM is being achieved from a review of the risks would have more impact;
- A clear statement on how engagement with the private sector and central government has prevented investment in the area, providing a consideration of other options of funding and setting out why Tendring should continue to invest in the project at this particular time; and
- Phase 2 of the project should analyse any capacity gaps in the Council's expertise and where external support would benefit the Council.

Key finding 2: Financial Resilience

We consider financial resilience to be a risk to the Value for Money Conclusion.

The Council continues to face a significant challenge to bridge the present funding gap estimated to be £7.8 million by 2019/20.

Tendring's financial forecasts that have been reported to Members make clear the scale of the challenge faced in the medium term:

- For 2015/16, the £1.8 million savings gap has been closed without recourse to reserves set out in the February 2015 Baseline Budget report to Council for 2015/16;
 - A revised savings gap of £2.2 million for 2016/17; and
 - An estimated cumulative budget gap of some £4.3 million by 2017/18.
-

Plans have yet to be developed to meet the cumulative budget gap at 31 March 2018.

We have assessed the level of savings required against the reserves held by the Council. As at 31 March 2015, The Council has a General Fund reserve of £4 million and an Earmarked Reserve of £22.2 million. Should savings not be made the Council does not have sufficient funds to cover the deficit in the medium term.

The Council is taking action to address the gap by:

- Reviewing the end of year variances for 2014/15 to identify where budget reductions can be made;
- Challenging departments and services to review how they deliver services to identify any savings that can be secured on an on-going basis;
- Progressing transformational activities to deliver savings over the life of the projects; and
- Taking savings identified ahead of the 2015/16 financial year to the Austerity Reserve to support the budget. The Council has increased its Austerity Reserve by £2.3million in 2014/15 and it currently stands at £3 million.

As government intentions are unknown beyond 2014/15, the Council needs to take a long term view in bridging the gap. The Austerity Fund is a non-recurrent means for identifying savings but does not provide a long term solution. The Council needs to bridge the gap through achieving recurrent savings, efficiencies or increased income.

In addition, Members need to consider carefully the impact of any decisions to freeze or reduce council tax as well as the level of reserves to support the Council's finances. Financial reports detailing the impact of council tax increases compared with taking the associated grant for freezing council tax would aid decision making.

Other finding 1: Coastal Protection Project

Tendring has obtained funding for a major £36 million coastal protection project from Clacton Pier to Holland Haven. Value for money may not arise where robust governance arrangements to manage the project are not in place.

Following our May 2014 review of the Council's arrangements for the procurement, contract and risk management of the coastal protection scheme we recommended the Council monitors:

- Cash flow arrangements to ensure that funding flows match expenditure; and
- Robust project management arrangements to manage the cost of the project and has an appropriate budget in order to maintain and repair the scheme where necessary after the work have been completed.

Our audit found that funding flows for 2014/15 have been made in line with contracts. Management note that payments from the Environment Agency and Essex County Council are being made in line with claims made to date and that drawing on internal borrowing will not be required.

Internal Audit undertook an audit in April 2015 to assess various aspects of project management of the coastal protection scheme including controls over contract variations, penalty notices and claims by the contractor. Reporting in July 2015, Internal Audit provided a substantial assurance opinion representing a sound system of internal control has been found with no findings identified.

Management has reported that the annual cost of maintaining the scheme on an ongoing basis is being included in future financial strategies. Feasibility studies to maximise commercial opportunities from the scheme are in progress with the aim of generating income to support the long term maintenance of the coastal defence scheme.

Other finding 1: Approach to local council tax support

The Local Council Tax Support (LCTS) scheme took effect from April 2013. This required Tendring to set local levels of council tax support.

The move to LCTS represented a significant change for the Council and has both financial and reputational risks.

In August 2014, the High Court ruled the residency criteria for LCTS operated by Sandwell Metropolitan Borough Council was unlawful. Tendring operated a similar scheme. The Council ceased its residency rule in 2014 and introduced a revised scheme for 2015/16. The changes may impact on collection rates for 2014/15 and 2015/16.

Cabinet formally approved the Local Council Tax Support Scheme: Council Tax Exemptions and Discounts for 2015/16 in November 2014 confirming the cessation of the residency rule.

To date, Tendring's collection performance for local council tax support is ahead of budget for both 2014/15 and 2015/16. There has been an impact from the Local Council Tax Support Scheme on collection rates for 2014/15, which the Council took into account in its medium term financial planning and forecasting. However, the costs of the Scheme continue to fall.

As such, while we will monitor collection rates during 2015/16, this is unlikely to feature as a risk area in our 2015/16 Audit Plan.

2.3 Whole of Government Accounts

We performed the procedures required by the National Audit Office on the accuracy of the consolidation pack prepared by Tendring District Council for Whole of Government Accounts purposes.

We reported our findings to the National Audit Office on 30 September 2015 that the Council's financial statements are below the threshold set and so do not require an audit.

2.4 Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's AGS, identify any inconsistencies with the other information which we know about from our work, and consider whether it complies with relevant guidance.

Management amended the AGS by including references to:

- The three Internal Audit reports for 2014/15 receiving an Improvement Required rating, namely:
 - Public Experience: Procurement;
 - Theatres and Entertainment; and
 - Clacton Leisure Centre;
- Show how the Council has addressed EY's 2013/14 recommendations from the review of contract management and procurement process; and
- Highlight the future budget gap and how the Council is managing financial resilience.

2.5 Objections received

We did not receive any objections to the Council's financial statements from members of the Public.

2.6 Other powers and duties

We identified no issues during our audit that required us to use powers under the Audit Commission Act 1998, including reporting in the public interest.

2.7 Independence

We communicated our assessment of independence to those charged with governance at the 19 March 2015 and on 24 September 2015 Audit Committees.

In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff have not been compromised within the meaning of regulatory and professional requirements

2.8 Certification of grant claims and returns

We will issue the Annual Certification report for 2014/15 in February 2016.

3. Control themes and observations

As part of our work, we obtained enough understanding of internal control 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 must tell the Council about any significant deficiencies in internal control we find during our audit.

We did not identify any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in the Council's financial statements.

4. Looking ahead

| Description | Impact |
|---|--|
| <p><i>Highways Network Asset (formerly Transport Infrastructure Assets):</i></p> | |
| <p>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.</p> <p>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.</p> <p>Nationally, latest estimates are that this will add £1,100 billion to the net worth of authorities</p> | <p>The Council will need to demonstrate it has assessed the impact of these changes. Even though it is not a highways authority, the requirements may still impact if it is responsible for assets such as:</p> <ul style="list-style-type: none"> • HRA infrastructure; • Footways; • Unadopted roads on industrial or HRA estates; • Cycleways; and • Street Furniture. |
| <p>Significant Capital Projects</p> | |
| <p>The Council has embarked on an ambitious programme of regeneration and capital works covering the coastal defence scheme from Clacton to Holland Haven, Weeley Crematorium, re-development of Jaywick and improvements to Frinton and Walton Swimming Pool.</p> | <p>The Council should continually review management capacity to progress this programme of work to ensure that appropriate governance is in place and applied to progress the projects.</p> |

5. Fees

Our fee for 2014-15 is in line with the scale fee set by the Audit Commission and reported in our Audit Plan which we took to the 19 March 2015 Audit Committee.

| | Proposed Final fee 2014-15 | Planned fee 2014-15 | Scale fee 2014-15 | Final fee 2013-14 |
|--|----------------------------------|------------------------|----------------------|----------------------|
| Total Audit Fee – Code work* | £78,277 | £78,277 | £78,277 | £93,699 |
| Total Audit Fee – Certification of claims and returns** | £19,090 | £19,090 | £19,090 | £23,746 |
| Non-audit work*** | | | | |
| Pooling of Local Authorities' Housing Receipts in England | £To Be Confirmed | £0 | £0 | £0 |

* **Total Audit Fee – Code work**

In 2013/14, the Audit commission's scale fee was £77,377. Management agreed scale fee variation increases approved by the Audit Commission for work on:

- Coastal protection of £13,500;
- The impact of the High Court Judgement on the Council's local council tax scheme of £1,026; and
- Questions and correspondence from the public of £896.

The further increase of £900 reflects extra audit procedures required to gain sufficient audit assurance around business rate income and expenditure within the Collection Fund.

The scale fee for 2014/15 of £78,277 now includes this sum of £900.

** **Certification of claims and returns**

The final fee for 2013/14 of £23,746 includes fees of £6,815 on the scale fee of £16,931 for extra testing on the housing benefits and pooling of capital receipts returns.

Our fee for the certification of grants and claims is yet to be finalised for 2014/15. We will report the final fees for our certification of the Council's Housing Benefit Claim to those charged with governance in March 2016 within the Annual Certification Report for 2014/15.

*** **Pooling of Local Authorities' Housing Receipts in England**

In previous years we have undertaken the certification of the Pooling of Local Authorities' Housing Receipts in England return in accordance with certification instructions from the Audit Commission.

For 2014/15, the pooling return is no longer part of the Audit Commission/Public Sector Audit Appointments Ltd grant claim regime. Any work specified by Tendring District Council will need to be undertaken under agreed upon procedures through an ISAE 3000 reasonable assurance engagement letter.

EY along with other audit firms, have been in discussion with DCLG to agree instructions to auditors. Once an agreed approach we will discuss a standard engagement letter and terms and conditions for use and agreement along with a suggested fee range.

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