

## AUDIT COMMITTEE

26 JANUARY 2017

### REPORT OF CORPORATE DIRECTOR (CORPORATE SERVICES)

#### A.4 EXTERNAL AUDIT'S ANNUAL AUDIT LETTER 2015/16 (Report prepared by Richard Barrett)

#### PART 1 – KEY INFORMATION

##### **PURPOSE OF THE REPORT**

To present to the Committee the External Auditor's Annual Audit Letter 2015/16.

##### **EXECUTIVE SUMMARY**

The Annual Audit Letter for 2015/16 has recently been received from the Council's External Auditors which primarily summarises the outcomes from various audit activities undertaken during the year. The key messages set out in the letter highlight that the Council received an unqualified opinion on both its financial statements and value for money arrangements.

##### **RECOMMENDATIONS**

**That the Audit Committee considers and notes the contents of the Annual Audit Letter 2015/16.**

#### PART 2 – IMPLICATIONS OF THE DECISION

##### **DELIVERING PRIORITIES**

The aim of continuing to be financially stable and well managed and provide good value for money is directly supported through learning and improving through audit and inspection.

##### **FINANCE, OTHER RESOURCES AND RISK**

###### **Finance and other resources**

There are no direct financial implications arising from this report although a number of small additional fees are expected as set out on page 23 of the attached.

###### **Risk**

Not responding practically and timely to outcomes from audit and inspection may have an impact on the delivery of the Council's priorities, reputation, governance arrangements and overall control environment.

##### **LEGAL**

The Accounts and Audit Regulations require that:

- (1) A committee must meet to consider the letter as soon as reasonably practicable;
- (2) following consideration of the letter in accordance with paragraph (1) the authority

must—(a) publish (which must include publication on the authority’s website) the audit letter; and (b) make copies available for purchase by any person on payment of such sum as the authority may reasonably require.

**OTHER IMPLICATIONS**

Consideration has been given to the implications of the proposed decision in respect of the following and any significant issues are set out below.

**Crime and Disorder / Equality and Diversity / Health Inequalities / Area or Ward affected / Consultation/Public Engagement.**

This report does not have a direct impact although items could feature in the recommendations and subsequent action plans in future external audit reports. Any actions that may have an impact will be considered and appropriate steps taken to address any issues that may arise.

**PART 3 – SUPPORTING INFORMATION**

**ANNUAL AUDIT LETTER FOR THE PERIOD ENDING 31 MARCH 2016**

There are a number of different strands of external audit work undertaken during the year such as specific activity in relation to the financial statements and value for money opinion. The outcomes from these activities are reported to the Council separately as they are completed during the year. The Annual Audit Letter is effectively an end of year report for the Council which captures and summarises these outcomes in one document. It is primarily directed to Members but it must also be made available as a public document.

The **Annual Audit Letter** relating to 2015/16 is attached. No significant concerns have been raised relating to 2015/16.

However the External Auditor has raised a number of points to consider in the future which are set out on pages 20 and 21 of the attached. This is in addition to the overall challenge of identifying the necessary savings to meet forecasted budget gaps in 2018/19 and 2019/20 which must remain one of the top priorities for the Council going into 2017/18.

Responses to the points raised by the External Auditor are as follows:

External Audit Comment	Response
Economic impact of EU Referendum	Rather than being a separate issue, this matter is being actively managed via the financial forecast process where all financial / economic issues are brought together as part of the medium term financial planning process.
Faster Closure of Accounts	Financial Services are responding to the requirement to close the Council’s Accounts earlier with a phased approach being taken in the interim years to meet the new requirements from 2017/18.

Appointment of External Auditors	The Council's proposed approach to appointing External Auditors from the financial year 2018/19 is set out elsewhere on the agenda.
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<b>BACKGROUND PAPERS FOR THE DECISION</b>
None

<b>APPENDICES</b>
<b>ATTACHED</b> Annual Audit Letter for the year ended 31 March 2016

# Tendring District Council

Annual Audit Letter for the year ended 31 March 2016

October 2016

Ernst & Young LLP



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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ‘Statement of responsibilities of auditors and audited bodies 2015-16’. 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 from 1 April 2015’ 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 Tendring District Council (the Council) following completion of our audit procedures for the year ended 31 March 2016.

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

Area of Work	Conclusion
Opinion on the Council's: ▶ Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2016 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 Annual Accounts.
Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We concluded that you have put in place proper arrangements to secure value for money in your use of resources.

Area of Work	Conclusion
Reports by exception: ▶ 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
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	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 15 September 2016 and discussed with the Audit Committee on 22 September 2016.
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 29 September 2016.

In February 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.

Kevin Suter

Executive Director

Luton

For and on behalf of Ernst & Young LLP, Appointed Auditor



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 2015/16 Audit Results Report to the 22 September 2016 Audit 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 2015/16 audit work has been undertaken in accordance with the Audit Plan that we presented to the 17 March 2016 Audit Committee 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 2015/16 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 thy 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 you 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. 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.

A blurred office desk with a laptop, glasses of water, and financial documents. The scene is brightly lit, likely from a window with blinds in the background. A yellow rectangular box is overlaid on the left side of the image, containing the text 'Financial Statement Audit'.

# 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 29 September 2016.

Our detailed findings were reported to the 22 September 2016 Audit Committee.

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

Significant Risk	Conclusion
<p>Management override of controls</p> <p>A risk present on all audits is that 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.</p> <p>Auditing standards require us to respond to this risk by testing the appropriateness of journals, testing accounting estimates for possible management bias and obtaining an understanding of the business rationale for any significant unusual transactions.</p>	<p>We have not identified any evidence of material management override.</p> <p>We obtained a full list of journals posted to the general ledger during the year, and analysed these journals using criteria we set to identify any unusual journal types or amounts. We then tested a sample of journals that met our criteria and tested these to supporting documentation. We have no matters to report.</p> <p>Our review of accounting estimates did not identify any evidence of management bias. We have not identified 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>Revenue and expenditure recognition</p> <p>Auditing standards also required us to presume that there is a risk that revenue and expenditure may be misstated due to improper recognition or manipulation.</p> <p>We respond to this risk by reviewing and testing material revenue and expenditure streams and revenue cut-off at</p>	<p>Our review concluded that the Council has appropriate revenue and expenditure recognition policies.</p> <p>Our review of accounting estimates did not identify any evidence of management bias.</p>

<p>the year end.</p> <p>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 therefore review capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.</p>	<p>We did not find errors in material revenue or expenditure streams.</p> <p>We did not find errors from testing cut-off processes.</p> <p>Our testing did not identify any expenditure which had been inappropriately capitalised.</p>
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Other Key Findings	Conclusion
<p>The Council succeeded in bringing forward its timetable for the preparation of the narrative report, financial statements and annual governance statement to meet the timetable for publication of 30 June 2016.</p>	<p>The Council completed its working papers to support the financial statements in the week of 27 June 2016. In addition, management created further working papers in response to our queries during the audit. Best practice is for all working papers to be prepared at the time of sign off of the financial statements to 30 June each year. As the timetable moves to 31 May in 2017/18, management needs to bring forward its preparations to meet this date.</p>
<p>Within Note 14 of the draft financial statements on Financial Instruments management included an internally calculated sum of £60.363 million to record fair values of PWLB loans.</p>	<p>Management has amended Note 14 Financial Instruments to record fair values of PWLB loans at £61.210 million as per the third party Debt Management Office website</p>
<p>Note 28 (c) Exit Costs and Note 29 Termination Costs of the draft financial statements did not include all relevant costs as required by the Code of Accounting Practice.</p>	<p>Management has updated Note 28 (c) Exit Costs and Note 29 Termination Costs to record all costs where the full conditions of the departure were known as at 31 March 2016 in line with the Code of Accounting Practice.</p>



A close-up, shallow depth-of-field photograph of a stack of coins. The coins are stacked vertically, with the edges of several coins visible. 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".

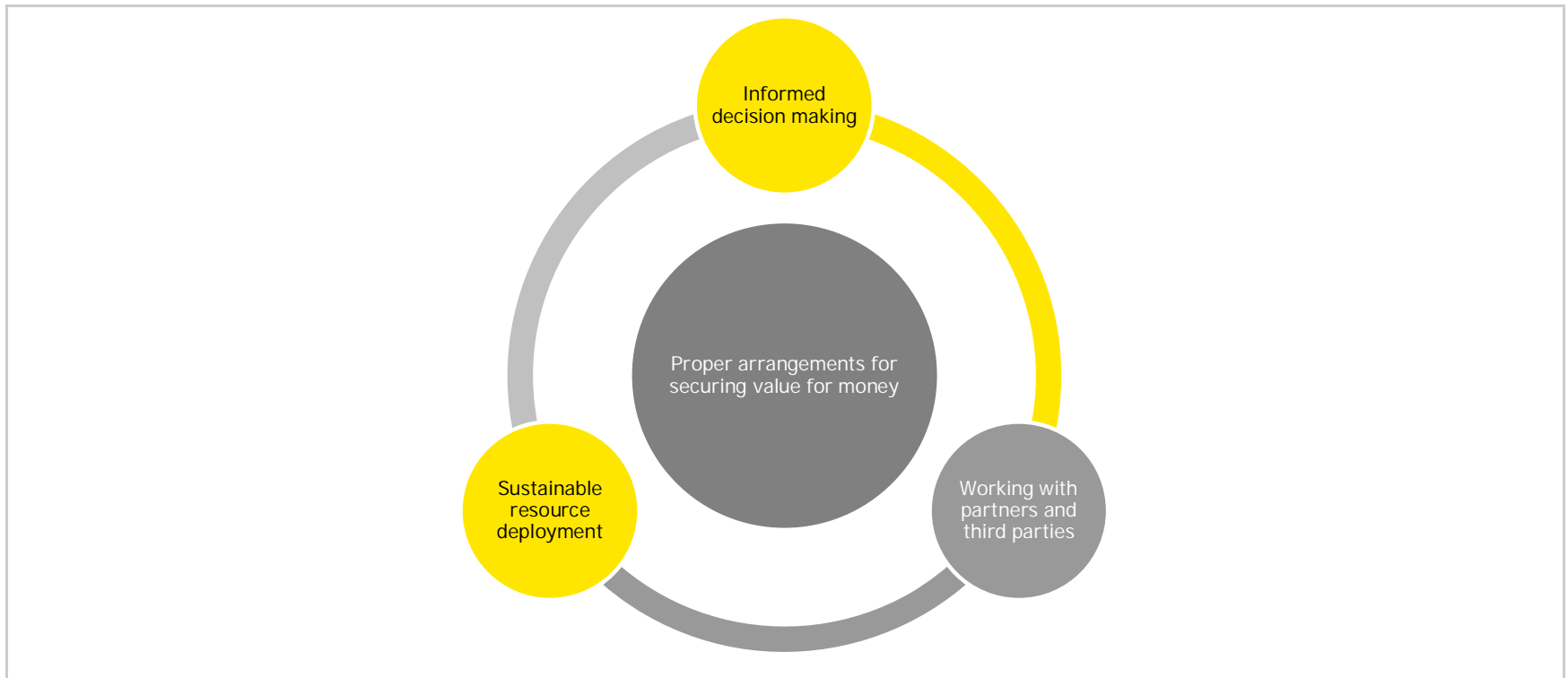
Value for Money

## 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 issued an unqualified value for money conclusion on 29 September 2016.

Our value for money arrangements risk assessment identified a significant risk in relation to the Council's arrangements to deploy resources in a sustainable manner. The risk concerns the Council's cumulative budget gap in the Medium Term Financial Plan (MTFP) over the next three years.

Our work did not identify any significant weaknesses in relation to the Council's arrangements. We therefore concluded that the Council had adequate arrangements in place.

As part of our work we made the following observations.

### Key Findings

Consideration of arrangements for deployment of resources to achieve planned and sustainable outcomes

The Council published its Medium Term Financial Plan (MTFP) in January 2016. The Council identified a cumulative funding gap of £5.023 million budget gap to 31 March 2020.

To deliver a balanced budget for 2016/17, the Council relied on £0.201 million from its Austerity Fund. Such funding represents a short term measure and is not sustainable over the medium term.

The Council has also updated its MTFP in August 2016 forecasting a reduced budget gap of £4.765 million to 2019/20, assuming a 1.9% increase in Council Tax for 2017/18. In addressing its budget gap, the Council has set in place a programme to achieve savings of £2.1 million in part through transforming services.

We have reviewed:

- The robustness of any assumptions used in medium term planning;
- The Council's approach to prioritising resources whilst maintaining services; and
- The savings plans in place, and assessing the likelihood of whether these can provide the Council with the required savings/ efficiencies over the medium term.

The robustness of any assumptions used in medium term planning

We have concluded that The MTFP identifies the key assumptions expected to underpin the 2016/17 budget. Assumptions include:

- Reductions in future levels of Revenue Support Grant;
- Using New Homes Bonus (NHB) to provide core funding to support the Council's transformation agenda, rather than the revenue base budget;
- Pay inflation, inflation for other costs and fees and charges; and
- Business rates pooling and council tax sharing.

We consider that the management can improve the MTFP by introducing sensitivity analysis to the assumptions and scenario analysis to help guide Members to determine options for budget setting.

The Council's approach to prioritising resources whilst maintaining services

Tendring ensures that resources are prioritised through the monitoring of 18 key project areas as well as 12 performance indicators, detailing business critical areas of the Council's work. For 2015/16, Cabinet were notified that of the 30 indicators reported, 24 are on or above their respective target, with six Building New Homes, Transforming Tendring, Review of Corporate Plan; Financial Self Sufficiency (Leisure Services), Recycling Rate and New Home Completions) behind target. We judged that there are no immediate pressing concerns that financial austerity is

impacting on Council performance as reported.

#### The savings plans in place

The savings plans of £2.1 million follow good practice in covering transformation projects and alternative service delivery to address the budget gap and by being managed by working parties led by portfolio holder Members. We noted that the savings plans are in development and need to be finalised with a risk assessment as to their likely success.

As at the end of 31 March 2016, the General Fund balance was £4 million with earmarked general reserves of £21.9 million. However, of these reserves of £21.9 million, £13.1 million relate to commitment reserves to fund specific projects by Members. Should these be spent, the remaining earmarked reserves available to the Council are £8.8 million. To 2019/20, should no savings plans materialise, the Council has sufficient reserves to meet the revised budget gap of £4.765 million. However, the Council needs to consider carefully all income streams including council tax increases in maintaining its reserves in the future.

Bridging the budget gap to ensure the Council's future financial viability presents a significant challenge for the Council. We have concluded that the Council is responding well to the financial challenges it is facing, but could improve arrangements for sensitivity and scenario analysis in its budget setting and to reduce its dependence on the Austerity Fund by finalising its savings plans promptly and risk assessing the likelihood of their success.

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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.

Management has amended the annual government statement for minor omissions from the Code of Practice and to provide the Head of Internal Audit Opinion in full.

### 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 2015/16 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 22 September 2016 Audit Committees. 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

We have adopted a fully substantive approach and have therefore not tested the operation of controls.

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
EU referendum	<p>Following the majority vote to end the UK’s membership of the European Union (EU) in the EU Referendum held on 23 June 2016 there is a heightened level of volatility in the financial markets and increased macroeconomic uncertainty in the UK. All three major rating agencies (S&amp;P, Fitch and Moody’s) took action on the UK Sovereign credit rating and, following the rating action on the UK Government. For entities in the public sector, there is likely to be an impact on investment property valuations if confidence in the wider UK property market falls; and the valuation of defined benefit pension obligations may also be affected. It is too early to estimate the quantum of any impact of these issues, but there is likely to be significant ongoing uncertainty for a number of months while the UK renegotiates its relationships with the EU and other nations.</p>	<p>Many of the issues and challenges that face the UK public sector will continue to exist, not least because continued pressure on public finances will need responding to. Additionally it may well be that the challenges are increased if the expected economic impacts of the referendum and loss of EU grants outweigh the benefits of not having to contribute to the EU and require even more innovative solutions.</p> <p>We are committed to supporting our clients through this period, and help identify the opportunities that will also arise. We will engage with you on the concerns and questions you may have, provide our insight at key points along the path, and provide any papers and analysis of the impact of the referendum on the Government and Public Sector market.</p>
Faster close	<p>From the 2017/18 financial year, the deadline for preparing the financial statements will move to 31 May from 30 June. In addition, the deadline for completing the statutory audit will move to 31 July from 30 September.</p>	<p>The faster closedown timetable requires the Council to adjust their timetables for preparing the accounts, as well as the budget setting process and the timing of committee meetings.</p> <p>It requires upfront planning to identify areas of the accounts that can be prepared earlier, before the 31 March, and there will be a need to establish robust basis for estimations across a wider number of entries in the financial statements.</p> <p>For the 2016/17 audit, we are working with officers to bring our work forward to support the transition ahead of the new deadlines in 2017/18.</p>
Appointment of auditors	<p>The current audit contracts expire on the completion of the 2017/18 audit. The expiry of contracts also marks the end of the current mandatory regime for auditor appointments.</p>	<p>Appointment of auditors for the 2018/19 financial year is required by 31 December 2017.</p> <p>The Council should consider whether they intend to opt</p>

Area	Issue	Impact
	<p>After this, the Council can exercise choice about whether they decide to opt in to the authorised national scheme, or whether to make other arrangements to appoint their own auditors.</p> <p>In July 2016, the Secretary of State for Communities and Local Government specified Public Sector Audit Appointments limited (PSAA) as an appointing person under regulation 3 of the Local Audit (Appointing Person) Regulations 2015.</p> <p>PSAA will be able to appoint an auditor to relevant authorities that choose to opt into its national collective scheme.</p>	<p>into the appointed person scheme to appoint your auditors from 2018/19 or if the Council should make their own arrangements following the legislative requirements.</p>

Appendix A

## Audit Fees



## Appendix A Audit Fees

Our March 2016 Audit Plan recorded planned fees for 2015/16 in line with the scale fee set by the PSAA Ltd.

Description	Final Fee 2015/16 £	Planned Fee 2015/16 £	Scale Fee 2015/16 £
Total Audit Fee – Code work	To be confirmed**	60,095*	58,708
Total Audit Fee – Certification of claims and returns	To be confirmed***	16,379	16,379

\* We agreed a scale fee variation of £1,387 for the extra work we undertook in 2015/16 with the Head of Finance, Revenues and Benefits for reporting on the results of our work on the proposed options and cost implications of the restructuring of the Management Team. The scale fee variation increase was approved by PSAA Ltd.

\*\* As reported in the Audit Results Report to those charged with governance, We have also undertaken extra work as a result of:

- The request for extra working papers during the audit; and
- Extra work to follow up the accounting and completeness of the disclosures related to the Management Team restructuring.

We anticipate a further scale fee variation will be necessary, which we will discuss in the first instance with the Head of Finance, Revenues and Benefits. Any extra fee is subject to approval by PSAA Ltd.

\*\*\*Our certification of the housing benefits claim takes place in October and November 2016. We will confirm the final fees charged in our certification report to be issued to the Council in February 2017.

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ED None

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