

South Cambridge District Council

Corporate Governance Committee Summary

For the year ended 31 March 2015

Audit Results Report – ISA (UK and Ireland) 260

14 September 2015



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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 **Corporate Governance 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 14 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 adequately.

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

- ▶ We are not required to report to the National Audit Office (NAO) regarding the Whole of Government Accounts, as the Council falls below the threshold for audit work.

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.

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
Significant audit risks (including fraud risks)		
<p>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 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.</p> <p>One area which may be susceptible to manipulation is the capitalisation of revenue expenditure on Property, Plant and Equipment given the extent of the Council's Capital programme.</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 the accounting estimates for evidence of management bias, and ▶ evaluated the business rationale for significant unusual transactions ▶ Tested the additions to the Property, Plant and Equipment balance to ensure that they are properly classified as capital expenditure. 	<p>Subject to clearance of final queries, no issues have been identified in relation to the testing of journals and assurance has been gained in this area.</p> <p>No issues have arisen with the testing of capital expenditure and assurance has been gained in the area.</p> <p>Our audit testing has not identified any instances of misstatement due to fraud and error.</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
Other audit risks		
<p>Group Accounts</p> <p>The Council is proposing to prepare group accounts for the first time. While the activities of the subsidiary company have been fairly limited to date there are considerable additional disclosures required within group accounts requirements.</p>	<ul style="list-style-type: none"> ► Testing the accuracy and completeness of the consolidation entries ► Testing the compliance of the group accounts with disclosure requirements. 	<p>We did not identify any issues in relation to the consolidation and production of group accounts.</p>
<p>Provision for business rate appeals</p> <p>In 2013/14 the Council was required to calculate a provision for business rate appeals for the first time. We found that the council had developed an appropriate methodology for the estimate once they had included the need for consideration of future appeals not yet lodged.</p> <p>This methodology needs to be reassessed to ensure that the assumptions made remain appropriate to prepare a reliable estimate.</p>	<p>Reviewed the Council's provision for business rate appeals to ensure it has been calculated on a reasonable basis in line with IAS 37 and that the assumptions underlying the estimate are reasonable. As part of this we ensured the provision is supported by appropriate evidence and that any level of estimation uncertainty is adequately disclosed in the accounts.</p>	<p>We did not identify any significant issues that we wish to bring to your attention in this regard.</p>
<p>Property Asset Valuations</p> <p>Due to the complexity in accounting for property, plant and equipment, the cyclical approach to valuations, and the material values involved, there is a higher risk that asset valuations contain material misstatements.</p>	<ul style="list-style-type: none"> ► Our assessment of management's valuation experts found them to be competent and objective and their work was adequate for our purposes. ► We considered whether the Council's property assets were valued appropriately and reasonably, including the choice of valuation technique and the presentation of gains and impairments in the Statement of Comprehensive Income as required by the Code. ► We sample tested valuation balances to ensure that they were correctly accounted for within the financial statements. ► We reviewed and tested journal entries to ensure that the valuation balances tested above were accurately disclosed within the financial statements. 	<p>We did not identify any significant issues that we wish to bring to your attention in this regard.</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 Corporate Governance Committee meeting:
 - ▶ Testing of cash flow statement
 - ▶ Finalisation of journals testing
 - ▶ Finalisation of payroll transactional testing
 - ▶ Receipt of a Letter of Representation
 - ▶ Final Manager and 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

- ▶ Our audit has identified one uncorrected misstatement within the draft financial statements. This is in relation to a misclassification between Debtors and Creditors of £0.17 million. This is detailed in Appendix A.

Corrected misstatements

- ▶ Our audit identified a small number of misstatements which our team have highlighted to management for amendment. The most significant of these was in relation to the omission of the revaluation on disposal of Assets Held for Sale (AHFS) - £1.3 million and £0.75 million in respect of the Comprehensive Income & Expenditure Statement and the Balance Sheet.
- ▶ Adjustments were made to Movement in Reserves Statement Note 5 & Comprehensive Income and Expenditure Account Note 7, Revaluation Reserve and Capital Adjustment Account (CAA) . Further details are in Appendix B.

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 other matters we wish to report.

- ▶ The Council's closedown processes and working papers are adequate to support the current audit timescales. However, they are not adequate to meet the demands of the faster close audit deadlines in 2017/18. There are also areas where the supporting documentation would improve the efficiency of the audit process.
- ▶ One example of this is in relation to the capitalisation of revenue expenditure. Whilst we have not reported any audit misstatements, we did however identify two small errors from our testing. We would recommend that the Council undertakes a detail review of all capitalised items to ensure they meet the criteria and are capitalised to the correct asset category.

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	
Planning Materiality and Tolerable error	<p>We determined planning materiality to be £1.318 million (2014: £ 1.528 million), which is 2% of gross expenditure reported in the accounts of £65.930million consisting of Gross expenditure (cost of services, other operating expenditure and financing expenditure).</p> <p>We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p> <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 higher level of the available range because there were limited errors reported in the Authority's 2013/14 financial statements.</p>
Reporting Threshold	<p>We agreed with the Corporate Governance Committee that we would report to the Committee all audit differences in excess of £0.066 million (2014: £0.076 million)</p>

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

- ▶ Remuneration disclosures including any severance payments, exit packages and termination benefits: Strategy applied: review and test transactions to supporting evidence and approvals
- ▶ Member allowances and audit fees: Strategy applied: review and test transactions to supporting evidence and approvals
- ▶ Related party transactions. Strategy applied: review disclosure for completeness, testing to supporting evidence

We evaluate any uncorrected misstatements against both the quantitative 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 tested the controls of the Council only to the extent necessary for us to complete our audit. 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. We have not requested any non-standard representations at this time.

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.
- ▶ The Council is below the £350 million reporting threshold, therefore we are not required to review the data collection tool.

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 South Cambridgeshire 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 identified one significant risk in relation to this criteria: criteria: *"Along with many other Council's, South Cambridgeshire is facing significant financial challenges over the next three to four years. The Council's external funding sources are reducing and are likely to be subject to change and uncertainty in future years."*
- ▶ We have undertaken a review of the medium term financial plan and the assumptions included within it. South Cambridgeshire District Council have robust plans in place to address the significant financial challenges they face in the coming years. The Medium Term Financial Strategy is robust, detailing a number of assumptions and scenarios. The Council refresh this on a regular basis for updates in circumstances. Savings plans have been put in place to address budget gaps.
- ▶ We have also assessed the level of reserves (both general fund and earmarked) that the Council has at the 31 March 2015.

We are comfortable that the level of reserves held by the Council (£16.4 million) covers the budget gap identified within the medium term financial plan, after excluding uncertain funding streams such as New Homes Bonus (£8.4 million) to an appropriate level.

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 identified one significant risk in relation to this criteria: *"The Council has established a wholly owned company (South Cambridgeshire Ltd) to take forward its strategic plans in the local housing market."*

The Council's governance arrangements should be adequate to ensure that these decisions are based on a sound assessment of the returns and value of this strategy to the Council."
- ▶ The governance arrangements over the set up of South Cambridgeshire Limited were discussed and formally agreed at the relevant Council committee meetings. A business plan for the Company are in place which is linked to the Council's medium term strategy and Housing Strategy.
- ▶ Formal agreement on whether the Council should extend the pilot scheme of the Company will take place in late 2015.

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.

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 3 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 Corporate Governance Committee on 25 September 2015.

- ▶ We confirm that we have met the reporting requirements to the Corporate Governance 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 3 March 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	Variation comments
	£	£	
Audit Fee: Code work	69,300	69,300	-
Certification of claims and returns	18,390*	18,390	See note 1 below

- ▶ 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.
- ▶ We confirm that we have not undertaken any non-audit work outside of the Audit Commission's Audit Code requirements.

Note 1 – Our fee for the certification of grant claims is based on the indicative scale fee set by the Audit Commission. This will be reviewed in light of the work required in 2014/15.

Section 7

Appendices

Appendix A – uncorrected audit misstatements

- ▶ The following misstatements, which are greater than £0.988m, 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

Item of account	Nature	Type	Balance sheet	Comprehensive income and expenditure statement
	Description	F, P, J	Debit/(credit)	Debit/(credit)
1. Current Liabilities – Short Term Creditors	Recycling credits had been included in creditors, however this is a debtor balance at year end.	F	(170,000)	
2. Current Assets – Short Term Debtors			170,000	
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 corrected misstatements, greater than £0.988 m have been identified during the course of our audit and warrant communicating to you.
- ▶ These items have been corrected by management within the revised financial statements.

Balance sheet and statement of comprehensive income and expenditure

Item of account	Nature	Type	Balance sheet	Comprehensive income and expenditure statement
	Description	F, P, J	Debit/(credit) - £'s	Debit/(credit) - £'s
1. Revaluation Reserve		F	(748,000)	
2. Capital Adjustment Account – write out of revaluation	Revaluation of Asset Held For Sale on disposal omitted from profit/loss on disposal calculation		748,000	
3. Note 7 – profit / loss on disposal				1,292,000
4. Note 5 – General Fund profit / loss on disposal				(1,292,000)
Cumulative effect of corrected misstatement			0	0

Key

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

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