AGENDA ITEM NO 6

East Cambridgeshire District Council

Annual Audit Letter for the year ended 31 March 2018

August 2018

Building a better working world

Contents

Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (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 (updated 23 February 2017)' 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 East Cambridgeshire District Council, 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.

01 Executive Summary

Executive Summary

We are required to issue an annual audit letter to East Cambridgeshire District Council (the Council) following completion of our audit procedures for the year ended 31 March 2018. 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 2018 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 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).	We had no matters to report

Executive Summary (cont'd)

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 presented to the Resources and Finance Committee on 26 July 2018
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 3 August 2018

Fees
Throughout the year we have engaged early and effectively with the finance team on matters relating to the Council's accounts. The finance team have been very receptive to our engagement and we have valued their openeness. During the course of the year end audit we did however experience some issues with the Council's preparation of working papers and overall coordination of dealing with the audit. Consequently we were required to input additional time to complete the audit procedures necessary to issue the auditor's report. As a result we have agreed an additional fee with the Section 151 Officer which we outline in Section 7.

Later this year we will also issue a report to the Resources and Finance Committee summarising the certification work we have undertaken, once this work has been completed.

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Suresh Patel

Associate Partner
For and on behalf of Ernst & Young LLP
Encl

02 Purpose and Responsibilities

Purpose and Responsibilities

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 2017/18 Audit Results Report to the 26 July 2018 Resources and Finance 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 of the Appointed Auditor

Our 2017/18 audit work has been undertaken in accordance with the Audit Plan that we issued on 29 January 2018 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 2017/18 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 the 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 £500m. 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 (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 putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

03 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 3 August 2018. Our detailed findings were reported to the 26 July 2018 Resources and Finance Committee.

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

Significant Risk	Conclusion
Risk of Fraud in Revenue and Expenditure Recognition Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.	We assessed that we were able to rebut the presumed fraud risk of revenue income/expenditure not being appropriately recognised with one exception: the risk that revenue expenditure could be charged against capital resources rather than to the general fund. We performed mandatory procedures, including: ‣ Reviewing and testing revenue and expenditure recognition policies; ‣ Reviewing and discussing with management any accounting estimates on revenue or expenditure recognition for evidence of bias; ‣ Developing a testing strategy to rest material revenue and expenditure streams; and ‣ Reviewing and testing revenue cut-off at the period end date. Our testing did not identify any material misstatements from revenue and expenditure recognition. Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Council's financial position.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Misstatements due to fraud or error As identified in ISA 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 would otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.	ISA 240 mandates we perform procedures on: accounting estimates, significant unusual transactions and journal entries to ensure they are appropriate and in line with expectations of the business. We are also required to identify specific additional risks of management override. The specific additional risk identified is with regards to manipulation of accounting estimates with the estimates most likely to be subject to management override of controls being non-routine income and expenditure accruals and provisions and specifically the Non Domestic Rates (NDR) appeals Provision. We performed mandatory procedures, including: ‣ Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements; ‣ Reviewing accounting estimates for evidence of management bias; ‣ Evaluating the business rationale for significant unusual transactions; and ‣ Reviewing managements specialist, Wilks, Head and Eve, who provide information to support the NDR appeals provision, testing the assumptions applied in the provision for reasonableness and ensuring it has been prepared in accordance with IAS37. Our testing did not identify any material misstatements from management override. We did not identify any instances of inappropriate judgements being applied. We did not identify any material issues or unusual transactions to indicate the misreporting of the Authority's financial position.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Area of Audit Focus	Conclusion
Property, Plant and Equipment Valuation Property, Plant and Equipment (PPE) represents a material balance in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end fixed assets balances held in the balance sheet. This is carried out by an expert valuer and is based on a number of complex assumptions. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We: ▸ Considered the reliance placed on management's valuation experts and undertook a review of the valuer's work. This included comparison to industry valuation trends and reliance on our own valuation experts; ▸ Considered the annual cycle of valuations to ensure that assets had been valued within a 5 year rolling programme as required by the Code for PPE. We have also considered if there were any specific changes to assets that have occurred and that these have been communicated to the valuer; ▸ Reviewed assets not subject to valuation in 2017/18 to confirm that the remaining asset base is not materially misstated by using market indices to assess movements from last revaluation dates; ▸ Tested the accounting treatment of valuations made in the year, including the assessment and treatment of impairments. Our testing did not identify any material misstatements from property, plant and equipment valuation. Our consideration of the annual cycle of valuations did not identify any issues with the implemented plan or with the movement on assets not revalued in year. The Authority agreed to include a disclosure note in respect of the valuation of Paradise Swimming Pool given the decision to demolish the pool was agreed during 2017/18 and works have now started.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Area of Audit Focus	Conclusion
Pension Liability Valuation The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Cambridgeshire County Council. The Council's pension fund deficit is a material and sensitive item and the Code requires that this liability be disclosed on the Council's Balance Sheet. At 31 March 2018 this totalled £22.4m. The information disclosed is based on the IAS19 report issued to the Council by the actuaries to the administering body. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We have: ▸ Liaised with the auditors of Cambridgeshire Pension Fund, and obtained assurances over the information supplied to the actuary in relation to East Cambridgeshire District Council; ▸ Assessed the work of the Pension Fund actuary (Hymans Robertson) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by National Audit Office for all Local Government sector auditors, and considered any relevant reviews by the EY actuarial team; and ▸ Reviewed and tested the accounting entries and disclosures made within the Council's financial statements in relation to IAS19. We have reviewed the assessment of the pension fund actuary by PWC and EY pensions and have undertaken the work required with no issues identified. A movement on the total fund asset between the estimated year end balance and the actual was identified by the pension fund auditor. The impact of this was an understatement of the Council's pension assets by £0.49 millions. We did not identify any issues with the accounting entries and disclosures made within the financial statements.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Area of Audit Focus	Conclusion
Assessment of the Group Boundary The Council has a number of joint arrangements which necessitate the preparation of group accounts. As previously, the Council needs to assess each arrangement to determine what falls within the group boundary and therefore requires consolidating into the Council's financial statements. The Council needs to ensure its consolidation procedures capture all the relevant information and enable it to meet the accounting and disclosure requirements for the Code. There is a risk that associate group changes may go undetected, and that the required disclosures are not made in accordance with the Code.	Our approach focused on the reasonableness of the Council's assessment by: ▸ Reviewing the Council's determination of where overall control lies with regard to the operation and delivery of services of the potential group bodies; ▸ Reviewing the consolidation procedures applied by the Council to those bodies that lie within the group boundary; and ▸ Engaging early with the auditors of East Cambs Trading Company and reviewing the financial information prepared by the Council in respect of the Business Centre to gain the necessary assurances for our audit of the group financial statements. The Council has consolidated East Cambridgeshire Business Centres Limited and East Cambs Trading Company Limited. We concurred with the Council's assessment. We received our required deliverables from Price Bailey. No issues were identified from our work on group accounts.

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	Thresholds applied
Planning materiality	We determined planning materiality to be £0.9m (2016/17 £0.8m), which is 2% of gross expenditure on provision of services reported in the accounts. We consider gross expenditure on provision of services to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.
Reporting threshold	We agreed with the Resources and Finance Committee that we would report to the Committee all audit differences in excess of £43k (2016/17 £40k).

04 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 identified one significant risk in relation to these criteria which we outline below. We have performed the procedures outlined in our audit plan. We did not identify any significant weaknesses in the Council’s arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Significant Risk

Pressure from Economic Downturn - Balanced budgets have been set for 2017/18 and 2018/19. We anticipate that the budget pressures facing the Council in 2019/20 will be significant. Work is underway developing the Medium Term Financial Plan for the coming 4 year period.

Conclusion

Our approach focused on:

- The adequacy of the Council’s budget monitoring process, comparing budget to outturn;
- The robustness of the Council’s arrangements for preparing and updating the Medium Term Financial Strategy, including how these arrangements take into account Council decisions over prioritising resources whilst maintaining services;
- The Council’s arrangements for delivering savings/efficiencies over the medium term.

In 2017/18 the Council continued its track record of meeting its annual budget, delivering a surplus of £0.82 million. The general fund balance stands at £1 million as at 31 March 2018, total earmarked reserves at £10.804 million, and the capital receipts reserve at £0.769 million. Total useable reserves are £12.573 million. The 2018/19 budget is balanced, through the use of efficiencies and income plans. Although it is still relatively early in the financial year, we assessed these as reasonably based taking into account the Council’s track record of delivering savings over the recent financial periods. While incrementally savings can become harder to achieve over time, the Council’s performance in delivering its plans gives confidence that it can continue to do so.

We also reviewed the key assumptions in the budget and MTFS (published in February 2018), which adequately took into account the economic environment at that time for business rate projections, and the forecast for reduced central government funding and the potential four year settlement. The budget gaps for 2018/19 and 2019/20 have been closed as a result of proactive action taken by management to reduce costs and generate new sources of funding. However there are significant budget gaps remaining in subsequent years. In 2020/21 the Council has to find savings of £2.267 million, rising to £3.284 million in 2021/22.

After 2021 the budget gaps become larger. Compared to a gross expenditure of approximately £45 million per annum, and historic performance of closing the gap, we assess the Council to have adequate arrangements, based on the known information as at the end of the financial year.

05 Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

The Council is below the specified audit threshold of £500 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. We did not identify any matters to report.

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 2017/18 financial statements from members 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 Resources and Finance Committee on 26 July 2018. 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

Our audit did not identify any controls issues to bring to the attention of the Resources and Finance Committee.

06 Focused on your future

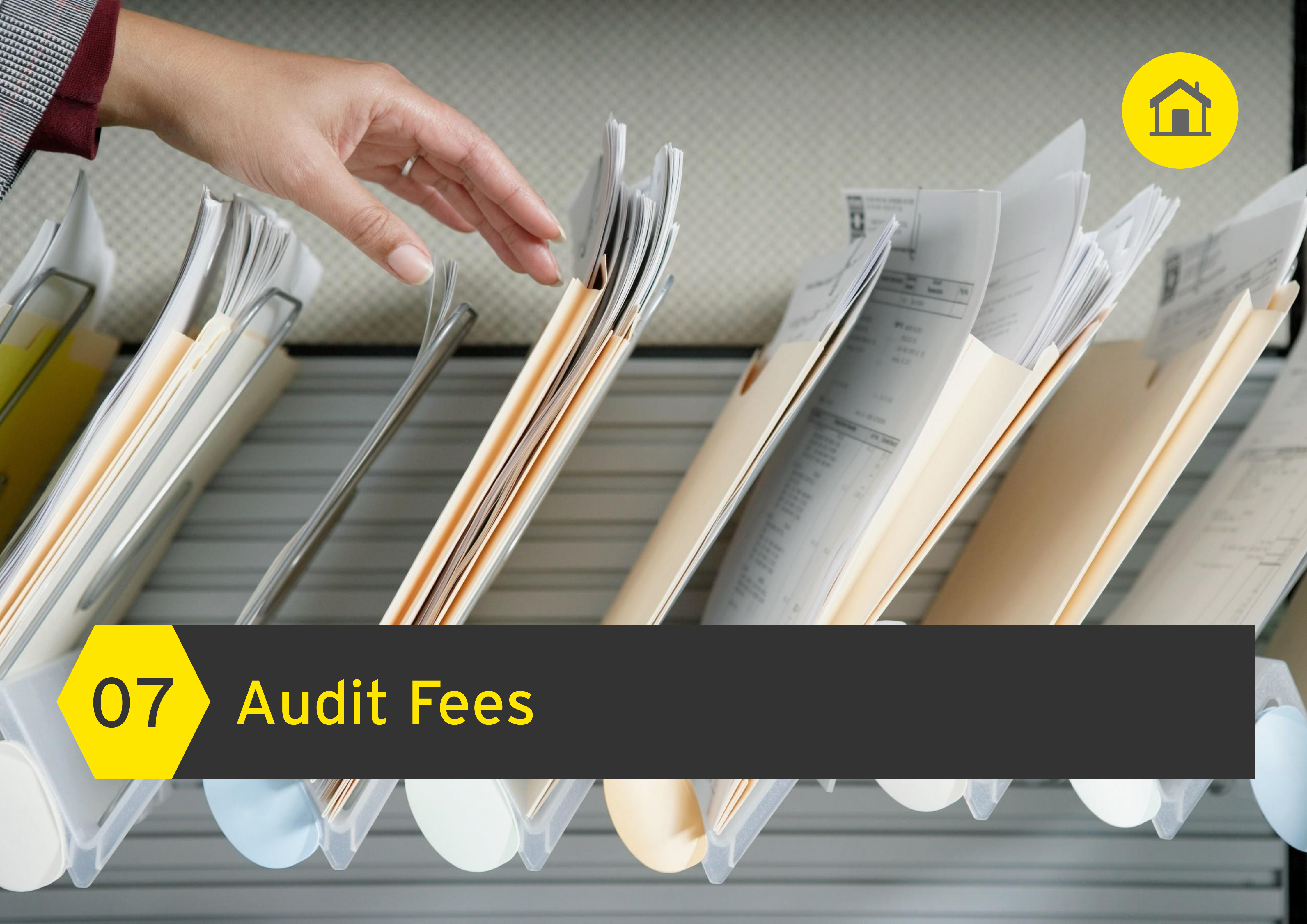
Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below. The Council will need to keep these standards under continued focus during 2018/19.

Standard	Issue	Impact
IFRS 9 Financial Instruments	Applicable for local authority accounts from the 2018/19 financial year and will change: ▸ How financial assets are classified and measured; ▸ How the impairment of financial assets are calculated; and ▸ The disclosure requirements for financial assets. There are transitional arrangements within the standard and the 2018/19 Accounting Code of Practice for Local Authorities has now been issued, providing guidance on the application of IFRS 9. In advance of the Guidance Notes being issued, CIPFA have issued some provisional information providing detail on the impact on local authority accounting of IFRS 9, however the key outstanding issue is whether any accounting statutory overrides will be introduced to mitigate any impact.	Although the Code has now been issued, providing guidance on the application of the standard, along with other provisional information issued by CIPFA on the approach to adopting IFRS 9, until the Guidance Notes are issued and any statutory overrides are confirmed there remains some uncertainty. However, what is clear is that the Council will have to: ▸ Reclassify existing financial instrument assets; ▸ Re-measure and recalculate potential impairments of those assets; and ▸ Prepare additional disclosure notes for material items.
IFRS 15 Revenue from Contracts with Customers	Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except: ▸ Leases; ▸ Financial instruments; ▸ Insurance contracts; and ▸ For local authorities; Council Tax and NDR income. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations.	As with IFRS 9, some provisional information on the approach to adopting IFRS 15 has been issued by CIPFA in advance of the Guidance Notes. Now that the Code has been issued, initial views have been confirmed; that due to the revenue streams of Local Authorities the impact of this standard is likely to be limited. The standard is far more likely to impact on Local Authority Trading Companies who will have material revenue streams arising from contracts with customers. The Council will need to consider the impact of this on their own group accounts when that trading company is consolidated.

Focused on your future (cont'd)

Standard	Issue	Impact
IFRS 16 Leases	It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. There are transitional arrangements within the standard and although the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.	Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.



07 Audit Fees

Audit Fees

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 March 2018.

We confirm we have not undertaken any non-audit work outside the PSAA Code requirements.

	Final Fee 2017/18	Planned Fee 2017/18	Scale Fee 2017/18	Final Fee 2016/17
	£	£	£	£
Audit Fee – Code work	41,500	41,500	41,500	41,500
Additional Code work:				
- Audit of group accounts	5,025	5,000	-	3,897
- Trial balance and analytics issues	-	-	-	1,000
- Impact of issues with working papers and coordination of the audit (note 1)	6,125	-	-	-
Total Audit Fee	52,650	46,500	41,500	46,397
Total non-audit services – Housing Benefit Subsidy (note 2)	tbc	12,004	12,004	15,632
Total Fees	**tbc**	**58,504**	**53,504**	**62,029**

Note 1:
We are seeking to agree this fee with the Section 151 Officer and is then subject to approval by the PSAA.

Note 2:
The final fee for the Housing Benefit Subsidy certification will be confirmed upon completion by the 30 November deadline. We will report the final fee in our annual grant certification report.

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ED None

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