

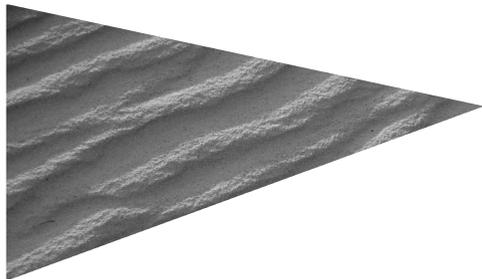
# Norwich City Council

## Audit Committee Summary

For the year ended 31 March 2014

Audit Results Report – ISA (UK & Ireland) 260

15 September 2014



Building a better  
working world

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# Executive summary

## *Key findings*

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### **Audit results and other key matters**

The Audit Commission's Code of Audit Practice (the Code) requires us to report to those charged with governance – the Audit 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 2013/14 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 15 September 2014, 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 expect to issue an unqualified confirmation to the National Audit Office (NAO) regarding the Whole of Government Accounts submission.

#### **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.

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# Extent and purpose of our work

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## 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 2013/14 financial statements
- Report on any exception on the governance statement or other information included in the foreword
- 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)

In addition, this report contains our findings related to the areas of audit emphasis, our views on the Council's accounting policies and judgments and significant deficiencies in internal control.

As a component auditor, we also follow the group instructions and send to the National Audit Office our group assurance certificate, audit results report and auditor's report on the consolidation schedule.

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.

# 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.

Audit risk identified within our Audit Plan	Audit procedures performed	Assurance gained and issues arising
Significant audit risks (including fraud risks)		
<p>1. Property Asset Valuation - Due to the complexity in accounting for property, plant and equipment and the material values involved, there is a higher risk that asset valuations contain material misstatements.</p>	<ul style="list-style-type: none"> <li>Reliance on management's valuations experts. This included comparison to industry valuation trends and reliance on our own valuation experts where significant unexplained variations were identified; and</li> <li>Tested the accounting treatment of valuations made in the year, including the assessment and treatment of impairments.</li> <li>Tested capital expenditure to ensure revenue items are not being capitalised.</li> </ul>	<ul style="list-style-type: none"> <li>We agreed the revaluation and impairments to reports provided by the Council's valuation expert. We assessed the qualifications, independence and scope of the Council's valuation expert to ensure we could rely upon the valuation reports provided.</li> <li>We have no issues to report from our comparison to industry trends, accounting treatment of revaluations, and testing of capital expenditure.</li> <li>We have identified an understatement of derecognition on HRA component capital expenditure. The work is ongoing, but the projected error is £0.728 million.</li> </ul>
<p>2. Assessment of the group boundary - This will be the first full year for the Norse Environmental Ltd arrangement. The Council will need to undertake an assessment of the group boundary against the criteria stipulated in the two relevant international accounting standards IAS27 and IFRS10. The purpose of the assessment is to conclude which functional bodies and other group entities fall within the boundary and therefore require consolidating into the Council's Financial Statements.</p>	<ul style="list-style-type: none"> <li>Assessing where overall control lies with regard to the operation and delivery of services of the potential group bodies.</li> <li>Ensuring that appropriate consolidation procedures are applied to those bodies that lie within the group boundary.</li> </ul>	<ul style="list-style-type: none"> <li>The Council assessed which functional bodies and other group entities fall within the group boundary but concluded that consolidating into the Council's Financial Statements was not required on the grounds of materiality.</li> <li>We have no issues to report from our review of the Authority's assessment.</li> </ul>

# 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
Significant audit risks (including fraud risks)		
<p>3. Localisation of business rates - There have been significant changes in the arrangements for business rate arrangements from April 2013. The detailed accounting arrangements for the new arrangement are not yet clear and this therefore presents a risk in terms of the financial statements.</p> <p>One of the main changes is that individual councils now need to provide for rating appeals. This includes not only claims from 1 April 2013 but claims that relate to earlier periods. As appeals are made to the Valuation Office, Councils may not be aware of the level of claims. Council's may also find it difficult to obtain sufficient information to establish a reliable estimate.</p>	<ul style="list-style-type: none"> <li>Reviewed the detailed accounting for business rates to ensure the Council's accounts are materially accurate and compliant with the CIPFA Code of practice.</li> <li>Reviewed the Councils provision for business rate appeals to ensure it has been calculated on a reasonable basis in line with IAS37. As part of this we will ensure the provision is supported by appropriate evidence and that the level of estimation uncertainty is adequately disclosed in the accounts.</li> </ul>	<ul style="list-style-type: none"> <li>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.</li> <li>The business rates appeals provision accounted for by the Council was deemed to have been calculated on a reasonable basis in line with the requirements of IAS 37.</li> <li>We have identified an understatement of £511,000 in the provision charged to the Collection Fund. This has not been corrected by management, Appendix 1 to this report sets out the uncorrected misstatements.</li> </ul>

# Addressing audit risks

## *Other audit risks (continued)*

Audit Risk identified within our Audit Plan	Audit Procedures performed	Assurance gained and issues arising
Significant audit risks (including fraud risks)		
<p>4. As identified in ISA (UK &amp; Ireland) 240, management is in a unique position to perpetrate fraud because of their ability to directly or indirectly manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. For district council's the potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.</p>	<ul style="list-style-type: none"> <li>• Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;</li> <li>• Reviewed accounting estimates for evidence of management bias;</li> <li>• Evaluated the business rationale for any significant unusual transactions; and</li> <li>• Tested capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised.</li> </ul>	<ul style="list-style-type: none"> <li>• Testing has not identified any material misstatement due to fraud and error.</li> </ul>

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# Financial statements audit

## *Issues and misstatements arising from the audit*

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### Progress of our audit

- ▶ The following areas of our work programme remain to be completed. We will provide an update of progress at the Audit Committee meeting:
  - ▶ Receipt of a Letter of Representation
  - ▶ Property, plant and equipment additions and revaluation testing
  - ▶ Income and expenditure transaction testing
  - ▶ Post balance sheet events review
- ▶ Subject to the satisfactory resolution of the above items, we propose to issue an unqualified audit report on the financial statements.

### Uncorrected Misstatements

- We have identified two misstatements within the draft financial statements, which management has chosen not to adjust.
- We request that these uncorrected misstatements be corrected or a rationale as to why they are not corrected be considered and approved by the Audit Committee and provided within the Letter or Representation
- Appendix 1 to this report sets out the uncorrected misstatements.

### Corrected Misstatements

Our audit identified a number of further misstatements which our team have highlighted to management for amendment. All of these have been corrected during the course of our work.

We do not consider any of these to be significant and therefore we have not provided further details of these corrected misstatements.

### Other Matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we are required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Council's financial reporting process including the following:

- Qualitative aspects of your accounting practices; estimates and disclosures;
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions; and,
- Any significant difficulties encountered during the audit; and
- Other audit matters of governance interest,

Please see the following page for comments on the qualitative aspects of your accounting practices for Property, Plant and Equipment (fixed assets) accounting records. We have no other matters we wish to report.

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## *Qualitative aspects of accounting practices*

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### **Fixed Asset Register**

We have commented in previous years on weaknesses in the spreadsheets used as a fixed asset register. The register is difficult to use and does not produce quality management information.

Every year that the Council delays in implementing a new fixed asset register makes the task more difficult as officers will have to consider data as far back as 1 April 2007, when the revaluation reserve was first introduced.

### **Fixed Asset Additions**

This area continued to be a cause of audit inefficiency. The working papers provided for audit lacked sufficient detail to enable us to select a sample of additions for audit testing again this year. The audit team will work together with officers to identify an alternative solution to this area in 2014/15.

### **De-recognition of components**

We estimate that the value of replaced components that has been de-recognised is understated by £728,000.

Where component parts of assets are replaced by the Council it is required to de-recognise the carrying value of the component that has been replaced. This avoids double counting components and overstating asset values.

Sample testing identified four instances where components had been replaced but the carrying value of the replaced component had not been removed. Our work also noted that the Council does not estimate the carrying value of roof, structural and 'whole house' components that have been replaced.

This work is still being concluded.

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# Financial statements audit (continued)

## *Internal Control, Written Representations & Whole of Government Accounts*

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### **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.

### **Whole of Government Accounts**

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the National Audit Office.

We are currently concluding our work in this area and will report any matters that arise to the Audit Committee.

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# Arrangements to secure economy, efficiency and effectiveness

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*The Code of Audit Practice (2010) sets out our responsibility to satisfy ourselves that Norwich City 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 Council 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 did not identify any significant risks in relation to this criteria.
- ▶ We have completed our work and plan to issue an unqualified value for money conclusion in relation to the Council's financial resilience. We do have some comments to report to those charged with Governance, as set out on the next page of this report.

## Criteria 2 - Arrangements for securing economy, efficiency and effectiveness

- ▶ *“Whether the Council is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.”*
- ▶ We did not identify any significant risks in relation to this criteria.
- ▶ We have no issues to report in relation to this criteria

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# Arrangements to secure economy, efficiency and effectiveness (continued)

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## Financial resilience

Along with many other Councils, Norwich City Council is facing significant financial challenges over the next three to four years.

The Council's external funding sources are reducing and are subject to change and uncertainty in future years. Some of the main areas of uncertainty relate to:

- ▶ Future levels of business rates income
- ▶ Future funding through the New Homes Bonus
- ▶ Level of Government funding through the Revenue Support Grant (RSG) and Baseline Funding (business rates)

The Council is acutely aware of the challenges it faces and is continually looking at ways in which services can be provided more efficiently and effectively over the coming years. Officers are also considering how the Council can generate income by operating on a more commercial basis.

The Council has a good track record of delivering savings and meeting its budget. Additional income projects and savings of £3.2 million are built into the 2014/15 budget and good progress has already been made on the 2015/16 savings requirement of £1.9 million.

The Council's financial forecasts that have been reported to Members make clear the scale of the challenge being faced. Some of the key issues reported include:

- ▶ The Council has a cumulative budget gap of around £9.5 million over the next 5 years (to 2019-20) which will need to be bridged through savings and efficiencies or increased income.
- ▶ The Council has included New Homes Bonus funding to support the base budget in each of the next 5 years. Although officers have calculated this funding on the basis of current trends, this funding stream has not been confirmed beyond 2016-17. If this source of funding was removed, or significantly reduced from 2017-18, the Council would have an additional base budget gap to address from 2017-18.
- ▶ The Council increased its council tax in 2014/15 by 1.95%. Decisions relating to council tax increases, or decreases, have an ongoing impact on the Council's ability to raise revenue in future years due to the annual restrictions on the level of annual increases

In light of the future financial pressures the Council is facing, Members need to continue to consider carefully the impact of any decisions to freeze or reduce council tax or use reserves to support the Council's finances, the ongoing sustainability of the Council's financial position and its ability to maintain service levels in future years.

# Independence and audit fees

## Independence

- ▶ We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated March 2014.
- ▶ We complied with the Auditing Practices Board's Ethical Standards for Auditors and the requirements of the Audit Commission's Code of Audit Practice 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 Audit Committee on 25 September 2014.

- ▶ We confirm that we have met the reporting requirements to the Audit Committee, as 'those charged with governance' under International Standards on Auditing (UK&I) 260. Our communication plan to meet these requirements were set out in our Audit Plan of March 2014.

## Audit fees

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

	Proposed final fee 2013-14	Scale fee 2013-14	Variation comments
	£s	£s	
Total audit fee - Code work	117,682	105,652	Correspondence from a member of the public
Certification of claims and returns	50,395	56,900	Fee reduced for claims no longer requiring certification.

- ▶ Our actual fee is higher than the scale fee as we have received correspondence from a member of the public which we have considered. Our proposed fee is at this point in time, and 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.

# Appendix 1 - Uncorrected audit misstatements

- The following misstatements have been identified during the course of our audit.
- These items have not been corrected by management.

## Balance Sheet and Statement of Comprehensive Income and Expenditure

Item of Account	Nature	Type	Balance Sheet	Statement of Comprehensive Income & Expenditure
	Description	F, P, J	Debit/(Credit)	Debit/(Credit)
1. Provisions	The NDR appeals provision is understated by £511,000 due to the Authority's calculation not considering how many years a successful appeal may be backdated. The additional £511,000 should be charged against the collection fund. The Authority's share is 40%.	J	(204,400)	204,400  Charge reversed out to collection fund adjustment account, so no impact on the general fund.
2. Property, plant and equipment	Understatement on derecognition of HRA component capital expenditure. The work is ongoing, but this is the projected error.	P	(728,000)	To be confirmed. Any charge is likely to be offset by upward revaluations. Any impact on the CIES will be reversed to the capital adjustment account, so no impact on the general fund.

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

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In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive 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 Audit Results Report 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.

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