

<b>Report to</b>	Audit committee 17 November 2015
<b>Report of</b>	Chief finance officer
<b>Subject</b>	Annual audit letter

## Purpose

## Recommendation

## Corporate and service priorities

## Financial implications

**Ward/s:** All wards

## Contact officers

## **REPORT**

### **Background**

1. The annual audit letter communicates to the members of Norwich City Council the key issues arising from the audit work carried out for the year ended 31 March 2015 by our external auditors. The letter is brought to the attention of all members and is also made available to external stakeholders, including members of the public, by publication on the council's website alongside the statement of accounts.

### **Key Findings, control themes and observations**

2. The detailed findings of the audit work were reported to this committee on 22 September 2015 in the 2014-15 audit results report. The key findings, control themes and observations contained in the letter are based on the findings in the audit results report.

### **Looking Ahead**

3. Section 4 of the letter draws attention to changes that will be needed to the accounts in the coming years. In particular, the Accounts and Audit Regulations will require the Council to produce draft accounts by 31 May each year, and these accounts to be audited by 31 July, from 2017-18.

### **Fees Update**

4. The audit committee should note the audit fees for the 2014-15 Statement of Accounts, which are equivalent to the scale fees, and the fee proposed for the certification of claims and returns.

# Norwich City Council

Annual Audit Letter for the year ended 31 March 2015

12 October 2015

Ernst & Young LLP





Members  
Norwich City Council  
City Hall  
St. Peter's Street  
Norwich  
NR2 1NH

12 October 2015

Dear Members

## **Annual Audit Letter 2014/15**

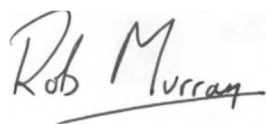
The purpose of this annual audit letter is to communicate the key issues arising from our work to the Members and external stakeholders, including members of the public.

We have already reported the detailed findings from our audit work in our 2014/15 audit results report presented to the 22 September 2015 Audit Committee, representing those charged with governance. We do not repeat those findings here.

The matters reported here are those we consider most significant for Norwich City Council.

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

Yours faithfully



Rob Murray

Executive Director  
For and on behalf of Ernst & Young LLP

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

The Audit Commission's 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the accountable officer of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

# 1. Executive summary

Our 2014/15 audit work was undertaken in accordance with our Audit Plan issued on 5 March 2015 and was conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

The Council is responsible for preparing and publishing its Statement of Accounts, accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for having proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

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

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

Area of work	Result
Audit of the financial statement of Norwich City Council for the financial year ended 31 March 2015 in accordance with International Standards on Auditing (UK & Ireland)	On 25 September 2015 we issued an unqualified audit opinion on the Council's financial statements
Form a conclusion on the arrangements the Council has made for securing economy, efficiency and effectiveness in its use of resources	On 25 September 2015 we issued an unqualified value for money conclusion
Report to the National Audit Office on the accuracy of the consolidation pack the Council needs to prepare for the Whole of Government Accounts	The Council is below the specified audit threshold of £350 million. Therefore we did not perform any audit procedures on the consolidation pack and submitted the required audit assurance statement confirming the threshold position.
Consider the completeness of disclosures on the Council's AGS, identify any inconsistencies with other information which we know about from our work and consider whether it complies with CIPFA/ SOLACE guidance	No issues to report
Consider whether we should make a report in the public interest on any matter coming to our notice in the course of the audit	No issues to report
Determine whether we need to take any other action in relation to our responsibilities under the Audit Commission Act	No issues to report

***As a result of the above we have also:***

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

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Our Audit Results Report was presented to the Audit Committee on 22 September 2015.

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

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We issued our certificate on 25 September 2015.

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In December 2015, we will also issue a report to those charged with governance of the Council summarising the certification (of grant claims and returns) work we have undertaken.



## 2. Key findings

### 2.1 Financial statement audit

The Council's Statement of Accounts is an important tool to show both how the Council has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission and issued an unqualified audit report on 25 September 2015.

Our detailed findings were reported to the 22 September 2015 Audit Committee.

In our view, the quality of the process for producing the accounts, including the supporting working papers was generally good.

The main issues identified as part of our audit were:

#### **Significant risk 1: Property, plant and equipment (fixed assets)**

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. This has contributed to errors and increased audit testing in previous years.

Due to the complexity in accounting for property, plant and equipment and the material values involved, these weaknesses increase the risk that asset valuations and capital expenditure contain material misstatements.

#### **Findings:**

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- ▶ **We did not identify any material misstatements or evidence of management bias in our testing of accounting treatment of valuations made in the year, including the assessment and treatment of impairments.**
  - ▶ **Our evaluation of the competence, capabilities and objectivity of the Council's valuation expert concluded we could place assurance on their work.**
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#### **Significant risk 2: Risk of management override**

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.

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.

#### **Findings:**

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- ▶ **We did not identify any material misstatements, evidence of management bias or significant unusual transactions in our testing of journals and estimates.**
  - ▶ **Our testing to identify if any expenditure had been inappropriately capitalised did not identify any material mis-statements.**
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We have no other matters to report.

## 2.2 Value for money conclusion

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

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

- ▶ securing financial resilience, and
- ▶ challenging how it secures economy, efficiency and effectiveness.

We issued an unqualified value for money conclusion on 25 September 2015.

We noted the following as part of our audit:

### **Arrangements to secure financial resilience: significant risk**

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Along with other Council's, 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 likely to be subject to change and uncertainty in future years. The Council's medium term financial strategy, approved in February 2015, identified a cumulative budget gap of £4.6 million over the next three years.

#### **Findings:**

**We have undertaken a review of the medium term financial strategy (MTFS) and the assumptions included within it. Norwich City Council has plans in place to address the significant financial challenges they face in the coming years. The Council's track record of achieving savings, and the level of general fund reserves held reduce the risk of the Council failing to effectively set and achieve its budgets over the medium term.**

**The Council have taken a prudent approach to future Government funding by assuming no new New Home Bonus and phasing out of formula funding by 2019/20.**

**We have also assessed the level of reserves, both general fund (£9.6 million) and earmarked reserves (£4.1 million) that the Council has at 31 March 2015. We are comfortable that the level of reserves held by the Council covers the budget gap identified within the MTFS.**

**Clearly, the Council needs to continue to review the delivery of the identified savings plans to ensure that they deliver the financial savings required in the planned timeframe. The MTFS should be updated to take account of this delivery and thus safeguard the level of general fund reserves that the Council holds.**

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## 2.3 Whole of Government Accounts

We performed the procedures required by the National Audit Office. The Council is below the specified audit threshold of £350 million and therefore we were not required to audit the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes. We made our audit assurance submission in line with the deadline.

## 2.4 Annual Governance Statement

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

We completed this work and did not identify any areas of concern.

## 2.5 Objections received

We did not receive any objections to the 2014/15 financial statements from members of the public.

## 2.6 Other powers and duties

We did not identify any issues during our audit that required us to use our powers under the Audit Commission Act 1998, including reporting in the public interest.

## 2.7 Independence

We communicated our assessment of independence to the Audit Committee on 25 September 2015. In our professional judgement the firm is independent and the objectivity of the audit engagement director and audit staff has not been compromised within the meaning of regulatory and professional requirements

## 2.8 Certification of grant claims and returns

We have not yet completed our work on the certification of the claims and returns. We will issue our Annual Certification report for 2014/15 in December 2015.

### 3. Control themes and observations

As part of our work, we obtained enough understanding of internal control to plan our audit and determine the nature, timing and extent of testing performed. We have not tested the individual system controls of the Council as we have adopted a fully substantive approach to our audit.

Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to tell the Council about any significant deficiencies in internal control we find during our audit.

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

## 4. Looking ahead

There are a number of changes in accounting and auditing requirements that could have a significant impact on the Council's arrangements for the production of its financial statements. We have outlined what we think are two of the main challenges below.

Description	Impact
<p><b>Highways Network Asset (formerly Transport Infrastructure Assets):</b></p> <p>The Invitation to Comment on the Code of Accounting Practice for 2016/17 sets out the requirements to account for Highways Network Assets under Depreciated Replacement Cost. This is a change from the existing requirement to account for these assets under Depreciated Historic Cost. This change is to be effective from 1 April 2016.</p> <p>This requirement is not only applicable to highways authorities, but to any local government bodies that have assets which fall into the definition. This could include, for example, footways and cycle ways, housing revenue accounts (HRA) infrastructure, unadopted roads on industrial or HRA estates, and street furniture.</p> <p>This may be a material change of accounting policy for the Council. It could also require changes to existing asset management systems and valuation procedures.</p>	<p>The Authority should consider whether it holds any assets that would be classified as highways network assets and, if so, whether they have the necessary information to implement the changes in accounting for these assets from 1 April 2016.</p> <p>Even though it is not a highways authority, the requirements may still impact if it is responsible for assets such as:</p> <ul style="list-style-type: none"> <li>• Footways</li> <li>• Housing revenue account (HRA) infrastructure</li> <li>• Unadopted roads in industrial or HRA estates</li> <li>• Cycleways</li> <li>• Street Furniture</li> </ul> <p>If the impact of this change in accounting policy is material, the Authority would also need to restate the balances for these assets as at 1 April 2015.</p>
<p><b>Earlier deadline for production and audit of the financial statements from 2017/18</b></p> <p>The Accounts and Audit Regulations 2015 were laid before Parliament in February 2015. A key change in the regulations is that from the 2017/18 financial year the timetable for the preparation and approval of accounts will be brought forward.</p> <p>As a result, the Council will need to produce draft accounts by 31 May and these accounts will need to be audited by 31 July in 2018.</p>	<p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p> <p>The Council is aware of this challenge and the need to start planning for the impact of these changes.</p> <p>This will include the need to review the current processes for the production of the accounts and the associated supporting working papers, including areas such as the production of estimates, particularly in relation to pensions and the valuation of assets, and the year-end closure processes.</p>

## 5. Fees

Our fee for 2014/15 is in line with the scale fee set by the Audit Commission and reported in our Audit Plan.

	Proposed final fee 2014/15	Scale fee 2014/15	Variation comments
	£	£	
Audit Fee: Code work	106,552	106,552	No change proposed
Certification of claims and returns	38,310	38,310	Note 1

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

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