

Report to Audit committee
 14 November 2017
Report of Chief finance officer
Subject Annual audit letter 2016-17

Item

5

Purpose

This report presents the annual audit letter.

Recommendation

The committee is asked to review and note the attached report from the council's external auditor.

Corporate and service priorities

The report helps to meet the corporate priority value for money services.

Financial implications

There are no direct financial implications arising from this report.

Ward/s: All wards

Cabinet member: Councillor Kendrick – Resources

Contact officers

Karen Watling, chief finance officer

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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 2017 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 26 September 2017 in the 2016-17 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. The "Focused on your future" section of the letter draws attention to the earlier deadline for production and audit of the financial statements from 2017/18. These changes will provide challenges for both the preparers and the auditors of the financial statements. We will continue to work closely with the auditors to identify ways to ensure the earlier deadlines, for both parties, can be achieved.

Fees Update

4. The audit committee should note the audit fees for the 2016-17 Statement of Accounts, are equivalent to the scale fees set by Public Sector Audit Appointments Ltd. The committee should also note the fee proposed for the certification of claims and returns.

Norwich City Council

Annual Audit Letter for the year ended 31 March 2017

October 2017

Ernst & Young LLP

Contents

Executive Summary	2
Purpose.....	5
Responsibilities.....	7
Financial Statement Audit	10
Value for Money	16
Other Reporting Issues.....	20
Focused on your future.....	23
Appendix A Audit Fees	25

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 the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

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

A hand with white nail polish is writing on a document with a blue pen. In the background, there is a calculator, a white cup, and a laptop. A yellow rectangular box is overlaid on the left side of the image.

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Norwich City Council (the Council) following completion of our audit procedures for the year ended 31 March 2017.

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 2017 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 Statement of Accounts.
Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We concluded that you have put in place proper arrangements to secure value for money in your use of resources.

Area of Work	Conclusion
Reports by exception:	
▶ Consistency of Governance Statement	The Annual Governance Statement was consistent with our understanding of the Council.
▶ Public interest report	We had no matters to report in the public interest.
▶ Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the consolidation pack.

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 31 August 2017.
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 27 September 2017.

In December 2017 we will also issue a report to those charged with governance of the Council summarising the certification work we have undertaken.

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

Mark Hodgson

Executive Director
For and on behalf of Ernst & Young LLP

Purpose



Purpose

The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2016/17 Audit Results Report to the 26 September 2017 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.



Responsibilities

Responsibilities

Responsibilities of the Appointed Auditor

Our 2016/17 audit work has been undertaken in accordance with the Audit Plan that we issued on 16 March 2017 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 2016/17 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 your Whole of Government Accounts return. The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the return.

Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (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.

Financial Statement Audit

The background of the image is a blurred office scene. In the foreground, there are several clear glass tumblers filled with water, some in sharp focus and others blurred. Behind the glasses, there are papers and documents, including one with a pie chart and another with a grid of small squares. A laptop is visible in the background, displaying some data. The overall lighting is bright and natural, suggesting a window nearby.

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 27 September 2017.

Our detailed findings were reported to the September 2017 Audit Committee.

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

Significant Risk	Conclusion
<p>Management override of controls</p> <p>A risk present on all audits is that management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly, and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.</p> <p>Auditing standards require us to respond to this risk by testing the appropriateness of journals, testing accounting estimates for possible management bias and obtaining an understanding of the business rationale for any significant unusual transactions.</p>	<p>We did not identify any material weaknesses in controls or evidence of material management override.</p> <p>We did not identify any instances of inappropriate judgements being applied.</p> <p>We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business.</p>

Risk of fraud in revenue recognition

Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue.

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 have rebutted this risk for the Council's income and expenditure streams except for the capitalisation of revenue expenditure on Property, Plant and Equipment given the extent of the Council's capital programme.

We have not identified any material weaknesses in the recognition of revenue.

We have not identified any instances of inappropriate judgements or estimates being applied.

Other Key Findings

Conclusion

Presentation of the financial statements

Amendments have been made to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the Code) changing the way the financial statements are presented.

The new reporting requirements impact the Comprehensive Income and Expenditure Statement (CIES) and the Movement in Reserves Statement, and include the introduction of a new Expenditure and Funding Analysis note as a result of the 'Telling the Story' review of the presentation of local authority financial statements.

The Code no longer requires statements or notes to be prepared in accordance with Service Reporting Code of Practice. Instead the Code requires that the service analysis is based on the organisational structure under which the authority operates. We expect this to show the Council's segmental analysis.

We proposed some minor disclosure amendments that management agreed to make in the financial statements.

In particular, we noted that the Expenditure & Funding Analysis (EFA), although positioned amongst them, is not a Primary Statement (consistent with the Code Guidance Notes). As such an additional narrative paragraph was added to the EFA to reflect this.

There were no other matters to report.

Other Key Findings (continued)	Conclusion
<p>Property, plant and equipment valuations</p> <p>Property, Plant and Equipment (PPE) represents a material item on the Council's balance sheet. PPE is initially measured at cost and then revalued to fair value (determined by the amount that would be paid for the asset in its existing use) on a 5 year rolling basis.</p> <p>This is carried out by an expert valuer and is based on a number of complex assumptions. Annually assets are assessed to identify whether there is any indication of impairment.</p>	<p>Following full consideration of their work, we placed reliance on the Council's valuer. We did not identify any material issues in relation to the valuations.</p> <p>We note the Council are implementing plans to replace the current fixed asset register.</p> <p>There were no other matters to report.</p>
<p>Assessment of the group boundary</p> <p>The Council set up a new company during 2015/16. The Regeneration Company Limited is an incorporated company wholly owned by Norwich City Council.</p> <p>During 2015/16 the nature of this arrangement was assessed to determine whether the company should be consolidated into the Council's financial statements. We agreed with your officers' assessment that no group accounts were required. This was revisited during 2016/17.</p>	<p>We have reviewed the Council's assessment and agree that although the company does fall within the group boundary, there are no material qualitative or quantitative factors that would require group accounts to be prepared.</p>

Other Key Findings (continued)	Conclusion
<p>Pensions valuations and disclosures</p> <p>The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding the Local Government Pension Scheme (LGPS) in which it is an admitted body.</p> <p>The Council's current pension fund deficit is a highly material and sensitive item and the Code requires that this liability be disclosed on the Council's Balance Sheet.</p> <p>The information disclosed is based on the IAS19 report issued to the Council by the actuaries to the Norfolk Pension Fund.</p> <p>As part of their actuarial review, councils are being asked to make additional payments to the pensions scheme to fund deficits.</p>	<p>Assumptions used by the actuary and adopted by the Council are considered to be generally acceptable.</p> <p>The sensitivities surrounding these assumptions have been correctly disclosed in Note 4 to the financial statements.</p> <p>No issues were identified in completing our work.</p>

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 £3.42 million (2016: £3.63 million), which is 2% of gross revenue expenditure on services reported in the accounts of £171.258 million. We consider gross revenue expenditure on services to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £171,259 (2016: £181,784).

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 - reduced materiality level of £5,000 applied in line with bandings disclosed.
- Related party transactions, members' allowances and exit packages - reduced materiality level applied equal to the reporting threshold.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.



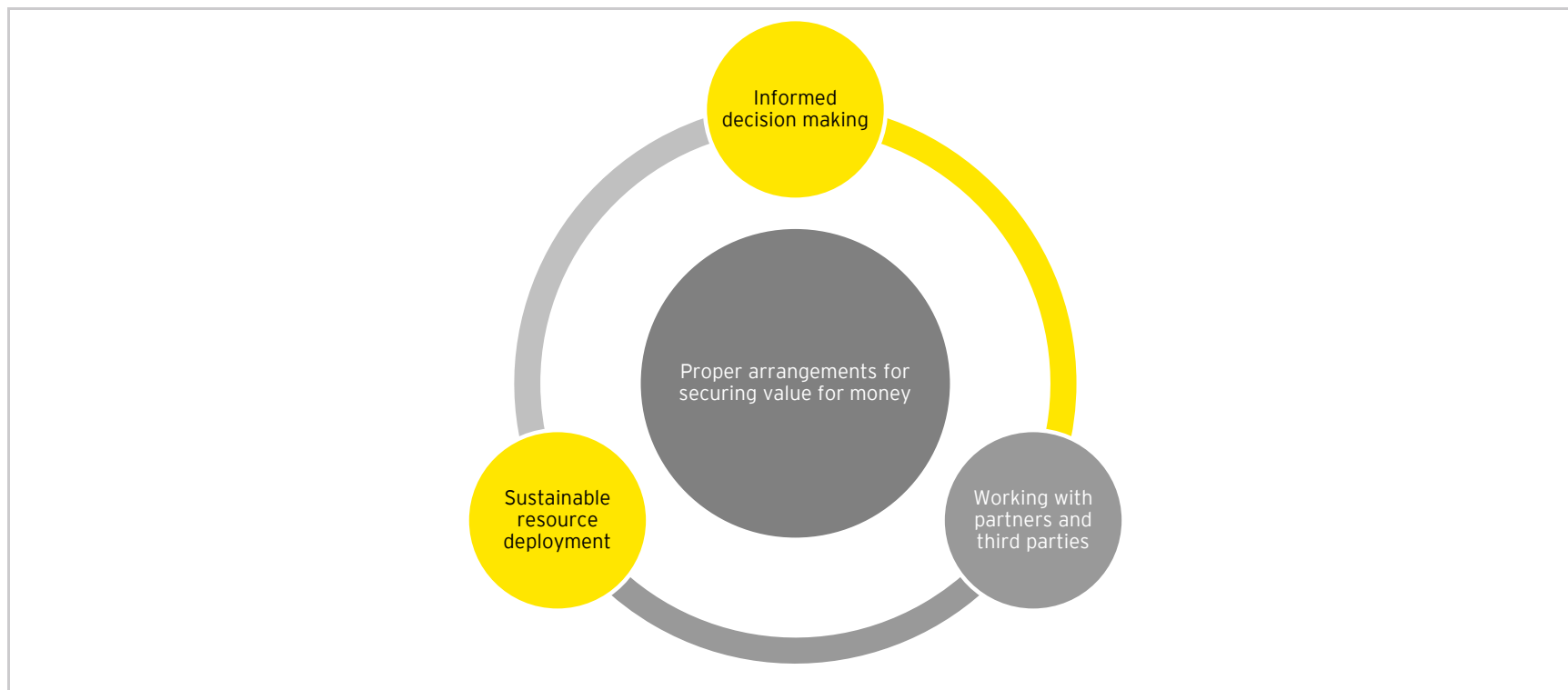
Value for Money

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.

Key Findings

Deploying resources in a sustainable manner

Risk

The medium term financial strategy (MTFS) sets a net savings requirement for the Council of £2.3 million each year for the next four years, reducing to £1.1 million in 2021/22. This is on top of £3.7 million transformation savings/income generation to be delivered in the 2016/17 budget.

Although the Council has assessed the savings/income generation targets for 2017/18 to 2021/22, detailed savings proposals will be presented to the Council for agreement on an annual basis.

Therefore a risk remains that further savings or increased income will not be identified to close the funding shortfall in 2017/18 to 2021/22.

Findings

The Council has a good record of identifying and making savings, and in meeting its budget.

- ▶ The Council currently has a high level of un-earmarked General Fund reserves. These are £14.344 million at 31 March 2017, which is significantly above the minimum levels range set by the Council's s151 officer of £4.3 million for the General Fund. These provide the Council with the flexibility to manage its financial position over the short-to-medium term, and reduce the risk that an unexpected overspend, or unexpected one-off item of expenditure, would have a detrimental impact on the Council's financial standing.
- ▶ The Council plans to maintain this minimum level of General Fund reserves indefinitely. The Council also have £30.383 million of HRA of un-earmarked General Fund reserves at 31 March 2017, the prudent level for HRA reserves is £5.9 million.
- ▶ The Council has plans to reduce the level of General Fund reserves over the next 4 years. However, the general trend over the last 4 years has been an increase in the level of General Fund reserves in line with budget underspends. Future projected levels of General Fund reserves remain in excess of the minimum recommended levels.
- ▶ The medium term financial strategy (MTFS) sets a net savings requirement for the Council of £2.3 million each year for the next four years, reducing to £1.1 million in 2021/22. This is on top of £3.7 million transformation savings/income generation to be delivered in the 2016/17 budget. The Council has assessed the savings/income generation targets for 2017/18 to 2021/22 and detailed savings proposals will be presented to the Council for agreement on an annual basis.

► The Council has established effective processes for setting its budget. In setting its general fund budget, the Council has been prudent in the assumptions it has made. This reduces the possibility of an unexpected overspend.

Challenges for the next year

Guided by the Council's corporate plan 2015-2020 and its 'changing pace blueprint' (operating model) a range of work has been carried out across the council through the transformation programme, to develop options for savings and additional income in order to meet the target within the MTFS and ensure a balanced budget.

The Council have taken the option to secure greater certainty and confidence in funding levels through the offer of a four year funding settlement for Local Authorities for 2016-17 to 2019-20, by submitting a four year efficiency plan.

The Council have based assumptions on the provisional local government finance settlement for 2017-18 which was presented to Parliament on the 15 December 2016. As part of the provisional settlement the DCLG has issued its estimates of the reduction in core spending power for each local authority. For Norwich City Council the reduction in spending power from 2016/17 to 2017-18 is 9%. The Council are planning for RSG to have ended completely for the council by 2020/21.

There is some reliance within the Council's MTFS on uncertain funding streams, such as New Homes Bonus which has been incorporated within the MTFS.

The latest published MTFS up to 2022/23 was approved by council on the 8 Feb 2017. The MTFS now shows a need to make further net savings of £9.6 million over the next 5 years, which following the "smoothed" approach equates to £1.9 million each year to 2022/23. This is a reduction on the £2.3 million set out in the 2016/17 budget papers as a result of a number of factors including Council tax revenues now being forecast £0.52 million higher than previously estimated for 2017/18 due to a higher than anticipated increase in the number of properties included in the calculations.

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.

We therefore issued an unqualified value for money conclusion on 27 September 2017.



Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

The Council is below the specified audit threshold of £350 million. Therefore, we did not perform any audit procedures on the consolidation pack.

Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

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

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 2016/17 financial statements from member of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 26 September 2017. 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

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. As we have adopted a fully substantive approach, we have therefore not tested the operation of controls.

Our audit did not identify any controls issues to bring to the attention of the Audit Committee.

Focused on your
future



Focused on your future

Area	Issue	Impact
<i>Earlier deadline for production and audit of the financial statements from 2017/18</i>	The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. From that year the timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the audited accounts by 31 July.	<p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p> <p>To prepare for this change the Council has reviewed and amended the closedown process to achieve draft accounts production by early June for 2016/17.</p> <p>We will work with the Council to engage early, following the completion of the 2016/17 audit, to facilitate early substantive testing for 2017/18 and also to consider steps the Council can take, for example:</p> <ul style="list-style-type: none"> ▶ Streamlining the Statement of Accounts removing all non-material disclosure notes; ▶ Bringing forward the commissioning and production of key externally provided information such as IAS 19 pension information, asset valuations; ▶ Providing training to departmental finance staff regarding the requirements and implications of earlier closedown; ▶ Re-ordering tasks from year-end to monthly/quarterly timing, reducing year-end pressure; ▶ Establishing and agreeing working materiality amounts with the auditors.

Appendix A

Audit Fees



Appendix A Audit Fees

Our fee for 2016/17 is in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA) and reported in our 26 September 2017 Audit Results Report.

Description	Final Fee 2016/17 £'s	Planned Fee 2016/17 £'s	Scale Fee 2016/17 £'s	Final Fee 2015/16 £'s
Total Audit Fee - Code work	79,914	79,914	79,914	79,914
Total Audit Fee - Certification of claims and returns	TBC - Note 1	29,819	29,819	35,780

Note 1- Our planned fee for the certification of claims and returns is based on the indicative scale fee set by the PSAA. The final fee will be reported to you in our annual certification report, upon completion of this work.

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

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ED None

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