

Colchester Borough Council

Annual Audit Letter for the year ended 31 March 2017

October 2017

Ernst & Young LLP



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Public Sector Audit Appointments Ltd (PSAA) has 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 laptop, and a white mug. 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 Colchester Borough 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 7 July 2017, and presented to the 25 July Governance & Audit Committee.
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 25 July 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.

Kevin Suter

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 25 July 2017 Governance and 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 7 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 thy 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 £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



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 25 July 2017.

Our detailed findings were reported to the July 2017 Governance and Audit Committee.

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

Significant Risk	Conclusion
<p>Management override of controls</p> <p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<p>We did not identify any material weaknesses in controls or evidence of material management override. We did not identify any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the Authority's normal course of business.</p>
<p>Risk of fraud in revenue recognition</p> <p>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. Having assessed the key income and expenditure streams of the Council, we judge that there is material opportunity and incentive for the incorrect classification of revenue spend as capital expenditure.</p>	<p>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 Authority's financial position.</p>

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.

This change in the Code will require a new structure for the primary statements, new notes and full retrospective restatement of comparatives. This restatement will require audit review, which could potentially incur additional costs, depending on the complexity and manner in which the changes are made.

Our testing performed has not identified any material misstatements in the 2016/17 statement of accounts.

Our work identified that the restated gross expenditure and gross income differed from the 2015/16 financial statements. The differences related mainly to the incorrect treatment in the prior year netting off HRA income and expenditure, which has been identified and corrected as a result of moving to the new Expenditure and Funding Analysis note.

The issue does not have an impact on the surplus/deficit on the CIES or the general fund.

No other issues were identified during our work performed in this area.

Property, plant and equipment valuations

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. 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. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of experts and assumptions underlying fair value estimates.

Our testing performed did not identify any material misstatements in the property, plant and equipment figures in the 2016/17 statement of accounts.

Pensions valuations and disclosures

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.

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.

The information disclosed is based on the IAS19 report issued to the Council by the actuaries to the Essex Pension Fund.

As part of their actuarial review, councils are being asked to make additional payments to the pensions scheme to fund deficits.

Both the NAO's consulting actuary and EY's internal specialists identified that the assumptions used by the pension fund actuary were considered to be at the optimistic end of the range for the discount rate and RPI inflation. Further consideration of the impact of these specific assumptions was therefore considered by EY's internal pension's specialist, concluding that the overall position is reasonable for the current year.

However in the opinion NAO's consulting actuary and EY's internal specialists the methodologies used to derive the discount rate and RPI inflation assumptions do not take adequate account of the specific duration of the scheme's liabilities.

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	<p>We determined planning materiality to be £2.9 million, which is 2% of gross revenue expenditure on services reported in the group accounts of £143.8 million.</p> <p>We consider gross revenue expenditure on services to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p>
Reporting threshold	<p>We agreed with the Governance and Audit Committee that we would report to the Committee all audit differences in excess of £0.143 million.</p>

We also identified areas where misstatement at a lower level than materiality might influence the reader and developed a specific audit strategy for them. They include:

- Remuneration disclosures including any severance payments, exit packages and termination benefits. As these disclosures are considered to be of interest to users of the accounts we have adopted judgement in ensuring that we have tested the disclosures in sufficient detail to ensure they are correctly disclosed. In particular we have confirmed the figures for senior officer remuneration in full.
- Related party transactions. The accounting standard requires us to consider the disclosure from the point of materiality to either side of the transaction. We have therefore considered the nature of the relationship in applying materiality.
- Councillors' allowances. As these disclosures are considered to be of interest to users of the accounts we have adopted judgement in ensuring that we have tested the disclosures in sufficient detail to ensure they are correctly disclosed.

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

A close-up, shallow depth-of-field photograph of a stack of coins. The coins are stacked vertically, with some showing their edges and others showing their faces. The lighting is warm, highlighting the metallic texture and the ridges on the edges. A bright yellow rectangular box is overlaid on the left side of the image, containing the text "Value for Money".

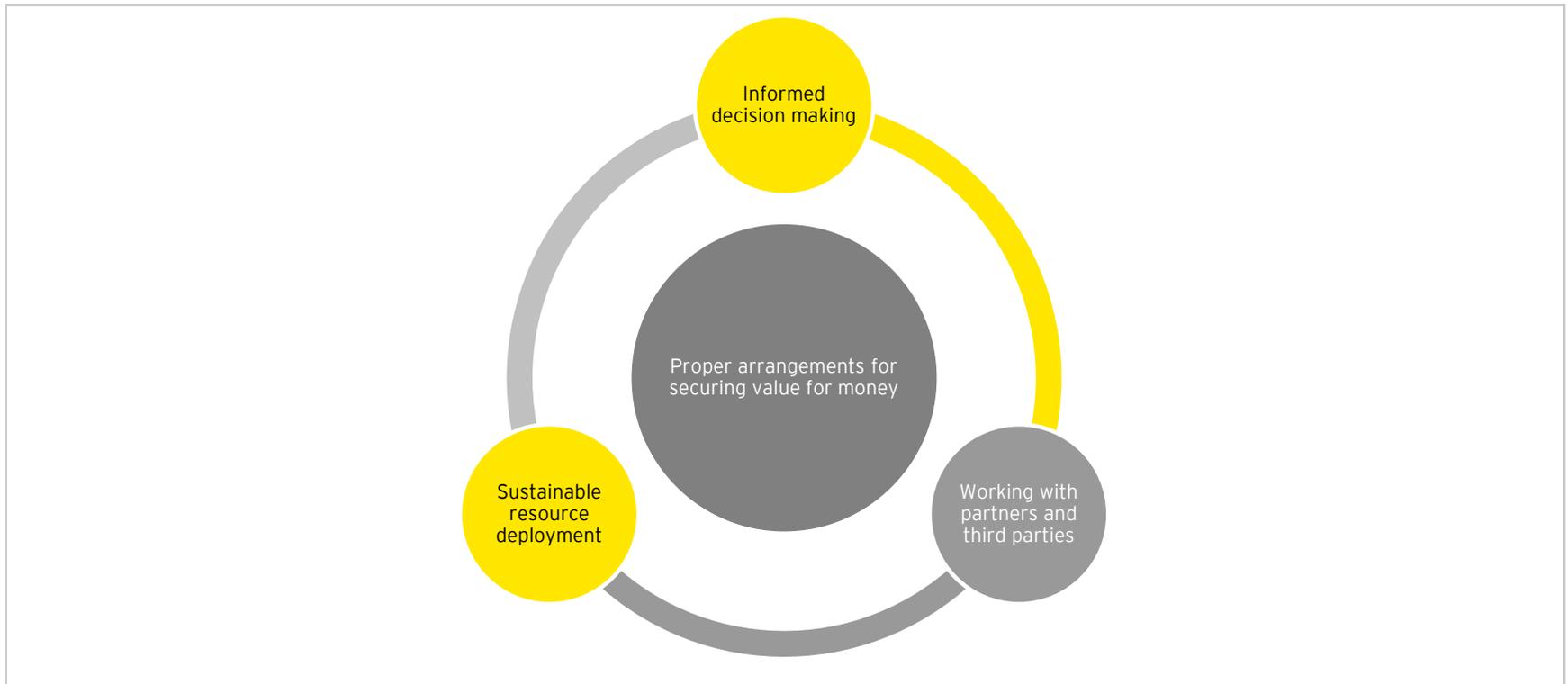
Value for Money

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 two significant risks in relation to these arrangements. The table below presents the findings of our work in response to these risks.

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 25 July 2017.

Significant Risk	Conclusion
<p>Sustainable resource deployment: Financial resilience - achievement of savings needed over the medium term</p> <p>To date the Council has responded well to the financial pressure resulting from the continuing economic downturn.</p> <p>However, the Council continues to face significant financial challenges over the next three to four years, with a forecasted underlying budget gap of £2.5m by 2020-21.</p> <p>Given the scale of the savings needed, there is a risk that savings plans to bridge this gap are not robust and/or achievable.</p>	<p>We undertook the procedures as set out in our audit strategy which have focused on:</p> <ul style="list-style-type: none"> • The adequacy of the Council's budget monitoring process, comparing budget to outturn. • The robustness of any assumptions used in medium term planning. • The savings plans in place, and assessing the likelihood of whether these plans can provide the Council with the required savings/efficiencies over the medium term. <p>Although the 2017/18 financial period sees the most challenging saving targets to date the Council has a strong history of delivering saving targets, has a strong and highly experienced management team and has taken effective steps to address future budget gaps.</p> <p>In 2016/17 the Council continued its strong performance against budget, delivering a small deficit of £0.1m, including approximately £1.5m of savings and additional income. The general fund balance stands at £9.4 million as at 31 March 2017.</p> <p>The 2017/18 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.</p> <p>The cumulative budget gap, taking into account the 2016/17 outturn, is now forecast at £2.5m to 2020/21. Compared to a gross expenditure of approximately £130m per annum, we judged this to be a manageable budget gap.</p> <p>Therefore, based on the known information as at the end of the financial year, we assessed the Council to have adequate arrangements.</p>

Work with Partners and Third Parties: Essex Garden Communities Project

Over the past eighteen months, the Council, jointly with Essex County Council, Braintree District Council and Tendring District Council have developed proposals for Garden Communities in North Essex.

The aim of the Garden Communities approach is to identify an agreed strategic approach to the allocation and distribution of large scale housing led mixed use development, including employment opportunities and infrastructure provision.

The Council has sourced a peer review, performed by Lord Kerslake. The review looked at the current approach to delivering Garden Communities in North Essex.

As a new and significant arrangement there may be risks relating to the governance and accounting arrangements for the establishment of the project that affect the Council.

We undertook the procedures as set out in our audit strategy which have focused on:

- Gaining an understanding of the governance structure; and
- Obtaining and assessing the findings of the peer review performed by Lord Kerslake.

Our work performed demonstrated that the North Essex Garden Communities project between Essex County Council, Braintree District Council, Colchester Borough Council and Tendring District Council is being governed appropriately and that there is a strong working relationship between the parties.

The Authorities have responded positively and in a timely manner to the recommendations provided in Lord Kerslake's peer review.

Given the early stage of the project we are likely to revisit this issue as the project develops.



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 Governance and Audit Committee on 25 July 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. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

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

A close-up photograph of a person's face as they look through a pair of black binoculars. The person's eyes are focused on the lenses, and their hands are visible holding the device. The background is a soft, out-of-focus white. A bright yellow rectangular box is overlaid on the left side of the image, containing the text "Focused on your future".

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>The Council has implemented a dry-run for 2016/17 and we issued our audit report by the 31 July 2017.</p> <p>This is an excellent achievement.</p> <p>Through working together, and reflecting on this year, there are a number of areas where the closedown and audit processes can be further improved going forward. We do not expect the formal earlier deadline to pose a significant issue for the Council.</p>

Appendix A

Audit Fees



Appendix A Audit Fees

Our fee for 2016/17 is in line with the scale fee set by the PSAA and reported in our 25 July 2017 Audit Results Report.

Description	Final Fee 2016/17 £	Planned Fee 2016/17 £	Scale Fee 2016/17 £	Final Fee 2015/16 £
Total Audit Fee - Code work (Note1)	64,066	64,066	62,582	62,582
Total Audit Fee - Certification of claims and returns (Note 2)	TBC	17,926	17,926	13,640
Non-audit work (Note 3)	TBC	4,250	N/A	4,250

Note 1: Due to additional work performed on the expenditure and funding analysis and the payroll data migration we have submitted a scale fee variation to PSAA of £1,484. We must seek the agreement from PSAA for this proposed variation, which has been agreed with the Council's Strategic Finance Manager.

Note 2: The planned fee for the certification of housing benefit subsidy is based on the indicative scale fee set by the PSAA, which itself is based on the programme of work carried out in 2014/15. The final fee will be reported to you in our annual certification report, upon completion of this work.

Note 3: The fee for non-audit work will be discussed with management and reported to the Governance and Audit Committee in subsequent reporting once the scope of work has been agreed for 2016/17. This work relates to the agreed upon procedures certification arrangements for the Pooling of Housing Capital receipts return.

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

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ED None

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