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External Audit Report 2015/16

London Councils

—
September 2016



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This report is addressed to London Councils and has been prepared for the sole use of London Councils. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.



Section one: Introduction



This document summarises:

The key issues identified during our audit of the financial statements for the year ended 31 March 2016 for the Joint Committee, Transport and Environment Committee and Grant Committee

Scope of this report

This report summarises the key findings arising from our audit work at London Councils in relation to the 2015/16 financial statements relating to the Joint Committee, Transport and Environment Committee and Grant Committee.

Financial statements

Our *External Audit Plan 2015/16*, presented to you in March 2016, set out the four stages of our financial statements audit process.



This report focuses on the second and third stages of the process: control evaluation and substantive procedures. Our on site work for this took place during March and July 2016.

We are now in the final phase of the audit, the completion stage. Some aspects of this stage are also included in this report.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out our key findings from our audit work in relation to the 2015/16 financial statements of the three Committees.

Our recommendations are included in Appendix 1. We have also reviewed your progress in implementing prior recommendations made by your previous auditor PriceWaterhouseCoopers.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.



Section two: Headlines



We anticipate issuing unqualified audit opinions on the Joint Committee, Transport and Environment Committee and Grant Committee financial statements by 30 September 2016.

We will also report that the Annual Governance Statements complies with guidance issued by CIPFA/SOLACE in June 2007.

This table summarises the headline messages. Sections three and four of this report provide further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion on the Joint Committee, Transport and Environment Committee and Grant Committee financial statements by 30 September 2016. We will also report that the Annual Governance Statements complies with guidance issued by CIPFA/SOLACE in June 2007.
Audit adjustments	Our audit has identified one audit adjustments with a total value of £15,738. This relates to the assignment of the Q4 administration costs for the ESF grant, which had been misallocated and as such, the creditor and debtor amount for the ESF grant is over-stated. The impact of these adjustments is to decrease the debtors and creditors on the balance sheet of the Joint Committee by £15,570 each. We identified a number of minor narrative and presentational adjustments required, throughout the accounts and accompanying notes. All of these were agreed with officers and adjusted.
Key financial statements audit risks	We review risks to the financial statements on an ongoing basis and tailor our audit procedures accordingly. In addition to the rebuttable presumption of the fraud risk from revenue recognition, we identified the following key financial statement audit risks in our 2015/16 External audit plan. — Management override of controls; and — Pension Liability assumptions. We have worked with officers throughout the year to discuss these audit risks. Our detailed findings are reported in section 3 of this report. We have agreed a recommendation on the evidenced review of information received from the actuary and reconciliation of figures provided to the actuary.

Section two

Headlines (cont.)



We have noted the high quality of the accounts and the supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.

At the date of this report our audit of the financial statements is substantially complete.

You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of London Councils.

Accounts production and audit process

We received complete sets of draft accounts for each of the three committees in line with the agreed timetable. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code.

We have noted the high quality of the accounts and the supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.

We will debrief with the Finance team to share views on the final accounts audit. Our objective is for this discussion to lead to further efficiencies in the 2016/17 audit process. In particular, we would like to thank those officers who were available throughout the audit visit and responded quickly to answer our queries.

Completion

At the date of this report our audit of the financial statements is substantially complete subject to completion of the following areas:

- Clearance of final review points
- Receipt of signed letter of representation
- Final Director closing procedures review.

You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We provided a draft of this representation letter to the Director of Corporate resources on 5 September 2016. We draw your attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are not asking management to provide specific representations on any balances.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of London Councils.



Section three: Financial Statements

Proposed opinion and audit differences



Our audit has identified one audit adjustment of £15k which reduces both debtors and creditors by this amount on the Joint Committee financial statements.

Proposed audit opinion

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Joint Committee, Transport and Environment Committee and Grant Committee financial statements following approval of the Statement of Accounts by the Audit Committee on 22 September 2016.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The materiality (see Appendix two for more information on materiality) level was set at differing levels for each Committee

Committee	Materiality	Trivial
Joint Committee - consolidated	£1,480k	£74k
Joint Committee core	£270k	£13k
Grant Committee	£220k	£11k
Transport and Environment Committee	£980k	£45k

Our audit identified an audit difference, which we set out in Appendix two. It is our understanding that this will be adjusted in the final version of the financial statements.

The table on the below illustrates the total impact of audit differences on the London Council's Joint Committee balance sheet as at 31 March 2016. Further details are included in Appendix three.

There is £nil net impact on the Reserves as a result of audit adjustments; however, the Current Assets and Current Liabilities balance at 31 March 2016 decrease by £15k each. This is the result of the following amendments:

- Overstatement of Debtor - £15k
- Overstatement of Creditor - £15k

Balance sheet as at 31 March 2016

£m	Pre-audit	Post-audit
Property, plant and equipment	1,722	1,722
Other long term assets	1	1
Current assets	21,736	21,721
Current liabilities	(10,590)	(10,575)
Long term liabilities	(23,380)	(23,380)
Net liabilities	(10,511)	(10,511)
Usable reserves	12,641	12,641
Unusable reserves	(23,152)	(23,152)
Total reserves	(10,511)	(10,511)

Proposed opinion and audit differences (cont.)



The wording of your Annual Governance Statement complies with guidance issued by CIPFA/SOLACE in June 2007.

In addition, we identified a small number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 ('the Code'). We understand that London Councils will be addressing these where significant.

Annual governance statement

We have reviewed the Annual Governance Statements and confirmed that:

- It complies with *Delivering Good Governance in Local Government: A Framework* published by CIPFA/SOLACE; and
- It is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Narrative report

We have reviewed the Narrative Statements and not identified any inconsistencies with the Statement of Accounts.

Significant audit risks



We have worked with London Councils throughout the year to discuss significant risks and key areas of audit focus.

Pension Assets and Liabilities - No issues were noted that impacted on the financial statements although we have made a recommendation to strengthen controls

In our *External Audit Plan 2015/16*, presented to you in March 2016, we identified the significant risks affecting the 2015/16 financial statements. We have now completed our testing of these areas and set out our evaluation following our substantive work.

The table below sets out our detailed findings for each of the risks that are specific to London Councils.

Pensions Assets and Liabilities

Risk: London Councils' staff are eligible to participate in the Local Government Pension Scheme (LGPS), administered by the London Pension Fund Authority. There is an inherent valuation estimate in respect of London Councils' defined benefit liability. Pension valuations require a significant level of expertise, judgement and estimation and are therefore more susceptible to error. This is also a very complex accounting area increasing the risk of misstatement.

Findings: As part of our 2015/16 audit, we have checked the information provided to the actuary from London Councils, reviewed the actuarial valuation while considering the disclosure implications, considered assumptions made by your actuaries to benchmarks, which are collated by our KPMG actuaries, and to the assumptions used for 2014/15 for consistency. We also reviewed management's assessment of the accounting requirements to satisfy ourselves that they comply with the requirements of the Local Government SORP for 2015/16. There are no issues impacting on the financial statements that we need to report to the Audit Committee.

Significant audit risks



We have worked with London Councils throughout the year to discuss significant risks and key areas of audit focus.

Fraud risk of revenue recognition - We do not consider this to be a significant risk for London Councils as there is unlikely to be an incentive to fraudulently recognise revenue.

Management override of controls - There are no matters arising from this work that we need to bring to your attention.

In our *External Audit Plan 2015/16* we reported that we would consider two risk areas that are specifically required by professional standards and report our findings to you. These risk areas were Management override of controls and the Fraud risk of revenue recognition.

The table below sets out the outcome of our audit procedures and assessment on these risk areas.

Fraud risk of revenue recognition

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk.

In our *External Audit Plan 2015/16* we reported that we do not consider this to be a significant risk for London Councils as there is unlikely to be an incentive to fraudulently recognise revenue.

This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.

Management override of controls

Risk: Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to this audit.

Findings: In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

There are no matters arising from this work that we need to bring to your attention.

Other areas of audit focus



We have now completed our testing. The table sets out our detailed findings for the area of audit focus.

No issues were noted as a result of these procedures.

In our *External Audit Plan 2015/16* we reported that we would review opening balances as an additional area of audit focus as it was our first year as auditors.

The table below sets out the outcome of our audit procedures and assessment on these risk areas.

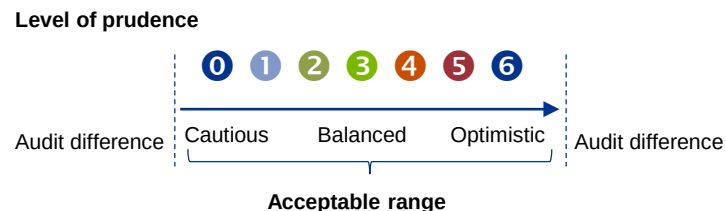
Opening Balances

- **Area of Audit Focus:** The balances reported as the opening position and comparators in the 2015/16 financial statements comprise an integral part of your financial statements and are included within the assurance opinion we provide to you. As this is our first year of your audit, we have to conduct further work over these balances to be able to assure those charged with governance that they are free from material misstatement due to fraud or error.
- **Findings;** We completed the handover process with the previous auditor (PricewaterhouseCoopers) and determined that there were no material issues that we should consider. We performed analysis over the opening balances recorded and agreed them to the audited 2014/15 financial statements.. No issues were noted as a result of these procedures.

Judgements



We always consider the level of prudence within key judgements in your financial statements. We have summarised our view below using the following range of judgement:



Assessment of subjective areas			
Asset/liability class	15/16	Joint Committee Balance (£m)	KPMG comment
Accruals	3	£2.94 million (PY: £3.51 million)	We have agreed a sample of the accruals recorded in your financial statements to supporting documentation, including confirmation of post-year end payment. We have reviewed a sample of post-year end payments to check the cut-off of expenditure recorded in the period and ensured there are no unrecorded liabilities at the year end. Based on the above work, we believe London Council's assessment to represent a balanced view of future payables and within the acceptable range of estimates
Grants	3	£8.97 million (PY: £9.78 million)	We selected items with high value or fluctuations from prior year and agreed these back to supporting documentation, including grant receipts to bank statements. For grants, we agreed a sample of grants back to supporting documentation and confirmed that conditions have been met to release income. We have performed additional procedures over the European Social Fund income, agreeing the budget and award to notification and sample of expenditure items to remittance advice. Based on the above work, we believe London Council's assessment to represent a balanced view of grant income recognised in the period.
Property, Plant and Equipment (valuations / asset lives)	3	£1.72 million (PY: £1.15 million)	We have reviewed management's assessment of property valuations and impairment calculations; confirmed that the asset life assessments were appropriate. Overall, we have concluded London Councils has made a balanced estimate and that the judgements represent a balanced assessment of asset usage.
Pensions	3	£64.18 million (PY: £66.63 million)	We have reviewed the actuarial valuation for pensions and considered the assumptions made by your actuaries in comparison to benchmarks, which are collated by our KPMG actuaries, and to the assumptions used in 2014/15. Our view is that London Councils and its actuaries are balanced in determining the net pension liability and well within the acceptable range of estimates.

Accounts production and audit process



We have noted the high quality of the accounts and the supporting working papers.

Officers dealt efficiently with audit queries and the audit process will be completed within the planned timescales.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of London Councils' accounting practices and financial reporting. We also assessed your process for preparing the accounts and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	We reviewed the methods of financial reporting and various accounting practices throughout our audit. Our review of the financial statements and the method through which they are prepared deemed that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts for each of the committees in line with the agreed deadline.
Quality of supporting working papers	Our <i>Accounts Audit Protocol</i> , which we issued on 6 June 2016 and discussed with the Head of Finance, set out our working paper requirements for the audit. The quality of working papers provided met the standards specified in our <i>Accounts Audit Protocol</i> .
Response to audit queries	Officers resolved the majority of audit queries in a reasonable time. In some cases, however, we experienced small delays, specifically around working papers for payroll and pension data that needed to be provided by the City of London.

Findings in respect of the control environment for key financial systems

We have completed our testing of controls operated during the closedown process and noted some improvements to strengthen the control environment on;

- invoicing of income to be received; and
- Review of information provided by experts for inclusion in the financial statements.

Appendix One provides further details.



We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the financial statements.

Before we can issue our opinion we require a signed management representation letter.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Joint Committee, Transport and Environment Committee and Grant Committee for the year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP and London Councils, its members and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards in relation to independence and objectivity.

We have provided a detailed declaration in Appendix four in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Director of Corporate Resources for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

We are not seeking any specific management representations beyond those considered as standard.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and
- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, opening balances etc.).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report.



Appendices

Appendix 1: Key issues and recommendations

Appendix 2: Audit differences

Appendix 3: Materiality and reporting of audit differences

Appendix 4: Independence and objectivity

Key issues and recommendations

We have given each recommendation a risk rating and agreed what action management will need to take.

London Councils should closely monitor progress in addressing specific risks and implementing our recommendations.

We will formally follow up these recommendations next year.

Priority rating for recommendations

1	Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	2	Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	3	Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.
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No.	Risk	Issue and recommendation	Management response/responsible officer/due date
1	2	Invoicing of Income receivable Where income is due to be collected an income request form should be prepared in order to generate an invoice. During our substantive testing of the income, we found that four out of 20 sampled income transactions did not have an income request form raised and one item had been incorrectly invoiced to the wrong customer but this had subsequently been corrected. Of the remaining 15 items tested, six out of 15 were not authorised in line with the expected procedures.. Recommendation All income due should be supported by an income request form that is fully completed in line with the expected procedures..	This recommendation is accepted and the relevant finance officers have been reminded that official invoices should only be raised on receipt of an appropriately completed invoice request form. Periodic spot checks will be carried out to ensure compliance with the instruction. Recommendation implemented by the Head of Financial Accounting in September 2016.

Key issues and recommendations

We have given each recommendation a risk rating and agreed what action management will need to take.

London Councils should closely monitor progress in addressing specific risks and implementing our recommendations.

We will formally follow up these recommendations next year.

No.	Risk	Issue and recommendation	Management response/responsible officer/due date
2	3	Pension submission reconciliation During our testing on the transactions relating to pensions, we found that there was no evidence to support whether the information provided by the actuary and included within the accounts had been reviewed for reasonableness and reconciled to figures provided to the actuary. Recommendation Evidence of a review of information provided by the actuary, and comparison with data provided should be retained in line with good practice.	This recommendation is accepted and a reconciliation of the information received from the actuary to the payroll data held by London Councils will be performed, documented and retained on an annual basis commencing from the closure of the 2016/17 accounts. Recommendation will be implemented by the Head of Financial Accounting in April 2017

Appendix two

Audit differences

This appendix sets out the audit differences we identified.

The financial statements have been amended for all of the errors identified through the audit process.

There is no net impact on the revenue account.

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Uncorrected audit differences

We are pleased to report that there are no uncorrected factual audit differences (see below for explanation of projected misstatement).

Corrected audit differences

During our debtor and creditor testing, we noted several instances where Q4 admin costs had not been assigned correctly for the European Social Fund grant. This misallocation of costing's lead to both debtors and creditors being overstated.

Officers agreed with the audit adjustments and have adjusted the Joint Committee accounts

Dr Current Creditors	£15,738
Cr Current Debtors	£15,738

Presentational improvements

There were a number of narrative adjustments throughout the accounts and accompanying notes. There was nothing specific to bring to the Audit Committees attention

Materiality and reporting of audit differences

For 2015/16 our materiality for the consolidated Joint Committee was £1.4 million. The materiality levels for the individual Committee's were as follows;

- Joint Committee core - £270k
- Grant Committee - £220k
- Transport and Environment Committee - £980k

We have reported all audit differences over each committee's triviality level, which is as follows;

- Consolidated Joint Committee - £70k
- Joint Committee core - £13k
- Grant Committee - £11k
- Transport and Environment Committee - £45k

Materiality

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

- Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.
- Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.
- Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2015/16, presented to you in March 2016.

Materiality for the Joint Committee accounts was set at £1.48 million which equates to around 2% percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision. For the Joint Committee core statements we have used £270k for materiality.

Materiality for the Transport and Environment Committee accounts was set at £986k which equates to around 2% percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Materiality for the Grant Committee accounts was set at £220k which equates to around 2% percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under ISA 260, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of London Councils, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £70,000 for the Joint Committee overall with £13,000 for its core activities, £11,000 for the Grant Committee and £45,000 for the Transport and Environment Committee.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.

Declaration of independence and objectivity

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the financial statements of the Joint Committee, Transport and Environment Committee and Grant Committee.

General procedures to safeguard independence and objectivity

KPMG's reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the *Ethics and Independence Manual* ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual ethics and independence confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of London Councils for the financial year ending 31 March 2016, we confirm that there were no relationships between KPMG LLP and London Councils, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards requirements in relation to independence and objectivity.

Audit Fees

Our fee for the audit was £35,100 plus for the audit of the financial statements of Joint Committee, Transport and Environment Committee and Grant Committee and £900 plus VAT for the audit of London Councils Limited. This fee was in line with that included within our audit plan agreed by the Audit Committee in March 2016.

Non-audit services

We have not been engaged to provide any non-audit services in the year.



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The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

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