

## **HAMBLETON DISTRICT COUNCIL**

**Report To:** Audit, Governance and Standards Committee  
14 June 2016

**From:** Head of Finance (s151 Officer)

**Subject:** **STATUTORY AUDITOR – INTERIM UPDATE**

All Wards

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### **1.0 PURPOSE AND BACKGROUND:**

- 1.1 The purpose of this report is to enable the Council's statutory auditor, Ernst & Young LLP, to update the Committee on its recent activities. A representative from Deloitte will be in attendance at the meeting to go over the report. It will also provide an opportunity for Members to question the auditor.
- 1.2 The report is attached as Annex A and includes:
- A summary of the work undertaken to date;
  - Changes to the risk assessment in the Audit Planning Report presented to Audit, Governance and Standards Committee on 2 February 2016;
  - An indication of initial materiality estimates for 2015/16 Accounts in the region of £808,000, with unadjusted misstatements to be reported over £200,000.
- 1.3 Also attached at Annex B is Ernst & Young LLP's most recent sector update paper which is provided for information.

### **2.0 RISK MANAGEMENT:**

- 2.1 There are no risks associated with approving the recommendation.

### **3.0 RECOMMENDATIONS:**

- 3.1 It is recommended that Members note the interim update from the external auditor.

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**Background papers:** None

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# External Audit – Interim Update

Hambleton District Council

May 2016



Building a better  
working world

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In April 2015, Public Sector Audit Appointments Ltd (“PSAA”) issued the ‘Statement of responsibilities of auditors and audited bodies 2015-16’. It is available from the Chief Executive of each audited body and via the [PSAA website](http://www.psaa.co.uk) (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 from 1 April 2015’ 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 report is prepared in the context of the Statement of responsibilities. It is addressed to the Audit, Governance and Standards Committee, and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

# Introduction

The purpose of this report is to provide members of the Audit, Governance and Standards Committee with an update on the progress of our external audit for the year ended 31 March 2016. In particular, it covers:

- ▶ A summary of the work we have undertaken to date;
- ▶ Changes to our risk assessment in our Audit Planning Report presented to the Audit Committee on 2 February 2016; and
- ▶ An indication of our initial materiality estimates.

We would welcome any comments or feedback on the content of this report or our work undertaken to date.

We have also provided our latest Audit Committee briefing as a separate paper for your information.

## Audit progress

Our audit team was onsite for the interim audit visit in the week commencing 8 February 2016 during which we completed the following audit procedures:

- ▶ We performed walkthroughs of the material financial systems of the Council to update our understanding of the financial processes followed;
- ▶ We met with Internal Audit to assist us in developing our understanding of the control environment of the Council;
- ▶ We obtained and reviewed documentation for the following significant transactions that have taken place in 2015/16:
  - ▶ Purchase of HMP Northallerton; and
  - ▶ Broadacres loan;
- ▶ We met with Officers to update our understanding of other significant audit and accounting matters to have occurred during 2015/16;
- ▶ We have obtained data downloads from the general ledger and payroll systems to test our data analytics tools in advance of their use at the year-end; and
- ▶ We performed a review of the 2014/15 statutory accounts against the requirements of the Code.

There were no significant findings arising from our interim audit work for reporting to the Audit, Governance and Standards Committee.

## Changes to our risk assessment

Following completion of our interim audit visit, we reviewed the risk assessment in our Audit Plan presented to the Audit, Governance and Standards Committee on 2 February 2016 and propose the following change.

### **Change in risk classification – accounting for pension obligations**

In our Audit Plan we identified 'accounting for pension obligations' as a significant risk. The reason being that the pensions liability is the most significant liability on the Council's balance sheet and is calculated through use of a number of actuarial assumptions and a small movement in these assumptions could have a material impact on the Statement of Financial Position.

For a risk to be designated as 'significant' for the purposes of our audit, there needs to be a higher likelihood of the risk occurrence and higher likelihood of material misstatement. We have reconsidered our original assessment and, although it is true that a small movement in the assumptions could result in a material impact on the liability, we do not consider that there is a high likelihood that misstatement could occur for the following reasons:

- ▶ The Council uses an actuary with significant experience in calculating local government pension scheme liabilities; and
- ▶ There have not been any issues identified with the assumptions used by the actuaries in previous years.

On this basis we propose that we downgrade accounting for pensions obligations from a significant risk to an 'other area of audit focus'.

We seek approval from the Audit, Governance and Standards Committee to make this change to our Audit Plan.

## Materiality update

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality also provides a basis for identifying and assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures.

In our Audit Plan presented to the Audit, Governance and Standards Committee on 2 February 2016, we committed to provide you with an update on our proposed materiality levels. At this stage, we consider the most appropriate basis for assessing materiality for the Council to be 2% of expenditure for the year. Based on 2014/15 expenditure in the audited accounts, we anticipate planning materiality to be in the region of £808,000. We will report all unadjusted misstatements over £200,000 identified during the course of our audit to the Audit, Governance and Standards Committee.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all the circumstances that might ultimately influence our judgement. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

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# Local government audit committee briefing

March 2016

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This sector briefing is one of the ways that we hope to continue to support you and your organisation in an environment that is constantly changing and evolving.

It covers issues which may have an impact on your organisation, the Local government sector and the audits that we undertake. The public sector audit specialists who transferred from the Audit Commission form part of EY's national Government and Public Sector (GPS) team. Their extensive public sector knowledge is now supported by the rich resource of wider expertise across EY's UK and international business.

This briefing reflects this, bringing together not only technical issues relevant to the local government sector but wider matters of potential interest to you and your organisation.

Links to where you can find out more on any of the articles featured can be found at the end of the briefing, as well as some examples of areas where EY can provide support to Local Authority bodies. We hope that you find the briefing informative and should this raise any issues that you would like to discuss further please do contact your local audit team.



# Government and economic news

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## Devolution

In EY's report 'From Whitehall to Townhall Preparing for devolution to England's city regions' it is noted that the UK has lagged behind other countries in decentralising its governance. But in recent years, 'localism' has gained momentum. In the last Parliament, the coalition government took a number of steps to empower city regions – through the creation of local enterprise partnerships, and City and Growth Deals – and the pace of change is quickening.

Large parts of England have started to agree Devolution Deals, which transfer powers in policy areas such as housing, planning and transport, education, employment, skills, health and policing. Eight deals have been announced so far, with five metro areas agreeing to directly elected mayors, and almost every other part of the country is involved in discussions. The recent progress is testament to the credibility that local government has established – with both the government and the public – as local leaders with a vision for local economies and wise stewards of public funds.

The UK is at an early stage of the devolution journey; much work still needs to be done. But the prize could be considerable. If managed well, it could help stimulate local economies to achieve higher levels of job creation and growth; improve public service outcomes through better local coordination of resources and funding; revitalise local democracy through more accountable governance; and improve the sustainability of public finances.

In this short report we look at progress so far and outline the factors that have driven success in winning more powers. We reflect on the readiness of different areas to make a success of devolution and speculate on the long-term impact on local government.

The debate will continue for some time to come, and lessons will be learned along the way. Drawing on our experience of working with a number of local authorities and cities, we are committed to helping facilitate debate and sharing best practices to help local government deliver the best services and outcomes to their communities and citizens.

## Retention of business rates

The Government has announced that for 2016/17, Councils across England expect to collect £23.5 billion from business rates. This is an increase of approximately £400 million, in part it is believed this is due to an increase in the number of new businesses across the country.

Under existing rules, councils are expected to retain £11.75 billion of the rates collected; however, in the 2016 Budget, George Osborne indicated that from 2017, 100% business rates retention would be piloted in Greater Manchester and Liverpool City Region, and that in London the share retained would be increased.



## Government and economic news

### Budget 2016

16 March saw the publication of Budget 2016.

On public finances, the Chancellor announced that a departmental efficiency review was expected to identify a further £3.5 billion of savings in 2019/20. Employer pension contributions for public sector pensions are also set to increase from 2019/20, with a reduction in the public service pension scheme discount rate.

Some other announcements included:

- ▶ All schools are expected to either become academies by 2020, or to have an academy order in place to convert by 2022.
- ▶ New mayoral devolution deals will be agreed with the West of England, East Anglia and Greater Lincolnshire. Additional deals will be agreed with Greater Manchester and Liverpool City Region; including working towards the devolution of criminal justice powers. Previously agreed deals will also receive unringfenced funding totaling £2.86 billion to support local priorities.
- ▶ Starting from 1 April 2017, business rates will be cut for half of all properties. Small business Rate Relief will be permanently doubled from 50% to 100%, and the threshold from which this applies will be increased so that it applies to properties with a rateable value of £12,000 and below. The threshold for the standard business rates multiplier will also be increased to those with a rateable value of £51,000. The budget comments that local government will be compensated for the loss of income as a result of these measures.

- ▶ From 2020, business rates annual indexation will be based on CPI rather than RPI. The government will also aim to introduce more frequent business rate revaluations. The government intends to outline options for achieving this in a discussion paper.
- ▶ The government will work with local authorities across England to standardise business rate bills and to provide ratepayers with the option of receiving and paying bills online by April 2017.
- ▶ The government plans to support Local Government Pension Scheme administering authorities' plans to establish a smaller number of British Wealth Funds by combining assets into larger investment pools by 2018. These pools are expected to deliver annual savings of £200-300 million or more.

### Off-Payroll working in the public sector

Budget 2016 included an announcement that it would reform the 'intermediaries' legislation' for public sector engagements.

This legislation dates back to 2000, and requires individuals who are working through an intermediary company to pay approximately the same tax and National Insurance contributions as they would if they were direct employees. Typically, intermediary companies have been an individual's own limited company. There is widespread non-compliance, perhaps because many find these rules confusing.

From April 2017, the liability to pay the correct employment taxes will transfer from the worker's own company to the public sector body that is paying the company. These changes, which are intended to be introduced by the 2017 Finance Bill, will be subject to consultation.



# Accounting, auditing and governance

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## PSAA Corporate Plan

Public Sector Audit Appointments (PSAA) published its Corporate Plan 2015-2018 in early 2016. PSAA was set up to manage the audit contracts which were originally let by the Audit Commission, and to put arrangements in place to support the new audit regime established through the Local Audit and Accountability Act 2014.

The Corporate Plan sets out three options available to audited bodies for appointing auditors from the financial year 2017/18 and onwards for NHS bodies and smaller local authorities; and from the financial year 2018/19 and onwards for principal local authorities and criminal justice bodies:

- ▶ Undertake an individual auditor procurement and appointment exercise.
- ▶ Undertake a joint audit procurement and appointing exercise with other audited bodies, e.g., those in the same locality.
- ▶ Join a 'sector led body' arrangement.

The Local Government Association's subsidiary, the Improvement and Development Agency (IDeA), has said that it wishes to secure the establishment of a sector led body to support audit appointments. It also considers that PSAA would be well placed to fulfil this role. Since local government bodies need to appoint auditors for the 2018/19 financial year by 31 December 2017, arrangements for a sector led body will need to be in place in 2016 to prepare for contract letting.

The Corporate Plan also includes the PSAA's current plans around redistribution of surplus fees to audited bodies:

1. For NHS bodies, the anticipated amount for redistribution is approximately 10% of 2016/17 scale audit fees, with expected payments in 2017.
2. For local government bodies, the anticipated amount is approximately 15% of 2017/18 scale audit fees, with expected payments in 2018.

The redistribution is subject to confirmation and approval from the PSAA Board.



# Accounting, auditing and governance

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## Flexibility on use of capital receipts in Local Government

In the 2015 Spending Review, the Government announced its intention to give local authorities the right to use capital receipts on the revenue costs of certain projects.

Two final directions for local government were issued in March 2016; one covering police and crime commissioners, and the other covering councils and fire authorities. There is also a general direction with further guidance.

These direct local government bodies to treat expenditure which is 'designed to generate ongoing revenue savings in the delivery of public services and/or transform service delivery to reduce costs and/or transform service delivery in a way that reduces costs or demand for services in future years for any of the public sector

delivery partners' as capital expenditure for expenditure incurred for the three financial years commencing 1 April 2016.

Expenditure which is treated as capital under these directions can only be funded from capital receipts which have been received in the same time period.

The general direction also states that each authority will need to disclose a Strategy which sets out the individual projects that will be funded or part funded through capital receipts flexibility. This should be presented to full Council or the equivalent either as part of the annual budget setting process, through the Mid-Term Financial Plan or equivalent, or as part of the Efficiency Plan.

The strategy setting out these projects should be prepared in advance of the start of each financial year where possible, or presented to full Council or the equivalent as soon as possible.



## Regulation news

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### The state of health care and adult social care in England

The Care Quality Commission has, based on a body of evidence across health and social care, published the above report aiming to give a full picture of the quality of care in England and identify and share key aspects of high-quality care/driving improvement.

Amongst the key messages in the report are:

- ▶ **Safety** – safety remains the biggest concern across all services, with 13% of hospitals, 10% of adult social care services, and 6% of primary medical services rated as inadequate for safety. The report highlights the rating of significant numbers of services as 'requires improvement'. Safety is seen to be affected by various factors including, ineffective safety and risk management systems, failure to fully investigate and learn from incidents, and, (in hospitals and adult social care) concerns with the adequacy of staffing numbers and skill mix.
- ▶ **Delivering quality under pressure** – efficiency savings, to meet the more complex needs of an older, changing population, at the same time as ensuring that the health and care system remains sustainable for the future, nearly 60% of adult social care and over 80% of GP practices were rated good or outstanding. At the same time the report highlights variation in quality, including between different services from the same provider and between different providers.
- ▶ **Ability to improve** – the report highlights an increase in enforcement actions from 4% in 2013/14 to 7% in 2014/15, and that initial results show that, on re-inspection, more than half of services were able to improve their ratings within six months.
- ▶ **What it takes to be outstanding** – the report emphasises that high-quality care can be provided under constrained financial conditions through managing resources well. Good and Outstanding providers are not simply relying on more money, the report highlighting that over 90% were also good or outstanding for their leadership.
- ▶ **Data and transparency** – across all sectors, continuing development of better data, which is available to all stakeholders is seen as important, particularly for adult social care and community and mental health services. In the absence of such information, understanding the quality of care beyond inspections, (or assessing the impact that changes are having on quality of care) is difficult.



## Regulation news

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### Personalised commissioning in adult social care

The National Audit Office (NAO) has recently published a report on commissioning in adult social care. Although personal budgets became mandatory for all eligible users from April 2015 under the Care Act, the NAO has concluded that the Department of Health (DH) requires a deeper understanding of implementing personalised commissioning in the best ways.

Long-term community care accounted for £6.3 billion of local authority spend in 2014/15, and the DH has plans to extend this.

The NAO also highlighted a difference in expectations between the DH and local authorities. Local authorities expect that savings can be made by personalising care, whereas DH anticipates improved value for money through improved outcomes. The Care Act guidance noted that responding to the needs of users and their desired outcomes could increase the cost of care, whereas

some local authorities are finding personalising commissioning challenging because of their need to reduce overall spending.

Current monitoring arrangements do not allow the Department to wholly understand how personal budgets and direct payments can lead to improved outcomes. Nor has it looked at how personal budgets can work when finances are challenged.

Amyas Morse, Head of the NAO, said:

“Giving users more choice and control over their care through personal budgets and direct payments can improve their quality of life, but much of the positive evidence for personalised commissioning of adult care services is old. The Department now needs to gain a better understanding of the different ways to commission personalised services for users, and how these lead to improvements in user outcomes.”



## Regulation news

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### Highways Network Asset

CIPFA has published a consultation on the **Draft Code of Practice on the Highways Network Asset** (HNA Code) with a closing date of 6 April 2016.

The draft HNA Code includes the following definition of the Highways Network Asset:

**Highways Network Asset is a network and grouping of interconnected inalienable components, expenditure on which is only recoverable by continued use of the asset created, i.e., there is no prospect of sale or alternative use. The interconnected network is made up of carriageways, footways and cycleways and the structures, street lighting and other assets that are directly associated with them.**

CIPFA is producing a series of briefings to support local authorities in the implementation of the new measurement requirements. The second briefing in this series is available from the CIPFA website, and includes guidance on reporting requirements for 2015/16. It notes that the requirements to restate opening balances at 1 April 2015 and prior year comparatives in the financial statements for 2016/17 relating to the Highways Network Asset has now been removed. Please liaise with your auditor to discuss how this will affect your organisation.

### 2016/17 work programme and scales of fees

The PSAA has published the work programme and scale of fees for 2016/17 audits of principal audited bodies. This set out the work the auditors will undertake for 2016/17 with associated scale fees for individual audited bodies. The key points are:

- ▶ No change to the overall work programme for 2016/17.
- ▶ Scale fees for 2016/17 have been set at the same level as the 2015/16 fee.

<http://www.psa.co.uk/audit-and-certification-fees/201617-work-programme-and-scales-of-fees/>



## Key questions for the audit committee

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### What questions should the Audit Committee be asking itself?

What assumptions have we included regarding business rates income in our medium term financial plan, and how is this impacted by the changes announced in Budget 2016, such as the increase in Small Business Rates Relief?

Have we determined how we will procure our external audits for the financial year 2018/19 and onwards?

Have we discussed and considered the advantages and disadvantages of the three possible approaches to procurement?

Have we considered how we can use capital receipts to support revenue projects?

Have we considered whether our savings requirements in the short and medium term impact on our capacity to meet the objectives of Personalised Commissioning and how we can address this?

Have we considered the impact of the Highways Network Assets, and are we prepared for this change?



## Find out more

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### **Devolution**

The full EY report is available at  
<http://www.ey.com/UK/en/Industries/Government---Public-Sector/EY-From-Whitehall-to-Townhall>

### **Retention of business rates**

See the government announcement at:  
<https://www.gov.uk/government/news/record-business-rates-predicted-as-devolution-revolution-kicks-off>

### **Budget 2016**

The full budget report is available at:  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/508193/HMT\\_Budget\\_2016\\_Web\\_Accessible.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/508193/HMT_Budget_2016_Web_Accessible.pdf)

See also EY's Budget alerts at:  
<http://www.ey.com/UK/en/Services/Tax/Budget>

### **Off-payroll working in the public sector**

Read more about the government's proposed changes at:  
<https://www.gov.uk/government/publications/off-payroll-working-in-the-public-sector-reforming-the-intermediaries-legislation>

### **PSAA Corporate Plan**

To read the Corporate Plan in full – visit:  
<http://www.psaa.co.uk/wp-content/uploads/2016/01/PSAA-Corporate-Plan-2015-2018.pdf>

### **Flexibility on use of capital receipts in Local Government**

See the final guidance and the issued directions at:  
<https://www.gov.uk/government/publications/guidance-on-flexible-use-of-capital-receipts>

### **The state of health care and adult social care in England**

Visit: <http://www.cqc.org.uk/content/state-care-201415>

### **Personalised commissioning in adult social care**

Find out more at:  
<https://www.nao.org.uk/press-releases/personalised-commissioning-in-adult-social-care/>

### **Highways network asset**

Read the consultation and respond via the CIPFA website at:  
<http://www.cipfa.org/policy-and-guidance/consultations/hna-consultation>

For further guidance on the implementation of the Highways Network Asset, see:  
<http://www.cipfa.org/policy-and-guidance/local-authority-highways-network-asset>

### **2016/17 work programme and scales of fees**

For further information:  
<http://www.psaa.co.uk/audit-and-certification-fees/201617-work-programme-and-scales-of-fees/>



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