

# AUDIT COMMITTEE

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**Tuesday, 23 July 2019 at 6.30 p.m.**

**Committee Room One - Town Hall Mulberry Place**

## **SUPPLEMENTAL AGENDA**

**This meeting is open to the public to attend.**

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**4. DELOITTE ITEMS FOR CONSIDERATION**

**4 .1 External Audit Report 2018-19**

**3 - 34**



## London Borough of Tower Hamlets

Report to the Audit Committee on the audit for the year ended 31 March 2019

Issued 19 July 2019 for the meeting on 23 July 2019

Deloitte Confidential: Government and Public Services

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# Introduction

## The key messages in this report

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the financial statements.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

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We have pleasure in presenting our final report to the audit committee of Tower Hamlets Council (the Council) for the 2019 audit. The scope of our audit was set out within our planning report presented to the committee in April 2019.

### **Status of the audit**

Our audit is ongoing and will not be completed prior to the deadline of 31 July for the publication of the statement of accounts.

This is because of delays in delivery of supporting working papers for audit from management and delays in receiving information and explanations in response to subsequent audit queries. We provide further detail on page 17 and 18. There are also open issues which need to be resolved prior to finalisation of our report on the financial statements. We have commented on the more significant items throughout this document.

This report does not cover the findings from our work to support our separate opinion on the pension fund financial statements. We would ordinarily expect to present a second report to this audit committee on the findings from that work. However, as we did not receive a trial balance and supporting work papers for the pension fund prior to the end of our scheduled audit visit, our work is not sufficiently advanced to be able to do so.

Officers have commented that it has been challenging within the reduced time now allowed by the statutory timetable for the publication of its statement of accounts to prepare the draft accounts and requested supporting information and carry out an internal quality review of the accounts and supporting documentation.

This year has been particularly challenging as the time needed to implement the restructuring has reduced the time available to officers for preparatory work ahead of the main accounts closure and audit period and meant that some activities have needed to be carried out by staff who are new into role. The finance team have also needed to respond to the higher volume of audit queries that is typical for a first year audit.

In these circumstances, the finance team has done well to meet its statutory obligation to publish its draft accounts by the 31 May deadline but needs to allow time within its overall closure timetable for preparation of a full set of supporting working papers and completion of all internal quality assurance processes prior to the start of the audit to enable the subsequent audit to be carried out efficiently and on time.

We have included a section in this report providing observations arising from the work we have so far carried out on the areas of significant risk and other areas of audit focus reported to you in our audit planning report. We have not included any commentary on our work on the significant risk of fraudulent misstatement of the financial statements through management override of controls. This work includes a test of journals which may exhibit characteristics which are indicative of fraud. We have not been able to start this work as we were only provided with a full data set which we can profile and select journals to test as were finalizing this document. We also look at whether there is evidence of management bias in estimates. Again we were provided with information relating to a number of estimates including information on how officers have calculated certain provisions and bad debt provisions as we were finalizing this report.

# Introduction

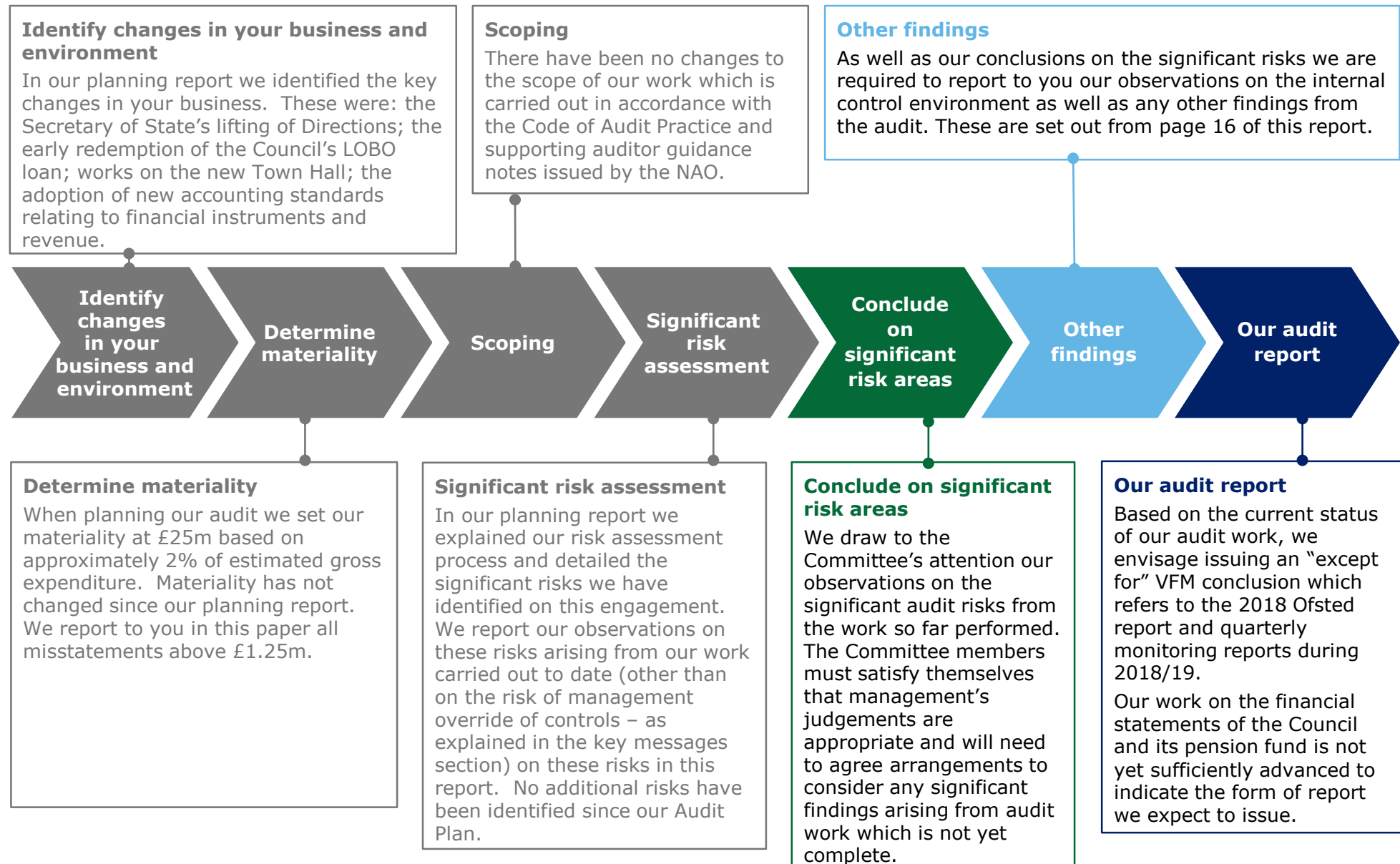
## The key messages in this report (continued)

<b>Conclusions from our testing</b>	<p>We have set out a summary of misstatements and disclosure deficiencies identified to date in an appendix to this report. As our audit work is ongoing, further misstatements may be identified through the completion of our remaining work.</p> <p>Based on the current status of our audit work, we envisage issuing a qualified “value for money conclusion” as Ofsted’s 2018 report and subsequent monitoring reports provide evidence (notwithstanding the improvement trajectory) that proper arrangements to secure to secure economy, efficiency and effectiveness in the use of resources were not in place throughout the whole of the period covered by our conclusion in that respect. Similar to last year, this will be on an “except for” basis, rather than an “adverse” basis.</p> <p>Our work on the financial statements of the Council and its pension fund is not yet sufficiently advanced to indicate the form of report we expect to issue.</p>
<b>Narrative Report and Annual Governance Statement</b>	<p>We have reviewed the Council’s Narrative Report and the Annual Governance Statement to consider whether it is misleading or inconsistent with other information known to us from our audit work.</p> <p>In our audit planning report we said that the Narrative Report in the Council’s 2018 annual financial report was significantly shorter than the average for London Boroughs and did not cover all of the items set out in the guidance in the CIPFA Code of Practice on Local Authority Accounting (the Code). The Narrative report in the Council’s 2019 draft annual financial report is similar in length and content to the 2018 Report and therefore does not comply with the Code guidance.</p>
<b>Duties as public auditor</b>	<p>We did not receive any queries or objections from local electors this year.</p> <p>We did not identify any matters that would require us to issue a public interest report.</p> <p>We have not had to exercise any other audit powers under the Local Audit and Accountability Act 2014.</p>
<b>Audit certificate</b>	<p>We are not able to issue our certificate until the certificates for earlier years have been issued. The prior year certificate has not yet been issued as we understand our predecessor is still considering objections. We do not have information on when our predecessor expects to conclude this work.</p> <p>We are also not able to issue our certificate until we have completed our work on the Council’s Whole of Government Accounts (WGA) return and pension scheme annual report. As there is a later reporting timetable for the issue of our opinion on the WGA return and pension scheme annual report, we do not expect this work to be complete by the time of issue of our opinion on the Council’s statement of accounts.</p>
<b>Audit fee</b>	<p>As explained in our fee letter, our audit fee is based on assumptions about the scope of our work and the completeness and quality of information provided to support the draft financial statements and the timeliness and quality of responses to subsequent requests for information and explanation. We expected our audit to be complete at this point but for the reasons set out above and on page 17 it is ongoing. We estimate the amount of additional cost incurred to date to be £15-20k and the further time needed to complete the audit from this point all represents additional cost which will be charged using the rate card in the appendix.</p>

# Our audit explained

## We tailor our audit to your organisation

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# Significant risks

## Valuation of property assets

### Risk identified

The Council is required to hold property assets within Property, Plant and Equipment at valuation. The valuations are by nature significant estimates which are based on specialist and management assumptions and which can be subject to material changes in value.

### Key judgements and our challenge of them

The Council held £2,043m of property assets at 31 March 2019, a reduction of £184m, including a net revaluation loss of £218m and £88m of additions.

The Council updates the valuation of its properties using a rolling revaluation programme. In 2018/19, it engaged valuers to carry out the following valuation exercises:

- Perform a desktop valuation of schools. The effective date of this valuation was 31 March 2019;
- Perform a full valuation of Council dwellings. The effective date of this valuation was 1 April 2018; and
- Perform a full valuation of other properties due for valuation under the Council's 5 year rolling programme of valuations. The effective date of this valuation was 1 April 2018.

In addition, the Council commissioned its valuer to perform a market review providing information on market changes across 2018/19. On the basis of information in this report, the Council elected to adjust the valuation of dwellings provided by the valuer to account for market changes during 2018/19.

The revaluation loss arose as follows:

- Council dwellings – a revaluation loss of £167m, of which £113m arose on the valuation performed by the Council's valuer with an effective date of 1 April 2018 and £54m on adjustments made by the Council to that valuation to take account of market changes during 2018/19;
- Schools – a valuation loss of £39m arising since the last valuation (which had an effective date of 1 April 2017); and
- Other assets – a valuation loss of £13m arising on market and other changes in the period from 1 April 2013 to 1 April 2018.

### Deloitte response

- We tested the design and implementation of key controls in place around the property valuation, including how the Council assures itself that there are no material impairments or changes in value for the assets not covered by the annual valuation.
- We obtained an understanding of the approach to the valuation, including assessing the valuer's qualifications, objectivity and independence and reviewing the methodology used.
- We used our valuation specialists, Deloitte Real Estate, to review and challenge the appropriateness of the assumptions used in the valuation of the Council's property assets.
- We considered the impact of uncertainties relating to the UK's exit from the European Union upon property valuations in evaluating the property valuations and related disclosures.
- We have planned tests of inputs and the calculation of the movement to be recorded in the financial statements to check correctly recorded.

### Status of our work and issues identified

Our work in response to this risk is ongoing.

We have identified control deficiencies and made recommendations for improvement on page 18.

As described above, the Council's finance team, and not its valuer, has determined the closing valuation of dwellings, using an index extracted from the market review report provided by its valuer.

The way in which the finance team has arrived at the closing valuation is not as we would expect. We are discussing with officers whether an adjustment is needed and recommend going forwards that all valuations are carried out by a qualified valuer.

The Code does not require properties to be revalued on an annual basis, but does require valuations to be carried out where there has been a material change.

The Council assesses whether there has been a material change over the financial year through its review of the market review report commissioned from its valuer. On the basis of this review, officers have concluded that there has not been a material change in the value of non dwelling properties which were not subject to valuation at the year end. The Council has not determined the level of change it considers to be material or evaluated the possible cumulative change since the date of the last valuation of properties (noting that for some properties this is earlier than the start of the financial year). We have requested this assessment to be prepared before we finalise our conclusion.



# Significant risks (continued)

## Capital expenditure

### **Risk identified**

The Council has a substantial capital programme of £0.6bn over the next three years, including £114m on Property, Plant and Equipment and £18m on revenue expenditure which, for funding purposes, is treated in the same way as capital expenditure (REFCUS) in 2018/19.

Determining whether or not expenditure should be capitalised can involve judgement as to whether costs should be capitalised under International Financial Reporting Standards.

The Council has greater flexibility over the use of revenue resource compared to capital resource. There is also, therefore, an incentive for officers to misclassify revenue expenditure as capital.

### **Deloitte response**

- We tested the design and implementation of controls around the capitalisation of costs.

We selected a sample of capital items (including REFCUS) in the year to test whether they have been appropriately capitalised in accordance with the accounting requirements.

### **Status of our work and issues identified**

We have identified control deficiencies on page 20.

Our work is not yet concluded as we have not received information for some sample items. We have not identified any exceptions for the items where we have received full information.

# Other matters

## Pension liability relating to the Tower Hamlets Pension Fund

### Background

The Council participates in the fund it administers, as well as the Local Government Pension Scheme fund administered by the London Pension Fund Authority (LPFA). Our comments on this page deal with the much larger liability relating to the Council's own pension fund and not to the liability relating to the LPFA fund.

The Council's pension liability is affected by the McCloud legal cases in respect of potential discrimination in the implementation of transitional protections following changes in public sector pension schemes in 2015. Subsequent to year-end, the Government was denied leave to appeal the case, removing the uncertainty over recognition of a liability. The actuary has not estimated the impact on the Council's liability but we understand has advised the Council that he does not expect the impact would be significant.

### Deloitte response

- We obtained a copy of the actuarial report for the Council Pension Fund produced by Hymans Robertson, the scheme actuary, and agreed in the disclosures to notes in the accounts.
- We assessed the independence and expertise of the actuary supporting the basis of reliance upon their work.
- We reviewed and challenged the assumptions made by Hymans Robertson, including benchmarking as shown in the table opposite.
- We assessed the reasonableness of the Council's share of the total assets of the scheme with the Pension Fund financial statements.
- We have reviewed and challenged the calculation of the impact of the McCloud case on pension liabilities.
- We performed substantive analytical procedures on movements.
- We reviewed the disclosures within the accounts against the Code.

	Council	Benchmark	Comments
Discount rate (% p.a.)	2.40%	2.36%	Within threshold
Consumer Price Index (CPI) Inflation rate (% p.a.)	2.50%	2.25%	Optimistic
Salary increase (% p.a.) (over RPI inflation)	-1.2%	n/a	Entity specific assumption. See below
Pension increase in payment (% p.a.)	2.5%	2.25%	Within threshold

### Deloitte commentary on findings to date

Our work is ongoing. The Council has not adjusted the pension liability for the impact of the McCloud case, in view of the advice from its actuary that adjusting for this would not have a significant impact. The scale of impact is in particular driven by assumptions on future salary increases and the age of the membership. An exercise performed by the Government Actuaries Department indicates that based on a salary increase of CPI and using the average age for the LGPS scheme as a whole of 46, the McCloud judgement would result in an increase in the pension liability relating to active members of 0.1% (or not more than £0.8m for the Tower Hamlets Pension Fund). The salary increase assumption used to calculate the pension liability relating to the Tower Hamlets Pension Scheme and the average age of the active membership is 52 years – both these factors indicating a smaller impact. We have noted that the Council has assumed a higher rate of salary increase in determining the value of its pension liability in respect of the London Pension Fund Authority (LPFA). We understand that that this is because the selection of the assumption was in this case driven by the fund actuary. The Council has only 31 active members in the LPFA fund and therefore neither the additional liability arising from the McCloud judgement, nor the base pension liability is significantly impacted by this assumption. This is not the case for the Council's own fund. Whilst the lower assumed salary increase is not inconsistent with recent experience or assumptions made in the Council's Medium Term Financial Strategy, the Council needs to be assured that it represents its best estimate.

The actuary has calculated the liability using membership information collected for the 2016 funding valuation. We have asked the Council for their assessment of whether there have been any significant member movements impacting on valuation of the liability. The actuary has also estimated the pension assets and not used actuals. The estimate is approximately £28m higher than the Council's share of the net assets shown in the pension fund financial statements and we have asked officers to assess the impact of this.

# Other matters (continued)

## Implementation of IFRS 9 and IFRS 15

### Matter identified

The Council is required to adopt the new accounting standards IFRS 9 *Financial Instruments* and IFRS 15 *Revenues from contracts with customers* in the year ended 31 March 2019. In both cases, the Council is using a modified retrospective approach to implementation where effectively the cumulative impact of transition to 1 April 2018 is posted as an adjustment to reserves.

The scope of IFRS 9 and IFRS 15 is limited to balances arising on "exchange" transactions. Non-exchange debtors, such as council tax, business rates and parking fines are outside of the scope of IFRS 9 and IFRS 15.

The Council has posted no retrospective adjustments with regard to IFRS 9 or IFRS 15 as there is no material impact on the financial statements.

### Response

We understand that officers held discussions on the impact of the new standards as part of the accounts closure process and concluded that there was no material impact but did not prepare a paper setting out information on their process, findings as support for this conclusion.

The statement of accounting policies in the original version of the financial statements had not been updated to reflect changes introduced by IFRS 9 including the classification of financial instruments and a different credit loss impairment model.

The key accounting impact of IFRS 9 is on the calculation of the bad debt provision, which must move to a methodology of expected credit losses. We have received information for the calculation of only one of the bad debt provisions and are therefore not yet able to assess whether or how officers have addressed changes in the way in which impairments should be calculated.

IFRS 9 also introduces new or changed disclosure requirements. The Council's accounts template was not updated for these changes and as a result the financial statements do not fully comply with the Code in this respect.

Regarding IFRS 15, officers were satisfied that no transitional adjustments would be required as the Council's larger sources of income including grant income, rents and taxation are outside of the scope of the standard and in other income streams which fall within the scope of IFRS 15 there are not material performance obligations which span the year end. This is consistent with a general expectation for local authorities which have not entered into material unusual transactions.

Again, the statement of accounting policies was not updated to bring the description of the Council's policy for the recognition of income into line with the requirements of IFRS 15.

IFRS 15 introduces new disclosures around the amount of income, deferred income and receivables which are accounted for under the standard. The Council's accounts template was not updated to include these new disclosures and as a result the financial statements do not fully comply with the Code in this respect.

The Council has not made any disclosure of the impact of the transition.

### Deloitte view

Officers conclusion that the new accounting standards do not have a material impact for the Council is consistent with the conclusion of other local authorities and the absence of unusual transactions or income streams which may require a different accounting treatment. We have noted uncorrected disclosure deficiencies in the appendices to this report.

# Other matters (continued)

## Other financial reporting matters

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Area	Observation
<b>Accounting policies</b>	<p>The Council has utilised example accounting policies published by CIPFA. As a result, the policies as described are standard for a local authority and comply with the Code. We have not identified any significant unusual income or expenditure transaction types or balances which require additional commentary to be added to the statement of accounting policies.</p>
	<p>In our planning report we highlighted recent guidance issued by CIPFA to local authorities to support them in streamlining their published financial statements. The Council has not taken the opportunity to review its statement of accounting policies so that only important and relevant information is included. As a result the statement includes accounting policies dealing with account balances, or aspects of the accounting, which are immaterial.</p>
<b>Critical accounting judgments</b>	<p>As explained further in the section on IFRS 9 and IFRS 15, accounting policies have not been updated to reflect changes in the Code resulting from the adoption of these standards or updated for a change to accounting standards incorporated into the Code in an earlier year relating to pension accounting.</p>
	<p>IAS 1 requires entities to make disclosures about the assumptions it has made about the future and other major sources of estimation uncertainty at the year end that have a significant risk of resulting in a material adjustment to the carrying amount of assets and liabilities within the next financial year. This situation would arise, for example, where an uncertain factor could cause the carrying amount of an asset or liability to change materially in the next year. This is an important disclosure as it helps a user of the accounts assess an entity's financial position and performance and understand the sensitivities to changes in assumptions.</p>
	<p>If a matter does not meet the criterion above, it should not be included in the disclosure on sources of estimation uncertainty. In our audit planning report we recommended that in preparing the 2018/19 statement of accounts, the Council re-look at whether the estimates it had disclosed in the prior year met this criterion.</p>
	<p>IAS 1 states that disclosures should be presented in a way that helps users of the financial statements to understand the judgements management makes about the future and about other key sources of estimation uncertainty.</p>
	<p>The Council's current disclosure, for example, includes the provision for NNDR appeals as a source of key estimation uncertainty. The provision made in the balance sheet is £1.3m. If the Council considers that there are changes in assumptions that are considered reasonably possible and which would lead to a material impairment, this is not clear from the disclosure and further disclosure would need to be added. If the Council considers that the provision could not be material under a range of reasonably possible outcomes, the item should not be included within the disclosure.</p>
	<p>This is a disclosure deficiency and request that this is addressed in the final version of the accounts.</p>

# Other matters (continued)

## Other financial reporting matters

Area	Observation
Infrastructure assets	The Council does not record infrastructure assets separately on the fixed asset register. Instead expenditure on infrastructure assets is grouped by type and by year of expenditure.
	Part of the annual amount capitalised relates to replacement of a component of asset (e.g. road re-surfacing). In this situation, whilst it may be appropriate to capitalise the new expenditure, an adjustment should be made to remove the existing component from the register and fixed asset balance. It is not part of the Council's process to do this and the organisation of the fixed asset register does not facilitate this.
	This practice is not uncommon in the sector and does not have a significant impact on the carrying amount of infrastructure assets where the actual asset lives approximate to the estimate of useful economic life used in the depreciation calculation (such that the asset or component of the asset has a nil net book value at the point of replacement).
	The Council's policy is to depreciate all infrastructure assets over a life of 40 years. We have benchmarked this against other authorities. A sample of 10 London Boroughs assigned a minimum life, on average, of 16 years and a maximum of 25 years, on average, to infrastructure assets. There is a risk both that the Council is depreciating infrastructure assets too slowly and is double-counting the cost of replacements with the remaining value of the asset which has been replaced. The impact on the depreciation charge of changing from a life of 40 years to 20 years would be to increased depreciation by £3.9m. The value of assets which were created more than 16 years ago (i.e. the average minimum life above) is £42m. We have requested officers either provide information supporting the appropriateness of the assigned life or, if they consider this life not to be appropriate, an estimate of the impact of the error.
Cash flow statement	The Council has included Money Market Funds (MMFs) and pooled investments within cash equivalents. Money market funds and pooled funds are generally excluded from cash equivalents unless it can be demonstrated that the particular assets are 'readily convertible to known amounts of cash' and 'subject to insignificant risk of changes in value'. This involves a careful assessment of factors such as the investment rules of the fund, controls over management of the fund's net asset value and mechanisms for redemption in stressed market conditions.
	This type of assessment has not been performed and we understand was not performed in the prior year in respect of MMFs held at that date. Officers have advised that they expect to reclassify instruments with a value of £20m from cash equivalents to investments and adjust the cash flow statement to reflect this. We have not yet seen the type of assessment described above to support the classification.
	In the original version of the cash flow statement, the cash flow from investing activities in the primary statement was not in agreement with the note. The note also omitted proceeds from the sale of non current assets. Cash flows from investment and loans have been disclosed on a net basis, rather than showing receipts and payments separately, as required by the Code.
	The Council has also not complied with a new disclosure requirement in respect of the reconciliation of financial liabilities. We request these issues are dealt with prior to finalising the accounts.

# Other matters (continued)

## Other financial reporting matters

Area	Observation
<b>Prior year restatement – academy conversions</b>	<p>As reported in our audit planning report, officers brought to our attention an error that they had identified in the prior year statement of accounts. During 2017/18, five grant maintained schools converted to academy status. On conversion, the Council entered into 125 year leases at peppercorn rent. The Council did not capture four of these transactions in preparing the 2017/18 accounts. As a result, non current assets were incorrectly accounted for on the balance sheet at 31 March 2018 on a freehold basis, without taking into account the leasehold interest which the Council had granted to the academy trusts.</p> <p>As a consequence, non current assets were overstated by £76m in the prior year. The Code requires material prior period errors to be corrected by correcting opening balances and restating the comparative information in the current year statement of accounts. We tested the calculation of the error, the accounting entries made and the additional disclosures. The Department for Education publishes information on the schools which have converted to academies and the date of conversion. We have confirmed by reference to this source, that consistent with the draft financial statements, there were no conversions in 2018/19. We also tested that all previous academy conversions had been removed from the fixed asset register. This did not identify any exceptions.</p> <p>Officers have explained the control which they have put in place to prevent of re-occurrence of this issue which involves strengthening internal communications. We recommend in addition that officers periodically download and follow-up the spreadsheet referred to which includes both conversions and the pipeline for future conversions.</p>
<b>Elimination of internal recharges</b>	<p>Internal recharges should be eliminated from the presentation of income and expenditure in the Comprehensive Income and Expenditure Statement. The process of doing this is complicated because the coding structure adopted does not enable the finance team to readily identify postings within income and expenditure. Our testing identified charges of £47m which had not been fully netted down. We understand that there is a similar misstatement in the prior year information (£45m). As this amount is material, the comparative information should be restated to correct this error.</p>
<b>Early redemption of LOBO</b>	<p>During the year the Council redeemed its LOBO loan early and paid a premium of £18m. The Council obtained advice from treasury specialists in entering into this transaction. As required by the Code this has been charged in full to the Comprehensive Income and Expenditure Statement but under legislation the charge to the General Fund is being over the term of the original loan with the deferred portion carried forward in the Financial Instrument Adjustment Account. There are no issues arising from our testing.</p>

# Other matters (continued)

## Other financial reporting matters

Area	Observation
<b>Release of creditor balance</b>	<p>A creditor balance of £20.0m at 31 March 2018, described in the trial balance as "Non-Grant Government Creditors - NNDR Accounting Adjustments" has been released to income during the year. We understand that the liability account was set up several years ago.</p> <p>We have not been able to obtain a clear explanation of the balance, the financial statement line item(s) which was charged on its creation or how the amount was calculated. We would not expect an item of this size to be recorded on the balance sheet without clarity on the these points. We understand that the liability may have been an additional provision against appeals to the amounts included in provisions for this purpose. Comments on the NNDR appeals provision are included below.</p> <p>The amount has been included within the "grants and contributions" line in the analysis of income by type in Note 42 and within the "corporate cost and central items" line in the Comprehensive Income and Expenditure Statement. As officers have not been able to provide information on the original accounting, we are not able to determine with certainty the presentation of this item, but would expect, based on the account description and the explanation partial explanation provided, we would expect the amount to be included within taxation lines.</p>
<b>Page 15 NNDR appeals provision</b>	<p>The Council has made a provision of £1.3m for appeals made by business ratepayers to their bills. We challenged the Council as the amount settled in the following year has been significantly in excess of the amount provided in each of the last two years. Officers have explained that in calculating the amount of income to be transferred from the Collection Fund in 2019/20, allowance has been made for a much higher appeals repayment amount. Officers have subsequently provided an analysis prepared by an external adviser which indicates a provision requirement of £8.9m for appeals made against the 2010 Ratings List, of which the Council's share would be £5.8m. No provision has been made for appeals against the 2017 Ratings List. We have requested that officers re-look at this area.</p>
<b>Deficit contribution</b>	<p>Following the 2016 triennial valuation, the Council repaid the equivalent of 3 years' deficit funding repayment instalments as a single lump sum of £43.4m. This was to secure revenue savings as the lump sum payment was lower than the alternative three instalments of £15m. The Council is allocating the charge to its General Fund over the 3 year period to the next triennial valuation, effectively treating part of the lump sum as a prepayment of the second and third year contributions (adding the amount of contribution carried forward to the pension reserve, rather than adding to net assets). In the pension fund financial statements, the full amount of the lump sum was recognised as income in 2017/18. We have requested but not yet seen correspondence with the actuary concerning this arrangement.</p> <p>The Council is required to obtain a "rates and adjustments" certificate from the actuary, to make contributions in accordance with that certificate and to record the amount of contribution payable as a charge against the General Fund in that year.</p> <p>Ordinarily, when an authority agrees to make a lump sum payment, that single payment is reflected within the certificate and the whole amount charged in year one. In this case the rates and adjustments certificate reflects three annual instalment of £15m. Whilst this is consistent with the Council's argument that it has prepaid contributions for the later years, the timing and total amount of contributions set down in the rates and adjustments certificate is not consistent with the payment actually made. There is also an inconsistency between the amount of expense recognised in the Council financial statements compared to the pension fund financial statement. We have requested the correspondence with the actuary about the payment schedule and are considering the implications of the inconsistencies set out above.</p>



# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources

## Background

Under the National Audit Office's Code of Audit Practice, we are required to report whether, in our opinion, the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

The Code and supporting Auditor Guidance Notes require us to perform a risk assessment to identify any risks that have the potential to cause us to reach an inappropriate conclusion on the audited body's arrangements. We are required to carry out further work where we identify a significant risk - if we do not identify any significant risks, there is no requirement to carry out further work.

## Our risk assessment

We set out the risk assessment procedures we had performed and our further planned procedures in our audit planning report. We also set out in our audit planning report the two areas of significant risk identified by our risk assessment procedures performed at that point. We have not identified any further significant risks from our updating our risk assessment procedures, although some of this work is ongoing. We set out information on the significant risks on the following pages.

## Deloitte view

Based on the current status of our audit work, we envisage issuing a qualified "value for money conclusion" as Ofsted's 2018 report and subsequent monitoring reports provide evidence (notwithstanding the improvement trajectory) that proper arrangements to secure economy, efficiency and effectiveness in the use of resources did not in place throughout the whole of the period covered by our conclusion in that respect.

The expected form of our conclusion (which will be on an "except for" and not "adverse" basis) is as follows:

### "Basis for qualified conclusion

An Ofsted inspection of the Council's services for children in need of help and protection, children looked after and care leavers undertaken in January and February 2017, which reported in April 2017, rated children's services, overall, as inadequate. The inspection also reviewed the effectiveness of the Local Safeguarding Children Board ("LCSB") and rated this as inadequate. The Ofsted report raised concerns in relation to poor frontline practice and non-compliance with basic standards (including legal requirements) which in some cases left children at risk of harm. The report also highlighted that there was insufficient scrutiny by senior leaders and non-compliance was not sufficiently challenged. In addition, performance management and quality assurance systems were not underpinned by reliable management information due to social workers and managers not updating records on the electronic recording system. The LCSB in Tower Hamlets was judged to be inadequate, as it was not discharging all of its statutory functions. The report concluded that there was insufficient monitoring of the quality of frontline practice which meant that the board was not aware of the failings to protect children reported on in the review. The Annual Governance Statement describes improvements which the Council has made in response to these findings. These improvements were not in place over the full year.

These conditions provide evidence that the Council did not have proper arrangements in place throughout the year to understand and use appropriate and reliable performance information to support informed decision making and performance management; manage risks effectively and maintain a sound system of internal control; and work with third parties effectively to deliver strategic priorities.

### Qualified conclusion

On the basis of our work, having regard to the guidance issued by the C&AG in November 2015, with the exception of the matter(s) reported in the basis for qualified conclusion paragraph above, we are satisfied that, in all significant respects, the London Borough of Tower Hamlets put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019."



# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)


Risk title	Ofsted rating of inadequate for children's services
<b>Risk description</b>	<p>In their inspection report published on 7 April 2017, Ofsted rated children's services in Tower Hamlets as "inadequate". This overall assessment incorporated inadequate ratings for the following assessment categories: children who need help and protection; and leadership, management and governance. Our predecessor concluded that these circumstances provided evidence of weaknesses in proper arrangements.</p> <p>There is a risk that the matters giving rise to the previous year's qualified conclusion are also relevant to the current year.</p>
<b>Procedures performed</b>	<p>We have read the original inspection report and reports from subsequent monitoring visits and discussed with the Corporate Director responsible for children's services.</p> <p>We have also read the Council's disclosures made about this issue in the Annual Governance Statement.</p>
<b>Conclusion on risk</b>	<p>We conclude that our VFM conclusion should be qualified in respect of this matter. This is because:</p> <ul style="list-style-type: none"> <li>• Children's services are an important and high profile service</li> <li>• The Council's rating from its regulator was "inadequate" during 2018/19</li> <li>• Whilst it is apparent from both the Council's own internal monitoring and monitoring visits that the CQC have carried out that improvements have been made, these arrangements were not in place throughout the year and in particular the Ofsted inspection reports from the early part of 2018/19 identify some areas where there had been limited improvement.</li> </ul>

# Conclusion on arrangements to secure economy, efficiency and effectiveness from the Council's use of resources (continued)

Risk title	Best value improvement plan
<b>Risk description</b>	<p>During 2017/18, the Council was subject to Directions issued by the Secretary of State which required the Council to set up a Best Value Improvement Board; submit quarterly progress reports on the Best Value Improvement Plan to the Secretary of State; and set up an independent review of the achievement of the Best Value Improvement Plan with a report to be provided to the Secretary of State by 1 August 2018.</p> <p>Our predecessor noted that not all actions were confirmed as completed or on track and anticipated that the impact of the work would not yet be embedded and concluded that these circumstances provided evidence of weaknesses in proper arrangements.</p> <p>There is a risk that the matters giving rise to the previous year's qualified conclusion are also relevant to the current year.</p>
<b>Procedures performed</b>	<p>During 2018/19, the Council completed the actions specified in Directions. On the basis of the peer challenge review submitted to the Secretary of State, the Directions were lifted.</p> <p>Our conclusion is given in respect of arrangements throughout the year and not just at the year end. We have reviewed the peer challenge review report and considered the scope and findings. We have also considered the significance of issues open at the start of the year and the timeline for their closure during the year.</p>
<b>Conclusion on risk</b>	<p>The areas of concern in the original PwC report do not involve individually significant areas of financial spend or key services but raised important questions about governance which are relevant to the sub criterion of "Acting in the public interest, through demonstrating and applying the principles and values of sound governance". These were developed further around this same theme within the Best Value Improvement Plan.</p> <p>It is apparent that in the specific areas covered by the original PwC investigation, and the Best Value Improvement Plan, that the Council has made significant progress in earlier years, resulting in the end of the intervention and the return in 2017/18 of the Council's functions (which had been carried out since 2015 by special commissioners).</p> <p>Whilst we recognise that a number of the actions were not complete at 1 April 2018, these were not individually significant to our conclusion. The LGA peer review (carried out in the first quarter of 2018/19) concluded satisfactorily on each of these areas and, of more significance, concluded there had been a significant improvement in the culture of the organisation.</p> <p>We have therefore concluded that these circumstances do not provide evidence that the Council does not have proper arrangements in 2018/19.</p> <p>The peer review identified other issues, which in part reflect the need to scale back the Council's "belt and braces" response to the original PwC investigation and subsequent intervention (including retention of decision making at a senior level to enable more agile decision-making), together with new issues raised by the Peer Challenge team, including development of IT. The Council has agreed an action plan to address the issues raised by the review (including a review of the scheme of delegation and wider constitution) which are being monitored by a member committee set up for this purpose and has earmarked reserves to support the IT development. Therefore we have not identified these matters as significant weaknesses in arrangements relevant to our conclusion.</p>

# Control observations

During the course of our audit we have identified a number of internal control findings, which we have included below for information.



Area	Observation	Priority
Quality of draft financial statements	<p>The initial draft statement of accounts which were published for public inspection and presented for audit were not of the expected standard. Issues noted included:</p> <ul style="list-style-type: none"> <li>• Narrative report not compliant with Code guidance</li> <li>• Inconsistencies between primary statements and notes in the financial statements;</li> <li>• Inconsistencies between notes in the financial statements;</li> <li>• Accounting policies not updated for the adoption of IFRS 9 and IFRS 15;</li> <li>• Accounts disclosures not updated for the adoption of IFRS 9;</li> <li>• Accounts disclosures not updated for the adoption of IFRS 15;</li> <li>• Accounts disclosures not updated for 2018/19 changes in the Code including in respect of the reconciliation of financial liabilities; and</li> <li>• Cash flow statement notes which were incomplete.</li> </ul>	
	<p>Together these indicate significant deficiencies in the financial reporting and close process. We recommend the Council reviews the year-end reporting and close process, including:</p> <ul style="list-style-type: none"> <li>• preparation of a skeleton draft of the financial statements ahead of year-end, reviewed against the Code for any changes in the year and for the disclosure requirements for any new or changed activities of the Council;</li> <li>• documentation and quantification of judgments in respect of materiality of disclosure requirements in preparing the accounts;</li> <li>• review of the completed CIPFA disclosure checklist;</li> <li>• documented and reviewed internal checks of internal consistency;</li> <li>• completion of the CIPFA "pre-audit checks on draft year-end accounts" checklist; and</li> <li>• documented and reviewed internal tie back and referencing of the draft financial statements to supporting working papers.</li> </ul>	

Low Priority



Medium Priority

High Priority

# Control observations (continued)

Area	Observation	Priority
<div>Preparation of accounting papers</div> <div>Page 20</div>	<p>Accounting papers were not prepared to explain and support key judgements and estimates, including the ongoing pertinence of judgements made in previous years or were not sufficiently detailed to explain and support those judgements and estimates. It is good practice (and the expectation of the Financial Reporting Council) for organisations to prepare accounting papers in respect of key matters in the application of accounting standards, in particular for matters of judgement or of estimation complexity. Typically these would include consideration of the relevant requirements of the accounting standards and the Code, the fact pattern (including details of relevant terms of contracts etc.), an assessment of how the standards apply in this context, consideration of potential alternative treatments, the proposed approach to measurement/calculation of accounting entries required, and the required disclosures.</p> <p>The preparation of accounting papers both supports accurate financial reporting, including facilitating both internal and external review and challenge, and provides a resource to ensure institutional knowledge in the organisation. We recommend the Council adopts an approach of preparing papers for any key accounting judgements or issues arising. We also recommend that accounting papers are presented to the same meeting of the audit committee at which the draft statement of accounts are approved (if not earlier) for scrutiny and to inform the audit committee's approval of the draft statement of accounts</p>	
<div>Accounts closure resourcing and processes</div>	<p>Very few of the requested documents were provided in the first week of the audit and into the second week. We have needed to request the finance team to follow-up on a number of items provided as breakdowns did not tie to the trial balance, were not in the level of detail requested, or it was not clear how the working papers provided related to the request. In many cases information for key samples has not been provided within the 2 day time frame agreed with the finance team. In relation to the pension fund financial statements, we were not provided with a trial balance and requested supporting working papers during the period when our specialist pension staff were scheduled to carry out the work. We have been provided with a trial balance subsequently but have needed to request a revised final, balanced TB, together with other requested supporting information. These issues have threatened achievement of the overall timetable and have led to additional audit costs.</p> <p>We recommend that the Council considers the resourcing of the closure process. We also recommend the Council considers whether there are year end processes which can be streamlined or pulled forward to earlier in the year.</p>	

# Control observations (continued)



Area	Observation	Priority
<b>New accounting standards – IFRS 9 and 15</b>	<p>Whilst we understand that officers discussed the impact of adoption of the new standards during the closure process, they did not prepare accounting papers on the transition to IFRS 9 and 15. The initial draft accounts were not updated for changes in disclosure requirements from IFRS 9 and 15. Although our work on IFRS 9 and 15 to date has not identified any material changes to the financial statements, we highlight that because the new standards have been discussed as a one off exercise, new requirements will not have been embedded in the Council's underlying systems, processes and controls. This presents a risk that new contracts or transaction may give rise to unanticipated impacts in future, or not be detected.</p>	
	<p>We recommend that the Council reviews how to update its day to day accounting processes, including any necessary system and control changes, to reflect the requirements of IFRS 9 and 15, and the process to be followed in assessing new and unusual transactions.</p>	
<b>Preparation for IFRS 16</b>	<p>The implementation of IFRS 16, Leases, for 2020/21 is expected to have a greater and more complex impact upon most Councils than the adoption of IFRS 9 and 15. The scope and potential complexity of work required, which may require system or process changes to underpin correct accounting under the standard, will require work to be completed at a significantly earlier stage than has been the case for IFRS 9 and 15 to allow for financial reporting timetables to be met.</p>	
	<p>We recommend that the Council targets completion of its IFRS 16 impact analysis during 2019/20, and to calculate an adjusted opening balance sheet position for audit following the 31 March 2020 audit. We recommend early consideration following the impact analysis of actions required to embed IFRS 16 accounting in the Council's underlying accounting systems.</p>	

# Control observations (continued)

Area	Observation	Priority
<b>Valuation of properties</b>	<p>The valuation of properties is dependent on officers' assumptions (or input from officers in forming assumptions) including the location and functional obsolescence of the existing properties and information provided by officers, including the number, type and condition of council dwellings and the floor space of schools. A paper was not prepared and reviewed setting out assumptions made (or information provided to the valuer to inform their formation of assumptions).</p>	
	<p>There are also no formal controls operating to ensure the completeness and accuracy of other information provided to the valuer.</p>	
	<p>We have not been provided with information about the Council's review of the reasonableness of the outcome of the valuation in 2018/19.</p> <p>We recommend the Council prepares and maintains a schedule which sets out the information which is provided to the valuer (including management assumptions and information provided to the valuer to inform assumptions made by the valuer) and identifies the controls over each category of information.</p>	
<b>Classification of expenditure as capital</b>	<p>We were not able to identify a documented internal control to prevent or detect the incorrect classification of revenue spend as capital.</p>	
	<p>Whilst testing to date has not identified any exceptions, the classification of expenditure between revenue and capital can involve the exercise of judgement. Projects which are of a capital nature can involve both revenue and capital elements which need to be accounted for differently.</p>	
	<p>We therefore recommend the Council implements such a control.</p>	

# Control observations (continued)

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Area	Observation	Priority
<b>Commissioning of property valuation</b>	<p>Our review of the valuer's report was complicated and lengthened by the following:</p> <ul style="list-style-type: none"> <li>• There is no summary in the report setting out what is comprised in the overall valuation and what the aggregates are of each category of asset valued. Nor is there is any linkage to the appropriate supporting information and valuation spreadsheets. This makes it impossible for the reader of the report to understand what has been valued without directly clarifying with the valuer.</li> <li>• The report does not contain any confirmation of the subject of the valuation or identify the assets that have been valued.</li> <li>• Two valuation dates have been adopted, representing the beginning and end of LBTH's financial year. However, the report is not at all clear and does not mention what assets have been valued at each respective valuation date.</li> <li>• The report does not include any commentary in relation to the possible differences between Existing Use Value and Market Value. This is a requirement of the Red Book - guidance issued by the Royal Institute of Chartered Surveyors (RICS) on the conduct of valuations and which is required to be followed by RICS members when performing valuations for financial reporting purposes.</li> </ul> <p>We recommend that these points are discussed with the valuer so that they can be dealt with in future reports.</p>	
<b>Elimination of internal recharges</b>	<p>Internal recharges should be eliminated from the presentation of income and expenditure in the Comprehensive Income and Expenditure Statement. The process of doing this is complicated because the coding structure adopted does not enable the finance team to readily identify postings within income and expenditure. Our testing identified charges of £47m which had not been fully netted down.</p> <p>We recommend that the coding structure is amended to facilitate elimination of internal recharges in the Comprehensive Income and Expenditure Statement and to readily demonstrate that this has been done in full.</p>	

The purpose of the audit was for us to express an opinion on the financial statements. The audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters being reported are limited to those deficiencies that we have identified during the audit and that we have concluded are of sufficient importance to merit being reported to you.

# Your annual report

We are required to report by exception on any where information in other information published with the financial statements (which is the Narrative Report and Annual Governance Statements) is inconsistent with the financial statements.

	Requirement	Deloitte response
Page 24	<b>Narrative Report</b>  The Narrative Report is expected to address (as relevant to the Council): <ul style="list-style-type: none"> <li>- Organisational overview and external environment;</li> <li>- Governance;</li> <li>- Operational Model;</li> <li>- Risks and opportunities;</li> <li>- Strategy and resource allocation;</li> <li>- Performance;</li> <li>- Outlook; and</li> <li>- Basis of preparation</li> </ul>	<p>As a whole, the narrative report is very short (4.5 pages, compared to an average for London Boroughs of 10.5 pages in 2017/18).</p> <p>The purpose of the Narrative Report is to provide information on the authority, its main objectives and strategies and the principal risks that it faces. The Report provides limited information on its operational model, for example on operational activities of the authority's key services and outcomes. The Report touches on financial risks but does not refer to broader risks in relation to future service provision and its risk mitigation strategy. The Report states that the impact of Brexit has not been quantified and does not provide further information of the risks to the Council.</p> <p>The Narrative Report must provide a fair, balanced and understandable analysis of the authority's performance. The Report sets out key achievements in the year but does not give similar weight to describing some of the challenges it has faced. Non financial KPIs selected appear to focus on volumes, rather than measuring progress towards the meeting the Council's strategic objectives. Comparative information is not consistently provided to give context.</p> <p>The narrative report should highlight and explain the linkages between information presented in the narrative report and the information within the financial statements, and information presented must be consistent with the information within the financial statements. The Report provides information on gross revenue expenditure and funding sources. It is not clear how total link to information in the financial statements. Care needs to be taken in how measures are described – for example the Narrative Report refers to a surplus of £6.1m – this value is in fact the movement on the HRA balance in the year, whereas the reported deficit is £41.1m. We will finalise our testing on checking the consistency of information in the Narrative Report with the financial statements once the financial statements have been adjusted. This type of issue will need to be resolved before we issue our opinion.</p> <p>The Code provides guidance on further information which authorities should consider including on the basis of preparation and presentation of the financial statements.</p> <p>We recommend the report is updated to do address these points.</p>
	<b>Annual Governance Statement</b>  The Annual Governance Statement reports that governance arrangements provide assurance, are adequate and are operating effectively.	<p>We have assessed whether the information given in the Annual Governance Statement meets the disclosure requirements set out in CIPFA/SOLACE guidance, is misleading, or is inconsistent with other information from our audit. We have no exceptions to report.</p>



# Purpose of our report and responsibility statement

## Our report is designed to help you meet your governance duties

### What we report

Our report is designed to help the Audit Committee and the Council discharge their governance duties. It also represents one way in which we fulfil our obligations under ISA 260 (UK) to communicate with you regarding your oversight of the financial reporting process and your governance requirements. Our report includes:

- Results of our work on key audit judgements and our observations on the quality of your Annual Report.
- Our internal control observations.
- Other insights we have identified from our audit.

### What we don't report

As you will be aware, our audit was not designed to identify all matters that may be relevant to the Council.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.

Finally, our views on internal controls and business risk assessment should not be taken as comprehensive or as an opinion on effectiveness since they have been based solely on the audit procedures performed in the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

### The scope of our work

Our observations are developed in the context of our audit of the financial statements. We described the scope of our work in our audit plan and again in this report.

This report has been prepared for the Audit Committee and Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

We welcome the opportunity to discuss our report with you and receive your feedback.

**Jonathan Gooding**  
for and on behalf of Deloitte LLP  
St Albans  
19 July 2019

# Appendices

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# Audit adjustments

## Unadjusted misstatements

The following uncorrected misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK). Uncorrected misstatements to date increase total comprehensive expenditure in the CIES by £4.7m, decrease net assets by £4.7m, and decrease usable reserves by £4.7m.

		Debit/ (credit) CIES £m	Debit/ (credit) in net assets £m	Debit/ (credit) prior year reserves £m	Memo: Debit/ (credit) usable reserves £m	If applicable, control deficiency identified
<b>Misstatements identified in current year</b>						
Expense deficit on DSG funding	[1]	4.7	(4.7)	-	4.7	
Reclassify cash in transit to cash and cash equivalents	[2]	-	-	-	-	
Eliminate internal recharges	[3]	-	-	-	-	Yes
<b>Misstatements identified in prior years</b>						
Eliminate internal recharges	[4]	-	-	-	-	Yes
<b>Total</b>		<b>4.7</b>	<b>(4.7)</b>	<b>-</b>	<b>4.7</b>	

- (1) Dedicated schools grant (DSG) was overspent by £4.7m in 2018/19. This deficit has been incorrectly carried forward in receivables, but should have been expensed.
- (2) Cash paid by individual schools into corporate bank accounts of £11.4m has been deducted from schools bank control accounts before year end but added to corporate bank control accounts until after the year end. Instead the amount has been included in receivables. This adjustment reclassifies the amount from receivables to cash and cash equivalents.
- (3) Internal recharges of £47.8m have been incorrectly included gross in income and expenditure in the Comprehensive Income and Expenditure Statement. This adjustment nets down the recharge income against the matching expenditure item. The same adjustment is required in the analysis of income and expenditure by type (Note 42) to net down recharge income within income from fees and charges against non pay expenditure. There are similar misstatement in the prior year comparative information (£45m) which requires restatement of the comparative information.

Our audit is ongoing and further misstatements may be identified through performance of our remaining procedures. In particular we have not yet determined whether any adjustment is required in respect of issues commented on in the body of the report relating to the impact of the McCloud case on the valuation of the pension liability, other issues raised in relation to the net pension liability or on the accounting for the deficit funding pension contribution.

# Audit adjustments

## Disclosures

### Disclosure misstatements

The following uncorrected disclosure misstatements have been identified up to the date of this report which we request that you ask management to correct as required by ISAs (UK).

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#### Disclosure

The cash flow from investing activities in the primary statement is not in agreement with the note.

The note also omits proceeds from the sale of non current assets.

Cash flows from investment and loans have been disclosed on a net basis, rather than showing receipts and payments separately, as required by the Code.

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### Other disclosure recommendations

Although the omission of the following disclosures does not materially impact the financial statements, we are drawing the omitted disclosures to your attention because we believe it would improve the financial statements to include them or because you could be subject to challenge from regulators or other stakeholders as to why they were not included.

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#### Disclosure

An authority shall explain the inputs, assumptions and estimation techniques used to apply the requirements in section 7.2.9. For this purpose an authority shall disclose:

a) the basis of inputs and assumptions and the estimation techniques used to:

i) measure the 12-month and lifetime expected credit losses

ii) determine whether the credit risk of financial instruments has increased significantly since initial recognition, and

iii) determine whether a financial asset is a credit-impaired financial asset

b) how forward-looking information has been incorporated into the determination of expected credit losses, including the use of macroeconomic information, and

c) changes in the estimation techniques or significant assumptions made during the reporting period and the reasons for those changes.

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# Audit adjustments

## Disclosures

### Other disclosure recommendations (continued)

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#### Disclosure

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To explain the changes in the loss allowance and the reasons for those changes, an authority shall provide, by class of financial instrument, a reconciliation from the opening balance to the closing balance of the loss allowance, in a table, showing separately the changes during the period for:

- a) the loss allowance measured at an amount equal to 12-month expected credit losses
- b) the loss allowance measured at an amount equal to lifetime expected credit losses for:
  - i) financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets
  - ii) financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired), and
  - iii) trade receivables, contract assets or lease receivables for which the loss allowances are measured in accordance with paragraph 7.2.9.17
- c) financial assets that are purchased or originated credit-impaired.

In addition to the reconciliation, an authority shall disclose the total amount of undiscounted expected credit losses at initial recognition on financial assets initially recognised during the reporting period.

To enable users of financial statements to understand the changes in the loss allowance disclosed in accordance with paragraph 7.3.3.13, an authority shall provide an explanation of how significant changes in the gross carrying amount of financial instruments during the period contributed to changes in the loss allowance. The information shall be provided separately for financial instruments that represent the loss allowance as listed in paragraph 7.3.3.13 a) to c) and shall include relevant qualitative and quantitative information. Examples of changes in the gross carrying amount of financial instruments that contributed to the changes in the loss allowance may include:

- a) changes because of financial instruments originated or acquired during the reporting period
  - b) the modification of contractual cash flows on financial assets that do not result in a derecognition of those financial assets in accordance with IFRS 9
  - c) changes because of financial instruments that were derecognised (including those that were written off) during the reporting period, and
  - d) changes arising from whether the loss allowance is measured at an amount equal to 12-month or lifetime expected credit losses.
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# Audit adjustments

## Disclosures

### Other disclosure recommendations (continued)

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#### Disclosure

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To enable users of financial statements to assess an authority's credit risk exposure and understand its significant credit risk concentrations, an authority shall disclose, by credit risk rating grades, the gross carrying amount of financial assets and the exposure to credit risk on loan commitments and financial guarantee contracts. This information shall be provided separately for financial instruments:

- a) for which the loss allowance is measured at an amount equal to 12-month expected credit losses
- b) for which the loss allowance is measured at an amount equal to lifetime expected credit losses and that are:
  - i) financial instruments for which credit risk has increased significantly since initial recognition but that are not credit-impaired financial assets
  - ii) financial assets that are credit-impaired at the reporting date (but that are not purchased or originated credit-impaired), and iii) trade receivables, contract assets or lease receivables for which the loss allowances are measured in accordance with paragraph 7.2.9.17 c) that are purchased or originated credit-impaired financial assets.

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An authority shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (see paragraphs 44B to C and 44E of IAS 7 for guidance on this disclosure) [Code: 3.4.2.83].

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# Fraud responsibilities and representations

## Responsibilities explained



### Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.



### Required representations:

We have asked the Council to confirm in writing that you have disclosed to us the results of your own assessment of the risk that the financial statements may be materially misstated as a result of fraud and that you have disclosed to us all information in relation to fraud or suspected fraud that you are aware of and that affects the Council.

We have also asked the Council to confirm in writing their responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error.



### Audit work performed:

In our planning we identified capital expenditure and management override of controls as key audit risks for your organisation where there is a significant risk of fraud in financial reporting.

During course of our audit, we have had discussions with management and those charged with governance.

During course of our audit, we have had discussions with relevant officers and those charged with governance.

In addition, we have reviewed management's own documented procedures regarding fraud and error in the financial statements.

We have reviewed the Annual Governance Statement.



# Independence and fees

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

## Independence confirmation

We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Council and will reconfirm our independence and objectivity to the Audit Committee for the year ending 31 March 2019 in our final report to the Audit Committee.

## Non-audit fees

We were appointed to carry out the audit of an unconsolidated subsidiary of the Council. There are also proposed audit related services to be carried out claims and returns. There are no other non-audit fees.

## Independence monitoring

We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.

## Relationships

We have no other relationships with the Authority, its members, officers and affiliates, and have not supplied any services to other known connected parties.



# Independence and fees

	Planned fee £'000s (excl. VAT)
Code audit fee - Council	161 See note 1
Code audit fee – Pension fund	16 See note 1
<b>Total audit</b>	<b>177</b>
Fees for audit of an unconsolidated subsidiary	5
Fees for reporting on the housing benefit subsidy claim	24
Fees for reporting on teachers pension	4
Fees for reporting on other government grants: Pooling of housing capital receipts return	4
<b>Total assurance services</b>	<b>31</b>
<b>Total fees</b>	<b>214</b>

We have incurred additional costs in our work on the 2018/19 audit due to difficulties and delays in obtaining information and errors identified in the report.

We estimate the amount of additional cost incurred to date to be £15-20k and that the further time needed to complete the audit from this point all represents additional cost which will be charged using the rate card below.

	Rate per hour (£)
Partner/director	132
Senior manager/manager	73
Senior auditor	47
Other staff	36

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