External Audit Report 2016/17

London Borough of Tower Hamlets

—

September 2017

Content

Contacts in connection with this report are:

Andrew Sayers
Partner

Tel: 0207 694 8981
andrew.sayers@kpmg.co.uk

Antony Smith
Manager

Tel: 07824 415 095
antony.smith@kpmg.co.uk

Bean Mhi O'Boyle
Assistant Manager

Tel: 07767 418 602
beanmhi.oboyle@kpmg.co.uk

This report is addressed to the London Borough of Tower Hamlets (the Authority) and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. PSAA issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on PSAA's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, you should contact Andrew Sayers, the engagement lead to the Authority and the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, who will try to resolve your complaint. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3H.

Important notice

This report is presented in accordance with our PSAA engagement. Circulation of this report is restricted. The content of this report is based solely on the procedures necessary for our audit. This report is addressed to the London Borough of Tower Hamlets (the Authority) and has been prepared for your use only. We accept no responsibility towards any member of staff acting on their own, or to any third parties. The National Audit Office (NAO) has issued a document entitled Code of Audit Practice (the Code). This summarises where the responsibilities of auditors begin and end and what is expected from the Authority. External auditors do not act as a substitute for the Authority's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

Basis of preparation: We have prepared this External Audit Report (Report) in accordance with our responsibilities under the National Audit Office Code of Audit Practice (the Code) and the terms of our Public Sector Audit Appointments Ltd (PSAA) engagement.

Purpose of this report: This Report is made to the Authority's Audit Committee in order to communicate matters as required by International Audit Standards (ISAs) (UK and Ireland) and other matters coming to our attention during our audit work that we consider might be of interest and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone (beyond that which we may have as auditors) for this Report or for the opinions we have formed in respect of this Report.

Limitations on work performed: This Report is separate from our audit opinion and does not provide an additional opinion on the Authority's financial statements nor does it add to or extend or alter our duties and responsibilities as auditors. We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report. The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

Status of our audit: Our audit is almost complete, but there is some on-going work and closing procedures to complete. As such matters communicated in this Report may change, although at this stage we are not anticipating anything of significance. We will provide an oral update on the status of our audit at the Audit Committee meeting.

Summary

Financial statements audit – see section 2 for further details

Subject to all outstanding queries and procedures being satisfactorily resolved we intend to issue an unqualified audit opinion on the Authority's financial statements for the deadline of 30 September 2017, following the Audit Committee adopting them and receipt of the management representations letter.

We also anticipate issuing an unqualified audit opinion in relation to the Pension Fund's financial statements for the deadline of 30 September 2017.

We have almost completed our audit of the financial statements. We have read the Narrative Report and reviewed the Annual Governance Statement (AGS). Our key findings are:

- There are no unadjusted audit differences.
- We agreed presentational changes to the accounts with Finance, mainly related to compliance with the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.
- In relation to grant payments and property leases the issues that we identified in our 2015/16 ISA260 report still apply (as the Authority have only addressed them in 2017/18). In summary several Mainstream Grant payments have been identified that were not made in accordance with all of the conditions set by Commissioners. Specifically for the organisations receiving the grant there was no formal agreement in place setting out the agreed use/occupation of the property. Thus for 11 organisations the Authority has concluded that no formal property agreement was in place for 2015/16 and that this continued to be the case in 2016/17. Therefore the xx payments made to these 11 organisations in 2016/17 are considered to unlawful. The total value of the payments made was £xxx,xxx. The position will be set out and summarised as an additional disclosure in the Authority's financial statements.
- In additional to our routine requests we are asking for management representations over the following, which are explained in section 2:

  - grants paid and significant grant funding schemes; and

  - section 106 and Community Infrastructure Levy (CIL) agreements.
- We will report that your AGS complies with delivering Good Governance guidance issued by CIPFA / SOLACE in April 2016.
- We reviewed the narrative report and have no matters to raise with you.
- We have received one proposed objection from a local elector this year.

We intend to issue our 2016/17 Annual Audit Letter in October 2017.

The audit cannot be formally concluded and an audit certificate issued as we are considering elector queries. One is in relation to parking matters and the Authority's 2013/14 financial statements. The other is an objection that refers to two of the Authority's Private Finance Initiative schemes and relates to 2016/17. Until we have completed our consideration of these, we are unable to certify that we have completed the audit of the accounts in accordance with the requirements of the Local Audit and Accountability Act 2014.

Summary

Value for money – see section 3 for further details

We identified one significant risk and two areas of audit focus in relation to our VFM work in our External audit plan 2016/17 issued in January 2017. The significant risk was in relation to the implementation of the Best Value (BV) action plans and the areas of focus were the Medium Term Financial Plan (MTFP); and the 'clear up' project.

We have worked with officers throughout the year to discuss these VFM risks and our detailed findings are reported in section 3 of this report.

In terms of our VFM conclusion our key consideration has been in relation to the progress made on the areas which led us to qualify our VFM conclusion in 2013/14, 2014/15 and 2015/16. These areas were grant payments and connected decisions; disposal of property and the granting of leasehold interests; spending on publicity; and corporate governance arrangements in the three areas. Our qualification for 2014/15 additionally referred to our Section 11 recommendation made in October 2015 reflecting our view that the Authority needed to ensure that its governance processes were appropriate in a wider sense for the Authority as a whole and as part of its programme of cultural change and not just the areas referred to in the BV Inspection report.

Consequently, in terms of 2016/17 we have considered the reporting by the Commissioners to the Secretary of State for Communities and Local Government (SoS for CLG) and the extent to which the Authority's BV action plans were reported as actions completed. In relation to our Section 11 recommendation, we are satisfied that the issues referred to have been incorporated into the Authority's BV action plan relating to organisational culture.

In their February 2017 letter to the SoS for CLG the Commissioners were positive and they set out their endorsement of the progress that had been made in all areas of the Direction regime. In particular the Commissioners welcomed the Authority's realistic appreciation not only of what has been done, but also what remains to be done to fulfil the expectations for the Directions. The Authority was clear in its February 2017 submission to the SoS for CLG, that it would take some 12 months to complete the work required. The Authority has developed this work into a BV Improvement Plan under five areas: elections; communications; property; grants; and organisational culture.

Following meetings with the Mayor, the SoS for CLG decided to end the 2014 Directions and not extend the appointment of the Commissioners beyond 2014 in recognition of the Authority's progress. In light of the remaining work the SoS CLG has made three new, less intrusive Directions (in force until 30 September 2018) which require the Authority to set up a Best Value Improvement Board (with cross party and independent membership); submit quarterly progress reports on the BV improvement plan to the SoS CLG; and set up an independent review of achievement of the BV improvement plan with a report to the SoS CLG by 1 August 2018.

The latest progress report shows that delivery is on track for around 80% of the 115 actions/milestones detailed in the Authority's BV improvement plan. The Authority is monitoring progress closely, has not identified any significant concerns with respect to the delayed/overdue actions, and is attempting to take corrective action to bring delayed/overdue actions back on track.

From all of the above commentary we have noted that the Authority has made good progress and this has been acknowledged by external parties. However, with respect to the VFM conclusion we are required to consider the financial year as a whole and thus there were a number of actions that were not completed within 2016/17.

We have therefore concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources throughout 2016/17. However, we are now satisfied that none of the remaining issues have an adverse impact on the 'sustainable resource deployment' sub criterion. We therefore anticipate issuing a qualified VFM conclusion on an 'except for' basis rather than the adverse basis that we have applied in 2013/14, 2014/15 and 2015/16. Our proposed opinion covering both the financial statements and the VFM arrangements is included in Appendix 6.

Summary

Value for money (continued)

In terms of the other areas of focus (MTFS and 'Clear Up' project) There are no significant matters arising.

For the MTFS the Authority has appropriate processes and mechanisms in place to manage its finances over the life of the MTFS, although there are significant agreed savings plans to be delivered and savings opportunities to be finalised and then delivered. Furthermore, the Authority is facing some significant challenges as it moves forward with an ambitious 3 year transformation programme.

In terms of the 'Clear Up' project, the investigations into matters brought to the Authority's attention have been completed with a final report of findings and issues arising being considered by Cabinet in June 2017. The Authority has set up comprehensive responsibility and public monitoring to ensure that all of the actions identified are completed.

Other matters

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

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

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority's 2016/17 financial statements.

Our 2015/16 ISA260 report contained two recommendation relating to 2015/16 and a prior year recommendation that required further action by Management. As this report was only finalised recently we intend to follow up on the Authority's progress as part of the 2017/18 audit. To the extent that we have tested these areas of the Authority's operations during this year's audit our approach and the results of our work are detailed in this report.

We have not made any new recommendations as a result of our 2016/17 work. However, this should be viewed in the context that the 2015/16 ISA 260, which included two recommendations, has only recently been finalised (the 2015/16 recommendations are included in Appendix 1); and the new Directions issued by the Secretary of State for Communities and Local Government in March 2017, which set out the Authority's Best Value Improvement Plan (referred to on the previous page).

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. The status of our grants and claim work is summarised below:

- Teacher's Pensions Return – this work is planned to be undertaken in October 2017 in order to meet the Teacher's Pensions agency deadline of 30 November 2017; and
- Housing Capital Receipts Return - this work is planned to be undertaken in October 2017 in order to meet the DCLG's deadline of 30 November 2017.

The fees for this work are explained in section two.

Financial statements audit

We audit your financial statements by undertaking the following:

	Accounts production stage		
Work Performed	**Before**	**During**	**After**
1. Business understanding: review your operations	✓	✓	–
2. Controls: assess the control framework	✓	–	–
3. Prepared by Client Request (PBC): issue our prepared by client request	✓	–	–
4. Accounting standards: agree the impact of any new accounting standards	✓	✓	–
5. Accounts production: review the accounts production process	✓	✓	✓
6. Testing: test and confirm material or significant balances and disclosures	–	✓	✓
7. Representations and opinions: seek and provide representations before issuing our opinions	✓	✓	✓

We have completed the first six stages and report our key findings below:

1. Business understanding	In our 2016/17 audit plan we assessed your operations to identify significant issues that might have a financial statements consequence. We confirmed this risk assessment as part of our audit work. We provide an update on each of the risks identified later in this section.
2. Assessment of the control environment	We assessed the effectiveness of your key financial system controls that prevent and detect material fraud and error. We found that the financial controls on which we seek to place reliance are operating effectively. We reviewed work undertaken by your internal auditors, in accordance with ISA 610 and used the findings to inform our work.
3. Prepared by client request (PBC)	We produced the PBC to summarise the working papers and evidence we ask you to collate as part of the preparation of the financial statements. We discussed and tailored our request with the Chief Accountant and the Interim Financial Accountant and this was issued as a final document to the finance team. The Council has continued to produce appropriate quality working papers with clear audit trails.

Financial statements audit

4. Accounting standards	We work with you to understand changes to accounting standards and other technical issues. For 2016/17 these changes related to: • Updates to the presentation of the Comprehensive Income and Expenditure Statement and the Movements in Reserves Statement and the introduction of the new Expenditure and Funding Analysis; • Amended guidance on the Annual Governance Statement; and • Changes in the format of the Pension Fund accounts. We have no significant comments/observations to bring to your attention in relation to these changes.
5. Accounts Production	We received complete draft accounts by 30 June 2017 in accordance with the deadline. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17. We will debrief with Finance to share views on the final accounts audit which hopefully will lead to further efficiencies in the 2017/18 audit process. The Authority has strengthened its financial reporting by finalising the accounts in a shorter timescale. This puts the Authority in a good position to meet the new accelerated 2017/18 deadline. We thank the Finance team for their cooperation throughout the visit which allowed the audit to progress and complete within the allocated timeframe.
6. Testing	We have summarised the findings from our testing of significant risks and areas of judgement in the financial statements on the following pages. During the audit we identified only presentational issues which have been adjusted, they have no material effect on the financial statements. In addition the Council has identified one material presentational change, relating to the gross value of pension assets and liabilities in note 41 of the financial statements. The amendment has decreased the gross value of the pension assets and liabilities by £50 million, but there is no impact on the net pensions liability, which remains as £619 million at 31 March 2017.
7. Representations	You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We provided a draft of this representation letter to the Corporate Director of Resources on [DD] September 2017. We draw attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking Management to provide specific representations on: • Grants paid and significant grant funding schemes; and • Section 106 and Community Infrastructure Levy (CIL) agreements.

Financial statements audit

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

— Significant difficulties encountered during the audit;

— Significant matters arising from the audit that were discussed, or subject to correspondence with Management;

— Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and

— Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, opening balances, public interest reporting, questions/objections, etc.).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority’s 2016/17 financial statements.

To ensure that we provide a comprehensive summary of our work, we have over the next pages set out:

- The results of the procedures we performed over Property, Plant and Equipment; Valuation of Pension Fund Assets; Pension liability including assumptions and having regard to the potential for significant changes arising from the LGPS Triennial Valuation; Declarations of interest; Section 106/CIL agreements; and Grant payments which were identified as significant risks within our audit plan and which will form a part of our audit opinion;
- The results of our procedures to review the required risks of the fraudulent risk of revenue recognition and management override of control; and
- Our view of the level of prudence applied to key balances in the financial statements (including provisions (for bad debts, NNDR etc); HRA assets; PPE assets; asset lives; accruals and de minimis levels; and pension liability) concluded that these were considered reasonable and we have not needed to comment further on these in this report.

Financial statements audit

SIGNIFICANT audit risk	Account balances affected	Summary of findings
Valuation of Pension Fund Assets (Pension Fund) At 31 March 2016 the Pension Fund had investment assets totalling £979 million. The investment portfolio includes derivative contracts which can be complex to value. Given the size and potential for complexity in the investment portfolio we consider this to be a significant audit risk for 2016/17.	Investment assets £1,353 million, PY £971 million	We have undertaken detailed testing of investments as part of our final accounts audit, including assessing the design and operation of controls in place, obtaining independent confirmations from the Custodian (and Fund Managers as necessary) to verify year end balances, undertaking substantive testing over sales and purchases made in the year, reviewing year on year movements, and comparing performance to known benchmarks. No issues were noted as a result of our procedures.
Pension liability including assumptions and having regard to the potential for significant changes arising from the LGPS Triennial Valuation (Authority) During the year, the Pension Fund has undergone a triennial valuation with an effective date of 31 March 2016 in line with the Local Government Pension Scheme (Administration) Regulations 2013. The share of pensions assets and liabilities for each admitted body is determined in detail, and a large volume of data is provided to the actuary to support this triennial valuation. The pension numbers to be included in the financial statements for 2016/17 will be based on the output of the triennial valuation rolled forward to 31 March 2017. For 2017/18 and 2018/19 the actuary will then roll forward the valuation for accounting purposes based on more limited data. There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the accounts. The Pension Fund only includes limited disclosures around pensions liabilities but we anticipate that this will be identified as a risk area by the Authority itself as the pension liabilities represent a significant element of its balance sheet. Further there are significant judgments made in relation to the assumptions to be adopted when calculating the pension liability.	Pensions reserve £619 million, PY £517 million	We have: ▪ Confirmed that the information provided to the actuary from the Authority is reasonable; ▪ Reviewed the actuarial valuation and considered the disclosure implications; and ▪ Considered the approach adopted and assumptions made by your actuaries to benchmarks (including independent experts engaged by the NAO) and other information available to us and to the assumptions used for 2016/17 for consistency with previous years. No issues were noted as a result of our procedures.

Financial statements audit

SIGNIFICANT audit risk	Account balances affected	Summary of findings
Property, Plant and Equipment (Authority) The Authority has a significant asset base primarily relating to Authority dwellings; and operational buildings. The potential for impairment/valuation changes makes this balance inherently risky due to the high level of judgement and estimation uncertainty.	Property, plant and equipment £2,275 million, £2,157 million	We have considered the Authority's approach to valuation of PPE with reference to accounting standards and the Code; the information provided to the valuer; reports received by the Authority from its valuer and the judgements made by the Authority in response to those reports. We have compared your valuer's assumptions to benchmarks and to assumptions used for 2016/17 for consistency and ensured that the valuer explicitly considered upward trends as well as impairments in conducting the valuations; and also whether there were material changes in valuations for asset classes valued more than 12 months ago. We also considered disposals including in relation to the BV Inspection findings and consequent Direction. We have no matters to bring to your attention as a result of completing this work.
Declarations of Interest (Authority) The Commissioners informed us that they remained concerned as to whether declarations were being made appropriately and completely by both officers and Members. Our 2015/16 consideration of the Authority's approach noted some weaknesses in the Authority's systems and approach to the new requirement for all staff to complete an annual declaration of interest. In particular these related to completeness of records to ensure all staff have completed a return; for those staff identified to date there had not yet been a 100% return of declarations; training should be enhanced to ensure staff understand the importance of the declarations and completing them fully and accurately; obtaining further assurance about the process and consideration/ assessment of the returns received and whether any further action is needed.	N/A	We have considered the actions taken by the Authority which include a requirement for all staff to complete an annual declaration. The most recent update is that over 99% of staff have completed a Declaration of Interest which has been approved by their line manager. There is a specific HR team set up to work on and monitor completion of declaration of interests, and provide support and training to staff and line managers. All interests are captured on the HR system. A report is sent to Divisional Directors informing them of the interests declared by their staff. Further, because line managers are required to approve the Declaration of Interest forms they should be aware of any interests that might harm the independence of their staff. HR have also provided managers with a checklist of what to do if their staff disclose certain interests. Managers are required to consider whether the interest disclosed could be perceived to impact the independence of staff and are required to raise it with their head of service if this is the case. Internal audit have also completed a review of interest declaration and the report was issued with a 'substantive' assurance. We have no further matters to bring to your attention as a result of the above considerations.

Financial statements audit

SIGNIFICANT audit risk	Account balances affected	Summary of findings
Section 106/CIL agreements (Authority) This has historically been highlighted as an additional area of concern by Commissioners from the enquiries they have made. The Authority has responded positively to an independent review of its arrangements in relation to s106 systems, processes, controls and monitoring arrangements. Although our 2015/16 testing did not identify any issues in terms of balances held and monies spent, we did note some issues regarding when funds where spent vis a vis the deadline set out in the final agreements.	Balances: developers' contributions (received in advance) £82 million; PY £68 million. Income: CIL (non-conditional) £18 million, PY £7 million; developers' contributions (conditional) £2 million, PY £4 million; and developers' contributions (credited to services £5 million PY £7 million	We have tested a selection of schemes and the overall controls employed by the Authority to ensure that section 106 agreement funds are being used in accordance with the conditions agreed as part of the planning process. Our testing of 28 schemes did not identify any issues in terms of balances held; monies spent during 2016/17; and plans for spending. No issues were noted from this testing. For the two schemes which had gone beyond the time when the s106 agreement requires the funds to have been spent that we identified in 2015/16 we noted: • (PA/06/01439 expired October 2015) – the balance at 31 March 2017 was £1.5 million, with expenditure of £2.1 million during 2016/17. We understand the balance is fully committed and expected to be largely spent during 2017/18; and • For the other small scheme (PA/02/1852 - £40,000), the Authority are awaiting the resolution of a legal dispute with the developers regarding how the development has been completed. Until this is resolved the contribution will be held in the account prior to programming or return. We understand that due to the circumstances of each scheme that there is very limited risk of the funds being lost. Last year we also noted that a further scheme was due to expire in January 2017. However, an additional contribution has now been received and therefore the date by which the funds need to be used has been revised to 2022. In respect of the independent review last year we noted that the Authority had reported that all recommendations had been implemented except those that required the implementation of a new software system which had been procured and was in the process of being implemented. This year we have noted that the database has now been scoped and purchased. The Authority is in the process of linking CIL, Accolade and Agresso and the links will need to be fully tested before final implementation.

Financial statements audit

SIGNIFICANT audit risk	Account balances affected	Summary of findings
Grant payments (Authority) The Best Value Inspection concluded that the Authority had not achieved its best value duty with regard to the payment of grants and connected decisions between 2010 and 2014. Consequently, the award of grants became the responsibility of independent Commissioners who were appointed by the Secretary of State for CLG from January 2015. A small number of grant payments (seven, with a value of £32,721 across the 2015/16 and 2016/17 financial years) were identified by the Commissioners/ Authority as not having been made in accordance with the conditions the Commissioners had set ie considered to be unlawful. Whilst our testing of payments in 2015/16 did not identify any further significant issues, the lack of a central record of all grant payments made it difficult to identify the population that we needed to sample test to address the risks identified in our 2015/16 audit plan. We understand that the Authority intends to move to a unified system for recording all grant payments in 2017.	Included within service expenditure. Value of grants paid £18.5 million (Non Domestic Rate discretionary relief £12.4 million; and Mainstream grants £2.9 million)	We have considered the detailed approach and systems put in place by the Authority and Commissioners and tested payments. We have also assessed whether any conditions/ delegation arrangements have been implemented effectively by Authority officers. We have completed detailed testing of 17 grants paid in 2016/17. All of the grant expenditure tested was found to have been incurred in line with the approval given; conditions of the specific grant stream; payments consistent with approval given; monitoring evidence had been received and considered by the Authority; and any other conditions imposed by the Commissioners. In 2015/16 we reported that the Commissioners/Authority officers have identified several Mainstream Grant payments that were made where the conditions set by Commissioners had not been met. Specifically for the organisations receiving the grant there was no formal agreement in place, between the organisation and the Authority, setting out the agreed use/occupation of the property. Consequently, these payments are considered to be unlawful. The Authority completed a detailed review of the position for 41 organisations in June 2017 and identified 27 organisations with issues requiring further work/assessment. Of these 27 organisations, the Council has concluded that as of June 2017, for seven organisations there was no evidence that a formal property agreement was not in place for 2015/16; for one organisation a lease was agreed in 2016/17 and consequently grant payments have been authorised; and for nine organisations the organisation is considered, by Members, to be working constructively with the Council to ensure formal arrangements will be in place as soon as possible and thus all previous grant payments have been authorised. For the remaining 11 organisations the Authority has concluded that no formal property agreement was in place for 2015/16 and that this continued to be the case for 2016/17. Therefore the XXX payments made to these 11 organisations in 2016/17 are considered to be unlawful. The total value of the payments made was £xxx,xxx. As our work has not identified any errors in terms of the recording of expenditure for financial statements purposes and we are already proposing a qualified opinion on the Authority's arrangements for securing VFM in its use of resources, we have not extended our work further. However, we did make a recommendation in our recently finalised 2015/16 ISA260 report referring to the need for the Authority to make further improvements relating to its systems/controls for grant payments.

Financial statements audit

Other areas of audit focus

We identified three other areas of audit focus. These are not considered to be significant risks as they are less likely to give rise to a material error. Nonetheless these are areas of importance where we carry out audit procedures to ensure that there is no material misstatement.

Other areas of audit focus	Account balances affected	Summary of findings
Payroll (Authority) Payroll represents a significant proportion of the Authority's annual expenditure (approaching 33% of gross spend at £482 million in 2015/16). Whilst not considered overly complex from a material error perspective, we consider that it is important from an audit perspective to understand the nature of the Authority's expenditure in this area.	Employee benefits expenses £477 million, PY 473 million	We have: ▪ Reviewed and tested reconciliations for gross pay and deductions (eg pensions, tax and national insurance). ▪ Completed substantive analytical reviews of payroll costs and tested supporting system information used to compile our analytical review. No issues were noted as a result of our procedures.
Youth Services (Authority) Reviews have uncovered historical shortcomings and wide spread malpractice in the Authority's youth service. The Authority has responded by putting in place an interim model to deliver services and is now moving to securing a long term strategic and operational plan for the service. There is an action plan in place to both deal with the historical matters and to move to the future service model.	Included within service expenditure	We have noted that the Authority had completed the interim actions to stabilise the Service. In December 2016 the Authority agreed to implement a proposal to transform the Council's youth service. This includes a restructure of the youth service, from January 2017 to enable the service to be delivered through a combination of internal resources and external commissioning. The new approach was also aimed at resolving the longstanding issues associated with service values and culture through a three year strategic and operational plan. No issues were noted as a result of our procedures.
Calculation of benefits (Pension Fund) The calculation of benefits can be complex. In 2015/16 a total of £52 million was paid out by the Pension Fund (pensions and lump sums). Given the quantity and complexity of these calculations there is a risk of misstatement.	Benefits (lump sum and pensions) £52 million, PY £52 million	We have completed a substantive analytical review of pensions in payment and tested supporting system information used to compile our analytical review. We have tested a sample of lump sum benefit calculations. No issues were noted as a result of our procedures.

Financial statements audit

Risks that ISAs require us to assess in all cases	Why	Our findings from the audit
Fraud risk from revenue recognition	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. We do not consider this generally to be a significant risk for local authorities (or the pension funds) as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebut this risk and do not incorporate specific work into our audit plan in this area over and above our standard fraud procedures, except for conditional grant income (which is predominantly made up of section 106 ie developers' contributions (80% of the total of £76 million in 2015/16)). We therefore combined this work with the significant audit risks for section 106/CIL agreements.	As noted, we have combined the work identified with our work on the significant audit risk for section 106/CIL agreements. The findings from our work have therefore been reported in that Section.
Fraud risk from management override of controls	Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual. We have not identified any specific additional risks of management override relating to this audit.	There are no matters arising from this work that we need to bring to your attention in relation to the Authority or Pension Fund.

Financial statements audit

Narrative report of the Authority

We have reviewed the Authority’s narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Pension fund audit

The audit of the pension fund and the Pension Fund Annual Report was completed alongside the main audit. There are no specific matters to bring to your attention relating to this.

Pension fund annual report

We reviewed the consistency of the Fund’s financial statements in the Fund’s Annual Report and the financial statements included in the London Borough of Tower Hamlets’ financial statements. We confirm that the Fund’s financial statements are consistent with the pension fund financial statements included in the accounts of the London Borough of Tower Hamlets. We read the information in the Fund’s Annual Report to identify material inconsistencies with the Fund’s financial statements. We can confirm it is not inconsistent with the financial information contained in the audited financial statements. As such we anticipate issuing an unqualified consistency opinion on the pension fund financial statements.

Queries from local electors

We have received one objection this year, that refers to two of the Authority’s Private Finance Initiative schemes. We are considering whether it meets the criteria to be accepted as an objection.

Audit certificate

In order for us to issue an audit certificate, we are required to have completed all our responsibilities relating to the financial year. The audit cannot be formally concluded and an audit certificate issued as we are considering two elector queries. One is in relation to parking matters and the Authority’s 2013/14 financial statements. The other is an objection that refers to two of the Authority’s Private Finance Initiative schemes and relates to 2016/17. Until we have completed our consideration of these, we are unable to certify that we have completed the audit of the accounts in accordance with the requirements of the Local Audit and Accountability Act 2014.

Financial statements audit

Whole of Government Accounts (WGA)

We reviewed your WGA consolidation pack and there are no issues to report. We anticipate issuing an unqualified consistency report.

Other grants and claims work

We undertake other grants and claims work for the Authority that does not fall under the PSAA arrangements. The status of our grants and claim work is presented below:

- Teacher's Pensions Return – this work is planned to be undertaken in October 2017 in order to meet the Teacher's Pensions agency deadline of 30 November 2017; and
- Housing Capital Receipts Return - this work is planned to be undertaken in October 2017 in order to meet the DCLG's deadline of 30 November 2017.

Audit fees

Our fee for the audit (Authority and Pension Fund) was £230,918 excluding VAT (£248,523 excluding VAT in 2015/16). This fee is in line with that highlighted in our audit plan approved by the Audit Committee in January 2017. Additional fees will be required for the additional work we have needed to undertake relating to the BV Inspection issues and the Authority's response. Further additional fee would also be needed if the objection to the Authority's PFI schemes were to be accepted.

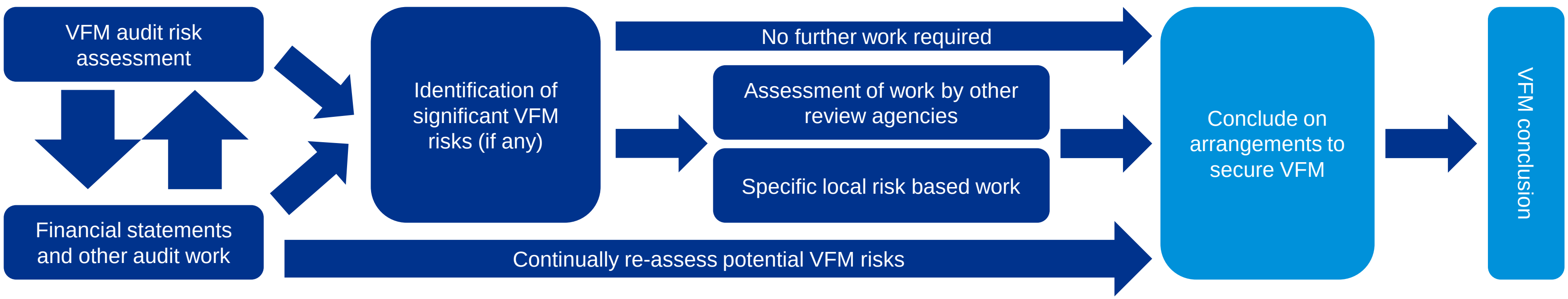
Our work on the certification of Housing Benefits (BEN01) is in progress, but is not yet complete. The planned scale fee for this is £22,838 excluding VAT (£20,327 excluding VAT in 2015/16). Planned fees for other grants and claims which do not fall under the PSAA arrangements is £7,000 excluding VAT (£6,500 excluding VAT in 2015/16).

We have not completed any other non-audit work at the Authority in 2016/17.

Value for money

For 2016/17 our value for money (VFM) work follows the NAO's guidance. It is risk based and targets audit effort on the areas of greatest audit risk. Our methodology is summarised below. We identified one significant VFM risk and two other areas of audit focus which are summarised on the following pages.

We have concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources throughout 2016/17. However, we are now satisfied that none of the remaining issues have an adverse impact on the 'sustainable resource deployment' sub criterion. We therefore anticipate issuing a qualified VFM conclusion on an 'except for' basis rather than the adverse basis that we have applied in 2013/14, 2014/15 and 2015/16.



Value for money

Significant risk based VFM audit work

Below we set out the detailed findings of our significant risk based VFM work. This work was completed to address the residual risks remaining after our assessment of the higher level controls in place to address the VFM risks identified in our planning and financial statements audit work.

Significant VFM risk	Why this risk is significant	Our audit response and findings
Implementation of BV Action Plans	The Authority monitors progress towards implementation regularly and reports on a monthly basis to the Best Value Programme Board with a summary report produced every 6 months for reporting to the SoS CLG. The latest report to the SoS CLG (September 2016) reported 95% completion of these Plans. In light of the Authority's report and the accompanying commentary from the Commissioners, the SoS CLG is proposing to reduce/end two of the Directions (procurement and grants) with the elections Direction potentially being ended pending consideration of the conduct of the December 2016 Whitechapel bi-election. On the remaining Directions the Commissioners have reported that the Authority has further work to do to either complete the identified actions; that the actions have had the planned impact; have addressed the weaknesses in the Authority's arrangements; and are embedded into the Authority's culture.	In seeking to satisfy ourselves that the Authority has made proper arrangements for challenging how it secures economy, efficiency and effectiveness in its use of resources, we have continued our consideration of the findings of the BV Inspection report and more specifically the Authority's progress towards implementing the action plans that it produced in response. Consequently, in terms of 2016/17 we have considered the reporting by the Commissioners to the Secretary of State for Communities and Local Government (SoS for CLG) and the extent to which the Authority's BV action plans were reported as actions completed. In relation to our Section 11 recommendation, we are satisfied that the issues referred to have been incorporated into the Authority's BV action plan relating to organisational culture. In their February 2017 letter to the SoS for CLG the Commissioners were positive and they set out their endorsement of the progress that had been made in all areas of the Direction regime. In terms of the specified areas in the Directions the Commissioners' views were: • Grants - the amendment to the Directions in January 2017 returned decision making powers in this area to the Council with Commissioner oversight. The Commissioners comment that the Council is still learning and improving how to do this effectively. The necessary changes to the officer support arrangements will provide a more professional and less conflicted service to Members and the voluntary sector but the Council will need to take care to ensure they have properly thought through the policy and practice implications as they seek to impose a consistent approach on the incoherence of the past. • Property - The policy framework for the proper use of the Council's physical assets is now in place. Working through the implications of past decisions to bring fairness, consistency and transparency will require determined effort and political support in doing the right thing rather than the expedient thing. • Publicity – no specific comment made. • Culture - The Clear Up team is part of a wider project to improve the culture and working relationships between Members and Officers and between Members on the Council. This is not explicitly covered by Directions and is necessarily of a much longer duration. It is however a crucial part of restoring the basics of good local government to Tower Hamlets and needs to continue beyond the 2018 election.

Value for money

Significant risk based VFM audit work (continued)

Significant VFM risk	Our audit response and findings
Implementation of BV Action Plans (continued)	Further, the Commissioners welcomed the Authority's realistic appreciation not only of what has been done, but also what remains to be done to fulfil the expectations for the Directions. The Authority was clear in its February 2017 submission to the SoS for CLG, that it would take some 12 months to complete the work required. The Authority has developed this work into a BV Improvement Plan under five areas: elections; communications; property; grants; and organisational culture. Following meetings with the Mayor, the SoS for CLG decided to end the 2014 Directions and not extend the appointment of the Commissioners beyond 2014 in recognition of the Authority's progress. In light of the remaining work the SoS CLG has made three new, less intrusive Directions (in force until 30 September 2018) which require the Authority to set up a Best Value Improvement Board (with cross party and independent membership); submit quarterly progress reports on the BV improvement plan to the SoS CLG; and set up an independent review of achievement of the BV improvement plan with a report to the SoS CLG by 1 August 2018. The latest progress report shows that delivery is on track for around 80% of the 115 actions/milestones detailed in the Authority's BV improvement plan. The Authority is monitoring progress closely, has not identified any significant concerns with respect to the delayed/overdue actions, and is attempting to take corrective action to bring delayed/overdue actions back on track. Also an Ofsted inspection undertaken in January and February 2017 rated the Authority's services for children in need of help and protection, children looked after and care leavers and the local safeguarding children board inadequate overall with some features requiring improvement. The report made 15 recommendations and highlighted poor frontline practice and ineffective, complacent and sometimes resistant management practices which enabled non-compliance with basic standards (including legal requirements) and in some cases left children at risk of harm. The report also highlighted the need for stronger leadership, management and governance to ensure there is robust performance management and scrutiny of children's social care. In consultation with the Department of Education (DfE), the Authority has established a Children's Services Improvement Board led by an Independent Chair and an Improvement Plan has been submitted to DfE in July 2017. The Board ensures that there is clear leadership of the improvement journey at corporate, political and partnership levels. The Board's key focus has been on understanding why this happened in Tower Hamlets and how to put this right through the development, implementation and monitoring of the Improvement Plan. Ofsted will be carrying out quarterly monitoring visits to ensure that its recommendations are being robustly addressed. The Children's Service Improvement Board will continue to focus on the themes identified in the Ofsted report looking at progress made and providing support and challenge on areas of on-going work. Quarterly progress updates will be provided to the Best Value Improvement Board and the Council's Cabinet and Overview and Scrutiny Committee.

Value for money

Significant risk based VFM audit work (continued)

Significant VFM risk	Our audit response and findings
Implementation of BV Action Plans (continued)	From all of the above commentary we have noted that the Authority has made good progress and this has been acknowledged by external parties. However, with respect to the VFM conclusion we are required to consider the financial year as a whole and thus there were a number of actions that were not completed within 2016/17. We have therefore concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources throughout 2016/17. However, we are now satisfied that none of the remaining issues have an adverse impact on the ‘sustainable resource deployment’ sub criterion. We therefore anticipate issuing a qualified VFM conclusion on an ‘except for’ basis rather than the adverse basis that we have applied in 2013/14, 2014/15 and 2015/16.

Value for money

Other areas of audit focus

Below we set out the detailed findings against other areas of audit focus for our VFM work.

VFM: other area of audit focus	Our audit response and findings
Medium Term Financial Strategy (MTFS)	We have reviewed overall management arrangements that the Authority has for managing its financial position, including the processes to develop a robust MTFS, ongoing monitoring of the annual budget, review of how savings plans have been developed and how their delivery is monitored, responsiveness to increasing costs of demand led services and changes in funding allocations and the governance arrangements of how the figures are reported through to the Authority. **2016/17 outturn** In terms of its financial standing the Authority is reporting that the revised budget has been met, with a small under spend of £0.7 million in total which meant that the planned use of reserves was not required (as contingencies in the budget were not needed to be applied). The Authority has also reviewed its reserves and has agreed to earmark reserves for key priorities, including the transfer of General Fund balances for priorities such as the new Civic Centre and IT and Transformation programmes. Following this review the General Fund reserve at 31 March 2017 is £31.7 million. **2017/18 budget** In relation to the MTFS we note that the Authority has agreed a balanced budget for 2017/18. The budget includes £20.4 million of agreed savings. The £21 million savings were agreed by Members in February 2017 as part of budget setting. All of the savings schemes were supported by detailed statements explaining what was being planned and how it would be delivered/achieved. The supporting papers also set out any changes to services; explained any equality implications and included a formal Equalities Impact Assessment (supported by an action plan for any groups affected adversely). In terms of monitoring the savings are built into base budgets and so they are monitored as part of on-going budget monitoring. **MTFS 2017 – 2020** For the period covered by the MTFS (three years from 2017 – 2020) the Authority has identified savings opportunities that largely meet the estimated £58 million budget gap and is looking to use less than £3 million from General Fund reserves over this period (leaving reserves at £28 million at 31 March 2020). Over the period of the MTFS there are clearly a number of risks that could affect either the level of service demand (and therefore service delivery costs) or sources of funding. In addition there are general economic factors, such as the level of inflation and interest rates that can impact on the net cost of services. Furthermore, the Authority is facing some significant challenges as it moves forward with an ambitious 3 year transformation programme. Consequently, the budget and savings delivery are being closely and continually monitored in addition to any changes/potential changes in assumptions made to ensure the Authority remains on track and capable of delivering the MTFS.

Value for money

Other areas of audit focus (continued)

VFM: other area of audit focus	Our audit response and findings
Progress on 'clear up' project	We reviewed the process by which the Clear Up Team, which was led by an independent investigator, conducted their investigations. At the close of the three month nomination period (which ran from September to December 2016) the Clear Up Project Board (comprising the three Authority Statutory Officers and a Secretary of State appointed Commissioner) agreed which of the allegations received should be investigated. In total 66 allegations were received. The final report from the Clear Up Team was considered by Cabinet on 27 June 2017. The Team reported that out of the 66 allegations: 10 were partially upheld; 5 were upheld; 1 had been referred to the Council for further consideration and investigation as the matter may be criminal; and 1 was partially upheld and partially rejected. The report also identified a number of themes which were considered by the Team to be areas for further consideration (such as improved training and enhanced procedures) by the Authority in terms of how allegations of various types have been dealt with/approached. The themes are set out in the report to Cabinet and included: • Organisational culture – whistle-blowing and reporting concerns; • Approach to investigations; • Monitoring compliance following Council decision points; • HR policies and practices; • Council Systems and Processes; • Member/officer protocols; and • Security/Confidentiality. Following receipt of the Clear Up Project report the Monitoring Officer considered the report and where further action is required by the Authority and has allocated all of the actions to various Corporate Directors and Divisional Directors. The Corporate Leadership Team will monitor progress every other month until all the matters have been completed. Quarterly reports on progress will be submitted to the Overview and Scrutiny Committee and if required to Cabinet. The Standards Advisory Committee will also receive regular reports as some of the issues raised fall within its terms of reference. Commissioners also commented positively in their February letter to the SoS CLG re the Council's progress. *Commissioners judge that this is on the way to being a significant success. It has proved to be a very useful way to lance long standing sores from the past and provide confidence in the Council's whistleblowing procedures for the future. Many lessons have been learned all of which are intended to be documented in a report to full Council in June 2017. Particular mention needs to be made of the work of the Project Co-ordinator, a secondee from the Cabinet Office, whose approach and diligence has driven the whole process forward to completion.*

Recommendations raised and followed up

We have not formally followed up the recommendations from the prior year's audit, as these have only recently been finalised in the 2015/16 ISA260 report. For clarity the recommendations included in the 2015/16 ISA260 are:

#	Risk	Recommendation
Financial statements		
1	2	**Grant Payments/Property Leases** Our work has identified several issues relating to grant payments and the controls over them. Matters arising include: • No central listing of grant payments in 2015/16 was available, making identification of grants paid difficult; • One instance where the allocation awarded by the Commissioners was exceeded by almost 20% (£34,000); and • Fifty grant payments made in 2015/16 (to 11 organisations), with a value of £152,000 have been identified by the Council as being unlawful due to the lack of a formal property agreement being in place; **Recommendation** The Authority should: • Ensure that the single system that the Authority now requires all Directorates to use to record all grant payments is used universally and all grant payments for 2016/17 onwards are captured on it; • Clarify the arrangements for grants (particularly demand led ones) to ensure that additional approval by Commissioners/ the relevant Authority Committee/officer is required (even where the over spend is being managed within the Directorate's overall resources); • Ensure that all unlawful grant payments have been identified and disclosed in the financial statements; and • Ensure that all grant programmes have been assessed to ensure that recipients are complying with the Commissioners' requirements that all grant recipients occupying Authority property must have a formal property agreement in place.

Recommendations raised and followed up

#	Risk	Recommendation
Financial statements		
2	3	**Section 106 agreements** Our testing of 27 schemes noted that there are two schemes which have gone beyond the time when the s106 agreement required the funds to have been spent. We understand that due to the circumstances of each scheme that there is very limited risk of the funds being lost. We have also noted a further scheme which is due to expire in January 2017 with a balance of £2.1m at 31 March 2016 where there are approved schemes in place that are due to use the balance during 2016/17. We will review the position on this scheme as part of our 2016/17 audit. We have also considered the results of the independent review and the Authority's response. The Authority has reported that all recommendations have been implemented except those that required the implementation of a new software system which has been procured and is in the process of being implemented. **Recommendation** The Authority needs to continue to monitor its performance compared with deadlines set out in section 106 agreements and try to ensure that there are no future instances where the monies are not spent in advance of the deadlines. The Authority also needs to complete the implementation of the new software system to address the remaining recommendations from the independent review.

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects:

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

We used the same planning materiality reported in our External Audit Plan 2016/17, presented to you in January 2017.

Materiality for the Authority's accounts was set at £15 million which equates to around 1.2% of gross expenditure.

Materiality for the Pension Fund was set at £20 million which equates to around 1.5% of gross assets.

We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work. Under *ISA 260*, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. *ISA 260* defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. *ISA 450* requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.75 million for the Authority and less than £1 million for the Pension Fund.

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

Appendix 3

Audit differences

Unadjusted audit differences

Under UK auditing standards (ISA (UK&I) 260) we are required to provide the Audit Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements.

There are no unadjusted audit differences that we need to bring to your attention.

Adjusted audit differences

To assist the Audit Committee in fulfilling its governance responsibilities we present a summary of any significant adjusted audit differences (including disclosures) identified during the course of our audit. We have not identified any such audit differences. The adjustments below have been included in the financial statements.

NOTE: None so far. The only significant adjustment was to the Pension's Liability note, where there had been a netting off in earlier years (value £50m) ie no impact on the balance sheet or CIES. Also it was identified by LBTH not the audit.

Appendix 4

Audit independence

This appendix communicates all significant facts and matters that bear on KPMG LLP's independence and objectivity and informs you of the requirements of *ISA 260 (UK and Ireland) Communication of Audit Matters to Those Charged with Governance.*

Integrity, objectivity and independence

We are required to communicate to you in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and audit team. We have considered the fees paid to us by the Authority for professional services provided by us during the reporting period. We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies all KPMG LLP audit partners and staff annually confirm their compliance with our Ethics and Independence Manual including in particular that they have no prohibited shareholdings. Our Ethics and Independence Manual is fully consistent with the requirements of the Ethical Standards issued by the UK Auditing Practices Board. As a result we have underlying safeguards in place to maintain independence through: instilling professional values; communications; internal accountability; risk management; and independent reviews. We would be happy to discuss any of these aspects of our procedures in more detail. There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed.

Audit matters

We are required to comply with *ISA (UK and Ireland) 260 Communication of Audit Matters to Those Charged with Governance* when carrying out the audit. ISA 260 requires that we consider the following audit matters and formally communicate them to those charged with governance:

- Relationships that may bear on the firm's independence and the integrity and objectivity of the audit engagement lead and audit staff;
- The general approach and overall scope of the audit, including any expected limitations thereon, or any additional requirements;
- The selection of, or changes in, significant accounting policies and practices that have, or could have, a material effect on the Authority's financial statements;
- The potential effect on the accounts of any material risks and exposures, such as pending litigation, that are required to be disclosed in the financial statements;
- Audit adjustments, whether or not recorded by the entity that have, or could have, a material effect on the Authority's financial statements;
- Material uncertainties related to events and conditions that may cast significant doubt on the Authority's ability to continue as a going concern;
- Disagreements with Management about matters that, individually or in aggregate, could be significant to the Authority's financial statements or the auditor's report. These communications include consideration of whether the matter has, or has not, been resolved and the significance of the matter;
- Expected modifications to the auditor's report;

Appendix 4

Audit independence

- Other matters warranting attention by those charged with governance, such as material weaknesses in internal control, questions regarding management integrity, and fraud involving management; and
- Any other matters agreed upon in the terms of the audit engagement.

We continue to discharge these responsibilities through our attendance at Audit Committees, commentary and reporting and, in the case of uncorrected misstatements, through our request for management representations.

Auditor declaration

In relation to the audit of the financial statements of the London Borough of Tower Hamlets and the London Borough of Tower Hamlets Pension Fund for the financial year ending 31 March 2017 we confirm that there were no relationships between KPMG LLP and the London Borough of Tower Hamlets and the London Borough of Tower Hamlets Pension Fund, their directors and senior management and their affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have not undertaken any non-audit services to the Council in 2016/17.

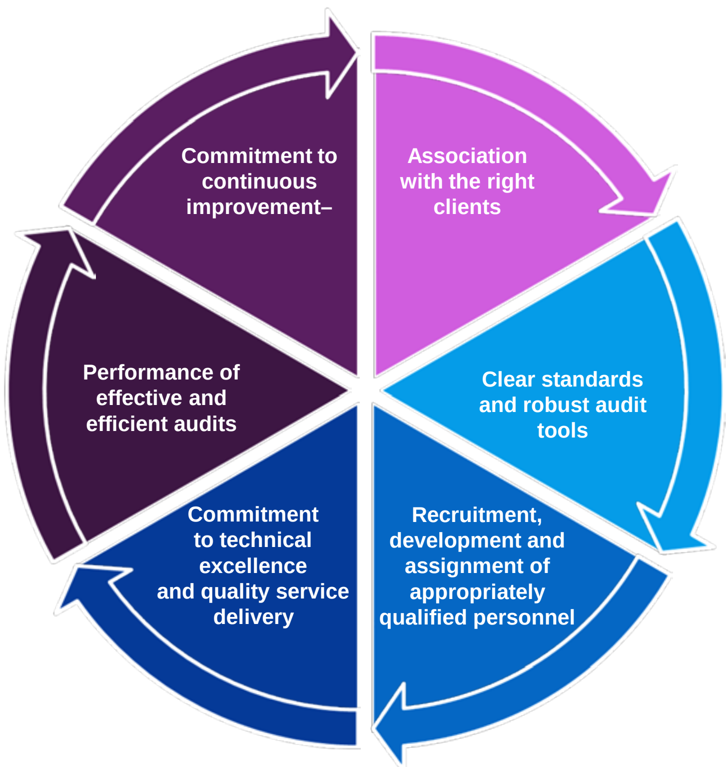
Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework

- Comprehensive effective monitoring processes
- Proactive identification of emerging risks and opportunities to improve quality and provide insights
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Relationships built on mutual respect
- Insightful, open and honest two way communications

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights



- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- Independence policies

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members and specialists

kpmg.com/socialmedia

kpmg.com/app