Derby City Council
Audit results report

Year ended 31 March 2017

EY
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Private and Confidential 13 December 2017

Dear Audit and Accounts Committee Members

We have substantially completed our audit of Derby City Council (the Authority) for the year ended 31 March 2017.

Subject to concluding the outstanding matters listed in our report, we confirm that we will issue an unqualified audit report on the financial statements in the form at section 3. We note that this is after the statutory deadline of 30 September 2017.

We are reporting a number of matters about your arrangements to secure economy, efficiency and effectiveness in your use of resources.

This report is intended solely for the use of the Audit and Accounts Committee, other members of the Authority, and senior management. It should not be used for any other purpose or given to any other party without obtaining our written consent.

We would like to thank your staff for their help during the engagement.

We look forward to discussing with you any aspects of this report or any other issues arising from our work.

Yours faithfully

Stephen Clark
Partner

For and on behalf of Ernst & Young LLP

United Kingdom

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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued "Statement of responsibilities of auditors and audited bodies". It is available from the via the PSAA website (www.PSAA.co.uk).

The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The "Terms of Appointment (updated February 2017)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature..

This report is made solely to the Audit and Accounts Committee, other members of the Authority and management of Derby City Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, other members of the Authority and management of [client] those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit and Accounts Committee, other members of the Authority and management of Derby City Council for this report or for the opinions we have formed. It should not be provided to any third-party without obtaining our written consent.

01 Executive Summary

Executive Summary

Overview of the audit

Scope and materiality

In our Audit Plan presented to the 19 September 2017 Audit and Accounts Committee meeting, we gave you an overview of how we intended to carry out our responsibilities as your auditor. We carried out our audit in accordance with this plan.

We planned our procedures using a materiality of £6.933m for the Authority and the Group. We reassessed this using the actual year-end figures, which has increased this amount to £7.139m. The threshold for reporting audit differences has increased from £0.345m to £0.357m. The basis of our assessment of materiality has remained consistent with prior years at 1% of gross revenue expenditure.

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

- Remuneration disclosures including any severance payments, exit packages and termination benefits.
- Related party transactions. For any errors identified, we have considered the concept of the materiality of transactions and balances as would be relevant to the related individual or organisation.
- Members' allowances.

Status of the audit

We have substantially completed our audit of Derby City Council's financial statements for the year ended 31 March 2017 and have performed the procedures outlined in our Audit plan. Subject to satisfactory completion of the following outstanding items we expect to issue an unqualified opinion on the Authority's financial statements in the form which appears at Section 3. However until work is complete, further amendments may arise:

- Review of the final version of the financial statements
- Review of the final annual governance statement
- Receipt of the signed management representation letter
- Completion of procedures required by the National Audit Office (NAO) regarding the Whole of Government Accounts submission

We will be unable to issue our audit certificate until the completion of procedures required by the NAO regarding the Whole of Government Accounts submission.

Executive summary (continued)

Audit differences

We identified 1 unadjusted audit differences in the draft financial statements for the year ended 31 March 2017 which management has chosen not to adjust. We ask that they be corrected or a rationale as to why they are not corrected be approved by the Audit and Accounts Committee and included in the Letter of Representation. The aggregated impact of unadjusted audit differences is £nil. We agree with management's assessment that the impact is not material.

We have also identified audit differences which have been adjusted by management. Details can be found in Section 4 Audit Differences.

Areas of audit focus

Our Audit Plan identified key areas of focus for our audit of Derby City Council's financial statements. This report sets out our observations and conclusions, including our views on areas which might be conservative, and where there is potential risk and exposure. We summarise our consideration of these matters, and any others identified, in the "Key Audit Issues" section of this report.

We ask you to review these and any other matters in this report to ensure:

- There are no other considerations or matters that could have an impact on these issues
- You agree with the resolution of the issue
- There are no other significant issues to be considered.

There are no matters, apart from those reported by management or disclosed in this report, which we believe should be brought to the attention of the Audit and Accounts Committee.

Executive summary (continued)

Our Value for Money conclusion relates to the year ended 31 March 2017.

We have considered your arrangements to take informed decisions; deploy resources in a sustainable manner; and work with partners and other third parties.
In our Audit Plan we identified 6 significant risks to our Value for Money conclusion. We performed the work set out in our audit plan in response to these risks and have concluded that a qualified 'adverse' VFM conclusion continues to be appropriate for the 2016/17 financial year. Details of our findings can be found in section 5 of this report.

From our discussions with the Authority's Chief Executive, Interim Director of Finance and s151 Officer, Monitoring Officer, and Head of Internal Audit we make the following observations to bring to the Committee's attention:

- Senior Officers have a good understanding of the changes which need to be made at the Authority to address the issues raised by various commentators and have documented action plans in place designed to affect these changes.
- Whilst it is too early for us to comment on the success of the Authority in achieving the actions set out in the plans, we can share with you our observations in respect of the issues we raised in our s24 written recommendations. During our 2016/17 audit we have noted an improvement in the quality of the basic accounting information being produced, and the working papers produced to support the statement of accounts. Whilst these remain far from best practice, the direction of travel is seen as positive. However, this has been achieved for the most part by means of significant management intervention rather than the result of a well embedded routine financial reporting process.
- For the changes to become embedded, a continued and sustained cultural shift will continue to be required.
- The Audit Committee seeks its assurance from three primary sources: Officers, Internal audit, and External audit. Our observation is that the relationship between the Council and the internal audit provider is dysfunctional. It is not operating in a way which enables the Audit Committee to obtain the assurance which it should be able to from an internal audit provider and this should be addressed as a matter of priority.

Executive Summary

Control observations

In June 2017, we used our statutory powers under Section 24 of the Local Audit and Accountability Act 2014 and issued written recommendations to the Council. This followed significant delays in the finalisation of the Council's 2015/16 Statement of Account and an unacceptable length of time being taken to respond to and correct control weaknesses identified in our audit procedures, and communicated to the Audit and Accounts Committee in September 2016. At the time of issue, the 2016/17 financial year had already ended. Therefore the control observations detailed within the written recommendations whilst first identified in the 2015/16 financial year, continued throughout the 2016/17 financial year. As such, we have adopted a fully substantive approach, so have not tested the operation of controls.

An additional control observation arising as a result of our 2016/17 audit procedures is detailed in section 7 of this report.

We have noted some positive changes since the balance sheet date, but there remains a risk that these are manual "forced" interventions rather than being embedded in the culture of the organisation – as such any reduction in the pressure to perform and/or loss of key people will mean controls will deteriorate again quickly until embedded.

Independence

Please refer to Appendix B for our update on Independence.

02 Areas of Audit Focus

Significant Audit risks and approach:

Revenue Recognition

What are our conclusions?

Our testing has not identified any material misstatements from revenue and expenditure recognition.

Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Authority's financial position.

What is the risk?

Risk of fraud in revenue recognition

Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue. In this public sector this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by manipulating expenditure recognition.

For Derby City Council we consider that this risk presents itself in Fees, Charges and Other Service Income and Other Service Expenditure.

Considered a particular risk are those items of income and expenditure which are non-routine and involve more management estimation and judgement such as year-end accruals and provisions.

Significant Risk

What did we do?

We performed the following audit procedures:

- Reviewed and tested revenue and expenditure recognition policies;
- Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias;
- Executed a testing strategy to test material revenue and expenditure streams;
- Reviewed and tested revenue cut-off at the period end date

Significant Audit risks and approach:

Management override

What are our conclusions?

We have not identified any material weaknesses in controls or evidence of material management override.

We have not identified any instances of inappropriate judgements being applied.

We did not identify any other transactions during our audit which appeared unusual or outside the Authority's normal course of business

We did identify a small number of low value items of expenditure which we believe were inappropriately capitalised. Weaknesses in controls with respect to expenditure capitalisation have previously been reported to management and we will continue to monitor the effectiveness of the control environment in this regard.

What is the risk?

Risk of management override

As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and to prepare fraudulent financial statements by overriding controls that otherwise seem to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

The potential for the incorrect classification of revenue spend as capital is a particular area where there is a risk of management override.

Significant Risk

What did we do?

We performed the following audit procedures:

- Tested, using a risk based approach, the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;
- Reviewed accounting estimates for evidence of management bias;
- Evaluating the business rationale for significant unusual transactions;
- Reviewed the accounting adjustments processed and disclosed in the Movement in Reserves Statement and supporting notes;
- Tested on a sample basis capital expenditure on property, plant and equipment to ensure it meets the relevant accounting requirements to be capitalised;
- Tested on a sample basis the physical existence of assets held on the fixed asset register.

Significant Audit risks and approach:

Valuation of Property, Plant and Equipment

What is the risk?

Land and buildings is the most significant balance in the Council's Statement of Financial Position.
The valuation of land and buildings is subject to a number of assumptions and judgements and even a small movement in these assumptions, could have a material impact on the accounts.

The Council experienced particular issues in the 2015/16 financial year with respect to the valuation of its land and buildings (excluding Council Dwellings). This is the area where we consider the significant risk to specifically lie.

What did we do?

Management has used external valuers – Cushmans and Wakefield, and Innes England, as experts to value its land and buildings at 31 March 2017. We have evaluated the qualifications and competency of Management's experts to perform this exercise to the required standard.

On a sample basis, we have used our own internal EY valuation experts to perform the following procedures:

- For the specific assets whose valuation at 31 March 2016 was examined in detail by EY Valuations experts in the prior year audit, reviewed the valuation movement between 31 March 2016 and 31 March 2017 to challenge whether this is in line with our expectation;
- For an additional sample of assets, review the asset valuation at 31 March 2017 in detail to ensure that assumptions used are appropriate, valuation basis is appropriate, calculations are accurate.

This work highlighted two assets where the Council's external valuers had made errors in the valuation. The total value of these errors was £4.9m and the Council has adjusted the financial statements.

In response to the errors, the following additional procedures have been performed:

- We have extended our sample of assets for which we have reviewed the asset valuation in detail to ensure that assumptions used are appropriate, valuation basis is appropriate, calculations are clerically accurate.
- We have obtained and reviewed the subsequent further assurances received from the external valuers with respect to the accuracy of valuations; and
- We have reviewed and challenged the work performed by the Council's estates team to review all externally valued assets.

Areas of Audit Focus

What are our conclusions?

Our additional sample of assets selected in order to test the valuations did not reveal further error.

The Council's own internal review of the valuations identified a variance to the GBV of all assets valued by Cushmans and Wakefield of £252,804 (0.06%) and Cushmans and Wakefield have confirmed their own review of their valuations has revealed no further errors.

We have therefore reached the conclusion that the valuation of property, plant and equipment is free from material misstatement.

Significant Risk

Significant Audit risks and approach:

Private Finance Initiative (PFI) Arrangements

What is the risk?

The Council has a number of assets held under PFI arrangements. Four of these are recorded on the Council's balance sheet, one is not. Such arrangements are complex and substantial in value.

What did we do?

We performed the following audit procedures:

- Updated our understanding of the schemes and consideration on whether the schemes falls within IFRIC 12 and should be accounted for on balance sheet;
- Used our PFI specialist to confirm the accounting model reflects the changes recommended in 2015/16 to operator's model and continues to produce reliable results for the financial statements;
- Ensured the outputs from the accounting model are correctly reflected in the financial statements, and relevant disclosures have been made; and
- On a sample basis, ensured the inputs into the model agree to cash payments made by the Authority.

What are our conclusions?

Our PFI expert has reviewed the accounting models for the four PFI schemes accounted for on the Council's balance sheet and we are satisfied the Council has updated the model to account for the changes identified in our 2015/16 audit.

Overall, we are satisfied that the PFI liability is not materially misstated.

Other Audit issues to bring to your attention

In addition to the matters noted above in relation to the significant risks we identified in our audit plan, our audit procedures have identified other matters which we feel it is appropriate to bring to your attention:

Accounting for pension fund liability

Funding of the Council's participation in the local government pension scheme will continue to have an impact on both Council cash flows and balance sheet liabilities.

The pension liability is the most significant liability on the Council's balance sheet and is calculated through use of a number of actuarial assumptions. A small movement in these assumptions could have a material impact on the balance sheet.

We have reviewed the inputs provided to the Council's actuary, reviewed the assumptions used by the Council's actuary, and their output – ensuring that the results are reflected in the Council's statement of account.

We have no issues to report as a result of the procedures performed.

Minimum Revenue Provision

Minimum Revenue Provision (MRP) is a statutory requirement to make a charge to the Council's General Fund to make provision for the repayment of the Council's past capital debt and other credit liabilities. The Council has set aside from revenue a minimum revenue provision of £6.9mn for the year ended 31 March 2017 (£12.3mn for the year ended 31 March 2016).

During 2016/17 the Council has amended its policy for calculating the MRP and have chosen to backdate the change in policy for supported borrowing and two elements of the transferred debt. This has resulted in "overpayment" of £39,505,084 as at 31.3.2016 which the Council intends to release over 9 years in equal instalments from 2016/17.

We have used our in-house MRP specialist to assist in our audit of the Council's amended approach to calculating MRP. The procedures undertaken involved an examination of the base calculation of the Capital Financing Requirement from the balance sheet, and assessing the Council's model for MRP calculation to confirm that it was consistent with the Regulations. In discussion with Management we agreed that further backdating of pre-2008 debt would be permissible under the regulations, resulting in a reduction of £2.143m of MRP which has been recorded as a corrected audit adjustment.

We have concluded that the MRP is not materially misstated.

Financial statements presentation – Expenditure and funding analysis (EFA) and Comprehensive income and expenditure statement

Amendments have been made to the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 (the code) this year changing the way the financial statements are presented. The new reporting requirements impact the Comprehensive Income and Expenditure Statement (CIES) and the Movement in Reserves Statement (MiRS), and include the introduction of the new 'Expenditure and Funding Analysis' note as a result of the 'Telling the Story' review of the presentation of local authority financial statements.

Areas of Audit Focus

This change in the code will require a new structure for the primary statements, new notes and a full retrospective restatement of impacted primary statements. The restatement of the 2015/16 comparatives will require audit review, which could potentially incur additional costs, depending on the complexity and manner in which the changes are made.

We have examined the expenditure and funding analysis, CIES and new notes to ensure disclosures are in line with the code. We have also examined how the figures in the EFA are derived, how the ledger system has been re-mapped to reflect the Council's organisational structure and how overheads are apportioned across the service areas reported.

We have no issues to report.

Consolidation of Derby Homes Limited

Derby City Council has a wholly owned subsidiary company, Derby Homes Limited. We have performed procedures to direct, oversee and conclude upon the work performed by BDO LLP as auditor of Derby Homes Limited in support of the group audit opinion. This has included the issuing of group instructions to BDO LLP, the receipt of formal reporting to EY on conclusion of their planning work and final audit opinion, as well as direct verbal communication between EY and BDO LLP to discuss the extent of work performed on the balances of Derby Homes Limited which are consolidated in the Council's group accounts and any issues arising.

We note that in our review of the audit reporting prepared by the auditors of Derby Homes Limited, there was also an unadjusted error in the Derby Homes Limited accounts that were included in the group accounts of Derby City Council. That misstatement of £107k was below our reporting threshold and therefore does not require further reporting to this committee.

We concluded that no significant issues have arisen as a result of the component auditor's audit procedures with respect to Derby Homes Limited.

Borrowings

The Council has £20m of long term borrowing on lender option, borrower option (LOBO) terms with Royal Bank of Scotland.

We are aware that there is currently sector wide focus on such arrangements as several authorities have received objections to their accounts challenging the legality of such arrangements. We have considered the implications of this for Derby City Council.
We have reviewed legal advice and concluded that even if the LOBO were determined to be unlawful, the lender would likely have recourse back to the Council (and so in effect the Council would end up paying the funds back anyway). We therefore conclude that a decision that LOBOs are unlawful is unlikely to lead to a material adjustment to the liability due by the Council.
At 31 March 2017 the LOBO is classified as a long term liability (as was the case in the prior year). We therefore consider whether the risk of the LOBO being considered illegal results in a need to reclassify the loan to short-term at the balance sheet date. Even if the Council had to repay the loans, they would have access to replacement (long term) loans at better rates in the market and therefore would be in a better rather than worse position. Therefore based on the evidence we have at the time of signing our audit opinion (almost 9 months after the balance sheet date), we do not believe that any adjustment is required to the financial statements.
The LOBO is correctly classified as long term borrowing as in the 12 months following the balance sheet date there has been no objection made nor any other indication that the loan will have to be repaid any sooner than the contracted arrangement would dictate.

03 Audit Report

Draft audit report

Our opinion on the financial statements

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DERBY CITY COUNCIL

Opinion on the Authority's financial statements

We have audited the financial statements of Derby City Council for the year ended 31 March 2017 under the Local Audit and Accountability Act 2014. The financial statements comprise the:

- Authority and Group Movement in Reserves Statement,
- Authority and Group Comprehensive Income and Expenditure Statement,
- Authority and Group Balance Sheet,
- Authority and Group Cash Flow Statement,
- Related Authority financial statement notes 1 to 47 and Group financial statements notes,
- Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement and related notes 1 to 9; and
- Collection Fund and the related notes 1 and 2.

The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.

This report is made solely to the members of Derby City Council, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of the Interim Director of Finance and auditor

As explained more fully in the Statement of the Director of Finance's Responsibilities set out on page 13, the Director of Finance is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Statement of Accounts 2016/17to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the financial position of Derby City Council and Group as at 31 March 2017 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.

Opinion on other matters

In our opinion, the information given in the Statement of Accounts 2016/17 for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we report by exception

We have nothing to report in respect of the following matters:

- in our opinion the annual governance statement is misleading or inconsistent with other information forthcoming from the audit or our knowledge of the Council;
- we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014;
- we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014; or
- we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014.

In respect of the following we have matters to report by exception:

- Matters were reported in the Public Interest

On 23 June 2016 our predecessor, Grant Thornton LLP issued a report in the public interest under section 8 of the Audit Commission Act 1998 in relation to identified failures of governance at Derby City Council in the management of major projects and in relation to Member conduct.

- Written recommendations to the audited body under Section 24 of the Local Audit and Accountability Act

On 27 June 2017 we made written recommendations to Derby City Council under Section 24 of the Local Audit and Accountability Act.

Conclusion on Derby City Council's arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

Auditor's responsibilities

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the National Audit Office (NAO) requires us to report to you our conclusion relating to proper arrangements.

We report if significant matters have come to our attention which prevent us from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criterion issued by the Comptroller and Auditor General (C&AG) in November 2016, as to whether Derby City Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. The Comptroller and Auditor General determined this criterion as that necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether Derby City Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2017.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, Derby City Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Basis for Adverse Conclusion

- Medium Term Financial Planning and strategic risk management

There was no corporate risk strategy in place for the year ended 31 March 2017. The draft strategic risk register went to Chief Officer Group in November 2015, as a working copy for them to comment on. At September 2017, the new strategy document was still in the process of being redrafted.

The risk management annual report for 16/17 which was presented to the Audit Committee on 31 October 2017 stated "One of the key tasks for 2017/18 will be to address the gaps in the Council's risk management procedures."

The continued absence of a corporate risk strategy and risk register lead us to conclude that the Council does not have proper arrangements in place to ensure informed decision making.

The Council have not had a robust MTFP in place throughout the year ended 31 March 2017, with identified savings and sensitivity analysis performed. This demonstrates that the Authority has not planned finances effectively over the entire year under review in order to effectively support the sustainable delivery of strategic priorities and maintain statutory functions.

- Completeness, Existence and Valuation of Property, Plant and Equipment (PPE).

The Council received a whistleblowing allegation with respect to its valuation processes in the financial year ended 31 March 2016 which led to a significant exercise being undertaken to review the Council's entire PPE portfolio to assess its completeness, existence and valuation and significant adjustment being required to the asset valuations previously reported. This work continued throughout the 2016/17 year of account. This provides evidence of weaknesses in proper arrangements for informed decision making.

- Governance issues and management of major projects

Derby City Council was the subject of a public interest report issued by Grant Thornton in June 2016 in relation to identified failures of governance at Derby City Council in the management of major projects and in relation to Member conduct.

The recommendations made in the public interest report are evidence of weaknesses in proper arrangements for informed decision making.

- Maintaining a sound system of internal control

We found that some of the basic financial controls were not working as expected, for example, the regular completion and review of reconciliations was not timely. This increases the risk of fraud or errors remaining undetected and provides evidence of weaknesses in proper arrangements for informed decision making. In July 2017 we issued a statutory written recommendation to the Council with respect to these issues.

- Working with third parties effectively to deliver strategic priorities

Our observation is that the Council has not worked effectively with the Central Midlands Audit Partnership to deliver a robust internal audit function throughout the 2016-17 financial year. Reporting to the Audit and Accounts Committee by internal audit is superficial, we have not seen evidence of Officers being held to account for issues highlighted in internal audit reports but not addressed in a timely manner, nor evidence of challenge where risks are considered 'acceptable' by Officers.

Adverse conclusion

On the basis of our work, having regard to the guidance issued by the C&AG in November 2016, we are not satisfied that, in all significant respects, Derby City Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2017.

Delay in certification of completion of the audit

We cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

Until we have completed these procedures 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 and the Code of Audit Practice issued by the National Audit Office.

Stephen Clark
for and on behalf of Ernst & Young LLP, Appointed Auditor
Birmingham
19 December 2017

The maintenance and integrity of the Derby City Council web site is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the web site.
Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

04 Audit Differences

Audit differences

In any audit, we may identify misstatements between amounts we believe should be recorded in the financial statements and disclosures and amounts actually recorded. These differences are classified as 'known' or 'judgemental'. Known differences represent items that can be accurately quantified and relate to a definite set of facts or circumstances. Judgemental differences generally involve estimation and relate to facts or circumstances that are uncertain or open to interpretation.

Summary of unadjusted differences

We highlight the following misstatements in the financial statements and/or disclosures which were not corrected by management. We ask you to correct these uncorrected misstatements or give a rationale as to why they have not been corrected. This should be considered and approved by the Audit and Accounts Committee] and included in the Letter of Representation:

Account 31 March 2017 (£'000)	Comprehensive income and expenditure statement Debit/(Credit) Current Period	Assets current Debit/ (Credit)	Assets non-current Debit/(Credit)	Liabilities current Debit/(Credit)	Liabilities non-current Debit/(Credit)
Known difference in the classification of Assets Held for Sale (AHFS). Management have decided not to adjust for but instead increase disclosure at the bottom of the AFHS note to state that these assets are now actively marketed.		(6,478)	6,478		
Balance sheet totals	(79,228)	118,389	1,329,590	67,890	876,407

Audit differences (continued)

Summary of adjusted differences

We highlight the following misstatements in the financial statements and/or disclosures which were over our reporting threshold of £357k and were corrected by management:

Account 31 March 2017 (£'000)	Comprehensive income and expenditure statement Debit/(Credit) Current Period	Assets current Debit/ (Credit)	Assets non-current Debit/(Credit)	Liabilities current Debit/(Credit)	Liabilities non-current Debit/(Credit)	Equity components Debit/(Credit)
Incorrect sign used for current service cost in Note 1 of group statements. Impacts only the Group Accounts Disclosure.	62,120			(62,120)		
Credit notes in the creditors control account for invoices that shouldn't have been paid – reclassification from creditors to debtors		425		(425)		
Derbyshire County Council debtor reclassified to long-term debtors.		(1,100)	1,100			
Residential Accommodation debtors reclassified to long-term debtors.		(1,464)	1,464			
Correction of valuation Errors in relation to schools			(4,896)			4,896
Correction of depreciation charge in respect of Council dwellings	1,750					(1,750)
Adjustment to minimum revenue provision: Capital adjustment account Earmarked reserves						 2,143 (2,143)
Correction of capital grants applied: Capital adjustment account Government grants unapplied Capital earmarked reserves						 955 (1,308) 353
Balance sheet totals	(79,228)	118,389	1,329,590	67,890	876,407	503,682

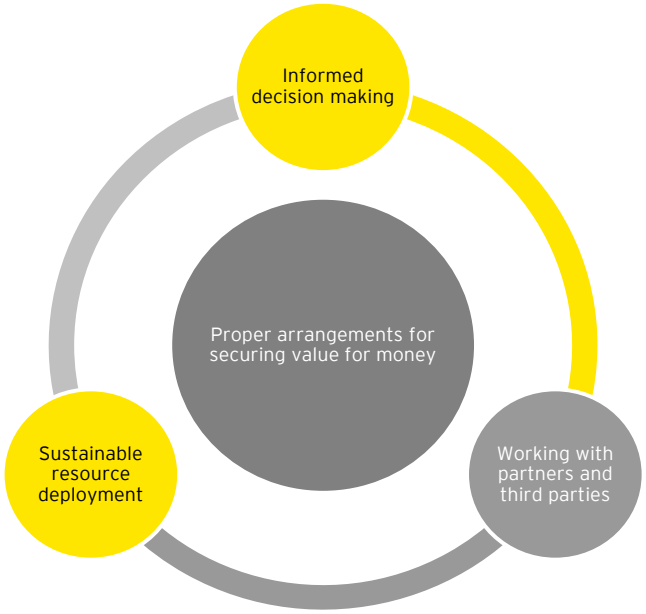
Audit differences (continued)

Summary of adjusted disclosure differences

Disclosure misstatement within Note 33: "the Council contributed £472m towards the cost of the Coroners service" – amended to be £0.472m.
Councillors & Directors Related Party Transactions amended to £394,327 for 9 members rather than £218,426 for 8 members
HRA note 1. Removal of £'000 from the headings of the columns
HRA note 1 figure for Flats (2016/17) is to change from 4,295 to 4,292
While no impact on the HRA surplus/deficit there had been a misclassification of Dwelling Rent income as Non-Dwelling income in both 2015/16 and 2016/17. 2016/17 adjustment reclassification was £250k and 2015/16 adjustment reclassification was £58k.
There has been a change in the disclosure of 'NNDR debtors' between the years. In 2015/16 the NNDR share to Central Government and Fire was included within 'NNDR Debtors' whereas in 2016/17 this has been disclosed within Central Government Debtors and Other Local Authorities debtors. 2015/16 NNDR debtors are £5,672k of which £2,893k relates to Central Government and Fire. The Council have added narrative to explain this change in treatment on the short term debtors note.
EFA note and CIES changes to adhere to Code requirements.
Accounting Policies xiv. A paragraph is to be added in relation componentisation.
Accounting Policies in relation to support service recharges. This paragraph was taken out but will be added back and amended to state that these recharges do not form part of the CIES as they are not reported / notional.
Note 5 (Critical Judgements) - Amendment to be made for decision Chief Operating Decision makers and hence segments for inclusion within the EFA and CIES.
Note 19 - Change in wording as repayment of capital grants is actually repayment of long term debt.
Internal Recharges on the CIES and EFA to be changed to 'Internal Trading'.
Note 7 and 32b amended on line ‘Movements in the market value of investment properties’ to split out AHFS and Investment Properties
EFA note 8 line within Income 'Transfer of interest received to financing and investment income and expenditure' of £11,618k is to be moved to line 'Fees and Charges'

05 Value for Money

Value for Money



Economy, efficiency and effectiveness

We must consider whether you have 'proper arrangements' to secure economy, efficiency and effectiveness in your use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- take informed decisions;
- deploy resources in a sustainable manner; and
- work with partners and other third parties.

In considering your proper arrangements, we use the CIPFA/SOLACE framework for local government to ensure that our assessment is made against an already existing mandatory framework which you use in documents such as your Annual Governance Statement.

Overall conclusion

We identified 6 significant risks around these arrangements. The tables below present our findings in response to the risks which were communicated in our Audit Plan.

We expect to report an adverse conclusion about your arrangements to secure economy, efficiency and effectiveness in your use of resources.

VFM risks

We are only required to determine whether there is any risk that we consider significant within the Code of Audit Practice, where risk is defined as:
"A matter is significant if, in the auditor's professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public"
Our risk assessment supports the planning of enough work to deliver a safe conclusion on your arrangements to secure value for money, and enables us to determine the nature and extent of any further work needed. If we do not identify a significant risk we do not need to carry out further work.
The table below presents the findings of our work in response to the risks areas in our Audit Plan.

What is the significant VFM risk?	What arrangements did this affect?	What are our findings?
June 2016 Public Interest Report Grant Thornton issued a Report in the Public Interest in June 2016 which highlighted governance issues which remained present in the 2016/17 year of account.	This report, and the Council's response to it therefore presents a significant risk to our VFM conclusion in terms of 'proper arrangements for informed decision making – by acting in the public interest, through demonstrating and applying the principles and values of sound governance'.	The public interest report issued by Grant Thornton in June 2016 made several recommendations with respect to issues continuing in the 2016/17 financial year which are relevant to the Council's arrangements for ensuring informed decision making, including: ▸ Review of project procurement and monitoring systems to ensure that appropriate decisions are made regarding externally commissioned services ▸ Ensure continued monitoring of Member interventions in operational matters relating to taxi licencing ▸ Review the quality of decision making by the taxi licencing committee ▸ Reinforce the need for officers to observe the Council's contract procedure rules. This impacts the Council's arrangements for Informed decision making and contributes to our qualified conclusion.
Robustness of medium term financial planning The Council's Medium Term Financial Plan and planning process is not sufficiently robust. Savings targets are not accompanied by detailed plans on how the savings are to be achieved. There is no provision for scenario planning to identify financial sensitivities within the Medium Term Financial Plan.	This presents a significant risk to our Value For Money conclusion in terms of 'sustainable resource deployment - Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions'.	We have met with Officers and Members who have concurred that the Authorities MTFP arrangements during the 2016/17 financial year were weak. The Authority is working to put in place more robust analysis and challenge (sensitivities, etc) however this was not in place for 2016/17. Since the Council has not had a robust MTFP in place throughout the entire period under audit with identified savings and sensitivity analysis performed, this contributes to our qualified VFM conclusion.

Value for Money

What is the significant VFM risk?	What arrangements did this affect?	What are our findings?
July 2017 written recommendations under s24 of Local Audit and Accountability Act In June 2017 EY exercised its powers under the Local Audit and Accountability Act 2014 and issued written recommendations to the Council. Although some progress had been made, it was our view that given the significance of the control weaknesses, insufficient progress has been made in the period following our report of 23 September 2016 to appropriately address the issues and strengthen the Council's control environment. The control issues identified across a significant number of areas of the Finance and associated supporting functions, most noticeably in respect of the Estates function, are pervasive and led to a significant number of errors identified in the 2015/16 published draft Financial Statements relating to both the current and prior year accounting periods. This could undermine the Council's ability to effectively demonstrate it has proper arrangements to safeguard and make informed decisions in respect of public funds and assets.	This presents a significant risk to our VFM conclusion in terms of: ▸ 'sustainable resource deployment - Managing and utilising assets effectively to support the delivery of strategic priorities'; and ▸ 'proper arrangements for informed decision making - Managing risks effectively and maintaining a sound system of internal control'	Subsequent to the issuance of our s24 recommendations the Authority put in place an action. This was a forward looking plan, so commencing in June 2017 meant that the 2016/17 accounting year had already concluded. Nevertheless, when the accounts team became familiar with basic controls such as meaningful reconciliations, they did 'go back' and reconcile accounts at 31 March 2017 in order to facilitate the 2016/17 audit process. That said, we can only conclude that the arrangements were not in place for the 2016/17 period and this contributes to our VFM qualification.
Provision of internal audit services EY have attended all Audit Committee meetings held throughout the 2016/17 reporting period. In our view, the reporting to the Committee by internal audit is superficial, and the challenge provided by the Audit Committee to the matters raised by internal audit is often weak. We have not seen evidence of Officers being held to account for issues highlighted in internal audit reports but not addressed in a timely manner, nor evidence of challenge where risks are considered 'acceptable' by Officers. In early 2017 the Council have initiated a review of the internal audit service offering, and a number of weaknesses have been identified which have led to a transformation programme being initiated.	This significant risk to our VFM conclusion affects the Authority's arrangements in respect of 'working with partners and other third parties - Working with third parties effectively to deliver strategic priorities.'	Whilst a program of change to the internal audit provision has now been initiated, this was still at a very early stage at 31 March 2017. This contributes to our qualified VFM conclusion.

What is the significant VFM risk?	What arrangements did this affect?	What are our findings?
Results of regulatory reviews and commentary The Council has received various commentaries throughout the year from regulatory bodies, the tone of which has been mixed. Recent findings in respect of education provision across the City from Ofsted and more broadly across the Council's activities from the Local Government Association (LGA) Peer Review indicate a significant risk to our VFM conclusion.	This significant risk to our VFM conclusion affects the Authority's arrangements in respect of 'Working with third parties effectively to deliver strategic priorities'	The LGA peer review contains many of the same issues already noted above from the Public interest report, s24 recommendations, and 2015/16 qualified VFM conclusion. There are no significant 'new' issues highlighted. We have discussed the Council's response to the Ofsted inspections with the Strategic Director of People Services. Whilst children's services received a 'good' assessment in the year, schools were less successful. This is in large part due to a small number of weak academies bringing overall scores down. Whilst the council retains statutory duty for service provision, the extent to which it can influence performance at academies is less than for LEA maintained schools. However, an action plan has been drawn up and interventions are taking place to bring together good practice examples and effect change. We have therefore concluded that this risk does not lead to a qualification of our VFM conclusion at 31 March 2017.
Absence of corporate risk strategy and risk register There was no corporate risk strategy in place that covered 2016/17. The draft strategic risk register went to Chief Officer Group in November 2015, as a working copy for them to comment on. It was agreed that a clearer definition of the risk appetite and what would and would not be tolerated was needed. At September 2017, the new strategy document was still in the process of being redrafted.	This presents a significant risk in respect of the Council's arrangements for managing risks effectively, and the ability to make informed decisions.	The risk management annual report for 2016/17 which was presented to the audit committee on 31 October 2017 stated "One of the key tasks for 2017/18 will be to address the gaps in the Council's risk management procedures." The continued absence of a corporate risk strategy and risk register lead us to conclude that the Council does not have proper arrangements in place to ensure informed decision making.

Other matters to bring to your attention

We noted the following issues as part of our audit

The Authority engaged the services of an Interim Director of Finance and s151 Officer in May 2017. This Officer has had responsibility for implementing an action plan (the Corporate Improvement Plan) to address the issues raised in the Grant Thornton Public Interest Report, the EY s24 Written Recommendations, and the Local Government Association Peer Review.

What are our findings?

From our discussions with the Authority's Chief Executive, Interim Director of Finance and s151 Officer, Monitoring Officer, and Head of Internal Audit we would make the following observations to bring to the Committee's attention:

- Senior Officers have a good understanding of the changes which need to be made at the Authority to address the issues raised by the various commentators noted above, and have documented action plans in place designed to affect these changes.
- Whilst it is too early for us to comment on the success of the Authority in achieving the actions set out in the plans, we can share with you our observations in respect of the issues we raised in our s24 written recommendations. During our 2016/17 audit we have noted an improvement in the quality of the basic accounting information being produced, and the working papers produced to support the statement of accounts. Whilst these remain far from best practice and the direction of travel is seen as positive, this has been achieved for the most part by means of significant management intervention rather than the result of a well embedded routine financial reporting process.
- For the changes to become embedded, a continued and sustained cultural shift will be required.
- The Audit Committee seeks its assurance from three primary sources: Officers, Internal audit, and External audit. Our observation is that the relationship between the Council and the internal audit provider is dysfunctional. It is not operating in a way which enables the Audit Committee to obtain the assurance which it should be able to from an internal audit provider and this should be addressed as a matter of priority.

06 Other reporting issues

Other reporting issues

Consistency of other information published with the financial statements, including the Annual Governance Statement

We must give an opinion on the consistency of the financial and non-financial information in the Statement of Accounts 2016/17 with the audited financial statements

We must also review the Annual Governance Statement for completeness of disclosures, consistency with other information from our work, and whether it complies with relevant guidance.

We have reviewed the financial and non-financial information in the Statement of Accounts 2016/17 and consider it to be consistent with the audited financial statements.

We have reviewed the draft Annual Governance Statement and can confirm it is consistent with other information from our audit of the financial statements and we have no other matters to report.

Whole of Government Accounts

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review, and the nature of our report, is specified by the National Audit Office.

We have yet to commence our work in this area and will report any matters arising to the Audit and Accounts Committee.

Other reporting issues

Other powers and duties

We have a duty under the Local Audit and Accountability Act 2014 to consider whether to report on any matter that comes to our attention in the course of the audit, either for the Authority to consider it or to bring it to the attention of the public (i.e. "a report in the public interest").

We also have a duty to make written recommendations to the Authority, copied to the Secretary of State, and take action in accordance with our responsibilities under the Local Audit and Accountability Act 2014.

On 23 March 2016, Grant Thornton, our predecessor, used their statutory powers to issue a Report in the Public Interest on 16 June 2016.

The report highlighted various matters of concern with respect to the Council's Governance arrangements (both historic and ongoing), Member/Officer relations, and Procurement and Project Management arrangements. Our audit approach has been responsive to the issues raised in Grant Thornton's Public Interest Report and the report is specifically referenced in our Value for Money conclusion.

In June 2017, we used our statutory powers under Section 24 of the Local Audit and Accountability Act 2014 and issued written recommendations to the Council. This followed significant delays in the finalisation of the Council's 2015/16 Statement of Account and an unacceptable length of time being taken to respond to and correct control weaknesses identified in our audit procedures, and communicated to the Audit and Accounts Committee in September 2016

Other reporting issues

Other matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we must tell you significant findings from the audit and other matters if they are significant to your oversight of the Authority's financial reporting process. They include the following:

- Significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures;
- Any significant difficulties encountered during the audit;
- Any significant matters arising from the audit that were discussed with management;
- Written representations we have requested;
- Expected modifications to the audit report;
- Any other matters significant to overseeing the financial reporting process;
- Related parties;
- External confirmations;
- Going concern;
- Consideration of laws and regulations; and
- Group audits

We have included all matters which we wish to communicate to you in this report.

07 Assessment of Control Environment

Assessment of control environment

Financial controls

It is the responsibility of the Authority to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Authority has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. As we have adopted a fully substantive approach, we have not tested the operation of controls.

Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control.

In June 2017, we used our statutory powers under Section 24 of the Local Audit and Accountability Act 2014 and issued written recommendations to the Council. These were presented at the meeting of the Full Council on 19th July 2017. This followed significant delays in the finalisation of the Council's 2015/16 Statement of Account and an unacceptable length of time being taken to respond to and correct control weaknesses identified in our audit procedures, and communicated to the Audit and Accounts Committee in September 2016. Given the timing of the written recommendations, all matters reported in those recommendations were also relevant to the 2016/17 year of account.

In addition to the matters previously reported to the Authority in the June 2017 written recommendations, the following control observations have been noted during the course of our 2016/17 audit procedures. The matters reported here are limited to those deficiencies identified during the audit and important enough for us to report to you.

Observation:

The Council incurs expenditure through an outsourced payroll provider – EPM. In 2016/17 £6million of expenditure has gone through EPM representing the 5 schools which use the provider.

No internal audit work is currently being performed over the internal control environment, operating effectiveness and reporting at EPM by the Council nor has any service organisation auditors report been requested from EPM by the Council.

Effect:

There is a risk that payroll processing by EPM is inaccurate, incorrect, or incomplete.

Recommendation:

The Council should seek assurance over the robustness of controls at the outsourced provider and the schools to ensure amounts being included in the financial statements of the Authority are free from material misstatement.

Management response:

To be provided.

08 Appendices

Appendix B

Required communications with the Audit and Accounts Committee

There are certain communications that we must provide to the Audit Committees of UK clients. We have done this by:

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, including any limitations.	19 September2017 Audit Plan
Significant findings from the audit	▸ Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▸ Any significant difficulties encountered during the audit ▸ Any significant matters arising from the audit that were discussed with management ▸ Written representations we have requested ▸ Expected modifications to the audit report ▸ Any other matters significant to overseeing the financial reporting process	13 December 2017 Audit Results Report
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: ▸ Whether the events or conditions constitute a material uncertainty ▸ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▸ The adequacy of related disclosures in the financial statements	No conditions or events were identified, either individually or together to raise any doubt about Derby City Council's ability to continue for the 12 months from the date of our report
Misstatements	▸ Uncorrected misstatements and their effect on our audit opinion ▸ The effect of uncorrected misstatements related to prior periods ▸ A request that any uncorrected misstatement be corrected ▸ Significant corrected misstatements, in writing	13 December 2017 Audit Results Report

Appendix B

Required communications	What is reported?	Our Reporting to you When and where
Fraud	▸ Asking the Audit Committee whether they have knowledge of any actual, suspected or alleged fraud affecting the Authority ▸ Unless all those charged with governance are involved in managing the entity, any fraud identified or information obtained indicating that a fraud may exist involving: (a) management; (b) employees with significant roles in internal control; or (c) others where the fraud results in a material misstatement in the financial statements. ▸ A discussion of any other matters related to fraud, relevant to Audit Committee responsibility.	We have asked management and those charged with governance about arrangements to prevent or detect fraud. We have not become aware of any fraud or illegal acts during our audit.
Related parties	Significant matters arising during the audit in connection with the Authority's related parties including, where applicable: ▸ Non-disclosure by management ▸ Inappropriate authorisation and approval of transactions ▸ Disagreement over disclosures ▸ Non-compliance with laws and/or regulations ▸ Difficulty in identifying the party that ultimately controls the entity	We have no matters to report
Subsequent events	▸ Where appropriate, asking the Audit Committee whether any subsequent events have occurred that might affect the financial statements.	We have asked management and those charged with governance. We have no matters to report
Other information	▸ Where material inconsistencies are identified in other information included in the document containing the financial statements, but management refuses to make the revision.	We have no matters to report
External confirmations	▸ Management's refusal for us to request confirmations ▸ We were unable to obtain relevant and reliable audit evidence from other procedures.	We have received all requested confirmations
Consideration of laws and/or regulations	▸ Audit findings of non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on "tipping off" ▸ Asking the Audit Committee about possible instances of non-compliance with laws and/or regulations that may have a material effect on the financial statements, and known to the Audit Committee.	We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations

Appendix B

Required communications	What is reported?	Our Reporting to you When and where
Significant deficiencies in internal controls identified during the audit	▸ Significant deficiencies in internal controls identified during the audit.	13 December 2017 Audit Results Report
Group Audits	▸ An overview of the type of work to be performed on the financial information of the components ▸ An overview of the group audit team's planned involvement in the component auditors' work on the financial information of significant components ▸ Instances where the group audit team's evaluation of a component auditor's work of gave rise to a concern about its quality Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted ▸ Fraud or suspected fraud involving group or component management, employees with significant roles in group-wide controls, or others where the fraud resulted in a material misstatement of the group financial statements.	19 September 2017 Audit Plan 13 December 2017 Audit Results Report
Independence	Communication of all significant facts and matters that have a bearing on EY's objectivity and independence. Communicating key elements of the audit engagement partner's consideration of independence and objectivity such as: ▸ The principal threats ▸ Safeguards adopted and their effectiveness ▸ An overall assessment of threats and safeguards ▸ Information on the firm's general policies and processes for maintaining objectivity and independence Communications whenever significant judgments are made about threats to objectivity or independence and the appropriateness of safeguards,	19 September 2017 Audit Plan 13 December 2017 Audit Results Report
Fee Reporting	Breakdown of fee information when the audit plan is agreed Breakdown of fee information at the completion of the audit Any non-audit work	19 September 2017 Audit Plan 13 December 2017 Audit Results Report
Certification work	Summary of certification work	Certification Report] – to be issued early 2018

Independence

We confirm that there are no changes in our assessment of independence since our confirmation in our audit planning board report dated 19 September 2017.

We complied with the APB Ethical Standards and the requirements of the PSAA's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that you consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the Audit Committee on19 December 2017.

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31March 2017.

We confirm that we have undertaken non-audit work outside the PSAA Code requirements as follows:

- Housing Benefit certification work
- Teachers' pension certification work

We have adopted the necessary safeguards in completing this work and complied with Auditor Guidance Note 1 issued by the NAO in December 2016.

Description	Scale Fee for 2016/17	Final fee for 2016/17
Opinion Audit and VFM Conclusion	£142,553	TBC*
Certification of Claims and Return	£19,725	£19,725
Non audit work	n/a	6,000

*scale fee variations are subject to PSAA approval.

All fees exclude VAT

Appendix C

Outstanding matters

The following items are outstanding at the date of this report:

Item	Actions to resolve	Responsibility
Management representation letter	Receipt of signed management representation letter	Management
Review of final Annual Governance Statement	Receipt of final Annual Governance Statement	EY and management
Procedures with respect to the Whole of Government Accounts return	Receipt of the Council's WGA submission Performance of audit procedures in accordance with NAO instructions	EY and management

Appendix D

Accounting and regulatory update

Accounting update

The following new accounting standards and interpretations have been issued. The following table provides a high level summary of those that have the potential to have the most significant impact on you:

Name	Summary of key measures	Impact on Derby City Council
IFRS 9 Financial Instruments	Applicable for local authority accounts from the 2018/19 financial year and will change: ▸ How financial assets are classified and measured ▸ How the impairment of financial assets are calculated ▸ Financial hedge accounting ▸ The disclosure requirements for financial assets. ▸ Transitional arrangements are included within the accounting standard, however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be and whether any accounting statutory overrides will be introduced to mitigate any impact.	Although some initial thoughts on the approach to adopting IFRS 9 have been issued by CIPFA, until the Code is issued and any statutory overrides are confirmed there remains some uncertainty. However, what is clear is that the Council will have to: ▸ Reclassify existing financial instrument assets ▸ Remeasure and recalculate potential impairments of those assets; and ▸ Prepare additional disclosure notes for material items The Council is awaiting clarification of the exact requirements before investing time in the above work.

Appendix D

IFRS 15 Revenue from Contracts with Customers	Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except: ▸ Leases; ▸ Financial instruments; ▸ Insurance contracts; and ▸ for local authorities; Council Tax and NDR income. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. ▸ There are transitional arrangements within the standard; however as the 2018/19 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be.	As with IFRS 9, some initial thoughts on the approach to adopting IFRS 15 have been issued by CIPFA. However, until the Code is issued there remains some uncertainty. However, what is clear is that for all material income sources from customers the Council will have to: ▸ Disaggregate revenue into appropriate categories ▸ Identify relevant performance obligations and allocate income to each ▸ Summarise significant judgements The Council is awaiting clarification of the exact requirements before investing time in the above work.
IFRS 16 Leases	IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease in a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. There are transitional arrangements within the standard, although as the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued it is unclear what the impact on local authority accounting will be or whether any statutory overrides will be introduced.	Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the Council will need to undertake a detailed exercise to classify all of its leases and therefore must ensure that all lease arrangements are fully documented. The Council is has yet to commence work in this area due to the timing of implementation.

Accounting and regulatory update (continued)

Progress report on implementation of new standards and regulations

In previous reports to the Audit and Accounts Committee, we have highlighted the issue of new accounting standards and regulatory developments. The following table summarises progress on implementation:

Name	Summary of key measures	Impact on Derby City Council
Earlier deadline for production and audit of the financial statements from 2017/18	▸ The Accounts and Audit Regulations 2015 introduced a significant change in statutory deadlines from the 2017/18 financial year. From that year the timetable for the preparation and approval of accounts will be brought forward with draft accounts needing to be prepared by 31 May and the publication of the audited accounts by 31 July.	These changes provide challenges for both the preparers and the auditors of the financial statements. Whilst many Councils have been taking active steps to prepare for this change in timetable, Derby City Council has been working towards achieving conclusion of its 2015/16 and 2016/17 financial statements – both of which missed the 30 September deadline. Nevertheless, the Authority has taken a number of steps as outlined below: ▸ Considered streamlining the Statement of Accounts removing all non-material disclosure notes ▸ Brought forward the commissioning and production of key externally provided information such as asset valuations ▸ Provided training to departmental finance staff regarding the requirements and implications of earlier closedown ▸ Commenced discussions with EY to consider which working papers could be provided early in order to bring forward audit work. As auditors, nationally we have: ▸ Issued a thought piece on early closedown ▸ As part of the strategic Alliance with CIPFA jointly presented accounts closedown workshops across England, Scotland and Wales ▸ Presented at CIPFA early closedown events and on the subject at the Local Government Accounting Conferences in July 2017

Appendix E

Management representation letter

Management Rep Letter

In addition to the 'standard' written representations which we are required by auditing standards to obtain from management, we consider it appropriate to request specific additional written representations in respect of the following matters:

- Tenants rent provision
- Equal pay provision
- HRA overpayments provision
- National Non-Domestic Rates provision
- Restatement of comparatives on introduction of the Expenditure and Funding Analysis

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ED None

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