



The Audit Findings Report for Southwark Council

Year ended 31 March 2017

13 September 2017

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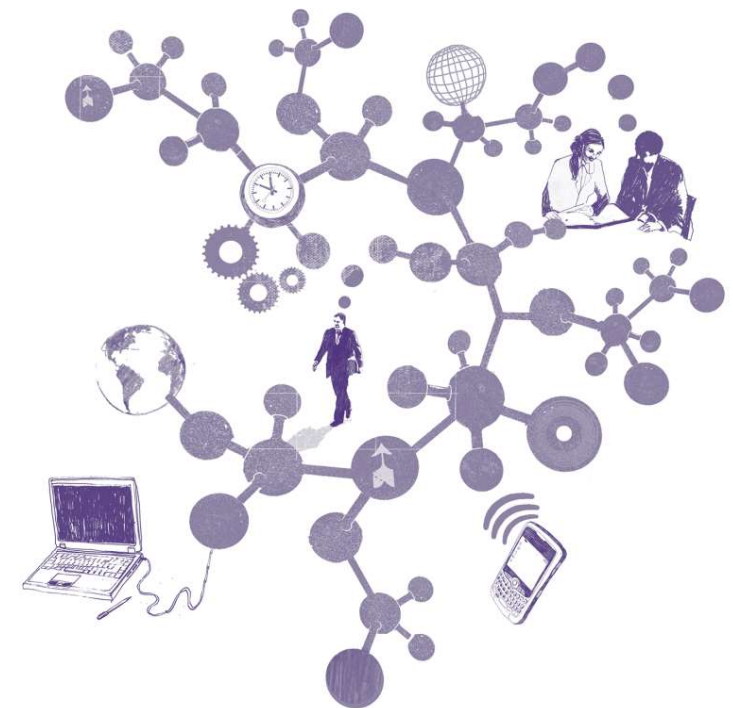
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Southwark Council
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13 September 2017

Dear Members of the Audit, Governance and Standards Committee

Audit Findings Report for Southwark Council for the year ending 31 March 2017

This Audit Findings Report highlights the key findings arising from the audit that are significant to the responsibility of those charged with governance (in the case of Southwark Council, the Audit, Governance and Standards Committee), to oversee the financial reporting process, as required by International Standard on Auditing (UK & Ireland) 260, the Local Audit and Accountability Act 2014 and the National Audit Office Code of Audit Practice. Its contents have been discussed with Management.

As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK & Ireland) ('ISA (UK&I)'), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements and giving a value for money conclusion. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

We would like to take this opportunity to record our appreciation for the kind assistance provided by the finance team and other staff during our audit.

Yours sincerely

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Section 1: Executive summary

01. Executive summary

02. Audit findings

03. Value for Money

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Purpose of this report

This report highlights the key issues affecting the results of Southwark Council ('the Council') and the preparation of the Council's financial statements for the year ended 31 March 2017. It is also used to report our audit findings to management and those charged with governance in accordance with the requirements of ISA (UK&I) 260, and the Local Audit and Accountability Act 2014 ('the Act').

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Council's financial statements give a true and fair view of the financial position of the Council and its income and expenditure for the year and whether they have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting. .

We are also required to consider other information published together with the audited financial statements (including the Annual Governance Statement (AGS) and Narrative Report, whether it is consistent with the financial statements, apparently materially incorrect based on, or materially inconsistent with, our knowledge of the Council acquired in the course of performing our audit; or otherwise misleading.

We are required to carry out sufficient work to satisfy ourselves on whether the Council has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources ('the value for money (VFM) conclusion'). Auditor Guidance Note 7 (AGN07) clarifies our reporting requirements in the Code and the Act. We are required to provide a conclusion whether in all significant respects, the Council has put in place proper arrangements to secure value for money through economic, efficient and effective use of its resources for the year.

The Act also details the following additional powers and duties for local government auditors, which we are required to report to you if applied:

- a public interest report if we identify any matter that comes to our attention in the course of the audit that in our opinion should be considered by the Council or brought to the public's attention (section 24 of the Act);
- written recommendations which should be considered by the Council and responded to publicly (section 24 of the Act);
- application to the court for a declaration that an item of account is contrary to law (section 28 of the Act);
- issue of an advisory notice (section 29 of the Act); and
- application for judicial review (section 31 of the Act).

We are also required to give electors the opportunity to raise questions about the accounts and consider and decide upon objections received in relation to the accounts under sections 26 and 27 of the Act.

Introduction

In the conduct of our audit we have not had to alter or change our audit approach, which we communicated to you in our Audit Plan dated February 2017.

Our audit is substantially complete although we are finalising our procedures in the following areas:

- our final internal reviews
- review of the final version of the financial statements
- obtaining and reviewing the management letter of representation
- updating our post balance sheet events review, to the date of signing the opinion
- Whole of Government Accounts

We have received one objection from a member of the public in respect of the Accounts which we are currently considering and we will keep the Council updated with our progress on this.

Key audit and financial reporting issues

Financial statements opinion

We have identified no adjustments affecting the Council's reported financial position (details are recorded in section two of this report). The draft financial statements for the year ended 31 March 2017 recorded net expenditure of £397,144k, which will be the figure disclosed in the audited financial statements. We have recommended a number of adjustments to improve the presentation of the financial statements.

The key messages arising from our audit of the Council's financial statements are:

- The draft statements presented for audit were of a good standard and the only adjustments required were minor classification and disclosure amendments.
- On the whole the working papers submitted to audit were of a good standard and the Council were responsive to the requests for audit evidence. However some of the detailed samples took longer to be collated than expected, and there were particular challenges in obtaining audit evidence from HR, as covered by the control point in the following column. We recognise a new Head of HR has been in post since October and we look forward to working with them to resolve these issues ahead of next year's move in the deadline to 31 July 2018.

Further details are set out in section two of this report.

We anticipate providing an unqualified audit opinion in respect of the financial statements (see Appendix B).

Other financial statement responsibilities

As well as an opinion on the financial statements, we are required to give an opinion on whether other information published together with the audited financial statements is consistent with the financial statements. This includes if the AGS and Narrative Report is misleading or inconsistent with the information of which we are aware from our audit.

Based on our review of the Council's Narrative Report and AGS we are satisfied that they are consistent with the audited financial statements. We are also

satisfied that the AGS meets the requirements set out in the CIPFA/SOLACE guidance and that the disclosures included in the Narrative Report are in line with the requirements of the CIPFA Code of Practice.

Controls

Roles and responsibilities

The Council's management is responsible for the identification, assessment, management and monitoring of risk, and for developing, operating and monitoring the system of internal control.

Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we report these to the Council.

Findings

We draw your attention in particular to the following control issues identified:

- As in the previous year, we encountered a challenge in obtaining copies of employee's contracts to confirm their existence and employment status with the Council. After some initial delays, the Council were able to provide all of these which shows some improvement from the position in the previous year.
- The Council were unable to locate a letter of engagement for a casual worker who formed part of our sample. Whilst we were able to obtain alternative audit evidence to confirm the existence of this individual, we have raised a recommendation to ensure formal documentation for casual workers is in place to confirm their employment status with the Council.
- We also identified minor issues with the termination benefit packages paid during the course of the year.

Further details are provided within section two of this report.

Value for Money

Based on our review, we are satisfied that, in all significant respects, the Council had proper arrangements in place to secure economy, efficiency and effectiveness in its use of resources.

Further detail of our work on Value for Money are set out in section three of this report.

Other statutory powers and duties

We have not identified any issues that have required us to apply our statutory powers and duties under the Act.

Further details of our work on other statutory powers and duties is set out in section four of this report.

Early close

From 2017/18, the statutory deadlines for preparation and audit of the financial statements will be brought forward and the Council will be required to produce draft statements by 31 May 2018, and secure an audit opinion by 31 July 2018. We had a successful interim audit, with a substantial amount of early audit testing completed during March. This has helped drive efficiencies within the year end audit process and as a result we were able to complete the majority of our substantive testing within six weeks.

The Council provided us with a good set of financial statements and a large number of the working papers by the end of June 2017. Moving towards an earlier deadline, the Council will need to ensure that its internal processes are streamlined to ensure, in particular, sample documentation is received back from the relevant Departments in a timely manner. This has been recognised by the finance team, and a full debrief will be held between the audit and finance team over the coming weeks to identify solutions to these challenges.

We have worked with many large clients to successfully implement faster close and will continue to work with you during the coming year to support you in achieving

the earlier deadlines. This will include the audit team holding a session with the Heads of Departments ahead of the 2017-18 audit to explain the audit process and the role they and their Departments play in ensuring the end of July 2018 statutory deadline is met.

Grant certification

In addition to our responsibilities under the Code, we are required to certify the Council's Housing Benefit subsidy claim on behalf of the Department for Work and Pensions. At present our work on this claim is in progress and is not due to be finalised until 30 November 2017. We will report the outcome of this certification work through a separate report to the Audit, Governance and Standards Committee due to be issued in early 2018.

The way forward

Matters arising from the financial statements audit and our review of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources have been discussed with the Strategic Director of Finance and Governance

We have made a number of recommendations, which are set out in the action plan at Appendix A. Recommendations have been discussed and agreed with the Strategic Director of Finance and Governance and the finance team.

Acknowledgement

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

Grant Thornton UK LLP
September 2017

Section 2: Audit findings

01. Executive summary

02. Audit findings

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05. Communication of audit matters

Materiality

In performing our audit, we apply the concept of materiality, following the requirements of ISA (UK&I) 320: Materiality in planning and performing an audit. The standard states that 'misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements'.

As we reported in our audit plan, we determined overall materiality to be £25,023k (being 2% of gross revenue expenditure). We have considered whether this level remained appropriate during the course of the audit and have made no changes to our overall materiality.

We also set an amount below which misstatements would be clearly trivial and would not need to be accumulated or reported to those charged with governance because we would not expect that the accumulated effect of such amounts would have a material impact on the financial statements. We have defined the amount below which misstatements would be clearly trivial to be £1,260k, which remains the same as reported in our audit plan.

As we reported in our audit plan, we identified the following items where we decided that separate materiality levels were appropriate. These remain the same as reported in our audit plan.

Balance/transaction/disclosure	Explanation	Materiality level
Cash and cash equivalents	Although the balance of cash and cash equivalents is immaterial, all transactions made by the Council affect the balance and it is therefore considered to be material by nature.	£500k
Disclosures of officers' remuneration, salary bandings and exit packages in notes to the statements	Due to public interest in these disclosures and the statutory requirement for them to be made.	£1k
Disclosure of auditor's remuneration	This is a statutory requirement and a requirement of ethical and auditing standards.	£1k

Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements; Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered. (ISA (UK&I) 320)

Audit findings against significant risks

In this section we detail our response to the significant risks of material misstatement which we identified in the Audit Plan. As we noted in our plan, there are two presumed significant risks which are applicable to all audits under auditing standards.

Risks identified in our audit plan	Work completed	Assurance gained and issues arising
<p>The revenue cycle includes fraudulent transactions</p> <p>Under ISA (UK&I) 240 there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.</p> <p>This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.</p>	<p>Having considered the risk factors set out in ISA240 and the nature of the revenue streams at Southwark Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:</p> <ul style="list-style-type: none"> • there is little incentive to manipulate revenue recognition; • opportunities to manipulate revenue recognition are very limited; and • the culture and ethical frameworks of local authorities, including the London Borough of Southwark, mean that all forms of fraud are seen as unacceptable. <p>Therefore we have determined that this is not a significant risk for Southwark Council.</p>	<p>Our audit work has not identified any issues in respect of revenue recognition.</p>
<p>Management over-ride of controls</p> <p>Under ISA (UK&I) 240 it is presumed that the risk of management over-ride of controls is present in all entities.</p>	<p>We have completed the following work in respect of this risk:</p> <ul style="list-style-type: none"> • reviewed the journal entry process and selected unusual journal entries for testing back to supporting documentation • reviewed the accounting estimates, judgements and decisions made by management • reviewed any unusual significant transaction recorded within the Accounts 	<p>Our audit work has not identified any evidence of management over-ride of controls. In particular the findings of our review of journal controls and testing of journal controls and testing of journal entries has not identified any significant issues.</p> <p>We set out later in this section of the report our work and findings on key accounting estimates and judgements.</p>

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, due to either size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty." (ISA (UK&I) 315) . In making the review of unusual significant transactions "the auditor shall treat identified significant related party transactions outside the entity's normal course of business as giving rise to significant risks." (ISA (UK&I) 550)

Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan. Recommendations, together with management responses are attached at Appendix A.

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Employee remuneration	<p>Payroll expenditure represents a significant percentage of the Council's gross expenditure.</p> <p>We identified the completeness of payroll expenditure in the financial statements as a risk requiring particular audit attention:</p> <ul style="list-style-type: none"> Employee remuneration accruals understated (Remuneration expenses not correct) 	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> documented our understanding of processes and key controls over the transaction cycle undertaken walkthrough of the key controls to assess the whether those controls were in line with our documented understanding tested a sample of revenue expenditure items across the whole financial year back to supporting documentation tested unrecorded liabilities to confirm the completeness and cut off of transactions included within the Accounts 	<p>Our audit work has not identified any significant issues in relation to the risk identified.</p> <p>As mentioned in the Executive Summary, a recommendation has been raised around ensuring sufficient documentation is in place for casual workers employed by the Council.</p>
Operating expenses	<p>Non-pay expenditure represents a significant percentage of the Council's gross expenditure. Management uses judgement to estimate accruals of un-invoiced non-pay costs.</p> <p>We identified the completeness of non- pay expenditure in the financial statements as a risk requiring particular audit attention:</p> <ul style="list-style-type: none"> Creditors understated or not recorded in the correct period (Operating expenses understated) 	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> documented our understanding of processes and key controls over the transaction cycle undertaken walkthrough of the key controls to assess the whether those controls were in line with our documented understanding performed substantive sampling of the employee remuneration costs included within the Accounts, testing back to supporting documentation reviewed the reconciliation between the subsidiary system interfaces and the general ledger control accounts completed a monthly trend analysis of the payments recognised by the Council 	<p>Our audit work has not identified any significant issues in relation to the risk identified.</p>

Audit findings against other risks (continued)

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Property, Plant and Equipment (PPE)	Property, plant and equipment activity not valid	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> documented our understanding of processes and key controls over the transaction cycle undertaken walkthrough of the key controls to assess the whether those controls were in line with our documented understanding completed substantive testing of the entries included within the PPE notes reviewed the capital programme against the additions recorded in the asset register in the financial year, including testing on a sample basis 	<p>During our testing we identified one property, with a value of £1.96m, which had been disposed in-year but remained in the Asset Register and the Accounts at year end. We have performed further work to confirm that this issue is isolated. Due to the fact that this item is immaterial, the Council are not proposing to amend, and thus this has been reported as an unadjusted misstatement later in this Report.</p> <p>No other issues were identified from the work performed in respect of the risk identified.</p>
Property, Plant and Equipment	Revaluation measurements not correct	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> documented our understanding of processes and key controls over the transaction cycle undertaken walkthrough of the key controls to assess the whether those controls were in line with our documented understanding reconciled the valuation report to the asset register and the accounts reviewed the competence, expertise and objectivity of management's experts reviewed the work performed by the valuer, including ensuring that any valuations have been undertaken in accordance with the requirements of the appropriate accounting and professional standards reviewed and challenged the data used by the valuer to ensure that it is complete, robust and consistent with our understanding 	<p>No significant issues were identified from the work performed in respect of the risk identified.</p>

"In respect of some risks, the auditor may judge that it is not possible or practicable to obtain sufficient appropriate audit evidence only from substantive procedures. Such risks may relate to the inaccurate or incomplete recording of routine and significant classes of transactions or account balances, the characteristics of which often permit highly automated processing with little or no manual intervention. In such cases, the entity's controls over such risks are relevant to the audit and the auditor shall obtain an understanding of them." (ISA (UK&I) 315)

Audit findings against other risks continued

Going concern

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of management's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK&I) 570).

We reviewed the management's assessment of the going concern assumption and the disclosures in the financial statements and concluded that we concur with management's assessment that the Council remains a going concern for the foreseeable future.

Changes to the presentation of local authority financial statements

CIPFA has been working on the ‘Telling the Story’ project, for which the aim was to streamline the financial statements and improve accessibility to the user and this has resulted in changes to the 2016/17 Code of Practice. The changes affect the presentation of income and expenditure in the financial statements and associated disclosure notes. A prior period adjustment (PPA) to restate the 2015/16 comparative figures is also required.

We have completed the following work in respect of this area:



- We have documented and evaluated the process for the recording the required financial reporting changes to the 2016/17 financial statements.
- We have reviewed the re-classification of the Comprehensive Income and Expenditure Statement (CIES) comparatives to ensure that they are in line with the Authority's internal reporting structure.
- We have reviewed the appropriateness of the revised grouping of entries within the Movement In Reserves Statement (MIRS).
- We have tested the classification of income and expenditure for 2016/17 recorded within the Cost of Services section of the CIES.
- We have tested the completeness of income and expenditure by reviewing the reconciliation of the CIES to the general ledger.
- We have tested the classification of income and expenditure reported within the new Expenditure and Funding Analysis (EFA) note to the financial statements.
- We have reviewed the new segmental reporting disclosures within the 2016/17 financial statements to ensure compliance with the CIPFA Code of Practice.

Assurance gained and issues arising:

- we identified that the Council had not included a new segmental reporting note, which they have added to the revised Accounts
- no other significant issues were identified from the work performed in respect of the risk identified

Accounting policies, estimates and judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Council's financial statements.

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	The Council's revenue recognition policy is disclosed within Note 1(ii) of the Accounts, within Accounting Policies, and covers each of the main areas of revenue received by the Council, including revenue received from the sale of goods, the provision of services along with how revenue is recognised for the non-exchange transactions such as Council Tax and Business Rates.	<p>Following the work performed we are satisfied that the Council's revenue recognition policies are in line with the requirements of the CIPFA Code.</p> <p>Our testing of your various revenue sources did not identify any instances of inappropriate revenue recognition.</p>	 Green
Judgements and estimates	<p>Key estimates and judgements include:</p> <ul style="list-style-type: none"> – Useful life of Property, plant and equipment – Revaluations – Impairments – Accruals – Valuation of pension fund net liability – Provision for Business Rate appeals – Other provisions 	<p>Following our consideration of these judgements we are satisfied they are in line with the Code of Practice, and with the approach taken by the Council in the previous year.</p> <ul style="list-style-type: none"> • We did not identify any issues with the items relating to property, plant and equipment, such as the calculation of depreciation, the asset lives applied, or the revaluations applied by the Council during the course of the year. • We confirmed the pension fund valuations were consistent with the reports received from the Fund's Actuary, Hymans Robertson. Our use of an expert, PwC, to assess the work performed by the Actuary did not identify any issues either. • Our work on the Business Rate Provision identified a considerable increase in provision from the previous year, which was largely due to the outcome of a recent court case in respect of tenants who occupy multiple floors in the same building. We reviewed the Council's approach and assumptions around this area and are comfortable with the revised provision included in this year's Accounts. 	 Green



Assessment

● - Red - Marginal accounting policy which could potentially attract attention from regulators



● - Green - Accounting policy appropriate and disclosures sufficient

● - Amber - Accounting policy appropriate but scope for improved disclosure

Accounting policies, estimates and judgements (continued)

Accounting area	Summary of policy	Comments	Assessment
Going concern	The Strategic Director of Finance and Governance, who is the s151 officer, has a reasonable expectation that the services provided by the Council will continue for the foreseeable future. Members concur with this view. For this reason, the Council continue to adopt the going concern basis in preparing the financial statements.	We have reviewed the Council's assessment and are satisfied with management's assessment that the going concern basis is appropriate for the 2016/17 financial statements.	 Green
Other accounting policies		We have reviewed the Council's policies against the requirements of the CIPFA Code of Practice. The Council's accounting policies are appropriate and consistent with previous years.	 Green

Assessment

 - **Red** - Marginal accounting policy which could potentially attract attention from regulators
 - **Green** - Accounting policy appropriate and disclosures sufficient

 - **Amber** - Accounting policy appropriate but scope for improved disclosure

Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

	Issue	Commentary
1.	Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with the Audit, Governance and Standards Committee. We have not been made aware of any other incidents in the period and no other issues have been identified during the course of our audit procedures.
2.	Matters in relation to related parties	<ul style="list-style-type: none"> From the work we carried out, we have not identified any related party transactions which have not been disclosed.
3.	Matters in relation to laws and regulations	<ul style="list-style-type: none"> You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
4.	Written representations	<ul style="list-style-type: none"> A standard letter of representation has been requested from the Council, which is included in the Audit, Governance and Standards Committee papers for this meeting.
5.	Confirmation requests from third parties	<ul style="list-style-type: none"> We requested from management permission to send confirmation requests to all of the Council's counter parties. This permission was granted and the requests were sent. All of these requests were returned with positive confirmation. We requested management to send letters to those solicitors who worked with the Council during the year. All responses have been received and no issues have been identified.
6.	Disclosures	<ul style="list-style-type: none"> Our review identified a number of disclosures which required amendment or expansion, and management agreed to amend all of the items identified. Further detail is provided within the Misclassifications and disclosure changes page, which is included later in the Report.
7.	Matters on which we report by exception	<ul style="list-style-type: none"> We are required to report on a number of matters by exception in a number of areas: We have not identified any issues we would be required to report by exception in the following areas If the Annual Governance Statement does not meet the disclosure requirements set out in the CIPFA/SOLACE guidance or is misleading or inconsistent with the information of which we are aware from our audit The information in the Narrative Report is materially inconsistent with the information in the audited financial statements or our knowledge of the Group/Council acquired in the course of performing our audit, or otherwise misleading.
8.	Specified procedures for Whole of Government Accounts	<p>We are required to carry out specified procedures (on behalf of the NAO) on the Whole of Government Accounts (WGA) consolidation pack under WGA group audit instructions.</p> <p>As the Council exceeds the specified group reporting threshold we examine and report on the consistency of the WGA consolidation pack with the Council's audited financial statements.</p> <ul style="list-style-type: none"> Note that work is not yet completed, and will be completed towards the end of September 2017, which is in line with the deadline for this work.

Internal controls – review of issues raised in prior year

	Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
1.	✓	<p>In 2014/15, we raised a recommendation for the Council to ensure that it performs a reconciliation of the asset register to the valuation reports before producing the accounts.</p> <p>Our review of progress made in 2015/16 identified that reconciliations had been performed for both dwellings and high value assets, but no reconciliation had been performed for investment properties, and thus this recommendation was carried forward to 2016/17.</p>	Our work in this area has identified has confirmed that the Council has provided reconciliations for all of the relevant areas, including Investment Properties, and therefore we are satisfied this issue has been resolved.
2.	✓	<p>As part of our audit testing in 2015/16 we picked a sample of employees which we attempted to trace back to contracts to evidence their employment at the Council. Of the sample of 40 contracts, we were unable to obtain 14, requiring alternative confirmation to be sought. In each of these cases, the Council was unable to access copies of these contracts that had been scanned and saved by Capita.</p> <p>Thus we recommended that the Council should ensure that a system is in place to enable access to scanned copies of all contracts.</p>	It is clear that progress has been made in this area, with HR able to provide contracts for all permanent members of staff selected for testing. However they were unable to provide a letter of engagement for one casual member of staff, as per the previous page, for which we have raised a separate recommendation. However we are satisfied that the issue around contracts for permanent members of staff has been resolved.

Assessment

- ✓ Action completed
- X Not yet addressed

"The purpose of an audit is for the auditor to express an opinion on the financial statements. Our audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters being reported are limited to those deficiencies that the auditor has identified during the audit and that the auditor has concluded are of sufficient importance to merit being reported to those charged with governance." (ISA (UK&I) 265)

Adjusted misstatements

No adjusted misstatements have been identified from the work performed to date.

Unadjusted misstatements

The table below provides details of adjustments identified during the audit which have not been made within the final set of financial statements. The Audit, Governance and Standards Committee is required to approve management's proposed treatment of all items recorded within the table below:

Detail	Comprehensive Income and Expenditure Statement £'000	Balance Sheet £'000	Reason for not adjusting
1 During our testing of Investment Properties, we identified one property with a total value of £1.96m which had been disposed of during the course of the year which was still included within the Accounts at year end. This property should have been removed from the Balance Sheet, along with the balance held in the Revaluation Reserve in respect of this property.	Dr Gain/Loss on Disposal 1,960	Cr Investment Property 1,960	The Council have not adjusted for this misstatement as it is immaterial to the overall financial statements, as well as the complexity of ensuring all the related PPE amendments are processed correctly.
	Cr MIRS 1,960	Dr Capital Adjustment Account 1,960	
		Dr Capital Adjustment Account 153	
		Cr Revaluation Reserve 153	
Overall impact	£1,960	£1,960	

Misclassifications and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Adjustment type	Value £'000	Account balance	Impact on the financial statements
1 Misclassification	Various	Note 17 – Provisions (Long Term)	We identified that the values for the Thames Water and Business Rate Appeals had been entered the wrong way round within the Note, and have now been amended to show the correct values, which is £3,449k for Thames Water and £1,436k for Business Rate Appeals.
2 Disclosure	Various	Notes 20 and 21 – Cash Flow Statement	We identified that the amounts shown in respect of the Purchase of PPE, Investment Property and Intangibles, and Cash Payments in respect of PFI Liabilities were incorrect. These have been subsequently amended in the revised Cash Flow Statement.
3 Disclosure	Various	Note 22 – Note to the Expenditure and Funding Analysis	We identified that the draft Accounts did not include a disclosure meeting the requirements under IFRS8 in respect of Segmental Reporting, which the Council has now added to the Accounts.
4 Disclosure	Various	Note 26 – Audit Fees	Our work identified that the Council had omitted the £23k fee in relation to our work on the Housing Benefit Certification, which has now been included within the revised note.
5 Disclosure	Various	Note 29 – Related Party Transactions	We identified a discrepancy in the prior year comparators for Voluntary or Charitable Bodies, along with expenses incurred in administering the Pension Fund. Both of these have been amended within the revised Accounts.
6 Disclosure	Various	Various Notes	Various minor disclosure amendments were made to improve the transparency of the disclosures in the Accounts.

Section 3: Value for Money

01. Executive summary

02. Audit findings

03. Value for Money

04. Fees, non-audit services and independence

05. Communication of audit matters

Background

We are required by section 21 of the Local Audit and Accountability Act 2014 ('the Act') and the NAO Code of Audit Practice ('the Code') to satisfy ourselves that the Council has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is known as the Value for Money (VFM) conclusion.

We are required to carry out sufficient work to satisfy ourselves that proper arrangements are in place at the Council. The Act and NAO guidance state that for local government bodies, auditors are required to give a conclusion on whether the Council has put proper arrangements in place.

In carrying out this work, we are required to follow the NAO's Auditor Guidance Note 3 (AGN 03) issued in November 2016. AGN 03 identifies one single criterion for auditors to evaluate:

In all significant respects, the audited body takes properly informed decisions and deploys resources to achieve planned and sustainable outcomes for taxpayers and local people.

AGN03 provides examples of proper arrangements against three sub-criteria but specifically states that these are not separate criteria for assessment purposes and that auditors are not required to reach a distinct judgement against each of these.

Risk assessment

We carried out an initial risk assessment in January 2017 and identified one significant risk in respect of specific areas of proper arrangements using the guidance contained in AGN03. We communicated this risk to you in our Audit Plan dated February 2017.

We have continued our review of relevant documents up to the date of giving our report, and have not identified any further significant risks where we need to perform further work.

We carried out further work only in respect of the significant risks we identified from our initial and ongoing risk assessment. Where our consideration of the significant risks determined that arrangements were not operating effectively, we have used the examples of proper arrangements from AGN 03 to explain the gaps in proper arrangements that we have reported in our VFM conclusion.

Significant qualitative aspects

AGN 03 requires us to disclose our views on significant qualitative aspects of the Council's arrangements for delivering economy, efficiency and effectiveness.

We have focused our work on the significant risks that we identified in the Council's arrangements. In arriving at our conclusion, our main considerations were:

- The Council faced considerable financial challenges during the course of 2016-17, having to use **£26.7m** of Reserves to achieve a balanced position at year end. A considerable proportion of these Reserves were used to offset overspends in Children's and Adult Social Care, where the Council overspent its original budget by **£25.5m**, which equates to 14.9% of its budget of **£171.5m**.
- A balanced budget has been set for 2017-18, which includes a considerable allowance for growth in the spend on Social Care, as the Council looks to get the spending in this area under control. The requirement for further savings and income generation schemes in year is **£26.4m**, which was fully identified at the start of the year.
- Longer term, the Council's current Medium Term Financial Plan covers the period up to 2018-19. This is due to the uncertainty around the revised Local Government Funding Settlement, which is due to be implemented in 2020.

We have set out more detail on the risks we identified, the results of the work we performed and the conclusions we drew from this work on the following page.

Overall conclusion

Based on the work we performed to address the significant risks, we concluded that:

- the Council had proper arrangements in all significant respects to ensure it delivered value for money in its use of resources.

The text of our report, which confirms this can be found at Appendix B.

Recommendations for improvement

We discussed findings arising from our work with management and have agreed one recommendation for improvement as follows.

- There is a need for the Council to continue to work to understand the causes of the overspends in Social Care to ensure the Council in a sustainable position ahead of the revised Local Government Funding Settlement in 2020.

Management's response to this can be found in the Action Plan at Appendix A.

Significant difficulties in undertaking our work

We did not identify any significant difficulties in undertaking our work on your arrangements which we wish to draw to your attention.

Significant matters discussed with management

There were no matters where no other evidence was available or matters of such significance to our conclusion or that we required written representation from management or those charged with governance.

Any other matters

There were no other matters from our work which were significant to our consideration of your arrangements to secure value for money in your use of resources.

Key findings

We set out below our key findings against the significant risks we identified through our initial risk assessment and further risks identified through our ongoing review of documents.

Significant risk	Work to address	Findings and conclusions
<p>Financial Performance</p> <p>The Council is facing significant financial pressures, particularly in relation to Social Care Budgets. We will consider the arrangements that are being put in place to secure a sustainable financial future for the Council.</p>	<p>We performed the following work in this area:</p> <ul style="list-style-type: none"> • review the 2016-17 Outturn, including details of performance against both the Revenue and Capital Budgets; • review progress against the 2017-18 financial plan up to the completion of our audit; and • obtain an update on the Council's Medium Term Financial Strategy, including progress on identifying the savings required in coming years including discussions with Management on progress to date. 	<p>The key points from our work in this area are as follows:</p> <ul style="list-style-type: none"> • The Council delivered a balanced General Fund position at the end of 2016-17, however this relied on the use of £27.4m of Reserves, which the Council is clear is not going to be sustainable given their current position and the pressures on Local Government financing going forward. • In terms of the reasons behind this large demand on Reserves during 2016-17, the main area of concern was Children's and Adult Social Care, which overspent its budget by £14.887m, which was after the use of £11.45m of Reserves, which in effect means these services were overspent by £26.3m, which equates to 15.36% of the original budget of £171.5m. This is on top of the £18.7m budget pressure which the Council had to manage in 2015-16, so it is clear this service is generating a significant pressure on the overall financial position of the Council. • Given the challenges which have been faced in this area over recent years, the Council has taken action by engaging RSM Tenon to undertake a review of the arrangements in place. They have also set up a Budget Recovery Board, which meets on a fortnightly basis to monitor the progress against budget in this area closely to ensure in-year overspends are identified and dealt with in a timely manner. • Other areas which were a challenge for the Council during the course of 2016-17 include the number of cases picked up under the Nil Recourse to Public Funds, which has come in over £3.7m above Budget. ICT Modernisation was another area which had a negative impact on the overall financial position, with £1.4m of exceptional costs (after drawdown) occurring across this area and Facilities Management, which have been long standing issues for the Council, which are likely to remain the case over the short term. • A balanced budget has been set for 2017-18, delivery of which will require savings and income generation schemes totalling £26.4m to be achieved during the course of the year. All of these schemes were identified in advance of 2017-18, set across all of the Council's Departments. We have reviewed the assumptions underlying this budget and are satisfied that they are reasonable given the Council's circumstances. These assumptions include a 4.99% increase in Council Tax in 2017-18, including the Adult Social Care Precept, along with allowances for increases in pay and other areas such as contracts. • As part of the 2017-18 Budget, the Council is allowing for a further £13m increase in spending on Social Care, which seems appropriate given the challenges which have been faced over the past two years. However this will need careful monitoring and management to ensure that these increases do not slip and have an impact on the savings plans which the Council has already identified. • Looking longer term, the Council's latest Medium Term Financial Plan covers the period up to 2018/19, which is largely due to the level of uncertainty around Local Government financing post-2020, which is when the new Local Government funding settlement is going to be implemented. At the moment the Council is struggling to come up with plans post this period, and thus they will need to monitor progress closely as 2020 gets closer to ensure they are well placed to react to the revised plans. <p>Overall, it is clear that the Council needs to ensure its Social Care spending is under control to ensure it is a strong position ahead of the challenges that 2020 is likely to bring for all Local Authorities. Whilst steps have been taken, it is clear there is still more for the Council to do in this area to have this completely under control.</p>

Section 4: Fees, non-audit services and independence

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05. Communication of audit matters

We confirm below our final fees charged for the audit and provision of non-audit services.

Fees

	Proposed fee £	Final fee £
Council audit	237,296	237,296
Grant certification	23,018	TBC
Total audit fees (excluding VAT)	260,314	TBC

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA)

Grant certification

Our fees for grant certification cover only housing benefit subsidy certification, which falls under the remit of Public Sector Audit Appointments Limited. Fees in respect of other grant work, such as reasonable assurance reports, would be shown under 'Fees for other services', but there are no items of this type to be considered in 2016-17.

Our final fee for this work will only be confirmed once we have completed all of the work required by this certification, which will be completed by the end of November 2017, which is the national deadline for the completion of this work.

Independence and ethics

- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and confirm that we are independent and are able to express an objective opinion on the financial statements.
- We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.
- For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council. The table below summarises all other services which were identified.

Fees for other services

Service	Fees £
Audit related services:	
• Teachers' Pensions Certification	4,500
• Pooling of Housing Capital Receipt Certification	4,500
Non-audit services:	
• Financial Resilience – Capacity Building Programme	3,500
• Cost Assurance	43,959
• CFO Insights Subscription	10,000

Independence and other services

We have considered whether other services might be perceived as a threat to our independence as the Council's auditor and have ensured that appropriate safeguards are put in place.

	Service provided to Southwark Council	Fees (£)	Threat?	Safeguard
Audit related services	Teachers' Pensions Certification	4,500	No	Fee is low in comparison to the Council's audit fee. A separate independent engagement is performed and a report will be given in line with a separate engagement letter.
	Pooling of Housing Capital Receipt Certification	4,500	No	Fee is low in comparison to the Council's audit fee. A separate independent engagement is performed and a report will be given in line with a separate engagement letter.
Non-audit services	Financial Resilience – Capacity Building Programme	3,500	No	Fee is low in comparison to the Council's audit fee. This work is merely training delivered to the Council's finance team by Grant Thornton colleagues who are not involved in the external audit of the Council.
	Cost Assurance	43,959	No	Whilst this fee is significant, this work is performed by a separate engagement team who are completely independent from the external audit team to reduce the risk.
	CFO Insights Subscription	10,000	No	Fee is low in comparison to the Council's audit fee. This work entails us providing the Council with information about the Council's position in relation to its peers and has no impact on the Council's financial statements or our audit.
	TOTAL	66,459		

The above non-audit services are consistent with the Council's policy on the allotment of non-audit work to your auditor.

Section 5: Communication of audit matters

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05. Communication of audit matters

Communication to those charged with governance

ISA (UK&I) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

This document, The Audit Findings, outlines those key issues and other matters arising from the audit, which we consider should be communicated in writing rather than orally, together with an explanation as to how these have been resolved.

Respective responsibilities

The Audit Findings Report has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by Public Sector Audit Appointments Limited (<http://www.psa.co.uk/appointing-auditors/terms-of-appointment/>)

We have been appointed as the Council's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England at the time of our appointment. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice ('the Code') issued by the NAO (<https://www.nao.org.uk/code-audit-practice/about-code/>). Our work considers the Council's key risks when reaching our conclusions under the Code.

It is the responsibility of the Council to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Council is fulfilling these responsibilities.

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	✓	
Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications	✓	
Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought		✓
Confirmation of independence and objectivity	✓	✓
A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged Details of safeguards applied to threats to independence	✓	✓
Material weaknesses in internal control identified during the audit		✓
Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements		✓
Non compliance with laws and regulations		✓
Expected modifications to auditor's report, or emphasis of matter		✓
Unadjusted misstatements and material disclosure omissions		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern	✓	✓

Appendices

- A. Action Plan
- B. Audit Opinion

Appendix A: Action plan

Priority

Rec no.	Recommendation	Priority	Management response	Implementation date and responsibility
1.	HR – Casual Workers The Council needs to ensure sufficient documentation is in place to confirm the employment status of casual workers employed during the course of the year.	Medium		
2	Value for Money – Social Care The Council needs to continue to work to understand the issues causing the overspends in Social Care to ensure the Council is in a sustainable financial position ahead of the revised Local Government Funding Settlement being announced in 2020.	Medium		

Controls

- High – Significant effect on control system
- Medium – Effect on control system
- Low – Best practice

Appendix B: Audit opinion

We anticipate we will provide the Council with an unmodified audit report

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF SOUTHWARK COUNCIL

We have audited the financial statements of Southwark Council (the "Authority") for the year ended 31 March 2017 under the Local Audit and Accountability Act 2014 (the "Act"). The financial statements comprise the Comprehensive Income and Expenditure Statement, the Movement in Reserves Statement, the Balance Sheet, the Cash Flow Statement, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement, the Collection Fund and the related notes. 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 the Authority, as a body, in accordance with Part 5 of the Act and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the Authority's members those matters we are required to state to them in an auditor's 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 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 Strategic Director of Finance and Governance and auditor

As explained more fully in the Statement of Responsibilities, the Strategic Director of Finance and Governance 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, which give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law, the Code of Audit Practice published by the National Audit Office on behalf of the Comptroller and Auditor General (the "Code of Audit Practice") 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's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Strategic Director of Finance and Governance; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Narrative Report and the Annual Governance Statement to 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 present a true and fair view of the financial position of the Authority as at 31 March 2017 and of its expenditure and income for the year then ended; and
- the financial statements have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 and applicable law.

Opinion on other matters

In our opinion, the other information published together with the audited financial statements in the Narrative Report and the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the audited financial statements.

Appendix B: Audit opinion (continued)

We anticipate we will provide the Council with an unmodified audit report

Matters on which we are required to report by exception

We are required to report to you if:

- in our opinion the Annual Governance Statement does not comply with the guidance included in 'Delivering Good Governance in Local Government: Framework (2016)' published by CIPFA and SOLACE; or
- we have reported a matter in the public interest under section 24 of the Act in the course of, or at the conclusion of the audit; or
- we have made a written recommendation to the Authority under section 24 of the Act in the course of, or at the conclusion of the audit; or
- we have exercised any other special powers of the auditor under the Act.

We have nothing to report in respect of the above matters.

Conclusion on the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources

Respective responsibilities of the Authority and auditor

The Authority is responsible for putting in place proper arrangements for securing 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.

We are required under Section 20(1)(c) of the Act to be satisfied that the Authority has made 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 the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria issued by the Comptroller and Auditor General in November 2016, as to whether the Authority 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 criteria as that necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether the Authority 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 the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of our work, having regard to the guidance on the specified criteria issued by the Comptroller and Auditor General in November 2016, we are satisfied that in all significant respects *the Authority* put in place proper arrangements for securing 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 in accordance with the requirements of the Act and the Code of Audit Practice until we have completed the work necessary to issue our Whole of Government Accounts (WGA) Component Assurance statement for the Authority for the year ended 31 March 2017. We are satisfied that this work does not have a material effect on the financial statements or on our conclusion on the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2017.

Paul Dossett
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

30 Finsbury Square
London
EC2Y 2YU

xx September 2017



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