

Central Bedfordshire Council

Annual Audit Letter for the year
ended 31 March 2018

August 2018

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Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and 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 23 February 2017)' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure - If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.



01

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Central Bedfordshire Council ['the Council'] following completion of our audit procedures for the year ended 31 March 2018. Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's:	Unqualified - the financial statements give a true and fair view of the financial position of the Council as at 31 March 2018 and of its expenditure and income for the year then ended
▶ Financial statements	
▶ Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts.
Concluding on the body's arrangements for securing economy, efficiency and effectiveness	We concluded that you have put in place proper arrangements to secure value for money in your use of resources

Area of Work	Conclusion
Reports by exception:	
▶ Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council.
▶ Public interest report	We had no matters to report in the public interest.
▶ Written recommendations to the Council which should be copied to the Secretary of State	We had no matters to report.
▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.

Area of Work	Conclusion
Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	We had no matters to report.



Executive Summary (cont'd)

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 24 July 2018.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	We have not as yet issued our audit completion certificate. 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 Council'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.

In December 2018 we will also issue a report to those charged with governance of the Council summarising the certification work we have undertaken.
We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Neil Harris
Associate Partner
For and on behalf of Ernst & Young LLP



02 Purpose and Responsibilities

Purpose and Responsibilities

The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2017/18 Audit Results Report to the 30 July 2018 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

Responsibilities of the Appointed Auditor

Our 2017/18 audit work has been undertaken in accordance with the Audit Plan that we presented at the 8 January 2018 Audit Committee meeting, as updated in the Audit Progress report presented at the 9 April Audit Committee, and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
 - ▶ On the 2017/18 financial statements, and
 - ▶ On the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
 - ▶ If the annual governance statement is misleading or not consistent with our understanding of the Council;
 - ▶ Any significant matters that are in the public interest;
 - ▶ Any written recommendations to the Council, which should be copied to the Secretary of State; and
 - ▶ If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the NAO. We have yet to issue our assurance statement in respect of the Council's Whole of Government Accounts consolidation pack.

Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement. In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.



03

Financial Statement Audit

Financial Statement Audit

Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 30 July 2018.

Our detailed findings were reported to the 30 July Audit Committee.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
Misstatements due to fraud or error The financial statements as a whole are not free of material misstatements whether caused by fraud or error. As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.	<p>We considered generic risk factors that could indicate how specific risks of management override manifests itself at the Council, such as the financial position and historic performance against budget. We have also considered the specific additional risks of management override as they relate to local government accounts. Based on our consideration of the key areas susceptible to management override we have concluded that the area that management have the greatest opportunity to override controls is within the following areas:</p> <ul style="list-style-type: none">• non system accruals where judgements and estimates are made• inappropriate capitalisation of revenue expenditure• Revenue items incorrectly identified as revenue expenditure funding by capital under statute (REFCUS) thus inappropriately funded from capital <p>In addition to the specific audit work above, we performed specific procedures including:</p> <ul style="list-style-type: none">• Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements• Assessing accounting estimates for evidence of management bias, and• Evaluating the business rationale for significant unusual transactions. <p>Based on our completed audit procedures:</p> <ul style="list-style-type: none">• We did not identify any evidence of material management override.• We did not identify any instances of inappropriate judgements being applied.• We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business <p>Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Council's financial position.</p>

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Risk of fraud in revenue and expenditure recognition Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the 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 the manipulation of expenditure recognition. This risk is focused around those items of income and expenditure which are non-routine and involve more management estimation and judgment such as year-end income and expenditure accruals and provisions	<p>We carefully considered the revenue and expenditure streams of the Council and considered each against the risk of fraud in revenue and expenditure recognition.</p> <p>We concluded that the risk of material misstatement arising from inappropriate revenue and expenditure recognition manifests itself in 'other service expenses'. Expenditure of £349 million was reported under this heading in 2017/18. It comprises a range of transactions, for example supplies and services and payments to contractors for services such as refuse collection but also items that are individually small and subject to individual invoice arrangements on a short term credit basis. Given the range of transactions included, we have concluded that there is a potential risk of manipulation in terms of recognition of expenditure and have tailored our audit testing to address this risk.</p> <p>To address this risk, we:</p> <ul style="list-style-type: none">• Disaggregated 'other service expenses' into material expenditure streams and obtained an understanding of the streams to direct testing.• Increased our testing of expenditure through to underlying documentation for reasonableness and business purpose.• Tested the completeness and valuation of expenditure accruals, to gain assurance that there have been no material amounts of expenditure omitted from the financial statements.• Tested expenditure cut-off through our unrecorded liabilities testing to gain assurance that there has been no material amounts of expenditure omitted from the financial statements and that expenditure has been accounted for in the correct period.• Completed our journal entry testing within specific parameters to focus this testing on key risk area. <p>Our testing has not identified any material misstatements from revenue and expenditure recognition.</p> <p>Overall our audit work did not identify any material issues or unusual transactions to indicate any misreporting of the Council's financial position.</p>

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Pension liability valuation The Council's current pension fund deficit is a highly material and sensitive item and the Code requires that this liability be disclosed on the Council's balance sheet. The information disclosed is based on the IAS 19 report issued to the Council by the actuary. As with other councils, accounting for this scheme involves significant estimation and judgement and due to the nature, volume and size of the transactions we consider this to be a higher inherent risk.	<p>In our Audit Planning Report, we designated the pension liability valuation as an 'other area of audit focus'. However, following a consideration of the complexity and range of assumptions that contribute to the pensions liability, and the material nature of the sums involved, we have increased this to a significant risk.</p> <p>We focused on aspects of the pension liability which could have a material impact on the financial statements, primarily:</p> <ul style="list-style-type: none">• significant changes in assumptions made by the actuary; and• the assessments of the actuary undertaken by PWC and the EY actuarial team. <p>To address this risk, we:</p> <ul style="list-style-type: none">• Liaised with the auditors of the Bedfordshire Pension Fund to obtain assurances over the information supplied to the actuary in relation to Central Bedfordshire Council;• Assessed the work of the Pension Fund actuary, Hymans Robertson, including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by NAO for all Local Government sector auditors, and considering the review of this work undertaken by the EY actuarial team; and• Reviewed and tested the accounting entries and disclosures made within the Council's financial statements in relation to IAS19. <p>In calculating the scheme assets as at 31 March 2018, the actuary performs a roll forward technique based on asset data submitted to the by the Pension Fund at 31 December 2017.</p> <p>The reporting from the pension fund auditors highlighted a difference between the market value of the pension fund assets at 31 March 2018 which when apportioned to Central Bedfordshire Council indicates a difference in a range up to £6.6 million for the Council.</p> <p>Due to the size of the difference, we did not seek an adjustment to the account but reported this as an unadjusted misstatement and asked for a representation from management to be included in their letter of representation.</p> <p>There are no other findings from our work.</p>

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Other Key Findings	Conclusion
<p>Property, Plant and Equipment</p> <p>Property, plant and equipment (PPE) represents a significant balance in the Council's accounts and are subject to valuation changes, impairment reviews and/or depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end PPE balances held in the balance sheet.</p> <p>As the Council's asset base is significant, and the outputs from the valuer are subject to estimation, there is a higher inherent risk PPE may be under/overstated or the associated accounting entries incorrectly posted.</p>	<p>We designed audit procedures to address this key area of audit focus, including considering the work of the valuer and challenging the assumptions used comparing, where possible, to observable data.</p> <p>We had no matters to report.</p>
<p>Earlier deadline for production and audit of the financial statements from 2017/18</p> <p>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.</p> <p>These changes provide challenges for both the preparers and the auditors of the financial statements.</p>	<p>The Council has been well placed to meet the demands of the earlier deadline, having produced their financial statements in line with the statutory deadline in previous years.</p> <p>There are areas where the Council can look to improve its arrangements to ensure the audit is completed in a shorter timeframe:</p> <ul style="list-style-type: none">- Identifying additional areas for early substantive testing prior to the final audit visit;- Reviewing how some working papers are presented for audit to facilitate a more efficient execution of audit procedures; and- Reviewing how the team is used to respond to queries so that query response times can be improved.

Financial Statement Audit (cont'd)

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	<p>We determined planning materiality to be £12mn (2017: £11.7mn), which is 75% of gross revenue expenditure reported in the accounts.</p> <p>We consider gross revenue expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p>
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £0.6mn (2017: £0.558mn)

We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include:

- ▶ Remuneration disclosures including any severance payments, exit packages and termination benefits
- ▶ Related party transactions.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

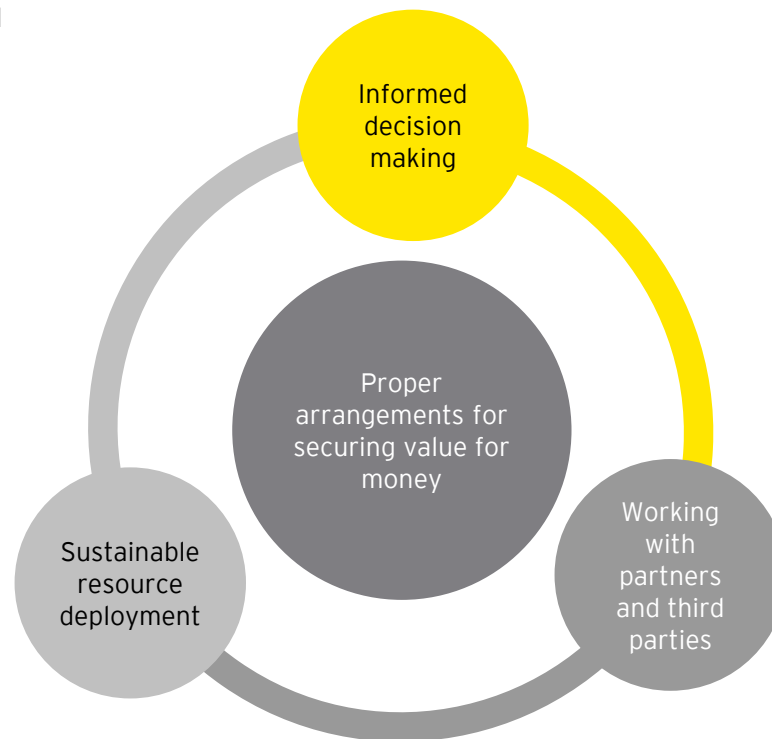


04 Value for Money

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its 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.



We did not identify any significant risks in relation to these criteria. We issued an unqualified value for money conclusion on 30 July 2018



05

Other Reporting Issues



Other Reporting Issues

Whole of Government Accounts

We have not yet completed the work necessary to issue our assurance statement in respect of the Council'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.

Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern.

Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.



Other Reporting Issues (cont'd)

Objections Received

We did not receive any objections to the 2017/18 financial statements from members of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 30 July 2018. 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 regulatory and professional requirements.

Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. 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 identified during our audit.

We have adopted a fully substantive approach and have therefore not tested the operation of controls.



06

Focused on your future



Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below.

Standard	Issue	Impact
IFRS 9 Financial Instruments	<p>Applicable for local authority accounts from the 2018/19 financial year and will change:</p> <ul style="list-style-type: none"> ▶ How financial assets are classified and measured; ▶ How the impairment of financial assets are calculated; and ▶ The disclosure requirements for financial assets. <p>There are transitional arrangements within the standard and the 2018/19 Accounting Code of Practice for Local Authorities has now been issued, providing guidance on the application of IFRS 9. In advance of the Guidance Notes being issued, CIPFA have issued some provisional information providing detail on the impact on local authority accounting of IFRS 9, however the key outstanding issue is whether any accounting statutory overrides will be introduced to mitigate any impact.</p>	<p>Although the Code has now been issued, providing guidance on the application of the standard, along with other provisional information issued by CIPFA on the approach to adopting IFRS 9, until the Guidance Notes are issued and any statutory overrides are confirmed there remains some uncertainty. However, what is clear is that the Council will have to:</p> <ul style="list-style-type: none"> ▶ Reclassify existing financial instrument assets ▶ Re-measure and recalculate potential impairments of those assets; and ▶ Prepare additional disclosure notes for material items.
IFRS 15 Revenue from Contracts with Customers	<p>Applicable for local authority accounts from the 2018/19 financial year. This new standard deals with accounting for all contracts with customers except:</p> <ul style="list-style-type: none"> ▶ Leases; ▶ Financial instruments; ▶ Insurance contracts; and ▶ For local authorities; Council Tax and NDR income. <p>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.</p> <p>Now that the 2018/19 Accounting Code of Practice for Local Authorities has been issued it is becoming clear what the impact on local authority accounting will be. As the vast majority of revenue streams of Local Authorities fall outside the scope of IFRS 15, the impact of this standard is likely to be limited.</p>	<p>As with IFRS 9, some provisional information on the approach to adopting IFRS 15 has been issued by CIPFA in advance of the Guidance Notes. Now that the Code has been issued, initial views have been confirmed; that due to the revenue streams of Local Authorities the impact of this standard is likely to be limited.</p> <p>The standard is far more likely to impact on Local Authority Trading Companies who will have material revenue streams arising from contracts with customers. Where appropriate, the Council will need to consider the impact of this on their own group accounts when that trading company is consolidated.</p>



Focused on your future (cont'd)

Standard	Issue	Impact
IFRS 16 Leases	<p>It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard and although the 2019/20 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.</p>	<p>Until the 2019/20 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.</p>

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