External Audit Report 2016/17

Spelthorne Borough Council

Year ended 31 March 2017

17 October 2017

Content

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

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Jo Lees, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers (0207 694 8981, andrew.sayers@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3H.

Important notice

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

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

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

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

Status of our audit: Our audit is not yet complete and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status of our audit at the Audit Committee meeting. The following work is ongoing:

— Financial statements audit:

- NDR balances testing;
- Accounting treatment of sale and leaseback transaction;
- Review of journals created since draft accounts produced;
- Whole of Government Accounts (WGA) audit;
- Casting and consistency check of latest Authority provided financial statements;
- Any subsequent finalisation points from Audit Manager and Director review; and
- Signed management representation letter.

— Value for money conclusion:

- Our work in this area is still ongoing.

Summary

Financial statements audit – see section 2 for further details

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

- There are no unadjusted audit differences, explained in section 2 and appendix 3.
- There are 12 adjusted audit differences. These are shown in appendix 3.
- We agreed presentational changes to the accounts with Finance, mainly related to compliance with the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.
- In additional to our routine requests we are asking for specific management representations, which are explained in section 2.
- We will report that your AGS complies with delivering Good Governance guidance issued by CIPFA / SOLACE in April 2016.
- We reviewed the Narrative Report and suggested a number of presentational amendments.
- We did not receive any queries or objections from local electors this year.

Value for money – see section 3 for further details

Our VFM audit work is still ongoing.

Summary

Other matters

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

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

The draft accounts published by the Authority on 17 July 2017 had not been adequately prepared or reviewed by an appropriate member of the Authority's finance team.

Due to staff turnover, both of the accounts preparers were both new joiners and did not have historical knowledge of the Authority's systems or operations in preparing the accounts. In addition, Furthermore there was limited evidence of independent review of the accounts by a senior member of the team before they were presented for audit.. Significant personnel changes have occurred across the Authority's financial team with further changes anticipated. As a result, there is increased risk around succession planning, retaining corporate memory and maintaining business as usual at the Authority.

In addition, during our testing of journals we identified issues relating to the way some transactions were processed and evidenced during the financial year 2016/17.

We have raised three high (red) priority recommendations in relation to the issues described above. We have made a total of five new recommendations as a result of our 2016/17 work. We also identified two prior year recommendations that require further action by Management. All recommendations are shown in appendix 1.

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

- Housing benefits certification: work is expected to be performed and completed in October and November 2017.

The fee for this work is explained in section 2 and appendix 4.

Financial statements audit

We audit your financial statements by undertaking the following:

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

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

1. Business understanding	In our 2016/17 audit plan we assessed your operations to identify significant issues that might have a financial statements consequence. We confirmed this risk assessment as part of our audit work. We provide an update on each of the risks identified later in this section.
2. Assessment of the control environment	We assessed the effectiveness of your key financial system controls that prevent and detect material fraud and error. We found weaknesses in financial controls on which we seek to place reliance, such as in the segregation of duties required for inputting and approving journal entries; suitable review of the draft financial statements prior to presentation for audit; and ensuring resilience within the Authority's finance team following staff changes. We have made three high priority recommendations relating to these issues. We have also raised two medium priority recommendations in relation to the external surveyor's valuation work and ensuring that the Authority has fixed asset registers in place with respect to IT equipment, intangible assets and heritage assets. We believe that these recommendations (see appendix 1) will strengthen your control environment. We reviewed work undertaken by your internal auditors, in accordance with ISA 610 and used the findings to inform our work.
3. Prepared by client request (PBC)	We produced the PBC to summarise the working papers and evidence we ask you to collate as part of the preparation of the financial statements. We discussed and tailored our request with the Interim Chief Accountant, and this was issued as a final document to the finance team. Due to delays in receiving information and significant staff turnover within the Authority's finance team we experienced difficulty in obtaining documentation to corroborate accounts balances and evidence for disclosures made. Audit trails and evidence for transactions were not consistently clear. As a result of these issues we were required to delay the start of our final onsite work on two occasions. We have raised a high priority recommendation in appendix 1 around the resilience of the finance team.

Financial statements audit

4. Accounting standards	We work with you to understand changes to accounting standards and other technical issues. For 2016/17 these changes related to: • Updates to the presentation of the Comprehensive Income and Expenditure Statement and the Movements in Reserves Statement and the introduction of the new Expenditure and Funding Analysis; and • Amended guidance on the Annual Governance Statement.
5. Accounts Production	We received draft accounts by 30 June 2017 in accordance with the deadline. Following initial review of the draft accounts, a number of amendments to figures and disclosure notes were required. Adjustments made by the Authority since the draft accounts were produced are shown at appendix 3. We have raised two high priority recommendations relating to: the financial accounts production and review; and to building resilience into the finance function to enable it to continue to operate effectively when staff leave the organisation. Management should consider these recommendations as a priority to ensure that the draft 2017/18 financial statements are completed to a sufficient level of quality. There is significant scope to improve the financial reporting process through putting in place additional reviews of reconciliations and finance working papers, particularly those that are new areas for the Authority and/or which involve key areas of judgement. This is of particular significance given the deadline for completion of the 2017/18 accounts audit has been brought forward to 31 July 2018. We will fully debrief with Finance to share views on the 2016/17 accounts audit in order to build in efficiencies for the 2017/18 audit process.
6. Testing	We have summarised the findings from our testing of significant risks and areas of judgement in the financial statements on the following pages. During the audit we identified presentational changes to the accounts along with audit adjustments which we have presented in appendix 3.
7. Representations	You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We will provide a draft of this representation letter to the Deputy Chief Executive. We draw attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking Management to provide specific representations on: • The accuracy of the balance sheet valuation as at 31 March 2017 of the pension liability due to the LGPS Triennial Valuation; • The accuracy of valuations as at 31 March 2017 attributed to Land and Buildings included within the financial statements; and • The completeness and accuracy of disclosures in relation to Knowle Green Estates Ltd, the Authority's subsidiary company set up in May 2016. We are not anticipating any furtheradditional areas of representation will be requested

Financial statements audit

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

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

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

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

- The results of the procedures we performed over changes to the pension liability, valuation of land and buildings and the sale and leaseback transaction with BP, which were identified as significant risks within our audit plan and which will form a part of our audit opinion;
- The results of our procedures to review the required risks of the fraudulent risk of revenue recognition and management override of control; and
- Our view of the level of prudence applied to key balances in the financial statements.

Financial statements audit

SIGNIFICANT audit risk	Account balances effected	Summary of findings
Significant changes in the pension liability due to LGPS Triennial Valuation	Net liability arising from defined benefit obligation: CY £34,768K, PY £44,129K	We agreed data provided by the Authority to the actuary, back to the relevant systems and reports from which it was derived. We also liaised with Grant Thornton, the auditors of the Pension Fund, where this data was provided by the Pension Fund on the Authority's behalf, to check the completeness and accuracy such data. No exceptions were identified.
Valuation of Land and Buildings	PPE: CY £46,346K, PY £44,960K	We reviewed the valuation methodology adopted by the Authority's valuer, to confirm that it is in accordance with RICS principles and the Authority's accounting policies for Property, Plant and Equipment and Investment Properties, and the valuation instructions provided. We reviewed the basis on which the valuation has been carried out to ensure it is in line with The Code of Practice on Local Authority Accounting in the United Kingdom 2016-17. We performed testing to ensure that revaluation gains and losses have been correctly reflected in the financial statements. We assessed the independence and objectivity of the surveyors and the terms under which they were engaged by Management. We undertook appropriate work to understand the basis upon which any impairments to land and buildings have been calculated. We engaged KPMG property experts to undertake an assessment of the revaluations carried out by the Authority's external valuers. Whilst we are satisfied that valuations included within the financial statements are unlikely to be materially misstated, we have identified some areas for improvement in this process at Appendix 1.
Sale leaseback arrangement with British Petroleum	Investment Properties: CY £392,145K, PY £215K Long term borrowing: CY £405,764K, PY £nil	The below work is ongoing: We vouched the value, transaction costs and date of the acquisition to sale and purchase agreements and bank statements. We inspected title deeds to assess whether the entity has legal title to the asset. We assessed the reasonableness of the valuation model used and the key assumptions applied, including the sensitivity of these assumptions. We confirmed that the accounting treatment is appropriate based on the entity's accounting policies and we reviewed the disclosures related to the sale leaseback agreement to ensure that they are in line with the Code.

Financial statements audit

Other areas of audit focus

We identified one other area of audit focus. This is not considered to be a significant risk as it is less likely to give rise to a material error. Nonetheless this is an area of importance where we carry out audit procedures to ensure that there is no material misstatement.

Other areas of audit focus	Summary of findings
Disclosures associated with retrospective restatement of CIES, EFA and MiRS	We assessed how the Authority has actioned the revised disclosure requirements for the CIES, MiRS and the new EFA statement as required by the Code. We validated the restated numbers and associated disclosures for accuracy, correct presentation and compliance with applicable Code guidance. No issues were identified as part of our work.

Financial statements audit

Risks that ISAs require us to assess in all cases	Why	Our findings from the audit
Fraud risk from revenue recognition	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. We do not consider this to be a significant risk for local authorities as there are limited incentives and opportunities to manipulate the way income is recognised. We therefore rebutted this risk in our External Audit Plan 2016/2017 and did not incorporate specific work in relation to this over and above our standard fraud procedures.	Since we have rebutted this presumed risk, there has been no impact on our audit work.
Fraud risk from management override of controls	Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk. In line with our methodology, we carry out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual. We have identified a risk of management override in relation to the processing of journal entries within the accounting system that is specific to this audit.	During our testing of journals we identified issues relating to the way some journal transactions were processed and evidenced during the financial year 2016/17. We identified instances where the segregation of duties control had failed and where evidence for transactions could not be provided. The Authority has concluded that it is not possible to recreate the evidence to support these journals. The individuals who processed and/or approved the journals have now left the Authority and have left no written record of why they were processed and the line descriptions are often inadequate. We have raised a high priority recommendation in relation to these issues in appendix 1.

Financial statements audit

Judgements in your financial statements

We consider the level of prudence in key judgements in your financial statements. We summarise our view below using the following scale:

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Provisions (excluding NDR)	3	4	£150k (PY:£69k)	We consider the provision disclosures to be balanced. The prior year rating of 4 was in relation to provisions in totality (including NDR).
NDR provisions	4	4	£1.6m (PY:£1.9m)	In 2013/14, local authority funding arrangements meant that the Authority is now responsible for a proportion of successful rateable value appeals. The Authority has provided for a fixed percentage of outstanding appeals in accounting for the potential liability, based on historical appeals success rates. The level of NDR provision has decreased from the prior year as more appeals become finalised. We consider the related disclosure to be proportionate, though slightly optimistic in line with the prior year.
Pension liability	3	3	£44.1m (PY:£34.8)	The pension liability has been assessed on an actuarial basis using the projected unit method, an estimate of the pensions that will be payable in future years dependent on assumptions about mortality rates, salary levels, etc. discounted to present values. We have reviewed the accounting entries for pensions supplied by the Surrey Fund actuary, Hymans Robertson and consider the disclosures to be appropriate.

Financial statements audit

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Property, Plant and Equipment	4	3	£46.3 (PY:£44.9m)	A full valuation took place in 2014/15 before the adoption of a 5 year rolling valuation programme in 2015/16. 20% of land and buildings were revalued in the current year with no material movements noted. We considered the revaluation basis to be appropriate. The Authority continues its use of the beacon methodology in line with the DCLG's *Stock Valuation for Resource Accounting* published in November 2016. The Authority has utilised an external valuation expert, Kempton Carr Croft to provide valuation estimates. We reviewed instructions provided and deem that the valuation exercise is generally in line with the instructions. We have a recommendation to strengthen this process at Appendix 1.
PPE: asset lives	3	3	No changes noted	Vehicles, plant, furniture and equipment is allocated over the useful life of the asset as defined by a suitable qualified officer. Our work on PPE has not indicated any significant losses on disposal or assets no longer in working order.
Debtors provisioning	2	2	£1.4m (PY:£1.9m)	The council had opening balances of £1.4m and has increased its provision by £0.5m This is a result of an increase in the outstanding business rates and housing benefit overpayments. We consider the provision disclosures to be acceptable, though this remains cautious.

Financial statements audit

Narrative Report of the Authority

We have reviewed the Authority's Narrative Report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Queries from local electors

We did not receive any questions or objections from members of the public this year.

Audit certificate

In order for us to issue an audit certificate, we are required to have completed all our responsibilities relating to the financial year. We are not in a position to issue our audit certificate until the areas listed on page 3 have been resolved.

Whole of Government Accounts (WGA)

We will undertake our work relating to review of the WGA consolidation pack once our audit of the financial statements is complete.

Other grants and claims work

We undertake housing benefits certification work for the Authority that does not fall under the PSAA arrangements. Work on this claim is currently underway at the date of this Report.

Audit fees

Our fee for the audit was £48,128 excluding VAT (£48,128 excluding VAT in 2015/16). This fee was in line with that highlighted in our audit plan approved by the Audit Committee in February 2017.

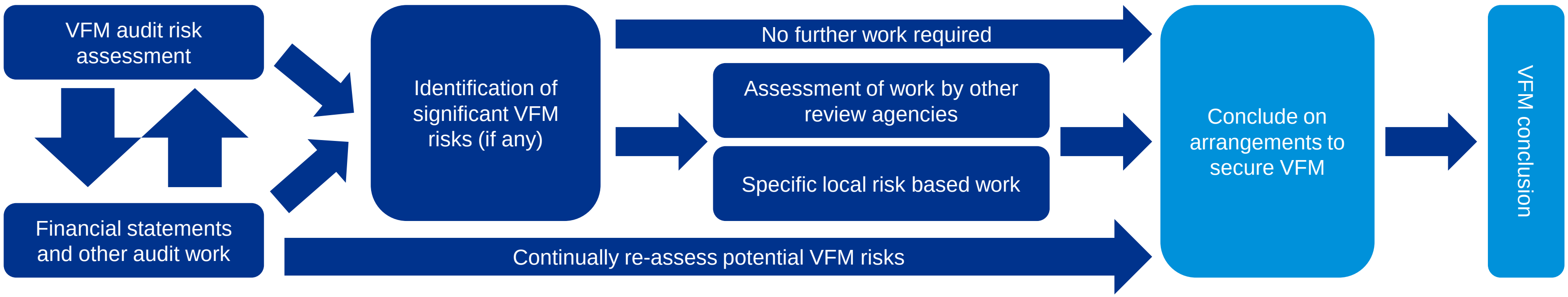
As a result of the delays in undertaking our audit work and the complexity of our VFM work relating to the sale and leaseback of the BP campus, we have incurred overruns on our audit costs. We will agree an additional fee with the Authority and the PSAA.

Our work on the certification of Housing Benefits (BEN01) is not yet complete. The planned scale fee for this is £7,568 excluding VAT (£7,102 excluding VAT in 2015/16).

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

Value for money

For 2016/17 our value for money (VFM) work follows the NAO's guidance. It is risk based and targets audit effort on the areas of greatest audit risk. Our methodology is summarised below.



Significant risk based VFM audit work

Our VFM audit work is still ongoing. As well as the overall arrangements that the Authority has in place, we are focusing on the sale and leaseback of the BP site, given the significance and materiality of this transaction. We will provide an updated report to the Audit Committee upon conclusion of our work.

Appendix 1

Recommendations raised and followed up

Recommendations raised as a result of our financial statements work in the current year are as follows:

Priority rating for recommendations					
❶	Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	❷	Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸	Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
1	❶	**Financial statements production** The draft accounts published by the Authority on 17 July 2017 had not been adequately prepared or reviewed by an appropriate member of the Authority's finance team. Due to staff turnover, both of the subsequent accounts preparers were new joiners and did not have historical knowledge of the Authority's systems or operations to prepare the accounts. There was limited evidence of independent review of the draft accounts. As a result, the accounts did not appropriately reflect significant transactions that took place during the year, such as the acquisition of the BP campus or the drawdown of over £400m in loans. In addition, we identified a significant volume of presentational/disclosure errors, material inconsistencies within the accounts, and departures from the CIPFA guidance notes. This caused significant delays in the audit timetable, and we were required to postpone our work mid-audit and reschedule the remaining fieldwork until the accounts had been corrected. We recommend that the financial statements are prepared by individuals with sufficient knowledge and experience of the organisation. Following preparation, the accounts should be independently reviewed by a senior officer and any errors or discrepancies identified should be recorded in advance of the onsite audit period. The Authority must strengthen its financial reporting in order to put it in a good position to meet the new 2017/18 deadline of 31 July. Additional reviews of working papers, particularly those that involve key areas of judgement, should be made a matter of routine.	**Management Response:** As the report highlights several key members of the Accountancy team left during the accounts process and there were issues with an interim individual. The Council now has in place a permanent Chief Accountant with many years experience of closing of accounts (and indeed has been involved recently in piloting CIPFA's "Big Red Button" process for speeding up accounts closure. We also now have in place a permanent Deputy Chief Accountant with a broad range of technical accounting experience. The Chief Accountant and Chief Finance Officer are undertaking a fundamental review of the close down process and will ensure that it is speeded up and additional review is built into the process to be completed before Christmas 2017. Other members of the team are being provided with additional training. The Accountancy team will also draw on its Treasury Management advisers to review relevant technical (financial instruments etc.) notes and treatment during the closure process. **Action by:** Chief Finance Officer / Chief Accountant **Due date:** 23 December 2017

Recommendations raised and followed up

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
2	❶	**Resilience of Authority finance team** Significant personnel changes have occurred across the Authority's financial team with further changes anticipated. As a result, there is increased risk around succession planning, retaining corporate memory and maintaining business as usual at the Authority. We recommended that the Authority develops a succession and stability plan to ensure that the finance team is resilient to personnel and structural changes and that stability is maintained when individuals leave. The Authority should also consider creating practical strategies that Management can use to engage and retain talent within its finance team.	**Management Response:** As per response to Recommendation 1, we are undertaking a training plan to develop the skills and experience of the team and to build in more experience. We are examining options to help retain talent within the team. The Chief Accountant will be reviewing succession planning and looking to ensure that there is greater resilience in the accountancy team. **Action by:** Chief Finance Officer / Chief Accountant **Due date:** 23 December 2017

Recommendations raised and followed up

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
3	❶	**Journal approvals and segregation of duties** During our testing of journals we identified issues relating to the way some transactions were processed and evidenced during the financial year 2016/17. The Authority has concluded that it is not possible to recreate the evidence for why these journals were processed. The individuals who processed and/or approved the journals have now left the Authority and have left no written record of why they were processed and the line descriptions are often inadequate. We recommend that for all journal entries, the Authority ensures: ▪ All journal entries are approved by an individual separate from the person who uploads them; ▪ Either the Deputy Chief Accountant or the Chief Accountant approves all journals over £20,000 in value; ▪ A meaningful description is provided for each journal entry stating the reason why the journal was necessary and what the journal represents in accounting terms; ▪ Adequate supporting evidence is kept on file for each journal raised; and ▪ Accountancy team Management regularly review the files to monitor compliance and raise with individuals through one to ones or the annual appraisal system if there are recurring issues.	**Management Response:** Chief Accountant will provide a quarterly review to Chief Finance Officer to confirm compliance. Action by Chief Accountant. **Action by:** Chief Finance Officer / Chief Accountant **Due date:** Now implemented

Recommendations raised and followed up

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
4	2	**Valuation of land and buildings** As part of our procedures to provide assurance over the valuation of land and buildings within the financial statements, a review of the year end Valuation Report produced by the external valuer and commissioned by the Authority was undertaken as well as a review of the Authority processes and controls in relation to the valuation exercise. From this review, we have identified a number of detailed recommendations to strengthen the approach that the Authority takes to the valuation of its land and buildings and have shared these with the Finance Team. This includes demonstration of the consideration and challenge of the assumptions applied by the external valuer and ensuring a robust data trail underpins the valuations applied to the accounts. We recommend that the Finance implement our action plan ahead of the next valuation exercise.	**Management Response:** Agreed. **Action by:** Chief Accountant **Due date:** 1 February 2018
5	2	**Fixed asset registers** During our testing of fixed assets we were unable to obtain Fixed Asset Registers in relation to IT equipment, intangible assets and heritage assets. Without a complete listing, the Authority is unable to effectively manage and report on the assets it holds. We recommend the Authority conducts an exercise to produce a full listing of assets held within the IT equipment, intangible and heritage asset categories. All assets should be assessed for impairment to ensure that the valuations held within the financial statements are materially correct.	**Management Response:** We will conduct an exercise to produce a full listing of IT equipment. Whilst we have in recent years reviewed heritage assets we will conduct further review. **Action by:** Chief Accountant **Due date:** 31 March 2018

Recommendations raised and followed up

We have followed up the recommendations from the prior year's audit, in summary:

Total number of recommendations	Number of recommendations implemented	Number outstanding (repeated below):
4	2	2

#	Risk	Recommendation	Management Response / Officer / Due Date	Status at October 2017
Financial statements				
1	2	**Valuation Frequency and Timing** While the Authority is moving to a programme of rolling valuation from 2015/16, up until this point the Authority obtained a full valuation of its land and buildings portfolio once every 5 years on 1 April for the financial year in which the valuation was accounted for. We recommend that the Authority should seek to obtain valuations as at 31 March to minimise the risk of potentially significant changes in valuation during the course of the financial year, either impairments or upwards movements. Due to the new policy of revaluing some assets each year this creates a risk that significant asset changes for those assets not valued in that year are not recorded in the intervening period, potentially leading to material movements at the end of the revaluation cycle. As a matter of course we would recommend that as part of its annual reporting that management formally communicate to members their in-year assessment of any impairment or potential upward valuation of assets where those assets have not been subject to valuation at year end. This is particularly important where the Authority elects to continue to obtain valuations dated 1 April.	**Accepted** We will change the valuation dates to 31 March. As part of the formal annual reporting management will report to councillors their in-year assessment of any impairment or upward revaluation of assets where those assets have not been subject to valuation at year end. Action by: Principal Accountant and Head of Asset Management Deadline: 30 June 2016 As part of the revaluation rolling programme, the valuers were instructed to value the properties which were due on the rolling programme valuation list for 2015/16 to be valued at 31 March 2016. Management has not reported to councillors on the in-year assessment of impairment and upward revaluation where those assets have not been subject to valuation at year end. Specific consideration should be given to management reporting to councillors in 2016/17. Action by: Principal Accountant and Head of Asset Management Revised deadline: 30 June 2017	**Management Response:** Action agreed outstanding. **Action by:** Chief Accountant in partnership with Commercial Property Manager **Due date:** 1 March 2018

Recommendations raised and followed up

#	Risk	Recommendation	Management Response / Officer / Due Date	Status at October 2017
Financial statements				
2	3	**Timeliness of reconciliations** During our testing of payroll controls it was noted that reconciliations are not being prepared and reviewed in a timely manner. During our testing of cash, it was noted that reconciliations were not performed for nine months. The main cause is due to the Council not having a contingency plan in place when staff are on sick leave or unavailable. We recommend that the Council implement a robust plan to ensure that there is sufficient resilience within the finance team to cope with short term absences.	**Accepted** We will review our procedures around preparing and reviewing the reconciliations that are preformed and will look at the resilience issues within the team to cover short term absences. The problems around the testing of cash were not as a result of staff being unavailable or on sick leave. Date: 31st December 2016	We reviewed two payroll reconciliations from the 2016/17 year and noted that neither had been reviewed within a month of the reconciliation being produced. We have therefore re-raised this recommendation to Management. **Management Response:** Action agreed outstanding. Sickness absences have impacted. **Action by:** Deputy Chief Accountant **Due date:** 30 November 2017

Appendix 2

Materiality and reporting of audit differences

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

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

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

Materiality for the Authority's accounts was set at £1.4 million which equates to around 2% of gross expenditure.

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

Reporting to Audit Committee

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

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £70K for the Authority.

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

Appendix 3

Audit differences

Unadjusted audit differences

Under UK auditing standards (ISA (UK&I) 260) we are required to provide the Audit Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are ‘clearly trivial’, which are not reflected in the financial statements. In line with ISA (UK&I) 450 we request that you correct uncorrected misstatements. However, they will have no effect on the opinion in our auditor’s report, individually or in aggregate. As communicated previously with the Audit Committee, details of all adjustments greater than £70K are shown. There are no unadjusted audit differences.

Audit differences

Adjusted audit differences

To assist the Audit Committee in fulfilling its governance responsibilities we present in the tables below a summary of adjusted audit differences (including disclosures) identified during the course of our audit. The adjustments below have been included in the financial statements.

Authority adjusted audit differences (£'000)						
#	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Comments
1					Dr Revaluation Reserve £12,356k Cr Capital Adjustment Account – Impairment £12,356k Dr General Fund – Impairment £12,356k Cr General Fund Movement – Impairment £12,356k	Recode revaluation previously coded to impairment following SBC fixed asset review.
2			Dr Investment Properties - Capital Expenditure £2,478k Cr PPE Land & Buildings - Capital Expenditure £2,478k			Reclassification of Fixed Asset expenditure to correctly account for Harper House investment property following SBC fixed asset review.

Appendix 3

Audit differences

Authority adjusted audit differences (£'000)						
#	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Comments
3	Dr Impairment £13,637k		Cr Investment Properties – Impairment £13,637k		Dr Revaluation Reserve £13,637k Cr General Fund Movement - Impairment £13,637k	Investment Properties Impairment correction following SBC fixed asset review.
4			Dr Investment Properties - Impairment £25,993k Cr Investment Properties - Revaluation £25,570k Cr PPE - Revaluation £423k			Reclassify Impairment to Revaluation following SBC fixed asset review.
5	Dr Impairment £450k		Cr PPE Vehicles, Plant & Equipment – Non Enhancing expenditure £450k		Dr Capital Adjustment Account – Impairment £450k Cr General Fund Movement – Impairment £450k	Write back of Capital to Revenue following SBC fixed asset review.

Audit differences

Authority adjusted audit differences (£'000)						
#	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Comments
6	Cr Impairment £2,943k		Dr PPE Land & Buildings – Revaluation £1,836k		Dr General Fund – Impairment £2,941k Dr Revaluation Reserve – Revaluations £1,088k Cr Capital Adjustment Account – Impairment £2,922k	Corrections to Revaluation gains/losses and impairments for Land & Buildings following SBC fixed asset review.
7					Dr Capital Adjustment Account – Impairment £25,993k Cr Revaluation Reserve £25,993k	Transfer of Investment price Impairment following SBC impairment review.
8			Dr PPE Land & Buildings – Depreciation £732k		Cr Revaluation Reserve £732k	Correction to revaluation depreciation on PPE following SBC fixed asset review.
9			Dr PPE Vehicles, Plant & Equipment – Revaluation £423k Cr PPE Land & Buildings – Revaluation £423k			Transfer Bugle Returns Public House valuation within PPE following SBC fixed asset review.

Audit differences

Authority adjusted audit differences (£'000)						
#	**Income and expenditure statement**	**Movement in reserves statement**	**Assets**	**Liabilities**	**Reserves**	**Comments**
10			Cr PPE Land & Buildings – Disposals £2,986k		Dr Capital Adjustment Account - Disposals £2,986k	Adjustments related to Harper House and Knowles Green Estates Limited (KGEL) following SBC fixed asset review: - Reclassification of Harper House - Donated Asset to KGEL - De recognition of asset.
11			Dr Long Term Investments £2,001k Cr Short Term Investments £2,001k			Balance sheet allocation correction between short term and long term investments following SBC accounts review.
12			Dr Short Term Payables £75k Cr Short Term Receivables £52k Cr Cash and Cash Equivalents £22k Cr Provisions £1k			Balance sheet allocation correction between receivables/payables/cash following SBC accounts review.
Total	**Dr £11,144k**		**Cr 14,505k**		**Dr £3,361k**	**Total impact of corrected audit differences**

Appendix 4

Audit independence

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

Integrity, objectivity and independence

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

General procedures to safeguard independence and objectivity

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

Audit matters

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

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

Audit independence

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

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

Auditor declaration

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

We summarise below the non-audit services that we have provided, the fee, the potential threats to auditor independence and the associated safeguards in place.

Description of non audit services	2016-17 fees	Potential threat to auditor independence	Associated safeguards in place
Housing Benefits claim certification	£7,568, excluding VAT	Audit of the annual Housing Benefits return. This is a standard return for which an agreed upon set of procedures is completed. There is no impact on the financial statements audit.	None required.
Total fees	**£7,568, excluding VAT**		
Total fees as a % of the external audit fees	15.7%		

We have considered the ratio of audit to non-audit fees and as required by the APB Ethical Standards. The principal threat which arises from fees from non-audit services which are large in absolute terms relative to the audit fee is the perception of self-interest and advocacy. In this regard, we do not consider that the above ratio creates such a self-interest or advocacy threat since the absolute level of non-audit fees is not significant to our firm as a whole and neither the audit partner nor members of the audit team are incentivised on, or rewarded in respect of, the provision of non-audit services to you. We believe that the question of perception is best addressed through appropriate disclosure as to use of the auditor for the provision of non-audit services in the Authority's annual report and accounts.

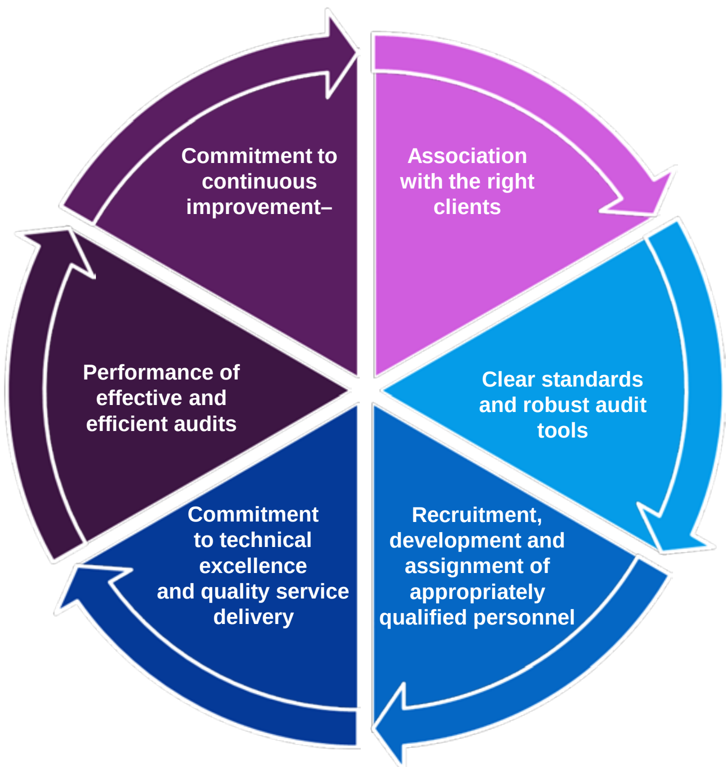
Audit quality framework

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

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

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

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



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

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

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

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