Annual Audit Letter on the 2018/19 External Audit

London Borough of Ealing

29 May 2020

Contents

1. Letter to Members

The Members
London Borough of Ealing
Perceval House
14-16 Uxbridge Road
London
W5 2HL

29 May 2020

Dear Sirs

We have pleasure in setting out this Annual Audit Letter to summarise the key matters arising from the work that we have carried out in respect of the audit for the year ended 31 March 2019.

Although this letter is addressed to the Members of London Borough of Ealing ("the Authority"), it is also intended to communicate the significant issues we have identified in an accessible style to key external stakeholders including members of the public. The letter will be published on the Public Sector Audit Appointments Ltd (PSAA) website at **www.psaa.co.uk** and on the Authority's website.

This letter has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by Public Sector Audit Appointments Ltd. This is available from **www.psaa.co.uk**.

This letter has been discussed and agreed with the Chief Finance Officer. A copy of the letter will be provided to all Members.

This is our first year as the external auditor of the Authority following the transition to the PSAA contract in 2018/19. We would like to take this opportunity to thank management for the assistance and support through the audit process.

Yours faithfully,

Deloitte LLP

Jonathan Gooding

Audit Partner

for and on behalf of Deloitte LLP

St Albans, United Kingdom

2. Key Messages

Statement of Accounts	
Unqualified opinion issued on 29 May 2020	**<u>Statement of Accounts</u>** In 2018/19 the Authority was required to prepare its Statement of Accounts in accordance with International Financial Reporting Standards ("IFRS") as defined in the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 and other relevant legislation. We issued our audit opinion on the financial statements on 29 May 2020. Our opinion was not qualified. The deadline for completing this work was set as 31 July 2019. The main reasons for the accounts being finalised after the deadline were: • The first draft of the Statement of Accounts included a high number of material errors, including in the prior year, which required a significant amount of work from both management and Deloitte to correct. • The high level of weaknesses identified in the control environment. • Working papers provided by the authority were not adequate (of the appropriate quality, in the level of detail, or in a format we would have expected) for our testing. • The level of information requested from officers and the nature of some of our procedures was different to prior years. Our opinion includes a section on "other information" in the statement of accounts such as the narrative report. Our responsibility is to read the other information and to consider whether it is materially consistent with the financial statements or our knowledge of the Council. We did not report any issues in respect of these matters. Materiality for the Authority's accounts was set at £25.3m. **<u>Pension Fund:</u>** We issued an audit opinion on the financial statements of the London Borough of Ealing Pension Fund on 29 November 2019. Our opinion was not qualified. This letter also covers the audit work performed in relation to the Pension Fund.

Value for Money ("VfM") conclusion	
An unmodified conclusion issued on 29 May 2020	We are required to base our statutory VfM conclusion on the criteria specified by the National Audit Office. This is an evaluation of whether the Authority has in place proper arrangements to ensure properly informed decisions were taken and the Authority deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

	We issued an unmodified VFM conclusion on 29 May 2020. This means we are satisfied that, in all significant respects, the Authority has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.

Audit findings	
We reported significant weaknesses in internal control and other findings to the Audit Committee	International Standards on Auditing (UK) require us to communicate in writing to those charged with governance the significant findings from our audit. In respect of the Authority's audit for 2018/19, there were a high number of internal control recommendations and findings that we brought to the attention of the Audit Committee. We include a summary of the key matters identified in Section 4 below.

Independence and Objectivity	
Independence and objectivity	An analysis of audit fees for the year ended 31 March 2019 is shown in Section 6 of this letter. In our professional judgement the policies and safeguards in place ensure that we are independent within the meaning of all regulatory and professional requirements and that the objectivity of the audit partner and audit staff is not impaired.

3. Responsibilities and Scope

Responsibilities of the Authority and Auditors

The Authority is responsible for maintaining the control environment and accounting records and preparing the accounting statements in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 based on IFRS and other relevant legislation.

We are appointed as the Authority's independent external auditors by PSAA, the body responsible for appointing auditors to local public bodies in England where they have opted into this programme.

As the Authority's appointed external auditor, we are responsible for planning and carrying out an audit that meets the requirements of the National Audit Office's Code of Audit Practice ("the Code"). Under the Code, we have responsibilities in two main areas:

- auditing the Authority's accounts; and
- evaluating whether the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources (the value for money ("VFM") conclusion).

The scope of our work

We conducted our audit in accordance with International Standards on Auditing (UK) as adopted by the UK Auditing Practices Board ("APB"). The audit opinion on the accounts reflects the financial reporting framework adopted by the Authority, being the Code of Practice on Local Authority Accounting in the United Kingdom 2018/19 based on IFRS and other relevant legislation.

We conducted our work on the 2018/19 VFM conclusion in line with guidance issued by the National Audit Office in November 2017.

4. Audit of the Accounts

Statement of Accounts	
Unqualified opinion issued on 29 May 2020	We issued an unqualified opinion on the Authority's 2018/19 accounts on 29 May 2020. Before we give our opinion on the accounts, we are required to report to those charged with governance (here the Audit Committee – "the Committee") any significant matters arising from the audit. To address this requirement, detailed reports on both the main Council and the Pension Fund audits were issued on 21 February 2020 and 19 November 2019 respectively. These reports were discussed with the members of the Committee on 4 March 2020 and 27 November 2019 respectively. These papers are available to view online as part of the report packs for those meetings. We can confirm that all outstanding matters included within the reports were resolved satisfactorily before issuing our opinions, resulting in no additional misstatements or control recommendations being identified. We note that the Covid-19 global pandemic in 2020 is a post balance sheet non-adjusting event and the Authority has provided adequate disclosure regarding this post balance sheet event in the Statement of Accounts.
Materiality	We define materiality as the magnitude of misstatement in the financial statements that makes it probable that the economic decisions of a reasonably knowledgeable person using those financial statements would be changed or influenced. We use materiality both in planning the scope of our audit work and in evaluating the results of our work. Based on our professional judgement, materiality for the Authority's accounts was set at £25.3m which equated to 2% of gross expenditure. This benchmark was chosen as the Authority is a non-profit organisation and total expenditure is a key measure of financial performance for users of the financial statements. We agreed with the Committee that we would report to the Committee all uncorrected audit differences in excess of £1.3m, as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds. We would also report to the Committee on any uncorrected disclosure matters identified when assessing the overall presentation of the financial statements. We reported matters of this nature in our March report and have summarised the key matters in the "Findings" section below.
Significant Risks	Our audit work was designed to specifically address the following significant audit risks which are presented in further detail below. Significant audit risks are the areas deemed to be those with the greatest potential for being materially incorrect in the financial statements and are therefore areas of greater focus for the audit team. ***Statement of Accounts*** 1. **Property valuation:** Our conclusion in this risk area is that the value of property assets is not materially misstated. The Council's valuation assumptions were generally reasonable and fell within an acceptable range. We have raised control recommendations is relation to the

	valuation exercise. See "Key findings and control recommendations" section below. **Risk identified:** The Council is required to hold property assets within Property, Plant and Equipment and Investment Properties at valuation. The valuations are by nature significant estimates which are based on specialist and management assumptions and which can be subject to material changes in value. **Deloitte response** a. We tested the design and implementation of key controls in place around the property valuation, including how the Council assures itself that there are no material impairments or changes in value for the assets not covered by the annual valuation. b. We obtained an understanding of the approach adopted to the valuation, including assessing the valuer's qualifications, objectivity and independence and reviewing the methodology used. c. We tested a sample of inputs to the valuation. d. We used our valuation specialists, Deloitte Real Estate, to review and challenge the appropriateness of the assumptions used in the valuation of the Council's property assets. e. We tested a sample of revalued assets and reperformed the calculation of the movement to be recorded in the financial statements to check that it was correctly recorded. f. We considered the impact of uncertainties relating to the UK's exit from the EU upon property valuations in evaluating the property valuations and related disclosures. **2. <u>Capital Expenditure:</u>** We concluded satisfactorily on our testing in this area and no adjustments were raised for the current year, although we did identify errors identified in the prior year, more details of which are included later in this report. In addition, we also raised control recommendations is relation to this risk. See "Key findings and control recommendations" section below. **Risk identified** The capital plans for the Council incorporate a number of large regeneration projects which extend from 2017/18 into 2018/19 and beyond, with £121m of capital expenditure during the year. Determining whether or not expenditure should be capitalised can involve judgement. There is an incentive for officers to misclassify revenue expenditure as capital. **Deloitte response** a. We tested the design and implementation of controls around the capitalisation of costs. b. We selected a sample of capital items (including revenue expenditure funded from capital under statute ("REFCUS")) in

	the year to test whether they have been appropriately capitalised in accordance with the accounting requirements. 3. **Management override of controls:** We concluded satisfactorily in this area. We did not identify any significant bias in the key judgements made by management based on work performed. Furthermore, we have not identified any instances of management override of controls in relation to the specific transactions tested based on work performed. We did, however, raise control recommendations is relation to this risk. See "Key findings and control recommendations" section below. **Risk identified** This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Council's controls for specific transactions. **Deloitte response** a. We have considered the overall sensitivity of judgements made in preparation of the financial statements, and note that: i. The Council's results throughout the year were projecting overspends in operational areas. This was closely monitored and whilst projecting overspends, the underlying reasons were well understood; and ii. Senior officer's remuneration is not tied to particular financial results. We have considered these factors and other potential sensitivities in evaluating the judgements made in the preparation of the financial statements. b. ***Significant and unusual transactions:*** We did not identify any significant transactions outside the normal course of business or any transactions where the business rationale was not clear. c. ***Journals:*** We have tested the design and implementation of the controls in place for journal approval. We have used "Spotlight", Deloitte's general ledger data analytics tool, to risk assess journals and select items for detailed follow up testing. The journal entries were selected using computer-assisted profiling based on areas which we consider to be of increased interest. We have tested the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting. ***d. Accounting estimates and judgements:*** We have tested the design and implementation of the key controls over key accounting estimates and judgements. We reviewed accounting estimates made in the period for biases that could result in material misstatements due to fraud. Each of the areas of estimation evaluated were found to be balanced and did not

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indicate a bias to achieve a particular result. We tested accounting estimates and judgements, focusing on the areas of greatest judgement and value. Our procedures included comparing amounts recorded or inputs to estimates to relevant supporting information from third party sources.
<u>Pension Fund</u>
1. <u>Management override of controls:</u> We concluded satisfactorily in this area. We did not identify any significant bias in the key judgements made by management based on work performed. We did, however, raise control recommendation is relation to this risk. See “Key findings and control recommendations” section below.
Risk identified
This risk area includes the potential for management to use their judgement to influence the financial statements as well as the potential to override the Authority’s controls for specific transactions.
Deloitte response
a. We have considered the overall sensitivity of judgements made in preparation of the financial statements, and note that the Fund’s results throughout the year are largely driven by movements in investments which are externally managed. We have considered these factors and other potential sensitivities in evaluating the judgements made in the preparation of the financial statements.
b. Significant and unusual transactions: We have not identified any significant transactions outside the normal course of business or any transactions where the business rationale was not clear in the current year.
c. Journals: We have tested the design and implementation of the controls in place for journal approval. We have used “Spotlight”, Deloitte’s general ledger data analytics tool, to risk assess journals and select items for detailed follow up testing. The journal entries were selected using computer-assisted profiling based on areas which we consider to be of increased interest. We have tested the appropriateness of journal entries recorded in the general ledger, and other adjustments made in the preparation of financial reporting.
d. Accounting estimates and judgements: We have performed a review of the accounting estimates. We reviewed accounting estimates for biases that could result in material misstatements due to fraud. We tested accounting estimates and judgements, focusing on the areas of greatest judgement and value. Our procedures included comparing amounts recorded or inputs to estimates to relevant supporting information from third party sources.
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<tr><td>Overall opinion</td><td>We issued an unqualified opinion on the Authority’s 2018/19 accounts on 29 May 2020. Our opinion stated that the accounts present a true and fair view of the financial position of the Authority as at 31 March 2019 and its income and expenditure for the year then ended.</td></tr>
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Annual Governance Statement and Other Information	
Recommendations were made during the process including some proposed improvements for 2019/20	As appointed auditors, we review the Annual Governance Statement ("AGS") and other information presented with the financial statements to check that information is consistent with the financial statements. Our reporting to the Committee included recommendations in relation to these documents which were accepted by officers. We do not have any significant findings to report in relation to the final versions of these documents but have raised some recommendations for improvement in this area for 2019/20.
Powers and Duties	
We did not receive any questions about the accounts or make any public interest reports	Under the Local Audit and Accountability Act 2014, auditors have specific powers and duties, including to give electors the opportunity to raise questions about the accounts and to consider and decide upon objections received in relation to the accounts. We did not receive any such questions or objections. We have a duty to consider whether to issue a report in the public interest about something we believe the Authority should consider, or if the public should know about. We have not identified any matters that would require us to issue a public interest report nor have we exercised our other statutory powers.
Whole of Government ("WGA") accounts return	
We did not identify any material inconsistencies between the accounts and the WGA return	The Authority prepares a consolidation pack to support the production of Whole of Government Accounts by HM Treasury. Under WGA requirements, we are required to submit a return outlining any issues arising from the audit. We did not identify any material inconsistencies between the accounts and the WGA accounts return. As required by the guidance, we submitted the return confirming this to the National Audit Office on 29 May 2020.
Audit Certificate	
We have issued our certificate	We have issued our certificate. The certificate confirms that we have concluded the audit for 2018/19 in accordance with the requirements of the Local Audit & Accountability Act 2014 and the Code of Audit Practice.
Key findings and control recommendations	
We raised several findings and control recommendations	The following is a summary of the key findings identified as part of the audit process and reported to the Committee. There is further detail in the papers presented to the 4 March 2020 Committee meeting with respect to the Authority and the 27 November 2019 Committee meeting regarding the Pension Fund specifically. We will follow up on these observations as part of the 2019/20 audit and report our view on progress to management and the Committee: • The initial draft financial statements, published for public inspection and presented for audit, were not of the expected standard, including a

	significant number of material errors in both the current and prior year. We note that the final amended report is satisfactory. • Accounting papers were not prepared to support management's decisions in key areas of the accounts such as the adoption of new accounting standards, key judgement areas and estimates included in the accounts. • Few of the requested documents were provided in the first week of the audit and into the second week and where information was provided follow-up was required as breakdowns did not tie to the trial balance, were not in the level of detail requested, or it was not clear how the working papers provided related to the request. • The grant register maintained by management had not been reconciled to the ledger. This resulted in both a material adjustment being required, as detailed below, together with a significant amount of time being spent by both management and Deloitte reconciling the two. • Several issues were identified in relation the methodology applied to the Council's property valuation exercise and we have proposed several improvements to this procedure area. The final property valuation amounts disclosed in the accounts are satisfactory • In some cases, an audit trail was not kept to evidence that a control had operated. It is important for officers to retain clear, documented evidence of the performance of controls. • The defined pension fund liability was understated by £73.8m as a result of not accounting for the McCloud judgement, together with not updating assumptions for the full year. • The Dedicated Schools Grant was overstated by £37.0m. • Gains on disposal of £41.4m could not be evidenced and required removal from the accounts. • The revaluation of fixed assets was performed incorrectly in the prior year, resulting in three related adjustments being required of £9.5m, £25.6m and £31.0m. • £33.0m of internal recharges (charges between internal Council services) needed to be removed from the Comprehensive Income and Expenditure Statement. • In relation to the Pension Fund, we identified a significant volume of material disclosures in both the current and prior years in respect of investment asset and financial instrument disclosures.
Uncorrected misstatements	
We communicated unadjusted misstatements to the Committee	All misstatements raised to management were subsequently corrected. The following immaterial disclosure deficiencies were reported to the Committee and remain uncorrected at the date of our opinion:

	Authority (1) The accounting policy for revaluation of property assets is missing detail regarding effective date of revaluation, whether an in-house or external valuer has been used and the significant assumptions applied. (2) CIPFA requires reconciliations from opening to closing balances for all unusable reserve accounts, showing the individual movements within those reserves. Currently the Authority shows this at a less granular level than required and does not include a note for each reserve. (3) CIPFA and IFRS 15 require debtors and creditors to be classified by nature rather than, or in addition to, being split by counterparty. (4) The level of detailed included within the narrative statement could be enhanced: a) Outlook – to add further detail around budgetary pressures, assumptions around sustainability, future cash flows, commitments etc. b) Risks – to add further detail regarding types of risks, likelihood of risks materialising, significance of said risks, mitigations etc. (5) The accounting policy for depreciation of fixed assets does not state the range of useful economic lives applied to asset types, instead stating that they will be depreciated over a life advised by a suitably qualified officer. (6) CIPFA requires a reconciliation from opening to closing provisions, including the amount utilised, the amounts released, the new provisions arising during the year and any movement due to discounting. The accounts only state the opening and closing balances. (7) The disclosures made around risks arising from financial instruments lack detail regarding quantification of risks. Pension Fund (1) Disclosures regarding sensitivities of pricing Level 3 Private equity investments with a market value of £3,681k have not been included. (2) Cash deposits of £3,052k were incorrectly included within pooled overseas equities in the prior year.

5. Value for Money

Background and approach

We are required to issue a value for money ("VfM") conclusion within our report on the financial statements. We are required to base our VfM conclusion on criteria specified by the National Audit Office ("NAO") where we are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources. Our assessment is based on the following reporting criterion:

"In all significant respects, the audited body 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 following sub-criteria are then used to inform and guide our work and inform our overall judgement although there is no requirement to separate these nor to report against each sub-criteria:

- Informed decision making
- Sustainable resource deployment
- Working with partners and other third parties.

It is the arrangements in place that we are required to assess, and not the actual decisions made by the Authority.

We planned our local programme of work based on our risk assessment, which was, in part, informed by a series of risk factors determined by the National Audit Office.

The following significant VFM risks were identified and are shown with the Deloitte response:

Risks identified

There is further detail on these risks in the reports presented to the 4 March 2020 Committee meeting:

There is a significant risk in respect of financial sustainability and resilience, highlighted by the CIPFA Financial Resilience benchmarking, the continued overspend in the area of Children's, Adults and Public Health and the ongoing use of resources over the last few years to fund gaps in revenue budgets (a reduction of £13.3m in earmarked reserves since 1 April 2016).

Deloitte Response

We have:

- Evaluated the Council's historical forecasting accuracy;
- Assessed the historical reliance on reserves to finance annual deficits;
- Assessed whether the current budget indicates the Council may not be financially sustainable;
- Considered the Council's track record for achieving cost saving schemes;

- Considered the medium term budgetary gap;
- Reviewed the Council’s historical reliance on borrowings;
- Reviewed the Council’s historical cash and investment balances for any indication of lack of available funds;
- Considered whether there are any indicators that services have been compromised to deliver budget; and
- Reviewed key elements of the Council’s financial management arrangements.

We identified a number of control recommendations with regards to the Authority’s financial management arrangements, but concluded that we do not consider these matters to be sufficiently significant to lead to a qualification of our value or money conclusion.

The VFM conclusion

We issued an unqualified VFM conclusion on 29 May 2020. This means “On the basis of our work, having regard to the guidance issued by the Comptroller and Auditor General in April 2019, we are satisfied that, in all significant respects, London Borough of Ealing put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2019.”

6. Other Matters

Reports issued

Reports issued during the course of the 2018/19 audit included:

- Audit Fee letter;
- Annual Audit Plan;
- The Report to Those Charged with Governance on the 2018/19 audit of the Authority; and
- This Annual Audit Letter.

Analysis of fees

Fees charged to date are as follows:

	2018/19 £000
Scale fees for the audit of the Authority's annual accounts, VfM conclusion and Whole of Government Accounts return	128.3
Scale fee for the audit of the London Borough of Ealing Pension Fund Accounts	16.2
Fee for audit of unconsolidated subsidiary	12.0
Additional fee agreed due to weaknesses in financial reporting and preparedness for the audit discussed earlier in this report.	138.0
TOTAL AUDIT FEES	**294.5**
Fees for reporting on the housing benefit subsidy claim	28.2
Fees for reporting on teachers' pension	4.0
Fees for reporting on other government grants: Pooling of housing capital receipts return	4.0
TOTAL ASSURANCE FEES	**36.2**
TOTAL FEES	**330.7**

Statement of Responsibilities

The Statement of Responsibilities of Auditors and Audited Bodies issued by PSAA explains the respective responsibilities of auditors and of the audited body and this report is prepared on the basis of, and our audit work is carried out in accordance with, that statement.

The matters raised in this report are only those that came to our attention during our audit and are not necessarily a comprehensive statement of all weaknesses that exist or of all improvements that might be made. You should assess recommendations for improvements for their full implications before they are implemented. In particular, we would emphasise that we are not responsible for the adequacy and appropriateness of the national data and methodology supporting our value for money conclusion as they are derived solely from the National Audit Office.

This report has been prepared for the Members, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other party.

An audit does not provide assurance on the maintenance and integrity of the website, including controls used to achieve this, and in particular on whether any changes may have occurred to the Annual Audit Letter since first published. These matters are the responsibility of the Authority but no control procedures can provide absolute assurance in this area.