



London Borough of Merton

Year ending 31 March 2013

Audit Plan

4 March 2013

Members of the General Purposes Committee
London Borough of Merton
Merton Civic Centre
London Road
Morden
SURREY
SM4 5DX

4 March 2013

Dear Members

Audit Plan

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. The purpose of this report is to provide the General Purposes Committee with a basis to review our proposed audit approach and scope for the 2012/13 audit, in accordance with the requirements of the Audit Commission Act 1998, the Code of Audit Practice, the Standing Guidance, auditing standards and other professional requirements, but also to ensure that our audit is aligned with the Committee's service expectations.

This report summarises our assessment of the key risks identified to date and which drive the development of an effective audit for the London Borough of Merton. It outlines our planned audit strategy in response to those risks.

We welcome the opportunity to discuss this report with you on 13 March 2013 as well as understand whether there are other matters which you consider may influence our audit.

We will issue a separate plan in respect of our audit of the London Borough of Merton's Pension Fund. A separate Director who specialises in pension fund audits will sign off the Pension Fund audit report.

Yours faithfully

David Wilkinson
Partner
For and behalf of Ernst & Young LLP

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1. Overview

Context for the audit

This audit plan covers the work that we plan to perform in order to provide you with:

- ▶ Our audit opinion on whether the financial statements of the London Borough of Merton give a true and fair view of the financial position as at 31 March 2013 and of the income and expenditure for the year then ended; and
- ▶ A statutory conclusion on the London Borough's arrangements to secure economy, efficiency and effectiveness.

We will also review and report to the National Audit Office ('NAO'), to the extent and in the form required by them, on your Whole of Government Accounts return.

When planning the audit we take into account several key inputs:

- ▶ Strategic, operational and financial risks relevant to the financial statements.
- ▶ Developments in financial reporting and auditing standards.
- ▶ The quality of systems and processes.
- ▶ Changes in the business and regulatory environment.
- ▶ Management's views on all of the above.

This enables us to focus our audit on the areas that matter. By focusing on these, our feedback is more likely to be relevant to the London Borough of Merton.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

In part 2 and 3 of this report we provide more detail on the areas which we believe present significant risk to the financial statements audit, and outline our plans to address these risks. Details of our audit process and strategy are set out in more detail in section 4.

We will provide an update to the General Purposes Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in September 2013.

Our process and strategy

- ▶ **Financial Statement Audit**
 - ▶ We will apply the concept of materiality in planning and performing our audit, in evaluating the effect of any identified misstatements and in forming our opinion. We set our materiality based on the London Borough's level of gross expenditure. We also consider its financial position, its public profile and reporting history. Our audit is designed to identify errors above materiality.
 - ▶ We intend to place reliance on the key controls in your key financial processes, where this is the most efficient audit approach. Alternatively, we will use substantive tests of detail.
 - ▶ To the fullest extent permissible by auditing standards, we are placing reliance on the work of internal audit wherever possible. We have agreed a programme of work with them.
 - ▶ Your new audit team is made up of a Partner, David Wilkinson, a Director, Paul King, a Senior Manager, Lizzie Peers, an Audit Manager, Michael Yeats and a qualified Executive, Aleks Bennett. We also have support from a specialist IT auditor. Detailed meetings were held with the outgoing audit team, including a review of their audit files in order to gain an understanding of the London Borough, to be aware of the issues that have arisen in previous audits and to ensure a smooth handover.

- ▶ **Arrangements for securing Economy, Efficiency and Effectiveness**
 - ▶ We adopt an integrated audit approach such that our work on the financial statement audit feeds into our consideration of the arrangements in place for securing economy, efficiency and effectiveness.
 - ▶ We have identified some areas of specific focus in relation to our work on your arrangements but we do not expect this to result in any additional work being performed, over and above our standard programme of work.

2. Financial Statement Risks

We outline below our assessment of the key strategic or operational risks and the financial statement risks facing the London Borough of Merton identified through our knowledge of the entity's operations and discussion with members and officers. As the audit progresses other risks may emerge and these will be reported to you in the September 2013 Governance Letter or earlier, if considered necessary.

These reflect an assessment of risk from our perspective as the new auditors of your financial statements. Their inclusion does not indicate that there has been any deterioration in these areas or that we have evidence that these are materially misstated.

We have also included a risk of misstatement due to fraud or error. This is a risk which we are required as auditors to consider under the International Standards on Auditing and again does not reflect a view that there is heightened risk of this arising at the London Borough.

At our meeting, we will seek to validate these risks with you.

Significant risks	Our audit approach
<p>Property, Plant and equipment (PPE)</p> <p>Errors in PPE valuation can lead to material misstatements. The valuation of PPE is a specialist area requiring complex estimation techniques. It is also highly material to the financial statements.</p> <p>During the 2010/11 audit, the previous auditors identified some areas for improvement in the London Borough's valuation process and documentation procedures.</p> <p>A material prior period adjustment of £62 million was agreed during the 2011/12 audit in relation to a 2006/07 overvaluation of an item of land associated with a school. The over valuation was identified by officers.</p> <p>As part of a recent valuation review, officers identified approximately £4 million of assets which have not previously been recorded on the balance sheet and which will need to be accounted for in the 2012/13 statements.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> ▶ Management controls over establishing valuation-related estimates, obtaining reliable valuations and over the completeness of the asset register. ▶ Arrangements for instructing your valuer and controls over information provided to the valuer. ▶ Procedures for reliance on the work of the valuer. ▶ Tests of detail on the reasonableness of the valuation including assessment against central reports provided by the Audit Commission's expert valuer. ▶ Tests of detail over completeness and valuation. ▶ Use of our own valuation expert. This will only be required if the results of our other work are unsatisfactory. We will consult with you before using our own expert to explain the reasons why we consider this to be necessary.
<p>Pension fund liability</p> <p>Errors on pension fund valuations can lead to material misstatement.</p> <p>Valuation is a specialist area requiring complex estimation techniques. A firm of consulting actuaries is engaged to provide the London Borough with expert advice about the assumptions to be applied. Valuations are subject to significant variances dependent on the assumptions used. Small changes in these assumptions can have a significant effect on the valuation figure.</p> <p>Pension fund valuation is highly material to the financial statements. During the inter-valuation period the funding level fell from 91% as at March 2007 to 84% at the last valuation date of 2010, resulting in a deficit of £67 million. The Pension Fund deficit, on an IAS19 basis, rose from £103 million to £190 million.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> ▶ Management controls over establishing assumptions and obtaining reliable actuarial valuations. ▶ Arrangement for instructing your actuarial expert and controls over information provided to your actuary. ▶ Procedures for reliance on the work of the actuary. ▶ Tests of detail on the reasonableness of the valuation, including assessment against central reports provided by the Audit Commissions expert actuary.

- ▶ Use of our own actuarial expert. Again, this will only be required if the results of our other work are unsatisfactory. We will consult with you before using our own expert to explain the reasons why we consider this to be necessary.

Private Finance Initiative (PFI) schemes

The London Borough had a net book value of £63.7 million of PFI assets disclosed in its accounts at 31 March 2012. It also has a range of liabilities associated with its PFI schemes.

These amounts are material and are based on a number of important assumptions. Small changes in these assumptions can lead to material changes in the values disclosed.

Our approach will focus on:

- ▶ Satisfying ourselves, as your new auditors, as to the soundness of the base assumptions and accounting treatments used in determining the values for the PFI scheme disclosed in the statements. We will also consider the management controls applied to these.
- ▶ Tests of the accounting transactions in year.

Other financial statement risks

Our audit approach

Transfer of a PFI school to academy status

Bishopsford School which is a PFI scheme school will become an academy during 2012/13. The London Borough will require expert advice in order to agree valuation and accounting treatment for the transfer.

Our approach will focus on:

- ▶ Management arrangements for obtaining specialist advice.
- ▶ Assessment of the reliability of your management expert.
- ▶ The proposed valuation and its reasonableness.
- ▶ The proposed accounting treatment and its appropriateness.

We will use our PFI expert to provide advice to us on the proposed accounting treatment.

Classification of revenue and capital expenditure

The London Borough has undertaken a review of the appropriateness of the classification of its capital and revenue expenditure and identified some errors and scope for improved awareness in this area.

Our approach will focus on:

- ▶ Management and other controls over the correct classification of expenditure between revenue and capital.
- ▶ Tests of detail of classification to confirm accuracy.

Other risks

Our audit approach

Risk of misstatement due to fraud and error

Management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has put in place a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

Based on the requirements of auditing standards our approach will focus on:

- ▶ Identifying fraud risks during the planning stages.
- ▶ Inquiry of management about risks of fraud and the controls put in place to address those risks.
- ▶ Understanding the oversight given by those charged with governance of management's processes over fraud.
- ▶ Consideration of the effectiveness of management's controls designed to address the risk of fraud.
- ▶ Determining an appropriate strategy to address those identified risks of fraud.
- ▶ Performing mandatory procedures regardless of specifically identified fraud risks.

We will consider the results of the National Fraud Initiative and may make reference to it in our reporting to you.

3. Economy, Efficiency & Effectiveness

Our work will focus on:

1. Whether there are proper arrangements in place for securing financial resilience at the London Borough of Merton and
2. Whether there are proper arrangements in place at the London Borough of Merton secure economy, efficiency and effectiveness in the use of resources.

The table below provides a high-level summary of our risk assessment and our proposed response to those risks.

We have not identified any significant risks to the value for money (vfm) conclusion. However, we have identified the following key areas that we will consider to support our vfm conclusion:

Value for money risks	Impacts arrangements for securing:	Our audit approach
2012/13 financial outturn and delivery of savings		
<p>As at January 2013, the London Borough is forecasting an under spend of approximately £4.8 million for 2012/13, after transfers of £1.19 million to capital financing reserves. Last year auditors reported a major area of focus for the London Borough over the coming year would be to ensure more consistent budgeting and financial monitoring across service departments, as in some cases there were significant under spends.</p>	Financial resilience	<p>Our approach will focus on a review of:</p> <ul style="list-style-type: none"> ▶ 2012/13 outturn and the robustness of forecasting in year. ▶ The reporting, analysis and action taken on budget variances in 2012/13. ▶ Savings plans to address identified shortfalls and performance on delivering these to 31 March 2013.
<p>The three areas which produced the largest under spends in the past two years (adult social care, children's social care and waste services) were forecasting an under spend of £1.5 million as at January 2013. This compares to a forecast under spend of £5.1 million at the same stage last year. However, in 2011/12 the actual under spend was £1.5 million greater than the January 2012 forecast suggested and so officers recognise that close monitoring of variances needs to continue.</p>		
<p>Significant overspends are now being forecast elsewhere in the budget that offset the under spend that is currently forecast for the main three services. Officers recognise that action is needed taken to address these overspends in future years or to re-align budgets to fund them.</p>		
<p>During 2012/13 £11.2 million of savings plans were agreed. As at January 2013, £9.7 million (87%) of these were expected to be achieved by year end.</p>		

Value for money risks	Impacts arrangements for securing:	Our audit approach
.Financial settlement 2013-15 and medium term financial plans (MTFPs)		
<p>The full implications of the provisional local government finance settlement 2013-15 which was announced in December 2012 are still being assessed in detail by officers.</p> <p>Current estimates are that there is a potential £1 million gap (net of savings) for 2013/14. By 2016/17 this gap increases to £15 million.</p> <p>Robust savings plans will need to be developed to address the gaps identified to 20016/17. Cumulative savings plans have been identified totalling £11.4 million to 2016/17 but £4.3 million of savings still need to be identified. These will need to generate recurrent and sustainable reductions in expenditure.</p> <p>The significant changes to the arrangements for both local council tax support and business rates which take effect from 1 April 2013 give rise to further important financial and reputational risks for the London Borough.</p> <p>There is also expected to be a significant increase in pressure on services as a result of welfare reforms and the UK economic environment. Service costs could rise quickly as a result making sustainable reductions in expenditure harder to achieve and sustain.</p>	<p>Financial resilience Economy, efficiency and effectiveness</p>	<p>Our approach will focus on a review of :</p> <ul style="list-style-type: none"> ▶ 2013/14 forecast financial performance. ▶ Management assessment of financial settlement and reasonableness of assumptions made. ▶ Your MTFPs and revisions to these in response to the settlement and changes to local council tax support and business arrangements. ▶ Savings plans to address identified shortfalls and performance on delivering these.
Transfer of Public health (PH) role		
<p>The London Borough has been provided with some £8.7 million to provide PH for Merton from 1 April 2013. Currently, the roles and responsibilities associated with this transfer of role from the NHS to local government are not clear. There are therefore potential financial risks associated for 2013/14 and beyond.</p>	<p>Financial resilience</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> ▶ Funding agreed for this role. ▶ Your assessment of service and cost implications of this transfer of role. ▶ Impact on MTFPs.

4. Our audit process and strategy

4.1 Objective and scope of our audit

Under the Audit Commission's Code of Audit Practice ('the Code'), dated March 2010, our principle objectives are to review and report on, to the extent required by the relevant legislation and the requirements of the Code, the London Borough of Merton's:

- ▶ financial statements; and
- ▶ arrangements for securing economy, efficiency and effectiveness in its use of resources.

We issue a two-part audit report covering both of these objectives.

i) Financial Statement Audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland).

We will also review and report to the National Audit Office ('NAO'), to the extent and in the form required by them, on your Whole of Government Accounts return

ii) Arrangements for securing economy, efficiency and effectiveness

The Code sets out our responsibility to satisfy ourselves that the London Borough [has](#) put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. In arriving at our conclusion, to the fullest extent possible we will place reliance on the reported results of the work of other statutory inspectorates in relation to corporate or service performance. In examining the London Borough's corporate performance management and financial management arrangements we have regard to the following criteria and areas of focus specified by the Audit Commission:

- ▶ arrangements for securing financial resilience – whether the London Borough has robust systems and processes to manage financial risks and opportunities effectively, and to secure a stable financial position that enables it to continue to operate for the foreseeable future; and
- ▶ arrangements for securing economy, efficiency and effectiveness – whether the London Borough is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

4.2 Audit process overview

We are assessing your entity level controls and IT general controls. We have identified the key controls in your major financial systems and are the process of testing these in co-operation with Internal Audit. As a result of our assessments we intend to place reliance on the key controls in your financial systems where this is the most efficient audit approach. Where this is not the most efficient approach we will adopt a substantive approach to gain the assurances we require.

To the fullest extent permissible by auditing standards, we are placing reliance on the work of internal audit wherever possible. We have agreed a programme of tests which is being undertaken by Internal Audit and upon which we will seek to rely. This covers all of the key processes we have identified, with the exception of financial closure and treasury management processes where we are completing the work.

Processes

Our initial assessment of the key processes across the London Borough has identified the following key processes which generate the key account balances within your accounts:

- Accounts receivable
- Accounts payable
- Council tax
- Cash and bank
- Social care-Care First
- Business rates
- Payroll
- Treasury management
- Housing Benefits

We are currently assessing the most efficient approach to obtaining the audit assurance we need on the key account balances.

Analytics

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular in respect of payroll, accounts payable, accounts receivable and journal entries. These tools:

- ▶ help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- ▶ give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the General Purposes Committee.

Internal audit

As in prior years, we will review internal audit plans and the results of work undertaken. We will reflect the findings from these reports, together with reports from other work completed in the year, in our regular progress reports, where issues are raised that could impact the year-end financial statements.

Use of experts

We will utilise specialist Ernst & Young resource, as necessary, to help us to form a view on judgments made in the financial statements. Our plan currently includes the involvement of our PFI specialist. In addition we will seek to draw assurance from the outputs from the Audit Commission's experts on actuarial and valuation matters. We may also use our own experts if required in those areas.

Other audit procedures

In addition to the key areas of emphasis outlined in section 2 and 3, we have to perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Mandatory procedures required by auditing standards on:

- ▶ Addressing the risk of fraud and error.
- ▶ Significant disclosures included in the financial statements.
- ▶ Entity-wide controls.
- ▶ Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements.
- ▶ Auditor independence.

Procedures required by the Code

- ▶ Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement and the Remuneration Report.
- ▶ Reviewing and reporting on the Whole of Government accounts return, in line with the instructions issued by the NAO.
- ▶ Reviewing, and where appropriate, examining evidence that is relevant to the London Borough of Merton's corporate performance management and financial management arrangements and reporting on these arrangements.

4.3 Materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements. We have set our materiality based on the London Borough's level of gross expenditure.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

ISA (UK & Ireland) 450 (revised) requires us to record all misstatements identified except those that are "clearly trivial". We intend to treat misstatements less than £248,000 as clearly trivial. All uncorrected misstatements found above this amount will be presented to you in our year-end report.

4.4 Fees

The Audit Commission has published a scale fee for all authorities. The scale fee is defined as the fee required by auditors to meet statutory responsibilities under the Audit Commission Act in accordance with the Code of Audit Practice 2010.

The indicative fee scale for the audit of the London Borough of Merton is £188,730. In addition, the Commission has indicated an expected fee of £42,450 for the certification of grant claims. However, as discussed with the Director of Corporate Services, we expect this fee will be higher based on our experience of the 2011/12 housing benefits audit.

Any work outside of our normal audit will incur additional audit fee. We are currently engaged in investigations in response to a question raised by a member of the public. This will give rise to additional fee. We will keep the Director of Corporate Services informed of these fees and provide a formal update to the General Purposes Committee.

4.5 Your audit team

The engagement team is led by David Wilkinson, Partner. David is supported by Paul King, Director. Lizzie Peers, Senior Manager, and Michael Yeats, Audit Manager.

The Managers are responsible for the day-to-day direction of audit work, and are the key points of contact for the Head of Accountancy and other Finance team members.

There is also an IT specialist assigned to your audit Sharon Okine who will assess the reliability of your IT general controls, working with Nick Robinson from our IT team.

4.6 Timetable of communication, deliverables and insights

We have set out below a timetable showing the key stages of the audit, including the value for money work and the whole of government accounts; and the deliverables we have agreed to provide to you through the General Purposes Committee cycle in 2013. These dates are determined to ensure our alignment with the Audit Commission's rolling calendar of deadlines.

We will provide a formal report to the General Purposes Committee in September 2013 on the outputs from our year-end procedures. From time to time matters may arise that require immediate communication with the General Purposes Committee and we will discuss them with the General Purposes Committee Chairman as appropriate. We will report any key findings from our work on your financial systems in our June 2013 progress report and these will be summarised in our letter to those charged with governance in September 2013.

Following the conclusion of our audit we will prepare an annual audit letter in order to communicate to the London Borough's external stakeholders, including members of the public, the key issues arising from our work.

Audit phase	Timetable	General Purposes Committee timetable	Deliverables
High level planning:	January-February 2013		Audit Fee letter
Risk assessment and setting of scopes	March 2013	General Purposes Committee	Audit Plan
Testing of routine processes and controls	March-April 2013	General Purposes Committee	Progress report
Year-end audit	July – September 2013		
Issue of audit opinion and vfm conclusion	September 2013	General Purposes Committee	Report to those charged with governance Audit report (including our opinion on the financial statements and a conclusion as to whether the

London Borough of Merton has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources).

Closure	Oct 2013	Audit completion certificate
Report on NAO whole of government accounts		Annual Audit Letter NAO return

In addition to the above formal reporting and deliverables we will seek to provide practical business insights and updates on regulatory matters. We have provided some early views in respect of the establishment of a wholly owned company, which we understand will be formed during 2013/14.

5. Independence

5.1 Introduction

The APB Ethical Standards and ISA (UK and Ireland) 260 “Communication of audit matters with those charged with governance”, requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our independence and objectivity. The Ethical Standards, as revised in December 2010, require that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	Final stage
<ul style="list-style-type: none"> ▶ The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us; ▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ▶ The overall assessment of threats and safeguards; ▶ Information about the general policies and process within EY to maintain objectivity and independence. 	<ul style="list-style-type: none"> ▶ A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ▶ Details of non-audit services provided and the fees charged in relation thereto; ▶ Written confirmation that we are independent; ▶ Details of any inconsistencies between APB Ethical Standards, the Audit Commission’s Standing Guidance and your policy for the supply of non-audit services by EY and any apparent breach of that policy; and ▶ An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

5.2 Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. However we have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective.

Self interest threats

A self interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees.

We are not currently involved in providing any permissible non-audit services to the Council. If these are requested we will comply with the policies that you have approved and that are in compliance with the Audit Commission's Standing Guidance.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard 4. We are not aware of any other self interest threats at the date of this report.

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements. We are not aware of any self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of your entity. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise. We are not aware of any other threats at the date of this report.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of David Wilkinson, your audit engagement partner, and the audit engagement team have not been compromised.

5.3 Other required communications

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year ended 29 June 2012 and can be found here:

[UK 2012 Transparency Report](#)

Appendix A Fees

A breakdown of our agreed fee is shown below.

	Planned Fee 2012/13	Actual Fee 2011/12	Explanation of variance
	£'000	£'000	
Total Audit Fee – Code work excluding Pension Fund audit(Note1)	188,730	337,267	Reduced fee after Audit Commission outsourcing exercise
Certification of claims and returns-(Note2)	42,450	tbc	for 2012/13 an indicative fee has been issued
Non-audit work	0	0	-

Note 1: Pension Fund fees are expected to be £21,000 for 2012/13 (£35,000 for 2011/12). There will be a separate Audit Plan issued for the Pension Fund. This will provide details of the fee and our proposed work on the Fund.

Note 2: The fee for the certification of grant claims of £42,450 is based on the indicative scale fee set by the Audit Commission, which was based on the outturn on certification of claims and returns for 2010/11. Based on our 2011/12 experience of the certification of the housing benefit claim we expect the 2012/13 fee to be higher.

The agreed fee presented above is based on the following assumptions:

- ▶ Officers meeting the agreed timetable of deliverables;
- ▶ We are able to place reliance, as planned, on the work of internal audit;
- ▶ The level of risk in relation to the audit of accounts is consistent with that in the prior year (where we have prior year experience);
- ▶ No significant changes being made by the Audit Commission to the use of resources criteria on which our conclusion will be based;
- ▶ Our accounts opinion and use of resources conclusion being unqualified
- ▶ Appropriate quality of documentation is provided by the audited body
- ▶ Effective control environment

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with you in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee. We are currently dealing with correspondence received from a member of the public.

Appendix B UK required communications with those charged with governance

There are certain communications that we must provide to the audit committee of audited clients. These are detailed here:

Required communication	Reference
Planning and audit approach Communication of the planned scope and timing of the audit including any limitations.	Audit Plan
Significant findings from the audit	Report to those charged with governance
<ul style="list-style-type: none"> ▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▶ Significant difficulties, if any, encountered during the audit ▶ Significant matters, if any, arising from the audit that were discussed with management ▶ Written representations that we are seeking ▶ Expected modifications to the audit report ▶ Other matters if any, significant to the oversight of the financial reporting process ▶ Findings and issues regarding the opening balance on initial audits 	
Misstatements	Report to those charged with governance
<ul style="list-style-type: none"> ▶ Uncorrected misstatements and their effect on our audit opinion ▶ The effect of uncorrected misstatements related to prior periods ▶ A request that any uncorrected misstatement be corrected ▶ In writing, corrected misstatements that are significant 	
Fraud	Report to those charged with governance
<ul style="list-style-type: none"> ▶ Enquiries of the audit committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▶ A discussion of any other matters related to fraud 	
Related parties Significant matters arising during the audit in connection with the entity's related parties including, when applicable:	Report to those charged with governance
<ul style="list-style-type: none"> ▶ Non-disclosure by management ▶ Inappropriate authorisation and approval of transactions ▶ Disagreement over disclosures ▶ Non-compliance with laws and regulations ▶ Difficulty in identifying the party that ultimately controls the entity 	
External confirmations	Report to those charged with governance]
<ul style="list-style-type: none"> ▶ Management's refusal for us to request confirmations ▶ Inability to obtain relevant and reliable audit evidence from other procedures 	
Consideration of laws and regulations	Report to those charged with governance
<ul style="list-style-type: none"> ▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▶ Enquiry of the audit committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the audit committee may be aware of 	

Required communication	Reference
<p>Independence Communication of all significant facts and matters that bear on Ernst & Young's objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> ▶ The principal threats ▶ Safeguards adopted and their effectiveness ▶ An overall assessment of threats and safeguards ▶ Information about the general policies and process within the firm to maintain objectivity and independence <p>For listed companies, communication of minimum requirements as detailed in the ethical standards:</p> <ul style="list-style-type: none"> ▶ Relationships between Ernst & Young, the audited body and senior management ▶ Services provided by Ernst & Young that may reasonably bear on the auditors' objectivity and independence ▶ Related safeguards ▶ Fees charged by Ernst & Young analysed into appropriate categories such as statutory audit fees, tax advisory fees, other non-audit service fees ▶ A statement of compliance with the ethical standards ▶ The audit committee should also be provided an opportunity to discuss matters affecting auditor independence 	<p>Audit Plan Report to those charged with governance</p>
<p>Going concern Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> ▶ Whether the events or conditions constitute a material uncertainty ▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▶ The adequacy of related disclosures in the financial statements 	<p>Report to those charged with governance</p>
<p>Significant deficiencies in internal controls identified during the audit</p>	<p>Report to those charged with governance</p>
<p>Certification work</p> <ul style="list-style-type: none"> ▶ Summary of certification work undertaken 	<p>Annual Report to those charged with governance summarising grant certification, and Annual Audit Letter if considered necessary</p>
<p>Fee Information</p> <ul style="list-style-type: none"> ▶ Breakdown of fee information at the agreement of the initial audit plan ▶ Breakdown of fee information at the completion of the audit 	<p>Audit Plan Report to those charged with governance and Annual Audit Letter if considered necessary</p>

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Ernst & Young LLP, 1 More London Place, London, SE1 2AF.

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