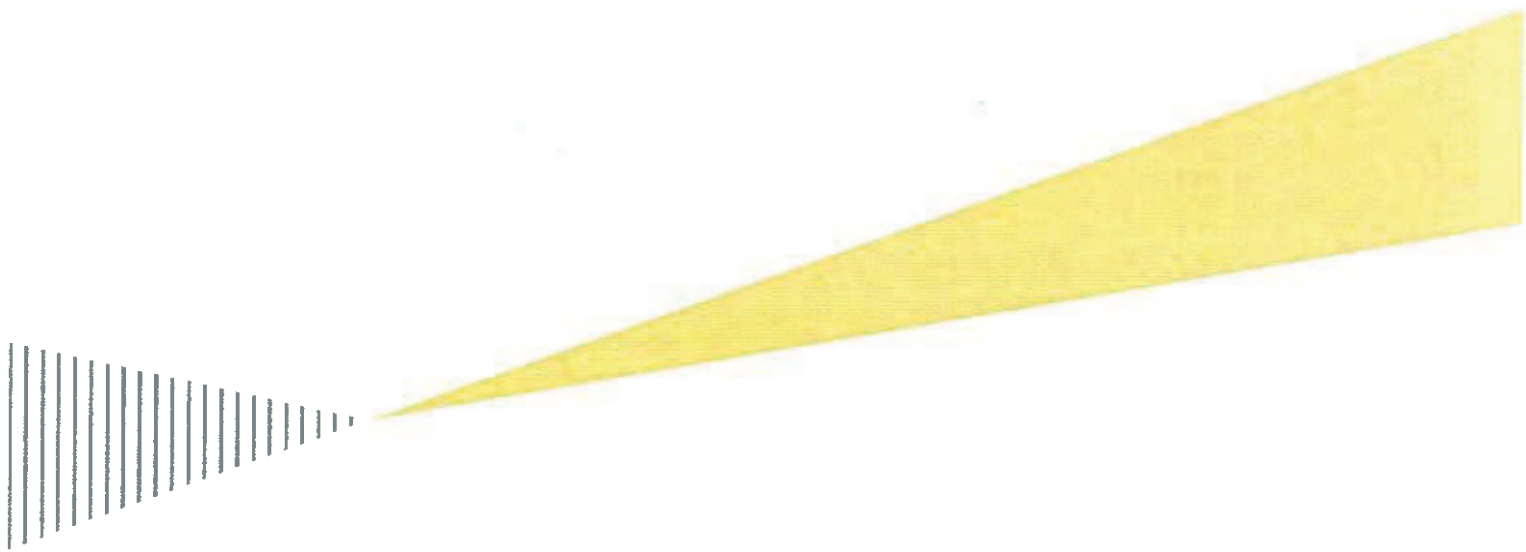


# Merton Council

Audit results report for the year ended 31 March 2013

FINAL October 2013

Ernst & Young LLP



**Private and confidential**  
Members of the General Purposes Committee  
Merton Council  
Civic Centre  
London Road  
Morden  
SM4 5DX

Dear Members

## **Audit results report**

We are pleased to attach our audit results report presented to the meeting of the General Purposes Committee on 26 September 2013. This report summarises our audit conclusion in relation to Merton Council's financial position and results of operations for 2012/13. We issued our final conclusion and opinion on 27 September 2013.

The audit is designed to express an opinion on the 2012/13 financial statements, reach a conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in the use of resources and address current statutory and regulatory requirements. This report contains our findings related to the areas of audit emphasis, our views on the Council's accounting policies and judgments and material internal control findings.

This report is intended solely for the information and use of the General Purposes Committee and the Council. It is not intended to be and should not be used by anyone other than these specified parties.

A copy of this report will be sent to the Audit Commission in accordance with the requirements of its Standing Guidance.

We discussed the contents of this report with you at the General Purposes Committee meeting on 26 September 2013.

Yours faithfully



David Wilkinson  
Partner  
For and on behalf of Ernst & Young LLP

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In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission.

The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

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

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

## 1. Overview of the financial statement audit

The Council is responsible for preparing and publishing its Statement of Accounts, accompanied by the Annual Governance Statement. In the Annual Governance Statement, the Council reports publicly on the extent to which they comply with their own code of governance, including how they have monitored and evaluated the effectiveness of their governance arrangements in the year, and on any planned changes in the coming period. The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

As auditors we are responsible for:

- ▶ Forming an opinion on the financial statements;
- ▶ Forming a conclusion on the arrangements that the Authority has in place to secure economy, efficiency and effectiveness in its use of resources; and
- ▶ Undertaking any other work specified by the Audit Commission.

Summarised below are the conclusions from all elements of our work:

### **Financial statements**

We issued an unqualified opinion on the Council's financial statements. Our main findings in relation to the areas of risk included in our Audit Plan are set out in Section 3 of the report.

### **Economy, efficiency and effectiveness**

We issued an unqualified value for money conclusion.

### **Whole of Government accounts**

We completed our report to the National Audit Office on the accuracy of the consolidation pack the Council is required to prepare for the Whole of Government Accounts. We had no issues to report.

### **Control themes and observations**

Our audit identified areas for improvement in: reconciliations between financial systems, linkage of budget monitoring reports to disclosures in the financial statements and monitoring school bank reconciliations. These are covered in Section 5.1 of this report.

There were no changes to the scope of our audit.

### **Summary of audit differences**

Our audit identified a number of misstatements in the accounts presented for audit, with the key items summarised below. Full details are in Section 8 of this report.

- 
- ▶ Removal of Bishopsford Academy from the Council's financial statements – reduction in assets of £11.74million. The Council has adjusted for this difference in the revised financial statements.
  - ▶ Transfer from usable reserves to unusable reserves of £2.465million due to incorrect treatment of the minimum revenue provision for the partial exemption element of two of the PFI-funded schools. The Council has adjusted for this difference in the revised financial statements.
  - ▶ The Council over-provided for bad debt provisions by £2 million on non-domestic rates (NDR) and £1.2million on council tax. The Council adjusted for council tax in the revised financial statements. No NDR adjustment is planned until 2013/14 when the position on collection rates and bad debts will become clearer. The Council sets out its position in the letter of representation at Appendix B.
-

## 2. Scope update

Our 2012/13 audit work has been undertaken in accordance with the Audit Plan issued on 4 March 2013 and is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

Our work comprises a number of elements. In our Audit Plan, we provided an overview of our audit scope and approach for the audit of the financial statements, our conclusion on the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources, and the work we are required to perform on the Whole of Government Accounts return.

We carried out our work in accordance with our Audit Plan.

### **Publication on electronic media**

The Council is responsible for the accurate presentation of the financial statements, audit report thereon and other reports submitted in relation to the audit and for establishing security and controls over them in order to ensure the continued integrity of the information presented. The examination of the controls over electronic presentation of audited financial information and reports by the auditor on the Council's web-site is beyond the scope of the audit of the financial statements.

### 3. Significant findings from the financial statement audit

In this section of our report we outline the main findings from our audit, including our conclusions on the areas of risk outlined in our Audit Plan.

#### Significant risks

##### Property, Plant and equipment (PPE)

- ▶ 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. We are aware of some areas for improvement identified in the 2010/11 audit with the Council's valuation process and documentation procedures.

##### Findings

- ▶ The Council carried out a prior period adjustment to account for investment properties not previously identified of £4.4million, and additional finance leases for properties of £3.97million. We reviewed and agreed these adjustments.

##### Pension fund liability

- ▶ Errors on pension fund valuations can lead to material misstatement. 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.

##### Findings

- ▶ Our review of the Council's pension liability did not identify any issues. The above position reflected the economic conditions in 2010; the next actuarial valuation will be based on the position in April 2013.

##### Private Finance Initiative (PFI) schemes

- ▶ The London Borough has a net book value of £63.7 million of PFI assets disclosed in its accounts as 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.

##### Findings

- ▶ As set out below, the Council needed to remove Bishopsford School from its property, plant and equipment assets following the school becoming an academy during 2012/13, an adjustment of £11.74 million.

#### Other financial statement risks:

##### Transfer of a PFI school to academy status

- ▶ Bishopsford School which is a PFI scheme school will become an academy during 2012/13. The transfer will require expert advice in order to agree valuation and accounting treatments.

##### Findings

- ▶ The financial statements presented for audit included Bishopsford School as an asset within property, plant and equipment in the balance sheet. We questioned this accounting treatment and the Council subsequently removed the school from the balance sheet. The adjustment was £11.74million, and we are content with the revised 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.

##### Findings

- ▶ Our review identified £0.66million of expenditure funded by Transport for London incorrectly treated as revenue expenditure charged to capital rather than as revenue expenditure. The Council adjusted the notes to the financial statements to reflect this. There is no effect on the expenditure disclosed in the income and expenditure statement.

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we include the following findings.

Other findings from our work

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**Non domestic rates provision for bad and doubtful debts**

- ▶ Based on previous collection rates, the Council over-provided for bad debt provisions by £2 million on non-domestic rates (NDR) and £1.2million on council tax. The Council has adjusted for council tax in the revised financial statements. However, given the uncertainty of the new non-domestic rating regime and the lack of clarity in accounting guidance, no NDR adjustment is planned until 2013/14 when the position on collection rates and bad debts will become clearer. The Council sets out its position in the letter of representation at Appendix B.

**Use of analytics tools for journal entry testing**

- ▶ We were unable to use our analytics tools to ensure the financial statements included all the Council's financial transactions and to direct our testing of journal entries raised in production of the financial statements.
  - ▶ We adopted alternative approaches to obtain assurance over the completeness of the financial statements and testing of journals.
- 

**Housing and council tax benefit parameters**

- ▶ Our review of the parameters set for housing and council tax benefit subsidy identified two not been updated since 2010. These errors had not been identified in prior periods.
  - ▶ These errors do not affect the financial statements. The Council is assessing the impact of these errors on its housing and council tax benefit subsidy claim.
-



## 4. Economy, efficiency and effectiveness

The Code of Audit Practice 2010 sets out our responsibility to satisfy ourselves that Merton Council has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. In examining the Council's corporate performance management and financial management arrangements we consider the following criteria and areas of focus specified by the Audit Commission:

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

The table below presents the findings of our work in response to the risk areas or areas of focus in our Audit Plan.

| Significant risks:   | Impacts arrangements for securing:                                       | Key findings:  |
|--|--|--|
| <p><b>2012/13 financial outturn and delivery of savings</b></p> <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> | <p>Financial resilience</p>  | <ul style="list-style-type: none"> <li>▶ We did not identify any areas which would lead to qualifying the financial resilience criterion.</li> <li>▶ <b>Improvement areas:</b></li> <li>▶ Keep core budgets under review, ensure there is a process of internal challenge as part of budget setting that challenges assumptions and supports robust revised in-year forecasting</li> <li>▶ Ensure in-year review of budgets identifies early changes that are reported to management and those charged with governance</li> <li>▶ Re-profile the capital programme in the light of consistent slippage on individual schemes and build realistic expectations into the medium term financial strategy and other shorter-term spending plans</li> </ul> |
| <p><b>Financial settlement 2013-15 and medium term financial plans (MTFPs)</b></p> <p>The full implications of the provisional local government finance settlement 2013-15 are still being assessed in detail by officers. Current estimates (January 2013) are that there is a potential £1 million gap (net of savings) for 2013/14. By 2016/17 this gap increases to £15 million. Robust savings plans will need to be developed to address the gaps identified to 2016/17.</p>                           | <p>Economy, efficiency and effectiveness</p> <p>Financial resilience</p> | <ul style="list-style-type: none"> <li>▶ We did not identify any areas which would lead to qualifying the economy, efficiency and effectiveness and financial resilience criteria</li> </ul>   |



**Transfer of Public Health (PH) role**

The 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.

Financial resilience

- ▶ We did not identify any areas which would lead to qualifying the financial resilience criterion.

## 5. Control themes and observations

As part of our work, we obtained sufficient understanding of internal control to plan our audit and determine the nature, timing and extent of testing. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you any significant deficiencies.

We have only reported here deficiencies we identified during the audit that we concluded are significant.

### 5.1 Current year observations

| Description  | Impact and Council's response  |
|--|--|
| Our work identified that, due to the large number of financial systems currently operated by the Council, monthly or quarterly reconciliations between many of the Council's main financial systems are not carried out. These include accounts receivable, accounts payable, Carefirst and a full reconciliation of bank and cash to the general ledger. These are reconciled instead at the financial year end only. | Problems with reconciliations place additional pressure on the financial closedown process. The Council's Finance team are carrying out monthly reconciliations and formal quarterly reviews of major financial systems in 2013/14. A more integrated suite of financial systems would reduce the number of reconciliations required.                          |
| There is a complex reconciliation required from the Cabinet Report on budget to outturn to the Note 29 subjective analysis in the financial statements.  | The reconciliation of the financial position shown in the financial statements to Cabinet reports is not straightforward. The Council should develop the presentation of reports to make clearer the financial movements from internal reporting to that disclosed in the Financial Statements (CIES and Note 29) and review presentation of service analysis. |
| We identified errors in bank reconciliations in six of 17 school bank reconciliations. All errors related to overstatement of cash due to cash inflows recognised on the Council's cashbook but not recognised in the bank statements.   | Refresher training is required for those who prepare and review the bank reconciliations to ensure that they have the necessary skills to create accurate reconciliations. Carry out a review of a sample of school bank reconciliations by internal audit until such time that schools' finance teams are more effective at preparing the reconciliations.    |
| We were unable to place reliance on the controls operating in your payroll system. This was due to issues identified by Internal Audit in a review of the implementation of the new payroll system introduced in April 2012.   | We carried out a programme of substantive testing to obtain assurance over the disclosure of payroll costs in your financial statements. There were no issues arising from our work.   |

### 5.2 Challenges for the coming year

| Description   | Impact  |
|---|---|
| The Council will need to manage the financial and activity consequences of taking on increased public health responsibilities.  | The respective responsibilities for the Council and healthcare providers in the local economy, and financial impact for the Council, are evolving. The Council will need to work closely with healthcare providers and other partners to ensure financial spending is matched to available resources. |
| The implications of the changes in the implementation of new arrangements for council tax benefit (localisation of council tax support) and the localisation of business rates could produce greater volatility and subsequent pressure on the Council's financial resources. | The Council will need to review its provisions to assess whether coverage is sufficient and adapt budgeting and forecasting accordingly.  |

The Council acknowledges it has a larger number of individual financial systems than equivalent councils and intends to move to a more integrated suite of systems.

This should improve efficiencies in the connectivity of systems and the processes for reconciliation of information flows.

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## **6. Status of our work**

### **6.1 Financial statement audit**

Our audit work for our opinion on the Authority's financial statements is complete. The annual accounts were approved by the General Purposes Committee and recertified by the Director of Corporate Services on 26 September 2013.

We issued an unqualified auditor's report on the Authority's financial statements on 27 September 2013.

### **6.2 Economy, efficiency and effectiveness**

Our work in respect of our conclusion on the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources is complete.

We issued an unqualified value for money conclusion in regard to the Council's arrangements to ensure economy, efficiency and effectiveness in its use of resources.

### **6.3 Objections and other questions received from members of the public**

We received no objections to the 2012/13 accounts from members of the public. We considered, and responded to, questions raised by one member of the public during 2012/13.

## 7. Fees update

A breakdown of our agreed fee is shown below.

|  | Proposed<br>final fee<br>2012/13<br>£ | Planned fee<br>2012/13<br>£ | Scale fee<br>2012/13<br>£ | Explanation<br>of variance |
|--|---------------------------------------|-----------------------------|---------------------------|----------------------------|
| <b>Total Audit Fee – Code work</b>         | <b>£188,730(**)</b>                   | £188,730                    | £188,730                  |                            |
| Certification of claims and<br>returns(**) | (**)                                  | £42,450                     | £42,450                   |                            |
| Non-audit work (provide details)           | 0                                     | 0                           | 0                         | See below                  |

*(\*) - Fees for the auditor's consideration of correspondence from the public and formal objections are charged in addition to the planned fee. There will be an additional fee in respect of our consideration and response to questions raised by a member of the public, which we will discuss and agree with the Council.*

*(\*\*) - Our fee for certification of grants and claims is yet to be finalised for 2012/13 and will be reported to those charged with governance in December 2013 within the Audit Certification Report for 2012/13.*

## 8. Summary of audit differences

In the normal course of any audit, we identify differences between amounts we believe should be recorded in the financial statements and amounts actually recorded. These differences are classified as either 'known' or 'judgemental'. Known differences represent items that can be accurately quantified and relate to a definite set of facts or circumstances. Judgemental differences generally involve estimation and relate to facts or circumstances that are uncertain or open to interpretation.

We have included all amounts greater than £240,000 relating to Merton Council in our summary of misstatements below.

We highlight in particular the following misstatements identified during the course of our audit that have been corrected by management:

- ▶ exclusion of Bishopsford School from property, plant and equipment - £11.74million reduction
- ▶ movement of £2.465million of usable reserves to the Capital Adjustment Account in unusable reserves to adjust for the minimum revenue provision for the partial exemption element for two of the PFI-funded schools
- ▶ overstatement of GLA precept of £1.1million
- ▶ overstatement of the provision for bad and doubtful debts for council tax of £1.2million, of which £0.941 relates directly to the Council
- ▶ removal of £661,000 of grant under Revenue Expenditure Funded Covered Under Statute to revenue expenditure and removal from notes to the financial statements
- ▶ increase in debtor and creditor balances from incorrect inclusion of a Pension Fund debtor within creditors of £377,000
- ▶ amendment of Note 39 - grant income to include correct treatment of relevant grants.

The Council also amended the analysis of financial instruments in Notes 16, 19 and 22 of the revised financial statements. These amendments were presented to the General Purposes Committee on 26 September 2013. We reviewed and agreed these changes.



We also highlight the following misstatements which were not corrected by management:

- ▶ based on previous collection rates, the Council over-provided for bad debt provisions by £2 million on non-domestic rates (NDR). Given the uncertainty of the new non-domestic rating regime and the lack of clarity in accounting guidance, no NDR adjustment is planned until 2013/14 when the position on collection rates and bad debts will become clearer. The Council sets out its position in the letter of representation at Appendix B. The impact of this is shown in the table below;
- ▶ the Council has also not adjusted the prior year figure (as at 31/3/2012) for the overstatement of provision for bad and doubtful debt in relation to council tax. The Council sets out its position in the letter of representation at Appendix B

|  | Assets<br>current  | Assets<br>non-<br>current | Liabilitie<br>s<br>current | Liabilitie<br>s non-<br>current | Income                                  | Expense<br>s                            |
|--|--------------------|---------------------------|----------------------------|---------------------------------|---|---|
|  | Debit/<br>(Credit) | Debit/<br>(Credit)        | Debit/<br>(Credit)         | Debit/<br>(Credit)              | Debit/<br>(Credit)<br>Current<br>period | Debit/<br>(Credit)<br>Current<br>period |
| Uncorrected misstatements  | £000               | £000                      | £000                       | £000                            | £000                                    | £000                                    |
| <b>Known differences:</b>  |                    |                           |                            |                                 |   |   |
| ▶ None   |                    |                           |                            |                                 |   |   |
| <b>Judgemental differences:</b>  |                    |                           |                            |                                 |   |   |
| ▶ No amendment to the bad and doubtful debt provision for non-domestic rates | 2000               |                           | 2000                       |                                 |   |   |
| <b>Balance sheet totals</b>  | <b>2000</b>        |                           | <b>2000</b>                |                                 |   |   |
| <b>Income effect of uncorrected misstatements</b>                            |                    |                           |                            |                                 |   |   |
| Cumulative effect of uncorrected misstatements before turnaround effect      | 2000               |                           | 2000                       |                                 |   |   |
| Turnaround effect. See note 1 below  | 0                  | 0                         | 0                          | 0                               | 0                                       | 0                                       |
| Cumulative effect of uncorrected misstatements, after turnaround effect      | 2000               | 0                         | 2000                       | 0                               |   | 0                                       |

We identified no amounts - individually or in aggregate - material to the presentation and disclosures of the financial statements for the year ended 31 March 2013.

Note 1: turnaround effect is the impact of uncorrected misstatements identified in the prior period, on results of the current period.

## 9. Independence confirmation: update

We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated 4 March 2013. We complied with the Ethical Standards for Auditors and the requirements of the Standing Guidance and in our professional judgement the firm is independent, and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter that should be reviewed by both you and us. It is therefore important that you consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the General Purposes Committee on 26 September 2013. No issues were raised at that meeting.

## Appendix A Required communications with the General Purposes Committee

We must provide certain communications to the General Purposes Committee. These are:

| Required communication   | Reference  |
|--|--|
| <b>Terms of engagement</b>   | The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. |
| <b>Planning and audit approach</b><br>Communication of the planned scope and timing of the audit including any limitations.  | Audit Plan   |
| <b>Significant findings from the audit</b>   | Audit results report   |
| <ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters, if any, significant to the oversight of the financial reporting process</li> <li>▶ Findings and issues regarding the opening balance on initial audits</li> </ul> |  |
| <b>Misstatements</b>   | Audit results report   |
| <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements relating to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ In writing, corrected significant misstatements</li> </ul>  |  |
| <b>Fraud</b>   | Audit results report   |
| <ul style="list-style-type: none"> <li>▶ Enquiries of the audit committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the Authority</li> <li>▶ Any fraud we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>  |  |
| <b>Related parties</b>   | Audit results report   |
| Significant matters arising during the audit in connection with the Authority's related parties including, when applicable:  |  |
| <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the Authority</li> </ul>  |  |
| <b>External confirmations</b>  | Audit results report   |
| <ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>   |  |

| Required communication   | Reference   |
|--|---|
| <p><b>Consideration of laws and regulations</b></p> <ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ 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 committee may be aware of</li> </ul>  | Audit results report                                      |
| <p><b>Independence</b></p> <p>Communication of all significant facts and matters that bear on Ernst &amp; Young's objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul> | Audit Plan and update in section 8 of this report         |
| <p><b>Going concern</b></p> <p>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"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>  | Audit results report                                      |
| <p><b>Significant deficiencies in internal controls identified during the audit</b></p>  | Audit results report                                      |
| <p><b>Opening Balances (initial audits only)</b></p> <ul style="list-style-type: none"> <li>▶ Findings and issues regarding the opening balance of initial audits</li> </ul>   | Audit results report                                      |
| <p><b>Fee reporting</b></p> <ul style="list-style-type: none"> <li>▶ Final, planned and scale fee broken down into the headings of Code audit work; certification of claims and returns; and any non-audit work (or a statement to confirm that no non-audit work has been undertaken for the Authority).</li> </ul>   | Audit Plan and Audit results report                       |
| <p><b>Summary of certification work undertaken</b></p> <ul style="list-style-type: none"> <li>▶ Annual report to those charged with governance summarising the certification work undertaken</li> </ul>  | Annual Certification Report – to be issued December 2013. |

## Appendix B Letter of representation

[To be prepared on the entity's letterhead]

*[Date]*

Ernst & Young LLP  
Apex Plaza  
Forbury Road  
Reading  
Berkshire RG1 1YE

This representation letter is provided in connection with your audit of the financial statements of Merton Council ("the Council") for the year ended 31 March 2013. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the financial statements give a true and fair view of the financial position of Merton Council as of 31 March 2013 and of its expenditure and income for the year then ended in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

We understand that the purpose of your audit of our financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK and Ireland), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

### **Financial Statements and Financial Records**

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the financial statements in accordance with the Accounts and Audit Regulations (England) 2011 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.
2. We acknowledge our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above give a true and fair view of the financial position, and of its expenditure and income of the Council in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 and are free of material misstatements, including omissions. We have approved the financial statements.
3. The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.
4. We believe that the Council has a system of internal controls adequate to enable the preparation of accurate financial statements in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 that are free from material misstatement, whether due to fraud or error.
5. We believe that the effects of any unadjusted audit differences, summarised in the accompanying schedule, accumulated by you during the current audit and pertaining to

the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. We have not corrected these differences identified by and brought to the attention from the auditor because

- We have reviewed the position on NNDR collection and provisions. While we note the view of the External Auditor, we feel that this is based upon a backward look at the old collection regime and does not reflect the potential impact of the new NNDR system. A new series of reliefs have to be introduced, collection rates have systematically fallen for the last few years, the provision required for valuation appeals is still uncertain and the accounting treatment for the collection fund remains unclear. On this basis it is proposed to leave the bad debt provision unchanged in 2012/13 and review the entire treatment of the NNDR collection fund and accounting in 2013/14”
- On the Council Tax bad debt provision our position is that the adjustment of the Council Tax bad debt provision was made in 2012/13 rather than 2011/12 because the amounts involved were not sufficient (or material) to justify a prior period adjustment.

### **Fraud**

1. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.
2. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
3. We have no knowledge of any fraud or suspected fraud involving management or other employees who have a significant role in the Council's internal controls over financial reporting. In addition, we have no knowledge of any fraud or suspected fraud involving other employees in which the fraud could have a material effect on the financial statements. We have no knowledge of any allegations of financial improprieties, including fraud or suspected fraud, (regardless of the source or form and including without limitation, any allegations by “whistleblowers”) which could result in a misstatement of the financial statements or otherwise affect the financial reporting of the Council.

### **Compliance with Laws and Regulations**

1. We have disclosed to you all known actual or suspected noncompliance with laws and regulations whose effects should be considered when preparing the financial statements.

### **Information Provided and Completeness of Information and Transactions**

1. We have provided you with:
  - Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters as agreed in terms of the audit engagement.
  - Additional information that you have requested from us for the purpose of the audit and
  - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
2. All material transactions have been recorded in the accounting records and are reflected in the financial statements.



3. We have made available to you all minutes of the meetings of the Council, and General Purposes Committee (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meeting on the following date: 27 June 2013.
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Council's related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the financial statements.
5. We have disclosed to you, and the Council has complied with, all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

#### **Liabilities and Contingencies**

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the financial statements.
2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in Note 49 to the financial statements all guarantees that we have given to third parties.

#### **Subsequent Events**

1. Other than described in Note 6 to the financial statements, there have been no events subsequent to period end which require adjustment of or disclosure in the financial statements or notes thereto.

#### **Accounting Estimates**

1. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
2. Accounting estimates recognised or disclosed in the financial statements:
  - We believe the measurement processes, including related assumptions and models, we used in determining accounting estimates is appropriate and the application of these processes is consistent.
  - The disclosures relating to accounting estimates are complete and appropriate in accordance with the applicable financial reporting framework.
  - The assumptions we used in making accounting estimates appropriately reflects our intent and ability to carry out specific courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures.
  - No subsequent event requires an adjustment to the accounting estimates and disclosures included in the financial statements.

### **Retirement benefits**

1. On the basis of the process established by us and having made appropriate enquiries, we are satisfied that the actuarial assumptions underlying the scheme liabilities are consistent with our knowledge of the business. All significant retirement benefits and all settlements and curtailments have been identified and properly accounted for.

### **Comparative information – when the comparative information has been restated (in the form of a prior year adjustment)**

The Council has restated the Balance Sheet and Notes 8, 10, 14, 16, 19, 22, 25 and 29 to the statements to reflect adjustment to investment properties and finance leases held by the Council. The comparative amounts have been correctly restated to reflect the above matters and appropriate note disclosure of these restatements have also been included in the current year's financial statements.

### **Segmental reporting**

1. I have reviewed the operating segments reported internally to the Authority and I am satisfied that it is appropriate to aggregate these as, in accordance with IFRS 8: Operating Segments, they are similar in each of the following respects:
  - The nature of the services
  - The nature of the processes
  - The type or class of customer for the services

### **Environmental Liabilities**

2. We have disclosed to you all liabilities or contingencies arising from environmental matters. These liabilities or contingencies have been recognised, measured and disclosed, as appropriate, in the financial statements. The environmental liability(ies) included in the balance sheet(s) represents our best estimate of the potential loss(es) using assumptions that we believe represent the expected outcomes of the uncertainties. With respect to the valuation of related assets, we have considered the effect of environmental matters, and the carrying value of the relevant assets is recognised, measured and disclosed, as appropriate, in the financial statements. Any commitments related to environmental matters have been measured and disclosed, as appropriate, in the financial statements.

### **Ownership of Assets**

1. Except for assets capitalised under finance leases, the Council has satisfactory title to all assets appearing in the balance sheet(s), and there are no liens or encumbrances on the Council's assets, nor has any asset been pledged as collateral, other than those that are disclosed in Note 12 to the financial statements. All assets to which the Council has satisfactory title appear in the balance sheet(s).
2. All agreements and options to buy back assets previously sold have been properly recorded and adequately disclosed in the financial statements.
3. We have no plans or intentions that will result in any excess or obsolete inventory, and no inventory is stated at an amount in excess of net realizable value.
4. There are no formal or informal compensating balance arrangements with any of our cash and investment accounts. Except as disclosed in the Notes to the financial statements, we have no other line of credit arrangements.

**Reserves**

1. We have properly recorded or disclosed in the financial statements the useable and unusable reserves.

**Purchase and Sales Commitments and Sales Terms**

1. Losses arising from purchase and sales commitments have been properly recorded and adequately disclosed in the financial statements.
2. At the year end, the Council had no unusual commitments or contractual obligations of any sort which were not in the ordinary course of business and which might have an adverse effect upon the company (e.g., contracts or purchase agreements above market price; repurchase or other agreements not in the ordinary course of business; material commitments for the purchase of property, plant and equipment; significant foreign exchange commitments; open balances on letters of credit; purchase commitments for inventory quantities in excess of normal requirements or at prices in excess of the prevailing market prices; losses from fulfilment of, or inability to fulfil, sales commitments, etc.).

**Income and Indirect Taxes**

1. We acknowledge our responsibility for the tax accounting methods adopted by the Council which have been consistently applied in the current period.

**Use of the Work of an Expert**

1. We agree with the findings of the experts engaged to evaluate the IAS19 disclosures of the Pension Fund and disclosure of property, plant and equipment and have adequately considered the qualifications of the experts in determining the amounts and disclosures included in the financial statements and the underlying accounting records. We did not give or cause any instructions to be given to the experts with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an effect on the independence or objectivity of the experts.

*Yours Faithfully,*

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Director of Corporate Services

I confirm that this letter has been discussed and agreed at the General Purposes Committee on 26 September 2013

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Chairman of General Purposes Committee

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