

Cherwell District Council

Annual Audit Letter for the year
ended 31 March 2019

February 2020

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow triangle is positioned above the 'Y'.

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Contents



Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psa.co.uk).

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

The 'Terms of Appointment (updated April 2018)' issued by PSAA set out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

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

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



01 Executive Summary



Executive Summary

We are required to issue an annual audit letter to Cherwell District Council (the Council) following completion of our audit procedures for the year ended 31 March 201[X]. Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's: ▶ Financial statements	Unqualified - the financial statements give a true and fair view of the financial position of the Council as at 31 March 2019 and of its expenditure and income for the year then ended
▶ Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts
Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We concluded that you have proper arrangements to secure value for money in your use of resources

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

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

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 31 July 2019.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 14 February 2020.



02 Purpose and Responsibilities

Purpose and Responsibilities

The Purpose of this Letter

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

We have already reported the detailed findings from our work in our 2019/20 Audit Results Report to the 31 July 2019 Accounts, Audit and Risk Committee, which represents those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

Responsibilities of the Appointed Auditor

Our 2018/19 audit work was undertaken in accordance with the Audit Plan issued on 23 January 2019 and conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
 - ▶ on the 2018/19 financial statements; and
 - ▶ on the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
 - ▶ if the annual governance statement is misleading or not consistent with our understanding of the Council;
 - ▶ any significant matters in the public interest;
 - ▶ any written recommendations to the Council which should be copied to the Secretary of State; and
 - ▶ whether we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on the Council's Whole of Government Accounts return. The Council is below the specified audit threshold of £500m, so we did not perform any audit procedures on the return.

Responsibilities of the Council

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

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



03

Financial Statement Audit

Financial Statement Audit

Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health. We audited the Council [and Pension Fund]'s Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office and issued an unqualified audit report on 14 February 2020. Our detailed findings were reported to the 31 July 2019 Accounts, Audit and Risk Committee.

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

Significant Risk	Conclusion
Misstatements due to fraud or error	We obtained a full list of journals posted to the general ledger during the year, and analysed these journals using criteria we set to identify any unusual journal types or amounts. We then tested a sample of journals that met our criteria and tested these to supporting documentation.
The financial statements as a whole are not free of material misstatements whether caused by fraud or error.	We considered the accounting estimates most susceptible to bias.
As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.	We evaluated the business rationale for any significant unusual transactions. We have not identified any material weaknesses in controls or evidence of material management override. We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business.

Financial Statement Audit (cont'd)

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

Significant Risk	Conclusion
<p>Risk of fraud in revenue and expenditure recognition</p> <p>Auditing standards also required us to presume that there is a risk that revenue and expenditure may be misstated due to improper recognition or manipulation.</p> <p>We considered this presumed risk in relation to those significant income streams and areas of expenditure which could be subject to manipulation, and identified the following area of risk:</p> <ul style="list-style-type: none"> - inappropriate capitalisation of revenue expenditure. <p>Linking to our risk of misstatements due to fraud and error above, we have considered the capitalisation of revenue expenditure on property, plant and equipment as a specific area of risk given the extent of the Council's capital programme</p>	<p>We carried out sample testing additions to property, plant and equipment to ensure that they have been correctly classified as capital and included at the correct value in order to identify any revenue items that have been inappropriately capitalised.</p> <p>We Included the risk of fraud in revenue expenditure recognition as a significant risk in our instructions to the auditors to Graven Hill Village Development Company Limited. We reviewed the work they did in relation to this risk.</p> <p>In conclusion:</p> <ul style="list-style-type: none"> • We have not identified any material weaknesses in controls or evidence of material management override. • We have not identified any instances of inappropriate judgements being applied. • We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business
<p>Valuation and classification of Castle Quay</p> <p>The fair value of the Castle Quay development represents a significant balance in the Council's group Statement of Accounts.</p> <p>The asset is subject to an annual revaluation, and management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end value recorded in the balance sheet.</p> <p>2018/19 sees the Castle Quay project entering its second phase.</p>	<p>We considered the work performed by the Council's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work. We used specialist support from our Real Estate team to support our testing of the valuation.</p> <p>We tested and challenged the information and assumptions used by the valuers in performing their valuation.</p> <p>We liaised with our specialist Real Estate team on their review of the valuation of Castle Quay.</p> <p>Our specialists concluded that the valuation in the financial statement falls within an acceptable range, and did not identify any evidence that would contradict the valuer's significant assumptions. They have however identified areas for improvement in the valuation methodology in future. These include:</p> <ul style="list-style-type: none"> - Current net rent was used without a robust assessment of anticipated future income. We would not expect this, particularly in view of the pressures on retail sector and downward pressure on both capital and rental values - The information we reviewed did not include total floor areas or market rents, so our specialist was unable to carry out full review procedures on individual valuation inputs.

Financial Statement Audit (cont'd)

Other Key Findings	Conclusion
<p data-bbox="91 355 450 384">Valuation of Land and Buildings</p> <p data-bbox="91 443 786 643">The fair value of Property, Plant and Equipment (PPE) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Management is required to make material judgemental inputs and apply estimation techniques to calculate the year-end balances recorded in the balance sheet.</p>	<p data-bbox="786 355 853 384">We:</p> <ul data-bbox="786 392 2145 778" style="list-style-type: none"> • considered the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work; • sample tested key asset information used by the valuers in performing their valuation (e.g. floor plans to support valuations based on price per square metre); • considered the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for PPE and annually for IP. We also considered if there are any specific changes to assets that have occurred and that these have been communicated to the valuer; • reviewed assets not subject to valuation in 2018/19 to confirm that the remaining asset base is not materially misstated; • considered changes to useful economic lives as a result of the most recent valuation; and • tested that accounting entries have been correctly processed in the financial statements,
<p data-bbox="91 946 394 975">Pension Liability Valuation</p> <p data-bbox="91 983 786 1126">The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Cherwell District Council.</p> <p data-bbox="91 1134 786 1246">The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2019 this came to £207 million.</p> <p data-bbox="91 1254 786 1302">The information disclosed is based on the IAS19 report issued to the Council by the actuary to the County Council.</p> <p data-bbox="91 1310 786 1477">Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.</p> <p data-bbox="91 1485 786 1533">The Council re-ran the actuary's report to take account of the McCloud case.</p>	<p data-bbox="786 946 853 975">We:</p> <ul data-bbox="786 983 2145 1422" style="list-style-type: none"> • liaised with the auditors of Oxfordshire Pension Fund to obtain assurances over the information supplied to the actuary in relation to Oxfordshire County Council; • assessed the work of the Pension Fund actuary (Hyman Robertson) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team; and • reviewed and tested the accounting entries and disclosures made within the Council's financial statements in relation to IAS19. • The Council has amended its financial statements to take account of the implications of the McCloud case, brought to address the impact of historical age discrimination in the treatment of pensioners. This decision came through in late June, after the statements were originally drafted. The effect is to increase expenditure by £0.855m, This is a national issue affecting many public sector bodies. The Council's actuary have advised that the impact of GMP is not material. We have corroborated the actuary's view that there is no material impact.

Financial Statement Audit (cont'd)

Other Key Findings	Conclusion
<p>Completion of financial statements</p> <p>We halted the audit when we had completed our work but awaited the opinion on one of the Council's significant components, Crown House Limited. This was delayed because of the need to investigate the arrangements by which the company had initially been set up, and how it disclosed its equity.</p> <p>£5.6m loans were being disclosed as share capital. Baldwins (the external auditors) were querying both the technical issues of accounting methodology, and the legal advice received. They liaised with us. We agreed that we could not conclude our audit of the group statements until they had completed their work. We are also required to perform detailed review procedures where we rely on the work of other component auditors. This meant that our review also needed to look into these areas of concern and go into more detail for us to gain the necessary assurance.</p> <p>Baldwins concluded their work and gave an opinion in December 2019. The statements required significant amendments. We reviewed their work in January 2020.</p>	<p>We liaised with Baldwins in advance using a detailed planning memorandum to lay out expectations. Baldwins informed us of their progress and concerns with the issues they raised.</p> <p>When completed, we reviewed the work carried out by Baldwins as the external auditors of the Crown House Ltd component to ensure that we could rely on it for our purposes. Our review was done at a level of detail which allowed us to rely on what they had done. Because of the wider issues which needed to be considered, this review was both wider and in more depth than in previous years.</p> <p>We concluded that Baldwins had performed their audit work in such a way that we could rely on it for our purposes.</p>
<p>We then completed the final stage of the audit by checking the draft statements to the final version. This was a more complex process than usual as amendments had been made some months before: the audit trail was complicated and in some cases had to be reconstructed by the finance department.</p> <p>There were also difficulties with version control in order to follow the amendments through between correct versions of the statements.</p>	<p>We were able to trace all amendments from the draft version of the statements to the final signed version.</p> <p>However we note that it took much longer than usual to complete the process.</p> <p>We are confident that finance staff have picked up the issues and included them in their closedown timetable and processes for the 2019/20 year of audit.</p>

Financial Statement Audit (cont'd)

Our application of materiality

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

Item	Thresholds applied
Planning materiality	We determined planning materiality as £2.409m (2017/18: £0.948m), which is 2% of gross expenditure on provision of services reported in the accounts. In 2017/18 it was 1% because of risks identified in 2016/17; in 2018/19 we were able to increase the percentage to the maximum allowed. We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council
Reporting threshold	We agreed with the Accounts, Audit and Risk Committee that we would report to the Committee all audit differences in excess of £0.122m (2017/18: £0.047m)

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

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

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

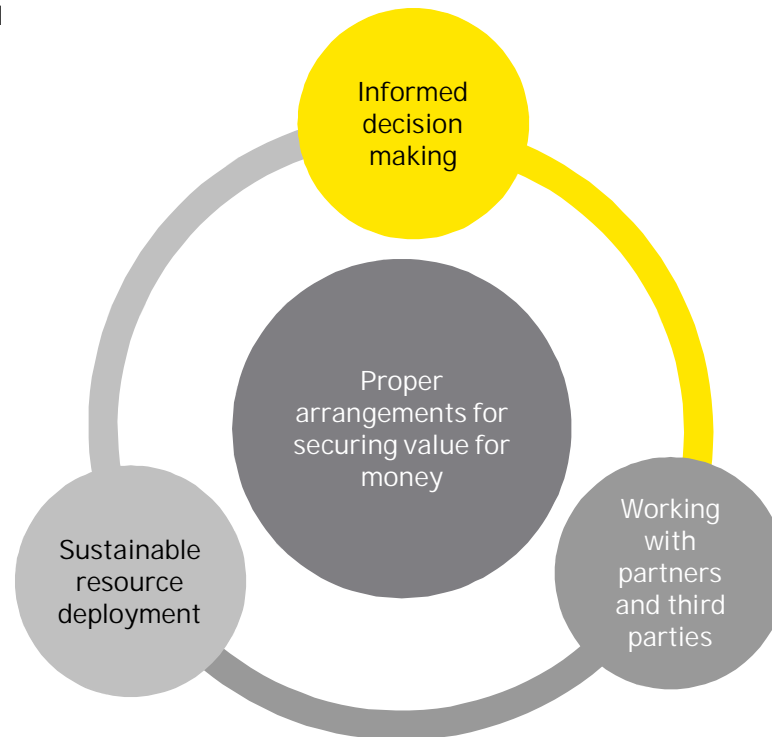


04 Value for Money

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness in its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- ▶ Take informed decisions;
- ▶ Deploy resources in a sustainable manner; and
- ▶ Work with partners and other third parties.



We did not identify any significant risks around these criteria at the planning stage. However we reviewed the Council's financial resilience by completing a quantitative and qualitative assessment of the Council's budget, medium term financial strategy and capital, treasury management strategies produced in the period to 31 March 2019.

We also reviewed how the Council has responded to the weaknesses in arrangements that led to a qualification of our Value for Money Conclusion in the 2017/18 financial year. This considered the arrangements the Council now has to support its decision-making on any future investment and commercial decisions.

Value for Money (cont'd)

We therefore issued an unqualified value for money conclusion on 14 February 2020

Key Findings	Conclusion
<p>We reviewed how the Council has responded to the weaknesses in arrangements that led to a qualification of our Value for Money Conclusion in the 2017/18 financial year. This considered the arrangements the Council now has to support its decision-making on any future investment and commercial decisions.</p>	<p>Our review of these arrangements identified that the Council had taken the 2017/18 weaknesses into account in its decision-making processes during 2018/19.</p>
<p>We reviewed the work of our Real Estates specialist team on the Castle Quay valuation, which was the subject of a qualification to the VFM conclusion in 2017/18.</p>	<p>Our specialists have made some suggestions for improving the methodology, but considered that the valuation received by the Council fell within the expected range. There were no concerns for our value for money conclusion</p>



05

Other Reporting Issues



Other Reporting Issues

Whole of Government Accounts

We must perform the procedures specified by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes. The Council is below the specified audit threshold of £500m, so we were not required to perform any audit procedures on the consolidation pack.

Annual Governance Statement

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

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

Report in the Public Interest

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

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

Written Recommendations

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

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

Other Reporting Issues (cont'd)

Objections Received

We did not receive any objections to the 2018/19 financial statements from members of the public.

Other Powers and Duties

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

Independence

We communicated our assessment of independence in our Audit Results Report to the Accounts, Audit and Risk Committee on 31 July 2019. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

Control Themes and Observations

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

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

When we issued our Audit Results Report on 31 July 2019, we were awaiting the results of the work being done by the external auditors on the Crown House component of the group statements. They have since reported that there were issues with how the financing of Crown House was initially recorded. There was a discrepancy between the company register and Registry records (the error being in the company's books): Crown House financial statements needed to be amended for £5.6m share equity which should have been disclosed as loans, as in previous years.

We asked for representations from management to confirm the Council's ongoing financial commitment to CHB Ltd, as the company was reliant on the Council and otherwise this would affect going concern.

We also requested a post-balance sheet event on the rectification of the share certificate.

We note that the Council has carried out the work necessary to correct the disclosures from previous years. There were governance issues around how the company was initially set up, but these have been reviewed and the position clarified as at 31 March 2019.

We observe that the weaknesses identified by Baldwins arose from the issues we raised in our 2017/18 VFM conclusion qualification, i.e. the Council's due diligence processes on the acquisition of the company. This was an area outside the Council's experience, and there were shortcomings in the knowledge and expertise available internally to the Council. This is a complex area where more specialised skills and capability are likely to be required. The Council has decided that it will engage more specialised advice in future if it considers buying a company again. However it is unlikely to do this, at least in the short term.



06

Focused on your future



Focused on your future

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

Standard	Issue	Impact
IFRS 16 Leases	<p>It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2020/21 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard and although the 2020/21 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.</p>	<p>Until the 2020/21 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However it is clear that the Council will need to undertake a detailed exercise to identify all its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.</p>
IASB Conceptual Framework	<p>The revised IASB Conceptual Framework for Financial Reporting (Conceptual Framework) will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>This introduces;</p> <ul style="list-style-type: none"> - new definitions of assets, liabilities, income and expenses - updates for the inclusion of the recognition process and criteria and new provisions on derecognition - enhanced guidance on accounting measurement bases - enhanced objectives for financial reporting and the qualitative aspects of financial information. <p>The conceptual frameworks is not in itself an accounting standard and as such it cannot be used to override or disapply the requirements of any applicable accounting standards.</p> <p>However, an understanding of concepts and principles can be helpful to preparers of local authority financial statements when considering the treatment of transactions or events where standards do not provide specific guidance, or where a choice of accounting policies is available.</p>	<p>It is not anticipated that this change to the Code will have a material impact on Local Authority financial statements.</p> <p>However, Authorities will need to undertake a review to determine whether current classifications and accounting remains valid under the revised definitions.</p>



07

Audit Fees

Audit Fees

Our fee for 2018/19 is in line with the scale fee set by the PSAA / as agreed with your in our Engagement Letter and reported in both our Audit Planning Report and Annual Results Report. We identified that there would be some areas over and above the scale fee and disclosed an estimate in these documents. We now include a final figure for these and for the extra work required for us to give an opinion. The final fees are subject to approval by PSAA Ltd.

8NB the claims and returns original fee was for the base certification work and excluded any extended testing that might be required. This approach was agreed in our separate Engagement Letter. In the event, we needed to perform seven areas of extended testing.

Description	Final Fee 2018/19 £	Planned Fee 2018/19 £	Scale Fee 2018/19 £	Final Fee 2017/18 £
Total Audit Fee – Code work	40,138	56,138*	40,138	52,127
Scale fee variations				
Impact of lower materiality level	0			12,500
Castle Quay valuation significant risk	6,000			7,850
Value for money significant risk	0			8,800
Area of audit focus: group considerations	15,000			9,600
Testing of PPE valuations/ errors in draft statements	5,000			N/A
Total Audit Fee	65,138			90,877
Non-audit work – Claims and returns	21,500*	4,500	N/A	8,844

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