

# *Internal Audit Annual Report 2015/2016*

**Cherwell District  
Council**

**June 2016**

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## Distribution List

For action and information:	Paul Sutton – Chief Finance Officer and S151 Officer
	Joint Management Team
	Accounts, Audit and Risk Committee

This document has been prepared only for Cherwell District Council and solely for the purpose and on the terms agreed with Cherwell District Council.

# 1. Executive summary

## Introduction

This report outlines the internal audit work we have carried out for the year ended 31 March 2016.

The Public Sector Internal Audit Standards require the Head of Internal Audit to provide an annual opinion, based upon and limited to the work performed, on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control (i.e. the organisation's system of internal control). This is achieved through a risk-based plan of work, agreed with management and approved by the Accounts, Audit and Risk Committee, which should provide a reasonable level of assurance, subject to the inherent limitations described below and set out in Appendix 1. The opinion does not imply that Internal Audit has reviewed all risks relating to the organisation.

The Accounts, Audit and Risk Committee agreed to a level of internal audit input of £47,355.

Internal audit work was performed in accordance with PwC's Internal Audit methodology which is in conformance with the Public Sector Internal Audit Standards.

## Head of Internal Audit Opinion

We are satisfied that sufficient internal audit work has been undertaken to allow an opinion to be given as to the adequacy and effectiveness of governance, risk management and control. In giving this opinion, it should be noted that assurance can never be absolute. The most that the internal audit service can provide is reasonable assurance that there are no major weaknesses in the system of internal control.

## Opinion

Our opinion is as follows:

Satisfactory	<b>Generally satisfactory with some improvements required</b>	Major improvement required	Unsatisfactory
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Defined as:

- Medium risk rated weaknesses identified in individual assignments that are *not significant in aggregate* to the system of internal control; and/or
- High risk rated weaknesses identified in individual assignments that are *isolated* to specific systems or processes; and
- None of the individual assignment reports have an overall classification of critical risk.

Implications of conclusion:

Governance, risk management and control in relation to business critical areas is generally satisfactory. However, there are some areas of weakness and non-compliance in the framework of governance, risk management and control which potentially put the achievement of objectives at risk.

Some improvements are required in those areas to enhance the adequacy and effectiveness of the framework of governance, risk management and control. Please see our Summary of Findings in Section 2.

An explanation of all the types of opinion that may be given can be found in Appendix 2.

## Basis of opinion

Our opinion is based on:

- All audits undertaken during the year.

- Any follow up action taken in respect of audits from previous periods.
- Any significant recommendations not accepted by management and the resulting risks.
- The effects of any significant changes in the organisation's objectives or systems.
- Any limitations which may have been placed on the scope or resources of internal audit.
- The proportion of the organisation's audit needs have been covered to date.
- Any reliance that is placed upon third party assurances.

The commentary below provides the context for our opinion and should be read together with the opinion in its entirety.

### **Commentary**

The key factors that contributed to our opinion are summarised as follows:

- No pervasive high or critical risk findings individually or in aggregate per report rating.
- All findings were generally medium or low risk rating.

There was also an investigation and report issued by KPMG in relation to weaknesses identified at the Council about an historical issue over collectability of its NNDR income, resulting in a Joint Finance Improvement Plan that has been put in place at both Cherwell and South Northants councils.

We undertook two additional pieces of work, focussed on the council's reconciliations and specific process around income/accounting debtors and aged debt, and found no additional matters that were not previously identified by the earlier report that indicate any further significant breakdown in council controls and processes.

We also note:

- a similar level of medium risk issues and the relatively low (albeit somewhat increased) low level risk findings raised; and
- the generally positive position on implementation of previous year's recommendations.

Please see sections two to four of this report.

### ***Acknowledgement***

We would like to take this opportunity to thank Cherwell District Council staff, for their co-operation and assistance provided during the year.

## 2. Summary of findings

Our annual internal audit report is timed to inform the Council's Annual Governance Statement.

A summary of key findings from our programme of internal audit work for the year work is recorded in the table below:

<i>Description</i>	<i>Detail</i>
<p><b>Overview</b></p> <p>We completed 8 internal audit reviews. This resulted in the identification of 34 findings to improve weaknesses in the design of controls and / or operating effectiveness. Refer to section 3 of this report for further details.</p>	<p>In addition we have carried out the following value enhancement/specialist reviews and additional pieces of work where no risk rating has been provided.</p> <ul style="list-style-type: none"> <li>• Year-end finance support</li> <li>• Risk Management training</li> </ul> <p>We also delivered additional reviews, following a request by management, in relation to report issued by KPMG that was specific to Cherwell District Council and has resulted in a Joint Finance Improvement Plan that has been implemented across both councils.</p> <p>These reviews were in relation to:</p> <ul style="list-style-type: none"> <li>• Council reconciliations</li> <li>• Income/accounting debtors and aged debt monitoring</li> </ul>
<p><b>Internal Control Issues</b></p> <p>During the course of our work we identified no pervasive high or critical risk weaknesses that we consider should be reported in the Council's Annual Governance Statement. Please refer to other weaknesses section below.</p>	
<p><b>Other weaknesses</b></p> <p>Other weaknesses were identified within the organisation's governance, risk management and control, which relate to findings identified from the KPMG review undertaken at Cherwell District Council that has resulted in a Joint Finance Improvement Plan.</p>	<p>A Joint Finance Improvement Plan has been developed as a result of this report and the council should consider where relevant what is included and disclosed within its 2015/16 annual governance statement.</p> <p>We undertook two additional reviews in relation to this and given the scopes agreed for these reviews, found that there were no additional significant control findings that had not been raised by the KPMG report and addressed through the Joint Finance Improvement Plan developed.</p>
<p><b>Good practice</b></p> <p>We also identified a number of areas where few weaknesses were identified and / or areas of good practice.</p>	<p>The following reviews were classified as low risk reports with mostly low risks findings and limited medium risk findings (if any):</p> <ul style="list-style-type: none"> <li>• Creditors</li> <li>• Housing Benefit</li> <li>• Joint Working</li> </ul>

# 3. Internal Audit work conducted

## Introduction

The table below sets out the results of our internal audit work and implications for next year's plan.

We also include a comparison between planned internal audit activity and actual activity.

## Results of individual assignments

Review	Report classification	Number of findings			
	Status	Critical	High	Medium	Low
Finance - Creditors	Low Final	0	0	0	4
Finance - Debtors	Medium Draft	0	0	1	6
Finance - Payroll	Medium Final	0	0	2	1
Finance – Housing Benefit	Low Final	0	0	1	1
Finance – Collection Fund	Medium Draft	0	0	2	4
Risk Management	Medium Draft	0	0	1	4
Joint Working	Low Draft	0	0	0	3
Programme Assurance / New IT System (Combined Review)	Medium Draft	0	1	1	2
	<b>Total</b>	<b>0</b>	<b>1</b>	<b>8</b>	<b>25</b>

In addition we have carried out the following value enhancement reviews and additional pieces of work where no risk rating has been provided.

- Year-end finance support
- Risk Management training

We also delivered additional reviews, following request by management, in relation to a report issued by KPMG that was specific to Cherwell and resulted in a Joint Finance Improvement Plan that has been developed and implemented. These are to be billed separately.

These were in relation to:

- Council reconciliations (Draft, Medium Risk, 9 low risk findings)
- Income/accounting debtors and aged debt monitoring (Draft, Low Risk, 3 low risk findings)






No additional significant control findings were noted in these reports for consideration in the Annual Governance Statement for the Council. There were no wider significant controls findings that had not already been reported and considered within the Joint Finance Improvement Plan.

Where reviews are draft we conclude there is no movement or implication anticipated for our overall opinion and individual report rating.

### *Implications for next year's plan*

As mentioned above, the Council has developed a Joint Finance Improvement Plan, this should be maintained and management should continue to consider whether the scope and budget remains appropriate to address improvements identified in this plan. We will continue to work with management on next year's plan, individual scopes or any additional pieces of work that may be requested to obtain the assurance required by management and the council.

### *Direction of control travel*

<i>Finding rating</i>	<i>Trend between current and prior year</i>	<i>Number of findings</i>			
		<i>2015/16</i>	<i>2014/15</i>	<i>2013/14</i>	<i>2012/13</i>
Critical		0	0	0	0
High		1	0	0	2
Medium		8	8	11	27
Low		25	19	35	35
<b>Total</b>		<b>34</b>	<b>27</b>	<b>46</b>	<b>64</b>

### *Implications for management*

It should be noted that the mix and focus of our internal audit plans have differed between years and therefore these results may not be directly comparable.

The overall message is one of findings being primarily low risk in nature, a low and stable level of total findings in the last two years and over the four years listed an approximate halving and overall a limited number of medium and/or high risk findings.

That having been said, the council should not be complacent and should continue to ensure its focus on continuous improvement especially given the ongoing changes around its joint working / transformation programme and unitary status discussions and ever increasing complex and / or different delivery models being introduced alongside continued funding pressures being faced in the sector.

## Comparison of planned and actual activity

<i>Audit Unit</i>	<i>Planned</i>	<i>Delivered</i>
<b>Finance Systems</b> <ul style="list-style-type: none"> <li>• Payroll</li> <li>• Debtors</li> <li>• Creditors</li> </ul>	Yes	Yes
<b>Finance Systems</b> <ul style="list-style-type: none"> <li>• Collection Fund (Council Tax and NNDR)</li> </ul>	Yes	Yes
<b>Finance Systems</b> <ul style="list-style-type: none"> <li>• Housing Benefits</li> </ul>	Yes	Yes
<b>Risk Management/Governance</b>	Yes	Yes
<b>Programme Management *</b>	Yes	Yes
<b>IT *</b>	Yes	
<b>Service Review - planning applications **</b>	Yes	No
<b>Joint Working and Transformation Programme</b>	Yes	Yes
<b>Finance Year End Support</b>	Yes	Yes
<b>Total (£)</b>	<b>47,355</b>	<b>45,355</b>

\* We combined our programme management and IT reviews to look at the programme implementation of the new finance system and the business continuity arrangements around the project and new finance system.

\*\* Deferred into Q1 of 2016/17 and being delivered during June early July. This cost has been allocated onto the 2016/17 plan fee.

## Implications for management

The main variation in the plan is due to the review previously deferred from 2014/15 in relation to planning applications. This has now been deferred again into Q1 of 2016/17 plan and is being delivered during June and early July. This is also a consequence of the observation in note 1 above.

As discussed above, we will continue to work with management to improve the process and agree a flexible but more structured delivery model for 2016/2017, especially now new management structure has been put in place for 2016/17 and the S151 Officer has been confirmed.



# 4. Follow up work conducted

## Introduction

In order for the organisation to derive maximum benefit from internal audit, agreed actions should be implemented. In accordance with our internal audit plan, we followed up a sample of recommendations made in prior years to ascertain whether action had been taken. The table below summarises the follow up work performed.

## Results of follow up work

Audit unit	Report classification	Number of agreed actions	Status of agreed actions			
			Implemented	Ongoing	Outstanding	Not yet due
Risk Management/ Governance	Medium	5	1	4	0	0
Payroll	Low	1	0	1	0	0
Collection Fund (Council Tax and NNDR)	Medium	6	2	4	0	0
Housing Benefits	Low	2	0	2	0	0
Joint working and Transformation Program	Low	1	0	1	0	0
	<b>Total</b>	<b>15</b>	<b>3</b>	<b>12</b>	<b>0</b>	<b>0</b>

## Summary

We recommend that ongoing assessment is conducted by Cherwell District Council to ensure all previously agreed recommendations are implemented at the earliest opportunity or considered further during 2016/17 where continuing operating effectiveness or design issues are identified. For those recommendations that are ongoing or outstanding, the majority are impacted by;

- the new finance system where findings relate to operational effectiveness issues and the risk versus cost of implementing additional controls for the 2015/16 year before new finance system is implemented is an appropriate consideration by management;
- ongoing changes and developments relating to joint working and transformation; and
- risk management developments being implemented across both councils.

Overall, we have no concerns to raise over the willingness or commitment of management to ensure recommendations are implemented as applicable and the timescales agreed are realistic and/or appropriate.

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# *Appendices*

# ***Appendix 1: Limitations and responsibilities***

## ***Limitations inherent to the internal auditor's work***

Our work has been performed subject to the limitations outlined below.

### ***Opinion***

The opinion is based solely on the work undertaken as part of the agreed internal audit plan. There might be weaknesses in the system of internal control that we are not aware of because they did not form part of our programme of work, were excluded from the scope of individual internal audit assignments or were not brought to our attention. As a consequence management and the Audit Committee should be aware that our opinion may have differed if our programme of work or scope for individual reviews was extended or other relevant matters were brought to our attention.

### ***Internal control***

Internal control systems, no matter how well designed and operated, are affected by inherent limitations. These include the possibility of poor judgment in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

### ***Future periods***

Our assessment of controls relating to Cherwell District Council is for the period 1 April 2015 to 31 March 2016. Historic evaluation of effectiveness may not be relevant to future periods due to the risk that:

- the design of controls may become inadequate because of changes in operating environment, law, regulation or other; or
- the degree of compliance with policies and procedures may deteriorate.

## ***Responsibilities of management and internal auditors***

It is management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.

We endeavour to plan our work so that we have a reasonable expectation of detecting significant control weaknesses and, if detected, we shall carry out additional work directed towards identification of consequent fraud or other irregularities. However, internal audit procedures alone, even when carried out with due professional care, do not guarantee that fraud will be detected, and our examinations as internal auditors should not be relied upon to disclose all fraud, defalcations or other irregularities which may exist.

## Appendix 2: Opinion types

The table below sets out the four types of opinion that we use, along with an indication of the types of findings that may determine the opinion given. The Head of Internal Audit will apply his/her judgement when determining the appropriate opinion so the guide given below is indicative rather than definitive.





<i>Type of opinion</i>	<i>Indication of when this type of opinion may be given</i>
<b>Satisfactory</b>	<ul style="list-style-type: none"> <li>• A limited number of medium risk rated weaknesses may have been identified, but generally only low risk rated weaknesses have been found in individual assignments; and</li> <li>• None of the individual assignment reports have an overall report classification of either high or critical risk.</li> </ul>
<b>Generally satisfactory with some improvements required</b>	<ul style="list-style-type: none"> <li>• Medium risk rated weaknesses identified in individual assignments that are <i>not significant in aggregate</i> to the system of internal control; and/or</li> <li>• High risk rated weaknesses identified in individual assignments that are <i>isolated</i> to specific systems or processes; and</li> <li>• None of the individual assignment reports have an overall classification of critical risk.</li> </ul>
<b>Major improvement required</b>	<ul style="list-style-type: none"> <li>• Medium risk rated weaknesses identified in individual assignments that are <i>significant in aggregate but discrete parts</i> of the system of internal control remain unaffected; and/or</li> <li>• High risk rated weaknesses identified in individual assignments that are <i>significant in aggregate but discrete parts</i> of the system of internal control remain unaffected; and/or</li> <li>• Critical risk rated weaknesses identified in individual assignments that are <i>not pervasive</i> to the system of internal control; and</li> <li>• <i>A minority</i> of the individual assignment reports may have an overall report classification of either high or critical risk.</li> </ul>
<b>Unsatisfactory</b>	<ul style="list-style-type: none"> <li>• High risk rated weaknesses identified in individual assignments that <i>in aggregate are pervasive</i> to the system of internal control; and/or</li> <li>• Critical risk rated weaknesses identified in individual assignments that are <i>pervasive</i> to the system of internal control; and/or</li> <li>• <i>More than a minority</i> of the individual assignment reports have an overall report classification of either high or critical risk.</li> </ul>
<b>Disclaimer opinion</b>	<ul style="list-style-type: none"> <li>• An opinion cannot be issued because insufficient internal audit work has been completed. This may be due to either:               <ul style="list-style-type: none"> <li>○ Restrictions in the audit programme agreed with the Audit Committee, which meant that our planned work would not allow us to gather sufficient evidence to conclude on the adequacy and effectiveness of governance, risk management and control; or</li> <li>○ We were unable to complete enough reviews and gather sufficient information to conclude on the adequacy and effectiveness of arrangements for governance, risk management and control.</li> </ul> </li> </ul>

# Appendix 3: Basis of our classifications

## Report classifications

The report classification is determined by allocating points to each of the findings included in the report

<i>Findings rating</i>	<i>Points</i>
<i>Critical</i>	40 points per finding
<i>High</i>	10 points per finding
<i>Medium</i>	3 points per finding
<i>Low</i>	1 point per finding

<i>Report classification</i>		<i>Points</i>
	Critical risk	40 points and over
	High risk	16– 39 points
	Medium risk	7– 15 points
	Low risk	6 points or less

## Individual finding ratings

<i>Finding rating</i>	<i>Assessment rationale</i>
<b>Critical</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Critical</b> impact on operational performance; or</li> <li>• <b>Critical</b> monetary or financial statement impact; or</li> <li>• <b>Critical</b> breach in laws and regulations that could result in material fines or consequences; or</li> <li>• <b>Critical</b> impact on the reputation or brand of the organisation which could threaten its future viability.</li> </ul>
<b>High</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Significant</b> impact on operational performance; or</li> <li>• <b>Significant</b> monetary or financial statement impact; or</li> <li>• <b>Significant</b> breach in laws and regulations resulting in significant fines and consequences; or</li> <li>• <b>Significant</b> impact on the reputation or brand of the organisation.</li> </ul>
<b>Medium</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Moderate</b> impact on operational performance; or</li> <li>• <b>Moderate</b> monetary or financial statement impact; or</li> <li>• <b>Moderate</b> breach in laws and regulations resulting in fines and consequences; or</li> <li>• <b>Moderate</b> impact on the reputation or brand of the organisation.</li> </ul>
<b>Low</b>	<p>A finding that could have a:</p> <ul style="list-style-type: none"> <li>• <b>Minor</b> impact on the organisation's operational performance; or</li> <li>• <b>Minor</b> monetary or financial statement impact; or</li> <li>• <b>Minor</b> breach in laws and regulations with limited consequences; or</li> <li>• <b>Minor</b> impact on the reputation of the organisation.</li> </ul>
<b>Advisory</b>	<p>A finding that does not have a risk impact but has been raised to highlight areas of inefficiencies or good practice.</p>

# Appendix 3: Performance of internal audit

## Key Performance Indicators

We agreed a suite of Key Performance Indicators (KPIs) with management and the Audit Committee in our annual plan. Our performance against each KPI is shown in the table below. These highlight the focus of our work and the standard attained:

KPI	Target	Performance	Comments
<b>Infrastructure</b>			
Audits budgeted v actual	+/- 10 plan days or resource requirement with management agreement	Met	We have deferred the planning review into Q1 2016/17 and is being delivered during June 2016.
<b>Planning</b>			
% of audits with Terms of Reference	100%	Met	
<b>Fieldwork</b>			
Average cost of an audit	N/A	Met  We have also delivered additional training in relation to risk management at a cost of £4,000 to the council.	We will provide the audit service for £47,355 fee but without being tied to fixed daily rates.  Additional work and fees will be agreed and billed separately as required.
<b>Reporting</b>			
Draft reports issued promptly	Within 3 weeks of completion of the audit site work.	Partially Met.  We have tried to work with management and be flexible in terms of delivery, completion of on-site work and reporting during the year. However, due to issues on both sides this has resulted in reviews being delivered later than planned and some follow up work being delivered after completion, resulting in overall delays to the expected completion of reviews against the plan.	We will continue to work to ensure exit meetings are planned on completion of the on-site work wherever possible rather than post on site work completion and this has led to some subsequent issues in issuing and clearing draft and final reports we will continue to work with management to improve the process and agree a flexible but more structured delivery model for 2016/2017, especially now new

<i>KPI</i>	<i>Target</i>	<i>Performance</i>	<i>Comments</i>
			management structure has been put in place.
Attendance at Audit Committee	100%	Met	
<b>Relationships</b>			
Overall client satisfaction score	8/10	TBC	To be sent out once final deliverable has been issued and approved.

We will look to discuss and modify our Key Performance Indicators where appropriate through discussions with the newly confirmed S151 Officer and the delivery of our 2016/17 plan.

### *Quality assurance and improvement programme*

Quality is embedded in everything we do. We have rigorous quality assurance processes and below is a table summarising how this is applied to this contract.

<b>Key Quality Assurance Systems</b>	<b>How this is applied</b>
<b>Global internal audit methodology, including working practices, documentation standards and software tools applied to all internal audits</b>	<p>All internal audits are conducted to minimum professional standards which include:</p> <ul style="list-style-type: none"> <li>• Approval of terms of reference, including stakeholder “buy in” and involvement;</li> <li>• Application of our global internal audit methodology;</li> <li>• Standardised reporting formats agreed with you; and</li> <li>• Key program steps that need to be completed on each assignment to comply with minimum quality assurance standards in line with the Public Sector Internal Audit Standards.</li> </ul>
<b>Regular internal audit training and development</b>	<p>We place great emphasis on developing and maintaining the skills of our people. We achieve this through a programme of regular management and technical training, attended by all our staff. This is supplemented by sector specific training. For the public sector, this includes:</p> <ul style="list-style-type: none"> <li>• Internal training courses on internal audit with a public sector focus;</li> <li>• National update seminars on, for example, risk management and governance;</li> <li>• Weekly newsletter containing new and emerging issues in the public sector; and</li> <li>• Distribution network for relevant internal and external documentation and publications.</li> </ul>



<b>Key Quality Assurance Systems</b>	<b>How this is applied</b>
<b>Compliance with professional practice and ethical standards</b>	<p>Quality is further underpinned by teams of appropriately trained people with industry experience, supported where necessary by specialist skills drawn from other service areas across the firm.</p> <p>The majority of our staff are members of professional institutes and comply with ethical rules, technical standards and professional practice laid down by those bodies. This is supplemented by the Firm's own professional practice and ethical standards.</p>
<b>Focus on staff performance and quality</b>	<p>All our auditors set performance objectives prior to conducting an audit assignment. A project appraisal form is then completed at the end of each assignment which covers both performance and overall behaviour. Should there be any problems the Engagement Manager and where necessary, Engagement Leader, will advise the staff member of any improvements that should be made in their performance.</p>
<b>Continuous communication with you throughout the audit</b>	<p>Key stakeholders are involved in developing terms of reference, which is approved by a client audit owner.</p>
<b>Customer feedback</b>	<p>To continue to develop our service, it is important that we understand the expectations of the council and receive feedback on our performance.</p> <p>The firm's quality control and assurance procedures additionally involve the use of an annual client satisfaction survey.</p>
<b>Key Performance Indicators</b>	<p>We agree with you Key Performance Indicators and make sure we as a team are meeting them, if not exceeding them.</p> <p>We will look to discuss and modify our Key Performance Indicators where appropriate annually and for 2016/17 we will revisit through discussions with the newly confirmed S151 Officer.</p>
<b>Quality Assurance programme</b>	<p>We run an annual Quality Assurance programme in which an independent team of practice partners and staff review completed engagements to assess compliance with our quality standards and regulatory requirements.</p>



In the event that, pursuant to a request which Cherwell District Council has received under the Freedom of Information Act 2000 (as the same may be amended or re-enacted from time to time) or any subordinate legislation made thereunder (collectively, the "Legislation"), it is required to disclose any information contained in this terms of reference, it will notify PwC promptly and consult with PwC prior to disclosing such information. Cherwell District Council agrees to pay due regard to any representations which PwC may make in connection with such disclosure and to apply any relevant exemptions which may exist under the Act to such information. If, following consultation with PwC, Cherwell District Council discloses any such information, it shall ensure that any disclaimer which PwC has included or may subsequently wish to include in the information is reproduced in full in any copies disclosed.

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