External audit report 2016/17

Northampton Borough Council

September 2017

(updated January 2019)

Summary for Audit Committee

Financial statements

This document summarises the key findings in relation to our 2016/17 external audit at Northampton Borough Council (‘the Authority’). We previously reported on our interim work in our *External Audit Interim Report 2016/17* in July 2017.

We issued our draft ISA260 report in September 2017, our progress report in June 2018, and a further update in November 2018. This updated ISA260 is the final document reporting on our 2016/17 audit.

This report focusses on our initial on-site work which was completed in July 2017 on the Authority’s significant risk areas, and our subsequent focus since then on resolving key issues which arose regarding valuations of Property, Plant and Equipment, and Council Dwellings. Our findings are summarised on pages 4 –16.

Following our initial work, we identified an additional significant risk area in the course of our fieldwork. This is the valuation of *‘other land and buildings’* and investment properties.

Our report also includes additional findings in respect of our control work which we have identified since we issued our interim report.

We have now completed all of our audit work in relation to the Authority’s financial statements following significant delays relating to fixed assets arising from initial delays to the valuation process and issues found in relation to the valuation exercise. Further detail can be found on pages 6 – 12. Subject to completion of our finalisation procedures, we anticipate issuing an unqualified audit opinion on the Authority's financial statements.

Based on our work, we have raised eleven recommendations, see Appendix one. This is in addition to the one recommendation raised in our interim report. Details on our recommendations can be found in Appendix one.

We cannot formally conclude the audit and issue an audit certificate until we have completed our consideration of matters brought to our attention by local authority electors in relation to the loan to Northampton Town Football Club. However, we are satisfied that this work does not have a material effect on the financial statements.

Use of resources

We have completed our risk-based work to consider whether in all significant respects the Authority has proper arrangements to ensure it has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We are therefore issuing an adverse value for money opinion.

See further details on page 30.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continued hard work and co-operation throughout the audit process.

We ask the Audit Committee to note this report.

The key contacts in relation to our audit are:

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This report is addressed to Northampton Borough Council (the Authority) and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. Public Sector Audit Appointments issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

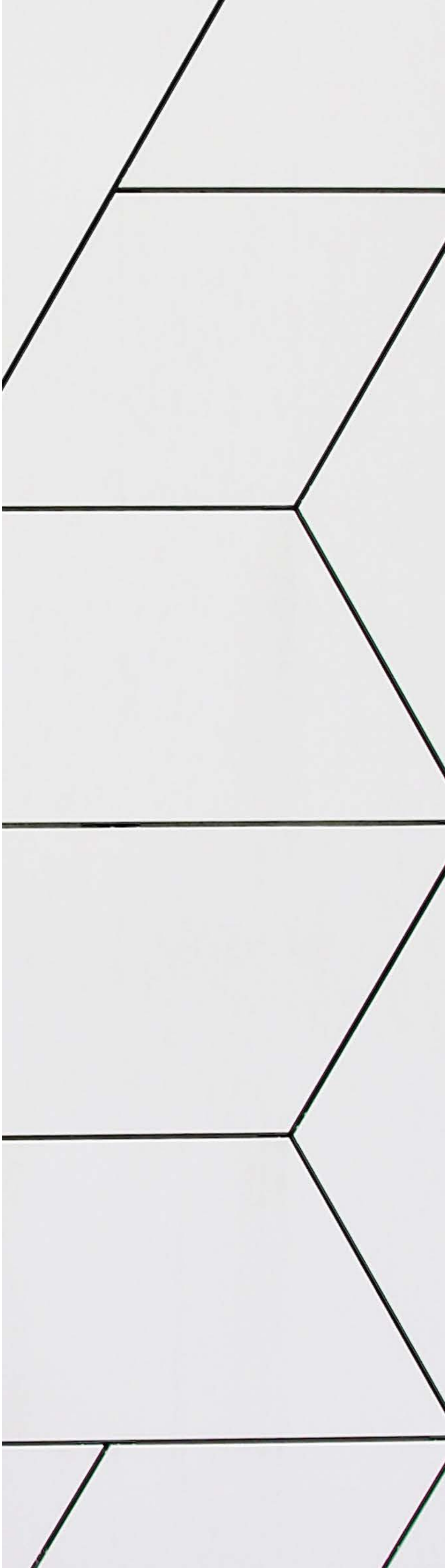
We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Andrew Cardoza, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers (on 0207 694 8981, or by email to andrew.sayers@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3H.

Section one

Financial Statements

We anticipate issuing an unqualified audit opinion on the Authority's 2016/17 financial statements. We will also report that your Annual Governance Statement complies with the guidance issued by CIPFA/SOLACE (*'Delivering Good Governance in Local Government'*) published in April 2016.

For the year ending 31 March 2017, the Authority has reported under the provision of services total income of £290 million against expenditure of £216 million. This has resulted in a net surplus on the provision of services of £77 million. The impact has been an increase in the General Fund.



Significant audit risks

Our *External Audit Plan 2016/17* sets out our assessment of the Authority's significant audit risks. We have completed our testing in these areas and set out our evaluation following our work:

Significant audit risks	Work performed
1. Valuation of Council Dwellings	**Why is this a risk?** Due to the identified risk in relation to the valuation of Council Dwellings, we engaged with the Authority earlier to ensure that appropriate arrangements had been considered and put in place to deliver the required valuations. In 2016/17, the Authority has engaged an external valuer to undertake a comprehensive review of beacon assets used within the valuation of the Authority's housing stock. This was in response to a higher-than-expected increase in the opening value of Council Dwellings during the course of the Authority's annual valuation exercise undertaken for the valuation as at 1 April 2016. For the year ended 31 March 2016, the Authority's housing stock was worth approximately £422 million, thus any change in the valuation is potentially a material change. There is also a risk that the beacon assets may not be representative of the Authority's housing stock, thus over or under-valuing the value of Council Dwellings on the balance sheet. The revision of beacon assets is a change in the Authority's estimate of the value of Council Dwellings. **Our work to address this risk** The Authority is required to value Council Dwellings in line with Code requirements and guidance published by the Department for Communities and Local Government (DCLG) within the *Stock Valuation for Resource Accounting* ("the SVRA"). We engaged our own internal KPMG valuation specialists to assist us with the assessment of the work performed by the Authority's external valuers. *Timeline of work* There were in total three teams of valuers involved with the valuation of the Authority's Council Dwellings in 2016/17. This was due to a lack of capacity within the Authority's Estates team. Appendix 4 summarise key events during the course of the financial year in relation to the valuation of Council Dwellings, other land and buildings and investment properties. As previously reported in our *External Audit 2016/17 Interim Report (April 2017)*, we had initially scheduled the KPMG specialist review of the valuation report to coincide with our interim work in March 2017 to assist the Authority with early closedown. This was ultimately not feasible due to capacity constraints within the Estates team and other valuation issues. In March 2017, we reviewed a version of the valuation exercise undertaken by Underwoods in February 2017. We queried the results of this as: — we were not able to review instructions provided to the valuer nor assess if the review was carried out in line with the instructions provided; — the valuation output did not set out the assumptions used by the valuer in forming its opinion;

Significant audit risks | **Work performed**

1. Valuation of Council Dwellings *(continued)*

- there was no confirmation from the valuer that the Beacon review had been carried out in line applicable guidance specific to Council Dwellings, such as the SVRA.

No report was provided per Code requirements. The requirement for a valuation report was specifically highlighted in our *ISA 260* recommendation in the previous year.

Instructions sent to the valuer

The Authority subsequently engaged Bruton Knowles in April 2017 to further review the work on the valuation of Council Dwellings. The valuer was instructed to:

- perform a valuation of the beacons *previously valued at 1 April 2016* by Underwoods; and
- utilise alternative beacons "where necessary" in order to produce a final report using a method of the valuers' choice, in compliance with the current RICS Valuation Standards and the SVRA.

The list of assets "*previously valued at 1 April 2016*" was initially sent to Underwoods for the initial work in February 2017. We reviewed this list to ensure that Bruton Knowles had carried out a review of the beacons as required by the Authority. Bruton Knowles confirmed that it had selected alternative beacons as part of its valuation process.

We understand that verbal instructions were provided to the valuer to undertake a desktop valuation of the beacons. This is not in compliance with Code requirements and is a departure from the Authority's accounting policies and previous years' practice. The Authority then instructed Bruton Knowles to carry out a full valuation exercise on the 20% of Council Dwellings on 16 September 2017.

Application of the social housing discount factor

The Authority's housing stock is valued using Existing Use Value – Social Housing, or EUV–SH. This involves applying a social housing discount factor to the valuation of the properties, as defined within Appendix 4 of the SVRA. The SVRA was updated in November 2016, which introduced a new social housing discount factor.

For the East Midlands, the relevant social housing discount factor is 42% (this was 34% in the previous version of the SVRA). This is summarised below:.

	Version published Jan 2011	Version published Nov 2016
East Midlands	34%	42%
South East	32%	33%
Used by the Authority	**34%**	**33%**

The Authority's valuer had applied a social housing discount factor of 33% instead, which is the discount factor applicable to the South East. Valuers are not obliged to use the adjustment factors, however the guidance requires that where discount factor varies by +/-5%, an auditable methodology should be established to provide assurance over this alternative adjustment factor. The SVRA further states that "*the reasons for departing from the factor provided…must be clearly stated by the valuer together with the methodology and sources of evidence adopted for preparing the alternative*". The Authority's valuer was unable to provide this.

Significant audit risks	Work performed

1. Valuation of Council Dwellings *(continued)*

Other local authorities with housing stock within Northamptonshire have used a social housing discount factor of 42%, which is consistent with the SVRA. Northampton Borough Council is thus an outlier.

Local authorities within Northamptonshire	With housing stock?	Social housing discount factor	Auditor
East Northants District Council	No	–	KPMG
South Northants District Council	No	–	E&Y
Corby Borough Council	Yes	42%	KPMG
Kettering Borough Council	Yes	42%	KPMG
Daventry District Council	No	–	KPMG
Borough Council of Wellingborough	No	–	KPMG
Northampton Borough Council	**Yes**	**33%**	**KPMG**

Given the above, the Authority agreed to amend the social housing discount factor in line with the DCLG guidance. This resulted in an adjustment of £86.7m to the net book value of Council Dwellings. See appendix 3 for details.

Full valuation intervals

The Code requires the Council Dwellings to be revalued at intervals no more than five years. The Authority's approach is to carry out a full valuation of approximately 20% of beacon assets every year, thus ensuring coverage and compliance with the Code.

For 2016/17, there is a departure from the approach in previous years, as only a desktop valuation had been carried out. This change in methodology has not been disclosed within the Authority's financial statements. The new approach this year is not in compliance with Code requirements, as for the 20% of beacons required to be valued, there has been a period of more than five years since the last full valuation.

The use of a desktop valuation has been necessitated by time pressures; we understand that Bruton Knowles was engaged on 20 April 2017 with the view to produce a valuation report by the end of May 2017.

However, on 16 September 2017 Bruton Knowles carried out a full valuation exercise on the same 20% of beacons upon request by the Council. This was in response to our initial feedback on the Authority's compliance with Code requirements.

Assessment of valuation methodology

Our valuation specialist has reviewed the valuation report and liaised with Bruton Knowles to understand and review the valuation basis, methodology, and assumptions used in the valuation exercise. Our specialist challenged the year-end uplift of 10%, due to reliance on one source of information.

Bruton Knowles subsequently agreed to amend the report to take into account the issues raised by KPMG. A revised report was issued in September 2017. We noted valuation methodology pages missing from the draft report and requested a final version. We did not receive the final report until July 2018 as internal inconsistencies resulted in an updated version being requested. See appendix 4 for timeline review.

Significant audit risks | **Work performed**

1. Valuation of Council Dwellings *(continued)*

Substantive testing of valuation figures

Due to the expectation that the Bruton Knowles valuation exercise will change the Authority's beacon values, we requested in December 2017 that the Authority provide a reconciliation between the draft version of the valuer's September 2017 report and the fixed asset register. The reconciliation process is important as it provides assurance both to the Authority and auditors that:

- all assets that should be valued have been valued;
- the correct information (asset name, type, value, etc) have been provided to the valuer; and
- the valuer's valuation has been correctly transacted by the Authority and correctly reflected within the fixed asset register.

As with the first report (May 2017), no reconciliation had been provided to us (despite multiple requests dating back to December 2017). We reiterated on 1 February 2018 that this is crucial to progressing the audit. A working paper was subsequently provided on 12 April 2018. We reviewed this working paper and found differences between the previous year's closing figures and the figures used by Bruton Knowles.

Application of uplift based on original valuation

Having received our queries on the reconciling figures (see previous page), the Authority informed us that this was due to the uplift of 4.08% which had been calculated and applied by the internal valuers on 1 Apirl 2016 - was the original valuation which has since been superseded by both the Underwoods and Bruton Knowles valuations.

It was unclear why this original uplift had been transacted given:

- Underwoods had found issues with the original beacons (although Underwoods' report has been challenged by us); and
- Bruton Knowles subsequently found issues with the valuation and the results materially differ from the internal valuer's original valuation.

This would typically not be an issue given the valuation should always reflect the balance sheet date. However, this 4.08% was applied to the 80% of beacons not valued by Bruton Knowles. This transaction has the effect of reflecting the internal valuer's assumptions and methodology—which have been challenged and superseded by Bruton Knowles. The calculation of the 4.08% uplift is based on the average valuation movement on the original sample of beacons revalued by the Authority's internal valuers.

We were also not made aware that the internal valuation had been transacted.

The Authority has informed us that the Bruton Knowles valuation as of 1 April 2016 was effectively ignored due to the overall impact being "relatively small". To illustrate, the Table below summarises the values from the May 2017 Bruton Knowles report and the internal valuer's report. Both retain the incorrect social housing adjustment factor to aid comparison.

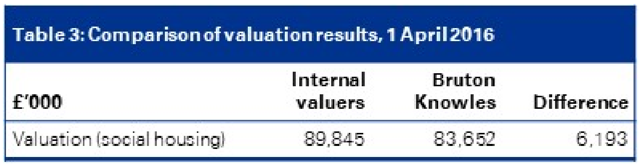


Table 3: Comparison of valuation results, 1 April 2016

£'000	Internal valuers	Bruton Knowles	Difference
Valuation (social housing)	89,845	83,652	6,193

A difference of £6.2 million is material for the purposes of the Authority's accounts.

Significant audit risks	Work performed

1. Valuation of Council Dwellings *(continued)*

Further use of the incorrect social housing adjustment factor

We were not initially provided with a copy of the internal valuer's report due to this valuation exercise being undertaken by the Authority's external valuers; we requested this on 20 April 2018. Upon receipt of the report on 30 April 2018, we reviewed and noted—again—that an incorrect social housing adjustment factor of 34% had been used. This was the social housing adjustment factor in the previous version of the guidance. The new guidance was released in November 2016 and applicable to valuations from 1 April 2016 onwards

The use of 34% instead of 42% by the internal valuers resulted in a material audit difference which is detailed in Appendix 3.

The reliance of the internal valuation is also an issue due to the same uplift calculated from the internal valuer's valuation, which as previously discussed, had been superseded by the Bruton Knowles valuation.

Our line of inquiry has also uncovered that whilst Bruton Knowles had adjusted for the correct social housing adjustment factor for its valuation as at 31 March 2017, this was not adjusted for its 1 April 2016 valuation. This is crucial as the valuation at the year end is a simple uplift of 7% on the 1 April 2016 figures, thus carrying forward the initial error.

Resolution

The Authority commissioned Bruton Knowles again to carry out a further valuation exercise for the valuation figures on the 20% they valued as at 1 April 2016 (due to the derivative nature of the year-end valuation).

We have subsequently undertaken the following additional work in July 2018:

- We have reviewed the valuation instructions provided to Bruton Knowles, for the valuation as at 1 April 2016;
- We have reviewed the valuation report resulting from these updated instructions; and
- We have reviewed an updated reconciliation between the final valuation report and the fixed asset register.

We also needed to reperform work previously undertaken due to the updated report, including but not limited to:

- We reviewed the list of assets to be valued (the input) against the Authority's records. This is to ensure compliance with the Code's requirement that assets should be valued at intervals of not more than five years and against the Authority's own policy of a rolling valuation basis;
- We rechecked that the assets' characteristics (value, type, etc) have been accurately provided to the valuer;
- We reviewed the completeness of the valuer's output; where there have been asset disposals, these were agreed to the work previously undertaken;
- We reviewed the reconciliation to be provided by the Authority; and
- We reviewed the mathematical accuracy of the report.

Significant audit risks	Work performed
1. Valuation of Council Dwellings *(continued)*	*Correction of audit misstatements* As reported above, the Authority has now undertaken the appropriate actions to correct the valuation of council dwellings due to the errors, including use of an incorrect methodology which had resulted in materially incorrect valuations. Following finalisation of the valuations, the Authority then needed to correct these in their RAM (Real Asset Management) System, which would then produce the reports/figures to be updated in the financial statements. The relevant adjustments to the accounts are detailed in Appendix 3. Due to the nature of the system, we were informed that significant work was required by a technical specialist to put these changes through the system as the version of RAM that the Authority was using was considerably out of date. This work was commissioned on 2 August 2018 with the expectation it would take a few weeks to complete. The work took longer than expected and was only completed during September 2018. This had a knock-on effect on our ability to close off this area from an audit perspective, but is now complete. We have raised a recommendation in Appendix 1 to update the RAM system in future years. As a result of the updates to the system, we have had to undertake further testing on RAM in order to provide assurance over the reports it generates which are used for the production of the financial statements. This work was performed by KPMG IT specialists. We have now received the final information and answers to our queries and this work is complete. We are satisfied that all material misstatements have now been corrected in the financial statements. See Appendix 3 for details of audit misstatements raised.

Significant audit risks	Work performed
1. Valuation of Council Dwellings *(continued)*	*Componentisation of Council Dwellings*

In second half of 2015/16, the Authority changed the way it accounted for components of Council Dwellings (for example, bathrooms, kitchens, etc.). This change involved grouping individual components by type into one "global" component type. As a result, additions or disposal of individual components cannot be directly identified on the fixed asset register. The Authority has determined that where a component is replaced, a percentage is disposed (or, "derecognised") according to a ratio determined by historic data for each type of component.

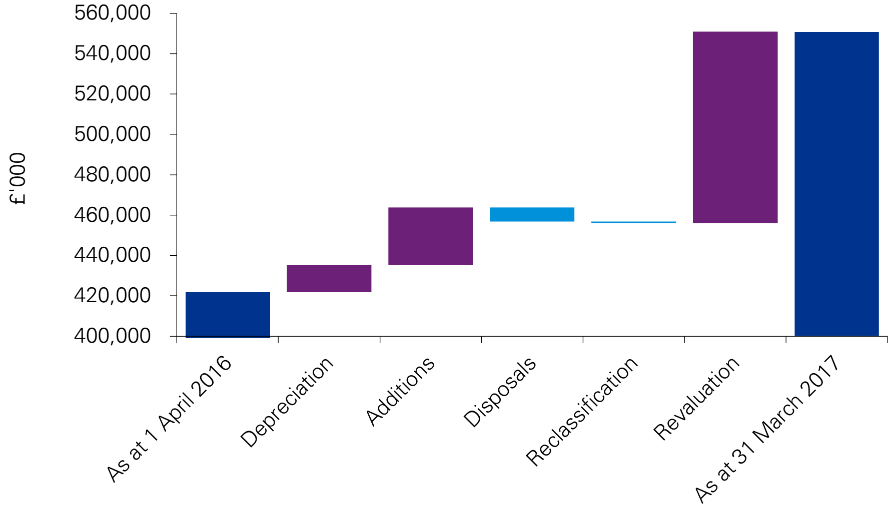
The change in accounting for components introduced an element of estimate and judgement. This is a move away from the purpose of componentisation, which was first introduced in IAS 16 (and adopted by the Code) in 2010/11 in order to refine asset values. Various elements of an asset do not have identical useful lives due to different depreciation rates. The use of componentisation allows the Authority to allocate values to individual components with greater accuracy. The move to group component types removes this refinement and introduces significant estimates.

In the prior year, we agreed with the Authority that this change should be quantified to allow us to come to an informed view of this change in accounting methodology. Due to the departure of a key member of the Closedown team, this was not provided to the audit team.

In the prior year, the amount calculated from this new methodology was not material; however in 2016/17 this balance is much larger, at £1.0 million. We had significant difficulty in assessing this balance. Our review of componentisation and the disposals of resulted in an audit adjustment of c£0.5 million. See Appendix 3 for audit adjustments.

We have again recommended that the Authority review the methodology for componentisation.

Chart 1: Summary of movements in Council Dwellings (net book value)



Significant audit risks | **Work performed**

2. Valuation of *'other land and buildings'* and investment properties

Why is this a risk?

During the course of the audit, we have identified that the valuation of *'other land and buildings'* and investment properties is a significant audit risk. The Authority had engaged the following valuers to carry out work on both *'other land and buildings'*, and investment properties:

- internal valuers on 26 September 2016; and
- subsequently Underwoods. We were informed that Underwoods was engaged on 6 October 2016, but there are no formal records from the Authority to confirm this.

The engagement of Underwoods was the result of capacity constraints due to internal valuers leaving the Authority. As of September 2017, there are no valuation specialists remaining with the Authority which creates a gap in both capacity and capability.

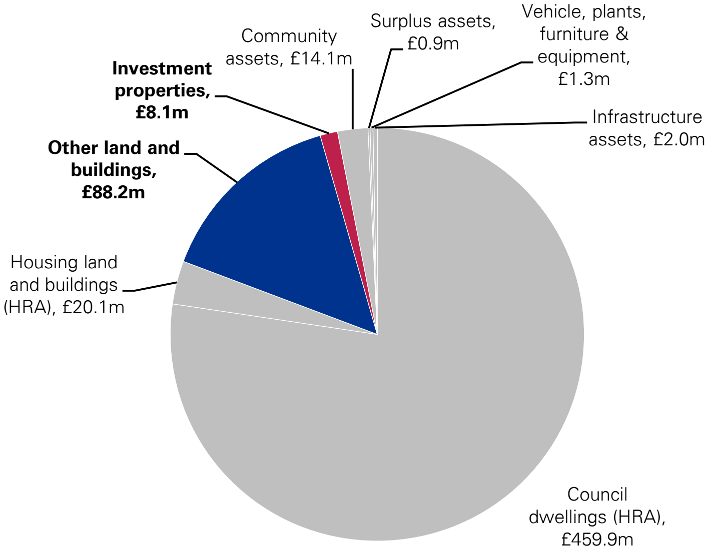
This has been further exacerbated by the departure of a key member of the Closedown Team which gave us concerns over continuity and on the oversight of the valuation process.

There are competing pressures within the Authority, and there is a risk that valuations may not be appropriately undertaken.

Our work to address this risk

'Other land and buildings' consists of non-housing property, with a net book value of £88.2 million and is valued on an Existing Use Value (EUV) basis. Investment property are assets used solely to earn rentals and/or for capital appreciation.

Chart 2: Net book values of PPE and investment properties



Note: Although 'Community assets', 'surplus assets', 'Vehicle, plants, furniture & equipment', and 'Infrastructure assets' are included within PPE, these classes of PPE are not revalued, per the Authority's accounting policy.

Significant audit risks	Work performed
2. Valuation of 'other land and buildings' and investment properties *(continued)*	*Instructions sent to the valuer* No written records of instructions were sent to Underwoods. We were not able to confirm that Underwoods had complied with the valuation request; we had to undertake additional work to reconcile the list of assets reviewed against the valuer's output. We are also not able to confirm that the Authority has instructed its external valuer in line with the requirements of the Code and other applicable valuation and accounting standards. We engaged our KPMG specialist to perform additional substantive work to provide assurance that the valuations were in line with applicable standards. *Assessment of valuation methodology* We received the valuation report on 4 August 2017, which was later than we anticipated as the original audit plan included a review of the report prior to us commencing the final audit in July 2017. Our KPMG valuation specialists engaged with the Authority's valuers in September 2017 to assess the work performed by the Authority's valuers. Our KPMG valuation specialist had raised a number of queries in relation to the assumptions used by Underwoods due to the absence of documented information within the reports. Further work was undertaken to clarify and agree specifics of the sampled assets, such as deeds and titles. One adjustment that resulted from our valuer's review relates to purchaser's costs, which have not been consistently deducted from the OLB or Investment Property assets reviewed in our sample. This adjustment has reduced the value of the Authority's assets by approximately £1.5 million, which is above our reporting threshold. See Appendix 3 for details. The work had also resulted in various other adjustments, including reclassification of assets from other land and buildings to investment properties. *Internal valuers* The Authority's internal valuers had valued a selection of the Authority's other land and buildings which were subject to valuation during the year, but there was no documented methodology by which those assets were selected for valuation. Our valuation specialist was unable to gain sufficient comfort over the assumptions and other inputs used due to the absence of documentation. This is also exacerbated by the departure of the Authority's internal valuers, who were interim staff. The Authority subsequently commissioned GVA to undertake a review of the assets previously valued by the Authority's internal valuers. *External valuers* We received GVA's reports in December 2017, and our valuation specialist completed the initial review in January 2018. Further work was undertaken to fully-reconcile the list of properties to ensure that all assets that were due for valuation have been revalued. *Correction of audit misstatements* We have now received the final information and answers to our queries and this work is complete. We are satisfied that all material misstatements have now been corrected in the financial statements.

Significant audit risks	Work performed
2. Valuation of 'other land and buildings' and investment properties *(continued)*	Two adjustments remain in the final accounts that are uncorrected but these are not deemed to be above our materiality threshold. Additional work included agreement of leases and review of classification of assets. Additional assets were revalued by GVA as a result of the review by the KPMG specialist. Total adjustments to OLB were £9.5 million, which included the reclassification of a number of assets such as Park Inn and Sixfields, which totalled c£4 million. Adjustments to investment properties were £3.5 million, which included the removal of purchase costs of c£1.5 million, which had been incorrectly treated as a disposal by the Authority. These needed to be reversed and put through Reserves. See appendix 3 for details.

Significant audit risks | **Work performed**

3. Significant changes in the pension liability due to the LGPS Triennial Valuation

Why is this a risk?

During the year, the Northamptonshire County Council Pension Fund (the Pension Fund) has undergone a triennial valuation with an effective date of 31 March 2016 in line with the Local Government Pension Scheme (Administration) Regulations 2013. The Authority's share of pension assets and liabilities is determined in detail, and a large volume of data is provided to the actuary in order to carry out this triennial valuation.

The pension liability numbers to be included in the financial statements for 2016/17 will be based on the output of the triennial valuation rolled forward to 31 March 2017. For 2017/18 and 2018/19 the actuary will then roll forward the valuation for accounting purposes based on more limited data.

There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the accounts. Most of the data is provided to the actuary by Northamptonshire County Council, who administer the Pension Fund.

Our work to address this risk

Controls

As part of the additional work on pensions due to the triennial valuation, we have reviewed the process used to submit payroll data to the Pension Fund, including year-end controls. As part of the submission process, we expect Management to formally assess and confirm that the actuarial assumptions used by the actuary are appropriate for the organisation and in line with expectations.

We have found that there is no formal review process, nor is Management able to evidence that it has considered the actuarial assumptions used. Management has subsequently confirmed to us that it considers the assumptions used by the actuary to be suitable for the Authority and are in line with the other members of the Northamptonshire Pension Fund. We also subsequently received emails from the Authority which demonstrated review of these actuarial assumptions. We have raised a recommendation that actuarial assumptions should be formally reviewed as part of the yearly closedown process to ensure that they are appropriate for the Authority, see recommendation 9 in Appendix 1.

Testing carried out at the Pension Fund

We liaised with your Pension Fund Audit team to gain assurance over:

- The operation of the Fund's controls, including the controls over the transfer of data to the Actuary;
- The figures submitted from the Fund to the Actuary, including the completeness and accuracy of the data;
- Investment balances;
- Monitoring arrangements; and
- Controls in relation to the calculation and authorisation of benefit payments.

The Pension Fund Audit team reported that there is no authorisation or segregation of duty in relation to the posting of journals for the Pension Fund. This has been reported with the Fund's ISA 260 (Communication to Those Charged with Governance). With the exception of journals, no further issues with the Fund were noted.

Significant audit risks	Work performed
3. Significant changes in the pension liability due to the LGPS Triennial Valuation *(continued)*	*Year end testing* We substantively agreed the total figures submitted to the Fund to the Authority's ledger. We also tested the IAS 19 reports produced by the Fund's Actuary to figures disclosed within the Authority's financial statements. No discrepancies were noted. *Review of actuarial assumptions* We used KPMG's actuary to review the assumptions used by the Fund's Actuary for the triennial valuation. Assumptions used are in line with the other members of the Northamptonshire Pension Fund and within our expectations.
4. Management override of controls	**Why is this a risk?** Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Although our audit methodology includes the risk of management override as a default significant risk, we have identified that the events surrounding the loss of £10.22 million in relation to the NTFC loan and the on-going police investigation are contributory factors in the increased risk, and specifically warrants management override of control as a significant risk to the financial statements. **Our work to address this risk** We have decreased materiality over the financial statements which resulted in additional testing over the Authority's financial statements. We enhanced our use of data analytics techniques over the Authority's transactional data (for example, journals, payroll, and non-pay expenditure) to allow us to gain additional assurance over the balances. We carried out additional work on the Authority's related party transactions to ensure disclosures and declarations are robust and complete. We applied professional judgement throughout our audit of your financial statements and performed robust procedures, including: — Examining journal entries and other adjustments; — Reviewing accounting estimates; — Evaluating the business purpose for significant unusual transactions; and — Other procedures as necessary. There were no significant issues or matters arising from our work in this area that we need to bring to Members' attention.

Considerations required by professional standards

Fraud risk of revenue recognition

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk.

In our *External Audit Plan 2016/17* we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.

Other areas of audit focus

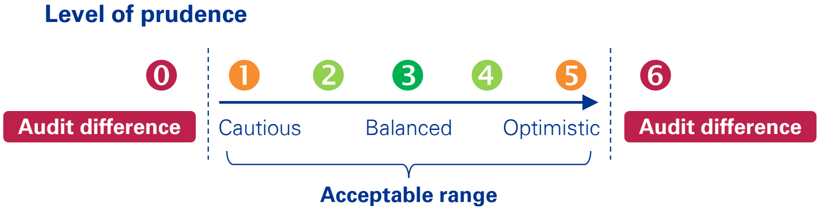
We identified two areas of audit focus. These are not considered as significant risks as they are less likely to give rise to a material error. Nonetheless these are areas of importance where we would carry out substantive audit procedures to ensure that there is no risk of material misstatement.

Other areas of audit focus	Our work to address the areas
1. Disclosures associated with retrospective restatement of CIES, EFA and MiRS	**Background** During past years, CIPFA has been working with stakeholders to develop better accountability through the financial statements as part of its 'telling the whole story' project. The key objective of this project was to make Local Government accounts more understandable and transparent to the reader in terms of how the Councils are funded and how they use the funding to serve the local population. Outcome of this project resulted in two main changes in respect of the 2016/17 Local Government Accounting Code (Code) as follows: — Allowing local authorities to report on the same basis as they are organised by removing the requirement for the Service Reporting Code of Practice (SeRCOP) to be applied to the Comprehensive Income and Expenditure Statement (CIES); and — Introducing an Expenditure and Funding Analysis (EFA) which provides a direct reconciliation between the way local authorities are funded and prepare their budget and the CIES. This analysis is supported by a streamlined Movement in Reserves Statement (MiRS) and replaces the current segmental reporting note. As a result of these changes, retrospective restatement of CIES (cost of services), EFA and MiRS is required from 1 April 2016 in the Statement of Accounts. New disclosure requirements and restatement of accounts require compliance with relevant guidance and correct application of applicable accounting standards. Though less likely to give rise to a material error in the financial statements, this is an important material disclosure change in this year's accounts, worthy of audit understanding. **What we have done** This additional work is driven by Code changes. The Authority has been sighted on this change in advance of the year end and had proactively liaised with KPMG to review the restated 2015/16 CIES during the interim audit in March 2017 however, during the interim audit, this work was not available for review and was performed as part of the year end work. For the restatement, we have obtained an understanding of the methodology used to prepare the revised statements. We reviewed the Authority's methodology for compiling the restated CIES and the new EFA. We agreed the Authority's disclosure and compliance with the Code requirements. The Authority has chosen not to apportion recharges of Investment Properties and Trading Accounts. This is in line with its own internal reporting methodology. This has resulted in the net expenditure in 2015/16 Cost of Services decreasing under the new model by £50,000. The 2015/16 Surplus on Provision of Services remains unchanged. The Authority has applied the internal reporting structure to the new CIES as allowed by the Code. The EFA is also in line with new Code requirements.

Other areas of audit focus	Our work to address the areas
1. Disclosures associated with retrospective restatement of CIES, EFA and MiRS *(continued)*	For the 2016/17 the Authority was consistent in the approach set out above. Initially the Authority did not provide us with the note to accompany the EFA however, this was subsequently provided. No issues were identified. In conjunction with the new CIES, the Code requires that the analysis of expenditure include depreciation, amortisation, and employee benefit expense. The Code guidance further provides an example disclosure. We note that this was missing from the Authority's initial draft accounts. This was subsequently provided to us during our audit visit. We did not find issues in relation to this. We have also agreed the 2016/17 figures disclosed in the notes to the Authority's general ledger and found no issues.
2. Change in the Non Domestic Rates (NDR) system	**Background** In April 2016, the Authority returned the business operation of the NDR system to Northampton Borough Council from the previous consortium arrangement with the Borough Council of Wellingborough. This involved the migration of the NDR database to the Authority and included the re-design of system processes and protocols to ensure that the controls within the system are fit for purpose. **What we have done** Our IT Specialists have liaised with the Authority and completed testing as necessary to obtain assurance that the NNDR data has been transferred completely and accurately, and to ensure that the new system operates effective and appropriate controls and processes to reduce any material risks. We have gained an understanding of the new system and controls in place at the Authority. The Authority originally transferred from the ICL system (in-house) to Academy (at the Borough Council of Wellingborough, operated by Capita) in 2003/04. The data conversion and cleansing process resulted in a difference of 13 pence between the starting and the finishing balance. This was due to rounding differences. Because this difference was minimal and involved a large quantity of historic data, this was previously agreed by the Authority as being acceptable. However, whilst the transactions balanced and were correct, this had the impact of causing Capita's integrity-checking process to fail. The amounts have been reported as part of the NNDR3 process, thus did not adversely impact on the Authority's reconciliation or funding arrangements. We understand from the Authority's documentation that a significant number of integrity checks have not been done. During our work in April 2017, there were 998 such cases totalling £5.1 million. The Authority has stated that work is ongoing in relation to this.

Judgements

We have considered the level of prudence within key judgements in your 2016/17 financial statements and accounting estimates. We have set out our view below across the following range of judgements.



Subjective areas	2016/17	2015/16	Commentary
Provisions (excluding NDR)	③	③	We tested the Authority's provision against IAS 37 with no issues to note. We consider the provision disclosures to be proportionate.
NDR provisions	③	⑤	In 2013/14, local authority funding arrangements meant that the Authority is now responsible for a proportion of successful rateable value appeals. The Authority has previously provided for a fixed percentage of outstanding appeals in accounting for the potential liability. We challenged this in the prior year and recommended that the Authority should review its Non Domestic Rates (NDR) provisions in line with applicable accounting guidance. The Authority has since reviewed its NDR provisions and incorporated detailed variables to fairly reflect local information. This has resulted in an increase of £800,000.
PPE: components	N/A	N/A	The Authority has changed the way it accounts for components of Council Dwellings. This new methodology is an estimate; this estimate has not been disclosed within the Authority’s financial statements. Whilst the Authority was unable to provide further detail regarding the calculation of this estimate, we were nevertheless able to carry out additional work (such as reviewing management assumptions and judgements behind the estimate) to gain sufficient comfort. However, further work by the Authority is being undertaken in future years to gain additional assurance over this estimate to generate a more accurate and reliable estimate. We have raised a high-priority recommendation, see recommendation 5 in Appendix 1.
Pension liability	③	③	During the year, the Northamptonshire Pension Fund had undergone a triennial valuation, which resulted in an increase in pensions liability of £23.3 million. The actuarial assumptions used drive the actuarial gains or losses as well as pensions liabilities. Management has confirmed that the assumptions used by the actuary are appropriate for the Authority. We have performed work on the assumptions used and have deemed the assumptions to be reasonable and within our expectations. Assumptions used are also in line with other local authorities within the Northamptonshire Pension Fund. We have requested specific representations in relation to this and have raised a low-priority recommendation, see recommendation 9 in Appendix 1.

Proposed opinion and audit differences

We anticipate issuing an unqualified audit opinion on the Authority's 2016/17 financial statements following approval of the Statement of Accounts by the Audit Committee.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality (see Appendix 4 for more information on materiality) level for this year's audit was set at £1.5 million. Audit differences below £75,000 are not considered significant.

A number of audit differences were identified as a result of our audit. The largest adjustment was in relation to the incorrect use of the social housing discount factir which increased Council Dwellings by £88.7m. There were also c£0.5 million of unadjusted audit differences. See Appendix 3 for details.

In addition, during the course of the audit we have identified a large number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 ('the Code'). The Authority has now addressed these, where significant, in the final draft of the 2016/17 financial statements.

Annual Governance Statement

We have reviewed the Authority's 2016/17 Annual Governance Statement and confirmed that:

— It complies with *Delivering Good Governance in Local Government: A Framework published by CIPFA/SOLACE*;

and

— It is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Narrative Report

We have reviewed the Authority's 2016/17 Narrative Report and have made comments in relation to compliance with Code requirements.

Following our feedback during the audit process, further work was undertaken to improve the Authority's Narrative Report. We have reviewed each iteration of the report and are content that the final version is complaint with Code requirements.

Accounts production and audit process

The Accounts and Audit Regulations 2015 introduces a statutory requirement to produce a draft set of financial statements earlier for the year 2017/18 onwards. It also shortens the time available for the audit.

Our audit standards (*ISA 260*) require us to communicate our views on the significant qualitative aspects of the Authority's accounting practices and financial reporting.

We also assessed the Authority's process for preparing the accounts and its support for an efficient audit. The efficient production of the financial statements and good-quality working papers are critical to meeting the tighter deadlines.

Introduction of KPMG Central

We introduced KPMG Central this year, which is a cloud-based document storage system to facilitate the secure transfer of large amounts of data between the Authority and the audit team. KPMG Central aligns to our Accounts Audit Protocol and allows the Authority's Closedown team to efficiently share requested information. Feedback from the Closedown team has been positive and allows us to keep track of uploaded documents.

Accounting practices and financial reporting

The Authority has recognised the additional pressures which the earlier closedown of its accounts will bring. We have engaged with the Authority in order to proactively address issues as they emerge.

However, when we began our on-site audit, in July 2017 we encountered significant delays with regard to the provision of working papers and valuation reports, which meant that the Authority was unable to meet the earlier agreed deadlines. The earlier deadlines for 2016/17 were suggested by the audit team as a trial run in anticipation of the earlier deadlines in 2017/18. As a result, this raises significant concerns over the Authority's ability to meet the early statutory deadlines going forward.

The Authority will need to strengthen its financial reporting by finalising the accounts in a shorter timescale. It should also consider a fundamental review of its approach to the closedown process, including the implementation of monthly or quarterly closedowns and early engagement with its external valuers. Going forward this will put the Authority in a better position to meet the 2018/19 deadline.

Officers took a proposal to Audit Committee on 6 March 2017 to make minor amendments to the Authority's accounting policies. We consider the accounting policies to be appropriate. However, we noted that the Council has not disclosed a change in the way it has accounted for components of Council Dwellings, which involves significant estimates. This change affects the full financial year for the first time in 2016/17. This new methodology is discussed further in the following sections.

Completeness of draft accounts

We received a set of draft accounts on 30 June 2017, which is the statutory deadline. However we noted the following:

- The cash flow statement was incorrect as the figures did not agree to the accounts. According to Officers, the provision of an incorrect cash flow was due to pressures faced by the Closedown team during the closedown process. A revised cash flow statement was subsequently provided three weeks after the audit began.

- For 2016/17, the Code introduced the requirement to analyse expenditure by nature. This analysis was missing from the initial draft accounts. Numerous versions of the draft accounts were subsequently provided to the audit team during the following months.

Supporting working papers

Quality and timeliness of working papers

Prior to issuing our *Accounts Audit Protocol 2016/17* ("Prepared by Client", or PBC request) we ran workshops in October 2016 to assist the Authority in understanding our PBC requirements. Our PBC document outlines our documentation request. This helps the Authority to provide audit evidence in line with our expectations.

A draft PBC was issued in December 2016 and post-discussion with Officers, was finalised the following month. We followed this up with a meeting with the Closedown team to discuss specific requirements of the document request list in March 2017. We have also offered further support and opportunities to discuss specific requirements of audit requests.

The quality of audit evidence initially provided did not fully-align to our expectations which were set out in our *Accounts Audit Protocol 2016/17*. For example:

- We were not provided with a full fixed assets register or a breakdown of fixed assets additions. More significantly, we were not provided with the valuation reports prior to the start of the final audit, as previously agreed with the Authority;
- The breakdowns for both debtors and creditors were incorrect and did not tie back to the accounts; and
- Working papers for payroll did not have robust audit trails, which made it difficult to understand what had been provided.

The quality issues above meant that we undertook additional work to understand the initial working papers. The audit team had to wait for the provision of revised working papers to address the issues we found. The delays meant that we spent additional time over and above what was originally planned including significant work undertaken after the agreed on-site visit, for example, over additions and disposals of fixed assets. These delays have had an impact on the final audit fee.

We note that due to the departure of a key member of the Closedown team, a number of previously-agreed approaches to audit evidence have changed, in particular the evidence requested for the componentisation of Council Dwellings. This has caused delays to the work on the derecognition of components.

Since our initial report in September 2017 in relation to the issues faced in respect of fixed asset valuations, we have faced further significant delays in closing these off and finalising our audit work in these areas.

We formally wrote to the Chief Finance Officer on 29 September 2017 stating that we had identified a number of issues relating to the Authority's fixed assets, including but not limited to the valuation of social housing, other land and buildings, and investment properties, as well as the methodology adopted towards componentisation.

Since then, in attempting to resolve these issues we have been provided with numerous updated working papers as time has progressed. Unfortunately, in many circumstances during the last 15 months, these updated working papers have been found to be of poor quality, have not been checked prior to submission to us for audit evidence, and rather than resolve issues, have created further work and queries. In some cases we have had multiple versions of working papers, all incorrect.

At each stage of the audit, the Authority has provided us with timelines for the provision of information, whether that be for example updated valuation reports, trial balance reconciliations, or a bridge document detailing adjustments from the initial draft set of financial statements. Unfortunately, in the majority of these cases, deadlines were not met and staff which we had booked in order to review the updated evidence provided and undertake the additional work required, could not be fully utilised.

As a result of all of this, there is clearly scope for significant improvement through further development of working papers to enhance understanding, clarity, and the audit trail. We have raised a recommendation in respect of this, see recommendation 3 in Appendix 1.

Update on the audit fees

We stated during the Audit Committee on 27 September 2017 that the additional cost in relation to the additional work and ongoing delays to the audit was likely to be £71,250. This was discussed with the former Chief Finance Officer (S151 Officer) and was subject to PSAA approval.

We stated during the Audit Committee on 26 November 2018 that this had now risen, at that date, to approximately £300,000 in total (i.e. including original scale fee).

Further time has passed since those initial updates / estimate. Due to the planned nature of our approach to scheduled audits, the additional responsive work which we had to undertake was predominantly fulfilled by senior staff. We also had to engage additional services from our KPMG valuation specialist due to the issues found and the lack of readily-available evidence to support the valuations.

This highlights the importance of robust management review and the provision of clear audit working papers within the agreed timeframes.

We will be discussing our final proposed fee with the Authority's Chief Finance Officer and PSAA which will reflect the additional amount of work needed to gain assurance over your financial statements.

Trial balance reconciliation

We requested a trial balance reconciliation as part of our initial audit documentation request. This has historically not been provided to the audit team. A workaround is typically used, where the trial balance is reconciled piecemeal per section, as each working paper typically contains an extract of the trial balance.

However, in January 2018, there were concerns expressed by Officers that the trial balance may not have been appropriately mapped due to recharges.

We formally re-requested a reconciliation between the trial balance and the Authority's draft financial statements on 23 February 2018. We received a working paper on 26 April 2018; however, we had a number of queries in relation to this. Issues arose due to the initial working paper only being understood by one member of the Closedown team who had produced it, and this individual subsequently going on maternity leave. This shows the importance of a robust Closedown team and quality review, ensuring that key working papers and methodologies for producing financial statements are understood by all key members of the team, and clearly documented for audit purposes.

Throughout the summer of 2018, the Authority worked on this, and following meeting with the Authority's officers on 12 July 2018, it was agreed that a revised version of the 2016/17 trial balance mapping document would be produced for audit purposes. This was finally provided to us in late October 2018.

Data analytics

In response to the increased risk profile this year, we agreed with Management that we would enhance our testing of the Authority's payroll by utilising Data and Analytics (D&A) techniques. The use of D&A techniques allows us to undertake testing of 100% of the population, thus offering greater assurance to the Authority. Our D&A requirements were also communicated to the Authority within our PBC request.

Our D&A testing during the interim audit in March 2017 found exceptions and we conveyed the results to the Authority for follow-up. The Authority subsequently found that the exceptions were due to incomplete data provided to the audit team. We repeated the work with a second set of data, which resulted in fewer exceptions produced.

We undertook the year-end D&A testing on payroll in July 2017, and found further exceptions. These were also the result of incomplete data provided to the audit team. Again, this required us to repeat the work with a second set of data.

The duplication of testing meant that we incurred additional time and cost. This also impacts our ability to follow-up genuine exceptions whilst on site, and significant work on payroll had to be undertaken after the conclusion of our agreed on-site visit.

Response to audit queries

During our initial on-site visit in July 2017 and our subsequent audit visits and requests for information, on average, Officers dealt with our audit queries within four working days of inquiry.

However, evidence relating to some areas of sample testing took upwards of three weeks to be provided, such as additions and breakdowns of fixed assets. This caused significant delays to the audit process. Issues in relation to additions and disposals stem from the way in which the Authority accounts for the components of Council Dwellings.

As reported above, following our initial reporting in September 2017 regarding the issues relating to fixed assets, significant work has been undertaken to resolve this area, as well as others such as the trial balance reconciliation.

Unfortunately further delays have arisen due to the nature of these issues, and this has been exacerbated by changes in the Closedown team, as well as staff absences and key staff members leaving too.

There was also a limited handover from the previous S151 Officer to the current interim Chief Finance Officer who has had to pick up responsibility for closing down the audit and producing an updated set of financial statements.

Group audit

To gain assurance over the Authority's group accounts, we placed reliance on the work completed by Grant Thornton on the financial statements of Northamptonshire Partnership Homes.

There are no specific matters to report pertaining to the group audit.

Additional findings in relation to the Authority's control environment for key financial systems

We have tested controls as part of our focus on significant audit risks and other parts of your key financial systems on which we rely as part of our audit. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

In our *External Audit 2016/17 Interim Report* tabled in July 2017, we reported that there were a number of year end controls that we would be testing during our year end audit.

We have highlighted exceptions in relation to controls in Table 1 below.

Further detail and associated recommendations can be found in Appendix 1.

Table 1: Summary of control deficiencies

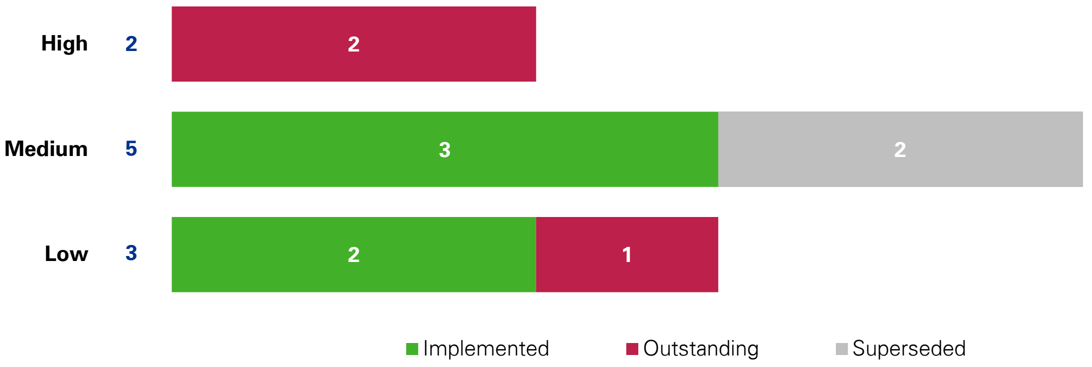
Control	Deficiency	Impact on audit	IA rating	Ref
Bank reconciliations	— There were unreconciled balances that the Authority has been unable to address. — A number of these balances relate to direct debit payments set up by third parties using the Authority's bank details. — A number of unreconciled items were incorrectly dated due to a system issue.	We could not place reliance on the Authority's bank reconciliations, particularly as the system does not correctly date the reconciling items. We performed substantive testing over the Authority's bank balance at the year end.	LGSS: Substantial PwC: N/A	*See rec. 1*
PPE instructions	— Formal instructions were not provided to the Authority's external valuers, Underwoods and Bruton Knowles. We understand instructions were provided verbally, and the overall points were followed-up by email.	We performed significantly more work to confirm that the valuation exercises were in line with Code requirements. We found that instructions were not properly-defined, which has led to numerous issues as discussed in the previous sections.	N/A	*See rec. 2*
General IT controls	— The Authority does not enforce its own password policy.	The Authority is not in compliance with its own IT policy; we have raised a recommendation in relation to this.	LGSS: Not reviewed PwC: Not reviewed	*See rec. 6*
Non-domestic rates (NDR) reconciliation	— We identified differences between cash and the expected payments as recorded by the Authority's NDR system (Academy). Some of these differences date from June 2016 which we would have expected to have cleared by year-end.	We performed additional work to understand the impact our findings have on the NDR balance.	LGSS: Substantial PwC: N/A	*See rec. 7*
Payroll reconciliation	— There is no evidence of review of the Authority's payroll reconciliation.	There is a risk that errors and fraud will not be detected. We have re-performed the control to obtain assurance over the reconciliation between the payroll system and the general ledger.	LGSS: Payroll not reviewed in 2016/17 PwC: Control not tested within the 2016/17 Payroll review	*See rec. 8*
Review of actuarial assumptions	— We were not originally provided with evidence to support the Authority's review of actuarial assumptions. Email evidence has subsequently been provided.	We were not able to conclude on this matter earlier, and additional work had to be undertaken to obtain assurance that actuarial assumptions have been reviewed by the Authority.	N/A	*See rec. 9*

Prior year recommendations

As part of our audit we have specifically followed up the Authority's progress in addressing the recommendations in last year's ISA 260 report.

Whilst the Authority has not fully implemented all or recommendations raised in our *ISA 260 Report 2015/16*, including the two high priority recommendations, we were satisfied the this has not impacted on our financial statements audit. See Appendix 2 for further details.

Chart 3: Summary of 2015/16 recommendations



Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 2016/17 financial statements.

Before we can issue our opinion we require a signed management representation letter. Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Northampton Borough Council for the year ending 31 March 2017, we confirm that there were no relationships between KPMG LLP and Northampton Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity. We have provided a detailed declaration in Appendix 5 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. A template will be provided to your Chief Finance Officer / Section 151 Officer for presentation to the Audit Committee upon the completion of our work. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgement, are significant to the oversight of the financial reporting process; and
- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc.).

Below we have set out matters of governance interest that have arisen during the audit or are matters which have been brought to our attention during the course of the audit. We will provide an update to the Audit Committee upon the presentation of this report, and will report in our Annual Audit Letter if there are further matters which we wish to draw to your attention in addition to those highlighted in this report.

Council Tax

During the course of the audit we have received, and accepted an objection from a local elector. The objection relates to the process the Authority has followed in setting Council Tax for 2017/18 and subsequent years, including the use of special expenses. Following completion of our work which included obtaining legal advice, we provided our findings to the individual in question, as well as the Authority. There were no issues to report.

Capital Projects: Procurement and Governance

During the course of the audit we also received an objection relating to the governance of a major capital works project. We were unable to accept this correspondence as an objection to the financial statements as it does not support there being sufficient evidence that the expenditure has been unlawful to date, which is one of the key requirements to accept an objection to the accounts.

Due to the nature of the matters bought to our attention during the course of the audit we have taken this into consideration as part of our overall value for money risk assessment in relation to the 2017/18 financial year, alongside wider matters of overall governance, procurement and contract management at the Authority. We are liaising with the Authority to obtain all necessary evidence and information to support this work and once completed will report back to the Audit Committee the findings of our work, included recommendations arising from any weaknesses we identify in the design or operation of the appropriate governance and financial control frameworks.

Completion

The departure of the Chief Executive

The Authority's previous Chief Executive departed the organisation in July 2017. The Chief Executive also acts in a statutory role as the Head of Paid Service. There is a risk that the terms and conditions of the departure, including any exit package, did not provide value for money to the Authority. We have reviewed the circumstances surrounding the departure of the Chief Executive in July 2017.

The Chief Executive resigned on 18 July 2017, and his last working day was effectively 31 July 2017 due to the Authority agreeing payment in lieu of notice. He also received outstanding holiday entitlement but no other payments were made at the time. As this was a resignation, no exit package was required nor agreed.

We have reviewed these payments and associated documentation and are content that the Authority followed appropriate processes.

However, we do note that Section 4 of the Local Government & Housing Act 1989 provides that it is the duty of every Local Authority to designate one of their officers as its Head of Paid Service.

During the period between 1 August 2017 and 6 September 2017 the Authority was in breach of legislation and did not have a Head of Paid Service in place as no interim measures had been prepared to deal with the departure of the previous Chief Executive in advance of his final leaving date.

The Authority stated that there were no other internal officers that could be appointed to the Head of Paid Service position given their experience and current workloads, and other statutory officers such as the Monitoring Officer could not act in dual statutory roles.

The Authority also stated that no significant staffing changes were being made that would engage the Head of Paid Service's statutory duties. The Chief Executive's powers, other than the Head of Paid Service's powers, were delegated to the Monitoring Officer who was supported by the Directors and the Section 151 Officer.

Full Council agreed on 17 August 2017 to approve the appointment of Simon Bovey as the Council's Head of Paid Service from 6 September 2017 until 5 March 2018. With George Candler now in post having been appointed the Authority's Chief Executive following Simon's departure.

Section three

Value for money

Our 2016/17 VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the Authority has not made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

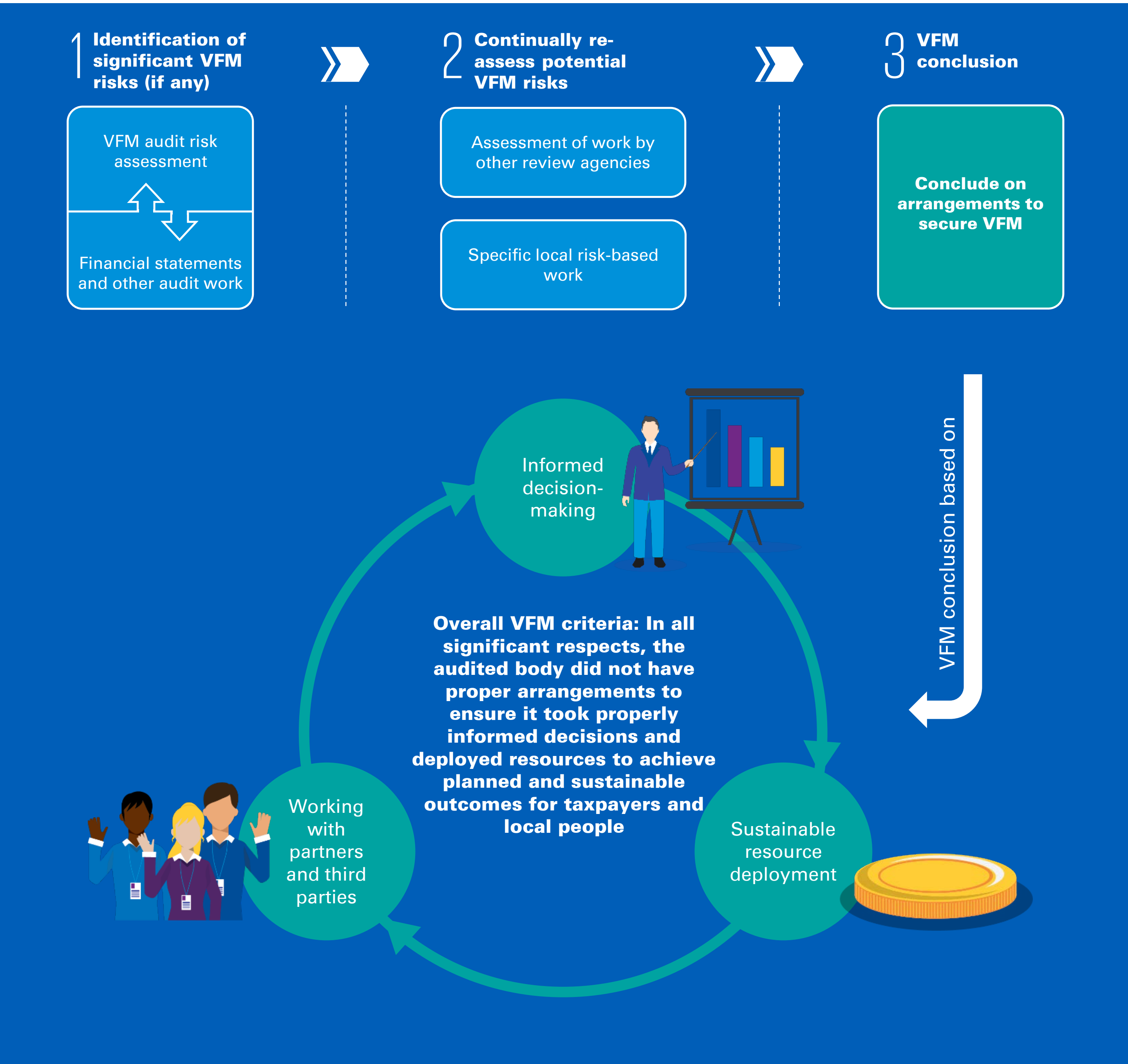
VFM conclusion

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority 'has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources'.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to 'take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor's judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body's arrangements.'

Our VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We follow a risk based approach to target audit effort on the areas of greatest audit risk.



1 Identification of significant VFM risks (if any)

VFM audit risk assessment

Financial statements and other audit work

2 Continually re-assess potential VFM risks

Assessment of work by other review agencies

Specific local risk-based work

3 VFM conclusion

Conclude on arrangements to secure VFM

VFM conclusion based on

Informed decision-making

Sustainable resource deployment

Working with partners and third parties

Overall VFM criteria: In all significant respects, the audited body did not have proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people

The table below summarises our assessment of the individual VFM risks identified against the three sub-criteria. This directly feeds into the overall VFM criteria and our value for money opinion.

Table 2: VFM assessment summary

VFM risk (2016/17)	Informed decision-making	Sustainable resource deployment	Working with partners and third parties
1. Governance action plan	✗	✗	✗
2. NTFC loan and the wider loans system	✗	✗	✗
3. Procurement	✓	✓	✓
4. Financial resilience in the local and national economy	✓	✓	✓
Overall summary	✗	✗	✗

In consideration of the above, we have concluded that in 2016/17, the Authority has not made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Further details on the work done and our assessment are provided on the following pages.

In arriving at this conclusion, we have reviewed the Authority's arrangements relating to a number of risks as documented in the table above.

Whilst we are satisfied that the Authority currently has appropriate arrangements in place to manage and deliver financial savings under increasingly difficult circumstances, as well as manage risks relating to the procurement of contracts during the year, our findings as a result of the NTFC loan and resulting internal audit report, as well as governance action plan, means we are unable to state that Northampton Borough Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Our findings indicate that there is an insufficiently systematic, robust, and objective due diligence process, and framework within which decisions can be made or documented.

Whilst we recognise that the Authority now has an action plan in place, as this was not produced until December 2016, it is clear that during this period there was an insufficiently systematic, robust, and objective governance process, and framework in place

We are therefore unable to state that Northampton Borough Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. As a result we anticipate issuing an adverse value for money opinion.

Further details on the work done and our assessment are provided on the following pages.

Significant VFM risks

We have identified five significant VFM risks, as communicated to you in our *2016/17 External Audit Plan*. In some cases we are satisfied that external or internal scrutiny provides sufficient assurance that the Authority's current arrangements in relation to these risk areas are adequate.

Significant VFM risks	Work performed
1. Governance Action Plan	**Why is this a risk?**

In December 2016, the Authority's internal auditors, PwC, issued a report on the Authority's Risk Management Policy and framework and to advise the Council on best practice. This was in response to the loss of £10.22 million in relation to the loan to Northampton Town Football Club (NTFC). In response to the PwC report, the Authority developed a Governance Action Plan in December 2016. This plan is a fundamental document for the Authority which contains all 11 recommendations made within PwC's report. There is a risk that issues and recommendations raised within the report are not addressed by the Authority.

Summary of our work

We obtained the Authority's Governance Action Plan and reviewed reported progress against this Plan. We have documented how the Authority measures and evaluates performance against each action, and assess this against supporting documentation.

The action plan is taken to each Audit Committee to update progress in implementation. As of 31 August 2017, the Authority recorded that 22 actions had been implemented (46%), whilst 21 had been partially implemented (44%) and a further 4 (8%) not implemented, and 1 (2%) to be confirmed.

Of those that are partially implemented, the Authority assigns a % complete status, which ranges from 15% to 90%, as well as a RAG on-track status. An example of measures included within the action plan but not yet fully implemented include:

- Monitoring of Cabinet decisions, implementation and compliance, including delegated decisions. To include regular reporting to the leader and audit committee;
- Post-implementation review of the operation and effectiveness of the Executive Programme Board since its establishment in late 2016;
- Identify and log all projects currently live and in the pipeline. Perform reviews of each project for feasibility and governance assurance;
- Risk reporting to be reviewed ensuring that there is an effective cascade and tracking of risk through governance arrangements;
- Develop and Implement enhanced Corporate project and Programme Management Framework and arrangements; and
- Establish a due diligence and compliance manual.

Significant VFM risks	Work performed
1. Governance Action Plan *(continued)*	Whilst we recognise that many of these actions have not yet passed their due date, in reviewing the arrangements in place during the 2016/17 financial year, it is clear that during this period there was an insufficiently systematic, robust, and objective governance process, and framework in place at the Authority. As the governance plan was only established in December 2016, it is clear that the actions can not have been suitably embedded during the 2016/17 financial year, and we are therefore unable to state that Northampton Borough Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.
2. NTFC loan and the wider loans system	**Why is this a risk?** In 2015/16, we issued an adverse conclusion on the Authority's arrangements to secure value for money. We were not satisfied that external or internal scrutiny provides sufficient assurance that the Authority's current arrangements in relation to loans is adequate. Subsequent to the loss of £10.22 million, the Authority has approved up to £950,000 to be spent on recovering the lost monies. **Summary of our work** The Authority advanced a loan of £10.25 million to Northampton Town Football Club (NTFC) to carry out works to improve stadium facilities and develop a hotel. The loans were due to be repaid through the provision of a first return to the Authority on the development of land adjacent to the stadium combined with some land previously leased to NTFC, and then through enhanced revenue streams available to NTFC through the hotel and stadium development. The loan made to NTFC and the financial management concerns around it have been widely publicised. Whilst our review into the circumstances surrounding the loan as well as subsequent actions undertaken is not yet complete, we have considered the information and findings so far as part of our VFM conclusion. We are unable to comment further on the findings of this specific review until complete. During the year, PwC issued their internal audit report into the loan in December 2016. A number of issues were raised and recommendations produced as a result. Internal Audit stated: *Cabinet approved a loan of up to £12 million, but this decision was based on limited information as a business case was not made available. A number of conditions were made by Cabinet and we have been unable to confirm that these were complied with fully, addressing all concerns. For these reasons, we have been unable to confirm that decisions taken were in line with the delegated authority…the information reviewed demonstrates that there was a lack of formal processes implemented and adhered to regarding risk management, project management, management information and performance management.* *We attempted to reconstruct the thought process for the decision made and for subsequent monitoring. Our view is that the Council failed to demonstrate this in its data room. This was made extremely difficult because of a lack of an approved business case, appropriate independent advice and documented risk management and governance processes.* *It is apparent that the overriding focus on the Sixfields redevelopment was on the operational aspects and subsequent governance arrangements failed to identify and address adequately the loan agreement.*

Significant VFM risks	Work performed
2. NTFC loan and the wider loans system *(continued)*	We have taken into account our findings from the 2015/16 and 2016/17 audits, our on-going investigation into the circumstances surrounding the loan agreement, and the internal audit report referenced above. Our findings indicate that there is an insufficiently systematic, robust, and objective due diligence process, and framework within which decisions can be made or documented. We are therefore unable to state that Northampton Borough Council had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. As a result we anticipate issuing an adverse value for money opinion.
3. Procurement	**Why is this a risk?** We identified management override of controls as a significant audit risk. Linked to this risk is the resulting impact on the Authority's procurement process. Non-pay expenditure was approximately £11.5 million (37% of total cost of services expenditure) in 2015/16. Discussions with NBC's internal auditors (PwC and LGSS Internal Audit) have highlighted that this is an area which has not been assessed in the last few years, which gives rise to a significant VFM risk. This is also linked to our prior year recommendations (see our ISA 260 reports in 2014/15 and 2015/16) where we recommended that the internal audit of key operational areas should be better co-ordinated between NBC's two internal audit providers. **Summary of our work** As part of our work we gained an understanding of controls over procurement and looked at how contracts are monitored throughout the year. During the year a new version of contract procedure rules were drafted but at the time of our review this was still awaiting authorisation from the Borough secretary prior to full Council approval. The Authority awarded four new contracts during the 2016/17 financial year and we reviewed how these had been procured and been awarded against the procurement policy and best practice guide. We found no issues to report back. As noted elsewhere in this report, during the course of the audit we received information relating to the governance of a major capital works project. We are currently conducting a separate review into this issue, as well as wider matters of overall governance, procurement and contract management at the Authority. We are liaising with the Authority to obtain all necessary evidence and information to support this work and once completed will report back to the Audit Committee the findings of our work, including recommendations arising from any weaknesses we identify in the design or operation of the appropriate governance and financial control frameworks.

Significant VFM risks	Work performed

4. Financial resilience in the local and national economy

Why is this a risk?

There has been a significant shift in the national outlook over the last 12 months, primarily driven by the outcome of the referendum on 23 June 2016 on the UK's membership of the European Union. Consequently GDP growth forecasts have been revised downwards, which potentially reduces the level of any growth in business rates income. Inflationary pressures, service pressures, and a reduction in the local government finance settlement will impact on the Authority's finances.

In December 2016, the Authority published a draft Medium Term Financial Plan 2017/18 – 2021/22 (which incorporates its Efficiency Plan published on September 2016) that sets out a balanced budget for 2017/18.

From 2018/19, the Authority has identified funding gaps; however it is confident that the targets in the Efficiency Plan are sufficient to bridge the forecast gap in the MTFP and are monitored by the management board. The Authority's proposed new governance arrangements include a specific officer board focussed on the delivery of the Efficiency Plan and associated improvement projects.

Summary of our work

Like most of local government, Northampton Borough Council faces a challenging future driven by funding reductions and an increase in demand for services. At a local level, this is compounded by the County Council's financial difficulties.

During 2016/17, the Authority set a General Fund Budget for controllable service budgets of £31.3 million. This consisted of a mixture of income generation and efficiency savings. The actual outturn reported was £29.9 million, a £1.4 million variance, mainly attributable to underspends relating to the Director of Customers and Communities (£1.3 million) and debt financing savings of £456k, which mitigated overspends in other areas such a £543k adverse variance to plan in Housing and Wellbeing relating to additional costs of Homeless Prevention schemes, Refuge funding, higher Temporary Accommodation costs and a reduction in Licensing Income.

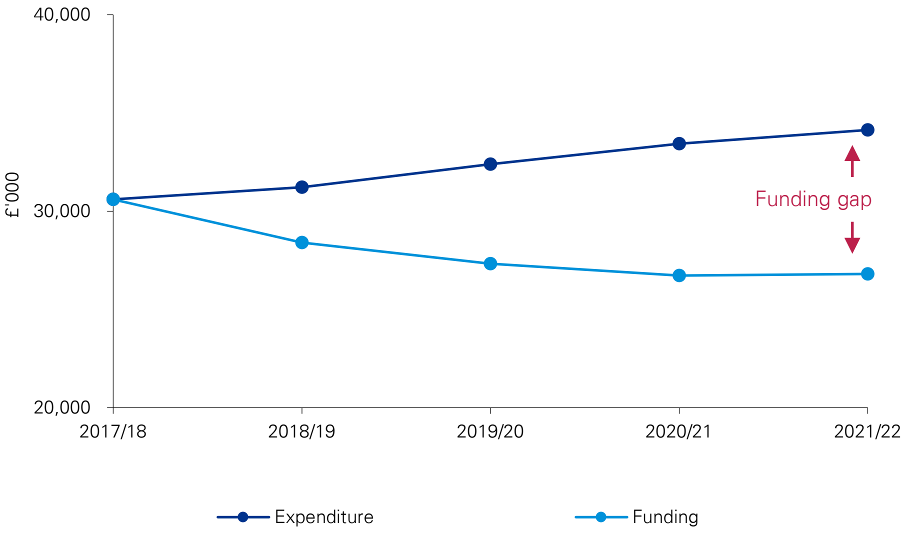
The Authority decided to use the underspend to mitigate risk and invest in future service improvements, with £1.048 million being used as contribution to the MTFP cash flow reserve, £181k towards the project budget carry forwards, and £124k for improved governance and the Greyfriars Redevelopment. As a result there was a £30k contribution to the General Fund.

Furthermore, the Housing Revenue Account had a budget of £7.5 million during the year, but reported an underspend of £366k due to a mixture of factors including lower interest and financing costs and bad debt provision not being required.

The Authority's capital budget for 2016/17 was £19 million, an increase of £5.8 million from the original budget of £13.2 million. Of this, capital outturn reported spend of £12.4 million, an underspend of £6.6 million, mainly relating to the timing of the commencement of various schemes which will continue into 2017/18, and fall within the Regeneration, Enterprise and Planning. Of the total spend, the Authority used borrowing of £4.7 million to fund capital works, with the rest being met by capital receipts, grants, and third party and revenue contributions. The use of borrowing in year helped mitigate the non-realisation of £5 million of budgeted capital receipts. These are now expected in 2017/18.

Significant VFM risks	Work performed
4. Financial resilience in the local and national economy *(continued)*	During the financial year the Authority has also utilised a total of £12.8 million in reserves. Of this £5.7 million was utilised from the General Fund, although £8.2 million of new reserves resulted in a net increase of £2.5 million. Of this, £1.2 million related to increases in the Future Pressures Reserve and £2 million relating to Rates Retention Deficit Funding. The Authority utilised £7.1 million from the HRA Reserve, resulting in an overall HRA reserves decrease from £18.2 million to £11.1 million. For 2017/18, the Authority set a net budget of £29.1 million, which includes the requirement to achieve £2.8 million of savings during the financial year, being a mixture of additional income generation (£683k) and reduced expenditure from general efficiencies (£1.6 million), economic growth (£172k) and other technical savings including debt financing (£282k). Over the subsequent years, the Authority has set an overall net budget requirement which increases from £29.1 million in 2017/18 to £32.5 million in 2021/22. Within this the service base budget increases negligibly from £28.52 million in 2017/18 to £28.55 million in 2021/22 (0.1%), with the majority of the increase stemming from budgeted contributions to reserves moving from £649k to £3.4 million in the same period. The result of the budgeted contribution to reserves is a perceived funding gap commencing in 2018/19 of £3.9 million, arising to £5.4 million in 2021/22, a total of £16.1 million during the period. Taking into account the £13.4 million allocated to building up reserves in the same period, the net funding gap would otherwise be £2.7 million. Feeding into the budget, the Authority has assumed a decrease in Revenue Support Grant from Central Government from £1.8 million next financial year to zero funding from 2019/20 onwards. Additionally funding from the New Homes Bonus reduces from £4.2 million in 2017/18 to £2.1 million by 2021/22.

Chart 4: The Authority's MTFP



Significant VFM risks	Work performed
4. Financial resilience in the local and national economy *(continued)*	However, it is worth noting that the Authority has budgeted based on the assumption that funding from the Business Rates Retention Scheme will continue to increase during the period, from £7.6 million to £8.1 million by the end of the Medium Term Financial Plan. There is a risk attached to this due to the uncertainty provided by Central Government as to how this scheme will operate going forward and the Authority needs to ensure that budgeted assumptions are based on the latest information available to them and updated accordingly as the future of the Scheme is debated. The financial pressure on the Authority is therefore likely to increase over the coming years and it is imperative that work continues to identify savings well in advance of the most difficult periods within the Medium Term Financial Plan, most especially savings which may require initial investment and a longer lead time to realise their benefits. The Authority has a positive track record of delivering savings, but this will only get more difficult. The Medium Term Financial Plan only detailed savings predicted up until 2020/21, and over this period a total of £7.5 million have been included in the budgets, although the Authority has set far higher targets of £21.9 million. This leaves unidentified savings of £14.4 million from 2018/19 onwards. Furthermore, difficult decisions will need to be made in respect of other sources of funding such as Council Tax, as more Authorities begin to increase this in order to mitigate the financial pressures felt elsewhere and maintain the desired level of services to the public. Careful financial planning is required, and the Authority should also ensure that the assumptions it feeds into its Medium Term Financial Strategy (such as demographics, service demand etc.) are regularly refreshed to provide an up-to-date and reliable indicator of future pressure points. We have reviewed the arrangements the Authority has in place to manage and deliver financial resilience during the 2016/17 financial year. Our work has included a critical assessment of the Authority's Medium Term Financial Plan and a review to ensure that budgeting is sufficiently robust to ensure the Authority can continue to provide services effectively. We continued to meet regularly with the S151 Officer to and key staff to understand the Authority’s financial position and assessed the adequacy of its arrangements to ensure it has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

Appendices

Appendix 1

Key issues and recommendations

Our audit work on the Authority's 2016/17 financial statements have identified a number of issues. We have listed these issues in this appendix together with our recommendations which we have shared with Management. Responses from Management are included after each recommendation.

The Authority should closely monitor progress in addressing the risks, including the implementation of our recommendations. We will formally follow up these recommendations next year.

Each issue and recommendation have been given a priority rating, which is explained below.

High priority	Issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.
Medium priority	Issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.
Low priority	Issues that would, if corrected, improve internal control in general but are not vital to the overall system. These are generally issues of good practice that we feel would benefit if introduced.

The following is a summary of the issues and recommendations raised in the year 2016/17.

2016/17 recommendations summary

Priority	Number raised in our interim report	Number raised from our year-end audit	Total raised for 2016/17
High	1	5	**6**
Medium	–	4	**3**
Low	–	2	**1**
Total	**1**	**11**	**12**

High priority

1. Review of bank reconciliations

We reviewed the Authority’s year-end bank reconciliation. There are unreconciled balances that the Authority has been unable to address. Some of these balances were over a month old.

A number of the unreconciled items within the Authority’s Benefits bank account relate to direct debit payments set up by third parties using the Authority’s bank details. The Authority provides its Benefits bank details on payment forms to allow individuals to deposit payments directly into the Authority’s bank account. The Authority’s banker had honoured those direct debits. These were reimbursed by the bank subsequent to queries by Officers.

We also identified that a number of unreconciled items were incorrectly dated, for example, an item which appeared to be a reconciling item from January 2016 was in fact a reconciling item from November 2016. Officers have stated that the system records an incorrect date when the reconciling item appears between the first and twelfth day of each month.

Based on the issues identified above, we were unable to place reliance on the Authority’s bank reconciliations.

Recommendation

The Authority should issue instructions to its banker not to honour direct debit payments out of its Benefits bank account.

The Authority should investigate and resolve all outstanding unreconciled items within the month in which it occurs. The Authority should also establish a system of reconciliation which supports monthly reconciliations on a timely basis and provides the correct date for each item.

Management response

Accepted.

The authority have contacted their banker who has advised they are unable to stop Direct Debits being set up on the account, however when a fraudulent DD is reported they refund the amount and put a block on that Direct debit being taken again. Internally there are two reconciliations undertaken which ensure that fraudulent direct debits are identified.

LGSS finance operations as the authority's provider of banking reconciliations have redesigned their bank reconciliation working paper and is applying this across all clients which resolves the date issue. Also the authority are focusing on resolving unreconciled items in a more timely manner and writing off any minor items where appropriate.

Owner

LGSS Business Systems Improvement Manager.

Deadline

Already actioned and ongoing.

High priority

2. Valuation of Property, Plant and Equipment (PPE), including Council Dwellings

We faced significant difficulty in our work on the Authority's PPE. In the prior year, we raised a recommendation on the valuation of Council Dwellings. Our work this year has found issues more broadly in relation to PPE.

In the current year, the Authority has used three separate valuers for the valuation of its PPE (including Council Dwellings) and investment properties:

- Land and buildings: internal valuers and Underwoods. Underwoods were engaged by the Authority due to capacity constraints within the Estates team.
- Council Dwellings: Underwoods, and subsequently Bruton Knowles
- Investment properties: Underwoods

Formal instructions to external valuers

We identified that no formal valuation instructions were sent to the external valuers, Underwoods and Bruton Knowles.

Summary of external valuation

Type of asset	Valuer	Assessment of instructions
— Land and buildings (non-HRA) — Investment properties	Underwoods, date instructed not available	No formal written records of instructions were sent to Underwoods. As a result, we were not able to confirm that Underwoods had complied with the valuation request, which would have included a list of assets to be valued. We had to undertake additional work to reconcile the list of assets reviewed against the valuer's output. We were also not able to confirm that the Authority has instructed its external valuer in line with the requirements of the Code and other applicable valuation and accounting standards. We engaged our KPMG specialist to perform additional substantive work to provide assurance that the valuations were in line with applicable standards.
— Council Dwellings	Underwoods, instructed February 2017 Bruton Knowles, instructed April 2017	Two in-year valuation exercises were requested: the first by Underwoods in February 2017, and the second by Bruton Knowles in April 2017. For the April valuation exercise, the Authority asked its valuer to utilise "alternative beacons where necessary", without considering the impact of this request. As a result, we were unable to initially agree inputs in relation to Council Dwellings. Further work was required to provide us with this assurance.

Valuation reports

The Authority did not request a full valuation report from Underwoods. This is not in line with Code requirements. In response to our inquiries, a second valuation was undertaken for Council Dwellings in April 2017 by Bruton Knowles, for which we have received a valuation report on 23 June 2017.

We received the valuation report for 'other land and buildings' and investment properties on 4 August 2017 which was undertaken by Underwoods. The late receipts of these reports delayed our assessment of the valuation results.

2. Valuation of Property, Plant and Equipment (PPE), including Council Dwellings *(continued)*

Valuation review and challenge

For Council Dwellings, we noted that there was an initial review by the Authority on the results of the valuation exercise undertaken by Underwoods. This review by the Authority was undertaken with incomplete information as no valuation report was prepared by the valuer. This had not been requested by the Authority.

Bruton Knowles subsequently took on the valuation review of Council Dwellings and provided both the valuation results and a valuation report. The Authority had performed a review of the valuation results. However we note that:

- the Authority was not aware that the valuer had used the social housing discount factor (EUV-SH) for the South East instead of East Midlands. This is evident during our initial discussions with the Authority.
- the Authority was also not aware that the social housing discount factor had changed. This is evidenced by the initial draft of the accounts, where the old EUV-SH of 34% was stated;
- the Authority had not considered the impact of instructing the valuer to use "alternative beacons where necessary"; and
- the valuation was performed on a desktop basis. We understand that this was requested verbally by the Authority, and this methodology was chosen due to time pressure. This methodology is a departure from Code requirements and the Authority's accounting policies. This departure was not disclosed within the Authority's accounts, nor assessed for compliance with Code requirements. Upon our initial feedback to the Authority on this matter, Officers made the decision to ask for a full valuation exercise. This was carried out on 16 September 2017 on the same 20% of beacons. We are still evaluating the results of this new exercise.

For 'other land and buildings', our valuation specialist was unable to obtain assurance over key inputs used for the valuation process due to the high turnover within the Estates team. Work on this is still ongoing.

Overall assessment

We note that there is no overall strategic ownership and compliance review by an appropriately-experienced individual at the Authority. The valuation process in the current year appears to be on an *ad hoc* basis, with no written process notes or standard valuation procedure. This is particularly important given the high turnover within the Estates team during the past two years. We note that there has been limited consideration of how the valuation exercise aligns with requirements of the Code or audit requirements, in particular:

- the requirement for a valuer's report;
- the formalisation of valuer's instructions, including a list of assets to be valued;
- consideration of an audit trail in relation to assets to be valued;
- an assessment of the impact of 'alternative' beacons, where identified;
- the requirement for a full valuation instead of a desktop valuation for assets valued within the 5-year cycle;
- an assessment of the valuer's assumptions, in particular the justification for a social housing discount factor outside of the DCLG's guidance; and

2. Valuation of Property, Plant and Equipment (PPE), including Council Dwellings *(continued)*

— the timeframe and output to allow early review and assessment in light of the early closedown period in 2017/18.

The reactive nature of this year's valuation process has resulted in significant delays and non-compliance with Code requirements.

Recommendation

The Authority should formulate a formal policy and process for valuation, including establishing an overall strategy and position responsible for oversight over the valuation process. The individual(s) responsible should be suitably-qualified or experienced. They should be able to assess compliance of the valuation process and results against Code requirements as well as other applicable valuation and accounting requirements. This includes awareness of valuation requirements that are specific to the local government sector, for example, the DCLG's *Stock Valuation for Resource Accounting (SVRA).*

The valuation process should align to the Authority's closedown timetable, including a consideration of deliverables ahead of the year-end period. The process should be co-ordinated across the various valuers used (whether internal or external). The individual(s) responsible should oversee the transaction of valuation outputs into the Authority's fixed asset register, and subsequently oversee the production of good-quality working papers which contain clear audit trails (see recommendation 3 for further commentary on working papers).

Written instructions should always be issued to the Authority's valuers, whether internal or external. The instructions should require the valuers to comply with the Code and other requirements, specifically, the *Red Book* (*RICS Valuation – Professional Standards UK January 2014, revised April 2015*) for all valuations prior to 1 July 2017, and the *RICS Valuation – Global Standards July 2017* for all valuations going forwards. Valuation instructions should be agreed in advance with the valuer, with any departure from standard practice and requirements highlighted in both the instructions and the valuation report. The instructions should also reflect any variations agreed verbally between the Authority and the valuers.

There should be a clear record of all assets, including the date of last valuation and the valuer responsible. Instructions sent to the valuer should be accompanied by a list of assets due to be valued in a particular year; this list should be readily reconcilable to the Authority's master records.

The process should also include a formal review of valuation results, including any assumptions made by the valuer. The valuer should be instructed to present key valuation considerations and supporting evidence to enhance credibility and transparency to the values reported. Where necessary, the results and/or assumptions should be challenged, including the use of any alternative social housing discount factor. This challenge should be recorded and an audit trail maintained to ensure availability of records.

The Authority should require a valuation report to be produced to accompany the numerical valuation outputs, in line with the *Red Book* (*RICS Valuation – Professional Standards UK January 2014, revised April 2015*) for all valuations prior to 1 July 2017, and the *RICS Valuation – Global Standards July 2017* for all valuations going forwards. Special consideration needs to be given to valuation of Council Dwellings and the reporting requirements contained within the DCLG's *SVRA*.

Clear rationale over inputs and records (for example, comparable market data) should be recorded by the Authority's internal valuers, given the high turnover within the Estates team. This will help mitigate the difficulty experienced in the current year over obtaining assurance over the valuation inputs.

2. Valuation of Property, Plant and Equipment (PPE), including Council Dwellings *(continued)*

Management response

Accepted.

A working group led by senior officers from Finance and Property, is considering all aspects of the valuation of PPE. The objective of the group is to provide accurate, evidenced valuations of the Authority's PPE. Where appropriate, external resource is being procured in order to provide both a new baseline for the valuations and a robust process that can be followed into the future. The various regulatory requirements, detailed in the SVRA and elsewhere, are being applied to direct this work. The focus will be on ensuring valuation reports include appropriate supporting evidence including comparables, etc, and this is contained within instructions to external valuers

Owner

Corporate Assets Team.

Deadline

The instructions to external valuers by end of January 2018 and review of received reports by end February 2018.

High priority

3. Preparation and review of audit working papers

We stated in our *External Audit 2016/17 Interim Report* dated April 2017 that the Authority had implemented our recommendation in relation to the preparation and review of audit working papers. Whilst we acknowledge that the Authority has made efforts to improve working papers (including the use of KPMG Central), we subsequently identified significant issues during our final audit in July 2017.

The audit team undertook an audit debrief and workshop in October 2016 to analyse key issues which we found with the prior year's working papers. We also worked with the Authority in the preparation of our draft *Accounts Audit Protocol* (PBC requirements) in December 2016, and based on our discussions with Officers, issued the final PBC requirements in January 2017. We followed this up with a meeting with the Closedown team to discuss specific requirements of the document request list in March 2016. We have also offered further support and opportunities to discuss specific requirements of audit requests.

Nonetheless we found quality issues on the Authority's working papers, which are similar to the issues which we identified last year. These are:

- Many working papers were not checked against the requirements listed in the *Accounts Audit Protocol*. Despite being signed off, we found gaps in the provision of information; and
- Breakdowns provided within working papers did not tie to the draft accounts. This demonstrates a lack of audit trail, which adds to the difficulty in understanding the Authority's working papers.

Key audit areas of concern are:

- Fixed assets: The Authority had not provided key outputs from valuers ahead of the audit as previously agreed. We did not receive any working papers on valuation which led to difficulty in agreeing valuers' reports to the accounts. In addition, Authority had significant difficulty and delayed providing us with a breakdown of additions and disposals of Council Dwelling components. We also had difficulty in understanding the Authority's workings in relation to componentisation;
- Payroll: There was no audit trail and we had to spend a significant amount of time with Officers to understand the working papers; and
- Debtors and creditors: Not all breakdowns were provided; this did not meet our PBC requirements which had been agreed with Officers. In addition, where breakdowns were provided, these did not always agree to the accounts or to the Authority's general ledger.

We note that some of the working papers with issues were prepared by individuals outside the Authority's Closedown team, but nevertheless should have been subject to senior management review prior to submission to the audit team.

There were numerous emails provided, both as part of the initial PBC but also subsequently throughout the audit (particularly in relation to PPE). We found working papers (in particular in relation to fixed assets) that consisted predominantly of embedded emails and documents. This led to significantly more work as information was dispersed within multiple emails and working papers.

Recommendation

All working papers should be provided by an agreed date, typically prior to the start of an on-site audit visit.

The Authority should ensure that all key closedown staff receive and review the agreed *Accounts Audit Protocol* prior to producing working papers for the audit. The review should be robust and reviewers should conduct an independent assessment of the working papers to ensure that the working papers can be understood by a third party.

3. Preparation and review of audit working papers *(continued)*

Where breakdowns of balances are required by the *Accounts Audit Protocol*, these should be provided. The sum of the breakdown should agree to the audited balance, per the figures in the accounts submitted for audit.

Information should be contained and set out clearly within working papers, as much as possible, without the need for the audit team to review multiple emails or embedded documents to understand the evidence. Where there is a need to support the evidence via emails, these can be referred to as supplementary documents, but these should not form the bulk of the working paper.

The overarching principle is that working papers should provide a clear and concise audit trail from the financial statements through to sufficient and appropriate evidence within supporting working papers. Working papers need to:

- be clear, with explanations if needed. The working papers need to be written from the view point of someone external to the organisation;
- be supported by strong evidence, for example, third party documentation; and
- agree to the financial statements provided for audit.

Management response

Accepted.

The audit working papers provided have not been of a consistently acceptable standard in certain areas and new requirements will be documented and communicated before the next closedown. This will be supported by training and coaching, followed by a final QA before papers are released to the audit team. The key objectives are to provide a standard template, which includes date and source, together with estimations that have been applied. The format and content is to be of sufficient clarity that a third party can understand the details without further reference to the author.

Improvements implemented for 2017/18 closedown.

Owner

LGSS Integrated Finance Group Accountant.

Deadline

March 2018 (missed – delivered January 2019).

High priority

4. Fundamental review of financial reporting and accounts production process

The *Accounts and Audit Regulations 2015* introduced a statutory requirement to publish the accounts with an audit opinion by 31 July. This requirement comes into effect in the financial year ending 31 March 2018. The Authority is aware of this and we have sought early engagement with the Authority this year, in line with guidance from the National Audit Office (NAO) in AGN 06.

In light of this, we have agreed a staged approach for 2016/17, with key audit areas to be reviewed during our interim audit visit beginning 6 March 2017. We reported in our *External Audit 2016/17 Interim Report* (dated April 2017) that we were not able to do this due to delays. These were primarily in relation to:

- fixed assets valuation reports; and
- the restated CIES and EFA.

During our final audit visit in July 2017, we noted not all working papers had been provided, most significantly for fixed assets. We also noted various issues with the quality and availability of audit evidence (see recommendation 3).

We understand the departure of valuers within the Estates team as well as a key member of the Closedown team contributed to the delays and issues noted.

We also noted issues in relation to the quality and completeness of the draft accounts provided for audit:

- the note to the EFA was missing; and
- the Cash Flow Statement was wrong. It contained figures which we did not recognise nor were we able to tie these back to the accounts. Upon query, we were advised that this was the result of time pressures. A version of the new Cash Flow Statement was provided for audit by the Closedown team to ensure the accounts were complete, despite being wrong. This doubled our audit work as we had to audit the statement twice.

Significant audit work continued from September 2017 until December 2018, finalising key areas, in particular, fixed assets. The audit work this year has been beyond the initial three-week final audit period in July 2017, which was planned, agreed, and budgeted with the Authority. As reported, the delays have had a significant impact on the final audit fee. This is additional to the extra work required for it being a “high risk” audit.

Given the issues we have seen, both in the production of the accounts and the provision of audit working papers, the Authority was unable to meet the earlier statutory deadlines in 2017/18, and this audit has yet to commence at the date of this updated report. There is also a risk that the Authority is unable to meet the deadline to produce draft 2018/19 financial statements without significant changes to the current manner by which it produces its draft accounts, including changes to ensure that it produces good-quality working papers to support the accounts.

Recommendation

There should be a strategic and fundamental re-evaluation of the Authority’s approach to the production of its financial statements and audit working papers. The Authority should aim to be in a position where key financial transactions such as additions, disposals, accruals, recharges, etc., are posted to the ledger on a regular basis. The Authority has put in place a new Closedown Team in 2016/17 to improve its accounts production and audit performance; this has not proven to be as effective as both sides had initially anticipated.

In line with best practice which we have seen elsewhere in the public and the private sector, the Authority should aim achieve financial closedown at the end of every month. The Authority currently achieves closedown once a year, which has the effect of accumulating financial transactions towards the financial year end. This places immense pressure on the Authority’s Finance team and Closedown team to meet year-end deadlines. The Closedown team is

4. Fundamental review of financial reporting and accounts production process *(continued)*

effectively being asked to compress a year's worth of financial transactions and analysis into a relatively short period of time.

The achievement of an earlier closedown in 2018/19 cannot be achieved by maintaining *status quo*. Initially, the Authority should aim to implement quarterly financial closedowns as an interim measure until monthly closedowns can feasibly be achieved. This will involve the wider finance team and a change in current processes. Budget holders and other key contributors (such as valuers) will also need to be part of this joint effort; this will be a significant change in the wider corporate culture.

Management response

Accepted.

The approach to financial reporting and accounts production process is being reviewed in order to ensure that outputs are complete, accurate and code compliant. This will be underpinned by a more robust approach to ledger maintenance and periodic reporting, by issuing procedure guides to relevant colleagues from other functions and external agencies and through delivering training and guidance within the finance team.

Owner

LGSS Integrated Finance Group Accountant.

Deadline

For Accounts production by 31st May 2018 (missed – now to demonstrate for SoA 2017/18).

High priority

5. Componentisation of Council Dwellings

The Authority changed the way it accounted for the components of Council Dwellings in the third quarter of 2015/16. The Authority had grouped individual components by type into one "global" component type, for example, kitchens, bathrooms, etc. We highlighted in our *External Audit Report 2015/16* that this was a change that introduced a new element of estimation which was not disclosed within the Authority's accounting policies. We note that this policy has also not been disclosed in this year's financial statements.

Calculation of the estimate

The Authority now estimates the amount of component disposals as a percentage of component additions. This percentage is based on historical data.

For example, if the Authority knows that on average it replaces a kitchen that was worth £2,000 with a new kitchen that is worth £10,000, the percentage calculated is 20%. Thus for every £10 it spends on kitchens, it derecognises £2.

Rationale for change

The Authority stated in 2015/16 that this change was designed to reduce the amount of manual inputs into the fixed asset register. The Authority was able to demonstrate that in 2015/16, the difference between the old and the new methodology was not material, however it anticipated this figure to be larger in 2016/17. We agreed with key Officers that for 2016/17, the Authority will need to demonstrate that the difference between the old and new methodology would not be material. However the Authority did not produce this analysis in the current year due to departure of a key member of the Closedown team.

Estimates, uncertainty, and complexity

This new methodology is an accounting estimate which introduces a particular margin of error. It is a move away from the purpose of componentisation, which was first introduced in IAS 16 and adopted by the Code in 2010/11 in order to further refine asset values, that is *to further refine an existing estimate*. The Code states that estimates can be a faithful representation if the amount is described clearly and accurately as being an estimate, the nature and limitations of the estimating process are explained, and no errors have been made in selecting and applying an appropriate process for developing the estimate. This has not been the case as no such disclosure exists.

The Code further states that 'as a result of the uncertainties inherent in delivering services, conducting trading or other activities, many items in financial statements cannot be measured with precision but can only be estimated'. We note that the use of this new estimate is not the result of inherent uncertainties, but a move to reduce processing of asset values.

Whilst the original methodology does to a certain extent involve estimates (for example, useful life of a component and the overall valuation of a building), these are established estimates and the estimation process of these values is governed by professional standards and carried out by qualified individuals. The new methodology introduces further uncertainties and decreases precision of the components' valuations. This new accounting estimate has ultimately increased uncertainty, adds complexity to the process, and significantly increases audit work.

Audit impact

We faced difficulty in understanding the Authority's working papers in relation to estimates. Conversely, the Authority had difficulty in providing the audit team with a breakdown of component additions and disposals in year and caused additional work in obtaining necessary audit evidence. As at the time of writing, we have further outstanding queries in relation to the derecognition of components in quarter 4. In line with accounting requirements, we have asked the Authority to prove that this new estimate is based on the latest available, reliable information.

We note that there was an audit difference found in the prior year resulting from the application of this new componentisation estimate, which was not adjusted.

5. Componentisation of Council Dwellings *(continued)*

Overall assessment

Whilst we understand the rationale driving this change in the accounting for components of Council Dwellings, the Authority has faced difficulty in justifying the reduction of precision on the basis of materiality. The calculation is complex and has caused delays to what should have been a straightforward area of audit. The amalgamation of components has removed the audit trail as the Authority is unable to easily reconcile the disposal of a particular component to the breakdown of its component disposals.

Recommendation

The Authority should account for its Council Dwellings components in line with IAS 16 and Code requirements going forwards. This will increase precision and provides a clear audit trail. It will also remove complexity from the process. The Authority should consider alternative methods in reducing the manual processing of asset values, for example, the use of automated scripts within its fixed asset register system.

However, should the Authority choose to continue using its new methodology of accounting for components of Council Dwellings, the Authority will need to be able to provide evidence that the estimates used are based on the latest available, reliable information. The Authority should disclose this change within its accounting policies, as well as explain the nature and limitations of the estimating process. In order to ensure that its estimates are current and based on the latest available, reliable information, the Authority will need to perform an annual assessment of this estimate. There should also be special consideration of the audit trail of additions and disposals, and the ease of which these can be evidenced to external auditors.

Management response

Accepted.

The Authority acknowledges that the approach previously taken to the componentisation of Council Dwellings was complex. A new process, focusing on the requirements of IAS16 and the Code, is being implemented and is supported by the wholesale review and revaluation of the housing stock. The Authority has also considered examples of best practice approaches applied in other authorities when confirming the changes required. Accounting policies will be amended as necessary in support of this change and disclosures on the nature, approach and extent of estimation will be clearly disclosed within the Statement of Accounts. The changes being applied will lead to more accurate, evidenced records and special emphasis will be placed on the need to provide details of the extent, value and implications of any changes to the housing stock during the year.

Owner

LGSS Integrated Finance Group Accountant.

Deadline

April 2018 (implementing for 2017/18).

Medium priority

6. General IT controls – Passwords

We tested the Authority’s general IT control environment this year and key IT applications, which are Agresso, Academy, Northgate, and RAM.

We noted that the Authority has documented a password policy as part of its information security policies:

- Use passwords with a minimum length of 8 characters.
- Change passwords at regular intervals of no more than 60 days, or as the application requires.
- Last 20 passwords remembered
- Complexity should be enabled

Our testing found that the password complexity option has not been enabled on Agresso and Academy. We also found that the minimum password length has not been enforced on RAM.

Recommendation

The Authority should enforce the password policy across all of the IT applications used by the Authority.

Management response

Accepted.

The Authority accept the finding and are instructing the system owners to implement password controls as per the current policy.

Owner

Head of Customer and Cultural Services.

Deadline

March 2018.

Medium priority

7. NDR reconciliations

We have identified differences between cash and the NDR system in relation to payments received by the Authority. Some of these differences date from June 2016, which has not been resolved at year end. We understand that these are still being investigated.

Recommendation

The Authority should continue to investigate reconciling items between cash received and its NDR system.

Management response

Accepted.

It is agreed that there were unreconciled items at the end of March 2017. The Authority considers these amounts as highly trivial as the total represents 0.007% of the total cash received for business rates, and therefore not efficient to continue to investigate further. However, the Authority accepts that the cash should reconcile and since April 2017 the staff within LGSS Revenues and Benefits have ensured that items are reconciled within the following month so that any issues can be identified and system corrections made promptly.

Owner

LGSS Revenues and Benefits Systems Team Leader.

Deadline

N/A

Medium priority

8. Payroll Reconciliations

The payroll function was transferred from LGSS to the Authority in January 2017. We were not able to review payroll reconciliations performed by LGSS from Period 1 to Period 9 as records were lost during this move.

For Periods 10 to 12, we were able to review the payroll reconciliation performed by the Payroll Manager. We understand that this reconciliation was meant to be reviewed by a member of the Finance team; however we were unable to verify this as no evidence has been retained. We were unable to state that there has been appropriate review and segregation of duty as part of the payroll reconciliation. There is a risk that this exposes the Authority to fraud and/or error.

We understand that the Payroll Manager is updating the payroll processes at the moment, and anticipates formalising this review process.

Recommendation

The review process should be formally documented. This allows the Authority to demonstrate review and reduces the risk of fraud and/or error. Where there are system changes, records of key controls will need to be retained for audit purposes going forwards.

Management response

Accepted.

The LGSS Finance Business Partner Team have been working with NBC Payroll to review and refine the monthly payroll reconciliations. This was finalised at the end of December for the cumulative reconciliation for the 9 months in 2017/18 to that point. Going forwards the counter sign-off from HR management and then LGSS Business Partner Finance will be done monthly.

Owner

LGSS Senior Finance Business Partner supporting Borough Secretary.

Deadline

December 2017 and ongoing monthly.

Low priority

9. Review of actuarial assumptions

The Authority is a member of the Northamptonshire Pension Fund (LGPS) which is required to undergo a full valuation every three years. As part of the full valuation process in 2016/17, the Authority is required to submit information about its members, as well as review and challenge the actuarial assumptions. These are both financial and non-financial assumptions.

The Authority's actuary has stated in its February 2017 briefing note:

> *"We therefore strongly recommend that you consider the suitability of the default assumptions to your specific organisation".*

Assumptions used will impact the balance sheet and the following year's CIES.

The Authority was initially unable to demonstrate a review of the assumptions or demonstrate the acceptance of the default actuarial assumptions used as part of the valuation process. Upon our feedback, the Authority subsequently produced emails which demonstrate review of actuarial assumptions.

Recommendation

The Authority should formally evidence the review of all assumptions used by the Actuary to ensure relevance to the organisation. Where appropriate, the Authority should challenge these assumptions.

Management response

Accepted.

The Authority will look to ensure that the actuarial assumptions are formally reviewed and challenged where appropriate.

Owner

LGSS Strategic Finance Business Partner.

Deadline

March 2018.

Low priority

10. ITGC – RAM Leavers

A member of finance (Amy Eyles) left NBC in September 2018 however it was noted that her RAM account had been used post her leaving date and her account. It had been used by the RAM consultant who was required for the volume of work required to remove original incorrect Council Dwellings valuations and upload correct valuations as a result of audit adjustments.

Best practice would suggest that all leavers are removed from entity systems in a timely manner. There is a risk that the leavers' account if not closed, could be used for inappropriate amendments to the system - especially given the user rights of this particular user. As part of our testing we confirmed that all the amendments made by the RAM consultant were only the amendments to council dwellings valuations and not to system configuration therefore minimising this risk.

Recommendation

The Authority should ensure that it has a formal process in place for removing individuals from all systems they have access to on the date they leave the organisation. Where temporary access is needed by other individuals or organisations, separate and identifiable usernames should be provided to them for audit purposes.

Management response

Accepted.

This will be addressed urgently by LGSS Finance and ICT Services.

Owner

NBC Chief Finance Officer.

Deadline

February 2019.

Medium priority

11. ITGC – RAM Update

Key financial systems should be kept updated. One of the issues that caused delays to the audit was a result of an outdated version of the Real Asset Management (RAM) system which holds fixed asset information. The outdated version resulted in a lack of support from third parties. A RAM consultant was required to come in and remove data from RAM to update it to the correct balances. This was a large piece of work and owuld not have been required if RAM was on a more recent version. We suggest that the RAM system is looked into for the 17/18 accounts preparation onwards and the system updated.

Recommendation

The Authority should ensure that all of its key systems, accounting and otherwise, are kept up-to-date with relevant patches and software releases as and when required. This will ensure that the latest version is serviceable, provides the most up-to-date functionality and mitigates against issues which may lead to a loss of data or the system being unable to operate as intended.

Management response

Accepted.

NBC Chief Finance Officer will seek regular, quarterly, assurance from LGSS as part of the contract monitoring / performance reviews, the status of all LGSS supported ICT systems and their currency/updates.

Owner

LGSS ICT and Finance.

Deadline

Ongoing – commencing February 2019.

The following is a recommendation which we have raised in our *External Audit 2016/17 Interim Report*. We have included this here for completeness.

High priority

10. Team resilience and use of interim staff

The Authority has a number of interim staff in key positions within its Estates and Integrated Closedown teams. The departure of the Interim Asset manager and a number of interim valuers has resulted in delays to the valuation process for Council dwellings. There are now no qualified valuers remaining in the Estates team. The knock-on effect has caused us to modify our audit approach to accommodate the Authority's new schedule.

A member of the Integrated Closedown team has also departed in year however the Authority has since recruited an interim replacement for the member of the Integrated Closedown team. Nonetheless, this is a real risk that corporate knowledge is lost upon the departure of interim staff and these potentially impact the valuation and accounts production process.

The use of interim staff has been a focus of the Audit Committee.

Update

We acknowledge that the Authority has been providing regular updates to the Audit Committee and plans are in place to address the use of interim staff. We also recognise that these are long-term plans but the use of interim staff has impacted the audit process for the year 2016/17.

Due to the departure of valuers within the Estates team, the Authority has had to engage two external valuers to carry out valuations on the Authority's property portfolio, and we noted that there had been no strategic oversight over this process. We also note that previously-agreed approaches to fixed assets had not been carried forward into this year's audit due to the departure of a key member of staff. Working papers provided for fixed assets were rolled-forward from the prior year, which we previously reported were inadequate and lacked audit trails. We have reported issues in relation to this, see recommendations 2, 3 and 5. These issues have caused significant delays to the audit process.

As such, our recommendation from the interim report remains open.

Recommendation

The Authority should appoint permanent members of staff as a matter of urgency.

Management's updated response – January 2019

Accepted.

The LGSS Integrated Finance Group Accountant role has been recruited to permanently and the individual took up the post before Christmas. The LGSS Finance Group has also been reorganised so as to provide more directed and consistent support to this area.

The NBC CFO role has moved from LGSS to NBC proper. The HoS for Economy, Assets and Culture has been appointed on a Fixed Term basis until April 2020 to gain consistency. Suitable senior staff in that group have also been appointed.

Owner

Chief Executive

Deadline

Ongoing

Follow-up of prior year recommendations

In the previous year, we raised ten recommendations which we reported in our *External Audit Report 2015/16 (ISA 260)*. The Authority has not implemented all of the recommendations. We re-iterate the importance of the outstanding recommendations and recommend that these are implemented by the Authority.

One recommendation was first raised in 2014/15.

Two recommendations were deemed to have been implemented in our *External Audit 2016/17 Interim Report*, dated April 2017. This appendix summarises outstanding recommendations in that report.

We have used the same rating system as explained in Appendix 1.

Each recommendation is assessed during our 2016/17 work, and we have obtained the recommendation's status to date. We have also obtained Management's assessment of each outstanding recommendation.

Below is a summary of the prior year's recommendations (all recommendations raised in 2015/16).

2015/16 recommendations status summary

Priority	Number raised	Number implemented	Number outstanding/ superseded
High	2	-	**2**
Medium	5	3	**2**
Low	3	2	**1**
Total	**10**	**5**	**5**

High priority

1. Controls and processes for issuing loans

There is no systematic formalised system of recording or documenting the due diligence process or results arising from the loan approval process. This includes the assessment of business cases, evidence to support key decisions made, any challenge put forward by the Authority to the loan applicant, and the Authority's internal review and approval process. The Authority had significant difficulty in obtaining the evidence required to substantiate this decision-making process. Our assessment of two loans is still ongoing due to the delayed provision of key documentation first requested in February 2016.

There is evidence that the due diligence process is not sufficiently formal nor are there a consistent set of requirements. This includes the lack of assessments regarding historic trading performance, cash flow, working capital requirements, sensitivity analysis etc. The Authority's Treasury Management Strategy, states that *"The Council will use specialist advisors to complete financial checks to ascertain the creditworthiness of the third party."* We note that the use of specialist advisors by the Authority varies across loans in relation to the scope and detail of work requested and undertaken.

The accountability and decision-making process is not sufficiently robust. We note that whilst Cabinet delegates authority to the Chief Executive or other appropriate officers, this has been done prior to finalising the due diligence process.

1. Controls and processes for issuing loans *(continued)*

Update

The Authority has developed a loans checklist to address our recommendation that there should be a systematic, robust, and objective process of assessing and documenting the due diligence procedures with regards to loans. This checklist has been shared with KPMG.

However, given the fact that due the Authority has taken a decision not to issue any loans this year or for the foreseeable future, the checklist has not been used in practice. Therefore we have not been able to critically assess the effectiveness of this new loans checklist. As such, we have also not been able to assess whether this checklist addresses and mitigates the previously-identified risks when used in a real-world situation. For the same reason were also not able to assess whether appropriate decision-making and approvals took place in line with the recommendation raised.

As a result, we deem this recommendation to be partially implemented until we can confirm effectiveness of this new process in practice.

Partially implemented

Recommendation

The Authority should put in place a systematic, robust, and objective process of assessing and documenting the due diligence procedures carried out on loan applicants. This process should be transparent and the due diligence process undertaken by qualified individuals. Any decision will need to be fully documented, including the reasoning and consideration of risks. The process should include a review by a senior officer and this should be evidenced.

Decision papers to Cabinet need to be robust and objective in order to allow informed and balanced decision-making. Decisions need to be made by Cabinet upon completion of required due diligence process. Officers will need to seek subsequent approval if terms of the loan are substantially revised.

Management's Original Response

Management accept that improvements should be made to the process for approving loans.

It should be noted that NBC have implemented a number of improvements in more recent loans issued, in particular the £46 million loan to the University of Northampton which was subject to an intense and closely scrutinised process by the Council and external bodies, including HM Treasury.

NBC will conduct a thorough governance review, in relation to project governance, risk management and due diligence. This review will consider Cabinet decision-making and clearance processes.

The review will draw on external and internal experts and will work closely with KPMG and PWC as appropriate, and the output from the review will include documented and robust processes and checklists for the approval of loans and decision-making processes. NBC using advice from KPMG have already introduced a summary checklist to ensure that all aspects of third party loans are appropriately considered and recorded prior to approval

Completion target dates: 31 March 2017

Responsible officer: Chief Finance Officer, and Monitoring Officer

Management's updated response – January 2019

The Governance review has been undertaken, new processes and due diligence processes exist.

High priority

2. Retrospective raising of Purchase Orders

Testing identified that purchase orders (POs) need to be raised prior to the Authority committing itself to purchasing goods/services. All purchases need to be authorised, and this authorisation is only carried out at purchasing order stage for those items that require a purchase order.

We noted that £7.7 million worth of expenditure in year was not appropriately authorised prior to placing an order with a supplier. In these cases purchase orders were raised retrospectively which potentially opens the Authority to potential fraud or impropriety and is contrary to the Authority's policy.

Update

This was initially raised as part of the 2014/15 audit.

From our testing in 2016/17, there was a total of 2,419 POs raised after the invoice which had a net total of £15.6 million. Communication from LGSS suggests that some of these were duplicates within the same PO and some related to homelessness whereby no PO is raised in such emergency circumstances. The Authority has stated that retrospective purchase orders were have decreased (by number) from 20% in 2015/16 to 18% in 2016/17. We are still waiting for supporting evidence to evidence the Authority’s calculations and the monetary value of this 18%.

Nonetheless, the use of retrospective orders is not in line with the Authority’s policies. There is a risk that these 18% were not initially authorised, and the Authority made a financial commitment without undergoing the required approval process.

Partially implemented

Recommendation

The Authority should ensure that purchase orders should be raised for the purchasing of goods and services through the purchase order process (where appropriate), prior to the Authority committing itself to the purchase.

Reports should be run on a regular basis to identify all non compliance and take appropriate follow up action.

Management’s updated response – January 2019

This has continued to be an issue, in some instances it is the nature of the task, e.g. temporary accommodation, the policies and process continues to be reviewed, along with whether Purchase Orders (and the associated process) is the correct way to access certain services, as opposed to a framework and procurement card approach.

Medium priority

3. Revaluation of Council Dwellings

The Authority revalues approximately 20% of its council dwellings annually, using the beacon methodology. This is where similar council dwellings are grouped with one dwelling chosen to represent each group (the 'beacon'). The remaining 80% of beacons are uplifted using the average movement of the 20%. The *Stock Valuation for Resource Accounting* guidance suggests that where a rolling valuation is performed, the Authority should undertake a desk top review of the remainder, informed by the results of the revaluation, market research and comparing prices of similar transactions in year.

The Authority was unable to provide evidence of the year-end valuation methodology until after our on-site visit had been completed (22 days working days after request), causing significant delays to the completion of our work.

Handwritten notes were then provided to us, but these did not provide a clear and concise audit trail detailing the methodology used, the assumptions made, nor how calculations had been applied. There was no evidence this working paper had been reviewed. Furthermore, whilst the Authority did take into account similar transactions in the year, it did not challenge the methodology used nor undertake any additional review such as looking at wider trends, indices and other information to inform the year end movement. The Authority did not perform its own assessment of the final valuation including challenge and confirmation of this in order to understand key movements for properties.

For both the initial and year end valuations, the valuer did not provide all the documents required by Code guidance including a separate overarching valuation report covering matters such as the process used to arrive at the estimate of the remaining useful life of individual properties, the valuer's proposed strategy,, arrangements for implementing the rolling programme; and proposals for carrying out additional and ad hoc valuations.

Update

This recommendation will be closed off and we have raised one new recommendation in 2016/17 to allow the Authority to respond to both Council Dwellings and PPE.

In April 2017, we were assured that there was a full documented audit trail. However when the work was reviewed, this was difficult to evidence and caused delays to the audit.

See recommendation 2 in Appendix 1.

Recommendation superseded

Recommendation

The information requested, and provided by the valuer, should meet all the criteria within the Code and provide a clear and concise audit trail relating to the methodology and assumptions used in the valuation process. All evidence should be maintained and made available prior to the start of the audit.

The Authority should ensure that it fully fulfils its responsibility to review, challenge and understand the information provided by the valuers as required by guidance.

Management's Original Response

Accepted. There was a change in key staff within the Asset Management team prior to the start of the audit. This combined with changes to finance staff meant that the process was not as smooth as in previous years.

3. Revaluation of Council Dwellings *(continued)*

Management recognise there is a need for a better documented internal review process within Asset Management, and between Asset Management and Finance. Officers will be working jointly to thoroughly document processes for future years.

Completion target dates: 31 December 2016

Responsible officer: Head of Asset Management, and Strategic Finance Manager

Medium priority

4. Reconciliations

During the course of our audit we reviewed a number of reconciliations performed by the Authority between key systems. These are important controls which provide assurance that due process is being followed and that values reflected in the financial statements are calculated on an appropriate basis. We noted a number of issues including:

- Our testing of the March 2016 payroll reconciliation showed a total of 99 unreconciled items with a net value of £46,000 (gross £95,000). We also noted historical brought-forward balances which have yet to be identified by payroll.
- The Authority reconciles weekly Valuation Office (VO) reports to Academy Capita. The Authority does not reconcile the number of hereditaments (properties which are subject to business rates) to the NNDR system. There remains a small unreconciled difference in property numbers each week.
- The Authority reconciles the annual housing benefits expenditure to Agresso at the end of the year. We identified that the Authority had used the 2014/15 figure instead of 2015/16 figure for the reconciliation, resulting in an unreconciled difference of £15,300, instead of the original £997. This was not identified despite having been reviewed and signed off as "quality assured" by Officers.

Update

- Payroll reconciliations: As part of our interim audit we tested the December 2016 payroll reconciliation. 27 reconciling items were present on the December 2016 reconciliation that were present on the July 2016 reconciliation. We recommend these are cleared as quickly as possible.
- NDR reconciliations: A reconciling item has been identified since June 2016, which has not been resolved at year end. Therefore all of the monthly reconciliations show a reconciling item, so they do not reconcile. Although the reconciling item is in the process of being investigated, it has not been cleared by year end.
- Housing benefits reconciliation: This reconciliation was tested as part of the year end audit. No issues were noted with the housing benefits reconciliation.

Two new recommendations have been raised in 2016/17 to separately identify issues with the payroll and NDR reconciliations.

See recommendations 7 (NDR reconciliations) and 8 (payroll reconciliations) in Appendix 1.

Recommendation superseded

Recommendation

The Authority needs to ensure that quality checks are undertaken on all key controls. This should be embedded within the reconciliation process. The Authority should ensure all the issues above are dealt with and that full reconciliations are carried out across all appropriate systems and balances. All unreconciled balances should be identified and cleared, or written-off in a timely manner

Management's Original Response

Accepted. Payroll reconciliation – Management accept there is a need to strengthen the reconciliation process. Reconciliation items must be identified and cleared within a timely period.

NDR property reconciliations - The Authority does reconcile the properties between the NDR and VO reports, and there are currently two cases where properties don't reconcile but officers are aware of the reasons why the systems don't reconcile and will be correcting them. The reconciliation amendment will not impact on the customers' liability or debit raised.

4. Reconciliations *(continued)*

Housing Benefit Agresso reconciliation - Management recognise that the reconciliation process needs to be improved, and officers will be revising the process to exclude prior balances from the reconciliation data to ensure it is not included in error.

Completion target dates:

Payroll: 31 October 2016

NDR: 31 October 2016

Housing Benefit: 31 December 2016

Responsible officer: Payroll Manager

Revenues Manager

Strategic Finance Manager

Medium priority

5. Cut-off and accruals accounting

We performed cut-off procedures over the Authority's non-pay expenditure controls. The Authority needs to recognise expenditure incurred within the correct financial year. Our cut-off procedures are designed to test the effectiveness of the Authority's process for identifying and allocating expenditure to the correct financial year.

We tested 10 transactions around the year-end closedown date and identified that one invoice which should have been accrued had not been. The value of this invoice was for £2,240, which is above the Authority's *de minimis* threshold and therefore should have been accounted for within 2015/16.

Whilst further investigation deemed the issue to be immaterial to the audit, and therefore no adjustments are proposed, this is a key control operated by the Authority and should be operated consistently during the year.

Update

No issues were found with our cut-off and accruals testing in the 2016/17 financial statements audit.

Fully implemented

Recommendation

The Authority should ensure it strengthens its year end cut-off procedures and that controls are sufficiently-robust to ensure correct procedure is followed. The Authority may wish to consider the impact on raising its de minimis level to reduce the manual input required in this process. A review of cut-off is particularly important given the move to a shorter timetable for the accounts process from 2017/18, and the reduced time to produce the financial statements.

Management's Original Response

Accepted. Management accept this advice and they intend to review the de minimis level for accruals from £1,000 to £5,000 in order to make the process more efficient in the future to enable the reduced statutory deadline for the closure of accounts to be achieved. This will allow more time for increased controls over the manual accruals process which arguably present a greater risk.

Completion target dates:

31 December 2016

Responsible officer: Head of Asset Management, and Strategic Finance Manager

Medium priority

6. General IT controls – leavers

We tested the Authority's general IT control environment this year. We carried out specific testing of key applications which are relied upon by the audit, including Agresso. For two applications, we found that staff who have left the organisation are still active on these applications:

- IBS Housing: 14 former staff had active accounts; and
- ICON: 12 former staff were on user list, of which five were disabled and seven still active users.

Update

No issues were found in our leavers testing as part of the 2016/17 audit.

Fully implemented

Recommendation

Timely leaver forms need to be completed and cascaded to the relevant departments, including to IT.

User access to applications needs to be reviewed on a periodic basis. In addition, the departing employee's access rights should be revoked as part of the standard leaving procedures. This process should be co-ordinated between HR and IT.

Management's Original Response

Accepted.

Management notes this recommendation and has taken the following action:

IBS Housing System. The recommendation for timely leaver forms needing to be completed and cascaded to the relevant departments has now been implemented.

ICON System. The staff responsible for maintaining user access to the ICON system have incorporated a review and disablement of users who have left into their routine monthly processes linking with the HR and Payroll teams.

Completion target dates:

Immediate

Responsible officer:

IBS Housing System: LGSS Business Systems Manager

ICON System: LGSS Exchequer team leader

Low priority

7. Payroll data quality

As part of our audit approach, we undertook data analytics over the Authority's payroll transactions for the year. We did not find any material issues; nonetheless, we noted some minor data quality issues, such as incorrect addresses and duplicate National Insurance numbers. We have provided the full results to the Authority separate from this report.

We noted salary payments made to employees after their effective end date. All of these have been investigated by the Authority and confirmed as appropriate.

Update

During interim, the original results of our work over payroll data and analytics highlighted a number of data quality issues. When communicated with the Integrated Closedown team, it highlighted that the data originally used was incorrect. A new data set has been provided and our Data & Analytics routines were re-performed. This has resulted in a delay to the work produced.

This occurred again as part of the final visit where incorrect data was provided requiring our Data & Analytics routines to be re-performed.

Findings from our Data & Analytics routines indicated that there are still a number of data issues such as incorrect addresses, duplicate NI numbers and employees with in correct bank details. Nonetheless, our Data & Analytics routines have not identified financial impacts on the Authority's financial statements.

Partially implemented

Recommendation

The Authority should investigate instances of data quality issues. In addition, the Authority should investigate all incidences of salary payments to staff after the end dates.

Management's Original Response

Management have reviewed the findings and whilst there are no significant issues, processes have already been updated during 2015/16 to address issues around national insurance numbers. A further review of data held around historic / incomplete postcodes will be undertaken

Completion target dates: 31 December 2016

Responsible officer: Payroll Manager

Due to the data requirements changing for this year's audit with the request for a single data report in this area, the Systems team had to pull together the data from different sources and undertake lookup processes between the different sources. There was an issue with this lookup with new cost centres not being picked up which led to the exceptions highlighted by KPMG. This has been corrected in a revised set of data and reports, which is expected to remove the vast majority of the exceptions initially identified. We await the outcome of the revised analysis.

Management's updated response – January 2019
None provided.

Low priority

8. NDR provision review

The Authority collects Non-Domestic Rates (NDR) from businesses in the Borough. NDR owed to the Authority is based on rateable values, as set by the Valuation Office Agency (VOA). Ratepayers are able to appeal these values if they do not agree with the valuation. If successful, the Authority is liable to repay its share of the difference.

This was first introduced in 2013-14 due to a move to localise business rates. The Authority has set an NDR provision level of 5% based on an estimate of successful appeals. This estimate is based on information from the VOA (across a range of percentages) and the DCLG's guidance on the national average success rate.

During the course of the audit we asked the Authority to provide evidence regarding its review and analysis of local historical data collected since April 2013 in order to inform its view of the appropriateness of its provision in this area, however none was provided at that time. In raising this issue with Management, we have now been provided with information pertaining to the Authority's approach. The Authority having analysed the local data has deemed that the current approach is prudent and therefore has not adopted the calculated figures. This has not resulted in a material impact on the financial statements.

Update

The Authority has worked hard to review the calculation of the appeals provision. There has been a change in how the provision is calculated, which is now based on more granular data. This change in methodology has resulted in an NDR provision increase of £800,000.

Fully implemented

Recommendation

The Authority should continue to use its own historical data to inform and refine its estimate of its share of liability arising from successful appeals. Notwithstanding whether the Authority decides it should change its provision based on this information, sufficient and appropriate audit evidence should be maintained and provided to evidence the decision process undertaken, as well as management review and sign-off of the final position. The Authority should provide appropriate and sufficient narrative explanations with regards to why the Authority believes that the approach taken is the most appropriate or prudent, especially when there are valuation differences between methodologies.

Management's Original Response

Accepted. The Council recognises the complexity of the business rates retention system and the importance of understanding its appeals position. The Council will continue to review the impact of successful appeals on a monthly basis to assess its impact on the financial position. The outcome of this analysis, along with other sources of intelligence, will inform the level of appeals provision for 2016/17.

Completion target dates: 31 March 2017

Responsible officer: Chief Finance Officer

Management's Update April 2017

Noted.

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

A significant number of minor amendments focused on presentational improvements have also been made to the 2016/17 draft financial statements. The Closedown Team is committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Adjusted audit differences

Table 1: Adjusted audit differences (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1	Dr Expenses 514	Dr Capital Adjustment account 514 Cr General Fund 514	Cr Council Dwellings 514		Dr Capital Adjustment account 514 Cr General Fund 514	Q4 disposals not included in July 17 draft accounts
2	Cr Expenses 725	Dr Capital Adjustment Account 725 Cr General Fund 725	Dr Assets Under Construction 5,312 Dr Housing L&B 701 Cr Council Dwellings 701 Cr OLB 9,327 Dr Investment Properties 4,741		Dr Capital Adjustment Account 725 Cr General Fund 725	Reclassification of assets within Property, Plant and Equipment
3	Cr Expenses 73,438	Cr Revaluation reserve 15,249	Dr Council Dwellings 88,687		Cr Revaluation reserve 15,249	Incorrect EUV-SH used for Council Dwellings

Appendix 3

Audit differences

Adjusted audit differences (cntd.)

Table 1: Adjusted audit differences (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
4	Dr Expenses 974	Dr Capital Adjustment account 974 Cr General Fund 974	Cr Housing L&B 172 Cr Council Dwellings 803		Dr Capital Adjustment account 974 Cr General Fund 974	Adjustment to Right to Buy disposals as a result of valuation changes
5	Dr Expenses 4,197	Cr Revaluation Reserve 735 Cr General Fund 2,042 Dr Capital Adjustment Account 2,006	Cr OLB 3,426		Cr Revaluation Reserve 735 Cr General Fund 2,042 Dr Capital Adjustment Account 2,006	Additional valuations and recognition of buildings as a result of KPMG valuer review
6	Dr Expenses 1,812	Cr General Fund 1,812 Dr Capital Adjustment Account 1,812	Cr Investment properties 310 Cr OLB 1,502		Cr General Fund 1,812 Dr Capital Adjustment account 1,812	Purchase costs on Other Land and Buildings and Investment Properties
7	Cr Expenses 1,502	Cr Capital Adjustment Account 1,502 Dr General Fund 1,502	Dr OLB 1,502		Cr Capital Adjustment Account 1,502 Dr General Fund 1,502	Incorrect treatment of purchase costs

Audit differences

Adjusted audit differences (cntd.)

Table 1: Adjusted audit differences (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
8	Dr Expenses 273	Dr Revaluation Reserve 747 Cr General Fund 273 Dr Capital Adjustment Account 273	Cr OLB 747 Cr Investment Properties 273		Dr Revaluation Reserve 747 Cr General Fund 273 Dr Capital Adjustment Account 273	Duplication of revaluations in RAM
	Cr 67,064	**Cr 15,273**	**Dr 83,168**	**–**	**–**	**Total impact of adjustments**

Appendix 3

Audit differences

Unadjusted audit differences

The following table sets out the uncorrected audit differences identified by our audit of Northampton Borough Council's financial statements for the year ended 31 March 2017. These differences are individually below our materiality level of £1.5 million. Cumulatively, the impact of these uncorrected audit differences is not material. We have also considered the cumulative impact of these unadjusted audit differences on the Authority's financial statements in forming our audit opinion.

Table 2: Unadjusted audit differences (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1		Revaluation reserve Cr 543k	Council Dwellings Dr 578k Other Land and Buildings Dr 35		Revaluation reserve Cr 543k	Guildhall Road and the Ecton Lane Travellers Site were revalued in 2016/17 however the revaluations have not been transacted into the accounts and are therefore understated in the 16/17 financial statements. In addition, the Travellors site should also be included in Council Dwellings and not OLB as travellers sites are registtered for council tax. This adjustment is a presentational error between Council Dwellings and OLB.
		Cr 543	**Dr 543**		**Cr 543**	**Total impact of uncorrected audit differences**

Appendix 4

Timeline of key events for PPE & investment properties

		INVESTMENT PROPERTIES	COUNCIL DWELLINGS	OTHER LAND & BUILDINGS
2016 **Sept**	**26 September 2016** Formal instructions were sent to the Authority's internal valuers. The instructions originally encompassed PPE (including Council Dwellings) and investment properties.			
Oct			**3 October 2016** Finance challenged the valuation of Council Dwellings by its internal valuers due to large variations from the March 2016 valuations. Movement was rechecked but confirmed as appropriate by the internal valuers.	**6 October 2016** Underwoods instructed via email to review part of the Authority's portfolio of other land and buildings. No formal written instructions were provided by the Authority. The Authority's internal valuers had no capacity to fully complete the valuation of land and buildings.
2017 **Jan**		**30 January 2017** Underwoods instructed via email to review investment properties. No formal written instructions were provided by the Authority.	**16 January 2017** Authority's interim valuers agreed with LGSS Finance that valuation work for Council Dwellings should be outsourced to Underwoods due to capacity issues within the Estates team.	**31 January 2017** Internal valuers' report issued for part of the Authority's portfolio of other land and buildings.
Feb			**1 February 2017** We were informed that the 1 April 2016 valuation exercise resulted higher-than-expected increase in valuation for Council Dwellings. This will form part of the Beacons review undertaken by Underwoods.	
Mar	**March 2017** Planned review of valuation report by KPMG valuation specialist. Interim on-site audit visit from 6 March 2017 to 24 March 2017.	*Note: we deferred engaging our valuation specialist until September 2017 as we had not received the Underwoods valuation report for investment properties.*	**1 Mar 2017** Council Dwellings valuations results received from Underwoods which indicated further work was necessary to ensure compliance with both Code and SVRA requirements.	*Note: we deferred engaging our valuation specialist until September 2017 as we had not received the Underwoods valuation report for other land and buildings.*
Apr			**20 April 2017** The Authority subsequently commissioned Bruton Knowles to carry out a valuation on Council Dwellings to comply with Code and SVRA requirements.	

Appendix 4

Timeline of key events for PPE & investment properties (cntd.)

		INVESTMENT PROPERTIES	COUNCIL DWELLINGS	OTHER LAND & BUILDINGS
May			**End of May 2017** Agreed deadline between the valuer and the Authority for the final valuation report.	
Jun			**23 June 2017** First version of the Council Dwellings valuation report passed on to KPMG for review.	
Jul	**July 2017** The final accounts audit visit took place on site from 10 July 2017 to 4 August 2017.	**17 July 2017** We received the first Underwoods valuation report for investment properties, totalling £7.7m. **24 July 2017** We received the second Underwoods valuation report for investment properties, totalling £8.3m.		
Aug				**1 August 2017** We received the internal valuers' report for other land and buildings. **4 August 2017** We received the Underwoods valuation report for other land and buildings.
Sept KPMG review of assets	**September to October 2017** Rescheduled review of valuation reports by KPMG valuation specialist. This resulted in a revised valuation report from Bruton Knowles for Council Dwellings, and commissioning GVA to re-do the valuations previously carried out by the internal valuers. Initial draft report received from KPMG valuation specialist on 19 September 2018. **29 September 2017** KPMG issued a letter to the former Chief Finance Officer, detailing issues found which will impact on our ability to provide an audit opinion by the statutory deadline.	**September 2017** Adjustments relating to purchase costs total £322,000. Further adjustment identified relating to the classification of Park Inn from other land and buildings to investment properties.	**22 September 2017** Second version of Bruton Knowles report provided to KPMG, in draft version. This included an amendment to the year-end social housing adjustment factor and a revision to the year-end indexation. *Note: this report omits the adjustment to the 1 April 2016 social housing adjustment factor; see Appendix 2.*	**September 2017** Adjustments relating to purchase costs identified. Supporting evidence for assets valued by internal valuers were not readily available; this resulted in further queries from the KPMG valuation specialist.

Timeline of key events for PPE & investment properties (cntd.)

			INVESTMENT PROPERTIES	COUNCIL DWELLINGS	OTHER LAND & BUILDINGS
KPMG review of assets	Oct	**October 2017** Valuation assessment paused due to uncovering issues including incorrect classification of assets, data anomalies, and the lack of evidence available to support valuations.	**4 October 2017** Incorrect classification of Sixfields land found, resulting in audit adjustment of £595,000.		
	Nov	**October to November 2017** Authority puts in place a "PPE taskforce" to provide an additional layer of review to audit queries.	**30 November 2017** Further samples provided to the Authority for review given issues found within the initial sample.		**30 November 2017** Further samples provided to the Authority for review given issues found within the initial sample.
	Dec	**December 2017** Second tranche of reviews by the KPMG valuation specialist, concentrating on resolving queries for other land and buildings and a further extension of our samples for investment properties.			**December 2017 to January 2018** GVA completed its review of other land and buildings. The final report was dated 19 January 2018.
	2018 Jan	**January 2018** Work undertaken in January 2018 on investment properties and other land and buildings including resolution of our valuation specialist's queries and obtaining supporting information (such as rental agreements).		**23 January 2018** Reconciliation between the second valuation report and the fixed asset register requested.	**23 January 2018** We received a schedule from the Authority which details multiple adjustments to other land and buildings as a result of the revised valuation.
KPMG review of assets	Mar	**March to April 2018** Addressing issues raised by KPMG valuation specialist. This includes reviewing lease terms, confirming yields, and other property-specific queries. We liaised with the KPMG valuation specialist to clear off outstanding valuation queries arising from our specialist's review of the valuations.			
	Apr			**20 April 2018** Reconciliation between second valuation report and the fixed asset register provided. Difference noted, due to the use of 4.08% uplift originally calculated by the internal valuers. We requested the internal valuer's original report, which we received 30 April 2018. We responded on 30 April 2018 that the internal valuers have used an incorrect social housing adjustment factor. Authority to investigate.	

Appendix 4

Timeline of key events for PPE & investment properties (cntd.)

KPMG review of assets

		INVESTMENT PROPERTIES	COUNCIL DWELLINGS	OTHER LAND & BUILDINGS
May	**May 2018** Further queries and clarification on specific valuation issues raised by KPMG valuation specialist.			
Jun			**June 2018** Communication with the Authority Finance staff that the Traveller's site should be reclassified as Council Dwellings and is incorrectly classified as Other Land and Building in financial statements. KPMG received third valuation report from Bruton Knowles, which contained the correct EUV-SH value of 42%.	**June 2018** An updated revaluation for Park Inn was provided by the Authority to the KPMG audit team for review.
Jul			**July 2018** 2 July - KPMG provided with fourth version of valuation report form Bruton Knowles: minor internal inconsistencies still to be updated. Final report received 9 July.	**12 July 2018** The revaluation of Old Gaol Block was provided by the Authoirty to KPMG for review.
Aug			**13 August 2018** KPMG were notified that the RAM consultant had started to remove incorrect valuations and update the Council Dwellings valuation with the correct EUV-SH. Five working days were estimated.	**2 August 2018** The Authority responds to queries sent 2 July regarding the Park in Valuation.
Sept			**4 September 2018** KPMG were notified that the RAM work was taking longer than anticipated and would be complete by 14 September.	
Oct	**October 2018** Once the RAM work was completed, a "final set of statements were produced. KPMG had an additional set of queries to confirm treatment of Council Dwellings and OLB were transacted and presented appropriately.	**October 2018** Final figures for Investment Properties agreed. All queries resolved.	**2 October 2018** KPMG were notified that the RAM work was now complete and the updated figures were being included in the financial statements.	
2019 Jan	**January 2019** Final set of Financial Statements for 2016/17 ready for presentation to Audit Committee.			

Appendix 5

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.

Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.

Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2016/17, presented to you in March 2017.

Materiality was set at £1.5 million for the Authority's standalone accounts and group accounts, which equates to 0.6% of the Group's gross expenditure. This is a reduction in the level of materiality compared to the prior year to reflect the increased risk to the audit (*2015/16:* £2.7 million, or 1% of the Group's gross expenditure).

We design our procedures to detect errors in specific accounts at a lower level of precision. This is £1.1 million.

Reporting to the Audit Committee

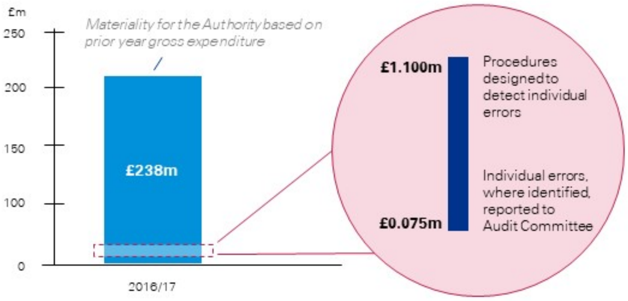
Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any misstatements of lesser amounts to the extent that these are identified by our audit work.

Under *ISA 260*, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. *ISA 260* defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £75,000 for the Authority.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit Committee to assist it in fulfilling its governance responsibilities.



We report all individual unadjusted differences greater than £75,000 to the Audit Committee.

We also have regard to other errors below this amount if evidence of systematic error or if material by nature.

Appendix 6

Declaration of independence and objectivity

Auditors appointed by Public Sector Audit Appointments Ltd must comply with the Code of Audit Practice (the 'Code') which states that:

> *"The auditor should carry out their work with integrity, objectivity and independence, and in accordance with the ethical framework applicable to auditors, including the ethical standards for auditors set by the Financial Reporting Council, and any additional requirements set out by the auditor's recognised supervisory body, or any other body charged with oversight of the auditor's independence. The auditor should be, and should be seen to be, impartial and independent. Accordingly, the auditor should not carry out any other work for an audited body if that work would impair their independence in carrying out any of their statutory duties, or might reasonably be perceived as doing so."*

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Public Sector Audit Appointments Ltd Terms of Appointment ('Public Sector Audit Appointments Ltd Guidance') and the requirements of APB Ethical Standard 1 Integrity, Objectivity and Independence ('Ethical Standards').

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Public Sector Audit Appointments Ltd guidance requires appointed auditors to follow the provisions of *ISA (UK&I) 260 'Communication of Audit Matters with Those Charged with Governance'* that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor's objectivity and independence.
- The related safeguards that are in place.
- The total amount of fees that the auditor and the auditor's network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed. We do this in our Annual Audit Letter.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor's professional judgement, the auditor is independent and the auditor's objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor's objectivity and independence may be compromised and explaining the actions which necessarily follow from his. These matters should be discussed with the Audit Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Engagement Lead and the audit team.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP Audit Partners and staff annually confirm their compliance with our Ethics and Independence Manual including in particular that they have no prohibited shareholdings.

Our Ethics and Independence Manual is fully consistent with the requirements of the Ethical Standards issued by the UK Auditing Practices Board. As a result we have underlying safeguards in place to maintain independence through: Instilling professional values, Communications, Internal accountability, Risk management and Independent reviews.

We would be happy to discuss any of these aspects of our procedures in more detail.

Auditor declaration

In relation to the audit of the financial statements of Northampton Borough Council for the financial year ending 31 March 2017, we confirm that there were no relationships between KPMG LLP and Northampton Borough Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

Non-audit work and independence

We have not undertaken any non-audit work for the financial year ending 31 March 2017.

Audit fees

Audit fees

As communicated to you in our *External Audit Plan 2016/17*, our scale fee for the audit is £80,775 plus VAT *(£80,775 in 2015/16)*, thereby preserving the 25 per cent reductions that were applied in the previous year. Our fee is based on a number of assumptions, including that Officers provide us with complete and materially-accurate financial statements, accompanied by good-quality supporting working papers within agreed timeframes.

During the audit, we experienced quality issues with working papers and various delays. These issues have been communicated to the Audit Committee within this report, and we are currently in discussions with the Section 151 Officer about the additional costs which we have incurred. We have discussed additional fees of approximately £200,000 with the Section 151 Officer. These are subject to PSAA approval. We have also undertaken additional work in response to Code changes and changes made by the Pension fund in response to the triennial pensions revaluation. We have discussed additional fees of £4,813 with the Section 151 Officer in relation to these two areas. See table below for further detail.

Our work on the certification of Housing Benefits (BEN01) was completed in November 2017. The planned scale fee for this is £18,972 plus VAT per PSAA notification. All PSAA scale fees are available on the PSAA's website.

PSAA fee table

Component of audit	2016/17 *(planned fee)* £	2015/16 *(actual fee)* £
Accounts opinion and use of resources work		
PSAA scale fee set in 2014/15	80,775	80,775
Code changes for 2016/17 and the triennial pensions revaluation (note 1)	4,813	–
Additional work to conclude our opinions (note 2)	200,000	17,250
Subtotal	**285,588**	**98,025**
Other		
Housing benefits (BEN01) certification work (PSAA scale fee)	18,972	10,579
Elector work – NTFC (note 3)	TBC	52,413
Elector work – Council Tax (note 4)	4,700	-
Total fee for the Authority set by the PSAA	**TBC**	**161,017**

All fees are quoted exclusive of VAT.

Note 1: Code changes and the triennial pensions revaluation

The Code introduced changes in the way the Authority is required to present its financial statements for the year 2016/17. This involved a restatement of the prior year's Comprehensive Income and Expenditure Statement (CIES) and the introduction of the Expenditure and Funding analysis (EFA), together with the corresponding notes to the EFA. We undertook additional work to gain understand and assurance over the restatement process and agreeing the new disclosures to the Authority's trial balance.

We also undertook additional work in relation to process changes introduced by the Pension Fund in response to the triennial pensions revaluation.

Note 2: Additional work to conclude our opinions

For 2015/16, an additional £17,250 was agreed by the Section 151 Officer and the PSAA to meet additional costs incurred by the audit team. These were predominantly caused by additional work and issues over the Authority's loans and fixed assets. We have reported these issues in our External Audit Report 2015/16 (ISA 260) and the 2015/16 Annual Audit Letter, which were previously presented to the Audit Committee.

For 2016/17, we have experienced significant delays and undertook additional work in the course of performing the audit. These predominantly relate to the Authority's fixed assets, including Council Dwellings. We have provided details of these issues in our initial reporting in September 2017, and subsequent updates to the Audit Committee. Further detail can be found throughout this report. The fee also includes additional work carried out by our valuation specialist over the Authority's fixed assets, additional work carried out by our Data & Analytics team due to incorrect data submitted for review, and additional work by our IT specialist team in response to the change in the Authority's Non Domestic Rates System, as well as the updated to the Real Asset Management System. The estimate of our additional fee to date is of £200,000 and this has been discussed throughout the audit with the Section 151 Officer who has been provided with detailed breakdowns at each stage. The final agreed fee will also be subject to PSAA determination.

Note 3: Elector work – NTFC objection

In 2015/16, we received an objection from a local elector in relation to the loan provided to the Northampton Town Football Club (NTFC). We reported in our *2015/16 Annual Audit Letter* that our work was temporarily suspended due to the on-going police investigation. The £52,413 disclosed in the 2015/16 column relate to costs incurred up to the temporary suspension of our work. We have since received permission from the police to recommence our work, and anticipate incurring further costs. We will discuss further costs with the Section 151 Officer and the PSAA.

Note 4: Elector work – Council Tax

In 2016/17, we received an objection from a local elector in relation to the setting of the Authority's Council Tax. We have accepted this objection and have issued our findings to the elector and the Authority. The additional fee of £4,700 was agreed with the Section 151 Officer and the PSAA.

Appendix 8

External Audit Letter - September 2017

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Private & confidential
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Section 151 Officer
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Our ref	DH/AC/NBC
Contact	Daniel Hayward 0121 232 3280

29 September 2017

Dear Glenn,

Northampton Borough Council – 2016/17 External Audit progress

Following the Audit Committee on Wednesday 27 September 2017 I am writing to you to provide an update regarding the status of our audit.

At the Audit Committee I had highlighted the potential risk that the audit may not be completed and the audit opinion issued before 30 September. Unfortunately as I have discussed with you this risk looks likely to be realised, and I know you share my disappointment in this situation. My team and I, as well as your team, have worked tirelessly to try avoid this situation, however, and again as discussed I am of the view that we have not as yet performed sufficient testing nor obtained sufficient evidence to enable me to issue an opinion.

As you are aware and as noted at the Audit Committee, and as per previous discussions with yourself, other Officers and Members at the time, our work to that point had identified a significant number of issues relating to the Authority's fixed assets, including but not limited to the valuation of social housing, other land and buildings, and investment properties, as well as the methodology adopted towards componentisation.

Whilst significant work has been undertaken by both my audit team and your Closedown team in order to respond to and address these issues, the result of our findings so far has provided me with insufficient assurance that your financial statements present a true and fair view in this respect and many of these issues remain unresolved.

Due to the number of areas of concern and errors found during KPMG's valuer's review of a sample of assets, my consideration in consultation with KPMG colleagues is that resolution of these specific issues currently would not provide sufficient audit assurance that the remaining population of assets, not sampled, are appropriately valued. Therefore there remains a risk of possible material misstatement.

Given the issues identified, and unanswered questions remaining around the reporting from the fixed asset system, this also brings into question the accuracy of those assets which have not been revalued in the year, transactions processed during the period and the accuracy of overall reporting and disclosures in this respect.

As you will no doubt appreciate the responsibility for ensuring that a materially correct set of accounts is presented for audit lies first and foremost with you as the section 151 officer. At this stage we think that there is still an uncertainty surrounding the robustness of the valuation that would enable you to be able to discharge your statutory responsibilities.

Appendix 8

External Audit Letter - September 2017

KPMG

KPMG LLP
Northampton Borough Council – 2016/7 External Audit progress
29 September 2017

It may be very likely that there is no change in the values in the accounts, I certainly hope that is the case. However, we will only be able to judge this when we have completed our testing and evaluated the evidence.

We are hoping to complete the audit as quickly as possible and I am aware that my team is in discussion with your team on what testing we still need to complete and what evidence that needs to be collected. Whilst we need to do this as quickly as possible I also am conscious that we need to avoid the situation of information being given to us in haste that raises further questions that often take longer to clear. We will be working with your team to try and avoid this situation.

If you have any questions please do not hesitate to contact me.

Yours sincerely

Andrew Cardoza
Director, KPMG LLP

cc: Northampton Borough Council Audit Committee