

Agenda Item
No.
<b>2</b>

# Hertfordshire County Council

Audit Results Report - ISA (UK and Ireland) 260  
for the year ended 31 March 2016

6 September 2016

Ernst & Young LLP



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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued “Statement of responsibilities of auditors and audited bodies 2015-16”. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psaa.co.uk](http://www.psaa.co.uk))

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

The ‘Terms of Appointment from 1 April 2015’ issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities. This report is intended solely for the use of the Members of the audited body. We, as appointed auditor, take no responsibility to any third party.

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

# 1. Executive summary

The National Audit Office's Code of Audit Practice (the Code) requires us to report to those charged with governance – the Audit Committee – on the work we have carried out to discharge our statutory audit responsibilities together with any governance issues identified. This report summarises the findings from the 2015/16 audit. It includes messages arising from our audit of the financial statements and the results of the work we have undertaken to assess the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources.

Below are the results and conclusions on the significant areas of the audit process.

Status of the audit	<p>We are completing our audit of the financial statements of Hertfordshire County Council for the year ended 2015/16. Subject to satisfactory completion of the outstanding items included in Appendix A we will issue an audit opinion in the form which appears in Appendix D.</p> <p>We have performed the procedures outlined in our audit plan and anticipate issuing an unqualified opinion on the Council's financial statements.</p> <p>We expect to conclude that the Council has put in place proper arrangements to secure value for money in its use of resources.</p> <p>We have not yet completed the procedures required by the National Audit Office (NAO) regarding the Whole of Government Accounts (WGA) submission. We will provide an update on the WGA at the Audit Committee on 23 September.</p>
Audit differences	<p>There are no unadjusted audit differences.</p> <p>Our audit identified some audit differences as well as some required corrections to disclosures which we have highlighted to management and which have been amended in the revised accounts. We do not consider these to be sufficiently significant to include in this report.</p>
Scope and materiality	<p>In our audit plan presented at the 23 March 2016 Audit Committee meeting, we communicated that our audit procedures would be performed using a materiality of £17.6 million. We have reassessed this based on the actual results for the financial year and have decreased this amount to £17.1 million. Our materiality is based on 1% of gross operating expenditure reported in the draft accounts of £1.6 billion adjusted to include other operating expenditure and financing and investment expenditure included in notes 9 and 10 in the accounts.</p> <p>The threshold for reporting audit differences which impact the financial statements has also decreased from £880,000 to £856,000.</p> <p>We also set separate materiality levels and reporting thresholds for the group accounts which consolidate the Council's accounts with those of Hertfordshire Catering Ltd and Herts for Learning Ltd, and the fire-fighters' pension fund based on the draft financial statements as follows:</p> <ul style="list-style-type: none"> <li>• Group accounts: We determined materiality to be £17.2 million, which we set on the same basis as for the single entity accounts based on the gross cost of services expenditure reported in the group accounts of £1.6 billion. We set a reporting threshold of £858,000.</li> <li>• Fire-fighters' pension fund: We set materiality at £0.135 million based on 1% of benefits payable of £13.5 million. We set a reporting threshold of £6,800.</li> </ul> <p>We also identified the following areas where misstatement at a level lower than our overall materiality level might influence the reader. For</p>

these areas we developed an audit strategy specific to these areas, the areas identified and audit strategy applied include:

- Officers' remuneration disclosures including exit packages and termination benefits: We agreed the numbers of employees disclosed as earning over £50,000 to payroll records, reviewed the disclosure and tested a sample of exit packages to approvals and calculations of the amounts payable.
- Members' allowances: We agreed the amounts disclosed in the note to payroll records, reviewed the disclosure note and confirmed that the disclosure was complete.
- Related party transactions: We assessed the related parties disclosed for completeness and accuracy through use of audit team knowledge, review of the register of interests and declarations and obtained supporting information for the entries disclosed in the note.

We carried out our work in accordance with our audit plan. This included carrying out controls testing of accounts receivable, accounts payable, cash processing and payroll, placing reliance on the work of Internal Audit. We also carried out early substantive testing of social care income and expenditure, Hertfordshire Business Services income and expenditure and waste management expenditure.

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Significant audit risks

We identified the following audit risks during the planning phase of our audit, and reported these to you in our audit plan:

- Property asset valuation.
- Better Care Fund.
- Risk of fraud in revenue recognition.
- Risk of management override.

The 'addressing audit risks' section of this report sets out how we have gained audit assurance over those issues and others identified during the audit.

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Other reporting issues

We have one matter we wish to report relating to a debt of £6.4 million in respect of St Mary's school. This debt, due from the Diocese of St Albans has been outstanding for several years. We are seeking specific representations on its collectability.

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Control observations

We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements of which you are not aware.

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We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Neil Harris

Director  
For and on behalf of Ernst & Young LLP

## 2. Responsibilities and purpose of our work

### The Council's responsibilities

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

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

### Purpose of our work

Our audit was designed to:

- Express an opinion on the 2015/16 financial statements of the Council, the Group and the fire-fighters' pension fund and the consistency of other information published with them;
- Report on an exception basis on the Annual Governance Statement;
- Consider and report any matters that prevent us being satisfied that the Council had put in place proper arrangements for securing economy, efficiency and effectiveness in the use of resources (the value for money conclusion); and
- Discharge our statutory duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

In addition, this report contains our findings related to the areas of audit emphasis and any views on significant deficiencies in internal control or the Council's accounting policies and key judgments.

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the National Audit Office.

### 3. Financial statements audit

#### Addressing audit risks

We identified the following audit risks during the planning phase of our audit, and reported these in our audit plan. Here, we set out how we have gained audit assurance over those issues.

A significant audit risk in the context of the audit of the financial statements is an inherent risk with both a higher likelihood of occurrence and a higher magnitude of effect should it occur and which requires special audit consideration. For significant risks, we obtain an understanding of the entity's controls relevant to each risk and assess the design and implementation of the relevant controls.

Significant Risks (including fraud risks)	Audit procedures performed	Assurance gained and issues arising
<p><b>Property asset valuation</b></p> <p>Valuation of property assets and capital expenditure are significant accounting estimates that have material impact on the financial statements.</p> <p>One area which may be susceptible to manipulation is the capitalisation of revenue expenditure on Property, Plant and Equipment given the extent of the Council's capital programme.</p>	<ul style="list-style-type: none"> <li>Assessed and placed reliance on property valuation specialists commissioned by the Council and the auditor.</li> <li>Assessed and used an independent valuer's market report to assess and challenge the assumptions and judgements used by the Council's external valuer in valuing the Council's property.</li> <li>Tested the accounting entries made for revaluations.</li> <li>Tested the additions to the Property, Plant and Equipment balance to ensure that they are properly classified as capital expenditure.</li> </ul>	<p>We have completed our planned procedures and have placed reliance on the work of the specialists.</p> <p>We used an independent valuer's market report to assess the overall reasonableness of the revaluations undertaken in the year. We also considered an impairment review undertaken by the Council's valuers.</p> <p>Our testing of the processing of revaluation entries revealed some errors which have been corrected in the accounts. These did not impact on the Council's reported financial position.</p> <p>The introduction of IFRS 13 –Fair Value Measurement has required surplus assets to be revalued on a new basis of highest and best use. Those surplus assets which were revalued in the year were done on the correct basis. However the Council has around 115 assets with a value of £36 million which had been valued in prior years and not been reassessed in 2015/16. These assets were subsequently reviewed by the valuer who has confirmed that the value at which they are currently held is in line with fair value given their current planning status.</p> <p>We have completed our testing of additions to ensure that they have been properly capitalised and have identified no evidence of mis-classification.</p>

Significant Risks (including fraud risks)	Audit procedures performed	Assurance gained and issues arising
<p><b>Better Care Fund</b></p> <p>The Better Care Fund (BCF) is a major policy initiative between local authorities, CCGs and NHS providers with a primary aim of driving closer integration and improving outcomes for patients, service users and carers. The intention is that partners use the BCF to jointly commission health and social care services at a local level.</p> <p>From 1 April 2015 BCF has been set up as a pooled budget between the Council and local Clinical Commissioning Groups (CCGs). The pool is managed by the Council and has total funding of £230 million in 2015/16. The Council has contributed £110 million.</p> <p>Local BCF arrangements may be complex and varied, involving a number of different commissioning, governance and accounting arrangements that raise risks of misunderstanding and inconsistencies between the partners. There are also structural, cultural and regulatory differences between local government and the NHS, and it is important that these are understood and considered by all of the partners in the operation of the BCF.</p>	<ul style="list-style-type: none"> <li>• Examined relevant S75 agreements entered into by the Council.</li> <li>• Reviewed proposed accounting treatments for the Better Care Fund and the disclosures made under relevant accounting standards. As part of this, we considered what relevant activities are undertaken and whether participants have control, either jointly or solely, over the arrangement.</li> <li>• Performed testing to gain assurance that the Council has appropriately accounted for its share of the pool.</li> </ul>	<p>We have considered the accounting treatment proposed by the Council and agreed with the CCGs. This analysed all the projects and funding streams within the Better Care Fund to determine which were jointly controlled and therefore pooled and which were controlled by only one of the participants. We agreed with the conclusions drawn.</p> <p>Our testing to confirm that the Council has correctly accounted for the transactions is complete and we are satisfied with the treatment adopted.</p> <p>We also noted that disclosures made by the Council in the pooled budget note in the accounts are in line with those made by the CCGs who prepared their accounts earlier in the year.</p>
<p><b>Risk of management override</b></p> <p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<ul style="list-style-type: none"> <li>• Tested the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.</li> <li>• Reviewed accounting estimates for evidence of management bias.</li> <li>• Evaluated the business rationale for any significant unusual transactions.</li> </ul>	<p>We have not identified any material weaknesses in controls or evidence of material management override.</p> <p>We obtained a full list of the journals posted to the general ledger during the year, and analysed these journals using criteria we set to identify unusual journal types or amounts. We then tested a sample of journals that met our criteria to supporting documentation.</p> <p>We considered that the accounting estimates most susceptible to bias were</p> <ul style="list-style-type: none"> <li>• Property valuations (see above)</li> <li>• Pensions entries based on figures supplied by the actuary</li> <li>• Private Finance Initiative schemes</li> </ul> <p>Overall there was no indication of bias within the calculation of these accounting estimates.</p> <p>We have identified no transactions during our audit which appeared unusual or outside the Council's normal course of business.</p>



Significant Risks (including fraud risks)	Audit procedures performed	Assurance gained and issues arising
<p><b>Risk of fraud in revenue recognition</b></p> <p>Under ISA240 there is a presumed risk that revenue may be misstated due to improper recognition of revenue.</p> <p>In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.</p>	<ul style="list-style-type: none"> <li>• Reviewed and tested revenue and expenditure recognition policies</li> <li>• Reviewed and discussed with management any accounting estimates on revenue or expenditure recognition for evidence of bias</li> <li>• Developed a testing strategy to test material revenue and expenditure streams</li> <li>• Reviewed and tested revenue cut-off at the period end date</li> </ul>	<p>Our testing focussed on the Council's main expenditure streams and on ensuring that creditors and provisions were not understated, as this would also understate expenditure.</p> <p>We also carried out cut-off testing where we examined a sample of receipts and payments after year end to ensure that where the transactions related to 2015/16 that they were properly recorded in the accounts.</p> <p>Overall our testing did not reveal any material misstatements with respect to revenue and expenditure recognition.</p>

We also identified the following audit risks during the planning phase of our audit, and reported these in our Audit Plan. Here, we set out how we have gained audit assurance over those issues.

Other Risks	Audit procedures performed	Assurance gained and issues arising
<p><b>Group accounts</b></p> <p>The Council set up two companies in September 2013:</p> <ul style="list-style-type: none"> <li>• Hertfordshire Catering Ltd, which is a wholly-owned subsidiary</li> <li>• Herts for Learning Ltd, of which 20% is owned by the Council and the remainder by schools.</li> </ul> <p>The Council continues to assess these interests as quantitatively and qualitatively material to the group and therefore the Council will continue to consolidate the companies into the Council's group accounts as required by the Code of Practice on Local Authority Accounting in the United Kingdom (Code of Practice).</p> <p>There is a risk that the group financial statements do not meet the requirements as defined by the Code.</p>	<p>We reviewed and tested whether the Council has:</p> <ul style="list-style-type: none"> <li>▶ Identified all potential group entities against accounting standards IFRS 10 and 11.</li> <li>▶ Adopted and correctly applied accounting policies that comply with the requirements of the Code.</li> <li>▶ Consolidated the companies' accounts appropriately into the group accounts.</li> <li>▶ Made all appropriate disclosures in accordance with adopted accounting policies and requirements of the Code.</li> </ul> <p>We are responsible for the direction, supervision and performance of the group audit. We therefore instructed the auditor of the companies as part of our audit procedures.</p>	<p>We reviewed the Council's assessment of its interests in companies and other entities which might require consolidation into group accounts. The Council has determined that only Hertfordshire Catering Ltd and Herts for Learning Ltd are sufficiently material to require consolidation. Other interests which do not require consolidation are disclosed in note 48.</p> <p>Earlier in the year we issued instructions to the auditor of these two companies and have maintained an appropriate relationship with them. They have reported to us on the results of their audits.</p> <p>The audit of both companies has been completed and we have received copies of the signed audited accounts. Post audit amendments to Hertfordshire Catering Ltd accounts to reflect the company's tax liability of £0.2 million will also be reflected in the group accounts.</p> <p>We have carried out testing of the consolidation of the Council's accounts with those of the companies and confirmed that appropriate disclosures have been made in the group accounts.</p>

## Other Risks

## Audit procedures performed

## Assurance gained and issues arising

**Highways expenditure**

Internal Audit issued a limited assurance opinion in 2014 on highways contract management, indicating that there were significant weaknesses in key controls. The report noted that weaknesses had been identified in areas of invoicing, reconciliations, budget monitoring and coding of expenditure. Progress has been made in these areas, but processes are still developing and are not yet embedded.

We carried out specific work to address this risk in 2014/15 and noted that there was uncertainty about the final amount which would be paid to the contractor. A final settlement is negotiated with the contractor post year end.

As a result there remains a risk that highways expenditure, both revenue and capital, may be misstated, as the final settlement position for 2015/16 will be estimated at year end.

- Reviewed and tested the reconciliation of payments made to claims submitted by the contractor to provide assurance across the full year's total expenditure.
- Reviewed an overall reconciliation of the amount processed as highways capital expenditure on infrastructure.
- Reviewed the estimates and assumptions made as part of closing the 2015/16 accounts about the final expenditure position which will be agreed with the contractor.
- Considered the outcome of the negotiations on 2014/15 expenditure and whether a final settlement has been agreed and reflected in the 2015/16 accounts.

We have reviewed the reconciliation of payments made during the year to claims submitted by the contractor and have tested nine months in detail. No issues were noted in this testing.

Our testing of infrastructure additions identified no evidence that expenditure had been misclassified as capital. We have reviewed the overall reconciliation of highways capital expenditure with no issues identified.

Last year we reported that the potential outcome for 2014/15 ranged from an over-accrual of £0.3 million if the Council's position was accepted to an under-accrual of £3 million if the deductions and performance caps proposed by the Council were not accepted by the contractor.

During 2015/16 the Council has paid the contractor £3.1 million to settle 2014/15 and a further £0.7 million to settle 2013/14. This was in line with the amount accrued at the end of 2014/15.

In respect of 2015/16 the Council has accounted for expenditure of £46.1 million which includes a year-end accrual of £4.5 million. Payments since year end have been analysed and indicate that the accrual is understated by £80,000. The contractor has confirmed that it has presented its full accounts for the year to the Council so there should be no further payments due.

We are therefore satisfied that revenue and capital highways expenditure in the 2015/16 accounts is not materially misstated.

Internal Audit has recently issued a report on the governance, performance and contract management of the highways contract. Internal Audit has now provided moderate assurance reflecting the improvements to contract arrangements which have been made since the original review in 2014 and noting that an annual plan has been agreed to improve them further.

Other Risks	Audit procedures performed	Assurance gained and issues arising
<p><b>Pensions Ombudsman case GAD v Milne</b></p> <p>In May 2015, the Pensions Ombudsman published a decision which affected fire-fighters who retired between 2001 and 2006. The Ombudsman found that Government Actuary Department (GAD) had not updated the commutation factors which were used to calculate lump sums due on retirement and that fire-fighters who retired in this period were disadvantaged as a result. As a result of this decision these retired fire-fighters were to be compensated.</p> <p>In 2014/15 this was disclosed as a post balance sheet event, but no amendments were made to the accounts.</p> <p>The Department for Communities and Local Government (DCLG) expects these payments to be calculated and paid to affected pensioners by April 2016 and has agreed to fund these payments. The exact method of funding and resulting accounting for these payments is not fully determined, in particular whether they will need to be accounted for via the fire-fighters' pension fund.</p> <p>Such payments would be expected to be material to the fire-fighters' pension fund.</p>	<ul style="list-style-type: none"> <li>Reviewed the progress made in calculating and paying the compensation due.</li> <li>Tested a sample of compensation payments.</li> <li>Performed testing to gain assurance that the Council has appropriately accounted for these payments and the expected DCLG funding.</li> </ul>	<p>During 2015/16 the payments due to the affected pensioners have been calculated and paid. These total £1.1 million and have been charged as benefits payable to the fire-fighters' pension fund.</p> <p>Our testing of a sample of the payments confirms that these have been calculated correctly.</p> <p>The expenditure has been funded by the pension fund top up grant payable by DCLG.</p> <p>The Council has added additional disclosure within the fire-fighters' pension fund accounts to explain the payments made. We have considered the treatment within the accounting for the overall pensions liabilities within the Council's accounts and have confirmed that these have been accounted for appropriately.</p>

## Other matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we are required to communicate to you significant findings from the audit and other matters that are significant to you oversight of the Council's financial reporting process, including the following:

- Qualitative aspects of your accounting practices; estimates and disclosures;
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions;
- Any significant difficulties encountered during the audit; and
- Other audit matters of governance interest

We wish to report the following matter:

### St Mary's school debtor

The Council has a debtor account with the Diocese of St Albans in respect of the former St Mary's school site for £7.4 million partially offset by a bad debt provision of £1 million. The debt has been incurred as the Council supported the Diocese in relocating the school to a different site. The debt is to be settled by the sale of the former school site, which is owned by the Diocese who would then use the proceeds to repay the Council.

This debt has been outstanding for several years and we have sought assurance in the letter of representation in prior years that the amount would be recoverable at or near the full value. During 2015/16 the site has been sold for £6.4 million and the proceeds are held by the Diocese's solicitor pending final negotiations between the buyer of the site, the Diocese and the Council on the final costs. Following agreement the Council expects to be paid the balance held by the solicitor. As in prior years we are seeking representations on the recovery of this debt.

## **Control themes and observations**

It is the responsibility of the Council to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Council has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

We have tested the controls of the Council only to the extent necessary for us to complete our audit. We are not expressing an opinion on the overall effectiveness of internal control.

We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements of which you are not aware.

We have reviewed the Annual Governance Statement and can confirm that it not misleading or inconsistent with other information forthcoming from the audit or our knowledge of the Council.

## **Request for written representations**

We have requested a management representation letter to gain management's confirmation in relation to a number of matters, as outlined in Appendix E. In addition to the standard representations, we have requested the following specific representations:

- The recoverability of a debtor of £6.4 million from the Diocese of St Albans in respect of St Mary's School.

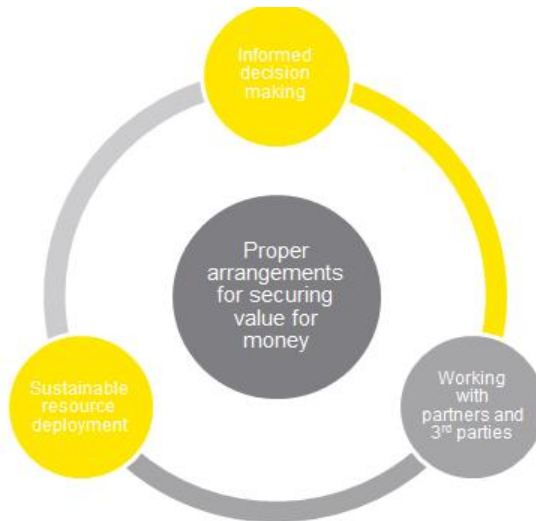
## **Whole of Government Accounts**

Alongside our work on the financial statements, we also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the National Audit Office.

There have been a number of technical issues with the documentation which local authorities are required to use to submit their returns. As a result of these issues the deadline for submission was extended into August. The Council has completed and submitted its return. The NAO has also extended the deadline for auditor completion and certification of the work to 21 October. We have not yet concluded work in this area.

We will provide a verbal update on WGA at the Audit Committee meeting. If we do not conclude our work on WGA prior to the opinion deadline we will be unable to issue our audit completion certificate. We can still issue our audit opinion. We will then need to complete some additional procedures after our completion and certification of the WGA return, prior to issuing the audit certificate.

## 4. Value for money



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

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

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

### Overall conclusion

We identified a significant risk in relation to the arrangements for sustainable resource deployment because the Council has a significant gap between its spending plans and expected income in its medium term financial strategy.

We have performed the procedures outlined in our audit plan. We did not identify any significant weaknesses in the Council's arrangements for sustainable resource deployment.

We therefore expect to conclude that the Council has put in place proper arrangements to secure value for money in its use of resources.

### Significant risk

The table below presents the findings of our work in response to the risk area in our audit plan.

## VFM risk identified within our audit plan

## Key findings

**Financial pressures**

The Council's finances continue to be under significant pressure in the medium term. When setting its 2015/16 budget in early 2015, the Council expected to make savings of £120 million per year by 2017/18. At the time the 2015/16 budget and Integrated Plan was finalised, £56.4 million of that amount was still to be found.

In December 2015 the provisional local government finance settlement was announced which included a significant reduction in government funding beyond that anticipated and already built into the Integrated Plan. Additional transitional grant has since been announced.

The Council is currently developing budget proposals to 2019/20. These show a gap of savings still to be found of £38.4 million in 2017/18 rising to £71.4 million in 2019/20.

The achievement of the Council's Integrated Plans to date has been good. However, the Council has to continue to deliver significant savings year on year in order to bridge the gap and balance its budget.

We reviewed the Council's Integrated Plan covering 2016/17 to 2019/20 and budget setting for 2016/17. We have also assessed the level of reserves (both general fund and earmarked) that the Council has at 31 March 2016.

The Council has well established arrangements for undertaking its medium term financial planning which incorporate key assumptions and sensitivity review.

The Council has a proven track record of achieving its savings and delivering within its budget.

By the end of 2015/16 the Council had underspent its budget by £7.5 million. This was due to a number of factors such as underspending on a number of services, additional grant income and interest on balances and a release of reserves no longer required. The Council has historically underspent its budget, reflecting the level of savings delivered in the year. However the level of underspend is reducing compared to prior years (£27.7 million in 2014/15), reflecting the increasing financial challenges the Council faces.

The General Fund balance at £32.1 million is in line with the minimum prudent level of reserves which is based on 4% of the Council's net budget.

The level of non-schools earmarked reserves have decreased from £89.5 million in March 2015 to £76.3 million in March 2016, a decrease of £13.2 million. This is due primarily to the use of some specific reserves to fund projects in the year.

The 2016/17 budget included an overall increase in council tax of 1.99% together with the social care precept of 2%. The budget was balanced by savings identified of £32.6 million.

The final Integrated Plan shows that the Council needs to make savings of £125 million per year by 2020 and that £75.5 million of that amount remains to be found. The Council is developing its plans for tackling the savings requirement.

We are comfortable that the level of reserves held by the Council at 31 March 2016 covers the budget gap identified within the Integrated Plan to an appropriate level.

On the basis of the work we have undertaken we have concluded that the Council has appropriate arrangements in place for deploying resources in a sustainable manner.

## Appendix A – Outstanding matters

The following items relating to the completion of our audit procedures are outstanding at the date of the release of this report

Item	Actions to resolve	Responsibility
Management representation letter	Receipt of signed letter of representation	Management and Audit Committee
Final accounts	<ul style="list-style-type: none"> <li>Review of final accounts to ensure all expected changes have been made</li> <li>Approval of accounts by Audit Committee</li> <li>Accounts re-certified by RFO</li> </ul>	EY, management and Audit Committee
Subsequent events review	Completion of the subsequent events procedures to the date of signing the audit report	EY and management
Areas of outstanding work	<p>The following are the major areas of work outstanding:</p> <ul style="list-style-type: none"> <li>Receipt of confirmation letters for investments</li> <li>WGA</li> </ul>	EY
Audit closing procedures	Final audit closing procedures and review procedures	EY



## Appendix B – Independence

We confirm there are no changes in our assessment of independence since our confirmation in our Audit Plan dated 29 February 2016.

We complied with the Auditing Practices Board's Ethical Standards for Auditors and the requirements of the Public Sector Audit Appointments Ltd (PSAA)'s Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We confirm that we are not aware of any relationships that may affect the independence and objectivity of the firm that we are required by auditing and ethical standards to report to you.

We consider that our independence in this context is a matter that should be reviewed by both you and ourselves. It is therefore important that you consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the Audit Committee on 23 September 2016.

We confirm that we have met the reporting requirements to the Audit Committee, as 'those charged with governance' under International Standards on Auditing (UK and Ireland) 260 – Communication with those charged with governance. Our communication plan to meet these requirements was set out in our Audit Plan of 29 February 2016.

## Appendix C – Auditor fees

The table below sets out the scale fee and our final proposed audit fees.

Description	Proposed final Fee 2015/16 £	Scale Fee 2015/16 £	Variation comments
Total Audit Fee – Code work	142,067	142,067	None

Our actual fee in in line with the scale fee set by the PSAA at this point in time, subject to satisfactory clearance of the outstanding work.

We confirm we have not undertaken any non-audit work outside of the PSAA's requirements to date in respect of the 2015/16 financial year. In previous years we have carried out work on the teachers' pensions return. We have currently not been requested to carry out work on the 2015/16 return.

## Appendix D – Draft audit report

### Independent auditor's report to the members of Hertfordshire County Council

#### Opinion on the Authority and firefighters' pension fund financial statements

We have audited the financial statements and the firefighters' pension fund financial statements of Hertfordshire County Council for the year ended 31 March 2016 under the Local Audit and Accountability Act 2014. The financial statements comprise the:

- Authority and Group Movement in Reserves Statement,
- Authority and Group Comprehensive Income and Expenditure Statement,
- Authority and Group Balance Sheet,
- Authority and Group Cash Flow Statement,
- Authority and Group Statements of Accounting Policies, the related notes 1 to 48 of the Authority financial statements and the related notes 1 to 4 of the Group financial statements,
- and include the firefighters' pension fund financial statements comprising the Fund Account, the Net Assets Statement and the related notes.

The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

This report is made solely to the members of Hertfordshire County Council, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of the Chief Finance Officer and auditor

As explained more fully in the Statement of the Chief Finance Officer's Responsibilities set out on page 12, the Chief Finance Officer is responsible for the preparation of the Statement of Accounts, which includes the Authority and Group financial statements and the firefighters pension fund financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group's and the firefighters pension fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Chief Finance Officer; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the Statement of Accounts 2015/16 to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially

inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion the financial statements:

- give a true and fair view of the financial position of Hertfordshire County Council and Group as at 31 March 2016 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

### **Opinion on other matters**

In our opinion, the information given in the Statement of Accounts 2015/16 for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which we report by exception**

We report to you if:

- in our opinion the annual governance statement is misleading or inconsistent with other information forthcoming from the audit or our knowledge of the Council;
- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014;
- we make written recommendations to the audited body under Section 24 of the Local Audit and Accountability Act 2014;
- we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014;
- we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014; or
- we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014.

We have nothing to report in these respects.

### **Conclusion on Hertfordshire County Council's arrangements for securing economy, efficiency and effectiveness in the use of resources**

#### **Authority's responsibilities**

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

#### **Auditor's responsibilities**

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the National Audit Office (NAO) requires us to report to you our conclusion relating to proper arrangements.

We report if significant matters have come to our attention which prevent us from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. We are not required to consider, nor have we considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

**Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources**

We have undertaken our review in accordance with the Code of Audit Practice, having regard to the guidance on the specified criterion issued by the Comptroller and Auditor General in November 2015, as to whether Hertfordshire County 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. The Comptroller and Auditor General determined this criterion as that necessary for us to consider under the Code of Audit Practice in satisfying ourselves whether the Council put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

We planned our work in accordance with the Code of Audit Practice. Based on our risk assessment, we undertook such work as we considered necessary to form a view on whether, in all significant respects, the Council had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

**Conclusion**

On the basis of our work, having regard to the guidance issued by the Comptroller and Auditor General in November 2015, we are satisfied that, in all significant respects, Hertfordshire County Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2016.

**Certificate**

We certify that we have completed the audit of the accounts of Hertfordshire County Council in accordance with the requirements of the Local Audit and Accountability Act 2014 and the Code of Audit Practice issued by the National Audit Office.

*OR*

**Delay in certification of completion of the audit**

We cannot formally conclude the audit and issue an audit certificate until we have completed the work necessary to issue our assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. We are satisfied that this work does not have a material effect on the financial statements or on our value for money conclusion.

## Appendix E – Management representation letter

*To be prepared on the Council's letterhead and addressed to Ernst & Young*

This letter of representations is provided in connection with your audit of the consolidated and council financial statements of Hertfordshire County Council ("the Group and Council") for the year ended 31 March 2016. The representations provided in this letter include the financial statements of the fire-fighters' pension fund which are included with the Council's consolidated financial statements.

We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the consolidated and council financial statements give a true and fair view of the Group and Council financial position of Hertfordshire County Council as of 31 March 2016 and of its financial performance and its cash flows for the year then ended in accordance with CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.

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

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

### **A. Financial Statements and Financial Records**

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the financial statements in accordance with the Accounts and Audit Regulations 2015 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16.
2. We acknowledge, as members of management of the Group and Council, our responsibility for the fair presentation of the consolidated and council financial statements. We believe the consolidated and council financial statements referred to above give a true and fair view of the financial position, financial performance and cash flows of the Group in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 and are free of material misstatements, including omissions. We have approved the consolidated and council financial statements.
3. The significant accounting policies adopted in the preparation of the Group and Council financial statements are appropriately described in the Group and Council financial statements.
4. As members of management of the Group and Council, we believe that the Group and Council have a system of internal controls adequate to enable the preparation of accurate financial statements in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2015/16 that are free from material misstatement, whether due to fraud or error.
5. We believe that the effects of any unadjusted audit differences, summarised in the accompanying schedule, accumulated by you during the current audit and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the consolidated and council financial statements taken as a whole. We have not corrected these differences identified by and brought to the attention from the auditor because [specify reasons for not correcting misstatement].

### **B. Fraud**

1. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.

2. We have disclosed to you the results of our assessment of the risk that the consolidated and council financial statements may be materially misstated as a result of fraud.
3. We have disclosed to you all significant facts relating to any frauds, suspected frauds or allegations of fraud known to us that may have affected the Group or Council (regardless of the source or form and including, without limitation, allegations by “whistle-blowers”), whether involving management or employees who have significant roles in internal control. Similarly, we have disclosed to you our knowledge of frauds or suspected frauds affecting the entity involving others where the fraud could have a material effect on the consolidated or council financial statements. We have also disclosed to you all information in relation to any allegations of fraud or suspected fraud communicated by employees, former employees, analysts, regulators or others, that could affect the consolidated or council financial statements.

### **C. Compliance with Laws and Regulations**

1. We have disclosed to you all identified or suspected non-compliance with laws and regulations whose effects should be considered when preparing the consolidated and council financial statements.

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

1. We have provided you with:
  - Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters;
  - Additional information that you have requested from us for the purpose of the audit; and
  - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
2. All material transactions have been recorded in the accounting records and are reflected in the consolidated and council financial statements.
3. We have made available to you all minutes of the meetings of the Council and its committees (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meeting on the following date: 23 September 2016.
4. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Group and Council’s related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the year ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the consolidated and council financial statements.
5. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
6. We have disclosed to you, and the Group and Council has complied with, all aspects of contractual agreements that could have a material effect on the consolidated and council financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

### **E. Liabilities and Contingencies**

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the consolidated and council financial statements.

2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in Note 42 to the consolidated and council financial statements all guarantees that we have given to third parties.

#### **F. Subsequent Events**

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

#### **G. Group audits**

1. There are no significant restrictions on our ability to distribute the retained profits of the Group because of statutory, contractual, exchange control or other restrictions other than those indicated in the Group financial statements.
2. Necessary adjustments have been made to eliminate all material intra-group unrealised profits on transactions amongst council, subsidiary undertakings and associated undertakings.

#### **H. Use of the Work of a Specialist**

1. We agree with the findings of the specialists that we engaged to evaluate the values of the Group and Council's land and buildings and surplus assets and have adequately considered the qualifications of the specialists in determining the amounts and disclosures included in the consolidated and council financial statements and the underlying accounting records. We did not give or cause any instructions to be given to the specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an effect on the independence or objectivity of the specialists.

#### **I. Estimates -Property Valuations**

1. We believe that the measurement processes, including related assumptions and models, used to determine the accounting estimate(s) have been consistently applied and are appropriate.
2. We confirm that the significant assumptions used in making the property valuations appropriately reflect our intent and ability to carry out specific courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures.
3. We confirm that the disclosures made in the consolidated and council financial statements with respect to the accounting estimate(s) are complete and made in accordance with the applicable financial reporting framework.
4. We confirm that no adjustments are required to the accounting estimate(s) and disclosures in the consolidated and council financial statements due to subsequent events.

#### **J. Retirement benefits**

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

#### **K. Going Concern**

1. We have made you aware of any issues that are relevant to the Group and Council's ability to continue as a going concern, including significant conditions and events, our plans for future action and the feasibility of those plans.



2. There are no significant restrictions on our ability to distribute the retained profits of the group because of statutory, contractual, exchange control or other restrictions other than those indicated in the accounts.
3. Necessary adjustments have been made to eliminate all material intra-group unrealised profits on transactions amongst parent, subsidiary undertakings and associated undertakings

**L. Specific Representations**

1. We believe that the debtor included in the financial statements with a net value of £6.4 million due from the Diocese of St Albans in respect of St Mary's school will be recoverable at or near full value by 31 March 2017 and so should be classified as a short term debtor at this value.

Yours sincerely

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Director of Resources

I confirm that this letter has been discussed and agreed at the Audit Committee on 23 September 2016

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Chair of Audit Committee

## Appendix F – Required communications with the Audit Committee

There are certain communications that we must provide to the Audit Committee of UK clients. These are detailed here:

Required communication	Reference
<p><b>Planning and audit approach</b></p> <p>Communication of the planned scope and timing of the audit, including any limitations.</p>	Audit Plan
<p><b>Significant findings from the audit</b></p> <ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	Audit Results Report
<p><b>Going concern</b></p> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	No conditions or events were identified, either individually or in aggregate, that indicated there could be doubt about the Council's ability to continue as a going concern for the 12 months from the date of our report.
<p><b>Misstatements</b></p> <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ In writing, corrected misstatements that are significant</li> </ul>	Audit Results Report
<p><b>Fraud</b></p> <ul style="list-style-type: none"> <li>▶ Enquiries of the audit committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	We have made enquiries of management. We have not become aware of any fraud or illegal acts during our audit.
<p><b>Related parties</b></p> <p>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</p> <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	We have no matters we wish to report.

Required communication	Reference
<p><b>External confirmations</b></p> <ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>	Audit Results Report
<p><b>Consideration of laws and regulations</b></p> <ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ Enquiry of the audit committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the audit committee may be aware of</li> </ul>	We have not identified any material instances of non-compliance with laws and regulations.
<p><b>Independence</b></p> <p>Communication of all significant facts and matters that bear on EY's objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	Audit Plan and Audit Results Report
<p><b>Significant deficiencies in internal controls identified during the audit</b></p>	Audit Results Report
<p><b>Group audits</b></p> <ul style="list-style-type: none"> <li>▶ An overview of the type of work to be performed on the financial information of the components</li> <li>▶ An overview of the nature of the group audit team's planned involvement in the work to be performed by the component auditors on the financial information of significant components</li> <li>▶ Instances where the group audit team's evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor's work</li> <li>▶ Any limitations on the group audit, for example, where the group engagement team's access to information may have been restricted</li> <li>▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements</li> </ul>	Audit Plan Audit Results Report
<p><b>Fee Information</b></p> <ul style="list-style-type: none"> <li>▶ Breakdown of fee information at the agreement of the initial audit plan</li> <li>▶ Breakdown of fee information at the completion of the audit</li> </ul>	Audit Plan Audit Results Report Annual Audit Letter

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