

NORTH LINCOLNSHIRE COUNCIL

AUDIT COMMITTEE

EXTERNAL AUDIT REPORTS

1. OBJECT AND KEY POINTS IN THIS REPORT

- 1.1 To consider external audit's reports:
- Audit Fee Letter 2012/2013
 - Audit Plan 2012/13;and
 - Certification of Claims and Returns.

2. BACKGROUND INFORMATION

- 2.1 The Audit Fee Letter (appendix A) sets out the audit arrangements for 2012/13 covering personnel, the indicative fee, billing arrangements and audit quality. The Audit Plan 2012/13 (appendix B) provides details of external audit's work required to give an opinion on whether the accounts give a true and fair view and a statutory conclusion on the council's arrangements to secure economy, efficiency and effectiveness. The proposed fee for the audit of £137,780 shows a significant reduction on that for 2011/12 of £229,633. However the fee only provides for basic audit work and does not include items such as challenge from ratepayers or following up detailed audit issues. Some extra costs above the basic fee could be incurred.
- 2.2 The Certification of Claims and Returns Report summarises the council's arrangements for claiming grants in 2011/12, and the level of assurance it provides on the operation of the council's procedures. The report is attached at appendix C. Overall there were no significant weaknesses in the council's arrangements to prepare grant claims reported.

3. OPTIONS FOR CONSIDERATION

- 3.1 The Audit Committee should consider the external auditor's reports and the assurance that has been given or can be implied from their conclusions. The Committee should seek clarification from the external auditors or council officers as necessary.

4. ANALYSIS OF OPTIONS

- 4.1 The Audit Plan is the result of a risk assessment and complies with statutory requirements governing external audit and inspection work.

4.2 The Certification of Claims and Returns Report provides a summary of improved performance compared to previous years.

5. RESOURCE IMPLICATIONS (FINANCIAL, STAFFING, PROPERTY, IT)

5.1 Audit Plan fees of £137,780 (plus £24,000 for certification of claims and returns) are met within existing budgets.

6. OTHER IMPLICATIONS (STATUTORY, ENVIRONMENTAL, DIVERSITY, SECTION 17 - CRIME AND DISORDER, RISK AND OTHER)

6.1 External Audit and inspection duties are statutory requirements under the provisions of the Audit Commission Act 1998, the Code of Audit Practice and the Local Government Act 1999.

7. OUTCOMES OF CONSULTATION

7.1 The Audit Plan and Certification of Claims and Returns Report are discussed and agreed with the Director of Policy and Resources.

8. RECOMMENDATIONS

8.1 That the Audit Committee notes the Audit Plan Report and Audit Fee Letter and receives further reports as the work is concluded in the Annual Governance Report and Annual Audit Letter.

8.2 That the Audit Committee notes the Certification of Claims and Returns Report.

DIRECTOR OF POLICY AND RESOURCES

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Author: C Andrews
Date: 07 January 2013

Background Papers used in the preparation of this report

KPMG reports:

Audit Fee Letter and Audit Plan 2012/13

Certification of Claims and Returns – Annual Report 2011/12



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Private & Confidential

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Our ref tr/lh

22 August 2012

Dear Mr Driver

Audit Arrangements for 2012/13

As promised, I am writing to set out the arrangements for the audit of the 2012/13 financial year at North Lincolnshire Council. This letter sets out:

- Audit Personnel;
- The Indicative Audit Fee;
- Billing Arrangements; and
- Audit Quality.

Audit Personnel

We propose that the Engagement Lead for your audit will remain Damian Murray, who is an experienced auditor joining KPMG from the Audit Commission. I have asked Damian to contact you in order to discuss any issues that you may have.

We have not yet allocated Managers or other team members to individual clients, but we will let you know once we have.

Indicative Audit Fee

Our proposals are based on the risk-based approach to audit planning as set out in the Code of Audit Practice and work mandated by the Audit Commission. As the audit for 2011/12 has not yet been completed and we have not yet begun our appointment as your auditors, we will review and update fees as necessary. This will take account of the audit planning process for 2012/13, including the risk assessment. We will naturally keep you informed if there are any changes.

The indicative fee for the audit for 2012/13 is £161,780 (exc VAT) and its breakdown is shown below. These figures incorporate the reductions that the Audit Commission has been able to implement following the market testing of audit services. As you will know, from 2012/13 the Audit Commission is introducing a composite indicative fee for grant certification work for each body. The Commission has calculated the indicative fee based on actual certification fees for 2010/11, adjusted to reflect the fact that a number of schemes will no longer require auditor certification, and incorporating the general reduction to its fee scales.

Audit area	Indicative fee 2012/13
Code of Audit Practice audit	£137,780
Certification of grant claims	£24,000

The indicative fees are based on a number of assumptions, which I have summarised in Appendix 1 to this letter.

In setting the fee at this level, we have assumed that the general level of risk in relation to the audit of the financial statements and certification work is not significantly different from that identified by your previous auditors for 2011/12.

A plan for the audit of the 2012/13 financial statements will be issued later this year. This will detail the risks identified, planned audit procedures and (if required) any changes in fee. If we need to make any significant amendments to the audit fee during the course of the audit, we will first discuss this with you and then prepare a report outlining the reasons why the fee needs to change.

The proposed fee excludes any additional work we may agree to undertake at your request. Any such piece of work will be separately discussed and a detailed project specification agreed with you.

Billing Arrangements

We are taking this opportunity to standardise the billing arrangements for all our audit clients and will bill for audit services quarterly in advance during the year of audit. As you will appreciate, no fees have been raised so far for the financial year 2012/13 so we will bill for the first two quarters on or around 1st September 2012.

Audit Quality

We are committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how we can improve our service, please contact your nominated Engagement Lead in the first instance. Alternatively, you may wish to contact me in my role as KPMG's national contact partner for Audit Commission work.



KPMG LLP
Audit Arrangements for 2012/13
22 August 2012

If we are unable to satisfy your concerns, you have the right to make a formal complaint to the Audit Commission. The complaints procedure is set out in the leaflet '*Something to Complain About*', which is available from the Commission's website (www.audit-commission.gov.uk) or on request.

Yours sincerely

A handwritten signature in black ink that reads 'Trevor Rees'.

Trevor Rees
Contact Partner for Audit Commission Work
KPMG LLP

cc: Damian Murray

Appendix 1 – Audit fee assumptions

In setting the fee, we have assumed that:

- the level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2011/12;
- you will inform us of significant developments impacting on our audit;
- internal audit meets the appropriate professional standards;
- internal audit undertakes appropriate work on all systems that provide material figures in the financial statements sufficient that we can place reliance for the purposes of our audit;
- you will identify and implement any changes required under the CIPFA IFRS-based Code of Practice on local Authority Accounting within your 2012/13 financial statements;
- your financial statements will be made available for audit in line with the timetable we agree with you;
- good quality working papers and records will be provided to support the financial statements in line with our *prepared by client* request and by the date we agree with you;
- requested information will be provided within agreed timescales;
- prompt responses will be provided to draft reports;
- complete and materially accurate claims and returns are provided for certification, with supporting working papers, within agreed timeframes;
- the grant claims and returns requiring certification are as advised to us by the Audit Commission; and
- additional work will not be required to address questions or objections raised by local government electors or for special investigations such as those arising from disclosures under the Public Interest Disclosure Act 1998. The fees for any such work will be agreed with you separately.

Improvements to the above factors may allow reductions to the audit fee in future years. Where these assumptions are not met, we will be required to undertake additional work which is likely to result in an increased audit fee. The fee for the audit of the financial statements will be revisited when we issue the financial statements audit plan.

Any changes to our audit plan and fee will be agreed with you. Changes may be required if:

- new residual audit risks emerge;
- additional work is required by the Audit Commission, KPMG or other regulators; or
- additional work is required as a result of changes in legislation, professional standards or as a result of changes in financial reporting.



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External Audit Plan 2012/13

North Lincolnshire Council

January 2013



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This report is addressed to the Council and has been prepared for the sole use of the Council. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.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.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Damian Murray, the appointed engagement lead to the Council, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by email to complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421.

This document describes how we will deliver our audit work for North Lincolnshire Council.

Scope of this report

This document supplements our *Audit Fee Letter 2012/13* issued to officers in August 2012 and presented to you in January 2013. It describes how we will deliver our financial statements audit work for North Lincolnshire Council ('the Council'). It also sets out our approach to value for money (VFM) work for 2012/13.

We are required to satisfy ourselves that your accounts comply with statutory requirements and that proper practices have been observed in compiling them. We use a risk based audit approach.

The audit planning process and risk assessment is an on-going process and the assessment and fees in this plan will be kept under review and updated if necessary.

Statutory responsibilities

Our statutory responsibilities and powers are set out in the *Audit Commission Act 1998*, the *Local Government Act 1999* and the Audit Commission's *Code of Audit Practice*.

The *Code of Audit Practice* summarises our responsibilities into two objectives, requiring us to review and report on your:

- *financial statements (including the Annual Governance Statement)*: providing an opinion on your accounts; and
- *use of resources*: concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the value for money conclusion).

The Audit Commission's *Statement of Responsibilities of Auditors and Audited Bodies* sets out the respective responsibilities of the auditor and the Council.

Structure of this report

This report is structured as follows:

- Section 2 includes our headline messages, focusing on the key risks identified this year for the financial statements audit.
- Section 3 describes the approach we take for the audit of the financial statements.
- Section 4 provides further detail on the financial statements audit risks.
- Section 5 explains our approach to VFM work.
- Section 6 provides information on the audit team, our proposed deliverables, the timescales and fees for our work.

Acknowledgements

We would like to take this opportunity to thank officers and members for their continuing help and co-operation throughout our audit work.

Delivery of the savings plans for 2012/13 and beyond continue to provide a challenge to the Council. However, we have not identified any significant risks to focus on during the audit of the 2012/13 financial statements.

The remainder of this document provides information on our:

- approach to the audit of the financial statements;
- approach to VFM work; and
- audit team, proposed deliverables, timescales and fees for our work.

Area	Issue	Audit work
Savings plans	<p>The Council estimates that is required to deliver some significant savings during 2013/14 to address reductions to local authority funding and continued cost pressures.</p> <p>Working towards this, the Council continues to monitor its budget position and in September 2012 reported that overall spending against the revenue budget was on target.</p> <p>The Council will need to establish and manage its savings plans to secure longer term financial and operational sustainability and ensure that any related liabilities are accounted for in its 2012/13 financial statements as appropriate.</p>	<p>Whilst this is not a significant risk to our audit of the financial statements, we will monitor the Council's financial standing and review how the Council is planning and managing its savings plans as part of our VFM work.</p>

We undertake our work on your financial statements in four key stages during 2013:

- **Planning**
(January to February).
- **Control Evaluation**
(February to April).
- **Substantive Procedures**
(July to August).
- **Completion** (September).

We have summarised the four key stages of our financial statements audit process for you below:



During January and February 2013 we complete our planning work.

We assess the key risks affecting the Council's financial statements and discuss these with officers.

We assess if there are any weaknesses in respect of central processes, including the Council's IT systems, that would impact on our audit.

We determine our audit strategy and approach, and agree a protocol for the accounts audit, specifying what evidence we expect from the Council to support the financial statements.

Our planning work takes place in January and February 2013. This involves the following aspects:

Planning

- Update our business understanding and risk assessment.
- Assess the organisational control environment.
- Determine our audit strategy and plan the audit approach.
- Issue our *Accounts Audit Protocol*.

Business understanding and risk assessment

We update our understanding of the Council's operations and identify any areas that will require particular attention during our audit of the Council's financial statements.

We identify the key risks affecting the Council's financial statements. These are based on our knowledge of the Council, our sector experience and our ongoing dialogue with Council staff. The risks identified to date are set out in this document. Our audit strategy and plan will, however, remain flexible as the risks and issues change throughout the year. It is the Council's responsibility to adequately address these issues. We encourage the Council to raise any technical issues with us as early as possible so that we can agree the accounting treatment in advance of the audit visit.

We meet with the finance team on a quarterly basis to consider issues and how they are addressed during the financial year end closedown and accounts preparation.

Organisational control environment

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would impact on our audit. In particular risk management, internal control and ethics and conduct have implications for our financial statements audit. The scope of their work of your internal auditors also informs our risk assessment.

The Council relies on information technology (IT) to support both financial reporting and internal control processes. In order to satisfy ourselves that we can rely on the use of IT, we test controls over access to systems and data, system changes, system development and computer operations. Whilst we undertake some general IT controls work, where relevant, we also focus on testing the specific applications and reports that are pivotal to the production of the financial statements.

Audit strategy and approach

The Engagement Lead sets the overall direction of the audit and decides the nature and extent of audit activities.

We design audit procedures in response to the risk that the financial statements are materially misstated. The materiality level is a matter of judgement and is set by the Engagement Lead.

Accounts audit protocol

At the end of our planning work we will issue our *Accounts Audit Protocol*. This important document sets out our audit approach and timetable. It also summarises the working papers and other evidence we require the Council to provide during our interim and final accounts visits.

Your prior auditors met with the finance team to discuss mutual learning points from the 2011/12 audit. We revisit progress against areas identified for development as the audit progresses.

During February to April 2013 we will complete our interim audit work.

We assess if controls over key financial systems were effective during 2012/13. We work with your Internal Audit team to avoid duplication.

We work with your finance team to enhance the efficiency of the accounts audit.

Where relevant, we will present our *Interim Report* to the Audit Committee in June.

Our interim visit on site will be completed during March 2013. During this time we will complete work in the following areas:

Control Evaluation

- Evaluate and test controls over key financial systems identified as part of our risk assessment.
- Review the work undertaken by the internal audit function on controls relevant to our risk assessment.
- Review the accounts production process.
- Review progress on critical accounting matters.

Controls over key financial systems

We update our understanding of the Council's key financial processes where our risk assessment has identified that these are relevant to our final accounts audit and where we have determined that this is the most efficient audit approach to take. We confirm our understanding by completing walkthroughs for these systems. We then test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Appendix 1 illustrates how we determine the most effective balance of internal controls and substantive audit testing.

Where our audit approach is to undertake controls work on financial systems, we seek to rely on any relevant work they have completed to minimise unnecessary duplication of work. Our audit fee is set on the assumption that we can place reliance on their work. We have met with the Head of Audit, Risk and Insurance to discuss the principles and timetables for the managed audit process for 2012/13.

Review of internal audit

Where we intend to rely on internal audit's work in respect of the key financial systems identified as part of our risk assessment, auditing standards require us to review aspects of their work. This includes re-performing a sample of tests completed by internal audit. We will provide feedback to the Head of Audit, Risk and Insurance at the end of our interim visit.

Accounts production process

A recommendation was raised in the 2011/12 Report to Those Charged with Governance (*ISA 260 Report*) in respect of the accounts production process. This principally related to the need to improve your quality assurance arrangements to identify errors in the draft accounts.

We will assess the Council's progress in addressing the recommendation and in preparing for the year-end closedown and accounts preparation.

Critical accounting matters

We will discuss the work completed to address the specific risks we identified at the planning stage. Wherever possible, we seek to review relevant workings and evidence and agree the accounting treatment as part of our interim work.

Following our interim visit, if required, we will issue our Interim Report which will set out the findings of our planning and interim work. This will be discussed at the Audit Committee meeting in June 2013.

During July to August 2013 we will be on site for our substantive work.

We complete detailed testing of accounts and disclosures and conclude on critical accounting matters, such as specific risk areas. We then agree any audit adjustments required to the financial statements.

We also review the Annual Governance Statement for consistency with our understanding.

We will present our ISA 260 Report to the Audit Committee in September 2013.

Our final accounts visit on site has been provisionally scheduled for the period 8 July to 9 August. During this time, we will complete the following work:

Substantive Procedures

- Plan and perform substantive audit procedures.
- Conclude on critical accounting matters.
- Identify and assess any audit adjustments.
- Review the Annual Governance Statement.

Substantive audit procedures

We complete detailed testing on significant balances and disclosures. The extent of our work is determined by the Engagement Lead based on various factors such as our overall assessment of the Council's control environment, the effectiveness of controls over individual systems and the management of specific risk factors.

Critical accounting matters

We conclude our testing of the key risk areas as identified at the planning stage and any additional issues that may have emerged since. We will discuss our early findings of the Council's approach to address the key risk areas with the Corporate Finance Manager in March 2013, prior to reporting to the Audit Committee in June 2013.

Audit adjustments

During our on site work, we will meet with the Corporate Finance Manager on a weekly basis to discuss the progress of the audit, any differences found and any other issues emerging.

At the end of our on site work, we will hold a closure meeting, where we will provide a schedule of audit differences and agree a timetable for the completion stage and the accounts sign off.

To comply with auditing standards, we are required to report uncorrected audit differences to the Audit Committee. 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.

Annual Governance Statement

We are also required to satisfy ourselves that your Annual Governance Statement complies with the applicable framework and is consistent with our understanding of your operations. Our review of the work of internal audit and consideration of your risk management and governance arrangements are key to this.

We report the findings of our final accounts work in our ISA 260 Report, which we will issue to Audit Committee in September 2013.

In addition to the financial statements, we also audit the Council's Whole of Government Accounts pack.

We may need to undertake additional work if we receive objections to the accounts from local electors.

We will communicate with you throughout the year, both formally and informally.

Whole of government accounts (WGA)

We are required to review and issue an opinion on your WGA consolidation to confirm that this is consistent with your financial statements. The audit approach has been agreed with HM Treasury and the National Audit Office.

Elector challenge

The Audit Commission Act 1998 gives electors certain rights. These are:

- the right to inspect the accounts;
- the right to ask the auditor questions about the accounts; and
- the right to object to the accounts.

As a result of these rights, in particular the right to object to the accounts, we may need to undertake additional work to form our decision on the elector's objection. The additional work could range from a small piece of work where we interview an officer and review evidence to form our decision, to a more detailed piece of work, where we have to interview a range of officers, review significant amounts of evidence and seek legal representations on the issues raised.

The costs incurred in responding to questions or objections raised by electors is not part of the fee. This work will be charged in accordance with the Audit Commission's fee scales.

Reporting and communication

Reporting is a key part of the audit process, not only in communicating the audit findings for the year, but also in ensuring the audit team are accountable to you in addressing the issues identified as part of the audit strategy. Throughout the year we will communicate with you through meetings with the finance team and the Audit Committee. Our deliverables are included on page 16.

Use of off-shore audit resources

During our audit work we may make use of our KPMG Global Services (KGS Audit) team in India to undertake certain basic audit tasks and functions. Use of this 'off-shore' team is one of many initiatives we employ to deliver a cost-effective audit service for our clients. Although based in India, the KGS Audit team works closely with our local audit teams to undertake certain audit procedures remotely. We have provided our UK teams with guidance on the types of audit procedures and other tasks that it is suitable and permissible to use KGS Audit for - we do not use KGS Audit for any audit procedures that involve access to personal, confidential or sensitive information. Audit tasks are then allocated by our UK-based engagement teams to dedicated teams in India, allowing local staff to control what work KGS Audit undertakes and what information is accessed. They operate to our same quality standards and all work undertaken by KGS Audit is reviewed by the UK team.

The KGS Audit team operates in a paperless environment and we apply robust processes to control how data is accessed and used:

- all work is conducted electronically;
- all data files are maintained on servers in the UK with restricted access and only viewed on screen in India. These servers are governed by established KPMG IT controls;
- policy and technology restrictions are in place to protect data, for example locked down USB ports, no external emailing, no printing;
- KGS Audit staff are based in an office with restricted access and security; and
- the team members adhere to global KPMG ethics and independence standards, along with requirements governing the non-disclosure of client information.

Our independence and objectivity responsibilities under the Audit Commission's Code of Audit Practice are summarised in Appendix 2. We confirm our audit team's independence and objectivity is not impaired.

Independence and objectivity confirmation

Professional standards require auditors to communicate to those charged with governance, at least annually, all relationships that may bear on the firm's independence and the objectivity of the audit engagement partner and audit staff. The standards also place requirements on auditors in relation to integrity, objectivity and independence.

The standards define 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case this is the Audit Committee.

KPMG LLP is committed to being and being seen to be independent. APB Ethical Standard 1 Integrity, Objectivity and Independence requires us to communicate to you in writing all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and the audit team.

Confirmation statement

We confirm that as of 15 January 2013 in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Engagement Lead and audit team is not impaired.

As at January 2013 we have not identified any key financial statements audit risks.

Key audit risks	Impact on audit
As at January 2013 we have not identified any key financial statements audit risks.	We will review and update our risk assessment as required throughout the year. Any risks arising during the year will be reported upon in our Interim Audit Report.

Our approach to VFM work follows guidance provided by the Audit Commission.

Background to approach to VFM work

In meeting their statutory responsibilities relating to economy, efficiency and effectiveness, the Commission's *Code of Audit Practice* requires auditors to:

- plan their work based on consideration of the significant risks of giving a wrong conclusion (audit risk); and
- carry out only as much work as is appropriate to enable them to give a safe VFM conclusion.

To provide stability for auditors and audited bodies, the Audit Commission has kept the VFM audit methodology unchanged from last year. There are only relatively minor amendments to reflect the key issues facing the local government sector.

The approach is structured under two themes, as summarised below.

Specified criteria for VFM conclusion	Focus of the criteria	Sub-sections
The organisation has proper arrangements in place for securing financial resilience .	The organisation has robust systems and processes to: <ul style="list-style-type: none"> ■ manage effectively financial risks and opportunities; and ■ secure a stable financial position that enables it to continue to operate for the foreseeable future. 	<ul style="list-style-type: none"> ■ Financial governance ■ Financial planning ■ Financial control
The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness .	The organisation is prioritising its resources within tighter budgets, for example by: <ul style="list-style-type: none"> ■ achieving cost reductions; and ■ improving efficiency and productivity. 	<ul style="list-style-type: none"> ■ Prioritising resources ■ Improving efficiency and productivity

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

Overview of the VFM audit approach

The key elements of the VFM audit approach are summarised below.



Each of these stages are summarised further below.

VFM audit stage	Audit approach
VFM audit risk assessment	<p>We consider the relevance and significance of the potential business risks faced by all local authorities, and other risks that apply specifically to the Council. These are the significant operational and financial risks in achieving statutory functions and objectives, which are relevant to auditors' responsibilities under the <i>Code of Audit Practice</i>.</p> <p>In doing so we consider:</p> <ul style="list-style-type: none"> the Council's own assessment of the risks it faces, and its arrangements to manage and address its risks; information from the Audit Commission's VFM profile tool and financial ratios tool; evidence gained from previous audit work, including the response to that work; and the work of the Audit Commission, other inspectorates and review agencies.

Our VFM audit will draw heavily on other audit work which is relevant to our VFM responsibilities and the results of last year's VFM audit.

We will then form an assessment of residual audit risk to identify if there are any areas where more detailed VFM audit work is required.

VFM audit stage	Audit approach
Linkages with financial statements and other audit work	<p>There is a degree of overlap between the work we do as part of the VFM audit and our financial statements audit. For example, our financial statements audit includes an assessment and testing of the Council's organisational control environment, including the Council's financial management and governance arrangements, many aspects of which are relevant to our VFM audit responsibilities.</p> <p>We have always sought to avoid duplication of audit effort by integrating our financial statements and VFM work, and this will continue. We will therefore draw upon relevant aspects of our financial statements audit work to inform the VFM audit.</p>
Assessment of residual audit risk	<p>It is possible that further audit work may be necessary in some areas to ensure sufficient coverage of the two VFM criteria.</p> <p>Such work may involve interviews with relevant officers and /or the review of documents such as policies, plans and minutes. We may also refer to any self assessment the Council may prepare against the characteristics.</p> <p>To inform any further work we must draw together an assessment of residual audit risk, taking account of the work undertaken already. This will identify those areas requiring further specific audit work to inform the VFM conclusion.</p> <p>At this stage it is not possible to indicate the number or type of residual audit risks that might require additional audit work, and therefore the overall scale of work cannot be easily predicted. If a significant amount of work is necessary then we will need to review the adequacy of our agreed audit fee.</p>
Identification of specific VFM audit work	<p>If we identify residual audit risks, then we will highlight the risk to the Council and consider the most appropriate audit response in each case, including:</p> <ul style="list-style-type: none"> ■ considering the results of work by the Council, the Audit Commission, other inspectorates and review agencies; and ■ carrying out local risk-based work to form a view on the adequacy of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources.

Where relevant, we may draw upon the range of audit tools and review guides developed by the Audit Commission.

We will report on the results of the VFM audit through our *Interim Audit Report* and our *Report to those charged with governance*.

VFM audit stage	Audit approach
Delivery of local risk based work	<p>Depending on the nature of the residual audit risk identified, we may be able to draw on audit tools and sources of guidance when undertaking specific local risk-based audit work, such as:</p> <ul style="list-style-type: none"> ■ local savings review guides based on selected previous Audit Commission national studies; and ■ update briefings for previous Audit Commission studies. <p>The tools and guides will support our work where we have identified a local risk that is relevant to them. For any residual audit risks that relate to issues not covered by one of these tools, we will develop an appropriate audit approach drawing on the detailed VFM guidance and other sources of information.</p>
Concluding on VFM arrangements	<p>At the conclusion of the VFM audit we will consider the results of the work undertaken and assess the assurance obtained against each of the VFM themes regarding the adequacy of the Council's arrangements for securing economy, efficiency and effectiveness in the use of resources.</p> <p>If any issues are identified that may be significant to this assessment, and in particular if there are issues that indicate we may need to consider qualifying our VFM conclusion, we will discuss these with management as soon as possible. Such issues will also be considered more widely as part of KPMG's quality control processes, to help ensure the consistency of auditors' decisions.</p>
Reporting	<p>We will report on the results of the VFM audit through our <i>Interim Audit Report</i> and our <i>Report to those charged with governance</i>. These reports will summarise our progress in delivering the VFM audit, the results of the risk assessment and any specific matters arising, and the basis for our overall conclusion.</p> <p>The key output from the work will be the VFM conclusion (i.e. our opinion on the Council's arrangements for securing VFM), which forms part of our audit report.</p> <p>If considered appropriate, we may produce a separate report on the VFM audit, either overall or for any specific reviews that we may undertake.</p>

Your audit team has been drawn from our specialist public sector assurance department. With the exception of the Manager, our audit team were all part of the North Lincolnshire Council audit last year. Contact details are shown on page 1.

The audit team will be assisted by other KPMG specialists as necessary.



Damian Murray
Director

“My role is to lead our team and ensure the delivery of a high quality external audit opinion. I will be the main point of contact for the Audit Committee and Executive Directors.”



Linda Wild
Manager

“I am responsible for the management, review and delivery of the whole audit and providing quality assurance for any technical accounting areas. I will work closely with the Director to ensure we add value. I will liaise with the Director of Policy and Resources, and the Head of Audit, Risk and Insurance.”



Matthew Moore
Assistant Manager

“I will be responsible for the on-site delivery of our work. I will liaise with the Finance Managers and Internal Audit . I will also supervise the work of our audit assistants.”

At the end of each stage of our audit we issue certain deliverables, including reports and opinions.

Our key deliverables will be delivered to a high standard and on time.

We will discuss and agreed each report with the Council's officers prior to publication.

Deliverable	Purpose	Committee dates
Planning		
External Audit Plan	<ul style="list-style-type: none"> ■ Outline audit approach. ■ Identify areas of audit focus and planned procedures. 	January 2013
Control evaluation		
Interim Report	<ul style="list-style-type: none"> ■ Details and resolution of control and process issues. ■ Identify improvements required prior to the issue of the draft financial statements and the year-end audit. 	June 2013
Substantive procedures		
Report to Those Charged with Governance (ISA 260 Report)	<ul style="list-style-type: none"> ■ Details the resolution of key audit issues. ■ Communication of adjusted and unadjusted audit differences. ■ Performance improvement recommendations identified during our audit. ■ Commentary on the Council's value for money arrangements. 	September 2013
Completion		
Auditor's report	<ul style="list-style-type: none"> ■ Providing an opinion on your accounts (including the Annual Governance Statement). ■ Concluding on the arrangements in place for securing economy, efficiency and effectiveness in your use of resources (the VFM conclusion). 	September 2013
Annual Audit Letter	<ul style="list-style-type: none"> ■ Summarises the outcomes and the key issues arising from our audit work for the year. 	November 2013

We will be in continuous dialogue with you throughout the audit.

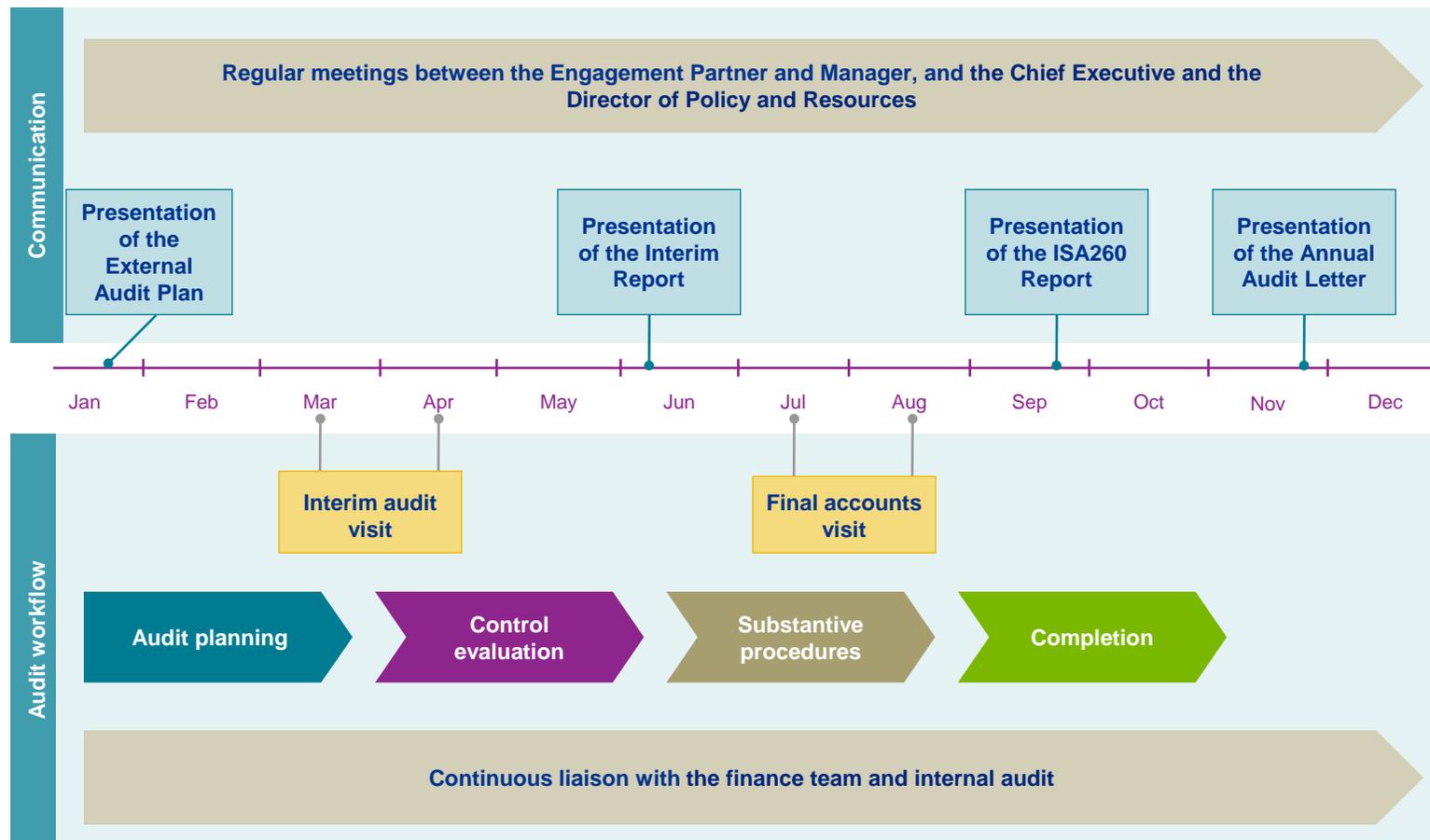
Key formal interactions with the Audit Committee are:

- January – Financial Statements Audit Plan;
- June – Interim Report (if required);
- September – ISA 260 Report;
- November – Annual Audit Letter.

We work with the finance team and internal audit throughout the year.

Our main work on site will be our:

- Interim audit visits during March and April.
- Final accounts audit during July and August.



Key: ● Audit Committee meetings.

The main fee for 2012/13 audit of the Council is £137,780. The fee has not changed from that set out in our Audit Fee Letter 2012/13 issued in August 2012.

Our audit fee remains indicative and based on you meeting our expectations of your support.

Meeting these expectations will help the delivery of our audit within the proposed audit fee.

Audit fee

Our Audit Fee Letter 2012/13 issued to the Council in August 2012 (and presented to you in January 2013) sets out our fees for the 2011/12 audit. We have not considered it necessary to make any changes to the agreed fees at this stage.

Element of the audit	2012/13 (planned)	2011/12 (actual)
Gross audit fee	£137,780	£229,633

Our audit fee includes our work on the VFM conclusion and our audit of the Council's financial statements. The fee for 2012/13 is £137,780. This is a reduction of 40 percent compared to the 2011/12 fee.

Audit fee assumptions

The fee is based on a number of assumptions, including that you will provide us with complete and materially accurate financial statements, with good quality supporting working papers, within agreed timeframes. It is imperative that you achieve this. If this is not the case and we have to complete more work than was envisaged, we will need to charge additional fees for this work. In setting the fee, we have assumed:

- the level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2011/12;
- you will inform us of any significant developments impacting on our audit;
- you will identify and implement any changes required under the *CIPFA Code of Practice on Local Authority Accounting in the UK 2012/13* within your 2012/13 financial statements;
- you will comply with the expectations set out in our *Accounts Audit Protocol*, including:
 - the financial statements are made available for audit in line with the agreed timescales;
 - good quality working papers and records will be provided at the start of the final accounts audit;

- requested information will be provided within the agreed timescales; and
- prompt responses will be provided to queries and draft reports;
- internal audit meets appropriate professional standards;
- internal audit completes appropriate work on all systems that provide material figures for the financial statements and we can place reliance on them for our audit; and
- additional work will not be required to address questions or objections raised by local government electors.

Meeting these expectations will help ensure the delivery of our audit within the agreed audit fee. Where these assumptions are not met, we will be required to undertake additional work which is likely to result in an increased fee.

The Audit Commission requires us to inform you of specific actions you could take to keep the audit fee low. Future audit fees can be kept to a minimum if the Council achieves an efficient and well-controlled financial closedown and accounts production process which complies with good practice and appropriately addresses new accounting developments and risk areas.

Changes to the audit plan

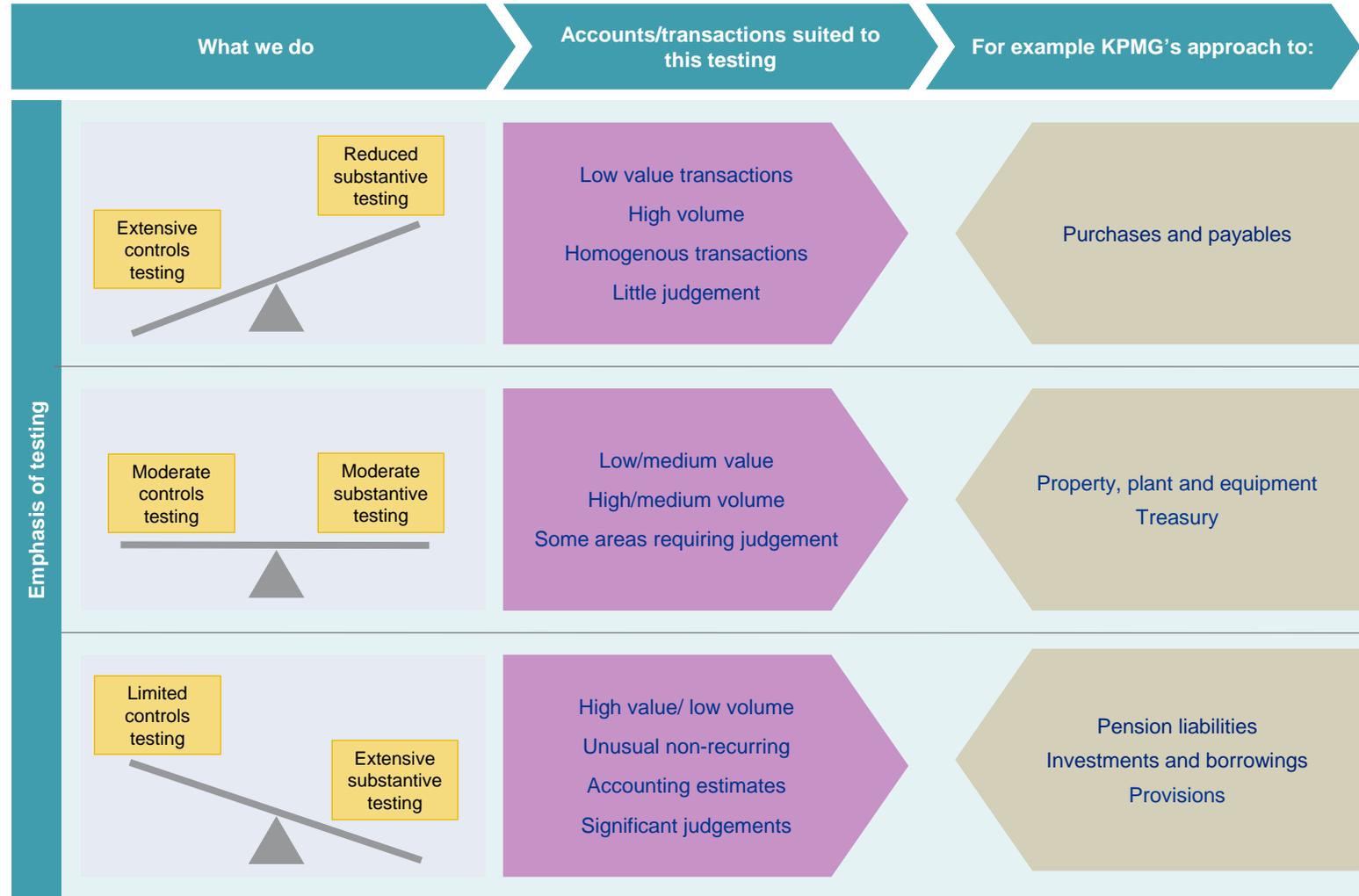
Changes to this plan and the audit fee may be necessary if:

- new significant audit risks emerge;
- additional work is required of us by the Audit Commission or other regulators; and
- additional work is required as a result of changes in legislation, professional standards or financial reporting requirements.

If changes to this plan and the audit fee are required, we will discuss and agree these initially with the Director of Policy and Resources.

Appendix 1: Balance of internal controls and substantive testing

This appendix illustrates how we determine the most effective balance of internal controls and substantive audit testing.



This appendix summarises auditors' responsibilities regarding independence and objectivity.

Independence and objectivity

Auditors are required by the *Code of Audit Practice (the Code)* to:

- carry out their work with independence and objectivity;
- exercise their professional judgement and act independently of both the Commission and the audited body;
- maintain an objective attitude at all times and not act in any way that might give rise to, or be perceived to give rise to, a conflict of interest; and
- resist any improper attempt to influence their judgement in the conduct of the audit.

In addition, *the Code* specifies that auditors should not carry out work for an audited body that does not relate directly to the discharge of the auditors' functions under *the Code*. If the Council invites us to carry out risk-based work in a particular area, which cannot otherwise be justified to support our audit conclusions, it will be clearly differentiated as work carried out under section 35 of the Audit Commission Act 1998.

The Code also states that the Commission issues guidance under its powers to appoint auditors and to determine their terms of appointment. The Standing Guidance for Auditors includes several references to arrangements designed to support and reinforce the requirements relating to independence, which auditors must comply with. These are as follows:

- Any staff involved on Commission work who wish to engage in political activity should obtain prior approval from the Partner.
- Audit staff are expected not to accept appointments as lay school inspectors.
- Firms are expected not to risk damaging working relationships by bidding for work within an audited body's area in direct competition with the body's own staff without having discussed and agreed a local protocol with the body concerned.

- Auditors are expected to comply with the Commission's statements on firms not providing personal financial or tax advice to certain senior individuals at their audited bodies, auditors' conflicts of interest in relation to PFI procurement at audited bodies, and disposal of consultancy practices and auditors' independence.
- Auditors appointed by the Commission should not accept engagements which involve commenting on the performance of other Commission auditors on Commission work without first consulting the Commission.
- Auditors are expected to comply with the Commission's policy for the Engagement Lead to be changed on each audit at least once every five years (subject to agreed transitional arrangements). Audit suppliers are required to obtain the Commission's written approval prior to changing any Engagement Lead in respect of each audited body.
- Audit suppliers are required to obtain the Commission's written approval prior to changing any Engagement Lead in respect of each audited body.
- The Commission must be notified of any change of second in command within one month of making the change. Where a new Engagement Lead or second in command has not previously undertaken audits under the Audit Commission Act 1998 or has not previously worked for the audit supplier, the audit supplier is required to provide brief details of the individual's relevant qualifications, skills and experience.

Appendix 3: KPMG Audit Quality Framework

We continually focus on delivering a high quality audit.

This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG.

The diagram summarises our approach and each level is expanded upon.

At KPMG we consider audit quality is not just about reaching the right opinion, but how we reach that opinion. KPMG views the outcome of a quality audit as the delivery of an appropriate and independent opinion in compliance with the auditing standards. It is about the processes, thought and integrity behind the audit report. This means, above all, being independent, compliant with our legal and professional requirements, and offering insight and impartial advice to you, our client.

KPMG's Audit Quality Framework consists of seven key drivers combined with the commitment of each individual in KPMG. We use our seven drivers of audit quality to articulate what audit quality means to KPMG.

We believe it is important to be transparent about the processes that sit behind a KPMG audit report, so you can have absolute confidence in us and in the quality of our audit.

Tone at the top: We make it clear that audit quality is part of our culture and values and therefore non-negotiable. Tone at the top is the umbrella that covers all the drives of quality through a focused and consistent voice. Damian Murray as the Engagement Lead sets the tone on the audit and leads by example with a clearly articulated audit strategy and commits a significant proportion of his time throughout the audit directing and supporting the team.

Association with right clients: We undertake rigorous client and engagement acceptance and continuance procedures which are vital to the ability of KPMG to provide high-quality professional services to our clients.

Clear standards and robust audit tools: We expect our audit professionals to adhere to the clear standards we set and we provide a range of tools to support them in meeting these expectations. The global rollout of KPMG's eAudit application has significantly enhanced existing audit functionality. eAudit enables KPMG to deliver a highly

technically enabled audit. All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.



Recruitment , development and assignment of appropriately qualified personnel: One of the key drivers of audit quality is assigning professionals appropriate to the Council's risks. We take great care to assign the right people to the right clients based on a number of factors including their skill set, capacity and relevant experience.

We have a well developed technical infrastructure across the firm that puts us in a strong position to deal with any emerging issues. This includes:

- A national public sector technical director who has responsibility for co-ordinating our response to emerging accounting issues, influencing accounting bodies (such as CIPFA) as well as acting as a sounding board for our auditors.

- A national technical network of public sector audit professionals is established that meets on a monthly basis and is chaired by our national technical director.

- All of our staff have a searchable data base, Accounting Research Online, that includes all published accounting standards, the KPMG Audit Manual Guidance as well as other relevant sector specific publications, such as the Audit Commission's *Code of Audit Practice*.

- A dedicated Department of Professional Practice comprised of over 100 staff that provide support to our audit teams and deliver our web-based bi-monthly technical training.

We continually focus on delivering a high quality audit.

This means building robust quality control procedures into the core audit process rather than bolting them on at the end, and embedding the right attitude and approaches into management and staff.

Quality must build on the foundations of well trained staff and a robust methodology.

Commitment to technical excellence and quality service delivery:

Our professionals bring you up- the-minute and accurate technical solutions and together with our specialists are capable of solving complex audit issues and delivering valued insights.

Our audit team draws upon specialist resources including Forensic, Corporate Finance, Transaction Services, Advisory, Taxation, Actuarial and IT. We promote technical excellence and quality service delivery through training and accreditation, developing business understanding and sector knowledge, investment in technical support, development of specialist networks and effective consultation processes.

Performance of effective and efficient audits: We understand that how an audit is conducted is as important as the final result. Our drivers of audit quality maximise the performance of the engagement team during the conduct of every audit. We expect our people to demonstrate certain key behaviors in the performance of effective and efficient audits. The key behaviors that our auditors apply throughout the audit process to deliver effective and efficient audits are outlined below:

- timely Engagement Lead and manager involvement;
- critical assessment of audit evidence;
- exercise of professional judgment and professional scepticism;
- ongoing mentoring and on the job coaching, supervision and review;
- appropriately supported and documented conclusions;
- if relevant, appropriate involvement of the Engagement Quality Control reviewer (EQC review);
- clear reporting of significant findings;
- insightful, open and honest two-way communication with those charged with governance; and
- client confidentiality, information security and data privacy.

Commitment to continuous improvement: We employ a broad range of mechanisms to monitor our performance, respond to feedback and understand our opportunities for improvement.

Our quality review results

We are able to evidence the quality of our audits through the results of National Audit Office and Audit Commission reviews. The results of the Audit Commission's annual quality review process is made publicly available each year (http://www.audit-commission.gov.uk/audit-regime/Pages/qualityreviewprocess_copy.aspx) . The latest report dated October 2012 showed that we performed highly against all the Commission's criteria.



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Certification of grants and returns 2011/12

North Lincolnshire Council

January 2013



The contacts at KPMG in connection with this report are:

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■ Headlines	2
■ Summary of certification work outcomes	3
■ Fees	5
■ Recommendations	6

This report is addressed to 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. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document.

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.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Damian Murray, who is the engagement leader to the Authority (telephone 01132 231 3510, e-mail Damian.Murray@kpmg.co.uk) who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees (telephone 0161 236 4000, e-mail trevor.rees@kpmg.co.uk) who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by e mail to: complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421.

Introduction and background	<p>This report summarises the results of work on the certification of the Council's 2011/12 grant claims and returns.</p> <ul style="list-style-type: none"> ■ For 2011/12 we certified: <ul style="list-style-type: none"> – 2 grants with a total value of £56m; and – 2 returns with a total value of £81m. 	<p>-</p>
Certification results	<p>We issued unqualified certificates for one grant and both returns , but a qualification was necessary for one grant.</p> <ul style="list-style-type: none"> ■ The qualification for the Housing Benefit and Council Tax Benefit claim was to inform the Department of the minor errors found and corrected within the claim; and ■ This compares favourably with the previous year when there was a specific issue with single residency discount as well as the details of the errors found and corrected. The issues around single residency discounts have been corrected during 2011/12. 	<p>Pages 3 – 4</p>
Audit adjustments	<p>One adjustment was necessary to the Council's grants and returns as a result of our certification work this year.</p> <ul style="list-style-type: none"> ■ The Housing Benefit and Council tax Benefit claim was amended however this had no impact on the subsidy received; and ■ This was an improvement from the previous year as the impact of the single residency discount issue meant a loss of subsidy in 2011/12 due to the errors in 2010/11 being corrected in the system in year. 	<p>Pages 3 – 4</p>
The Council's arrangements	<p>The Council has good arrangements for preparing its grants and returns and supporting our certification work.</p> <ul style="list-style-type: none"> ■ We have no recommendations for improvement this year and this was also the situation in 2010/11. 	<p>Page 6</p>
Fees	<p>Our overall fee for the certification of grants and returns has been contained within the original estimate.</p> <ul style="list-style-type: none"> ■ The actual fee was £35,853 against the estimate of £40,000. ■ The actual fee has reduced by £15,626 compared to 2010/11. 	<p>Page 5</p>

Overall, we certified four grants and returns:

- Three were unqualified with no amendment;
- One required a qualification to our audit certificate.

Detailed comments are provided overleaf.

Detailed below is a summary of the key outcomes from our certification work on the Council's 2011/12 grants and returns, showing where either audit amendments were made as a result of our work or where we had to qualify our audit certificate.

A qualification means that issues were identified concerning the Council's compliance with a scheme's requirements that could not be resolved through adjustment. In these circumstances, it is likely that the relevant grant paying body will require further information from the Council to satisfy itself that the full amounts of grant claimed are appropriate.

The work to certify the claims below was done by the Audit Commission as appointed auditor for 2011/12, and KPMG is therefore only reporting the outcome of their work.

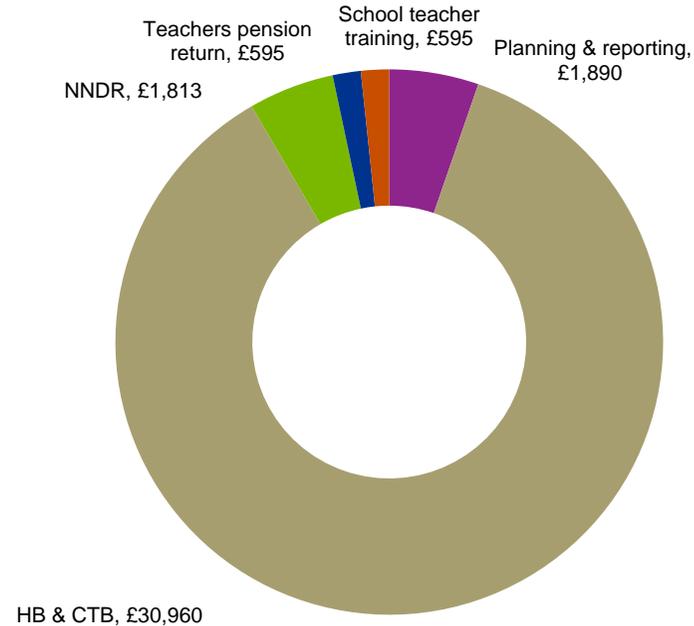
	Comments overleaf	Qualified certificate	Significant adjustment	Minor adjustment	Unqualified certificate
Housing Benefit and Council Tax Benefit scheme	1				
National non-domestic rates return					
Teachers pensions return					
School centred initial teachers training					
		1	0	1	3

This table summarises the key issues behind each of the adjustments or qualifications that were identified on the previous page.

Ref	Summary observations	Amendment
1	<p>Housing Benefit and Council Tax Benefit</p> <ul style="list-style-type: none"> ■ Amendments were made to the backdate cells due to the incorrect use of the week 1 indicators. ■ The qualification letter referred to the actual errors identified and stated that these will be corrected in Northgate in 2012/13 ■ The single residency discount errors identified in the 2010/11 qualification letter have been corrected in Northgate in 2011/12, no issues were identified in 2011/12 testing. 	<p>£2,000 with no impact on subsidy claimed</p>

Our overall fee for the certification of grants and returns has been contained within the original estimate.

Breakdown of certification fees 2010/11



Breakdown of fee by grant/return

	2011/12 (£)	2010/11 (£)
Planning and Reporting	1,890	2,570
Housing benefit and council tax benefit scheme	30,960	32,958
National non-domestic rates return	1,813	3,575
Teachers' pensions return	595	425
School centred initial teacher training	595	1,020
Other claims not audited in 2011/12	0	11,527
Total fee	35,853	52,075

Our initial estimated fees for certifying 2011/12 grants and returns was £40,000. The actual fee charged was lower than that estimate.



Certification of grants and returns 2011/12

Recommendations

We have not made any recommendations for improvement in 2011/12.



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