External Audit Report 2016/17

London Borough of Lambeth

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September 2017

Content

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This report is addressed to the London Borough of Lambeth (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. PSAA issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on PSAA's website (www.psaa.co.uk).

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

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

Important notice

This report is presented in accordance with our PSAA engagement. Circulation of this report is restricted. The content of this report is based solely on the procedures necessary for our audit. This report is addressed to the London Borough of Lambeth (the Authority) and has been prepared for your use only. We accept no responsibility towards any member of staff acting on their own, or to any third parties. The National Audit Office (NAO) has issued a document entitled Code of Audit Practice (the Code). This summarises where the responsibilities of auditors begin and end and what is expected from the Authority. External auditors do not act as a substitute for the Authority'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.

Basis of preparation: We have prepared this External Audit Report (Report) in accordance with our responsibilities under the National Audit Office Code of Audit Practice (the Code) and the terms of our Public Sector Audit Appointments Ltd (PSAA) engagement.

Purpose of this report: This Report is made to the Authority's Corporate Committee in order to communicate matters as required by International Audit Standards (ISAs) (UK and Ireland) and other matters coming to our attention during our audit work that we consider might be of interest and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone (beyond that which we may have as auditors) for this Report or for the opinions we have formed in respect of this Report.

Limitations on work performed: This Report is separate from our audit opinion and does not provide an additional opinion on the Authority's financial statements nor does it add to or extend or alter our duties and responsibilities as auditors. We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report. The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

Status of our audit: Our audit is complete and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status of our audit at the Corporate Committee meeting. The following work is ongoing:

- WGA,
- Final checks on the Narrative Statement and the Financial Statements
- Receipt of management representations;
- Clearance of the partner and manager review points; and
- Value for money conclusion.

Summary

Financial statements audit – see section two for further details

Subject to all outstanding queries and procedures being satisfactorily resolved we intend to issue an unqualified audit opinion on the Authority's financial statements for the deadline of 30 September 2017, following the Corporate Committee adopting them and receipt of the management representations letter.

We also anticipate issuing an unqualified audit opinion in relation to the Pension Fund's financial statements for the deadline of 30 September 2017. The Pension Fund financial statements have been approved by Pensions Committee on 14 September 2017.

We have completed our audit of the financial statements. We have read the Narrative Report and reviewed the Annual Governance Statement (AGS). Our key findings are:

- There is one unadjusted audit difference explained in appendix two.
- We agreed presentational changes to the accounts with Finance, mainly related to compliance with the CIPFA / LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2016/17.
- In additional to our routine requests we are asking for management representations over the judgements reached in recording disclosure on potential claims which could results from the potential redress scheme for cases of historic child abuse and their decision by Officers of the Authority to treat a commercially sensitive litigation provision as contingent.
- We will report that your AGS complies with delivering Good Governance guidance issued by CIPFA / SOLACE in April 2016.
- We reviewed the narrative report and have no matters to raise with you.
- We received commentary from the public, some of which are expressed as questions or objections on the following issues: head teacher's high pay; tables 35 (housing stock) and 36 (HRA assets); possible unlawful expenditure; possible misclassifications of expenditure; assets held for sale; special responsibility allowances; HRA repairs and maintenance expenditure; contract management over regeneration; members' allowances; the cost of the Your New Town Hall project; duplicate invoices; disclosure of school salaries and a Public Building Safety objection in relation to PFI contracts.

We are now in the completion stage of the audit and anticipate being in a position to sign the financial statements and VFM conclusion on 29 September. We also intend to issue our 2016/17 Annual Audit Letter following that. The audit cannot be formally concluded and an audit certificate issued as we are considering elector queries relating to 2015/16 and 2016/17. Until we have completed our consideration of these, we are unable to certify that we have completed the audit of the accounts in accordance with the requirements of the Local Audit and Accountability Act 2014.

Value for money – see section three for further details

We have worked with officers throughout the year to discuss these VFM risks and our detailed findings are reported in section three of this report.
For 2016/17, we have concluded that the Authority has not made proper arrangements to secure economy, efficiency and effectiveness in its use of resources particularly in relation to Children's Services, although we note progress has been made in this regard and within the internal control environment.

Summary

Other matters

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

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

In auditing the accounts of the Authority, auditors must consider whether, in the public interest, they should make a report on any matters coming to their notice in the course of the audit, in order for it to be considered by Those Charged with Governance or brought to the attention of the public; and whether the public interest requires any such matter to be made the subject of an immediate report rather than at completion of the audit. There are no matters that we with to report.

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority’s 2016/17 financial statements.

We identified one prior year recommendation that require further action by Management. We have made seven new recommendations as a result of our 2016/17 work. They key recommendations relate to general IT controls, the preparation of the higher earners disclosure and the preparation of the impairment of debtors note. All recommendations are shown in appendix one.

The status of our grants and claim work is that the Housing Benefit Grant Claim is scheduled for October 2017 in time for the 30 November 2017 sign off. We undertake the audit of the Teachers’ Pension Return and the Pooling of Housing Capital Receipts Grant that does not fall under the PSAA arrangements. These have not yet been started and the deadlines are 30 November and 31 October respectively. The fees for this work is explained in section two.

Financial statements audit

We audit your financial statements by undertaking the following:

Work Performed	Accounts production stage: Before	During	After
1. Business understanding: review your operations	✓	✓	–
2. Controls: assess the control framework	✓	–	–
3. Prepared by Client Request (PBC): issue our prepared by client request	✓	–	–
4. Accounting standards: agree the impact of any new accounting standards	✓	✓	–
5. Accounts production: review the accounts production process	✓	✓	✓
6. Testing: test and confirm material or significant balances and disclosures	–	✓	✓
7. Representations and opinions: seek and provide representations before issuing our opinions	✓	✓	✓

We have completed the first six stages and report our key findings below:

1. Business understanding	In our 2016/17 audit plan we assessed your operations to identify significant issues that might have a financial statements consequence. We confirmed this risk assessment as part of our audit work. We provide an update on each of the risks identified later in this section.
2. Assessment of the control environment	We assessed the effectiveness of your key financial system controls that prevent and detect material fraud and error. We found that the financial controls on which we seek to place reliance are operating effectively. We have made seven recommendations which relate to High Earners Remuneration, Northgate application controls, the accounts payable / general ledger reconciliation, the sundry debtors provision and the fixed asset register / Northgate system reconciliation. We believe that these recommendations (see appendix one) will strengthen your control environment. We reviewed work undertaken by your internal auditors, in accordance with ISA 610 and used the findings to inform our work. We have chosen not to place reliance on their work due to the approach we adopted for the financial statements audit. For the pension fund, we relied on service organisation auditors to assess the investment fund managers' control environments and that of the custodian. We received ISAE 3402 reports from those auditors in order to gain comfort over the control environment at those organisations.
3. Prepared by client request (PBC)	We produced the PBC to summarise the working papers and evidence we ask you to collate as part of the preparation of the financial statements. We discussed and tailored our request with the Group Manager and Assistant Director of Finance and this was issued as a final document to the finance team. We are pleased to report that this has resulted in good-quality working papers with clear audit trails and documentation on the Lambeth SharePoint.

Financial statements audit

4. Accounting standards	We work with you to understand changes to accounting standards and other technical issues. For 2016/17 these changes related to: • Updates to the presentation of the Comprehensive Income and Expenditure Statement and the Movements in Reserves Statement and the introduction of the new Expenditure and Funding Analysis: this resulted in changes to the year on year to the presentation of the financial statements. We have audited the presentation and content of the current and prior year restated disclosures, and are satisfied they are materially accurate; • Amended guidance on the Annual Governance Statement. We reviewed the Annual Governance Statement against the updated requirements in the CIPFA code and are satisfied the content is compliant; and • Changes in the format of the Pension Fund accounts: there were updates to the presentation of management fees, which have been audited, and we are satisfied the content is compliant.
5. Accounts Production	Draft accounts were published online on 30 June. The accounting policies, accounting estimates and financial statement disclosures are in line with the requirements of the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17. We will debrief with Finance to share views on the final accounts audit which hopefully will lead to further efficiencies in the 2017/18 audit process. We do however note there is a considerable undertaking required in order to prepare for the early close required for 2017/18. We have raised a recommendation (see appendix one) to this effect and we will work with the finance team to ensure a suitable coordinated approach is in place. We thank Finance for their cooperation throughout the visit which allowed the audit to progress and complete within the allocated timeframe.
6. Testing	We have summarised the findings from our testing of significant risks and areas of judgement in the financial statements on the following pages. We have identified presentational changes to the accounts along with audit adjustments to HRA expenditure, which we have presented in appendix two.
7. Representations	You are required to provide us with representations on specific matters such as your going concern assertion and whether the transactions in the accounts are legal and unaffected by fraud. We provided a draft of this representation letter to the Director of Finance on 14 September 2017. We draw attention to the requirement in our representation letter for you to confirm to us that you have disclosed all relevant related parties to us. We are asking you to provide specific representations on the judgements you have reached about the potential for liabilities to arise from the potential commencement of a redress scheme for cases of historic child abuse as well as about the judgements reached about the potential for liabilities to arise as a result of other legal proceedings with commercial counter parties.

Financial statements audit

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

— Significant difficulties encountered during the audit;

— Significant matters arising from the audit that were discussed, or subject to correspondence with Management;

— Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and

— Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, opening balances, public interest reporting, questions/objections, etc.).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Authority’s 2016/17 financial statements. To ensure that we provide a comprehensive summary of our work, we have over the next pages set out:

- The results of the procedures we performed over five key areas which were identified as significant risks within our audit plan and which will form a part of our audit opinion;
- The results of our procedures to review the required risks of the fraudulent risk of revenue recognition and management override of control; and
- Our view of the level of prudence applied to key balances in the financial statements.

Financial statements audit

Significant audit risk	Account balances affected	Summary of findings
Land and buildings	Property, plant and equipment: £3,703,254k (PY £3,591,711); gain on revaluation of non-current assets: £27,837k (£322,825k)	We assessed the expertise of the valuers, considering their professional experience, qualifications and independence. We did not identify any issues arising from this review and determined that the valuers are appropriate to undertake the valuation. We reconciled the fixed asset register to the valuation and to the financial statements, to ensure the completeness of the valuation undertaken by the valuers. We are satisfied the valuer, Wilks Head & Eve, was provided a complete list in line with the Authority's revaluation methodology and that the complete valuation was reflected in the financial statements. Impairments amounted to £10,756k (PY £5,128k), driven predominantly by a number of assets being taken out of use, and revaluations were £27,837k (PY £322,825k). The comparatively small revaluation uplift compared to prior year in revaluation was due to the fact that a significantly smaller portion of assets were revalued this year in line with the requirements of the Code. We also ensured we were satisfied that the valuation was in line with the Authority's accounting policy and that appropriate coverage was provided over the Authority's estate. This testing did not identify any issues. We assessed the controls in place to ensure the GL and the financial statements were complete and accurate, and that they are in line with the asset register. We considered the basis upon which impairments to land and buildings were calculated and considered the underlying assumptions supporting these assessments. This testing did not identify any issues. We reviewed the revaluation basis and considered its appropriateness, drawing on national benchmarks. We also engaged our property team experts to undertake an assessment of the revaluation. This testing did not identify any issues. We reviewed the floor plans and GIA information that was sent to the valuers to ensure they were accurate. This testing did not identify any issues. We have sighted an agreement relating to the northern line extension, dated 12 November, signed by Transport for London, London Underground Limited and the Mayor and Burgesses of the London Borough of Lambeth which authorised the demolition of the lodge. We have reviewed the documentation in relation to the demolition of, and subsequent sale of, the Kennington Park Keepers Lodge. We have found the sale to be governed by contracts and the asset correctly classified in the accounts.

Financial statements audit

Significant audit risk	Account balances affected	Summary of findings
Significant changes in the pension liability due to LGPS Triennial Valuation	Pension liability: £631,155k (PY £599,147k)	We assessed the expertise of the actuaries, considering their professional experience, qualifications and independence. We did not identify any issues from this review. We reviewed the source data, such as lists of active, deferred and frozen members, provided by the Authority to the actuaries to confirm it was complete and accurate. This review did not identify any issues and we are satisfied that the instructions provided to the actuaries were appropriate. We assessed the changes in the contribution rate owing to the LGPS triennial revaluation. We ensured that the underlying data that feeds into the LGPS Triennial Revaluation was complete and accurate through sample testing for completeness and accuracy of the underlying data.
Abuse redress scheme	Contingent liability disclosure and reserves drawdown £399k (PY £0)	The potential redress scheme had not commenced as at the time of audit. We have tested the contingent liability disclosure in the accounts and assessed it as reasonable. We are satisfied this is correctly recorded as a contingent liability in the financial statements. A corrected audit adjustment was noted relating to the Authority disclosing “management judgement”. We have audited the amended disclosure and we are satisfied this has been correctly disclosed. There were drawdowns from reserves relating to the work to put in place the potential redress scheme and we tested this back to invoices and for appropriate authorisation.
Restatement of CIES, EFA and MIRS	Income £905,397k (PY £910,078k) and expenditure £1,203,340k (PY £1,151,547k)	We assessed how the Authority actioned the revised disclosure requirements for the CIES, MiRS and the new EFA statement as required by the Code; and We checked the restated numbers and associated disclosures for accuracy, correct presentation and compliance with applicable Accounting Standards and Code guidance. We performed audit testing on the restated figures. This involved ensuring that the presentation of the notes was in line with the Authority’s internal reporting and monitoring structure. We agreed prior year figures back to the audited 2015/16 accounts and gained an understanding of the adjustments that were posted in order to restate the prior year figures. We ensured that the presentation of the new format notes was in line with the presentational requirements outlined in the CIPFA 2016/17 Code of Practice. We sample tested cost apportionment as part of our work over the restatement and did not find any issues. We did not identify any issues with the restatement.

Financial statements audit

Other areas of audit focus

We identified 11 other areas of audit focus. These are not considered to be significant risks as they are less likely to give rise to a material error. Nonetheless these are areas of importance where we carry out audit procedures to ensure that there is no material misstatement.

Other areas of audit focus	Account balances affected	Summary of findings
Cash	Cash, £27,980k (PY £40,986k)	We agreed bank balances to external confirmations requested from the banks. We reviewed controls over bank reconciliations and we reviewed the classification of cash equivalents. We further performed cut off testing to ensure that cash is recorded in the correct period. We found no issues with this at the Authority or the Pension Fund.
Payroll	£190,388k (PY £202,707k)	We reviewed the approach and tested the systems and specific transactions to ensure completeness, existence and accuracy of the payroll balance. We formed our own expectation of payroll costs for the year, disaggregated across different grades of employees and tested national insurance payments and pension costs substantively. We substantively tested payroll records to ensure that amounts paid out are materially correct, including total staff costs and the appropriateness and legality of members allowances. We performed testing over the headteachers' pay. This note was initially omitted from the draft financial statements due to an ongoing legal case. We have confirmed the disclosure accurately reflects the salaries received. We audited special responsibility allowances. We compared this with the regulations and additional guidance set out by the independent remuneration panel and found that Lambeth's special responsibility allowances were of a nature and quantum in line with the regulations and guidance as expressed in the independent remuneration panel's recommendations.
Non-pay expenditure	£953,200k (PY £834,061)	We performed controls and sample testing on non pay expenditure to give us assurance that the amounts being paid out are reasonable and have followed the Authority's procedures. We tested payments made to Transport Trading Ltd and noted that all had supporting invoices receipted against approved purchase orders. We further found that the supporting documentation for these invoices was detailed and appropriate for transactions of this size.
Minimum Revenue Provision	£200k (PY £292k)	We documented and agreed the calculation provided to supporting third-party documentation, and ensured this is calculated in line with policy and DCLG guidance. We further sought technical accounting advice on this from our specialists.
Housing benefit	Housing and Council Tax (Benefit and Subsidy) £252,329k (PY £260,071)	We documented the process, tested the year end system reconciliation and tested system parameters which produce the Housing Benefit Subsidy claim, to ensure amounts paid out are accurate and correctly accounted for. We did not find any issues.

Financial statements audit

Other areas of audit focus	Account balances affected	Summary of findings
HRA Income and Repairs and Maintenance expenditure	HRA income £189,690k (PY £190,270k); HRA repairs and maintenance expenditure £27,589k (PY £28,253k)	We documented the process to ensure that housing stock records are accurate and rent payments reflected in the GL, and performed substantive analytical procedures over dwelling rents and service charge income. We substantively tested maintenance expenditure. We documented the process to ensure repairs and maintenance are accurate, performed controls testing, and sample tested the balance. There are no issues to note. We investigated two differences. One was on the data supplied to an objector to support the number of houses in the annual report, and found the difference to be 16 travellers' berths, which cannot be classed as housing stock, and 181 hostels. The second was on discrepancies between Table 35 "Housing Stock" and Table 36 "HRA Assets" regarding the number of council dwellings. The data underpinning Table 36 included 23,987 assets and 14 blank assets, totalling 24,001 assets per the FAR. We investigated why there were not matching entries for each of the 23,958 assets in the HRA assets table. We noted a reconciliation had been performed between the underlying data for these notes and the difference were not found to be material to the accounts. The differences were due to: 181 hostel dwellings which are not classed as housing stock on the fixed asset register; 61 rent to mortgage properties, present on the fixed asset register but not on the housing system; 2 properties which were found to be land or to be apportioned in 2017/18. This totals 23,757 properties as actual operational dwelling stock on the fixed asset register. The following should not have been on the fixed asset register: 3 properties (£242,500 in value) which had been sold and not removed from the fixed asset register; 7 properties (£872,250) which should have been derecognised from the accounts as they were PFI-built houses; 4 of the properties under investigation (£361,000) will be derecognised from the fixed asset register. The total of properties to be derecognised from the fixed asset register amount to £1,476k. This has been raised as an audit difference in appendix 3. There were also 10 further properties (£773,000) have been bought back by the Council and used as temporary accommodation appear on the fixed asset register but not on the housing system. These will remain as reconciling items. The following were also not on the fixed asset register or on the housing system: 5 properties which were void and will be added to the fixed asset register at a value to be decided; A number of properties (£3,271k) into which the Council are investigating the reasons why they are on the fixed asset register but not on the housing system, for example, they have been converted or there has been a change in use. A recommendation has been raised in appendix 1.

Financial statements audit

Other areas of audit focus	Account balances affected	Summary of findings
Housing benefit	Housing and Council Tax (Benefit and Subsidy) £252,329k (PY £260,071)	The Authority awards housing benefits to claimants in the borough each year. We documented the process, substantively tested a sample of cases and tested system parameters which produce the Housing Benefit Subsidy claim, to ensure amounts paid out are accurate and correctly accounted for.
Council Tax and Business Rates income	Council tax income £136,150k (PY £127,165k); NNDR income £127,857k (PY £125,720k)	We documented the process and substantively tested both business rates and council tax, and confirmed rates and calculations against external documentation. We found no issues.
Benefits payable (Pension Fund only)	£55,794k (PY £50,765k)	We substantively tested a sample of deaths and a sample of commutation benefits to Oracle and to supporting documentation. We also compared this balance to 2015/16; adjusting our assumptions for movements within the year. We found no issues.
Contributions receivable (Pension Fund only)	£56,512k (PY £54,598k)	We tested a sample of members' contribution rates to Oracle and compared the balance to 2015/16, adjusting our assumptions for movements within the year. We found no issues.
Investments (Pension Fund only)	Investment income £31,935k (PY £32,434k); investments £1,341,138k (PY £144,728k)	The Pension Fund held over £1.1 billion of investments at 31 March 2017. Quarterly valuations are provided by fund managers, which are compiled by Mercer. They assess the Fund and the individual managers against the benchmarks set. The quantum and estimated nature of this balance makes it an area of audit focus. We obtained confirmations from the fund managers, custodians, and the London collective investment vehicle, reconciliations between the two, and we reviewed ISAE3402 compliance reports on each fund manager. We also compared the assumptions made by your actuaries to benchmarks collated by KPMG actuaries, and to the assumptions used for 2015/16 for consistency. We found no issues.

Financial statements audit

Risks that ISAs require us to assess in all cases	Why	Our findings from the audit
Fraud risk from revenue recognition	Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. We do not consider this to be a significant risk for the majority of the Authority's income as there are limited incentives and opportunities to manipulate the way income is recognised. In our External Audit Plan 2016/17 we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.	We rebutted this risk as communicated to you in our Audit Plan and therefore there are no matters arising from this work that we need to bring to your attention.
Fraud risk from management override of controls	Management is typically in a powerful position to perpetrate fraud owing to its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Our audit methodology incorporates the risk of management override as a default significant risk.	In line with our methodology, we carried out controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual. We have not identified any specific additional risks of management override relating to this audit.

Financial statements audit

Judgements in your financial statements

We consider the level of prudence in key judgements in your financial statements. We summarise our view below using the following scale:

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
Provisions (excluding NDR)	4	3	£8,952k (PY:£16,858k)	Lambeth have reduced the provision for the Insurance Fund as it was previously topped up every year without being utilised. We consider this balance to lean slightly towards the optimistic end of the spectrum as it is no longer being topped up to the level advised by the actuaries. We note a valuation is expected in 2017/18 along with a budgeted top up to the fund should it be required.
NDR provisions	3	3	£6,513k (PY:£8,355k)	From 2013/14, local authority funding arrangements meant that the Authority is responsible for a proportion of successful rateable value appeals. The Authority has provided for a fixed percentage of outstanding appeals in accounting for the potential liability, based on historical appeals success rates. We consider this to be a balanced judgement as it is based on historical data and the Authority makes its total appeal based on categories of properties' success ratings at appeal.

Financial statements audit

Assessment of subjective areas				
Asset / liability class	**Current year**	**Prior year**	**Balance (£m)**	**KPMG comment**
PPE: HRA assets	3	3	£2,227m (PY: £2,169m)	The Authority continues its use of the beacon methodology in line with the DCLG's *Stock Valuation for Resource Accounting* published in November 2016. The Authority has utilised Wilks, Head & Eve to provide valuation estimates. We reviewed instructions provided and deem that the valuation exercise is in line with the instructions. The resulting increase of 2.6% is in line with regional indices provided by Gerald Eve, the valuation firm engaged by the NAO to provide supporting valuation information, as such we consider this to represent a balance area of judgement.
PPE: asset lives	3	3	£3,703m (PY: £3,591m)	We deem the Authority to have taken a balanced approach to estimating asset lives, based on our work over the full revaluation undertaken last year and the desktop revaluation undertaken this year. Lambeth have implemented the response to our prior year audit recommendation to remove assets with a zero year asset life.
Debtors provisioning	3	4	£32.2m (PY:£31.8m)	The provision for sundry debtors has decreased by £1.6m based on historic collectability, which represents a balanced judgement.
Pension liability	3	3	£631m (PY: £599m)	We assessed the pension liability calculation and agreed it back to the IAS 19 valuation provided. We also reviewed the capability of the actuaries. Our review of the actuarial assumptions considers this to be a reasonable balance.

Section Two

Financial statements audit

Narrative report of the Authority

We have reviewed the Authority’s narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Pension Fund audit

The audit of the Pension Fund and the Pension Fund Annual Report was completed alongside the main audit. There are no specific matters to bring to your attention relating to this.

Pension Fund annual report

We reviewed the consistency of the Fund’s financial statements in the Fund’s Annual Report and the financial statements included in Lambeth’s financial statements. We confirm that the Fund’s financial statements are consistent with the pension fund financial statements included in the accounts of the London Borough of Lambeth. We read the information in the Fund’s Annual Report to identify material inconsistencies with the Fund’s financial statements. We can confirm it is not inconsistent with the financial information contained in the audited financial statements. As such we anticipate issuing an unqualified consistency opinion on the pension fund financial statements.

Queries from local electors

We received queries on the following issues: headteachers’ high pay; tables 35 (housing stock) and 36 (HRA assets; possible unlawful expenditure; possible misclassifications of expenditure; assets held for sale; HRA repairs and maintenance expenditure; contract management over regeneration; members’ allowances; the cost of the Your New Town Hall project; duplicate invoices; disclosure of school salaries and a health and safety issue~~s~~ relating to PFI contracts. There are three objections from 2015/16, which we are still investigating, on contract management.

We are satisfied we have performed sufficient procedures over the comments and potential objections relating to the financial statement captions for this not to prevent us to sign our opinion. This includes the comments over headteachers’ high pay, tables 35 (housing stock) and 36 (HRA assets); possible misclassifications of expenditure; assets held for sale; special responsibility allowances; HRA repairs and maintenance expenditure and the disclosure of school salaries.

We have considered whether any of these objections prevent us from issuing our financial statements audit opinion or our value for money conclusion and do not believe that, as presented or raised, they prevent us finalising those two aspects of our work. We will need to complete further work to decide the objections before we can issue our audit certificate.

Audit Certificate

In order for us to issue an audit certificate, we are required to have completed all our responsibilities relating to the financial year. We are not in a position to issue our audit certificate with the audit opinion as we have not completed our work over the objections received from local electors and the WGA.

Financial statements audit

Other grants and claims work

We undertake additional grant claim certification work which has not yet started:

- Housing benefits grant claim, expected to start in October 2017
- Teachers' Pension Return, expected to start in October 2017
- Pooling of Housing Capital Receipts Grant, expected to start in October 2017
- Housing benefits grant claim certification: October 2017

Audit fees

Our fee for the audit was £207,841 (2015/16: £207,841) for the 2016/17 Code of Practice audit; £21,000 (2015/16 £21,000) for the Pension Fund; and £31,688 (2015/16: £35,376) for the certification of grant claims and returns.). This fee was in line with that highlighted in our audit plan approved by the Corporate Committee on June 2017.

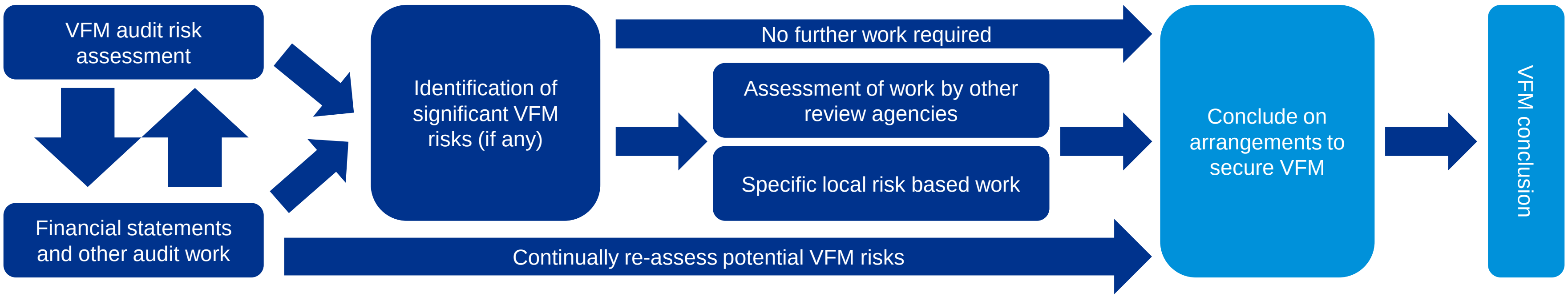
The estimated fees for our audit of the Teachers' Pension Return and the Pooling of Housing Capital Receipts Grant is £10,000.

Objections fee

There are audit fees accruing relating to 2015/16 and 2016/17 objections, but these are ongoing and are not yet authorised by the PSAA. The estimated fee to date is £30,000.

Value for money

For 2016/17 our value for money (VFM) work follows the NAO's guidance. It is risk based and targets audit effort on the areas of greatest audit risk. Our methodology is summarised below. We identified two significant VFM risks which are reported below, in addition to one area of audit focus arising from our VFM work overleaf. We are satisfied that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2017, based upon the criteria of informed decision making, sustainable resource deployment and working with partners and third parties in all areas except for children's services and controls over contract management.



Below we set out the detailed findings of our significant risk based VFM work. This work was completed to address the residual risks remaining after our assessment of the higher level controls in place to address the VFM risks identified in our planning and financial statements audit work.

Significant VFM risk	Why this risk is significant	Our audit response and findings
Securing economy, efficiency and effectiveness in Children's Services	Last year our VFM opinion was qualified due to 'inadequate' ratings given by inspection reports on children's safeguarding.	We examined relevant reports by Ofsted, HMI, the CQC and internal audit, in order to establish whether action plans have been designed and implemented. We also reviewed minutes from meeting at which the action plans have been discussed and met with the Director of Children's Services. We have found that although progress has been made, the Authority has been unable to evidence sufficient improvement in Children's Services. Ofsted reports as well as Internal Audit reports note that whilst progress has been made, the standards remain too variable as a number of failures were noted on visits. We therefore acknowledge that progress continues to be made to address these adverse findings. However, all recommendations and weaknesses have not yet been fully addressed and therefore we will be continuing to monitor progress over 2017/18.

Value for money

Significant VFM risk	Why this risk is significant	Our audit response and findings
Treatment of historic claims – abuse redress scheme	Lambeth is in the process of consulting on the approach to historic child abuse claims at its children's homes, and whether to compensate those who can prove that they were at the homes between two dates. The estimated value of the scheme is between £30-60 million.	The process has not yet begun and therefore we have audited the set up costs and the authorisation of these. We did not identify any issues as the amount in question is below our lower materiality threshold.
Financial stability and internal control	Given the continued straitened climate for local authorities, financial sustainability remains an issue within the sector. Although Lambeth is on track to deliver its 2020 plan and is raising council tax by 3.99%. In past years the value for money conclusion has been qualified to reflect the continued work to strengthen the internal control environment, as reflected in the Head of Internal Audit Opinion.	To assess if the authority has robust systems and processes in place to effectively manage financial risks and opportunities and to secure a stable financial position, we reviewed the Financial Management Strategy and budget reports in place to deliver its 2020 plan, in addition to relevant Council minutes. We noted that while Lambeth is on track to deliver its medium term plan, it is having to raise council tax by 3.99%. We conclude that the decision making is robust and informed, and supported by financial reporting processes. We are not amending our opinion in this respect. We also considered how the Authority has addressed the previously noted weaknesses in internal controls and non-compliance with policies. Although the Head of Internal Audit Opinion this year reflected an overall improved picture, we have noted improvements are still required with respect to contract management and other areas where financial control plans have been targeted. As a result of this on-going programme of work we continue to qualify our opinion to reflect these issues.

Appendix 1

Recommendations raised and followed up

Recommendations raised as a result of our work in the current year are as follows:

Priority rating for recommendations					
❶	Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	❷	Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸	Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

#	Risk	Recommendation	Management Response / Officer / Due Date
Financial statements			
1	❸	**Higher earners' remuneration disclosure** There were errors in the higher earners' remuneration disclosure due to amalgamation of employees with the same name and transcription errors from schools' returns. We recommend that Finance review the returns from schools, and ensure council employees' salaries are banded on unique ID, not employee name.	**Agreed** This will be implemented for 2017/18 closedown
2	❸	**Provision for sundry debtors** We identified that debtors older than six years are not written off or provided for, and the likelihood of recoverability improves by 13% between year five and year six. There are also unreconciled items for £2m for which no provision has been made. We recommend that the Authority should review its methodology for its provision for sundry debtors.	**Agreed** The external auditors have confirmed that the overall provision for Sundry Debtors represents a balanced view. Percentages used in calculating this provision will be reviewed for 2017/18 closedown
3	❸	**Approval of new users for Northgate** As part of our controls testing over general IT systems, we found that 66% (10 out of 15) new users reviewed for Northgate did not have supporting evidence showing that they had been approved for access to the system and that this is currently evidenced by email trails. This means that inappropriate users could be given access. We recommend that a starter form, requiring review, is introduced in order to strengthen this control.	**Agreed** Processes for approving new users and the removal of leavers for Northgate will be reviewed to ensure controls and strengthened in this regard.

Recommendations raised and followed up (cont…)

#	Risk	Recommendation	Management Response / Officer / Due Date
4	3	**Removal of leavers from Northgate** As part of our controls testing over general IT systems, we ensured that leavers were removed from Northgate after not having changed their password for 150 days. We found 2 out of the entire population of leavers whose passwords had not been changed for more than 150 days. One was a member of the system admin group and therefore was not subject to the 150-day rule and the other was subsequently removed but no reason was provided as to why this user had not been removed initially. We recommend that regular checks are carried out and documented, to ensure that leavers are removed from Northgate on a timely basis.	**Agreed** Processes for approving new users and the removal of leavers for Northgate will be reviewed to ensure controls are strengthened in this regard.
5	3	**AP to GL reconciliation** We found that AP to GL reconciliations are being carried out but are not signed off or dated as prepared and reviewed. Errors may therefore go unidentified. We recommend that the AP to GL reconciliations are signed and dated as prepared and reviewed.	**Agreed** AP to GL reconciliations will be signed off in future.
6	3	**Faster close preparations** In preparation for the mandatory faster close timetable for 2017/18 onwards, Finance could benefit from ensuring that the accounts timetable has sufficient time set aside for preparing and quality assuring its draft accounts and supporting working papers. This should help to ensure that the tighter deadlines are met next year. A detailed 2016/17 debrief should take place internally to identify lessons leant and potential efficiencies for next year's process, which we would be happy to take part in.	**Agreed** Debrief and planning session have been arranged across Finance in October/November and a firm plan is being developed to meet the earlier closedown deadlines.
7	3	**Northgate / FAR reconciliation** Following a reconciliation of the Fixed Asset Register and Northgate, we noted a number of properties (£3,271k) on the fixed asset register but not on the housing system. We recommend the Council reconcile this variance and understand why this discrepancy exists.	**Agreed** Management will investigate this variance before KPMGs 17/18 interim audit.

Appendix 1

Recommendations raised and followed up

We have followed up the recommendations from the prior year's audit, in summary:

Total number of recommendations	Number of recommendations implemented	Number outstanding (repeated below):
7	6	1

#	Risk	Recommendation	Management Response / Officer / Due Date	Status at September 2017
Financial statements				
1	1	**Cash reconciliations** We identified that while reconciliations were being performed, the unreconciled differences had not been cleared or followed up. This resulted in the identification of a £10.7 million unreconciled difference. **Recommendation** Ensure that all bank accounts are reconciled, the unreconciled difference is cleared on a timely basis and there is oversight and follow up of any issues.	We will ensure that bank accounts are reconciled, the unreconciled difference is cleared on a timely basis, and there is oversight and follow up of any issues.	**Implemented** Bank reconciliations have been carried out retrospectively back to 2014. They are being prepared and reviewed on a monthly basis.
2	1	**AIM System** The AIM system automatically posts cash payments or receipts (from the cash book) to the general ledger, and operates alongside the cash management system (Oracle reconciliation tool). We noted a failure of this automated process in the year which has resulted in a £10.7m unreconciled balance. **Recommendation** We recommend management investigate the root cause of this system failure and take necessary steps to resolve as a matter of urgency.	We have commissioned a report from an AIM specialist to assess whether this is a system or a process issue. We have cleared the control account and are reconciling the general bank account on a monthly basis.	**Implemented** Bank reconciliations have been carried out retrospectively back to 2014. They are being prepared and reviewed on a monthly basis. The control account has been cleared as a result of this work.

Appendix 1

Recommendations raised and followed up

#	Risk	Recommendation	Management Response	Status at September 2017
Financial statements				
3	3	**High level review of changes** We identified some areas where changes were made or developments were taking place and these updates were not included in the first draft of the accounts. This relates to updates in capital commitments, sale of fixed assets, leases and short and long term liabilities,. **Recommendation** We recommend that high risk areas where changes or updates are taking place are highlighted and re-reviewed prior to finalising the accounts.	We will ensure that all working papers are reviewed prior to finalising the accounts.	**Implemented** This was not an issue in the 2016/17 audit.
4	3	**Exit packages** There was an error in the exit packages note as a result of the duplication of information from payroll and finance. This resulted in an overstatement within the note. **Recommendation** We recommend that the final figures are reviewed by both Finance as well as Payroll to ensure any errors are identified.	We will ensure that the exit packages note is reviewed by both Finance and Payroll.	**Implemented** There were no issues with the Exit Packages note this year.
5	3	**Floor Plans** We were unable to easily obtain floor measurements from the asset management teams. **Recommendation** We recommend that these measurements are recorded and maintained by a central asset management team to ensure there is a reliable record for valuations.	We will ensure that the floor plans are easily obtainable and put the auditors in touch with the relevant staff.	**Implemented** We obtained floor plans direct from the valuers.

Recommendations raised and followed up

#	Risk	Recommendation	Management Response	Status at September 2017
Financial statements				
6	3	**Regular review of fixed asset register** We identified through our testing 68 assets which had not been revalued since 2008. Of which that one asset had not been removed from the Register despite being at nil value and no longer owned by the Council. In addition, an adjustment of £4.6m was made for council properties which should have been removed due to transfer of economic benefits agreed in 2012,. **Recommendation** We recommend the Fixed Asset Register is reviewed regularly to ensure transfers and disposals are correctly recorded and to ensure all assets are revalued which should be.	We have completed this review work. We will move the Fixed Asset Register to an automated system in 2017/18.	**Implemented** Review work has been completed and there are plans to move the Fixed Asset Register to a specific system in 2017/18.
7	3	**Regular review of aged creditors** We reviewed the aged creditors, and while there were no issues identified, we noted that an aged creditors report is not regularly produced or reviewed **Recommendation** We recommend that an aged creditors report is regularly produced and reviewed to ensure that all aged creditors are monitored and cleared in a timely manner.	We have produced quarterly aged creditor reports.	**Outstanding** There was no aged creditors report available for review.

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects:

- Material errors by **value** are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements;
- Errors which are material by **nature** may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff; and
- Errors that are material by **context** are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2016/17, presented to you on 30 March 2017.

Materiality for the Authority's accounts was set at £15 million which equates to around 1.32% of gross expenditure.

Materiality for the Pension Fund was set at £20.5 million which equates to around 1.8% of gross assets.

We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to Corporate Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Corporate Committee any misstatements of lesser amounts to the extent that these are identified by our audit work. Under *ISA 260*, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. *ISA 260* defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. *ISA 450* requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.75 million for the Authority and less than £1 million for the Pension Fund.

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

Audit differences

Unadjusted audit differences

Under UK auditing standards (ISA (UK&I) 260) we are required to provide the Corporate Committee with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements. In line with ISA (UK&I) 450 we request that you correct uncorrected misstatements. However, they will have no effect on the opinion in our auditor's report, individually or in aggregate. As communicated previously with the Corporate Committee, details of all adjustments greater than £750K are shown below.

Unadjusted audit differences (£'000)						
#	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Comments
1	Dr P&L £1,476k		Cr PPE £1,476k			These are assets that should have been derecognized from the fixed asset register.
	Dr £1,476k		**Cr £1,476k**			**Total impact of uncorrected audit differences**

Adjusted audit differences

To assist the Corporate Committee in fulfilling its governance responsibilities we present in the tables below a summary of adjusted audit differences (including disclosures) identified during the course of our audit. The adjustments below have been included in the financial statements.

Authority adjusted audit differences (£'000)						
#	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Comments
1	Dr Grant revenue £1,560				Cr reserves £1,560	£1.56 m was recognised as a carry forward to 2017/18 advance. We suggest this is adjusted against reserves.
	Dr £1.560	**Dr/Cr […]**	**Dr/Cr […]**	**Dr/Cr £[…]**	**Cr £1,560**	**Total impact of corrected audit differences**

Appendix 3

Audit differences

Corrected audit differences

Corrected misstatements are summarised below:

- Higher earners have been reduced from 649 to 601 due to amalgamation of earners and transcription errors (material by nature rather than amount);
- The Better Care Fund note was not initially included and it was omitted from Related Parties;
- A key management judgement was omitted on the Redress Scheme; and
- A contingent liability relating to ongoing litigation was omitted from the Contingent Liabilities note.

Our audit identified a small number of presentational misstatements in the notes to the financial statements. These have been discussed with management and the financial statements have been amended for all of them.

Appendix 4

Audit independence

This appendix communicates all significant facts and matters that bear on KPMG LLP's independence and objectivity and informs you of the requirements of *ISA 260 (UK and Ireland) Communication of Audit Matters to Those Charged with Governance.*

Integrity, objectivity and independence

We are required to communicate to you in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and audit team. We have considered the fees paid to us by the Authority for professional services provided by us during the reporting period. We are satisfied that our general procedures support our independence and objectivity.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies all KPMG LLP audit partners and staff annually confirm their compliance with our Ethics and Independence Manual including in particular that they have no prohibited shareholdings. Our Ethics and Independence Manual is fully consistent with the requirements of the Ethical Standards issued by the UK Auditing Practices Board. As a result we have underlying safeguards in place to maintain independence through: instilling professional values; communications; internal accountability; risk management; and independent reviews. We would be happy to discuss any of these aspects of our procedures in more detail. There are no other matters that, in our professional judgement, bear on our independence which need to be disclosed.

Audit matters

We are required to comply with *ISA (UK and Ireland) 260 Communication of Audit Matters to Those Charged with Governance* when carrying out the audit. ISA 260 requires that we consider the following audit matters and formally communicate them to those charged with governance:

- Relationships that may bear on the firm's independence and the integrity and objectivity of the audit engagement lead and audit staff;
- The general approach and overall scope of the audit, including any expected limitations thereon, or any additional requirements;
- The selection of, or changes in, significant accounting policies and practices that have, or could have, a material effect on the Authority's financial statements;
- The potential effect on the accounts of any material risks and exposures, such as pending litigation, that are required to be disclosed in the financial statements;
- Audit adjustments, whether or not recorded by the entity that have, or could have, a material effect on the Authority's financial statements;
- Material uncertainties related to events and conditions that may cast significant doubt on the Authority's ability to continue as a going concern;
- Disagreements with Management about matters that, individually or in aggregate, could be significant to the Authority's financial statements or the auditor's report. These communications include consideration of whether the matter has, or has not, been resolved and the significance of the matter;
- Expected modifications to the auditor's report;

Appendix 4

Audit independence

- Other matters warranting attention by those charged with governance, such as material weaknesses in internal control, questions regarding management integrity, and fraud involving management; and
- Any other matters agreed upon in the terms of the audit engagement.

We continue to discharge these responsibilities through our attendance at Corporate Committees, commentary and reporting and, in the case of uncorrected misstatements, through our request for management representations.

Auditor declaration

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

There were no non-audit services provided in year.

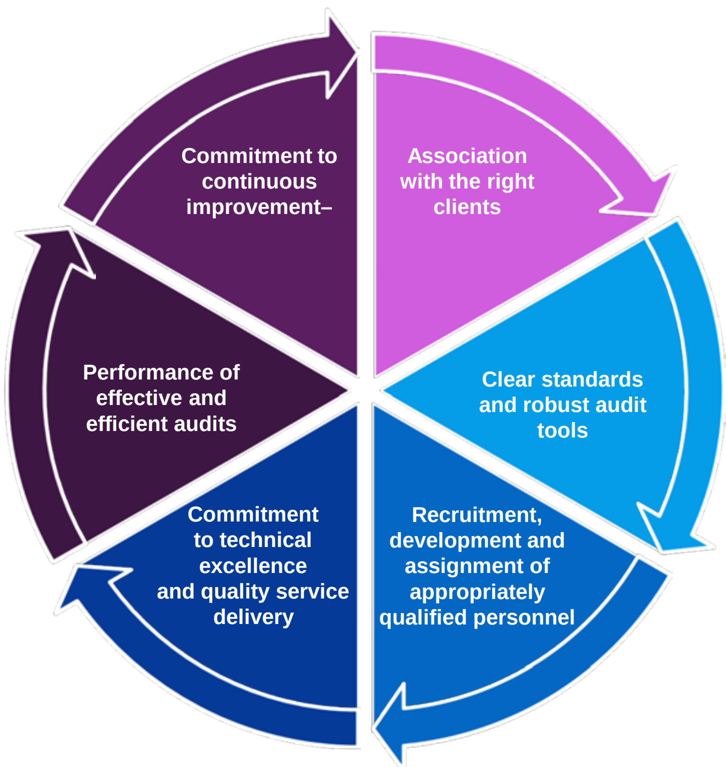
Appendix 5

Audit quality framework

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework

- Comprehensive effective monitoring processes
- Proactive identification of emerging risks and opportunities to improve quality and provide insights
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management



- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Relationships built on mutual respect
- Insightful, open and honest two way communications

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- Independence policies

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members and specialists

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