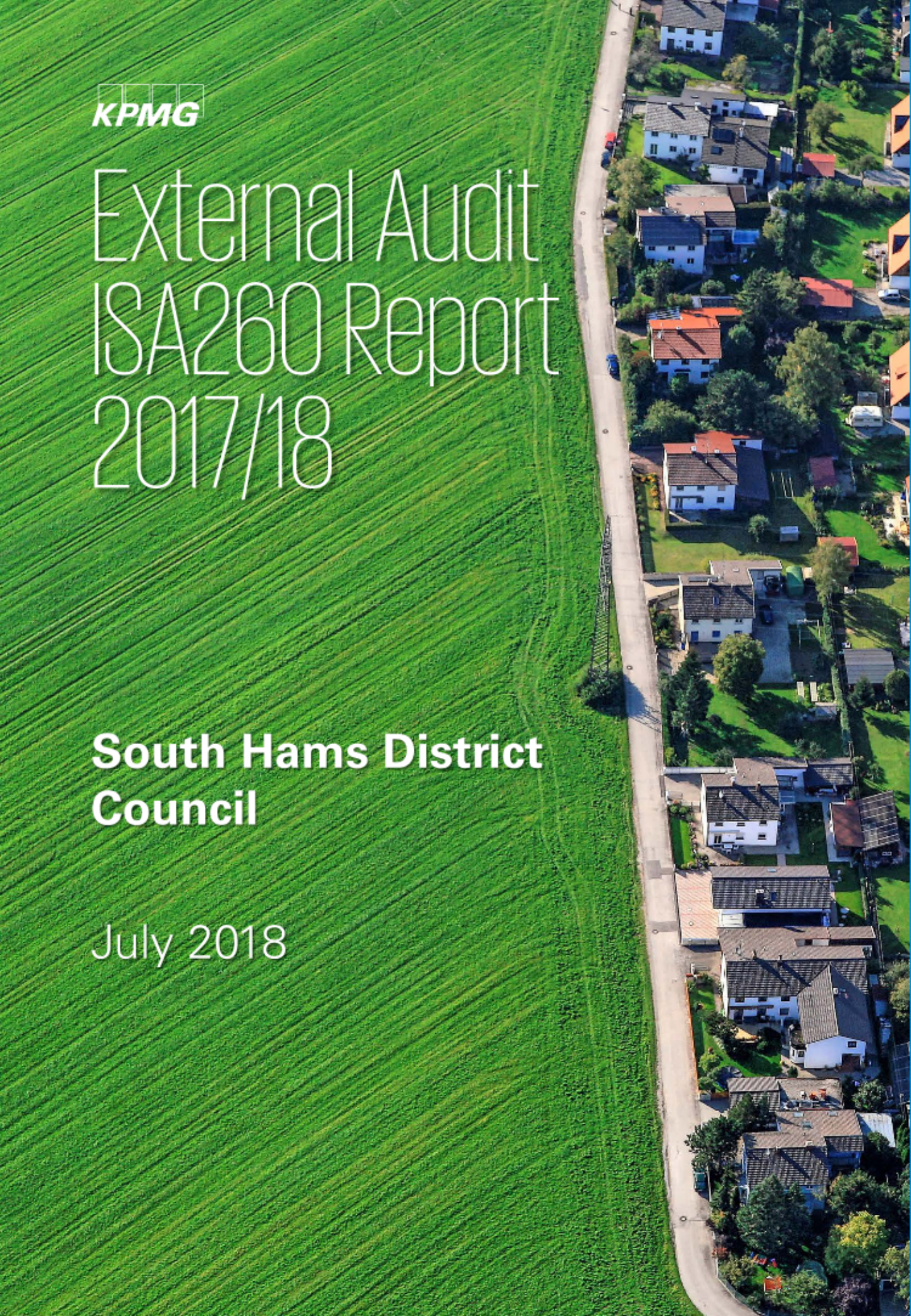




External Audit ISA260 Report 2017/18

**South Hams District
Council**

July 2018



Summary for Audit Committee

This document summarises the key findings in relation to our 2017-18 external audit at South Hams District Council ('the Authority')

This report covers both our on-site work which was completed in March and June 2018 on the Authority's significant risk areas, as well as other areas of your financial statements, and the control environment in place to support the production of timely and accurate financial statements.

Organisational control environment

We have identified no significant issues with the Authority's organisational control environment and consider that the overall arrangements that have been put in place are reasonable.

Controls over key financial systems

The controls over the majority of the key financial systems are sound. However, we have raised one new recommendation in relation to the monthly reconciliation of business rates income.

We updated our audit approach due to the control deficiency to complete additional substantive testing in this areas, with no further issues noted.

Accounts production

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

We also assessed the Authority's process for preparing the accounts and its support for an efficient audit.

The Authority has prepared the accounts to a faster timetable in the current period, whilst maintaining the quality of the financial statements and working papers. This has taken significant effort from the Finance Community of Practice and we would like to thank the team for their support during this period.

Financial statements

Subject to all outstanding queries being resolved to our satisfaction we anticipate issuing an unqualified audit opinion on the Authority's financial statements before the deadline of 31 July 2018.

Based upon our initial assessment of risks to the financial statements (as reporting to you in our *External Audit Plan 2017/18* and updated during our audit) we identified the following significant risks (excluding those mandated by International Standards on Auditing – see Page 9).

- **Valuation of PPE** – Whilst the Authority operates a cyclical revaluation approach, the Code requires that all land and buildings be held at fair value. We considered the way in which the Authority ensures that assets not subject to in-year revaluation are not materially misstated, as well as reviewing the basis of valuation for those assets that have been revalued. We are satisfied there is no material misstatement within the assets not subject to in-year revaluation.
- **Pension Liabilities** – The valuation of the Authority's pension liability, as calculated by the Actuary, is dependent upon both the accuracy and completeness of the data provided and the assumptions adopted. We reviewed the processes in place to ensure completeness and accuracy of data provided to the Actuary and considered the assumptions used in determining the valuation. We are liaising with the auditors of the Pension Fund in order to gain an understanding of the effectiveness of those controls that they operate. This is ongoing at date of this report.

Summary for Audit Committee (cont.)

Financial statements (continued)

- **Faster Close** – The timetable for the production of the financial statements was significantly advanced with draft accounts having to be prepared by 31 May (2017: 30 June) and the final accounts signed by 31 July (2017: 30 September). We reviewed the closedown plan for accounts production and monitored progress against these deadlines. We are pleased to confirm that we received draft accounts in advance of the revised deadline and anticipate issuing our opinion prior to the 31 July deadline.
- **Allocation of Shared Costs** – The Authority operates on a shared service basis with its neighbour, West Devon Borough Council. As a result of this arrangement, costs are initially borne by each authority individually and then an exercise is undertaken to allocate them on an appropriate and consistent basis. We reviewed the appropriateness of the basis of allocations, reviewed evidence of management approval and re-calculated based on the cost drivers with no issues being identified.

We have identified one adjusted audit difference as a result of our audit work (see Appendix 3). In addition we have suggested a number of presentational corrections which have been corrected in the final draft of the financial statements.

Based on our work, we have raised one new recommendation and re-raised a previous year recommendation relating to a monthly reconciliation of housing benefits expenditure which remains outstanding. Details can be found in Appendices 1 & 2.

We are now in the completion stage of the audit and anticipate issuing our completion certificate and opinion on 26 July 2018 and Annual Audit letter in August 2018.

Value for money arrangements

We have completed our risk-based work to consider whether in all significant respects the Authority has proper arrangements to ensure has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money opinion

We set out our assessment of those areas requiring additional risk based work in our *External Audit Plan 2017/18* and have updated this assessment during our interim visit. As a result we identified the following significant VFM audit risk:

- **Delivery of Budgets** – As a result of reductions in central government funding, and other pressures, the Authority is having to make additional savings beyond those from prior years and also pursue income generation strategies. We reviewed the controls in place to ensure financial resilience, specifically that the Medium Term Financial Plan has duly taken into consideration relevant factors and sensitivity analysis. We also considered the way in which the Authority identified, approved, and monitored both savings plans and budget as well as the way in which proposed income generation projects were assessed. No issues were identified as a result of our work.

See further details on page 17.

Summary for Audit Committee (cont.)

Exercising of audit powers

We have a duty to consider whether to issue a report in the public interest about something we believe the Authority should consider, or if the public should know about.

We have not identified any matters that would require us to issue a public interest report.

In addition, we have not had to exercise any other audit powers under the Local Audit & Accountability Act 2014.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help.

Section one

Control Environment



Organisational control environment

We have identified no significant issues with the Authority's organisational control environment and consider that the overall arrangements that have been put in place are reasonable.

Work completed

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit. We obtained an understanding of the Authority's overall control environment and determined if appropriate controls have been implemented. We do not complete detailed testing of these controls.

Key findings

We consider that your organisational controls are effective overall.

Aspect of controls	Assessment
Organisational controls:	
Management's philosophy and operating style	3
Culture of honesty and ethical behaviour	3
Oversight by those charged with governance	3
Risk assessment process	3
Communications	3
Monitoring of controls	3

Key	
1	Significant gaps in the control environment.
2	Deficiencies in respect of individual controls
3	Generally sound control environment.

Controls over key financial systems

The controls over the majority of the key financial systems are sound. However, there are some weaknesses in respect of housing benefits expenditure and business rates income.

We needed to complete additional substantive work in these areas at year-end.

Work completed

We evaluated the design and implementation of key financial system controls and then tested selected controls that address key risks within these systems. The strength of the control framework informed the substantive testing we completed during our final accounts visit.

Key findings

Based on our work we have determined that the controls over the majority of the key financial systems are sound, although we noted two weaknesses in respect of individual financial systems that impacted on our audit:

- **Housing Benefit Monitoring** – we noted that the monitoring of housing benefit controls was not completed on a monthly basis. This recommendation was raised in the prior year and remains outstanding.
- **Business Rates Income** - we noted that the reconciliation of national-non domestic rates cash and refunds to the general ledger were performed outside a reasonable timeframe, and that reconciling items were not being cleared in a timely fashion.

These weaknesses meant that we adapted our audit strategy in relation to housing benefits expenditure and business rates income through the inclusion of additional substantive testing at year-end. No issues were noted through this additional testing.

Recommendations are included in Appendix 1 and Appendix 2.

Aspect of controls	Assessment
Property, Plant and Equipment	3
Cash and Cash Equivalents	3
Pension Assets and Liabilities	3
Non pay expenditure	3
Payroll	3
Housing benefits expenditure	2
Business rates income	2
Council tax income	3
Journals	3

Key

1	Significant gaps in the control environment
2	Deficiencies in respect of individual controls
3	Generally sound control environment

An overhead photograph of four business professionals sitting around a white conference table. A woman in a grey top is at the top, looking at a laptop. A man in a light blue shirt is on the left, also looking at a laptop. A woman in a white top and black skirt is at the bottom left, with her arms crossed. A man in a light blue shirt is at the bottom right, with his hands clasped. The scene is brightly lit, with shadows cast across the table and floor.

Section two

Financial Statements

Accounts production and audit process

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

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

The Authority's overall process for the preparation of the financial statements is adequate.

Accounts practices and production process

The Authority incorporated a number of measures into its closedown plan to further improve the project management of this complex process. This included a detailed closedown plan which listed the key requirements and timescales by officer in the process. Specifically, the Authority recognised the additional pressures which the earlier closedown brought and we engaged with officers in the period leading up to the year end in order to proactively address issues as they emerge.

We consider that the overall process for the preparation of your financial statements is good. The accounts were produced ahead of the deadline of 31 May and the first draft was of a high standard, despite the pressures brought by an earlier deadline.

We would like to thank the Finance Community of Practice for their hard work in meeting the deadlines.

Going concern

The financial statements of the Authority have been prepared on a going concern basis. We confirm that we have identified no significant matters which would, in our view, affect the ability of the Authority to continue as a going concern.

Further commentary on the Authority's arrangements in place to secure the effective delivery of budgets is included at page 20.

Quality of supporting working papers

We issued our Accounts Audit Protocol to Pauline Henstock in May 2018. This important document set out our audit approach and timetable. It also summarised the working papers and other evidence we required the Authority to provide to support our audit work. This helped the Authority to provide audit evidence in line with our expectations.

We worked with management to ensure that working paper requirements are understood and aligned to our expectations. We are pleased to report that this has resulted in good quality working papers with clear audit trails.

Response to audit queries

We are pleased to report that our agreed turnaround time for dealing with audit queries was achieved by Officers, including those who are not part of the Finance Community of Practice. As a result of this, all of our audit work were completed within the timescales expected with no outstanding queries despite the advance in statutory deadlines.

Specific audit areas

We anticipate issuing an unqualified audit opinion on the Authority's 2017-18 financial statements by 31 July 2018. We will also report that your Annual Governance Statement complies with the guidance issued by CIPFA/SOLACE ('Delivering Good Governance in Local Government') published in April 2016.

For the year ending 31 March 2018, the Authority has reported an underspend against budget of £84k resulting in an increase to the General Fund balance. The financial statements report a deficit on the provision of services of £6.6m, including items that do not impact the General Fund (such as capital charges). The Authority has used £1.2m of capital receipts against its revenue expenditure. The underlying deficit before the use of capital receipts is £7.8m.

Auditing standards require us to consider two standard risks for all organisations. We consider these as a matter of course in our audit and will have set out the findings arising from our work in our ISA 260 Report below.

01

Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to this audit.

In line with our methodology, we carried out appropriate 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.

There are no matters arising from this work that we need to bring to your attention.

02

Fraudulent revenue recognition

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

In our *External Audit Plan 2017-18* we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

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

Over the following pages we have set out our assessment of the specific significant risks and areas of audit focus we identified in relation to the audit of the Authority's financial statements.

Specific audit areas

Significant Audit Risks – Authority

Those risks requiring specific audit attention and procedures to address the likelihood of a material financial statement error in relation to the Authority.

Risk:	Valuation of PPE <p>The Code requires that where assets are subject to revaluation, their year end carrying value should reflect the appropriate fair value at that date. The Authority has adopted a rolling revaluation model which sees all land and buildings revalued over a five year cycle. As a result of this, however, individual assets may not be revalued for four years.</p> <p>This creates a risk that the carrying value of those assets not revalued in year differs materially from the year end fair value. In addition, as the valuation is undertaken as at 31 December, there is a risk that the fair value is different at the year end.</p>
Our assessment and work undertaken:	<p>We reviewed the approach that the Authority adopted to assess the risk that assets not subject to valuation were materially misstated and considered the robustness of that approach.</p> <p>In addition, we considered movements in market indices between revaluation dates and the year end in order to determine whether these indicate that fair values had moved materially over that time. There was no indication of a material movement between these dates.</p> <p>In relation to those assets which have been revalued during the year we reviewed the accounting entries made to record the results of the revaluation in order to ensure that they were appropriate. It was noted that the revaluation date had moved from 1 April to 31 December in year to reduce the risk of material movements occurring between revaluation date and year-end.</p> <p>We also assessed the valuer's qualifications, objectivity and independence to carry out such valuations and reviewed the methodology used (including testing the underlying data and assumptions). No issues were noted with our testing.</p> <p>We have set out our view of the assumptions used in relation to accounting for Property, Plant & Equipment on page 13.</p>

Risk:	Allocation of Shared Costs <p>The Authority operates a shared service basis with its neighbour, West Devon Borough Council. As a result of this arrangement, costs are initially borne by each authority individually and then an exercise is undertaken to allocate them on an appropriate and consistent basis. This is essential to ensuring that the Authority recognises its full costs and to prevent cross subsidy between the two authorities. In order to operate effectively, the allocation of costs must be undertaken on an appropriate basis which reflects the nature of the underlying activities and the way in which resources are consumed.</p>
Our assessment and work undertaken:	<p>Building upon our work undertaken during the previous year audit, we reviewed the way in which shared costs have been allocated to the Authority and ensured that:</p> <ul style="list-style-type: none">— The basis of allocation is appropriate and reflects the nature of the activities involved;— The allocation basis, and any changes from prior year, have been approved appropriately by management and was subject to appropriate review; and— The allocation had been appropriately calculated and the resulting costs recognised.

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

<p>Risk:</p>	<p>Pension Liabilities</p> <p>The pension liability represents a material element of the Authority's balance sheet. The Authority is an admitted body of Devon County Pension Fund, which had its last triennial valuation completed as at 31 March 2016. This forms an integral basis of the valuation as at 31 March 2018.</p> <p>The valuation of the Local Government Pension Scheme relies on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which results in the Authority's overall valuation.</p> <p>There are financial assumptions and demographic assumptions used in the calculation of the Authority's valuation, such as the discount rate, inflation rates, mortality rates etc. The assumptions should also reflect the profile of the Authority's employees, and should be based on appropriate data. The basis of the assumptions is derived on a consistent basis year to year, or updated to reflect any changes.</p> <p>There is a risk that the assumptions and methodology used in the valuation of the Authority's pension obligation are not reasonable. This could have a material impact to the pension liability accounted for in the financial statements.</p>
<p>Our assessment and work undertaken:</p>	<p>As part of our work we reviewed the controls that the Authority has in place over the information sent directly to the Scheme Actuary. We are currently liaising with the auditors of the Pension Fund in order to gain an understanding of the effectiveness of those controls operated by the Pension Fund. This will include a consideration of the process and controls with respect to the assumptions used in the valuation.</p> <p>We also evaluated the competency, objectivity and independence of Barnett Waddingham. There were no issues with these areas.</p> <p>We reviewed the appropriateness of the key assumptions included within the valuation, compared them to expected ranges and involved a KPMG Actuary to provide a specialist assessment of those assumptions. We also reviewed the methodology applied in the valuation by Barnett Waddingham. Our work over key assumptions did not highlight any areas of concern – we have set out our view of the assumptions used in valuing pension assets and liabilities on page 14.</p> <p>In addition, we reviewed the overall Actuarial valuation and considered the disclosure implications in the financial statements. We noted some minor presentational differences which have been corrected.</p> <p>We are liaising with the Pension Fund auditors to gain assurance over the controls operating by the Pension Fund and the provision of information to the actuary to support their calculation of the pension liabilities.</p> <p>As a result of this work we determined that there are no issues with the pensions liabilities, subject to completion of the final elements of testing.</p>

Specific audit areas (cont.)

Significant Audit Risks – Authority (cont.)

<p>Risk:</p>	<p>Faster Close</p> <p>In prior years, the Authority has been required to prepare draft financial statements by 30 June and then final signed accounts by 30 September. For years ending on and after 31 March 2018 however, revised deadlines apply which require draft accounts by 31 May and final signed accounts by 31 July.</p> <p>These changes represent a significant change to the timetable that the Authority has previously worked to. The time available to produce draft accounts has been reduced by one month and the overall time available for completion of both accounts production and audit is two months shorter than in prior years. Whilst we are aware that the Authority has begun to plan and prepare for the revised timetable, there is still significant amount of work to be completed.</p> <p>In our External Audit Plan we highlighted that in order to meet the revised deadlines the Council may need to make greater use of accounting estimates. In order to do so the Council would have had to ensure that those estimates remain valid at the point of finalising the financial statements. We also highlighted a number of logistical challenges that needed to be managed including:</p> <ul style="list-style-type: none">— Ensuring that any third parties involved in the production of the accounts (including valuers and actuaries) were aware of the revised deadlines and had made arrangements to provide the output of their work in accordance with this;— Revising the closedown and accounts production timetable to ensure that all working papers and other supporting documentation were available at the start of the audit process;— Ensuring that the Audit Committee meeting schedules had been updated to permit signing in July; and— Applying a shorter paper deadline to the July meeting of the Audit Committee to ensure accommodation of the production of the final version of the accounts and our ISA 260 report.
<p>Our assessment and work undertaken:</p>	<p>We liaised with officers in preparation for our audit in order to understand the steps that the Authority was taking in order to ensure it met the revised deadlines. We also advanced audit work into the interim visit in order to streamline the year end audit work.</p> <p>We received draft financial statements in advance of the statutory deadline of 31 May 2018. The quality of this draft was consistent with that of prior years.</p> <p>In a number of areas the Authority made increased use of estimates. In these areas we considered the assumptions used and challenged the robustness of those estimates. Our work over post year-end journals tested was performed to a lower threshold to address the faster close risk.</p> <p>As a result of this work we determined that there were no issues identified.</p>

Judgements

We have considered the level of prudence within key judgements in your 2017-18 financial statements and accounting estimates. We have set out our view below across the following range of judgements.

Level of prudence

0	1	2	3	4	5	6	
Audit Difference	Cautious		Balanced		Optimistic		Audit Difference
	Acceptable Range						

Subjective area	2017-18	2016-17	Commentary
Provisions	3	3	<p>The Authority's provision has increased from the previous year due to a larger number of appeals in progress.</p> <p>We identified no issues in relation to the appropriateness of the provision.</p>
Accruals de minimis level	3	3	<p>The Authority has maintained its de minimis accruals at £5k. We have compared the threshold used to that applied at other authorities and have confirmed it is in line with the general approach adopted.</p> <p>We did not note any issues with this in current year testing.</p>
Property Plant & Equipment: Asset lives/valuations	3	3	<p>The Authority has utilised internal valuation experts to provide valuation estimates. We have reviewed the methodology and assumptions used and have concluded that the valuation exercise is in line with the CIPFA Code and external guidance.</p> <p>We have reviewed the methodology for the revaluation performed as at 31 December. A full valuation is performed on a rolling basis to cover 20% of the assets per annum over a five-year cycle. Assets not included in the full valuation are also assessed in order to ensure that carrying amounts are not materially different to current values at the year-end.</p> <p>Based on the last five years of valuations, 100% of the asset value for land and buildings have been valued accordingly (31% in 2017/2018). We have gained assurance that the assets not revalued during the year have not materially changed as at 31 March 2018, ensuring compliance with the CIPFA Code. It was noted that both the industrial units and office facilities that the Council holds have not been revalued for a number of years, and should be subject to review in 2018/2019.</p>

Judgements (cont.)

Subjective area 2017-18 2016-17 Commentary

Valuation of pension assets and liabilities

3

3

The Authority continues to use Barnett Waddingham to provide actuarial valuations in relation to the assets and liabilities recognised as a result of participation in the Local Government Pension Scheme. Due to the overall value of the pension assets and liabilities, small movements in the assumptions can have a significant impact on the overall valuation.

The overall set of assumptions proposed by the Authority can be considered to be balanced relative to our central rates for a typical UK scheme with a duration of 19 years and within our normally acceptable range.

Assumption	Actuary Value	KPMG Range	Assessment
Discount rate	2.55%	2.50%	3
CPI inflation	2.30%	2.16%	2
Net discount rate	0.25%	0.34%	2
Salary Growth	3.80%	2.30-4.30%	3
Life expectancy			
Current male / female	23.5 / 25.6	22.1 / 23.9	2
Future male/female	25.7 / 27.9	23.5 / 25.4	

Proposed opinion and audit differences

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's 2017-18 financial statements following approval of the Statement of Accounts by the Audit Committee on 24 July 2018.

Audit differences

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

The final materiality (see Appendix 4) for this year's audit was set at £1.2 million. Audit differences below £60,000 are not considered significant.

We did not identify any material misstatements.

We identified a small number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2017-18 ('the Code'). We understand that the Authority will be addressing these where deemed significant.

Annual governance statement

We have reviewed the Authority's 2017-18 Annual Governance Statement and confirmed that:

- It complies with Delivering Good Governance in Local Government: A Framework published by CIPFA/SOLACE; and
- It is not misleading and is consistent with other information we are aware of from our audit of the financial statements.

We have made a number of comments in respect of its format and content which the Authority has agreed to amend where significant.

Narrative report

We have reviewed the Authority's 2017-18 narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 2017/18 financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

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

In relation to the audit of the financial statements of South Hams District Council for the year ending 31 March 2018, we confirm that there were no relationships between KPMG LLP and South Hams District Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 6 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to Lisa Buckle for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

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

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional 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.).

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 2017-18 financial statements.

Section three

Value for Money Arrangements



Specific value for money risk areas

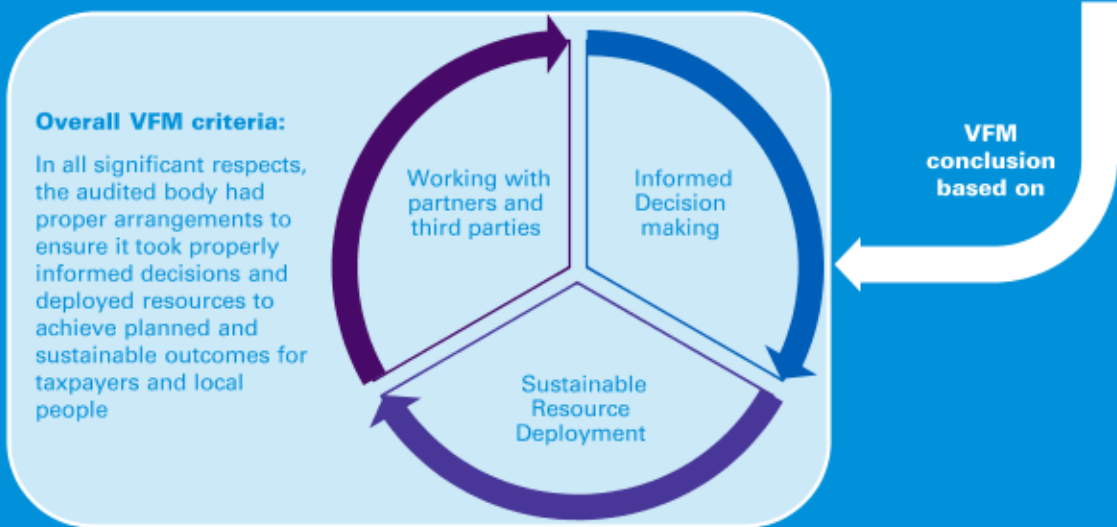
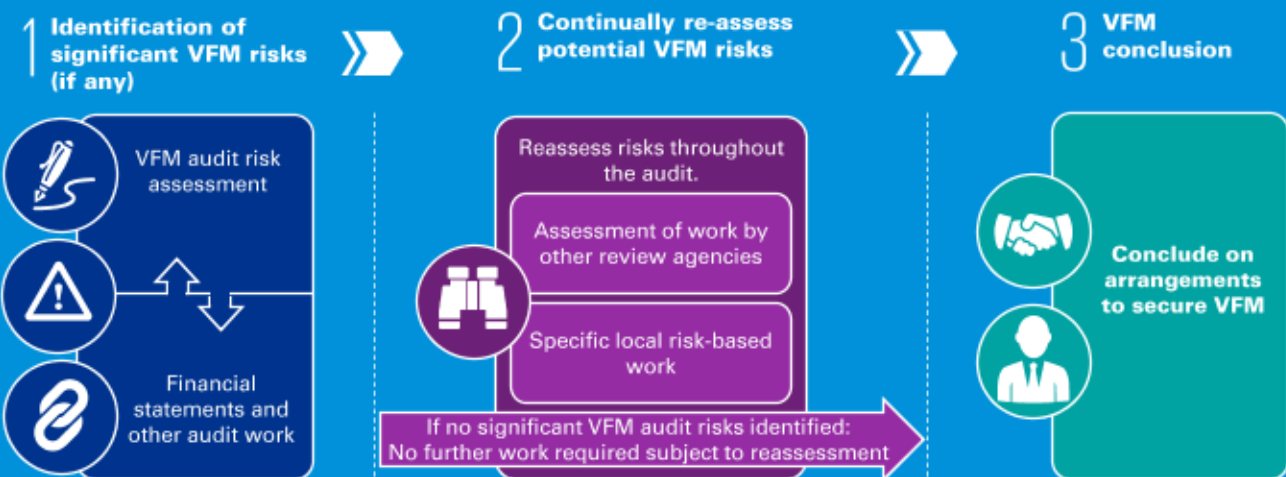
Our 2017-18 VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

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

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

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



Specific value for money risk areas (cont.)

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

Applicability of VFM Risks to VFM sub-criteria

VFM Risk	Informed decision making	Sustainable resource deployment	Working with partner and third parties
Delivery of budgets	✓	✓	✓

In consideration of the above, we have concluded that in 2017-18, the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

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



Specific value for money risk areas (cont.)

As communicated to you in our *External Audit Plan 2017-18*, we have identified two risks requiring specific audit attention and procedures to address the likelihood that proper arrangements are not in place to deliver value for money.

In all cases we are satisfied that external or internal scrutiny provides sufficient assurance that the Authority's current arrangements in relation to these risk areas are adequate.

We have provided below a summary of the risk areas identified, our work undertaken and the conclusions reached.

Risk:	Delivery of budgets The Authority identified the need to make savings of £878k in 2017/18 (in addition to those already delivered in prior years). The most recent budget monitoring report (presented to the Executive on 1 February 2018) showed a forecast underspend of £103k which amounts to 1.2% of budgeted expenditure. The 2018/19 budget (which was approved by the Council on 22 February 2018) included in-year savings of £689k and an identified budget gap for 2019/20 of £639k. The Council is identifying and developing proposals to meet this forecast budget gap.
Our assessment and work undertaken:	Like most of local government, the Authority faces a challenging future driven by funding reductions and an increase in demand for services. Post-audit, the Authority is reporting an overall underspend of £84k in the General Fund Balance and a transfer of £13.4 million in the Earmarked Reserves balance for 2017/18 (due to timing of business rates provisions which will subsequently be released back into the General Fund in 2018/2019) with the overall balance of £1.5 million as of 31 March 2018. This contains £1.8 million of General Fund reserves and £(0.3) million of Earmarked reserves. We have performed a budget review for 2017/18 compared to actual results for the year and note that the budgeted figures for the period do not differ significantly from the actual figures in the Statement of Accounts and as such, the budgeting process can be seen as reliable and prudent. The spending, savings and service delivery continues to be monitored through the quarterly budget monitoring reports within the Executive and Board meetings.

Appendices



Appendix 1:

Key issues and recommendations

Our audit work on the Authority's 2017-18 financial statements has identified one issue. We have listed this issue in this appendix together with our recommendations which we have agreed with Management. We have also included Management's responses to these recommendations.

The Authority should closely monitor progress in addressing the risks, including the implementation of our recommendations.

We have given each recommendation a risk rating and agreed what action management will need to take.

Priority Rating for Recommendations

1	<p>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.</p> <p>Recommendations Raised: 0</p>	2	<p>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.</p> <p>Recommendations Raised: 1</p>	3	<p>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.</p> <p>Recommendations Raised: 0</p>
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No.	Risk	Issue & Recommendation	Management Response
1	1	<p>Reconciliation of National-Non Domestic Rates Cash and Refunds</p> <p>It was noted during our interim audit that the reconciliation of national-non domestic rates cash and refunds to general ledger were not being performed in a reasonable timeframe, and that some reconciling items were not being cleared in a timely fashion.</p> <p>Risk</p> <p>There is a risk that reconciling items are not appropriately followed up and remain on the reconciliation for longer than would be reasonably expected.</p> <p>Recommendation</p> <p>Ensure that all reconciliations are completed in a timely manner and fluid items are appropriately followed up on.</p>	<p>The recommendation is agreed. This has already been addressed and monthly reconciliations are being submitted to the Finance Community of Practice Lead for approval.</p> <p>Responsible Officer</p> <p>Senior Case Manager</p> <p>Implementation Deadline</p> <p>Immediately, this has already been addressed and implemented</p>

Follow-up of prior year recommendations

The Authority has not implemented all of the recommendations raised through our previous audit work.

We re-iterate the importance of the outstanding recommendations and recommend that these are implemented as a matter of urgency.

This appendix summarises the progress made to implement the recommendations identified in our Interim Audit Report 2016/17 and ISA 260 Report 2016/17 and outstanding recommendations from previous audit years and re-iterates any recommendations still outstanding.

Number of recommendations that were

Included in the original report	1
Implemented in year or superseded	-
Outstanding at the time of our interim audit	1

No.	Risk	Issue & Recommendation	Management Response	Status as at July 2018
3	3	<p>Performing Monthly Reconciliations</p> <p>Risk We have identified three non-significant control deficiencies during our 2016/17 audit in regards to monthly reconciliation controls over housing benefits and trade payables.</p> <p>We acknowledge that there was an absence of staff responsible for performing the reconciliations however there is a monthly process checklist that provides guidance on required tasks to be completed every month. The Authority should have allocated staff to cover the key members to ensure that monthly processes are completed.</p> <p>In our 2017/2018 interim audit, it was noted that the monthly reconciliation controls over housing benefit payments were not being completed.</p> <p>Recommendation Ensure that sufficient closedown staff are trained to complete the monthly process checklist over the financial statement balances to ensure that adequate review is performed over the monthly financial information.</p> <p>The overarching principle is that monthly reconciliations should be completed and reviewed in a timely manner throughout the year and any reconciling items be explained and cleared the following month.</p>	<p>The recommendation is agreed. Officers will ensure reconciliations are completed on a timely basis.</p> <p>Responsible Officer Housing Benefits Manager</p> <p>Implementation Deadline This has been addressed.</p>	<p>It was noted during our interim audit that the completion of monthly benefit payment checks by officers was not being documented so as to evidence their completion.</p> <p>We determined that it was necessary to adjust our audit approach to reflect the impact of this control failing during the year. We have not performed a follow up to confirm whether this has been resolved since our interim work.</p> <p>As a result, we are re-iterating that this issue will need to be resolved.</p>

Appendix 3:

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee).

We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

A number of minor amendments focused on presentational improvements have also been made to the 2017-18 draft financial statements. The Finance Community of Practice is committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Adjusted audit differences – Authority

The following table sets out the significant audit differences identified by our audit of South Hams District Council's financial statements for the year ended 31 March 2018. This has been adjusted in the final set of financial statements to be presented to the Audit Committee on 26 July 2018.

Table 1: Adjusted audit differences – Authority (£'000)

No.	Income and expenditure statement	Movement in reserves statement	Assets	Liabilities	Reserves	Basis of audit difference
1			DR Investment Property 75			During the year the Authority has decided to sell one of its investment property assets. To reflect this they have reclassified the asset in question as "Assets Held For Sale".
			CR Assets Held for Sale (75)			The Code specifies that where investment properties meet the definition of assets held for sale they should either: <ul style="list-style-type: none">— continue to be classified as an investment property; or— be classified as a separate asset category of "Investment Property Assets Held for Sale". There is no net impact on assets, this is a presentational change between investment properties and assets held for sale.
	Nil	Nil	Nil	Nil	Nil	Total impact of adjustment

Unadjusted audit differences

There were no unadjusted audit differences..

Materiality and reporting of audit differences

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

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

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

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

We used the same planning materiality reported in our *External Audit Plan 2017-18*, presented to you in January 2018.

Materiality for the Authority's accounts was set at £1.2 million which equates to around 1.5 percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit Committee

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

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

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

In the context of the Authority, an individual difference is considered to be clearly trivial if it is less than £60,000 for the Authority.

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

Appendix 5:

Required communications with the Audit Committee

We have provided below at-a-glance summary of the information we are required to report to you in writing by International Accounting Standards.

Required Communication	Commentary
Our draft management representation letter	We have not requested any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2018.
Adjusted audit differences	We have identified one adjusted differences as a result of our audit of the Authority's financial statements. Please see appendix 3.
Unadjusted audit differences	We have identified no unadjusted difference as a result of our audit of the Authority's financial statements.
Related parties	There were no significant matters that arose during the audit in connection with the entity's related parties.
Other matters warranting attention by the Audit Committee	There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
Control deficiencies	<p>We have set out our assessment of the Authority's internal control environment, including confirmation there were no significant deficiencies identified, in Section one of this report (see pages 5 and 6).</p> <p>We have communicated all deficiencies in internal controls over financial reporting of a lesser magnitude than significant deficiencies identified during the audit in the body of this report (see page 6)</p>
Actual or suspected fraud, noncompliance with laws or regulations or illegal acts	We identified no actual or suspected fraud involving the Authority's Member or officers with significant roles in internal control, or where the fraud resulted in a material misstatement in the financial statements.
Significant difficulties	No significant difficulties were encountered during the audit.
Modifications to auditor's report	There are no modifications to our audit report.
Disagreements with management or scope limitations	The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.
Other information	<p>No material inconsistencies were identified related to other information in the Narrative Report or Annual Governance Statement.</p> <p>These reports were found to be fair, balanced and comprehensive, and compliant with applicable requirements.</p>
Our declaration of independence and any breaches of independence	<p>No matters to report.</p> <p>The engagement team [and others in the firm, as appropriate, the firm and, when applicable, KPMG member firms] have complied with relevant ethical requirements regarding independence.</p> <p>See Appendix 6 for further details.</p>

Appendix 5:

Required communications with the Audit Committee (cont.)

Required Communication	Commentary
Accounting practices	<p>Over the course of our audit, we have evaluated the appropriateness of the Authority's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate.</p> <p>We have set out our view of the assumptions used in valuing pension assets and liabilities at page 14.</p>
Significant matters discussed or subject to correspondence with management	<p>There were no significant matters arising from the audit which were discussed, or subject to correspondence, with management.</p>



Declaration of independence

ASSESSMENT OF OUR OBJECTIVITY AND INDEPENDENCE AS AUDITOR OF SOUTH HAMS DISTRICT COUNCIL

Professional ethical standards require us to provide to you at the conclusion of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code of Audit Practice, the provisions of Public Sector Audit Appointments Limited's ('PSAA's') Terms of Appointment relating to independence, the requirements of the FRC Ethical Standard and the requirements of Auditor Guidance Note 1 - General Guidance Supporting Local Audit (AGN01) issued by the National Audit Office ('NAO') on behalf of the Comptroller and Auditor General.

This Statement is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

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 partners, Audit Directors and staff annually confirm their compliance with our ethics and independence policies and procedures. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management
- Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

Declaration of independence (cont.)

Independence and objectivity considerations relating to the provision of non-audit services

Summary of fees

We have considered the fees charged by us to the authority and its controlled entities for professional services provided by us during the reporting period. We have detailed the fees charged by us to the authority and its controlled entities for significant professional services provided by us during the reporting period in Appendix 6, as well as the amounts of any future services which have been contracted or where a written proposal has been submitted. Total fees charged by us for the period ended 31 March 2018 can be analysed as follows:

	2017-18 £	2016-17 £
Audit of the Authority	43,404	43,404
Total audit services	43,404	43,404
Mandatory assurance services	7,670	7,328
Total Non Audit Services	7,670	7,328

We are required by AGN 01 to limit the proportion of fees charged for non-audit services (excluding mandatory assurance services) to 70% of the total fee for all audit work carried out in respect of the Authority under the Code of Audit Practice for the year. The ratio of non-audit fees to audit fees for the year was 18%. We do not consider that the total of non-audit fees creates a self-interest threat since the absolute level of fees is not significant to our firm as a whole.

We confirm that all non-audit services were approved by the audit committee or equivalent.

Facts and matters related to the provision of non-audit services and the safeguards put in place that bear upon our independence and objectivity, are set out in the table below.

Analysis of Non-audit services for the year ended 31 March 2018

Description of scope of services	Principal threats to independence and Safeguards applied	Basis of fee	Value of services delivered in the year ended 31 March 2018 £	Value of services committed but not yet delivered £
Mandatory assurance services				
Grant Certification – Housing Benefit Subsidy Return	The certification of the Housing Benefits Subsidy return forms part of our contractual responsibilities as the Authority's appointed auditor. The nature of this audit-related service is such that we do not consider it to create any independence threats.	Fixed Fee	7,328	7,670

No non-audit services required specific approval from PSAA as the relevant thresholds were not breached.

Independence and objectivity considerations relating to other matters

There are no other matters that, in our professional judgment, bear on our independence which need to be disclosed to the Audit Committee.

Declaration of independence (cont.)

Confirmation of audit independence

We confirm that as of the date of this report, in our professional judgment, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Audit Director and audit staff is not impaired.

This report is intended solely for the information of the Audit Committee of the authority and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

KPMG LLP

Appendix 7:

Audit fees

As communicated to you in our *External Audit Plan 2017-18*, our scale fee for the audit is £39,396 plus VAT (£39,396 in 2016/17), which is consistent with the prior year.

Our work on the certification of the Authority's Housing Benefit Subsidy return is planned for September 2018. The planned scale fee for this is £5,630 plus VAT (£5,340 in 2016/17).

Component of the audit	2017-18 Planned Fee £	2016-17 Actual Fee £
Accounts opinion and value for money work		
PSAA Scale fee (South Hams District Council)	43,404	43,404
Total audit services	43,404	43,404
Mandatory assurance services		
Housing Benefits Certification (work planned for September 2018)	7,670	7,328
Total mandatory assurance services	7,670	7,328
Grand total fees for the Authority	51,074	50,732

All fees quoted are exclusive of VAT.





The key contacts in relation to our audit are:

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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. We draw your attention to the Statement of Responsibilities of auditors and audited bodies, which is available on Public Sector Audit Appointments' 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 Rees Batley 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, by email to Andrew.Sayers@kpmg.co.uk. After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, Local Government House, Smith Square, London, SW1P 3HZ.

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